A Current Analysis of the Usury Laws
A National View

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Usury is not a novel concept. References can be found in the legal and religious annals of the last 2,500 years![1] Nevertheless, most modern legal practitioners probably have had little contact with the subject of usury until the last several years. The current money market has brought into focus the problem of legal limitations on interest rates including, most importantly, the law of usury.

Each of the fifty states (plus Puerto Rico, the Virgin Islands and the District of Columbia) has a usury law,[2] and no two laws are identical. Thus, in today's commerce, with many interstate loan transactions, counsel may be called upon not only to determine which state law will apply, but also to understand the applicable law and, if possible, tailor the transaction so that the most favorable law will be applied to the transaction.[3]

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1. *Deuteronomy* 23:16, *Psalms* XV; 13 Eliz., c. 8 (1561); Statute of Anne, 12 Anne, c. 16 (1713).
2. *See* Addendum *infra.*
3. The subject of conflict of law in respect to usury will not be covered

Usury, simply stated, is charging more interest on a loan transaction than is allowed by law. Though the principle is relatively simple, its application to the numerous types of transactions in which usury may be involved is a difficult task. The purpose of this article will be to summarize the law of usury as it has developed and to point out, where possible, patterns in the laws among the various states.

I.

HISTORY

A reflection on the history of usury is important in order to give the reader insight into the rationale and structure of modern usury legislation, as well as to illustrate the tradition of the accompanying public policy.

The doctrine of usury, being approximately 2,500 years old, had its first recorded history in the Old Testament,[4] where the ancient laws forbade any interest against a brother, but permitted interest against a stranger.[5] Conversely, the economics of ancient Egypt and the Roman Empire were not so concerned with the taking of interest; and it was not until the reformation and the rise of Christianity that the Old Testament view again prevailed.[6]

The most recent usury statute adopted in England was the Statute of Anne (1713).[7] There, the maximum allowable rate was set at 5 percent;[8] and, furthermore, if the maximum rate was exceeded, with no exceptions, the contract was void.

The Statute of Anne remained in force in England for 141 years. However, a change in public policy could be seen in 1830, when holders in due course of securities were permitted recovery although the securities arose out of a usurious transaction.[9] Finally, in 1854, England repealed all usury legislation;[10] and since that date, the courts have resorted merely to striking down *unconscionable* contracts.[11]

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in this article. The broad dimensions of the subject are such that the subject should be treated separately. For an excellent article, *see Usury in the Conflict of Laws: The Doctrine of the Lex Debitoris*, 55 CALIF. L. REV. 123 (1967).

4. *Deuteronomy* 23:19.
5. *Id.*
6. 6 S. WILLISTON, CONTRACTS, § 1682, at 4754-55 (rev. ed. 1958) [hereinafter cited as WILLISTON]; 13 Eliz., c. 8 (1561).
7. 12 Anne, c. 16 (1713).
8. *Id.*
9. 17 & 18 Vict., c. 90 (1830).
10. Woolf v. Hamilton, 14 T.L.R. 499 (1830).
11. WILLISTON, *supra* note 6.

The Statute of Anne, however, was the law in England during a critical period in American history, and, in fact, is the model upon which most American usury statutes are predicated. Although the Statute of Anne was repealed in 1854, every state, plus Puerto Rico, the Virgin Islands, and the District of Columbia, have usury legislation in some form.

II.

ELEMENTS OF USURY

Usury consists of three elements—(A) a loan or forbearance, (B) exaction of excessive interest, and (C) wrongful intent. All elements must be present for usury to exist.

A. The Loan or Forbearance.

The typical usury law is based on the Statute of Anne[12] and provides that excessive interest may not be charged on "any loan or forbearance of any money, goods or things in action."[13] Even in jurisdictions broadening the definition of usury to include "all written contracts whatsoever" providing for interest[14] or "any contract founded upon any sale or loan of real or personal property,"[15] the law requires that there be a debt obligation requiring the payment of interest.

Loan. A loan is defined as:

> 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.[16]

The essential element of any loan transaction is that it requires the absolute commitment by the borrower to repay the principal sum; the lender does not run any risk of loss of principal other than as a result of the borrower's insolvency.[17] The principle is illustrated in a series of cases concerned with whether or not the party obtaining the money had an absolute obligation to repay the principal sum obtained.

12. 12 Anne, c. 16 (1713).
13. CAL. CONST. art. XX, § 22 (1919).
14. 15 TEX. CIV. STAT. art. 5071 (Vernon 1962).
15. IOWA CODE ANN. § 535.4 (1962).
16. CAL. CIV. CODE § 1912 (West 1954).
17. Martin v. Ajax Construction Co., 124 Cal. App. 2d 425, 269 P.2d 132 (1954).

In *Martin v. Ajax Construction Co.*,[18] A advanced to B the sum of $5,000 for the purpose of assisting B in undertaking a construction program to build 150 duplexes and 40 single-family residences. A was to be repaid $10,000 within one year by the payment to him of $100 upon the sale of each duplex and $50 upon the sale of each single-family residence. The trial court was of the opinion that there was no absolute obligation to repay the sum since the primary source of repayment was from the sales proceeds; the various properties might not be sold or, if sold, might not result in sufficient proceeds to pay the obligation, causing a loss of principal to A. On that basis, the trial court found that a joint venture existed. In reversing, the appellate court held that regardless of the primary source of funds for the payments of the obligation, there was an unconditional promise to pay $10,000 within one year, and the transaction constituted a loan. Therefore, the law of usury applied to the transaction.

Another case raising the same issue is *Moore v. Dealy*.[19] There, Reeves and Moore deposited the sum of $25,000 in a special account to be withdrawn upon the joint signatures of Dealy and Reeves or Moore. The moneys were to be used to pay certain construction costs incurred by Dealy as contractor. In addition to recovering $25,000, Reeves and Moore each were to be paid $5,000 for making the moneys available. Although the contract stipulated that the relationship was not a partnership or joint venture, the court found that a joint venture existed; that an implied provision of the agreement was that Reeves and Moore would share in the losses of the enterprise. Since the transaction constituted a joint venture rather than a loan, usury did not apply.

A third case raising the same issue is *Wooton v. Coerber*.[20] In that case, B entered into a transaction to buy property, but he had no money with which to make the down payment. A put up all the money as *lender*. A was to receive a limited share of the proceeds if the property was resold quickly; otherwise, A would acquire ownership of the property if no sale could be made within a reasonable time. The court found that the whole sum was put in hazard, the sum being repaid in the last resort out of the property itself. Therefore, the transaction was not a loan but was a joint venture. In reaching its decision, the court was impressed with the fact that A took all of the risk of financial loss.

The three cases just discussed raise the issue of whether the

18. *Id.*
19. 117 Cal. App. 2d 89, 254 P.2d 888 (1953).
20. 213 Cal. App. 2d 142, 28 Cal. Rptr. 635 (1963).

transaction was a loan or a joint venture. In each of the three cases, the court's rationale was based on whether the party furnishing the financing was to bear any risk of loss of principal from the operation of the debtor's business. In the *Moore* and *Wooten* cases, the courts even ignored language in the documents referring to the financial parties as *lenders*, and in each instance held the transaction to be a joint venture.[21]

A similar issue is raised where a party *purchases* a debt obligation but the *seller* guarantees the purchaser against loss of principal. As an example, the seller may sell a debt obligation *with recourse.* The usury laws do not generally apply to a true purchase and sale transaction.[22] However, if the seller guarantees the purchaser against loss of principal, the court may be concerned that the parties have created a loan transaction.

A typical case is *Milana v. Credit Discount Co.*[23] There, the plaintiff-manufacturer agreed to sell defendants her accounts receivable which she warranted to be good and collectible; in return, the defendant-purchaser agreed to pay full face value, less agreed upon discounts. The plaintiff's guarantee of principal was for a specified time period, and defaulted accounts were charged by defendants against reserves. The court found the transaction to be merely an advancement of money to be repaid with interest at a rate greater than allowed by law, and therefore it was usurious.[24]

Although the presence of a guarantee does not in and of itself mean that the transaction is a loan, its mere presence raises a *red flag*, and in some cases where it is present, particularly where the

21. A similar principle appears to have been applied by the court in Leibovici v. Rawloki, 57 Misc. 2d 141, 290 N.Y.S.2d 997 (1968). In that case, A turned over to B the sum of $5,000. B guaranteed the return of principal plus the first earnings of the property up to an amount per annum equal to 10% of the investment (rate in excess of New York usury limits). The court held that the contract was legal since it did not constitute a loan. The contract concept before the court was developed in the 13th and 14th centuries as a type of joint venture to escape the usury laws. *Without passing judgment on the importance of the case in New York, outside that state it is doubted whether the decision of a lower court would be followed.*

22. *See* text accompanying note 135, *infra.*

23. 27 Cal. 2d 335, 163 P.2d 869 (1945).

24. *See* Kelter v. American Bankers' Finance Co., 306 Pa. 483, 160 A. 127 (1932); Home Bond Co. v. McChesney, 239 U.S. 568 (1916); Petition of National Discount Co., 272 F. 570 (6th Cir. 1921).

parties have a continuing relation, the court is likely to find that the transaction is a loan. In such cases, the only hazard to the principal is the insolvency of the borrower.

Forbearance. A forbearance has been defined as the giving of further time for the repayment of an obligation or an agreement not to enforce a claim at its due date.[25]

The most common situation giving rise to a *forbearance* is illustrated by the case of *London v. Toney*.[26] In that case, the debtor could not pay his obligation upon its due date. Therefore, the creditor agreed to extend the period of repayment of the debt for an additional consideration. The new consideration, when added to the interest provided for in the original contract, caused the overall interest obligation to exceed the usury limitations of the State of New York.

Suppose that the creditor agrees to waive personal liability in exchange for an additional consideration. The waiver of personal liability has been held to be permanent forbearance, thus bringing the transaction within the usury laws.[27]

B. Excessive Interest.

Excessive interest (usury's second element) has been broadly defined as the exaction of a greater profit than is allowed by law for the use of money or for the forbearance of a debt.[28] An analysis of interest and whether it exceeds the usury limit falls into five categories: (1) a technical definition of interest, (2) a description of charges which normally are included within interest for purposes of determining whether usury exists, (3) a description of charges which normally are not included within interest, (4) a description of the methods utilized to compute the rate of interest charged, and (5) a description of certain loan transactions involving interest charges outside the scope of usury.

1. *A Technical Definition of Interest.* In the words of California Civil Code § 1915:

> Interest is the compensation allowed by law or fixed by the parties for the use, or forbearance, or detention of money.[29]

Thus, if the charge to the borrower is for any purpose other than

25. 1 B. Witkin, Summary of California Law § 169, at 183-84 (7th ed. 1960).
26. 263 N.Y. 439, 189 N.E. 485 (1934).
27. Calimpco v. Warden, 100 Cal. App. 2d 429, 224 P.2d 421 (1950).
28. Prather, *Mortgage Loans and the Usury Laws*, 16 Bus. Lawyer 181 (1960) [hereinafter cited as Prather].
29. Cal. Civ. Code § 1915 (West 1954).

for the use of money arising out of a loan or upon a forbearance (or detention), it is not interest for the purpose of determining usury.

One major line of cases in which the courts generally have found the laws of usury not to apply pertains to the *sale of credit.* In such cases, the courts have found that the charge to the obligor is not for the use of money or for a forbearance but is for a *sale of credit* to him by the obligee. The principal involved is set forth by the court in *Chakales v. Djiovanides.*[30] There, the court stated that one may sell his credit to a borrower for a consideration, and to that end may endorse, guarantee or become a surety for the payment of a loan made to the borrower by third persons at an interest rate determined without regard to the usury laws; the arrangement will not render usurious either the contract for the sale of credit or the loan made by the third party.

The particular cases to be analyzed fall into two areas, namely, (1) the guarantee and (2) the furnishing of credit and financing for the benefit of the borrower.

The Guarantee. An agreement guaranteeing payment of a loan is not usurious, regardless of the amount charged by the guarantor for the loan of his credit (through his guarantee) for the reason that the charge is not for the use of money or for a forbearance.

In *White v. Anderson,*[31] plaintiff sold coupons to customers who would use them in lieu of cash or other credit to purchase goods from local merchants. The merchants accepted the coupons pursuant to an agreement with plaintiff and on presentment of the coupons, plaintiff paid the respective merchant. Upon purchasing the coupons, defendant signed a promissory note in favor of plaintiff for the full amount of the credit furnished plus five percent of such amount. The five percent bonus was an absolute sum, and there was no adjustment based on the period of time for which credit was to be extended. Defendant contended that the charge was usurious. On the other hand, plaintiff argued that he was doing nothing more than furnishing his credit; thus, the transaction was outside the scope of usury. The court found that the essential nature of the transaction was not the guarantee or sale of credit

30. 161 Va. 48, 170 S.E. 848 (1933).
31. 164 Mo. App. 132, 147 S.W. 1122 (1912).

but was a loan (evidenced by the promissory note). Therefore, the transaction was usurious. The court pointed out:

> The one important feature which the transaction lacks of being a sale of credit, such as in the sale of a guaranty or endorsement, is that in those instances there is no advance of money made by the guarantor or endorser to or for the party guaranteed or endorsed and he still owes the debt; while in this case there is an advance of money for the defendant by the plaintiff in full discharge of his debt and he does not owe anything to the merchant, but does owe the plaintiff. When he gave plaintiff his note, ostensibly for coupons, it was, in reality, for the money which plaintiff used in paying for his goods.[32]

In summary, a charge for a guarantee is not an interest charge for the purpose of determining usury if the charge relates solely to the providing of credit or security to the borrower; that is, the charge is for furnishing credit and not for the use of the guarantor's money. The money is obtained from a third party.[33]

Furnishing Credit and Financing. In the second group of cases, one party furnishes his credit to a second party to assist the second party in acquiring goods from a third party. Courts have distinguished these cases on the theory that the charges made are for the sale (or furnishing) of credit, rather than for a loan, and thus are not interest charges for purposes of determining usury.

A frequently cited case is *Oil City Motor Company v. C.I.T. Corporation*,[34] a decision based on Oklahoma law. In that case, plaintiff was an auto dealer selling cars at retail upon terms other than cash. Since that method of operation required more cash than plaintiff had available, plaintiff entered into a *Floor Plan* agreement with defendant. Under the plan, plaintiff would draw sight drafts on defendant to pay for new vehicles purchased from the manufacturer. Prior to shipping of the automobiles to plaintiff, the manufacturer would deliver the trust receipt and draft to defendant in Detroit who then paid the amount of the draft to the manufacturer. Upon receipt of the car, plaintiff reimbursed defendant for 10 percent of the purchase price and gave to defendant plaintiff's 90-day accepted draft for the balance. The court found that defendant lent or extended its credit which plaintiff used in the operation of its business; the consequent charge to plaintiff was for the extension of credit, as distinguished from a loan. Thus, the court held that the transaction did not constitute a loan of money, and there was no usury.

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32. *Id.* at 138, 147 S.W. at 1124.
33. GMAC v. Weinrich, 218 Mo. App. 68, 262 S.W. 425 (1924); Grannis v. Temple, 84 Misc. 415, 146 N.Y.S. 239 (1914).
34. 76 F.2d 589 (10th Cir. 1935).

A second case involving the same issue is *Klett v. Security Acceptance Company.*[35] There, defendant furnished trust receipt financing to plaintiff in an amount equal to 90 percent of the manufacturer's sales price for furniture inventory acquired by plaintiff. Defendant would pay for the furniture, and upon its delivery to plaintiff, plaintiff would execute a trust receipt, acknowledging that he was holding title to the furniture in trust for defendant and that the furniture could only be released from the trust upon payment in cash for it. Ordinarily, the inventory remained subject to the trust receipt until it was sold by plaintiff. However, if defendant repossessed the furniture and sold it to satisfy the debt, any surplus from the sale would be the property of the Trustee (plaintiff); a deficiency, if any, would be paid by plaintiff to defendant. For the financing described above, defendant charged to plaintiff a charge of 1 percent per month for the total financing furnished during that month. The court held that the monthly charge was for the furnishing of financing, not for a loan or forbearance, and thus did not constitute interest for purposes of determining usury.

The court in *Klett* distinguishes the *Oil City Motor Company* case, indicating that the latter was excluded from the usury laws because it was based upon an extension of credit and not a loan.[36] The court indicated that the *Klett* transaction was excluded from the usury laws because the charge by the defendant was for the financing arrangement (that is, furnishing financing), not for a loan. The argument certainly seems to create a distinction without a difference. The financing arrangements in the two cases were very similar, and to the extent that the theory excluding those cases from the usury law is sound, it is because the obligee furnished (or sold) its credit to the obligor.

A very recent case in California has placed the status of the problem in doubt. In *Burr v. Capital Reserve Corp.*,[37] defendant used his credit to acquire certain personal property for plaintiff who could not otherwise obtain the credit. Defendant borrowed the money from Union Bank, purchased equipment and leased it

35. 38 Cal. 2d 770, 242 P.2d 873 (1952).
36. *Id.* at 783, 242 P.2d at 882.
37. Civil No. 32067 (2nd Dist. Court of App., Dec. 13, 1968), 74 Cal. Rptr. 141 (1968).

to plaintiff. Pursuant to the agreement with the bank, defendant also was obligated to repay the loan. Plaintiff gave a trust receipt for the equipment to the bank. The appellate court found that the entire transaction was a financing arrangement, not a loan, and in reliance on the *Klett* decision ruled that the charges by defendant, although in excess of 10 percent per annum, were not interest within the scope of the usury statute.[38]

However, the California Supreme Court reversed the lower appellate court decision in *Burr*,[39] holding that the lease arrangement, in fact, constituted a loan from defendant to plaintiff and the usury laws applied. Most important, the supreme court in its decision completely ignored the argument that the interest was paid other than for a loan or forbearance. Thus, at the present time in California, if flooring or similar financing is furnished, the issue is in doubt as to whether charges for such financing are interest within the scope of the usury laws.

Regardless of the arguments used by the courts in the *Oil City Motor Company* and *Klett* cases, and the lower appellate court in the *Burr* case, there appears to be a serious question of whether charges under those cases should be outside the scope of usury. In all three cases, there was a debtor-creditor (loan) transaction between the parties as of the moment the debtor took possession of the goods purchased. The utilization of trust receipts in all three cases merely furnished security to the party actually advancing the purchase money. And the primary obligation in all three cases was to the person furnishing the credit. The situation does not appear to be unlike that in *White v. Anderson*[40] where the person furnishing credit (through the sale of coupons) also took back a promissory note from each purchaser of the coupons. There, the court found that the charge to the purchaser was upon the accompanying promissory note (loan) and applied the usury law. The situation in the above cases is significantly different than the *guarantee* cases where the guarantor did not furnish the money but merely furnished his credit as surety.

2. *Charges Included Within Interest.*

Generally, any compensation, remuneration or other benefit exacted by a lender as a part of a loan (or forbearance) transaction is *interest*.[41] The imagination of lenders has caused such

38. *Id.*
39. Burr v. Capital Reserve Corp., 71 Cal. 2d 983, 80 Cal. Rptr. 345, 458 P.2d 185 (1969).
40. 164 Mo. App. 132, 147 S.W. 1122 (1912).
41. CAL. CIV. CODE § 1915 (West 1954).

benefits to take many different forms, undoubtedly due (in part) to the presence of the usury laws and apparent attempts to avoid the limitations of such laws.

Perhaps the best approach to defining *interest* is to state generally what charges or benefits are not *interest* for purposes of determining usury. In most states, payments by the borrower to or for the benefit of the lender of reasonable expenses incidental to the loan and as consideration for it are not *interest* charges.[42] All other benefits paid to the lender or accrued or applied for his benefit will be *interest*.[43]

In 1967, the State of Maryland adopted a different approach in determining what is *interest*.[44] If a fee or charge is retained by the lender, whether or not it was for an expense incurred in respect to the loan, it is *interest*. Only if the lender is a mere conduit, collecting money to pay independent and unrelated parties, will the fee not be *interest*.[45]

In comparing the two approaches, it appears that the major conflict pertains to the treatment of internal expenses of the lender, for example, charges for house counsel or an in house appraiser. Under the Maryland approach,[46] if these charges are retained by the lender, they are interest. If similar specific charges are retained by lenders in other states, it is possible that the charges may not be deemed *interest*.

Even in the great majority of states where reimbursement of internal expenses is not per se *interest*, it is far easier for the court to justify such charges if the borrower had full knowledge of the facts and agreed in advance to the payment.[47] Furthermore, reimburse-

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42. Haines v. Commercial Mortgage Co., 200 Cal. 609, 254 P. 956 (1927); Klett v. Security Acceptance Corp., 38 Cal. 2d 770, 242 P.2d 873 (1952); Silver Homes, Inc. v. Marx & Bensdorf, Inc., 206 Tenn. 361, 333 S.W.2d 810 (1960).

43. Mong v. Bass, 248 Cal. App. 2d 377, 56 Cal. Rptr. 579 (1967); Charlotte Guyer and Associates v. Franklin Factors, 211 Cal. App. 2d 690, 27 Cal. Rptr. 575 (1963).

44. ANN. CODE OF MD. art. 49, § 1(a)(b) (Supp. I, 1969) *amending* ANN. CODE OF MD. art. 49, § 1 (Replacement Vol. 1968).

45. B.F. Saul Co. v. West End Park North, Inc., 250 Md. 707, 246 A.2d 591 (1968).

46. *Id.*

47. Rossberg v. Holesapple, 128 Utah 544, 260 P.2d 563 (1953). The court held that the reimbursement of travel expenses incurred by the lender in

ment must be for specific expenses. A charge to compensate the lender for a portion of his overhead has been generally held to be an additional interest charge.[48]

Interest most frequently is defined by that term in the debt instrument. However, *interest* also generally includes points, bonuses, commissions, and origination and closing fees paid to or for the benefit of the lender, to the extent that any such payments do not constitute reimbursement of expenses which the borrower has agreed to pay.[49]

The issue of what is *interest* can best be summarized by reference to two California cases. In the case of *In re Fuller*[50] the court held that the usury law operates only as a limitation upon the *interest* which a lender may charge and does not exclude, regulate or limit legitimate expenses or service charges that may be borne by the borrower when incurred in connection with the loan transaction. In the case of *Mong v. Bass*,[51] the lender had attempted to recover a *documentary charge* of $25.00 per month for each car upon which the lender had furnished trust receipt financing. The court also found that the particular charge was not related to a specific recoverable expenditure, stating:

> The record here supports the determination that the $25 was a general charge not attributable to any particular service. The expenses which plaintiff has described are a part of the necessary cost of doing business by anyone who is engaged in automobile financing. A lender who makes a flat charge in excess of the legal rate of interest may not defend a usury charge merely by showing that he had some business expenses which reduced his net profit to a figure within the legal rate of interest.[52]

Commissions. A particular problem arises in determining whether the commission paid by the borrower to the lender or to an agent is *interest* to the lender. Clearly, a commission paid directly to the lender is interest.[53] However, whether a commission paid to an agent is included within the interest income attributable to the lender generally depends upon whether the agent was acting for the

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investigating the loan application constituted "interest" since reimbursement had not been agreed upon in the loan application agreement.

48. Vee Bee Service Co. v. Household Finance Corp., — Misc. 2d — 51 N.Y.S.2d 590 (Sup. Ct. 1944), *aff'd mem.* 269 App. Div. 772, 55 N.Y.S.2d 570 (1945); Gangadean v. Flori Investment Co., 11 Ariz. App. 512, 466 P.2d 63 (1970).

49. B.F. Saul Co. v. West End Park North, Inc., 250 Md. 707, 246 A.2d 591 (1968).

50. 15 Cal. 2d 425, 433-34, 102 P.2d 321, 329-31 (1940).

51. 248 Cal. App. 2d 377, 56 Cal. Rptr. 579 (1957).

52. *Id.* at 383-84, 56 Cal. Rptr. at 584.

53. Wheeler v. Superior Mortgage Co., 160 Cal. App. 2d 246, 325 P.2d 156 (1958).

lender or for the borrower.

An illustrative case is *Clarke v. Hornay*.[54] In that case, the lender employed an agent to renegotiate an existing loan. The new agreement was executed establishing a loan in the amount of $23,000, bearing interest at the rate of ten percent per annum, all due and payable in eight months. The borrower was required to pay a $4,000 commission to the lender's agent for negotiating the loan. The court held that the loan was usurious, pointing out that: "the exaction of a commission from the borrower by the lender's agent will render the transaction usurious on the facts described if such exaction is known to and authorized or ratified by the lender."[55] In adding the agent's commission to the lender's interest, the court reasoned that the borrower was paying the lender's obligation; thus, the benefit derived constituted additional interest income to the lender.

Suppose, however, that the lender's agent obtains the commission without the knowledge or consent of the lender. A review of the cases in that instance indicates that in a majority of jurisdictions, the commission is not deemed a part of the lender's interest.[56]

Suppose that the commission is paid by the borrower to his own agent. Under those circumstances, generally the commission is not an *interest* charge.[57] As the court pointed out in *Altschul v. Martin*,[58] the decisive question is one of agency. The court stated:

> It is settled by our decisions that if such a broker is the borrower's agent his fee is not treated as interest on the loan, but the rule is otherwise if the broker is the lender's agent.[59]

Suppose that the borrower's agent, in order to obtain a loan, agrees to split his commission with the lender, thus providing an additional benefit to the lender. Generally, the share received by the lender is deemed additional interest to the lender for purposes of determining whether usury exists.[60] However, in *Pushee v.*

54. 212 Cal. App. 2d 307, 27 Cal. Rptr. 901 (1963).
55. *Id.* at 310, 27 Cal. Rptr. at 903, *quoting* Penziner v. West American Finance Co., 133 Cal. App. 578, 589, 24 P.2d 501, 506 (1933).
56. Harrell, *Mortgage Investments and the Usury Problem*, 10 CLEV.-MAR. L. REV. 343 (1961).
57. Klein v. Mathewson, 384 Pa. 298, 121 A.2d 577 (1956).
58. 227 Ark. 816, 301 S.W.2d 571 (1957).
59. *Id.* at 818, 301 S.W.2d at 573.
60. Jones v. Philippe, 135 Ark. 578, 206 S.W. 40 (1918).

Johnson,[61] the Florida Supreme Court held that where the agent and the lender had no pre-arranged plan and the burden on the borrower is not increased, the lender's share of the commission did not constitute *interest* for purposes of the usury statute. The court reasoned that under the circumstances, the sharing of the commission served a useful purpose (inducing the loan).[62]

Other Charges Found to be Interest. In the portion of this article entitled "Special Situations",[63] a number of different types of transactions are discussed which raise the issue of whether the lender (if a loan is involved) has derived a benefit which may not appear to be interest on the face of the loan documents or whether the lender has derived a benefit out of a collateral transaction. Under certain circumstances, the additional benefit will be construed as interest for purposes of determining usury.

3. *Charges Not Included Within Interest.*

Earlier in this article, there was discussed the particular types of benefits which may be interest. It was pointed out that any compensation, remuneration or other benefit exacted by the lender will be deemed interest unless the charge is to reimburse or compensate the lender for a specific expenditure or service which he is entitled to recover without it being considered interest. In *Klett v. Security Acceptance Co.*,[64] the California Supreme Court stated the rule to be as follows. In order for the charge not to be considered interest, it:

> [M]ust be confined to a specific service or expense incidental to the loan incurred in such a way as to preclude it being a device through which additional interest or profit on the loan may be exacted.[65]

Not only must the charge be related to a specific service, but as a general rule it also must be reasonable in amount in relation to the actual services rendered incidental to procuring the loan. Generally, courts also will be concerned with whether the borrower gave his prior consent and agreement to compensate the lender for the particular expenses.[66]

Generally, to assist the lender in recovering expenses without such recovery being deemed *interest*, the following four rules should be followed. First, where possible, the lender should at-

61. 123 Fla. 305, 166 So. 847 (1936).
62. *Accord*, Patterson v. Blomberg, 196 N.C. 433, 146 S.E. 66 (1929).
63. See text accompanying notes 166-76, *infra*.
64. 38 Cal. 2d 770, 242 P.2d 873 (1952).
65. *Id.* at 787-88, 242 P.2d at 884.
66. For a general discussion, see § 11:5 Annot., 91 A.L.R.2d 1391 (1963).

tribute and relate the fee to an actual out-of-pocket expense incidental to the loan. Secondly, the charge should be classified and defined according to some service or expense commonly used and accepted in the lending community for services related to obtaining a loan.[67] Thirdly, the expense should be reasonable in relation to the service rendered. Fourthly, the borrower, where possible, should agree in advance to the payment of the expense.

With the above general considerations in mind, specific categories of charges related to loans normally not deemed *interest* will be reviewed.

Loan Origination and Closing Expenses. Loan origination and closing expenses generally are those costs incurred by the lender in investigating, making, and consummating the particular loan. Examples of such charges are: appraisal fees, title examination costs, title insurance, attorney's fees, costs of preparing loan documents, escrow fees and recording fees. To the extent that charges to the borrower meet the four rules previously stated, the charges herein described should not be *interest* for purposes of determining usury.

Under circumstances of the particular cases, the following charges have been found to be legitimate expenses, not included within *interest.*

1. A property inspection fee to reimburse the lender for its expenses in inspecting the property.[68]

2. Title examination fees and traveling expenses paid to an independent attorney and inspector designated by the lender.[69]

3. FHA insurance premium.[70]

4. Charges for Mechanic's Lien insurance (premium retained by the lender who was to issue the insurance) and

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67. Ideally, the category of expense is one where the courts have determined that the charge may be passed on to the borrower without it being classified as "interest".
68. Winston v. Personal Finance Co. of Pine Bluff, 220 Ark. 580, 249 S.W.2d 315 (1952).
69. Mathews v. Georgia State Savings Association, 132 Ark. 219, 200 S.W. 130 (1918).
70. Silver Homes, Inc. v. Mark & Bensdorf, Inc., 206 Tenn. 361, 333 S.W. 2d 810 (1960).

completion insurance.[71]

5. Broker's fee or other compensation paid to a third person and appraisals, recording fees and insurance charges.[72]

6. A charge for supplying supervision during the course of construction if the charge bears a reasonable relation to the cost normally of such charges.[73]

Expenses During Term of Loan. The lender is entitled to recover for reasonable expenses incurred during the course of the loan (for example, inspection and disbursement expenses incurred during construction) and it may be possible to exact such expenses in advance.[74] Ideally, of course, the payment of such charges for future services should be agreed upon at the time the loan is negotiated.

Charges Payable by Borrower Upon Default. Charges payable by the borrower upon default would include a reasonable default charge, foreclosure and title costs and attorney's fees incurred by the lender. The prevailing rule in most jurisdictions is that such charges are not *interest* within the meaning of the usury statute since the incurrence of the expense is within the control of the borrower.[75]

In the case of *Abbot v. Stevens,*[76] the California court (in dealing with the related issue of prepayment penalties), stated that where the charge is under the borrower's control, its payment by the borrower does not make the transaction usurious. And in another California case, the court held that attorney's fees incurred by the trustee and beneficiary of the deed of trust prior to its foreclosure is a legitimate expense chargeable to the borrower and is not *interest* within the meaning of the usury statute.[77]

A case dealing particularly with the late charge is *Camilla Cotton*

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71. Hance Hardware Co. v. Denbigh Hall, Inc., 17 Del. Ch. 234, 152 A. 130 (1930).

72. *In re* Fuller, 15 Cal. 2d 425, 434, 102 P.2d 321, 330 (1940); *but see* limitations discussed on brokers' and agents' fees paid in a manner to benefit the lender. See text accompanying notes 53-62, *infra.*

73. Altherr v. Wilshire Mortgage Corp., 104 Ariz. 59, 448 P.2d 859 (1968); Modern Pioneers Insurance Co. v. Nordin, 103 Ariz. 125, 437 P.2d 658 (1968).

74. Haines v. Commercial Mortgage Co., 200 Cal. 609, 618-19, 254 P. 956, 965-66 (1927); Klett v. Security Acceptance Corp., 38 Cal. 2d 770, 787-88, 242 P.2d 873, 890-91 (1952).

75. Prather, *supra* note 28.

76. 133 Cal. App. 2d 242, 284 P.2d 159 (1955).

77. Penziner v. West American Finance Co., 10 Cal. 2d 160, 180-81, 74 P.2d 253, 272-73 (1937).

Oil Company v. Spencer Kellog and Sons, Inc.[78] There, the plaintiff brought an action under Georgia law to recover the balance due on a promissory note. The lender included in its complaint a claim for late charges based upon a provision in the promissory note which read as follows:

> If for any reason any of said payments are not made promptly on the date due, a late charge of five cents per $1.00 of the payment in default will be made and shall be added to the annual payment when paid . . . .[79]

The court held that the charge is solely within the control of the borrower, there being no late charge if the loan payments had been paid when due. Therefore, the loan was not usurious.

Prepayment Penalties. Frequently, the loan agreement provides that if the borrower elects to prepay a portion or all of the principal obligation, he must pay a premium or penalty. The courts generally have held that such charges are not *interest* for purposes of determining usury, justifying the results upon two theories. First, since the contingency is solely within the control of the borrower (in the absence of coercion by the lender), the penalty is not interest for purposes of determining usury.[80] Secondly, other courts have reasoned that the charge is not for the use or forbearance of money but is for the privilege of terminating the indebtedness and the obligation to pay interest.[81]

Commitment Fees. Cases interpreting commitment fees and the legal theories which create the obligations of the parties to perform under a commitment fee agreement vary widely.[82] Nevertheless, it appears that if a true commitment fee is involved, the charge is not for the use of money and thus is not interest for purposes of determining usury.[83]

78. 257 F.2d 162 (5th Cir. 1958).
79. *Id.* at 163 n.2.
80. Abbot v. Stevens, 133 Cal. App. 2d 242, 284 P.2d 159 (1955); Glushorn, *The California Usury Law: The Lender's Trap and the Borrower's Windfall,* 43 J. STATE BAR CAL. 56 (1968).
81. *See* Webb v. Southern Trust, 227 Ky. 79, 11 So. 2d 988 (1928); Lyons v. National Savings Bank, 280 App. Div. 339, 113 N.Y.S.2d 685 (1952); Atlantic Life Ins. Co. v. Wolf, 54 A.2d 641 (D.C. Mun. Ct. App. 1947); Feldman v. Kings Hwy., 278 App. Div. 589, 102 N.Y.S.2d 306 (1951); McCarty v. Mellinkoff, 118 Cal. App. 11, 4 P.2d 595 (1931).
82. Wolf, *The Refundable Commitment Fee,* 23 BUS. LAWYER 1065 (1968).
83. Pivot City Realty Co. v. State Savings & Trust Co., 88 Ind. App. 222,

An excellent description of the commitment fee and the application of the usury laws generally is found in *The Business Lawyer*[84] wherein it is stated:

> The commitment fee buys a commitment; the fee paid is not "for the use of money," but for the privilege later of actually borrowing the money. It is an option, not a loan. There is a risk involved to the lender for which it is equitable that he be paid. In committing to lend money in the future, the lender is taking a risk that the yield, rate committed for, and security terms will not be less favorable at the time the loan actually is made than at the time of the commitment. Most certainly if the committed loan never is made, no question of usury could be raised. Indeed, this demonstrates even more clearly that the prospective borrower has bought something other than money, namely, the right to secure a loan of money if he later decides he wants it. In some instances mortgage lenders choose to refund the commitment fee if the loan actually is made. If this is done, of course, there could be no involvement with the usury laws, at least with respect to the fee . . . .[85]

Suppose, however, that the lender attempts to exact an unusually high commitment fee as a means of obtaining an additional profit on his loan in the event the loan is made. Two recent cases shed considerable light on whether (under those circumstances) the fee will be deemed *interest* for determining if usury exists.

In the first case, *D & M Dev. Co. v. Sherwood and Roberts, Inc.*,[86] defendant Sherwood and Roberts, Inc., entered into an agreement with the prospective borrower (D & M Dev. Co.) to make or obtain three commitments for loans in respect to a shopping center development as follows: (1) a land loan for $306,000; (2) an interim construction loan for $1,650,000; and (3) a permanent loan for $1,650,000. In exchange for obtaining the commitments, the developer paid a commitment fee of $56,250. The developer obtained the land loan but did not utilize either of the other loans because it had obtained more favorable loans elsewhere.

The developer then sued Sherwood and Roberts, Inc., claiming that the commitment fee constituted interest which made the total interest charge on the land loan usurious. The court held that the fee was not *interest*, indicating that a commitment fee is not "for the use of money" but for the privilege (option) of later actually obtaining the loan. The court indicated that the purpose of the commitment is to transfer the risk of the money market from the borrower to the lender; however, the fee must be reasonable and not out of line with the going rate within the commercial com-

162 N.E. 27 (1928); Paley v. Barton Savings and Loan Association, 82 N.J. Super. 72, 196 A.2d 682 (1964).

84. Prather, *supra* note 28.

85. *Id.* at 188.

86. 93 Idaho 200, 457 P.2d 439 (1969).

munity. By its decision, the court ruled that unreasonable compensation for the commitment could constitute an extra interest payment on the accompanying loan for the purposes of determining usury.

The second recent case in respect to commitment fees was *Altherr v. Wilshire Mortgage Corp.*[87] In that case, the court in dictum indicated that a reasonable commitment fee is not interest; however, an unreasonable commitment fee can be a cloak for usury. The court stated that the reasonableness of the fee requires an ad hoc approach. Pertinent factors are: the tightness or looseness of money, the amount of the fee and the rates prevailing in the money market where the lender might keep his funds while waiting for the borrower to call for the loan. And what would be a reasonable fee at one time might be an unreasonable fee at another.

In summary, a reasonable commitment fee is not a charge for the use of money but for the commitment to obtain a loan in the future; thus, it is not an *interest* charge for purposes of determining if usury exists. The test of whether the fee is reasonable is explained in the *Altherr* case.

Builder's Payment. Suppose that the builder makes a payment to the lending institution to obtain a loan for a prospective purchaser. Probably the payment will not be construed as interest since it is not made strictly for a loan or forbearance but is made to obtain a commitment.[88]

4. *A Description of the Methods Utilized to Compute Interest.*

After the various items of interest have been ascertained, it must be determined whether the lender's charges are usurious. That is, does the total interest to be earned exceed the legal limits of the applicable usury statute?

The general formula for determining whether usury exists was set forth by the court in *Penziner v. West American Finance Co.*[89] There the court first computed the actual profit (that is, interest) paid to the lender. The court next determined the maximum amount which the lender was permitted to charge pursuant to the

87. 104 Ariz. 59, 448 P.2d 859 (1968).
88. Prather, *supra* note 28; RESTATEMENT OF CONTRACTS § 531 (1932).
89. 10 Cal. 2d 1960, 74 P.2d 252 (1937).

usury law over the actual life of the loan. Since the actual interest charged exceeded the legal maximum amount allowed, the loan was usurious.

In applying the general formula described above, a number of special problems may arise. Certain special problems will be discussed below.

Compounding Interest. Interest at the maximum rate allowed by law may be compounded no more frequently than annually.[90] And, keep in mind that interest is not compounded unless compounding is expressly provided for.[91]

Points, Discounts, Bonuses and Interest in Advance. Points, discounts and bonuses constitute interest unless the charge is supported by an expense which the law allows the lender to pass on to the borrower. In almost all instances it is the practice of lenders to deduct such charge from the loan proceeds prior to disbursement of the proceeds to the borrower.

The courts generally have followed the rule that interest taken in advance (including points, discounts and bonuses to the extent that they constitute interest) shall be deducted from the face amount of the loan to determine the net proceeds. Interest for purposes of the usury statute is computed on the net proceeds.[92]

The decisions are split on the issue of whether the taking of interest in advance at the maximum rate constitutes usury. In some jurisdictions, the usury statute will indicate that interest taken in advance for not longer than the first year will not be deducted from the face of the loan to determine net proceeds. In other jurisdictions, the courts have condoned the practice because of the custom and practice in the banking community, and the courts will not discriminate between banks and other creditors.[93]

In some jurisdictions, where interest at the maximum rate was payable quarterly or monthly in advance, it was held to be usurious.[94] However, if the borrower voluntarily pays the interest in advance for reasons other than contractual compulsion there is no usury.[95]

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90. Heald v. Friis-Hansen, 52 Cal. 2d 834, 839, 345 P.2d 457, 461 (1959); Haines v. Commercial Mortgage Co., 200 Cal. 609, 616, 254 P. 956, 958 (1927).

91. Haines v. Commercial Mortgage Co., 200 Cal. 609, 616, 254 P. 956, 958 (1927).

92. Devers v. Greenwood, 139 Cal. App. 2d 345, 293 P.2d 834 (1956).

93. Annot., 57 A.L.R.2d 630, 657 (1958).

94. Purvis v. Frink, 57 Fla. 519, 49 So. 1023 (1909); Paillet v. Wroman, 52 Cal. App. 2d 297, 126 P.2d 419 (1942); Taylor v. Budd, 217 Cal. 262, 18 P.2d 333 (1933).

95. 79 Ariz. 381, 290 P.d 735 (1955).

The courts generally require that discounts, points, bonuses and loan charges (which are deemed to be interest but are deducted in advance) to be amortized over the life of the loan for the purposes of determining usury.[96]

Computation on the Net Proceeds. The principle (discussed above) that interest is to be computed on the net funds made available to the borrower relates to two other lending practices; namely, (1) the *wrap-around* or *all-inclusive loan* and (2) *compensating balances.*

The first example of computing interest on the net funds made available pertains to the *wrap-around* or *all-inclusive loan.* To illustrate, suppose the owner of property elects to borrow money in the sum of $20,000, using the property as security for the loan. The property already is encumbered wth a first trust deed or mortgage securing a note with an unpaid balance of $10,000 which is on advantageous terms and which the owner would like to preserve. He obtains a new lender who will make an all-inclusive loan. The new lender advances the sum of $20,000 but takes back a promissory note in the sum of $30,000. As a part of the transaction, the new lender agrees to make the debt-service payments on the $10,000 obligation. The advantage to the new lender is that he will charge interest on the full $30,000. The advantage to the borrower is that he will preserve the advantageous existing financing.

The principle is illustrated in the case of *Mindlin v. Davis.*[97] There, the plaintiff owned property encumbered by a mortgage note of $1,488. Defendant loaned plaintiff $3,300; however, defendant retained $1,488 with which he agreed to pay off the mortgage note. Defendant failed to pay off the mortgage note, but instead made the required debt service payments on it. The interest rate charged on the loan was not usurious if computed on the $3,300, but if it was computed on the net funds made available to plaintiff ($1,812), it clearly was usurious. The Florida court held that the loan was usurious since interest is computed on the net funds made available to plaintiff.[98]

96. Brown v. Cardoza, 67 Cal. App. 2d 187, 192, 153 P.2d 767, 769-70 (1944); B.F. Saul Co. v. West End Park North, Inc., 250 Md. 707, 246 A.2d 591 (1968).
97. 78 So. 2d 789 (Fla. 1954).
98. *Id.* On the other hand, the lender might argue that the assumption

In *Mindlin*, the borrower did not consent to the manner in which the lender elected to pay off the principal of the prior indebtedness. In the normal *wrap-around loan*, the borrower has consented to the overall plan of payment. Regardless of that distinction, however, the rule of the case is well taken. There appears to be no case dealing with the application of usury to the *wrap-around loan* since the *Mindlin* decision.

The second example of computing interest on net funds made available pertains to *compensating balances.* On occasion, a lender will require a portion of the loan funds (or other funds) to be placed or retained in a bank account in a manner to derive a particular benefit for the lender. Suppose (at the same time) the lender is earning interest at the maximum legal rate on the particular loan.

The *Restatement of Contracts*[99] indicates that if the lender requires a compensating balance (upon which no interest is paid) and it is maintained on the terms described above, the loan is usurious for the reason that the lender has obtained an advantage from the collateral bargain for which he gives no equivalent.[100]

The case of *Planters' National Bank of Virginia v. Wysong & Miles Co.*,[101] supports the *Restatement* position. There, plaintiff bank made a loan with the understanding and agreement that it would retain twenty percent of the amount loaned as a deposit of the defendant borrower in the bank. The deposit was not subject to withdrawal by the borrower but was held in a general account in its name. At the same time, plaintiff bank charged interest at the maximum legal rate on the total loan. The court found that the transaction was usurious, the lender having derived a gain in excess of that allowed by law.

A second case in point is *Vee Bee Service Co. v. Household Finance Corp.*[102] There, the lending bank caused five percent of the loan to be set aside as security for risk of loss due to nonpayment. Interest computed on the net funds made available exceeded the statutory limit. The court stated: "The risk of nonpayment is inherent in every loan and may be compensated for only out of the

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of the underlying first mortgage is a consideration which is either a part of or independent of the transaction and sufficient to support the additional interest charge.

99. RESTATEMENT OF CONTRACTS, Explanatory Note 2, § 528 (1932).

100. Suppose, however, that the normal interest rate payable at the bank to its customers is paid on the compensating balance. Such payment might alter the results.

101. 177 N.C. 380, 99 S.E. 199 (1919).

102. 51 N.Y.S.2d 590 (Sup. Ct. 1944).

statutory interest allowed."[103] The court pointed out that *interest* is the compensation for (1) the inconvenience of parting with principal and (2) the hazard of losing principal. Loss of principal through the insolvency of the borrower is the ordinary risk for which the lender is compensated by the payment of interest. It is not a risk that justifies interest beyond the legal limit. The court then went on to hold that the lender cannot charge the legal maximum interest rate on the full amount of the loan where it requires that a portion of the loan proceeds remain in its possession as security for the loan's repayment; the borrower did not receive the use of the full sum on which interest was being charged.

However, the court in *Deposit Guaranty National Bank v. Shipp*[104] reached a contrary result. There, plaintiff bank made loans but withheld 10 percent from the loans as "compensating balances." Such sums were deposited in the bank (in a non-interest-bearing account) to the credit of the borrower but could not be withdrawn without the consent of the bank. The court held that the loan was *not* usurious; the compensating balances were the property of the borrower and, as security for the loan, could be liquidated to pay the indebtness. Thus, the compensating balances were not deducted from the face amount of the loans for the purpose of determining the actual interest rate.

The last case clearly appears to be out of line with the general rules in the United States that (1) interest is computed on the net funds made available to the borrower and (2) the lender will be held responsible (in determining whether usury exists) for any unusual benefit obtained from a collateral transaction.

Delay in Delivery of Principal to Borrower. If the delay is inadvertent and the lender volunteers to correct for the overcharge of interest, generally the courts will find that there is no usury.[105] On the other hand, if the scheme of payment is such that the total loan is not delivered, interest will be computed on the net proceeds made available to determine usury.[106]

103. *Id.* at 599.
104. 205 So. 2d 101 (La. Ct. App. 1967).
105. Mindlin v. Davis, 78 So. 789 (Fla. 1954); Shaffran v. Holness, 93 So. 2d 94 (Fla. 1957).
106. Penziner v. West American Finance Co., 10 Cal. 2d 160, 74 P.2d 252 (1937).

Statutes Describing More Than One Legal Rate. Most usury statutes distinguish between written contracts where interest is specified and other obligations where it is unspecified. A problem arises in written contracts where the interest is unspecified, and where the effective rate is in excess of the maximum rate prescribed by statute for oral contracts. In *Orlando v. Berns*,[107] the contract was in writing but purported to be a *sale*. The court found the contract to be a loan but applied the rate applicable to written contracts. Thus, in California, if the contract is in writing, interest need not be specified in order to apply the maximum rate (10 percent). The law in other states may depend upon the specific language of the statute.

5. *A Description of Certain Loan Transactions Involving Interest Charges Outside the Scope of Usury.*

Certain loans, although involving charges which may or will be deemed interest, are outside the scope of usury. Several examples are explained below.

The Lender's Recovery is Subject to Special Hazards. Suppose that the loan transaction provides that the lender is to receive as a part (or all) of his interest for the loan a share in the profits or rents from the property of the borrower. If the potential recovery to the lender may exceed the legal maximum interest rate, the transaction will be usurious unless the recovery is subject to substantial contingencies or hazards.

The principle is set forth in the *Restatement of Contracts*.[108] Where the promise (made in consideration of a loan) is conditioned upon a contingency that may provide the lender with a profit in excess of the maximum statutory limit, the loan is not usurious if the repayment would be materially less than the maximum statutory limit if the contingency did not occur.

In a recent California case, *Tommassen v. Carr*,[109] the lender made a very speculative loan to a real estate speculator who was in poor financial condition. The loan was subordinated to a construction loan. The lender was to receive in return for his loan, repayment of all principal plus 30 percent of the net profits from the operation and sale of the property. The lender also obtained an opinion from prominent legal counsel that the loan was not usurious. The court held that the loan was not usurious, reasoning that

107. 154 Cal. App. 2d 753, 316 P.2d 705 (1957).
108. RESTATEMENT OF CONTRACTS, § 527 (1932).
109. 250 Cal. App. 2d 341, 58 Cal. Rptr. 297 (1967).

the venture was extremely speculative and the lender was taking a real gamble that he would recover nothing more than the principal. As it worked out, he ultimately recovered interest in excess of the maximum (10 percent) usury limit.

In *American Insurers v. Regenold*,[110] the lender made a loan for $18,000 secured by land worth twenty times that amount. In addition to repayment of principal, he was to receive six percent interest plus one-half of the net profits on the sale of the land. The loan was negotiated under circumstances of extreme need, and the court found that a large profit on the sale of the land was reasonably certain. It further found that no special hazard existed. The court stated that if the probability of the contingency of loss is remote, or if it does occur, the diminution of the profits is slight as compared to the possible profit, the loan is usurious.[111]

In summarizing the *Tommassen* and *American Insurers* cases, it appears that the court weighs the upside risk of gain versus the downside risk of loss measured from the point of the maximum legal interest rate limitation in the particular jurisdiction.

Suppose that the contingency is a cost-of-living index applied to the principal. Would it make any difference whether adjustments were upwards only?[112]

Once Non-Usurious, Always Non-Usurious. Numerous cases cite the principle that if the loan transaction is non-usurious at its inception, it will remain non-usurious under all circumstances (except for an amendment of the agreement). The principle is illustrated by two cases.

In *Penzer v. Foster*,[113] the debtor allowed the loan to go into default for a substantial period of time. The note was non-usurious at its inception and would have remained so had the debtor complied with its terms. However, when the interest was compounded after default (pursuant to the agreement) the interest recovered exceeded the aggregate maximum recovery allowed by the usury statute for the life of the loan. The court held that the loan was

110. 243 Ark. 906, 423 S.W.2d 551 (1968).

111. *See also*, Jameson v. Warren, 91 Cal. App. 590, 267 P. 372 (1928); Martyn v. Leslie, 137 Cal. App. 2d 41, 290 P.2d 58 (1955); Maze v. Sycamore Homes, 230 Cal. App. 2d 746, 41 Cal. Rptr. 338 (1964).

112. *See* 18 HAST. L.J. 973 (1967).

113. 170 Cal. App. 2d 106, 338 P.2d 533 (1959).

non-usurious, reasoning that a loan which was non-usurious at its inception could not be made usurious by the default of the borrower.

In *Mong v. Bass*,[114] the lender made a profit upon the sale of repossessed vehicles which the trustee in bankruptcy for the borrower claimed was additional interest for purposes of determining usury. The court held, however, that the transaction was not usurious. The court stated[115] that in order for the contract to be usurious, it must require the payment of usury at its inception. The debtor cannot subject his credit to the penalties of the usury laws by his voluntary default in respect to the obligation where there was no violation of the law present at the inception of the contract.

C. Wrongful Intent.

The third element of usury is that there must be an intention by the lender to exact an illegal charge. Where the agreement is clearly usurious on its face, the intention to violate the law is "conclusively presumed." It is sufficient that by the terms of the contract the lender was willing to accept more interest than the law allows.[116] Further, usurious intent is established by the amount of interest the borrower has agreed to pay—not what he has actually paid.[117]

There are two situations where the general rule (that is, that usurious intent is conclusively presumed) does not apply. The first situation pertains to the agreement which is unclear on its face or which does not purport to be a loan. There, the court will make a finding that usurious interest was present.[118] The second situation pertains to the transaction where there has been (1) a bona fide error or miscalculation, (2) a minimum of damage, and (3) a rectification of the situation upon discovery. In the second situation, some courts have indicated that there is no usurious intent.[119]

III.

EXEMPTIONS FROM THE USURY LAWS

Certain major areas are frequently exempted by the laws of the

114. 248 Cal. App. 2d 377, 56 Cal. Rptr. 579 (1957).
115. *Id.* at 384, 56 Cal. Rptr. at 584.
116. Martin v. Ajax Constr. Co., 124 Cal. App. 2d 425, 269 P.2d 132 (1954).
117. Wood v. Angeles Mesa Land Co., 120 Cal. App. 313, 7 P.2d 748 (1932).
118. Maze v. Sycamore Homes, Inc., 230 Cal. App. 2d 746, 41 Cal. Rptr. 338 (1964).
119. Shaffran v. Holness, 93 So. 2d 94 (Fla. 1957). *See* Prather, *supra* note 28 at 196; RESTATEMENT OF CONTRACTS § 537 (1932).

various states from the application of usury. Important areas discussed in this part III are: (A) the corporate borrower exemption, (B) the business purpose exemption, (C) FHA loans, and (D) the purchase money exemption. A fifth major area to be discussed is the special treatment frequently provided for banks and savings and loan associations (see Part IV below).

A. The Corporate Borrower Exemption.

The most important and prevalent exemption to the usury laws deprives corporate borrowers of the defense of usury on a transaction otherwise subject to the usury laws. The exemption (found in 32 states)[120] appears in different forms. In some states, as New York,[121] the corporation is merely denied the defense of usury. In some states the law applies different maximum rates to individuals and to corporations. In a third group of states, there is absolutely no interest limitation applied to corporations. And in a fourth group of states, the corporate borrower exemption applies only if the loan exceeds a certain amount.[122]

Suppose that the lender (in order to make a loan) requires the borrower to incorporate solely for the purpose of avoiding the usury laws. Will the court pierce the corporate veil to find that the borrower was (in fact) an individual (that is, the shareholder)? There is a split in the decisions.

In New York, it makes no difference that the borrower was required to form his corporation solely to avoid the usury laws.[123] However, in the leading case of *Jenkins v. Moyse*,[124] the court indicated that the lender could not agree to make the loan to the individual and then use the corporation to conceal the usurious transaction. The lender would have to take the position from the beginning of negotiations that the loan would be made only to a corporation.

In New Jersey and Florida, on the other hand, if the lender requires the debtor to form a corporation for the sole purpose of act-

120. *See* Addendum *infra.*
121. N.Y. GEN. OBLIGATIONS LAW § 5-521 (McKinney 1964).
122. *See* Addendum *infra.*
123. Leader v. Dinkler Management Corp., 20 N.Y.2d 393, 230 N.E.2d 120 (1967).
124. 254 N.Y. 319, 172 N.E. 521 (1930).

ing as the borrower, the courts will pierce the corporate veil, holding that the individual (shareholder) is the borrower.[125] It also appears that the courts in Arizona may question whether the borrower was a viable corporation created by the borrower for a purpose other than to avoid the application of the usury laws.[126]

B. Business Purpose Exemption.

The second exemption (applicable in at least three states) exempts loans made "for a business purpose" from the usury laws.[127] Each state which may subsequently adopt the *Uniform Consumer Credit Code* as presently drafted also will exclude business or commercial loans.[128]

C. FHA Loan Exemptions.

Statutes in at least twenty-six states exclude FHA insured loans from the application of the usury laws.[129]

D. Purchase-Money Credit Obligations.

Most usury statutes in the United States generally have been patterned after the Statute of Anne, requiring that there be a loan or forbearance.[130] Thus, if the debt obligation arose out of a purchase and sale, rather than a loan or forbearance, many courts have ruled that the usury laws do not apply. The justification for the exemption is that, unlike the loan or forbearance, a sale does not normally involve a necessitous borrower in the hands of a rapacious lender.[131]

To determine whether the exemption may apply in any particular state, the respective usury statute should be examined. For instance, the Iowa statute applies the law of usury to "any contract founded upon any sale or loan of real or personal property."[132] In states broadening the coverage of their usury laws beyond the loan

125. *In re* Greenberg, 21 N.J. 213, 121 A.2d 520 (1956); Atlas Subsidiaries v. O. & O. Inc., 166 So.2d 458 (Fla. Dist. Ct. App. 1964).

126. Gangadean v. Flori Investment Co., 11 Ariz. App. 512, 466 P.2d 63 (1970). For a good article on this subject *see* Hershman, *Usury and the Tight Mortgage Market—Revisited*, 24 Bus. Lawyer 1121 (1969) [hereinafter cited as Hershman].

127. Ill. Rev. Stat. ch. 74, § 4 (Supp. I, 1970); Ann. Code of Md. art. 49, §§ 1-11 (Replacement Vol., 1968); Vt. Stat. Ann. tit. 9, §§ 41, 46, 50 (Supp. 1968).

128. *See* Hershman, *supra* note 126 at 1121-25.

129. *See* Prather, *supra* note 28 at 193.

130. Williston, *supra* note 6, § 1682 at 4754-55 (Rev., 1958).

131. Hafer v. Spaeth, 22 Wash.2d 378, 156 P.2d 408 (1945); GMAC v. Weinrich, 218 Mo. App. 68, 262 S.W. 425 (1924).

132. Iowa Code Ann. § 535.4 (1962).

or forbearance, the usury laws may be applied to debt obligations arising out of purchases and sales.

Even in states applying the purchase-money exemption to the usury laws, cases should be distinguished where the purchase-money credit obligation (subject to the exemption) is altered, amended, or extended by a subsequent agreement. In *London v. Toney*,[133] the parties entered into a credit sales transaction. Subsequently, for a fee, the seller extended the time of payment of the mortgage debt. The court held that the subsequent transaction was a new agreement (constituting a forbearance) and was subject to the usury laws.

Definition of Purchase Money Credit Obligation. Since the exemption applies to purchase and sale transactions, the cases have limited the exemption to purchase money credit obligations.[134] *Purchase money* has been defined as the monies paid by the vendee to the vendor in payment of the purchase price of property. It includes the down payment, as well as the debt, if any, payable to the vendor arising out of the purchase transaction.[135] The portion of the purchase price other than the down payment is the purchase-money credit obligation.

Although the purchase-money obligation may be in the name of the seller, the situation should be examined when the financing is furnished by a third party. As an example, suppose the seller of an automobile takes back the security agreement or conditional sales contract arising out of the sale, but he immediately sells or discounts it to a finance company pursuant to a pre-arranged agreement. In *Grand Island Finance Co. v. Fowler*,[136] the buyer argued that the seller was the agent of the finance company and that usury should apply. The court found that no such agency existed but it did *not* indicate that the theory of agency was not available.

Suppose that *A* Corp. sells property to a buyer and the sale is financed by *B* Corp. (a wholly-owned subsidiary of *A* Corp.). The vendor did not itself extend credit, and the credit obligation runs from the buyer to *B* Corp. It would appear that if *A* Corp. and *B*

133. 263 N.Y. 439, 189 N.E. 485 (1934).
134. Verbeck v. Clymer, 202 Cal. 557, 261 P. 1017 (1927).
135. Eyster v. Hathaway, 50 Ill. 521, 99 Am. Dec. 537 (1864); Heuisler v. Nickum, 38 Md. 270 (1873).
136. 124 Neb. 514, 247 N.W. 429 (1933).

Corp. elected to do business in the manner herein described, they must take the consequences with the benefits. It appears likely that the debt obligation arose out of a loan (made by *B* Corp.), rather than the sale (by *A* Corp., the parent), and the law of usury would apply.

Application of the Purchase-Money Credit Exemption. Virtually all states having statutes patterned after the Statute of Anne follow the general rule that it makes no difference that the sales price on a credit sale exceeds the cash-sales price.[137] A seller may charge one price if the sale is for cash and a higher price if the sale is upon credit. The difference between the two prices is not relevant to the issue of usury since the courts indicate that usury does not apply to a credit obligation arising out of a purchase and sale transaction.

Suppose, however, that the purchase money credit obligation calls for the payment of interest in excess of the statutory limit, or, due to the manner in which the contract is drawn, it is clear that the sales price includes such an interest charge. There is a split of decisions as to whether usury applies to the transaction.

The leading case in California is *Verbeck v. Clymer.*[138] In that case, *P* sold land to *D* for $20,000, *D* paid $5,000 down and was to pay the balance ($15,000) in monthly payments of $200 for 180 months. Even though the seller clearly was charging interest in excess of California's usury limit, the court held that California's usury law did not apply for the reason that the credit obligation was a purchase-money trust deed note. Thus, in California it makes no difference that the interest charged by the seller on a purchase money credit obligation exceeds the legal rate.[139]

In other states, however, the courts have treated the credit-sale agreement and the debt obligation as two separate obligations, regardless of the fact that they are integral parts of the same agreement. As an example, see *G.F.C. Corp. v. Williams.*[140] There, the court stated that independent of the sales arrangement, if the financing arrangement of the deferred balance includes an interest

137. Rose v. Wheeler, 140 Cal. App. 217, 35 P.2d 220 (1934); Wilson v. J.E. French Co., 214 Cal. 188, 4 P.2d 537 (1931); Verbeck v. Clymer, 202 Cal. 557, 261 P. 1017 (1927); Atlas Securities Co. v. Copeland, 124 Kan. 393, 260 P. 659 (1927); WILLISTON, *supra* note 6 at § 1685.

138. 202 Cal. 557, 261 P. 1017 (1927).

139. For a similar holding, *see* Wilson v. J.E. French Co., 214 Cal. 188, 4 P.2d 537 (1931); *and* Atlas Securities Co. v. Copeland, 124 Kan. 393, 260 P. 659 (1927).

140. 231 S.W.2d 565 (Tex. Civ. App., 1950).

charge in excess of the legal limit, the transaction is usurious.[141]

At the present time, the law in the State of New York (as evidenced by lower court decisions) appears to be in conflict. In *Congress Financial Corp. v. Patti*,[142] the court held that the usury law did not apply to a credit-sales transaction, regardless of what interest rate may be charged. On the other hand, in *Raben v. Overseas Barters, Inc.*,[143] and in *Mandolino v. Fribourg*,[144] the courts held that the extension of credit in a credit sale constituted *forbearance*, and the usury laws applied.

In the *Raben* case, the court analogized the situation to the case of *London v. Toney*.[145] However, in that case, there was a true forbearance because subsequent to the credit-sales transaction, the parties entered into a new agreement extending the time of payment of the debt in exchange for a fee.

There appears to be no justification in holding that the deferred balance is an independent obligation (constituting a forbearance) which is subject to usury. In fact, a California court has expressly held that there is no forbearance under the circumstances.[146] If the transaction is exempt because it involves a credit sale, rather than a loan or forbearance, then it should make no difference that the credit sale also calls for the payment of interest in any amount. In states where the lender's credit obligation is deemed a forbearance, the lender would merely have to raise the price of the credit sale to compensate himself in the manner which he would otherwise seek compensation by way of additional interest. It seems that nothing is gained by the cases calling the credit obligation a *forbearance* except a trap for the unwary.

The basis of excluding the credit sale from the usury laws is that it does not involve the needy borrower and the rapacious lender.[147] The bargaining power of the parties is on a more equal basis, and they should have the freedom to negotiate the terms of the sale

141. For a similar holding, *see* GMAC v. Weinrich, 218 Mo. App. 68, 262 S.W. 425 (1924).
142. 26 App. Div. 2d 924, 274 N.Y.S.2d 711 (1966).
143. 55 Misc. 2d 618, 286 N.Y.S.2d 404 (Sup. Ct. 1967).
144. 29 App. Div. 2d 675, 287 N.Y.S.2d 611 (1968).
145. 263 N.Y. 439, 189 N.E. 485 (1934).
146. Upton v. Gould, 64 Cal. App. 2d 814, 149 P.2d 731 (1944).
147. Hafer v. Spaeth, 22 Wash. 2d 378, 156 P.2d 408 (1945); GMAC v. Weinrich, 218 Mo. App. 68, 262 S.W. 425 (1924).

without limitation. The courts have indicated that a seller may contract to sell his property at any price and upon whatever terms he may obtain.[148] To apply the usury law to any aspect of the credit sale transaction will limit the terms of sale, including the interest rate, upon which the parties might otherwise agree.

IV.

Special Statutory Treatment For Banks And Certain Savings Institutions

Banks and savings institutions frequently are singled out for preferred treatment. Examples are as follows:

In California, all banks and building and loan associations are exempt from the usury laws.[149]

In New York, if a non-institutional lender makes a usurious loan, it is void. If a bank or savings institution makes a usurious loan, it may recover the principal of the loan, but all interest is forfeited and the lender is liable for double damages based on the interest actually received.[150]

Because banks and savings institutions frequently obtain special treatment as described above, other lenders may seek the benefit of such special treatment by (1) purchasing loans from the bank or savings institution, or (2) participating in the making of any such loan. To examine the legal position of the parties, three possible situations will be examined. For purposes of the illustration, it is assumed that the applicable usury law exempts loans by any bank or savings institution from its coverage. And except for such exemption, the loans would be usurious. Those situations are:

Illustration One. An exempt lender makes the loan without relying upon or contemplating a subsequent participation in the loan by a non-exempt lender. Subsequently, the non-exempt lender purchases all (or a portion) of the loan.

Illustration Two. The exempt lender and the non-exempt participant jointly organize and commit to make the loan under circumstances in which the exempt lender is unwilling (alone) to make the loan.

Illustration Three. The participant organizes the loan package and submits it to the exempt lender. The exempt lender is to act as

148. Wilson v. J.E. French Co., 214 Cal. 188, 4 P.2d 537 (1931).
149. Cal. Const. art. XX, § 22 (1919); Larwood v. San Diego Federal Savings & Loan Association, No. 237216 (S.D. Sup. Ct., Nov. 18, 1960).
150. N.Y. Gen. Obligations Law § 5-511 (McKinney 1964).

lender for a fee solely, or primarily, to avoid the application of the usury laws.

The liability for usury will be examined in two aspects, namely, (1) the non-exempt participant's liability and (2) the exempt lender's liability, and it is anticipated that the non-exempt lender may purchase a substantial portion of the loan contract.

The Non-Exempt Participant's Liability.

In *Illustration One,* the loan is not usurious in its inception because it is made by an exempt lender. The issue is: Following the purchase of the obligation (or of an interest therein) by a non-exempt participant, does the accrual and payment of interest in excess of the legal limit to the participant constitute a violation of the usury laws? There appears to be no case authority directly on point.

In order to find liability on the part of the non-exempt lender, one would have to assume that (subsequent to the purchase) the interest paid to the participant is usurious. Assuming that there is usurious interest, the assignee of the contract will be liable for the usurious benefits he has received unless he is a holder in due course.[151] Of course, one cannot be a holder in due course if the obligation on its face calls for usurious interest or if the holder (prior to his acquisition of the loan) otherwise learns that the loan is usurious.

Under the circumstances of *Illustration One,* probably the better view is that the interest paid to the non-exempt participant is not usurious. Three arguments support the conclusion.

1. The purpose of the usury law is to protect the necessitous borrower in dealing with the rapacious lender.[152] The time at which the usury law is intended to apply is at the inception of the loan transaction. The point is illustrated by the situation where a purchaser of property assumes a usurious loan made to the seller and secured by the property. The purchaser cannot raise the defense of usury because it is not available to him. He was not a party to the transaction at the time that the usury law afforded its

151. Calimpco, Inc. v. Warden, 100 Cal. App. 2d 429, 224 P.2d 421 (1950).
152. Cases cited at note 144 *supra.*

protection.[153]

In *Illustration One*, the non-exempt participant acquired the interest in a loan that was theretofore exempt. He was not a party to the transaction at its inception, and the policy of the usury law would not be served by subsequently subjecting him to its penalties. Viewing the other side of the coin, commerce (the sale of notes and the flow of money) will be promoted by not applying the usury law to the transaction.

2. There is considerable authority under other circumstances that if a loan is non-usurious at its inception, it will remain non-usurious for the life of the loan.[154] Thus, upon the acquisition of an interest in the loan by a non-exempt participant, the loan would remain non-usurious even though the subsequent interest payments exceeded the maximum statutory limit.

3. In an analogous situation, the Insurance Commissioner obtained an opinion from the Attorney General of the State of California on the issue of whether an insurer could take as an assignee a promissory note given by the insured to a bank to finance the payment of an insurance premium. The interest rate charged by the bank was in excess of the usury limit. The Attorney General rendered his opinion that the usury laws of the State of California would not be violated.[155]

It would appear that the Attorney General's opinion is based on sound law, provided that there is a valid transaction between the borrower and the bank. The effect of the opinion is questioned, however, if the bank's usury exemption is used merely to obtain interest in excess of the maximum legal limit for the benefit of the non-exempt participant.

Summarizing the arguments in respect to *Illustration One*, although there is no authority directly in point, it would seem that if a non-exempt lender obtains a participation in the loan under the circumstances stated, the loan is not usurious.[156]

In *Illustration Two*, the non-exempt lender participates directly

153. Read v. Mortgage Guarantee Co., 11 Cal. App. 2d 137, 53 P.2d 377 (1936).

154. Penzner v. Foster, 170 Cal. App. 2d 106, 338 P.2d 533 (1959); Mong v. Bass, 248 Cal. App. 2d 377, 56 Cal. Rptr. 579 (1967).

155. 50 Op. Cal. Att'y Gen. 110 (1967).

156. The contrary proposition is not true, however. Where the bank purchased two usurious notes from a non-exempt lender, the loans being void under Nebraska law at their inception, the court held that the notes were void in the hands of the bank. Hills v. Burnett, 172 Neb. 370, 109 N.W.2d 739 (1961); Robertson v. Burnett, 172 Neb. 385, 109 N.W.2d 716 (1961).

in making the loan. Whereas there appears to be no authority directly on point, probably the portion of the loan attributable to the non-exempt lender, being that portion on which it earns interest in excess of the maximum legal limit, would be usurious. Since the usurious benefits are limited to those received by the non-exempt lender, it would not appear that (a) the exempt lender received usurious interest or (b) the non-exempt lender is liable for the interest received by the exempt lender.

In *Illustration Three,* it is clear that to the extent of the participation by the non-exempt lender, the involvement of the exempt lender's name has been primarily for the purpose of avoiding the usury law.

In *Coral Gables First National Bank v. Constructors of Florida Inc.*[157] a national bank made a loan with the obvious intention of assigning a major portion of the loan to a state bank. The national bank's assets did not allow it legally to make a loan of the size involved. The note was usurious, and if Florida law applied, there was a loss of principal as well as interest. However, if federal law applied, damages were limited to double the interest actually received, and all other interest was forfeited. The state bank argued that because the loan was made by a national bank, federal law[158] applied to determine the damages attributable to the state bank's share of the loan. However, the court held that the national bank was a mere *conduit* for the funds of the state bank and applied Florida law to determine the penalties resulting to the state bank.

In summarizing the non-exempt lender's prospective liability under *Illustrations Two* and *Three,* it is likely that the benefits derived from the transaction by the non-exempt lender will be deemed usurious.

The Exempt Lender's Liability.

In referring to the three illustrations, an analysis must now be made regarding the liability of the exempt lender to the extent that usury, if any, is involved.[159] Keep in mind that a common fact

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157. 110 So. 2d 741 (Fla. Dist. Ct. App. 1960).
158. 12 U.S.C.A. § 86 (1945).
159. The analysis in this Article is limited to prospective civil liability; aspects of potential criminal liability are not discussed.

assumed in all of the illustrations was that the applicable usury law (such as that found in California[160]) exempts loans of the lender (bank or savings institution) from its provisions. Thus, the only usury that can be involved is that which may accrue to the non-exempt lender.

In California, it is clear that the exemption of lenders within the specified class relates to all provisions of the usury laws.[161] Thus, the exempt lender cannot be directly liable as a principal for receiving more interest than allowed by the usury law. However, it must be determined whether the exempt lender can be vicariously liable for the activities of the non-exempt lender in receiving usurious interest.

Referring back to the illustrations, the conclusion in reference to *Illustration One* was that there was no usurious interest involved. However, in the latter two illustrations, the law probably is to the contrary. The latter illustrations also raise the issue of whether the exempt lender is liable as a partner, joint venturer, agent or conspirator with the non-exempt lender.

As was pointed out in *Clarke v. Horany*,[162] usury is a statutory devise and liability can be imposed only by the express language of the statute. In that case, the court held that a defendant (agent) was not liable for usurious interest because the California statute did not impose liablity on an agent, abettor, or conspirator of the offending creditor.[163]

However, the California statute does place vicarious liability on partners of the individual responsible for the loan, regardless of whether the partner participated in making the loan.[164] Thus, if the court found that the two lenders were partners or joint venturers, it is possible that the exempt lender might be vicariously liable for the usurious interest paid to the non-exempt participant.

In summary, it appears that the exempt lender is not liable for the usurious interest received by the non-exempt lender on the basis that he was an agent of the non-exempt lender or a co-conspirator to exact usurious interest for the benefit of the non-exempt lender. However, if the facts indicate that the two lenders are partners or joint venturers, the exempt lender could be liable for the usurious interest collected by the non-exempt lender.

160. CAL. CONST. art. XX, § 22 (1919).
161. Carter v. Seaboard Finance Co., 33 Cal. 2d 564, 203 P.2d 758 (1949).
162. 212 Cal. App. 2d 307, 27 Cal. Rptr. 901 (1963).
163. For a similar holding *see* Penziner v. West American Finance Co., 10 Cal. 2d 160, 74 P.2d 252 (1937).
164. Calimpco, Inc. v. Warden, 100 Cal. App. 2d 429, 224 P.2d 421 (1950).

V.

SPECIAL SITUATIONS

In utilizing the principals previously outlined in this article, lenders, on occasion, have attempted to avoid or circumvent the usury laws by (A) entering into a *purchase and sale* with a lease-back and option, or (B) deriving an unusual benefit out of a collateral transaction. Each of these areas will be examined.

A. *Purchase and Sale.*

Frequently, a transaction is couched in terms of a *purchase and sale* with an accompanying lease-back and option or obligation of the seller to repurchase the property at some time in the future. Because of the manner in which the transaction was set up, the court has found that no *purchase and sale* was ever intended; that, in fact, the parties used the language of a purchase and sale to disguise a loan. Three cases illustrate the point.

In *Martyn v. Leslie*,[165] defendants loaned money to plaintiff at 6 percent interest. In addition, defendants purchased a 15 percent interest in plaintiff's television shows for $500. At the same time, defendants granted plaintiff an option to repurchase the interest for $8,000. Two independent parties were required to execute a guarantee that if plaintiff did not exercise the option the guarantors would buy the portion of the business subject to the option for $8,000. The court held that the transaction was a loan and the difference between the fair market value of the option and the actual value of the business was additional interest for purposes of the usury statute.

In *Orlando v. Berns*,[166] defendants purchased property from plaintiff for $178,000, also granting to plaintiff an option to repurchase the property for $200,000. The actual fair market value of the property conveyed to defendants was $292,000. The court held that the transaction was a loan after determining that the sale and option prices had no relation to the fair market value of the property; thus, the parties could not have intended the transaction to be a purchase and sale.

165. 137 Cal. App. 2d 41, 290 P.2d 58 (1955).
166. 154 Cal. App. 2d 753, 316 P.2d 705 (1957).

In *Golden State Lanes v. Fox*,[167] defendant purchased a leasehold estate from plaintiff for $150,000. The cash was placed in a joint account to pay for improvements to the property. Plaintiff then subleased the premises for eight years and agreed to repurchase premises at the end of eight years for $150,000. The repurchase was guaranteed by two individuals. In discussing whether the transaction constituted a sale or a loan, the court stated that a sale is the transfer of property for a price. The transfer is the essence of the transaction. The transfer is general and absolute in nature. A loan, on the other hand, is the delivery of money under a contract to return it at a future time. The court found that the parties entered into a loan transaction.

In conclusion, the court in each of the three cases readily looked through the form to reach the substance, finding that the parties had actually entered into a loan agreement. The court thereupon applied the law of usury. It is clear, also, that in determining whether usury is present in such cases, the courts ignore the parol evidence rule and (where necessary) have held that the rule is inapplicable.[168]

B. Benefits Derived from Collateral Transactions.

The parties to a loan agreement may enter into a collateral transaction, possibly to accomplish some function complementary to the loan. For instance, where flooring financing or a loan is obtained by a merchant, the party furnishing the monies may require the merchant to "discount" (that is, sell back) his *paper* obtained from customers to the financing party. In such instances, if the profit on the discount is unusually large, the court may hold that the collateral advantage obtained constitutes additional interest on the loan.[169]

The *Restatement of Contracts*[170] describes a number of collateral transactions where a collateral advantage, if abnormally large, could constitute additional interest on the accompanying loan. For instance, in conjunction with a loan, suppose (1) the borrower is employed by the lender at an unusually low salary, (2) the borrower is required to purchase shares of stock from the lender at an

167. 232 Cal. App. 2d 135, 42 Cal. Rptr. 568 (1965).
168. Haines v. Commercial Mortgage Co., 200 Cal. 609, 254 P. 956 (1927); Martyn v. Leslie, 137 Cal. App. 2d 41, 290 P.2d 58 (1955); Abbott v. Stevens, 133 Cal. App. 2d 242, 284 P.2d 159 (1955); Murphy v. Ablow, 123 Cal. App. 2d 853, 268 P.2d 80 (1954); Vee Bee Service Co. v. Household Finance Corp., 51 N.Y.S.2d 590 (Sup. Ct. 1944).
169. Terry Trading Corp. v. Barsky, 210 Cal. 428, 292 P. 474 (1930).
170. RESTATEMENT OF CONTRACTS § 528 and Explanatory Notes (1932).

unusually high profit to the lender, (3) the borrower agrees to purchase from the lender all of the goods he will require of a particular type for the following year or (4) the lender requires the borrower to deposit a compensating balance (without interest) for the benefit of the lender.

Suppose that an insurance company enters into a transaction with a developer as follows: (1) the insurance company will purchase the land from the developer and lease it back to him, normally at a rental based on a percentage of the cost of the land plus a portion of the building rentals from the property; and (2) the insurance company will make the necessary long-term loan to finance the development of the property. If the insurance company derives an unusually high ground-rent (compared to competitive ground rentals in the area), it is arguable that it has derived an unusual collateral advantage attributable to the accompanying loan for purposes of determining usury.

VI.

Rights And Liabilities Of The Parties

Previously, this article has dealt with the rights and liabilities of the principals involved directly in the transaction. Now the relationship of a number of other parties to the loan transaction will be examined.

A. *Right of Guarantors to Plead Usury.*

The right of the guarantor to raise the defense of usury depends upon the law applicable to the maker (borrower) in the same transaction. In states (such as California) where the defense of usury is available to all borrowers, it is available to all guarantors.[171] On the other hand, in states where the defense is not available to the borrower, for example, a corporate borrower, it is not available to the guarantor.[172]

B. *Liability of Partners for Usury.*

Partners are jointly and severally liable on loans made by one

171. Martin v. Ajax Constr. Co., 124 Cal. App. 2d 425, 431, 269 P.2d 132, 135 (1954).
172. Cabrera v. Olsen, 165 Misc. 374, 300 N.Y.S. 524 (Sup. Ct. 1937).

partner on behalf of the partnership. Where the loan was made by one of several partners, all of the partners were liable for the usurious nature of the transaction and it was not necessary that they join in or ratify the loan.[173] The theory on which the decisions are based is that all three of the partners benefited from the loan.[174]

C. Liability of Officer or Director of Lender for Usurious Loan.

The defense of usury was not available at common law. Thus, the right to assert usury arises only by statute.[175] Under California law, a director or officer who violates the usury law is personally liable for damages incurred by the corporation.[176]

D. Liability of Agent of Lender for Usury.

Since the defense of usury is strictly statutory, the language of any applicable statute must be examined. Under the California statute, the agent of the lender is not designated as a liable party; thus, in California, the agent is not liable for the usurious loans of his principal.[177]

E. Liability of an Assignee of a Note for Usury.

Where an assignee of the promisee's interest in a promissory note has received usurious benefits, he will be liable for damages unless he is a holder in due course in which event the original payee is the proper party defendant.[178]

F. Availability of Defense of Usury to Party Assuming Obligation.

Generally, a person who has purchased real property and as a part of the purchase price assumed and agreed to pay an existing encumbrance thereon is estopped to raise the defense of usury in respect to the encumbrance.[179] However, suppose an accommoda-

173. Calimpco, Inc. v. Warden, 100 Cal. App. 2d 429, 224 P.2d 421 (1950); Vee Bee Service Co. v. Household Finance Corp., 51 N.Y.S.2d 590 (Sup. Ct. 1944); Robertson v. Merwin, 154 App. Div. 713, 139 N.Y.S. 726 (1913).

174. However, since the law of usury is statutory, the result in some jurisdictions may vary from that set forth above because of a strict interpretation of the relevant usury statute.

175. Clarke v. Horany, 212 Cal. App. 2d 307, 310-11, 27 Cal. Rptr. 901, 904 (1963).

176. CAL. CIV. CODE § 1916-3 (West 1954).

177. Clarke v. Hornay, 212 Cal. App. 2d 307, 27 Cal. Rptr. 901 (1963).

178. Calimpco, Inc. v. Warden, 100 Cal. App. 2d 429, 224 P.2d 421 (1950).

179. Read v. Mortgage Guarantee Co., 11 Cal. App. 2d 137, 53 P.2d 377 (1936).

tion party assumes the obligation with the consent of the lender in such a manner that there is a novation (that is, the new party actually is substituted for the original debtor). Under those circumstances, the new debtor would have the right to assert usury in respect to the transaction.[180]

G. Right of Junior Encumbrancer to Assert Claim of Usury.

Suppose that the person is merely a junior encumbrancer on certain property, and the usurious loan secured by a senior encumbrance on the same property is in default. The person's only remedy is to cure the default. He cannot raise the defense of usury nor sue to recover for usurious damages.[181]

VII.

PENALTIES FOR VIOLATION OF THE USURY LAWS

One the violation is established, the court will be called upon to impose the penalty. An understanding of the source, nature and extent of such penalties includes: (A) an analysis of the source of law applicable to the usury violation, (B) a determination of the limitations on damages in usury cases, and (C) a determination of the discretion in the trial court to vary the penalty within the statutory requirements.

A. Source of Law Applicable to the Usury Violation.

Cases generally in the United States indicate that since there was no usury at common law, the law governing usury is statutory.[182] Thus, resort is made solely to the applicable statute to determine the penalties to be applied.

In all instances (except where the liable party is a national bank) the law applicable in determining civil penalties is state law. As can be seen from the Addendum following this article, there is a

180. Rodecker v. Littauer, 59 F. 857 (8th Cir. 1894); Plitt v. Kaufman, 188 Md. 608, 53 A.2d 673 (1947); Doster v. English, 152 N.C. 339, 67 S.E. 754 (1910).

181. Barnes v. Hartman, 246 Cal. App. 2d 215, 54 Cal. Rptr. 514 (1966).

182. Clarke v. Hornay, 212 Cal. App. 2d 307, 27 Cal. Rptr. 901 (1963); Coral Gables First National Bank v. Constructors of Florida, Inc., 119 So. 2d 741 (Fla. Dist. Ct. App. 1960).

wide variation of penalties among the various states. In many states, there is a forfeiture of all interest, while in other states the lender forfeits either a multiple of all interest or the excess interest. In several states there is a forfeiture of a percentage of the principal plus all interest. Finally, a number of states provide for a forfeiture of all principal and interest.

The law applicable to national banks is federal law. Almost without exception, it has been held that a national bank is subject only to the penalties set forth in Section 86 of the National Banking Act.[183] One exception to the general rule, however, is found in the cases of *Robertson v. Burnett*[184] and *Hills v. Burnett*[185] discussed earlier. There, a private lender made two usurious loans. Under Nebraska law, the loans were void. Thus, when the private lender sold those notes to the Michigan National Bank, the bank acquired void obligations. The Nebraska court held that since those notes were void at their inception, they also were void in the hands of the bank. Thus, on the narrow fact situaton of those two cases, state law determined the effective penalty applicable to the national bank.

B. *Limitations on Damages in Usury Cases.*

Suppose that as a result of a particular usurious transaction, the borrower suffered substantial consequential damages. Can the borrower recover such damages solely on the basis that the damages resulted from the usurious charges?

The issue was covered in *Coral Gables First National Bank v. Constructors of Florida, Inc.*[186] There, the court held that the plaintiff could not obtain an award of consequential damages resulting from a violation of the usury statute; that his only damages to which he was entitled as a result of the violation of the usury statute were the penalties prescribed by statute. The court pointed out that but for the usury statute, the loan was legal, indicating that the subject of usury was one entirely of statutory regulations and prohibition.

Thus, it appears that the court can invoke no penalty on the usurious lender other than that penalty prescribed by the applicable statute.

183. 12 U.S.C.A. § 86 (1945); *See* 45 AM. JUR. 2d, *Interest and Usury* § 308 (1969) for a discussion of usury penalties applicable to national banks.

184. 172 Neb. 385, 109 N.W.2d 716 (1961).

185. 172 Neb. 370, 109 N.W.2d 739 (1961).

186. 119 So. 2d 741 (Fla. Dist. Ct. App. 1960).

C. An Analysis of the Discretion of the Trial Court to Vary the Penalty Within the Statutory Requirement.

Historically, the courts have rigidly applied the provisions of the applicable usury statute, levying on the usurious lender the full statutory penalty. The defense of *pari delicto* has been expressly held to be not available in usury cases.[187] However, the courts in two recent cases have indicated that the trial court has some discretion in adjudging punitive damages.

In *White v. Seitzman*,[188] the court indicated that the borrower could be estopped from recovering all or a portion of his damages where he had initiated the transaction. The court based its reasoning upon the theory of relative guilt.

In *Golden State Lanes v. Fox*,[189] upon a retrial of the damages issue, the trial court found that the lender was two-thirds guilty and the borrower was one-third guilty, thereby rendering a judgment to the borrower for double damages (instead of the treble damages allowed by California law).

The policy of the law in all jurisdictions is to protect the borrower. Where the borrower has been instrumental in engineering the transaction, he should not be able to benefit therefrom, especially where he is the prime mover and dictates the terms.

187. Martyn v. Leslie, 137 Cal. App. 2d 41, 290 P.2d 58 (1955); Seebold v. Eustermann, 216 Minn. 566, 13 N.W.2d 739 (1944).
188. 230 Cal. App. 2d 756, 41 Cal. Rptr. 359 (1964).
189. 232 Cal. App. 2d 135, 42 Cal.Rptr. 568 (1965).

ADDENDUM

STATE	LEGAL RATE	MAXIMUM RATE	PENALTY FOR USURY	QUALIFICATIONS AND EXEMPTIONS	
ALABAMA	6%	8%	Forfeiture of all interest, and the borrower may recover any interest actually paid.	Loans to corporations for more than $10,000 but less than $100,000 have maximum rate of 15%. Loans over $100,000 to corporations are exempt. Industrial Development Boards and Medical Clinic Boards meeting statutory standards are exempt.	ALA. CODE tit. 9, §§ 60, 65-67, tit. 37, §§ 825(1), 858 (1) (1969).
ALASKA	6%	4 percentage points above federal reserve discount rate in the 12th Fed. Res. Dist. (until 2/15/72, then set at 8%).	Double damages for interest paid by borrower. All other interest is forfeited.	State Banks, Federal Banks and State chartered savings and loan associations are exempt.	ALASKA STAT. tit. 45, §§ 45, 45.030, .040 (1962); ALASKA STAT. tit. 45, § 45.45.010 (1962), *as amended*, (Supp. I, 1970).
ARIZONA	6%	10%	Forfeiture of all interest, and any interest paid may be recovered or applied against principal indebtedness.	Where obligation is in writing, corporation may be required to pay up to 1-1/2% per month on loans over $5,000.00.	ARIZ. REV. STAT. ANN. §§ 44-1201 to -1203, 10-177 (1970).
ARKANSAS	7%	10%	All principal and interest forfeited.		ARK. CONST. art. 19, § 13; ARK. STAT. §§ 68-602, -608, -609 (1957).

CALIFORNIA	7%	10%	Treble damages for interest paid by borrower, and forfeiture of all other interest. Usury is a misdemeanor.	State Chartered Building and Loan Associations; certain Industrial Loan Corporations; credit unions; National and State Chartered Banks, and Agricultural Cooperatives, are exempt from the usury laws.	CAL. CONST. art. XX, § 22; CAL. CIV. CODE § 1916-1, -2, -3 (West 1954).
COLORADO	5%	None above $1,500 as long as loan agreement is in writing. (Licensing requirement if lender is making loans in excess of 12%.) 12% below $1,500.	Forfeiture of all interest, and the borrower can recover treble damages for interest paid within the preceding year. Usury is a misdemeanor.	Banks, trust companies, savings and loan associations, savings banks, industrial banks, credit unions and pawn-brokers are exempt from the usury laws.	COL. REV. STAT. §§ 73-1-1, -3, 73-2-7, -9, 73-3-3 (1963).
CONNECTICUT	6%	12%	Forfeiture of all principal and interest; except that borrower cannot recover anything paid. Usury is a misdemeanor.	Banks, trust companies, and notes in excess of $5,000 secured by a mortgage or real property are exempt from the usury laws.	CONN. GEN STAT. §§ 37-1, -2, -4, -7, -8, -9 (1958).
DELAWARE	6%	8%, where secured by mortgage or trust deed.	Borrower may recover any interest paid in excess of the legal rate.	Special provisions for loans of less than $500. Corporations cannot plead the defense of usury.	DEL. CODE ANN. tit. 6, § 2306 (1953), tit. 6, §§ 2301 & 2304 (1968).
DISTRICT OF COLUMBIA	6%	8%	All interest is forfeited and, if paid, recoverable by borrower, and any interest paid may be used to set off a portion of the unpaid principal.	Loans to corporations are exempt from usury laws.	DIST. OF COL. CODE §§ 28-3303, to -3305, 29-904 (h) (1961).

FLORIDA	6%	10%	Double damages for interest actually paid; forfeiture of all other interest. If interest charged is greater than 25%, both interest and principal are forfeited and the violation is a misdemeanor.	15% is the highest rate for corporations. Bonds in excess of $100 are exempt.	FLA. STAT. §§ 687.01 -.04 (1965).
GEORGIA	7%	8%; 9% for loans secured by real property.	Forfeiture of all interest.	Corporations are exempt from the usury laws on any loan where the principal exceeds $2,500.	GA. CODE ANN. §§ 57-101, -112 (1953); §§ 57-101.1, -118 (Supp. I, 1969).
HAWAII	6%	12%	Forfeiture of all interest; usury is a misdemeanor.		HAWAII REV. STAT. §§ 478-1, -3, -4, -6 (1959).
IDAHO	6%	10%	Double damages for interest actually paid; forfeiture of all other interest.	Corporate maximum of 12% on loans over $10,000.	IDAHO CODE §§ 28-22-104, -105, -107 (1967).
ILLINOIS	5%	8%	Double damages for interest called for in contract; forfeiture of all interest.	Loans to corporations and loans made for any business purpose are exempt from the usury laws.	ILL. REV. STAT. ANN. ch. 74, §§ 1, 3, 6 (1967); ch. 74, § 4 (Supp. 1970).
INDIANA	6%	8%	All interest above 6% is forfeited and recoverable by borrower if paid. Borrower can recover costs if principal and interest had been tendered.	Partnerships, limited partnerships, trusts and corporations are exempt from the usury laws if the loan agreement is in writing.	IND. STAT. ANN. § 19-12-104 (Burns 1964); § 19-12-101 (Burns Supp. 1970).

IOWA	5%	9%	Forfeiture or fine of 8% on outstanding principal to be paid to the state; lender forfeits outstanding principal to borrower. Usury is a misdemeanor if interest exceeds 2% per month.	Corporations cannot plead usury if contract is in writing.	IOWA CODE ANN. §§ 535.5, .6 (1962); § 535.2 (Supp. 1970).
KANSAS	6%	10%	Any remaining interest is forfeited; any interest paid is credited against unpaid principal.	BFP of usurious negotiable paper forfeits only excess interest. Borrower has cause of action against original lender for any interest paid (to BFP).	KAN. STAT. ANN. §§ 16-201, -203 (1969).
KENTUCKY	6%	7%	On any loans exceeding $300, all interest over 7% is forfeited and borrower may recover any interest paid.		KY. REV. STAT. §§ 360.010, .020, .025, .040 (1953).
LOUISIANA	5%	8%	Forfeiture of all interest, and borrower may recover interest paid. Usury is a misdemeanor.	Loans to corporations are exempt from the usury laws.	LA. CIVIL CODE ANN., art. 2924 (1952); LA. STAT. ANN. §§ 9-3501, 12-603 (1952).
MAINE	6%	16% on a non-business loan in excess of $2,000; graduated maximum interest rates in non-business loans below $2,000.	Forfeiture of principal and interest; borrower may recover attorney fees.		MAINE REV. STAT. ANN., tit. 9, § 228 (1964); tit. 9, § 229 (Supp. 1970).

MARYLAND	6%	8% (12% on unsecured loans).	Treble damages on portion of interest paid in excess of legal rate or $500, whichever is greater; lender may correct contract prior to action.	BFP of usurious note is exempt. Any loan for a business purpose or commercial investment is exempt if principal is in excess of $5,000.	ANN. CODE OF MD. art. 49, §§ 1, 2 (1968 Replacement vol.), art. 49, §§ 3, 5, 7, 8 (Supp. 1969).
MASSACHUSETTS	6%	No limit.	No statutory provisions.		MASS. GEN. LAWS ANN. ch. 107, § 3 (1967).
MICHIGAN	5%	7%	Forfeiture of all interest. Usury is a felony if interest is in excess of 25% of principal.	Corporations cannot plead the defense of usury.	MICH. COMP. LAWS ANN. §§ 438.31, .32, .41, 450.78 (1970).
MINNESOTA	6%	8%	Borrower may recover all interest paid; however, 1/2 of recovery goes to public school fund.	BFP of negotiable paper is exempt, and corporations cannot plead the defense of usury.	MINN. STAT. ANN. §§ 334.01, .02 (1967); § 334.021 (Supp. 1970).
MISSISSIPPI	6%	8%	Forfeiture of all interest, and borrower may recover any amount paid.	Corporations are exempt from the usury laws.	MISS. CODE ANN. § 36 (1942); § 5309-04(h) (Supp. I, 1964).
MISSOURI	6%	8%	Borrower may recover all interest paid, plus costs.	Corporations may not plead the defense of usury.	ANN. MO. STAT. §§ 408.020, .040, .050, .060 (1949).
MONTANA	6%	10%	Double damages for interest set out on the face of the loan agreement.		REV. CODES MONT. §§ 47-124, -125, -126 (1961).

NEBRASKA	6%	9%	Forfeiture of all interest, and any interest paid is credited to principal. The borrower may recover costs.	Corporations cannot plead the defense of usury.	Rev. Stat. Neb. §§ 45-101, -102, -105 (1968).
NEVADA	7%	12%	Forfeiture of interest in excess of maximum.		Nev. Rev. Stat. §§ 99.040, .050 (1959).
NEW HAMPSHIRE	6%	None, if contract is in writing.	No statutory provisions .		N.H. Rev. Stat. Ann. § 336.1 (1966).
NEW JERSEY	6%	8%	Forfeiture of all interest and any actual interest payment is credited to principal. Borrower may recover his costs.	Corporations cannot plead the defense of usury. State and Municipal bonds are exempt from the usury laws.	N.J.S.A. §§ 31:1-1, -3, -6, -7 (1963), *as amended,* (Supp. 1970).
NEW MEXICO	6%	12% on unsecured loans; 10% when collaterally secured.	Forfeiture of all interest, and the borrower may recover twice interest actually paid. Usury is a misdemeanor.		N.M. Stat. Ann. §§ 50-6-3, -15, -16, -18, -19 (1953).
NEW YORK	6%	7-1/4% between 1968 and 9/2/71.	On loans by banks and savings and loan associations, the borrower may recover double damages for interest actually paid; all interest is forfeited. Usurious loans by lender other than those described above are void. Usury, when interest is in excess of 25% is a felony.	FHA loans are exempt from usury laws. Corporations cannot plead the defense of usury (unless criminal usury). Court will penetrate the corporate veil in certain restricted situations.	N.Y. Bank Law § 14-a (McKinney Supp. 1970); N.Y. Gen. Ob. Law §§ 5-501, -511, -521 (McKinney 1964); N.Y. Penal Law § 190.40 (McKinney 1967); N.Y. Bank Bd. Reg. § 34.1 (June 6, 1968).

NORTH CAROLINA	6%	6%	Double damages for interest actually paid, all interest forfeited.	Corporations may contract to pay a rate in each 12-month period, not in excess of 6% of the original amount of the loan.	N.C. GEN. STAT. §§ 24-1, -2 (1965).
NORTH DAKOTA	4%	7%	All interest is forfeited, and an additional penalty of 25% of principal is awarded to the borrower. The borrower may recover double damages for interest paid plus the 25% penalty; or off-set double the interest paid against any outstanding principal.		N.D. GEN. CODE §§ 47-14-05, -09, -10 (1960).
OHIO	6%	8%	Any interest paid is applied to the outstanding principal.	Corporations cannot plead the defense of usury. All loans over $100,000 are exempt.	OHIO R.C. §§ 1343.03, 1701.68 (1964); § 1343.01 (1969).
OKLAHOMA	6%	10%	Double damages for interest called for on the face of the note, whether or not paid.	Corporations cannot plead the defense of usury.	OKLA. STAT. ANN. tit. 15, §§ 266, 267 (1966); tit. 18, § 1.26 (1953).
OREGON	6%	10%	Forfeiture of all interest, and any interest paid is credited to principal. Lender must pay amounts equal to payments received to school fund.	Corporations cannot plead the defense of usury unless interest exceeds 12%.	ORE. REV. STAT. §§ 82.010, .120 (5) (1969).
PENNSYLVANIA		6% (no limit on FHA or VA loans other than limits prescribed by the respective agency.)	Borrower may withhold excess interest, but if principal and interest have been paid, there is a 6-month Statute of Limitations upon borrower's recovery of excess interest.	Any loan exceeding $5,000, secured by negotiable personal property is exempt from usury. Corporations cannot plead the defense of usury [repealed insofar as it relates to foreign business corporations]. All loans over $50,000 are exempt.	PA. STAT. ANN. tit. 41, §§ 1, 2, 4 (1954); §§ 2, 3 (Supp. 1970).

RHODE ISLAND	6%	21%	Forfeiture of interest and principal. Usury is a misdemeanor.	Pawnbrokers are exempt.	R.I. GEN. LAWS §§ 6-26-1, -3, -4, -5 (1956); § 6-26-2 (Supp. 1967).
SOUTH CAROLINA	6%	8% (if loan greater than $50,000; 10%.)	Forfeiture of all interest. Double damages for interest actually paid may be recovered by borrower, or set off against remaining principal. Usury is a misdemeanor.	Corporations with more than $40,000 par value of capital stock outstanding are exempt.	S.C. CODE OF LAWS §§ 8-2, -5, -9 (1962); §§ 8-3, -8, -8.1, -10 (Supp. 1970).
SOUTH DAKOTA	6%	10% (between 2/24/70 to 7/1/72) and then revert to 8%).	Forfeiture of all interest. Usury is a misdemeanor.	Corporations may not plead the defense of usury.	S.D.C.L. §§ 54-3-4, 9 (1967); §§ 54-3-7, 7.1 (Supp. 1970).
TENNESSEE	6%	10%	Forfeiture of excess interest. Borrower may recover any excess paid.		TENN. CODE ANN. § 47-14-115 (1964); § 47-14-104 (Supp. 1970).
TEXAS	6%	10%	Double damages for interest required in contract. If interest charged exceeds 20%, forfeiture of principal.	Corporations may contract to pay up to 18% on loans exceeding $5,000.	TEX. CIV. STAT. art. 5069 §§ 1-.01, -.04, -.06 (1971).
UTAH	6%	10%	Forfeiture of all interest, and the borrower may recover treble damages for interest actually paid. Usury is a misdemeanor.	Corporations may contract for interest up to a maximum of 14%.	UTAH CODE ANN. §§ 15-1-1, -5, -7 (1953); § 15-1-2 (Supp. 1967).

VERMONT	7½%	7½%	The borrower may recover any excess interest paid, plus costs; the lender cannot recover any interest at all, and only 1/2 the principal. Usury is a misdemeanor.	Exempt from usury laws are: any loans to corporations, and any loans made to any person, partnership, entity, etc., wholly or in part for use in a business activity, any U.S. insured loans.	VT. STAT. ANN. tit. 9, §§ 41, 46, 50 (Supp. 1970).
VIRGINIA	6%	8%	Borrower may recover double damages for interest actually paid.	Corporations may not plead the defense of usury.	VA. CODE ANN. § 6.1-327 (1966); §§ 6.1-318, -319, -326 (Supp. 1968).
WASHINGTON	6%	12%	Forfeiture of all interest, and the borrower may recover double any interest actually paid.		WASH. R.C. § 19.52.010 (1957); §§ 19.52.020, .030 (Supp. 1970).
WEST VIRGINIA	6%	6%	Interest in excess of 6% is forfeited, recoverable if paid, or can be credited against outstanding principal.	Corporations cannot plead the defense of usury.	W. VA. CODE §§ 47-6-5, -6 (1966).
WISCONSIN	5%	12%	Forfeiture of all interest.	Corporations cannot interpose the defense of usury.	WIS. STAT. ANN. §§ 138.04-.06 (Supp. 1970).
WYOMING	7%	10%	Forfeiture of all interest, and any interest paid may be applied to outstanding principal.		WYO. STAT. §§ 13-476, -477 (1965).
PUERTO RICO	6%	9% if less than \$3,000; 8% if greater than \$3,000.	Forfeiture of all interest, and lender must forfeit 25% of the principal to the commonwealth. Usury is a misdemeanor.		P.R. LAWS ANN. tit. 31, §§ 4591, 4594 (1968); tit. 33, § 1751 (1969).

VIRGIN ISLANDS	6%	10%	Forfeiture of all interest.	Maximum of 9% where loans on real estate. Corporations cannot plead the defense of usury.	V.I. .CODE ANN tit. 11, § 951 (1966), *as amended*, (Supp. 1970); tit. 13, § 347 (1966).
UNITED STATES	Laws of the state where bank is located is determinative; or, 1% above Fed. Reserve discount rate on 90-day commercial paper.		The borrower may recover double damages for interest paid; forfeiture of all other interest paid.		12 U.S.C.A. § 85 (1945).