STATE OF TEXAS

OFFICE OF CONSUMER CREDIT COMMISSIONER

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SAM KELLEY, Commissioner

September 3, 1981 No. 81-19

Ms. Marsha L. Williams
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First Texas Savings Association
14951 Dallas Parkway, 8th Floor
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Dear Ms. Williams:

This is to acknowledge receipt of your letter dated May 29, 1981 wherein you pose four questions concerning Article 5069, V.T.C.S., as recently amended by H.B. 1228. I have paraphrased three of your questions as follows:

(1) May the alternative rates provided for in H.B. 1228 (Article 1.04) be used in interest-bearing as well as precomputed transactions which are subject to the provisions of Chapter 5, Article 5069?

(2) On the above transactions, may the "Rule of 78's" be used upon repayment of a precomputed transaction even though the resulting yield would exceed the applicable rate ceiling?

(3) Does Article 5069 as recently amended now allow the parties to contract for a "balloon payment" in a transaction subject to Chapter 5?

In a letter I wrote on June 12, 1981 to Mr. Cullen A. Rogers, I set out the position of this Office on these three questions. I am attaching hereto a copy of that letter interpretation No. 81-5, and I consider the statements made therein to be part of my response to your questions. You may consider Mr. Rogers' letter to be an accurate representation of our position and as being included in my reply to you.

Without going into detail here as I did in the Rogers letter, in reply to your questions I would state that our position is that it is now possible to have a "balloon payment" in a transaction subject to Chapter 5. We are of the opinion that Chapter 5 transactions may now be constructed so as to be either precomputed or interest-bearing. Also, as set out in the Rogers letter and within the limitations described therein, the "Rule of 78's" or the "Sum of the Periodic Balances" methods of refunding may be utilized in a Chapter 5 transaction using Article 1.04 rates even though the resulting yield in the event of prepayment exceeds the applicable rate ceiling. As pointed out in the Rogers letter, neither of these methods would be appropriate in an interest-bearing contract.

Since the amendments to Article 5069 by H.B. 1228, we have not expressed our view as regards the fourth question you asked, which is:

> What rate of interest may be charged after a note has matured? Can the rate charged after maturity be at the rate provided in the revised Article 1.04?

A relatively recent court decision and some of the language of recently enacted H.B. 1228, now a part of Article 1.04, Article 5069, have caused this Office to alter somewhat our position concerning this question.

In Bundrick v. First National Bank of Jacksonville, 570 S.W.2d 12 (Tyler Ct. of Civ. App., n.r.e., 1978), the parties to a loan made pursuant to Chapter 4, Article 5069, V.T.C.S., agreed that "all past due principal and interest shall bear interest from the date it is due until paid at the highest legal contract rate." The borrower contended that since Chapter 4 limited default charges to five cents for each one dollar of any scheduled installment which was not paid as agreed that the above-quoted provision in the contract resulted in a contract for usurious interest. The court disagreed and stated that the limitation on default charges for failure to make an installment payment as scheduled did not affect the right of the lender to contract for interest after maturity. The court stated that:

> "It is generally held that parties to a contract validly may agree that past due principal and interest shall bear the highest lawful contract rate, whether the obligation matures in the ordinary course according to the terms thereof, or by reason of acceleration."

In the Bundrick case (an acceleration), the court said that "The highest legal contract rate of interest on a loan is 10%." That had been the position of this Office for many years with respect to interest after maturity on credit transactions subject to Article 5069.

Then in 1980 the Beaumont Court of Civil Appeals decided the case of Ford Motor Credit Co. v. Long, 608 S.W.2d 293 (Beaumont Ct. of Civ. App., n.r.e., 1980). The court, with very little discussion, held that after maturity (acceleration in this instance) the same rate of interest could be collected as was originally contracted for during the term of the contract, even though the terms of the agreement were silent as to what rate could be collected after maturity. This case involved a Chapter 7 contract. Time price differential rather than interest was and still is charged in these transactions. The court did not mention that distinction, however, and just stated that the interest rate agreed to for the term of the contract could be charged on the balance due after maturity even though the contract was silent on this point. The court in the Ford Motor Credit Co. case made no mention of the earlier Bundrick case.

Articles 1.04(a)(1) and (2) and 1.04(c) provide that the parties may agree to any rate of interest or time price differential producing a rate that does not exceed the various ceilings described therein. These sections which authorize the parties to so agree do not limit the interest so agreed upon to the stated term of the contract. Stated another way, there is nothing in these statutory authorizations indicating that the parties may not agree to the various authorized interest charges after maturity. On the contrary, they all authorize the parties to agree to the authorized rates with no restrictions on the time period. They all, however, contain the restriction that the rate agreed upon may not exceed the ceiling applicable to the contract.

Article 1.04(f) provides in part as follows:

> "The parties to any contract, including a contract for an open-end account, may agree to and stipulate for a rate or amount by contracting for any index, formula, or provision of law, by or under which the numerical rate or amount can from time to time be determined. However, the rate or amount so produced may not exceed the ceiling that may from time to time be in effect and applicable to the contract, for so long as debt is outstanding under the contract."

I believe that the underlined words evidence legislative intent to allow the contracted for rates in variable rate contracts to be charged so long as the debt is outstanding; i.e. after maturity, if applicable. But, as pointed out with respect to the other provisions, Article 1.04(f) also provides that the contracted for rate must not exceed the ceiling applicable to the contract as it is from time to time in effect.

Then, Article 1.04(b)(1) provides that no matter what the various ceilings are because of the computations based on the Treasury Bill rates, 18% per annum may always be contracted for pursuant to the provisions of Article 1.04.

Notwithstanding the Ford Motor Credit Co. case mentioned earlier where the contract did not contain a provision relating to interest after maturity, our position on this question is based on the premise that Article 1.04 requires that interest after maturity must be contracted for in writing.

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It is our position that in any written contract entered into pursuant to the provisions of Article 1.04, the parties may always agree to interest after maturity at the rate of 18% per annum. This of course would most normally occur in closed-end accounts but could happen in an "open-end account" which was for some reason accelerated with a balance still owing.

On a closed-end, fixed-rate contract, the parties may contract for interest after maturity at the same rate contracted for in the agreement for its stated term. If the applicable rate ceiling is 20%, and the parties agree to that rate (20%) for the term of the contract, they can also contract for 20% after maturity. However, since the 20% per annum was the applicable rate ceiling at the time the contract was consummated, they could not agree to a higher rate after maturity since the various sections of Article 1.04 mentioned earlier state that the parties may contract for a rate not to exceed the applicable ceiling. Also, if the rate ceiling applicable to the contract is 24%, the parties may contract for a rate of 20% during the stated term of the contract and 24% after maturity. Our reasoning on this point is that the parties could have contracted for 24% for the stated term of the contract as well as after maturity, and I find nothing to prevent the parties from contracting for a rate which is lower than the ceiling for the term of the contract and for the lawful applicable ceiling after maturity.

On closed-end variable rate contracts the parties may contract for interest after maturity not to exceed the ceiling applicable to its term prior to maturity as it is from time to time in effect. However, the interest after maturity should not exceed the appropriate ceiling since, as mentioned earlier, Article 1.04(f) provides that the interest rate in variable rate contracts may never exceed the applicable ceiling from time to time in effect for so long as the debt is outstanding; i.e. during the stated term and after maturity.

Interest after maturity will not normally be important in open-end contracts, but the appropriate ceiling would be that which was applicable to the contract before maturity.

I hope this response is satisfactory.

Sincerely yours,

Sam Kelley

Sam Kelley
Consumer Credit Commissioner

Enclosure