STATE OF TEXAS

OFFICE OF CONSUMER CREDIT COMMISSIONER

SAM KELLEY, Commissioner

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February 10, 1983 No. 83-2

Mr. Jack Welch
Attorney at Law
P. O. Box 568
Marlin, Texas 76661

Dear Mr. Welch:

This is to acknowledge receipt of your recent letter concerning procedures which might be used by a creditor who wishes to reduce the rate of finance charge on open-end accounts which are subject to the provisions of Article 5069-1.04, V.T.C.S. (All statutory references herein are to provisions of Article 5069, V.T.C.S. unless otherwise noted.)

For the purpose of this response it is assumed that a retailer is extending credit by use of an open-end account program subject to the provisions of Chapter 6, Article 5069. The retailer has previously, effective October 1, 1981, implemented a time price differential charge equivalent to a rate of 21% per annum subject to the annualized ceiling. Since the annualized ceiling on this plan was implemented as of October 1, 1981, the time price differential rate charged on the program was subject to adjustment on October 1, 1982, (at which time it was not required to be reduced) and will not be subject to a possible mandatory adjustment again until October 1, 1983. However, the retailer just described wants to voluntarily lower the time price differential charge assessed under the program on new purchases made on and subsequent to March 1, 1983.

You then pose several questions in your letter relating to this proposed change in the rate of charge. I will state your questions and set out my response directly following each question.

Question No. 1. May the retailer reduce the rate without giving the notice set out in Article 5069-1.04(i)? What notice would be required, if any?

Response to Question No. 1. It is our opinion that the above described retailer may reduce the rate of charge on purchases made pursuant to the plan on and after March 1, 1983 without giving the notice described in Article 5069-1.04(i). The participants (obligors) in the program have previously agreed to a rate of charge of 21%. Such charge on the plan will be an authorized charge at least until October 1, 1983. Article 1.04(g) provides as follows:

"(g) Unless otherwise agreed, when the parties have agreed to a rate, they are considered also to have agreed to any lesser rate that the creditor may elect, or is required under Section (h) of this Article to implement."

It is our view that Article 1.04(g) authorizes a creditor to elect to charge a lesser rate than that previously agreed to by the obligors if the creditor elects to do so. In addition, I can think of no policy reason which would argue against a creditor being able to voluntarily reduce the rate of charge on such a program as described. It is our position that the earlier described retailer may reduce the rate of charge on the described plan as of March 1, 1983 and not be required to give the notice described in Article 1.04(i). If the open-end account plan is subject to Article 1.04(h)(1) the only notice requirements would be those of Regulation Z of the Truth in Lending Act.

Question No. 2. On new accounts established after March 1, 1983, may the retailer use present agreements which include an agreement to pay a rate of 21%, and charge only 18% on these, or must new agreements with an 18% rate be prepared?

Response to Question No. 2. On new accounts established after March 1, 1983 the retailer may use present agreements which provide for a finance charge of 21% per annum but charge a rate of only 18% on those accounts. Again, the 21% rate on this program will be lawful until October 1, 1983. Also, Article 1.04(j) provides that a previously implemented lawful ceiling on an open-end account plan will also be the ceiling for any new participants entering the program while that ceiling is in effect. Therefore, in our view, the retailer may use the agreements providing for a rate of charge of 21% per annum for new customers entering the program after March 1, 1983 and prior to October 1, 1983.

Question No. 3. If the retailer desires for the rate change to apply only to purchases made after March 1, 1983, may he continue to charge the 21% rate on purchases made between October 1, 1981 and March 1, 1983? If he may do so, would this change your answer to any of the other questions raised?

Response to Question No. 3. The retailer may apply the new rate of charge of 18% per annum only to new purchases made on or after March 1, 1983 and continue to charge the rate of 21% per annum to purchases made on or after October 1, 1981 and prior to March 1, 1983. The 21% rate has been, still is, and will be an authorized charge on this program at least until October 1, 1983. Since the reduction in the rate from 21% to 18% is voluntary

on the part of the creditor and has not been mandated by a reduction in the annualized ceiling applicable to this plan, the rate of charge of 21% on balances incurred from October 1, 1981 to March 1, 1983 will be lawful until and including September 30, 1983. Article 1A.01 is not applicable to those purchases made under the plan on and after October 1, 1981 since they would not be part of any balance existing as of the implementation of the provisions of Article 1.04 by the creditor.

Question No. 4. Assume that the retailer has determined that the balances that were in existence on all, or a definable group, of his customers' accounts as of October 1, 1981, have now been reduced to $500 or less. These balances were incurred under an agreement that a rate of 18% applied to balances of $500 or less. On such accounts where the balance "grandfathered" under Article 1A.01 is now $500 or less, may the retailer combine that "grandfathered" balance with the new balance being incurred at 18% for purposes of disclosure, computation of finance charge, etc.?

Response to Question No. 4. Our reply to this question is "Yes." Prior to October 1, 1981 a rate of charge of 18% per annum was lawful on these types of accounts on amounts of $500 or less. Any balances in existence on October 1, 1981 would have had to have been "grandfathered" at their old rate of charge because of Article 1A.01. If the existing balances were in excess of $500 such excess amount would have to have been "grandfathered" at a rate less than 18%. However, if it is assumed that all such balances have now been reduced to $500 or less, a rate of charge of 18% is lawful on such balances. Since the rate of charge on new purchases under the program as of March 1, 1983 will be assessed at the same rate of charge (18%) any such remaining "grandfathered" balances of $500 or less may be combined with the new balances incurred on and after March 1, 1983 on which a rate of charge of 18% is assessed.

Question No. 5. Assume that the retailer will charge the new 18% rate on charges made after March 1, 1983, but that charges made between October 1, 1981 and March 1, 1983 will continue to accrue a charge of 21% per annum (as described in Section 3 above). May the retailer apply payments received first to the balance which accrues interest at the rate of 21% and thereafter to the balance which accrues interest at the rate of 18%? Must the retailer so apply payments, or may he apply them in any manner that would otherwise be legally permitted?

Response to Question No. 5. It is our opinion that the retailer may apply payments received first to the balance which accrues interest (time price differential) at the rate of 21% per annum and thereafter to the balance which accrues interest (time price differential) at the rate of 18% per annum unless for some reason the agreements under the plan mandate otherwise. The Article 1A.01 language relating to application of payments is permissive in nature and neither that section nor any other of Article 5069 requires any particular

method of application of payments. If there is no contractual impediment, the retailer may utilize the above described method of payment application or some other. It should be noted, however, in the event payments are first applied to the balances with a rate of 21% and some accounts have old balances of $500 or less which have been "grandfathered" from the implementation date of the Article 1.04 provisions those old balances might not be paid off for some time. If the retailer at some future date should wish to increase the rate of charge on the program in excess of 18% care should be taken that any then still existing "grandfathered" balances not be assessed a rate of charge in excess of 18%.

Question No. 6. Assume that the retailer implemented a floating rate formula under Article 5069 - 1.04(h)(2) on October 1, 1981, rather than implementing a particular numerical rate under Article 5069 - 1.04(h)(1). Would this factor change your answer to any of the other questions?

Response to Question No. 6. Our answers would be the same as previously given if the plan were subject to Article 1.04(h)(2). The notice requirements of Article 1.04(h)(2), second paragraph, would not be required since the rate change is not brought about by the operation of an index, formula or provision of law.

Question No. 7. Assume that after reducing the rate actually charged to 18% the creditor later wanted to charge 19% (or any other rate not exceeding 21%) on the account of a customer who had signed an agreement agreeing to pay 21% or agreeing to a formula which at that later time produced a rate of 21% (or as to whom the creditor had sent the customer a notice setting out the 21% rate or the formula producing that rate, in accordance with Article 5069 - 1.04(i)). What notice, if any, would be required by Texas law? I understand that the Federal Truth In Lending law might well require a notice. I also understand that changes produced by the formula used in an Article 5069 - 1.04(h)(2) type of agreement would require a notice to the customer of the change dictated by the formula previously disclosed. However, would Texas law require any notice when the creditor simply returns to a rate not exceeding the rate previously disclosed under Article 5069 - 1.04(h)(1) or, in the case of an account subject to Article 5069 - 1.04(h)(2), if the creditor simply returns to charging a rate which is equal to or less than the rate which the formula previously disclosed produces. For purposes of this question, assume that the new rate would be legal under the appropriate ceiling at the time that the new rate was charged.

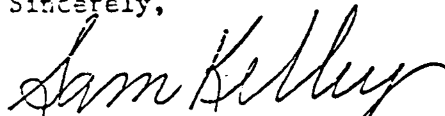
Response to Question No. 7. If the obligors in a plan have previously agreed to pay a rate of 21% per annum or (if a variable rate program) agreed to pay a rate not in excess of 21% per annum, the above described creditor does not have to comply with Article 1.04(i) if the creditor subsequently wishes to increase the rate charged on the program to some amount not in excess of 21% per annum. The parties have previously agreed to a rate not to exceed 21% per annum and no further agreement or notice is required. For the reasons stated in the response to question number 6 the notice requirements of Art. 1.04(h)(2) would not be required in this instance on a variable rate program. Any notice required by the Federal Truth in Lending law should be given.

February 10, 1983

<u>Question No. 8.</u> If the creditor were not a retailer operating under Chapter 6, but a creditor operating under some other Chapter of Article 5069, would this change any of your answers?

<u>Response to Question No. 8.</u> All of the above given responses would be the same for any type of creditor who is extending credit pursuant to an open-end account credit program which is subject to the provisions of either Articles 1.04(h)(1) or 1.04(h)(2).

Sincerely,



Sam Kelley
Consumer Credit Commissioner

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