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Creditor's Demand upon Buyer's Default for Amount Including Unearned Interest Constitutes Charging.

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guidance for the court to decide whether to extend further the doctrine of strict liability in tort. Until the supreme court addresses the issue, the *Hovenden* decision will grant protection only in a specific geographical location—the jurisdictional area of the San Antonio Court of Civil Appeals.

Israel Ramòn, Jr.

USURY—Installment Sales—Creditor's Demand Upon Buyer's Default for Amount Including Unearned Interest Constitutes "Charging"

Moore v. Sabine National Bank,
527 S.W.2d 209 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.).

Andrew Moore entered into a retail installment contract with Oak Hill Mobile Homes. Oakhill's interest in the contract was sold to the Sabine National Bank. After Moore defaulted on the monthly payments, the bank sent a notice of acceleration, demanding the total amount due under the contract. Subsequently the bank filed suit alleging that the total sum of the contract, including the unearned portion of the finance charge, was payable. The bank also filed for a writ of sequestration. In his counterclaim Moore alleged that the bank's failure to rebate the unearned finance charge was a violation of the Texas Consumer Credit Code.[1] The district court held for the bank as to the counterclaim, concluding that it had never intended to collect any unearned finance charge. The court stated that the bank's notice of intention to repossess, its original petition, and its sequestration affidavit did not constitute "charging" under Article 5069-8.01 of the Texas Consumer Credit Code. On appeal, Moore contended that the district court's construction of the term "charging" was too narrow and that the bank's conduct violated article 5069. Held—*Reversed.* The inclusion in a creditor's notice of intention to repossess, original peititon, and sequestration affidavit of an amount which includes both earned and unearned finance charges constitutes "charging" of unearned time price differential under Article 5069-8.01 of the Texas Consumer Credit Code.[2]

1. TEX. REV. CIV. STAT. ANN. art. 5069 (1971).

2. Moore v. Sabine Nat'l Bank, 527 S.W.2d 209, 214 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.); TEX. REV. CIV. STAT. ANN. art. 5069-8.01 (1971), provides in part:

> Any person who violates this Subtitle by contracting for, charging or receiving interest, time price differential or other charges which are greater than the amount authorized by this Subtitle . . . shall forfeit to the obligor twice the amount of in-

"Interest" is the compensation which the law permits to be charged for the use or forbearance or detention of money.[3] "Usury" is defined as interest in excess of the amount allowed by law.[4] Distinct and technically excluded from either term is "time price differential."[5] The time price differential is defined as the difference between the cash price and a much larger deferred payment price, and is generally considered an exception to usury statutes.[6] The reason for the distinction is that no loan or forbearance of money exists in an installment sales situation.[7] For usury law purposes, the charge is considered part of the price rather than interest. The purchaser, however, must have an actual choice between paying a cash sale price and an advanced credit purchase price before the charge can properly be precluded from being designated usurious interest.[8]

The interest/time price differential dichotomy has troubled the courts for some time, but in Texas the courts have been aided by legislative action.[9] The Texas Consumer Credit Code has incorporated the time price differential into the general usury statute, and it imposes penalties for charging, receiving, or contracting for amounts exceeding the statutory rates for interest or time price differential.[10] Since time price rates may be considerably higher than the interest rates, the intent of the parties becomes a factor and the credit price may be attacked as a "cloak for usury."[11] As a general

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terest or time price differential and default and deferment charges contracted for, charged or received . . . provided that there shall be no penalty for a violation which results from an accidental and bona fide error.

3. TEX. REV. CIV. STAT. ANN. art. 5069-1.01(a) (1971).

4. TEX. REV. CIV. STAT. ANN. art. 5069-1.01(d) (1971). The essential elements of usury are: (1) a loan or forbearance of money, (2) an agreement for a return of the money in all events, and (3) an agreement to pay more than the legal rate of interest for its use. Seebold v. Eustermann, 13 N.W.2d 739, 743 (Minn. 1944); *see In re* Bibey, 9 F.2d 944, 945 (D. Minn. 1925).

5. TEX. REV. CIV. STAT. ANN. art. 5069-1.01(a) (1971).

6. Note, 39 MO. L. REV. 111 (1974); *see, e.g.*, Avant v. Gulf Coast Inv. Corp., 457 S.W.2d 134, 136 (Tex. Civ. App.—Dallas 1970, no writ); Hernandez v. United States Fin. Co., 441 S.W.2d 859, 861-62 (Tex. Civ. App.—Waco 1969, writ dism'd).

7. Hogg v. Ruffner, 66 U.S. [1 Black] 115 (1861); *see, e.g., In re* Bibbey, 9 F.2d 944, 946 (D. Minn. 1925); Sliger v. R.H. Macey & Co., 283 A.2d 904, 906 (N.J. 1971); Gifford v. State, 229 S.W.2d 949, 951 (Tex. Civ. App.—El Paso 1950, no writ); Gardner v. Associates Inv. Co., 171 S.W.2d 381, 383 (Tex. Civ. App.—Amarillo 1943, writ ref'd w.o.m.); Rattan v. Commercial Credit Co., 131 S.W.2d 399 (Tex. Civ. App.—Dallas 1939, writ ref'd). *But see* Note, 48 WASH. L. REV. 479, 481 (1973).

8. Daniel v. First Nat'l Bank, 227 F.2d 353, 357 (5th Cir. 1955); Day v. Garland Chrysler-Plymouth, Inc., 460 S.W.2d 272, 275 (Tex. Civ. App.—Dallas 1970, no writ); Bradford v. Mack, 359 S.W.2d 936, 939 (Tex. Civ. App.—El Paso 1962, writ ref'd n.r.e.).

9. Texas follows the majority of jurisdictions in accepting the time price doctrine. Lusk v. General Motors Acceptance Corp., 395 S.W.2d 847, 851 (Tex. Civ. App.—Tyler 1965, no writ). For a survey of the doctrine as treated by other states see Annot., 14 A.L.R.3d 1065 (1967).

10. TEX. REV. CIV. STAT. ANN. art. 5069-8.01 (1971).

11. Poole v. Bates, 520 S.W.2d 273, 274 (Ark. 1975).

rule, however, intent is irrelevant where the contract is usurious on its face,[12] but where the buyer is not given a choice between paying the sales price and the higher credit price, the intent to charge interest will be presumed regardless of the label affixed by the seller.[13]

Some installment contracts become usurious through the terms of payment,[14] while others are made usurious by the terms of an acceleration clause inserted within the contract.[15] An acceleration clause is designed to protect the creditor against financially irresponsible debtors by allowing the creditor to declare default upon the occurrence of some contingency, and demand immediate payment of the entire amount due.[16] Acceleration clauses are widely used in installment contracts and generally upheld, subject to some qualifications.[17] The general rule in Texas is that an acceleration clause will render a contract usurious if the terms require default payments in excess of the principal and legal interest.[18] Clauses which authorize the creditor to demand upon default the "principal and interest," the "whole thereof, principal, interest, and attorney's fees," or "principal and all interest accrued thereon" are not usurious since the clauses clearly allow the collection of only the principal and accrued interest.[19] If the clause merely

12. *See, e.g.*, Walker v. Temple Trust Co., 124 Tex. 575, 577-78, 80 S.W.2d 935, 936 (1935); Dorfman v. Smith, 517 S.W.2d 562, 566 (Tex. Civ. App.—Houston [1st Dist.] 1974, no writ); Hernandez v. United States Fin. Co., 441 S.W.2d 859, 862 (Tex. Civ. App.—Waco 1969, writ dism'd).

13. Bradford v. Mack, 359 S.W.2d 936, 939 (Tex. Civ. App.—El Paso 1962, writ ref'd n.r.e.). *See also* UNIFORM CONSUMER CREDIT CODE § 2.110, Comment 1.

14. Strictly speaking, the term "usury" found in the Consumer Credit Code does not apply to time price differential, but it will be used herein to refer to any violation involving interest or time price differential to avoid confusion. *E.g.*, General Am. Life Ins. Co. v. Ramp, 135 Tex. 84, 87, 138 S.W.2d 531, 533 (1940) (interest on 10 year loan "squeezed" into first four years); Southwestern Inv. Co. v. Hockley County Seed & Delinting, Inc., 511 S.W.2d 724, 732 (Tex. Civ. App.—Amarillo), *writ ref'd n.r.e. per curiam*, 516 S.W.2d 136 (Tex. 1974); McDonald v. Savoy, 501 S.W.2d 400, 408 (Tex. Civ. App.—San Antonio 1973, no writ) (improper disclosure of insurance charge).

15. *E.g.*, Deming Inv. Co. v. Giddens, 120 Tex. 9, 13-14, 30 S.W.2d 287, 289 (1930) (acceleration clause demanding unearned interest); Shropshire v. Commerce Farm Credit Co., 120 Tex. 400, 405-406, 30 S.W.2d 282, 283 (1930); Ward v. Pace, 73 S.W.2d 959, 960 (Tex. Civ. App.—El Paso 1934, writ ref'd) (acceleration clause in trust deed securing note).

16. *See* Baltimore Life Ins. Co. v. Harn, 486 P.2d 190, 193 (Ariz. Ct. App. 1971). The usual situation involves either nonpayment or repeated delinquency, depending on the terms of the clause.

17. *See, e.g.*, Guaranty Fin. Corp. v. Harden, 416 S.W.2d 287, 288 (Ark. 1967); Industrial Nat'l Bank v. Stuard, 318 A.2d 452, 453 (R.I. 1974); Doppke v. American Bank & Trust Co., 402 S.W.2d 317, 320 (Tex. Civ. App.—Houston 1966, writ ref'd n.r.e.). *See also* Annot., 66 A.L.R.3d 650 (1975).

18. Shropshire v. Commerce Farm Credit Co., 120 Tex. 400, 410-11, 30 S.W.2d 282, 285 (1930), *cert. denied*, 284 U.S. 675 (1931); *accord*, Imperial Corp. of America v. Frenchman's Creek Corp., 453 F.2d 1338, 1344 (5th Cir. 1972); W.E. Grace Mfg. Co. v. Levin, 506 S.W.2d 580, 584 (Tex. 1974).

19. Sinclair v. Mack Trucks, Inc., 355 S.W.2d 563, 564 (Tex. Civ. App.—Fort Worth 1962, writ ref'd n.r.e.).

provides for maturity of the debt, it is not usury because the unearned interest could not be collected. It must definitely appear that the intention shown by the express terms of the contract is to exact more payment than the law allows.[20]

The Austin Court of Civil Appeals confronted a related problem in *Moore v. Sabine National Bank*.[21] The primary issue involved judicial construction of the term "charging" in article 5069-8.01.[22] The finance charge and acceleration clause were both legal. The court held, however, that the bank's notice of acceleration, original petition, and sequestration affidavit constituted "charging" since they included the *unearned* time price diffential. In its analysis, the court relied heavily on *Monroe Loan Society v. Morello*[23] for the statement that a "charge" could be the debiting of an amount due, or any act by the promisee establishing or implying a demand for its payment. An example would be specifying the amount in a statement of indebtedness submitted to the debtor.[24] *Morello* involved a 15 per cent collection fee stipulated in the note. Under the controlling statute, such fees could not be "charged or collected." The fee was not included in the judgment, and no demand was made. The court reasoned that the fee was an inactive "charge" in the sense that it required no performance at the inception of the contract, and until it was actually demanded there could be no "charging." The "charging" required the occurrence of a contingency—the necessity of forced collection due to default. A charge entails more than a stipulation, agreement, or unilateral promise to pay.[25] The *Morello* court determined the missing ingredient to be an overt act.[26] This could not be found by examining the noun "charge." The verb form must necessarily be employed, and an overt act was necessary to constitute active "charging." Thus, the collection fee in *Morello* was a "charge" (noun) that was contracted for, but not "charged" until the contingency arose and an overt act made.[27]

The time price differential in *Moore* was contractually included in the total amount due. It was paid concurrently with the principal, both amounts being merged into a lump sum. In effect, the entire amount, including the time price differential, was actively "charged" at the inception of the contract. Having been calculated at the legal rates, the original "charging" could not logically constitute usury. This "charging" is subject only to the contingency of an early satisfaction of the note. Thus, *Moore* relied on the

20. *Id.* at 564.
21. 527 S.W.2d 209, 211 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.).
22. TEX. REV. CIV. STAT. ANN. art. 5069-8.01 (1971).
23. 51 A.2d 347 (Pa. Super. Ct. 1947).
24. *Id.* at 349.
25. *Id.* at 349.
26. *Id.* at 349.
27. A 1937 amendment to the statute in *Morello* included "contracted for" with "charged and received" to remedy the situation.

dicta of *Morello*, but without its supporting logic. A bare demand, unaccompanied by an overt act evincing positive intent, cannot constitute "charging."

There is specific evidence to support the contention that the unilateral demands for payment made in *Moore* do not constitute "charging" but rather should be compared to a prepayment situation. The Texas Consumer Credit Code provides for a refund of unearned interest when a loan contract is prepaid in full by cash, a new loan, renewal, or otherwise.[28] A cash payment satisfies the debt, while a new loan or renewal simply terminates the old contract and initiates a new one. The elements of contractual agreement and decisiveness are necessary to constitute prepayment in these latter instances. A unilateral demand does not involve any type of agreement which may give rise to a contract. A final judgment, however, is as binding as a contract for renewal, and as legally conclusive as a cash prepayment. The Uniform Consumer Credit Code clarifies the analogy:

> If the maturity is accelerated for any reason and judgment obtained, the buyer is entitled to the same rebate as if payment had been made on the date judgment is entered.[29]

The use of the term "rebate" in relation to a judgment obtained on a debtor's default anticipates the inclusion in the decree of the entire amount contracted for and a subsequent duty to return or credit the unearned portion.[30] Ordinarily, rebates are referred to only in conjunction with prepayment, where the entire amount, including unearned interest, is tendered by the debtor. In 1967, the Arkansas Supreme Court held that a creditor who had exercised his option to accelerate and had filed suit for the full amount without making any deduction for the unaccrued interest was not guilty of usury, and that in such a situation the court should merely refuse to permit the creditor to recover the unaccrued interest.[31] A strong dissent contended

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28. TEX. REV. CIV. STAT. ANN. art. 5069-3.15(6) (1971). Technically, interest and time price differential are separate concepts, but from a practical standpoint they are similar in application.

29. UNIFORM CONSUMER CREDIT CODE § 2.210(8). *See also* NATIONAL COMMISSION ON CONSUMER FINANCE, REPORT ON THE STUDY OF CONSUMER CREDIT IN THE UNITED STATES, CCH INSTALLMENT CREDIT GUIDE 40 (1972); Smyer, *A Review of Significant Legislation and Case Law Concerning Consumer Credit*, 6 ST. MARY'S L.J. 549, 551 (1974).

30. In its original suit in district court, it should be noted that the bank included not only unearned time price differential, but also the down payment and monthly payments actually made. Moore v. Sabine Nat'l Bank, 527 S.W.2d 209, 210 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.). This seems to fortify the bank's contention, which the trial court accepted, that it was the regular business practice of the bank to "rebate and figure unearned interest either after repossession of the collateral or upon final judgment," and that there was never an intention to collect any unearned finance charge. *Id.* at 211.

31. Guaranty Fin. Corp. v. Harden, 416 S.W.2d 287, 288 (Ark. 1967); *see* Green Ridge Corp. v. South Jersey Mortgage Co., 211 So. 2d 70, 71 (Fla. Ct. App. 1968).

that an acceleration clause is itself a contract, and that the statute in question voided all contracts without distinction as to whether the contract was presently binding or arose as a result of an option exercised by the lender.[32] This "separate contract" analysis is the most compelling reason to uphold the *Moore* decision; simply treat the acceleration clause as a separate contract. In effect, it provides for a new contractual amount due upon acceleration—the balance of the principal owed plus all earned time price differential. Any additional unilateral demand would be interpreted as a usurious charge, and distinct from the contract.

The time price differential in *Moore* was contracted for, the article 5069-8.01 provides specific language applicable to the situation. Most cases are satisfied under the "contracting for" provision. To illustrate this point, if the amount or "charge" was not usurious when contracted for, it cannot *become* usurious unless on the theory of a separate and superceding contract. In effect, this analysis precludes the possibility that "charging" could apply to the time price differential at all. Certain unilateral demands that would be construed as "interest" or "other charges" could be made subsequent to the original contract. If these demands were not acceded to by the debtor, they would not be "contracted for," and "charging" would apply, thus giving the term a useful meaning.

The commercial implications of the *Moore* interpretation of "charging" are substantial. The court has severely eroded the element of intent required for a finding of usury. Discovering no inherent illegality in the contract, the court discerned an implied intent to collect usurious rates from a debt collection method which was completely collateral to the contract itself. Two of the three documents relied upon by the court—the original petition and sequestration affidavit—were communications made primarily to initiate the judicial process. It is highly unlikely that the bank would so openly and publicly admit to a violation of the usury statutes if its intent was in fact to violate those statutes. It is more logical to assume that the bank had made a mistake which might be excused as a bona fide error under article 5069-8.01.[33] This mistake resulted in a windfall to the debtor, Andrew Moore.[34]

The opinion does not disclose whether it was the cumulative effect of the repossession notice, original petition, and sequestration affidavit that defeated the bank's defense, or if any one or two in combination would have done so. To avoid these consequences, a creditor must accurately compute the amount due, including adjustments for unearned interest or time price

32. Guaranty Fin. Corp. v. Harden, 416 S.W.2d 287, 290 (Ark. 1967) (dissenting opinion).

33. TEX. REV. CIV. STAT. ANN. art. 5069-8.01 (1971).

34. The bank forfeited twice the unearned time price differential plus attorney's fees under article 5069-8.01, and the balance of the principal under article 5069-8.02. Moore v. Sabine Nat'l Bank, 527 S.W.2d 209, 214 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.).