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Remedies and Defenses Student Symposium: A Study of Texas Usury Law.

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Louisiana law controlled.¹⁹⁷ Texas usury laws, therefore, are not applicable to a contract made in Texas when it is to be performed or executed in another state.¹⁹⁸

II. REMEDIES AND DEFENSES

BETTY L. NEWCOMB HOLLOWELL

Texas law provides various remedies by way of statute, common law, and equity for victims of usurious practices.¹⁹⁹ Contracts for usury are, by statute, contrary to public policy,²⁰⁰ and the penalty for usury is severe.²⁰¹ The policy of the legislature in regulating interest rates is essentially that of borrower protection.²⁰² In enforcing usury laws, Texas courts have generally viewed the borrower as a victim, rather than as a participant in the transaction in *pari delicto* with the lender.²⁰³ Under the *pari delicto* approach, the parties to a usurious contract are considered to be equally at fault if the usurious contract was entered into knowingly and voluntarily.²⁰⁴ The courts, therefore, will leave the parties as they found them.²⁰⁵ Under the victim approach, on the other hand, since the contract is illegal, the

197. *Id.* at 189.

198. *See, e.g.,* Connor & Walker v. Donnell, Lawson & Co., 55 Tex. 167, 174 (1881); Bullard v. Thompson, 35 Tex. 313, 319-20 (1871); Apodaca v. Banco Longoria, S.A., 451 S.W.2d 945, 947 (Tex. Civ. App.—El Paso 1970, writ ref'd n.r.e.).

199. *See, e.g.,* First State Bank v. Miller, 563 S.W.2d 572, 577 (Tex. 1978) (statutory remedy applied); Ferguson v. Tanner Dev. Co., 541 S.W.2d 483, 495 (Tex. Civ. App.—Houston [1st Dist.] 1976), *rev'd on other grounds*, 561 S.W.2d 777 (Tex. 1977) (common law remedy available); Irving Bank & Trust Co. v. Second Land Corp., 544 S.W.2d 684, 688 (Tex. Civ. App.—Dallas 1971, writ ref'd n.r.e.) (equitable remedy of injunction used).

200. *See* TEX. REV. CIV. STAT. ANN. art. 5069-1.02 (Vernon 1971).

201. *See* Tanner Dev. Co. v. Ferguson, 561 S.W.2d 777, 787 (Tex. 1977). The severity of the penalty for usury led to action by the 66th Legislature to reduce the penalty by amendment. The amendment, H.B. 616, was sent to the Governor on May 15, 1979, and is reprinted at footnote 215 *infra*.

202. *See* Autocredit of Fort Worth, Inc. v. Pritchett, 223 S.W.2d 951, 954 (Tex. Civ. App.—Fort Worth 1949, writ *dism'd*); Glenn v. McCarty, 130 S.W.2d 295, 301 (Tex. Civ. App.—Amarillo 1939), *aff'd*, 155 S.W.2d 912 (Tex. 1941); *Declaration of Legislative Intent*, 15 TEX. REV. CIV. STAT. ANN. 1-2 (Vernon 1971); *cf.* O.R. Mitchell Motors, Inc. v. Bell, 528 S.W.2d 856, 860 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.) (legislature intended to achieve its goal of borrower protection by imposing duties on creditors); Guetersloh v. C.I.T. Corp., 451 S.W.2d 759, 761 (Tex. Civ. App.—Amarillo 1970, writ ref'd n.r.e.) (purpose of usury statutes to penalize those who intentionally charge excessive interest).

203. *See* First State Bank v. Miller, 563 S.W.2d 572, 578 (Tex. 1978) (dissenting opinion); Bexar Bldg. & Loan Ass'n v. Robinson, 78 Tex. 163, 167-68, 14 S.W. 227, 228 (1890); Hampton v. Guaranty State Bldg. & Loan Ass'n, 63 S.W.2d 873, 876 (Tex. Civ. App.—Amarillo 1933, no writ).

204. *See* Bexar Bldg. & Loan Ass'n v. Robinson, 78 Tex. 163, 167-68, 14 S.W. 227, 228 (1890); 10 ST. MARY'S L.J. 357, 358 (1978).

205. *See, e.g.,* Gladwin State Bank v. Dow, 180 N.W. 601, 605 (Mich. 1920); Sienkiewicz v. Leonard Mortgage Co., 229 N.W.2d 352, 353-54 (Mich. Ct. App. 1975); Beach v. Guaranty Sav. & Loan Ass'n, 76 P. 16, 18 (Or. 1904).

borrower is viewed as a victim and allowed to sue for a remedy.²⁰⁶

Because of the illegality of usury,²⁰⁷ it logically follows that a lender cannot sue successfully to recover usurious interest.²⁰⁸ The underlying agreement to pay the principal remains enforceable²⁰⁹ unless the transac-

206. See *Bexar Bldg. & Loan Ass'n v. Robinson*, 78 Tex. 163, 167-68, 14 S.W. 227, 228 (1890). *But see Smail v. Sequoya Mobile Homes, Inc.*, 568 S.W.2d 385, 389 (Tex. Civ. App.—Amarillo 1978), *aff'd in part, rev'd in part sub nom. General Elec. Credit Corp. v. Smail*, 22 Tex. Sup. Ct. J. 319 (April 25, 1979); *cf. American Century Mortgage Investors v. Regional Center, Ltd.*, 529 S.W.2d 578, 583-84 (Tex. Civ. App.—Dallas 1975, writ *ref'd n.r.e.*) (borrower precluded from asserting subterfuge of its own making to establish usury in absence of lender's knowledge thereof). In *Smail* the court found that the plaintiff was in *pari dilecto* with the lender under a retail installment contract that failed to disclose the proper amount of the down payment as required by the Texas Consumer Credit Code. The down payment was intentionally overstated by both parties in order to facilitate financing for the transaction. See *Smail v. Sequoya Mobile Homes, Inc.*, 568 S.W.2d 385, 389 (Tex. Civ. App.—Amarillo 1978), *aff'd in part, rev'd in part sub nom. General Elec. Credit Corp. v. Smail*, 22 Tex. Sup. Ct. J. 319 (April 25, 1979); TEX. REV. CIV. STAT. ANN. art. 5069-7.02(6)(b) (Vernon 1971). It is thus apparent that the approach used by the courts will depend on the facts of the case in question.

207. See *F.B. & D., Inc. v. Nathan Alterman Elec. Co.*, 394 S.W.2d 821, 823 (Tex. Civ. App.—San Antonio 1965, writ *ref'd n.r.e.*). The purpose of the usury statutes is to prohibit usury in any form. See *id.* at 823. Prior to the 1967 statute, article 5069, the usury statutes expressly provided that all usurious contracts were "void as to interest." See 1915 Tex. Gen. Laws, ch. 28, § 13, at 50. Although the words "void as to interest" were deleted in the enactment of article 5069-1.06, the Texas Supreme Court has recently held that the borrower's obligation to pay interest is unenforceable. *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 921 (Tex. 1976). The obligation is not entirely void, however, since once the debtor has paid usurious interest, it cannot be recovered in addition to the statutory penalty. See *First State Bank v. Miller*, 563 S.W.2d 572, 576-77 (Tex. 1978).

208. *Laid Rite, Inc. v. Texas Indus., Inc.*, 512 S.W.2d 384, 392 (Tex. Civ. App.—Fort Worth 1974, no writ). In *Laid Rite* the plaintiff lender, as a condition of the loan and in consideration for making it, required the borrower to assume a note for another's debt. This note was considered interest in determining that the loan was usurious. In a suit upon the second note, the court held that when the note was assumed as part of a usurious interest rate, there could be no recovery on that note by the lender. *Id.* at 389, 392; see *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 921 (Tex. 1976) (lender cannot recover usurious interest to offset penalty of twice the interest rate).

Under article 5069-1.06(1) as it existed before the 1979 amendment, the lender was required to forfeit twice the amount of interest contracted for, charged, or received, and was prohibited from recovering any of the interest portion of the obligation. See *id.* at 921; TEX. REV. CIV. STAT. ANN. art. 5069-1.06(1) (Vernon 1971). Under the 1979 amendment, however, the forfeiture has been reduced to "three times the usurious interest contracted for, charged or received." See 1979 Tex. Sess. Law Serv., ch. 281, § 1, at 604-05 (Vernon). The unstated purpose of the amendment is apparently to allow for the enforcement of so much of the interest obligation as is legal under the applicable usury ceiling, and to allow treble damages to the debtor on the excess.

209. See *Graham & Locke Invs., Inc. v. Madison*, 295 S.W.2d 234, 245 (Tex. Civ. App.—Dallas 1956, writ *ref'd n.r.e.*). The penalty statute provides for forfeiture of twice the interest contracted for, charged, or received, but makes no mention of the effect of usury upon the principal. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06(1) (Vernon 1971). Article 5071,

tion involves more than twice the allowable interest rate under the applicable provision of the credit code.²¹⁰ In certain instances the creditor also may be able to recover attorney's fees incurred in enforcing his claim.²¹¹ Furthermore, although a note may provide for usurious interest before maturity, when there is no agreement for interest after maturity the lender may recover legal interest²¹² on the obligation of six percent from the date due.²¹³

the predecessor to the present penalty statute, expressly provided that "the principal sum or value of the contract may be received and recovered." 1963 Tex. Gen. Laws, ch. 205, § 28, at 550. Although the express provision for recovery of principal was deleted in the enactment of the credit code, the courts have nevertheless continued to enforce the underlying obligation. See *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 921-22 (Tex. 1976). Also, although the transaction involves usury, the lender may resort to foreclosure to enforce his right to the principal. See *Tanner Dev. Co. v. Ferguson*, 561 S.W.2d 777, 778, 787 (Tex. 1977); *Graham & Locke Invs., Inc. v. Madison*, 295 S.W.2d 234, 245-46 (Tex. Civ. App.—Dallas 1956, writ ref'd n.r.e.). The debtor may, however, be able to get an injunction restraining a foreclosure pending determination of the usury issue. See notes 286-296 *infra* and accompanying text for a discussion of injunctions.

210. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971) (additional forfeiture of principal when transaction involves twice allowable interest).

211. See *Miles v. W.C. Roberts Lumber Co.*, 561 S.W.2d 256, 259 (Tex. Civ. App.—Eastland 1978, writ ref'd n.r.e.); *General Am. Life Ins. Co. v. Hamor*, 95 S.W.2d 975, 978 (Tex. Civ. App.—Amarillo 1936, writ ref'd). In *Miles* the creditor brought suit for the principal due on a sworn account. Article 2226 allows recovery of attorney's fees on these claims when demand therefor remains unsatisfied after thirty days. The debtor's failure to pay the principal, which remained a valid and enforceable debt, activated article 2226 even though the lender had charged usurious interest on the account. *Miles v. W.C. Roberts Lumber Co.*, 561 S.W.2d 256, 259 (Tex. Civ. App.—Eastland 1978, writ ref'd n.r.e.); see TEX. REV. CIV. STAT. ANN. art. 2226 (Vernon Supp. 1978-1979). In *Hamor* the court allowed recovery of attorney's fees by the defendant, who was an assignee of the principal notes only and had no claim to the interest. See *General Am. Life Ins. Co. v. Hamor*, 95 S.W.2d 975, 978 (Tex. Civ. App.—Amarillo 1936, writ ref'd).

212. See TEX. REV. CIV. STAT. ANN. art. 5069-1.03 (Vernon 1971).

213. See, e.g., *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 921 (Tex. 1976); *General Am. Life Ins. Co. v. Hamor*, 95 S.W.2d 975, 978 (Tex. Civ. App.—Amarillo 1936, writ ref'd); *Deming Inv. Co. v. Clark*, 89 S.W.2d 853, 856 (Tex. Civ. App.—Waco 1935, no writ). In *Hamor* and *Deming* the award of legal interest on the principal was not based on the absence of an agreement to pay interest after maturity. Rather, the courts based their opinions on reasoning that since under repealed article 5071, 1915 Tex. Gen. Laws, ch. 18, § 13, at 50, usurious contracts were "void" as to interest, there was no agreement for interest and so the legal rate of six percent per annum could be applied to the obligation. See *General Am. Life Ins. Co. v. Hamor*, 95 S.W.2d 975, 978 (Tex. Civ. App.—Amarillo 1936, writ ref'd); *Deming Inv. Co. v. Clark*, 89 S.W.2d 853, 856 (Tex. Civ. App.—Waco 1935, no writ). There is some question whether this construction would be possible under the current statutes, since there is no provision that usurious contracts are void regarding the interest, but only that they shall be subject to the penalties provided. See TEX. REV. CIV. STAT. ANN. art. 5069-1.02 (Vernon 1971). The supreme court in *Wall* cited both *Hamor* and *Deming* as authority for its holding that in the absence of an agreement about interest after maturity, and although the agreed rate of interest prior to maturity was usurious, a six percent rate may be implied on the debt after maturity. See *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 921 (Tex. 1976). This reliance is questionable at best, since cases interpreting the statutes that

STATUTORY REMEDIES: ARTICLE 5069-1.06

One of the most far reaching, yet surprisingly uncontroversial, usury bills in the Sixty-sixth Legislature was House Bill 616, which amended article 5069-1.06,²¹⁴ and severely reduced the penalty for usury.²¹⁵ The pre-

were repealed by the enactment of the credit code are of doubtful precedential value. See *Houston Sash & Door Co. v. Heaner*, 577 S.W.2d 217, 220 (Tex. 1979). It is submitted that the holding in *Wall* should be confined solely to the facts of that case; that is, to instances in which there is no agreement about interest after maturity, and should not be extended to cases in which there is an agreement for interest after maturity that is rendered unenforceable because of its usurious nature. Any other construction would serve to defeat the purposes of the usury statutes by awarding interest to the lender although the agreement for interest between the parties is illegal and unenforceable. See *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 921 (Tex. 1976).

214. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06 (Vernon 1971). The statute sets out remedies available to victims of usurious transactions:

(1) Any person who contracts for, charges or receives interest which is greater than the amount authorized by this Subtitle, shall forfeit to the obligor twice the amount of interest contracted for, charged or received, and reasonable attorney fees fixed by the court provided that there shall be no penalty for a violation which results from an accidental and bona fide error.

(2) Any person who contracts for, charges or receives interest which is in excess of double the amount of interest allowed by this Subtitle shall forfeit as an additional penalty, all principal as well as interest and all other charges and shall pay reasonable attorney fees set by the court; provided further that any such person violating the provisions of this section shall be guilty of a misdemeanor and upon conviction thereof shall be punished by fine of not more than One Thousand Dollars. Each contract or transaction in violation of this section shall constitute a separate offense punishable hereunder.

(3) All such actions brought under this Article shall be brought in any court of this State having jurisdiction thereof within four years from the date when the usurious charge was received or collected in the county of the defendant's residence, or in the county where the interest in excess of the amount authorized by this Subtitle has been received or collected, or where such transaction had been entered into or where the parties who paid the interest in excess of the amount authorized by this Subtitle resided when such transaction occurred, or where he resides.

Id. Article 5069-1.02 provides that all usurious contracts are subject to the penalties of article 5069-1.06. See *id.* art. 5069-1.02. Other usury penalties for specific Consumer Credit Code violations in subtitle 2, however, are found in article 5069-8.01 to 8.06. See TEX. REV. CIV. STAT. ANN. art. 5069-8.01 to 8.06 (Vernon Supp. 1978-1979). House Bill 616 amends only section (1) of article 5069-1.06. Although the words to section (2) are unchanged, the consequence of this provision may have also been altered by this amendment. See text accompanying footnotes 263-265 *infra*.

215. House Bill 616 reads in pertinent part as follows:

Section 1. Subsection (1) of Article 1.06, Title 79, Revised Civil Statutes of Texas, 1925 (Article 5069-1.06, Vernon's Texas Civil Statutes), is amended to read as follows:

(1) Any person who contracts for, charges or receives interest which is greater than the amount authorized by this Subtitle, shall forfeit to the obligor three times the amount of usurious interest contracted for, charged or received, such usurious interest being the amount the total interest contracted for, charged or received exceeds the

amendment article, which remains effective only for those claims pending in litigation before the effective date of the amendment,²¹⁶ provides for a forfeiture of twice the entire rate of interest contracted for, charged, or received.²¹⁷ Under the amended article, however, the forfeiture will be "three times the amount of usurious interest contracted for, charged or received."²¹⁸ By the use of the term "usurious interest," the legislature has obviously attempted to introduce a new concept into Texas usury law: a distinction between the legal interest on an obligation, the portion of an interest obligation that is within the applicable interest ceiling, and "usurious interest," or that portion of the obligation attributable to the excess over the usury rate.²¹⁹ Although not expressly stated, the amendment apparently contemplates that the legal portion of the interest charged, received, or contracted for will remain an enforceable obligation, but the debtor is to be allowed treble damages on the "usurious interest," or excess.²²⁰ Another new provision in the usury remedy is the clause that

amount of interest allowed by law, and reasonable attorney fees fixed by the court except that in no event shall the amount forfeited be less than Two Thousand Dollars or twenty percent of the principal, whichever is the smaller sum; provided, that there shall be no penalty for any usurious interest which results in an accidental and bona fide error.

Section 2. This act shall be applicable to all claims of forfeiture made after the effective date of this Act but, with respect to claims of forfeiture in litigation pending at such effective date, the amount forfeited shall be determined under the provisions of this subsection as originally enacted.

1979 Tex. Sess. Law Serv., ch. 281, §§ 1-2, at 604-05 (Vernon).

216. *See id.* § 2. The amendment clearly states that all claims filed after the effective date of the act are subject to the new statute. Thus, although the transaction may have been entered into, and usurious interest contracted for, received or collected before the effective date of the amendment, unless a claim is filed for usury before that date then the new statute is retroactive to encompass the pre-existing debt. *Id.* § 2.

217. *See* TEX. REV. CIV. STAT. ANN. art. 5069-1.06(1) (Vernon 1971). It was the severity of the penalty under this statute, coupled with the various uncertainties of Texas usury law that led to moves in the 1979 legislative session to reduce the usury penalty. Twice the interest contracted for in a long term home mortgage or other large loan generally runs into many thousands of dollars. Moreover, the various methods of calculating interest rates, particularly with respect to front-end charges and accelerated interest, often yield substantially different results. *See generally* St. Claire, *The Spreading of Interest Under the Actuarial Method*, 10 ST. MARY'S L.J. 753 (1979).

218. *See* 1979 Tex. Sess. Law Serv., ch. 281, § 1, at 604-05 (Vernon). The bill is reprinted at footnote 215 *supra*. As originally introduced, the bill would also have deleted the provision allowing recovery for usurious interest "contracted for." The provision was reinstated, however, by floor amendment.

219. *See id.* Under the statute prior to amendment, any interest exaction that pushed the rate above the usury ceiling made the entire amount of interest usurious and subject to a penalty of twice that amount. *See* TEX. REV. CIV. STAT. ANN. art. 5069-1.06 (Vernon 1971).

220. *See* 1979 Tex. Sess. Law Serv., ch. 281, § 1, at 604-05 (Vernon). Under the prior statute, the Texas Supreme Court had held that, at least as regards the entire amount of interest, a usurious contract is unenforceable. *See* Wall v. East Tex. Teachers Credit Union,

reads "except that in no event shall the amount forfeited be less than Two Thousand Dollars or twenty percent of the principal, whichever is the smaller sum."²²¹ The amendment retains the clauses allowing recovery of reasonable attorney's fees, and the exception for an accidental and bona fide error to the forfeiture provision.²²²

The remedy for usury is available to the debtor either as a defensive offset to an action on a note or contract, or as an affirmative action to recover the statutory penalty.²²³ Unless the transaction involves more than twice the applicable rate of interest,²²⁴ the maximum forfeiture on a usurious transaction can be awarded only once, regardless of how many parties

533 S.W.2d 918, 921 (Tex. 1976). See notes 207 & 208 *supra* and accompanying text. The courts will no doubt be called upon to determine how much of the obligation will be enforceable under the new statute. There are three possibilities. The courts could, as in *Wall*, refuse to enforce the entire interest obligation, and award the debtor three times the amount the rate exacted exceeds the applicable ceiling. See *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 921 (Tex. 1976). But see *Houston Sash & Door Co. v. Heaner*, 577 S.W.2d 217, 220 (Tex. 1979) (cases interpreting prior statutes of little value in construing new ones). Second, the courts could enforce only so much of the interest obligation as falls within the applicable ceiling, and then award the debtor three times the amount of the excess. This construction would comply with the distinction, discussed above, between "legal interest" and "usurious interest" on the same obligation. See note 219 *supra*. Finally, the courts could also enforce the entire interest obligation, despite the presence of usury, and then award the debtor his remedy of three times the amount that the applicable interest rate is exceeded. This construction would alleviate the problem encountered in a recent case—what to do when usurious interest has already been paid. See *First State Bank v. Miller*, 563 S.W.2d 572, 577 (Tex. 1978) (penalty does not include recovery of usurious interest paid). This construction would also yield the smallest amount of recovery to the debtor, however, since he would, in effect, receive only twice the amount of the excess. See the discussion of *Miller* at footnotes 246-256 *infra* and accompanying text. It is apparent that until interpreted by the courts, this new amendment will inject a fair amount of uncertainty into this area of usury law.

221. See 1979 Tex. Sess. Law Serv., ch. 281, § 1, at 604-05 (Vernon).

222. *Id.*

223. *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 922 (Tex. 1976); *Miller v. First State Bank*, 551 S.W.2d 89, 99 (Tex. Civ. App.—Fort Worth 1977), *aff'd as modified*, 563 S.W.2d 572 (Tex. 1978); see *Commerce Sav. Ass'n v. GGE Management Co.*, 539 S.W.2d 71, 77 (Tex. Civ. App.—Houston [1st Dist.]), *aff'd as modified per curiam*, 543 S.W.2d 862 (Tex. 1976). It has been stated that there is a difference between the defense of usury in an action to recover the principal, and an affirmative action to recover usury penalties: "The former is defensive and the latter affirmative." *Employees Loan Co. v. Templeton*, 109 S.W.2d 774, 779 (Tex. Civ. App.—Fort Worth 1937, no writ). Thus, although the debtor may not collaterally attack a judgment on a note of which he was the maker on the ground that the judgment is excessive because of usury, he may nevertheless bring a subsequent action to recover usury penalties based on a note for which he has been adjudged liable. See *Mercer v. Bonner Loan & Inv. Co.*, 73 S.W.2d 988, 989 (Tex. Civ. App.—Fort Worth 1934, no writ). Further, although the four year statute of limitations on actions to recover statutory penalties is applicable to affirmative actions based on usury, limitations do not run against the defense of usury. See *Adleson v. B.F. Dittmar Co.*, 124 Tex. 564, 568, 80 S.W.2d 939, 941 (1935).

224. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971).

are liable on the transaction, or how many parties have rights of recovery.²²⁵ The supreme court has also clearly stated, in *Windhorst v. Adcock Pipe & Supply*,²²⁶ that only one of the three statutory conditions—either contracting for, charging, or receiving usurious interest—need occur to trigger the penalties provided in article 5069-1.06.²²⁷

A conflict of authority exists in Texas concerning whether the usury statutes are to be strictly or liberally construed. Most courts have found that usury statutes are penal in nature and subject to strict construction.²²⁸ This approach generally inures to the benefit of the lender since in a questionable case the contract is construed as not usurious.²²⁹ On the other hand, some courts have noted that the legislature intended that usury statutes should be construed liberally to accomplish the objectives of the

225. *Pinemont Bank v. DuCroz*, 528 S.W.2d 877, 879 (Tex. Civ. App.—Houston [14th Dist.] 1975, writ ref'd n.r.e.). The court of civil appeals reversed the trial court's award of twice the interest rate to each of the claimants and allowed only the total of twice the rate to be divided among them all. *Id.* at 879. *But see* *Houston Sash & Door Co. v. Heaner*, 577 S.W.2d 217, 221-22 (Tex. 1979). In *Houston Sash* the court allowed two recoveries for usury on account of the same transaction. The primary recovery was by Bedford Corporation on an open account upon which the plaintiff, Houston Sash, had made unauthorized interest charges. Bedford recovered twice the amount of interest charged as well as all of the principal of the account under subsection two of article 5069-1.06. *See* TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971). Heaner had executed a separate written agreement guaranteeing all sums owed Houston Sash by Bedford. The court found that this separate contract, which provided for an interest rate of twelve percent per annum, was sufficient to give rise to a separate liability for usury "contracted for." *See* *Houston Sash & Door Co. v. Heaner*, 577 S.W.2d, 217, 221-22 (Tex. 1979).

226. 547 S.W.2d 260 (Tex. 1977).

227. *Id.* at 261. By using the disjunctive for conditions precedent to recovery, the legislature clearly intended that only one condition is needed to set into motion the applicable penalties. *Id.* at 261; *see* *Tanner Dev. Co. v. Ferguson*, 561 S.W.2d 777, 788 (Tex. 1977) (on motion for rehearing); TEX. REV. CIV. STAT. ANN. art. 5069-1.06(1) (Vernon 1971). At least two courts have held that "contracting for" is sufficient to trigger statutory penalties. *See* *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 921 (Tex. 1976); *Riverdrive Mall, Inc. v. Larwin Mortgage Invs.*, 515 S.W.2d 5, 7 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.). Two more cases found that "charging" of usurious interest invokes the penalties. *See* *Windhorst v. Adcock Pipe & Supply*, 547 S.W.2d 260, 261 (Tex. 1977); *Moore v. Sabine Nat'l Bank*, 527 S.W.2d 209, 211-12 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.). One court has limited recovery to twice the amount "received" or actually paid. The reasoning was based on the lack of a contract for usurious interest. *See* *W.E. Grace Mfg. Co. v. Levin*, 506 S.W.2d 580, 584-85 (Tex. 1974).

228. *E.g.*, *First State Bank v. Miller*, 563 S.W.2d 572, 577 (Tex. 1978); *Pinemont Bank v. DuCroz*, 528 S.W.2d 877, 879 (Tex. Civ. App.—Houston [14th Dist.] 1975, writ ref'd n.r.e.); *Home Sav. Ass'n v. Crow*, 514 S.W.2d 160, 165 (Tex. Civ. App.—Dallas 1974), *aff'd*, 522 S.W.2d 457 (Tex. 1975); *see* *Pearce & Williams, Punitive Past to Current Convenience—A Study of the Texas Law of Usury*, 22 Sw. L.J. 233, 249 (1968).

229. *See* *Home Sav. Ass'n v. Crow*, 514 S.W.2d 160, 165 (Tex. Civ. App.—Dallas 1974), *aff'd*, 522 S.W.2d 457 (Tex. 1975). *See also* *Stacks v. East Dallas Clinic*, 409 S.W.2d 842, 844-45 (Tex. 1966) (no penalty to one merely collecting for another).

law.²³⁰ Although *First State Bank v. Miller*,²³¹ the latest case in this conflict, seems to settle the issue in favor of strict construction of the usury statutes,²³² recovery for usurious interest is provided for by a civil statute²³³ and is more a remedy than a penalty.²³⁴ It seems, therefore, that strict construction conflicts not only with prior cases²³⁵ and the general provisions for construction of civil statutes,²³⁶ but also with the legislative intent of protecting the borrower from abusive credit transactions.²³⁷

Texas cases have also evidenced a lack of consistency in the determination of the amount recoverable under article 5069-1.06(1).²³⁸ The inconsis-

230. See, e.g., *Southwestern Inv. Co. v. Mannix*, 557 S.W.2d 755, 769 (Tex. 1977) (on motion for rehearing) (inference of broad interpretation in construing statute to be reasonable and fulfill legislative intent); *Walker v. Ross*, 548 S.W.2d 447, 450 (Tex. Civ. App.—Fort Worth), writ ref'd n.r.e. per curiam, 544 S.W.2d 189 (Tex. 1977) (although penal in nature, usury statutes not to be strictly construed); *O.R. Mitchell Motors, Inc. v. Bell*, 528 S.W.2d 856, 859-60 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.) (liberal construction of usury statute). See also TEX. REV. CIV. STAT. ANN. art. 10, §§ 6, 8 (Vernon 1969) (section 6 requiring courts to follow legislative intent and section 8 requiring liberal construction to attain legal objectives and promote justice). The Texas Penal Code has been amended to state that the rule that a penal statute is to be strictly construed does not apply to the code. See TEX. PEN. CODE § 1.05(a) (Vernon 1974). See generally 10 ST. MARY'S L.J. 357, 361 (1978).

231. 563 S.W.2d 572 (Tex. 1978).

232. *Id.* at 577.

233. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06 (Vernon 1971).

234. See 10 ST. MARY'S L.J. 357, 361 (1978). See generally Pearce & Williams, *Punitive Past to Current Convenience—A Study of the Texas Law of Usury*, 22 Sw. L.J. 233, 249 (1968). The code does provide, however, that a violation of the double usury prohibition is a misdemeanor, punishable by a fine up to one thousand dollars. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971).

235. See, e.g., *Southwestern Inv. Co. v. Mannix*, 557 S.W.2d 755, 769 (Tex. 1977) (on motion for rehearing); *Walker v. Ross*, 548 S.W.2d 447, 450 (Tex. Civ. App.—Fort Worth), writ ref'd n.r.e. per curiam, 544 S.W.2d 189 (Tex. 1977); *O.R. Mitchell Motors, Inc. v. Bell*, 528 S.W.2d 856, 859-60 (Tex. Civ. App.—San Antonio 1975, writ ref'd n.r.e.).

236. See TEX. REV. CIV. STAT. ANN. art. 10, §§ 6, 8 (Vernon 1969). See generally Comment, *The Judicial Avoidance of Liberal Statutory Construction: Is Article 10, Section 8 Lost and Forgotten?*, 10 ST. MARY'S L.J. 163 (1978).

237. See *Declaration of Legislative Intent*, 15 TEX. REV. CIV. STAT. ANN. 1-2 (Vernon 1971).

Much lip-service, of course, has been given to the canon that a statute which imposes a penalty should be 'strictly' construed. *Van Zandt v. Fort Worth Press*, 359 S.W.2d 893, 895 (Tex. 1962). But this canon is simply a guide to be used when resort to it furthers the legislative purpose. The cardinal rule of construction which, significantly, has been expressly adopted by the legislature, is that 'the court shall look diligently for the intention of the Legislature, keeping in view at all times the old law, the evil and the 'remedy.' TEX. REV. CIV. STAT. ANN. art. 10(6) (Vernon 1969).

O.R. Mitchell Motors, Inc. v. Bell, 528 S.W.2d 856, 859 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.).

238. See 10 ST. MARY'S L.J. 357, 365 (1978). Compare *First State Bank v. Miller*, 563 S.W.2d 572, 577 (Tex. 1978) (amount recoverable did not include refund of interest paid) and *W.E. Grace Mfg. Co. v. Levin*, 506 S.W.2d 580, 585 (Tex. 1974) (amount recovered did not include refund of interest paid) with *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 919-21 (Tex. 1976) (dictum) (amount recoverable should include refund of interest paid).

tency has pertained to whether recovery of statutory penalties includes a refund of usurious interest paid under the agreement as well as a forfeiture of twice the usurious interest contracted for or charged.²³⁹ In *Wall v. East Texas Teachers Credit Union*²⁴⁰ the supreme court, in dictum, stated that if a lender is allowed to recover usurious interest, then forfeiture of twice the interest rate "contracted for" would be offset by that recovery, and the actual penalty to the lender would be less than twice the interest rate.²⁴¹ But in *Wall* no interest had been paid, so there was no offset for the lender, and the borrower recovered the full penalty.²⁴² In *W.E. Grace Manufacturing Co. v. Levin*,²⁴³ however, the lender had received usurious interest and he was required to pay twice the interest rate, but he was not required to return the interest received.²⁴⁴ The result was an offset in the lender's favor.²⁴⁵

This conflict concerning statutory recovery was resolved in the recent case of *First State Bank v. Miller*,²⁴⁶ in which the Texas Supreme Court stated that the usury penalty in article 5069-1.06(1) does not include the recovery of interest already paid.²⁴⁷ The court at the same time refused to express an opinion on the availability of a common law action for that recovery.²⁴⁸ The *Miller* court awarded only twice the interest contracted for, with \$14,000 of interest already paid acting as an offset in that amount for the lender.²⁴⁹ The result of *Miller* is that a lender who has already

239. Compare *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 919-21 (Tex. 1976) (indicating that refund of interest paid proper) with *First State Bank v. Miller*, 563 S.W.2d 572, 577 (Tex. 1978) (no refund allowed under statutory penalties).

240. 533 S.W.2d 918 (Tex. 1976).

241. *Id.* at 921.

242. *Id.* at 919.

243. 506 S.W.2d 580 (Tex. 1974).

244. *Id.* at 585.

245. See 10 ST. MARY'S L.J. 357, 364 (1978).

246. 563 S.W.2d 572 (Tex. 1978), noted in 10 ST. MARY'S L.J. 357 (1978).

247. *Id.* at 577. The court's express holding was that the maximum recovery authorized by section (1) of the penalty statute was twice the amount of usurious interest contracted for, charged, or received. The holding was based on reasoning that section (2) of the same statute expressly authorizes recovery of interest and other charges "as an additional penalty" in cases in which double the allowable interest rate has been exacted. The court reasoned: "If the Legislature had intended the additional penalty of forfeiture of interest paid under Section (1), it would have been a simple matter to have so stated, as in Section (2)." *Id.* at 577. The majority holding on this point evoked a forceful dissent that argued that the construction of the statute would result in inequitable enforcement of the statute depending upon whether or not the borrower had paid usurious interest. The dissent also pointed out that in cases in which the amounts of interest contracted for, charged, or received all differ, the standard for recovery, under the majority opinion, is uncertain. *Id.* at 578-80 (dissenting opinion).

248. *Id.* at 577.

249. See *id.* at 577.

collected usurious interest is allowed to retain that amount to offset the penalty.²⁵⁰ Only the lender who has not collected any interest pays the full statutory penalty without offset, and only the debtor who has paid *no* interest is returned to his original position in addition to recovering the statutory remedy.²⁵¹ The illogical result is that of placing a lender who has actually received usurious interest in a more favorable position than one who has merely contracted for usury. Also, under these interpretations, the only remedy available for recovery of usurious interest paid appears to be a common law action in the nature of a debt.²⁵² *Ferguson v. Tanner Development Co.*²⁵³ is authority for the proposition that interest paid may be recovered based upon common law pleadings rather than statutory provisions.²⁵⁴ Although the usury penalty was amended in 1979, the new statute contains no reference to a refund of usurious interest paid.²⁵⁵ *Miller* can be interpreted as a strict judicial construction of a very severe penalty,²⁵⁶ and subsequent judicial consideration of the new, less stringent penalty could call for a re-evaluation of the *Miller* case.

The second remedy, found in subsection two of article 5069-1.06, provides that when the interest contracted for, charged, or received is more than double the applicable rate, all principal, interest, and other charges, as well as attorney's fees, are forfeited as additional penalties.²⁵⁷ Subsection two was interpreted in *Lafferty v. A.E.M. Developers & Builders Co.*,²⁵⁸ in which the court held that the subsection two penalty was recoverable in addition to the penalty recoverable under subsection one.²⁵⁹ Thus, subsection two authorizes a recovery of double the interest rate contracted for, charged, or received, a refund of all interest paid and other charges,²⁶⁰

250. See *id.* at 577; *Ferguson v. Tanner Dev. Co.*, 541 S.W.2d 483, 495 (Tex. Civ. App.—Houston [1st Dist.] 1976), *rev'd on other grounds*, 561 S.W.2d 777 (1977); 10 ST. MARY'S L.J. 357, 361 (1978).

251. See 10 ST. MARY'S L.J. 357, 363-66 (1978).

252. See *First State Bank v. Miller*, 563 S.W.2d 572, 577 (Tex. 1978); *Ferguson v. Tanner Dev. Co.*, 541 S.W.2d 483, 495 (Tex. Civ. App.—Houston [1st Dist.] 1976), *rev'd on other grounds*, 561 S.W.2d 777 (1977); 10 ST. MARY'S L.J. 357, 363 (1978).

253. 541 S.W.2d 483 (Tex. Civ. App.—Houston [1st Dist.] 1976), *rev'd on other grounds*, 561 S.W.2d 777 (1977).

254. *Id.* at 495. The supreme court reversed on other grounds without addressing the issue of common law pleadings. See *Tanner Dev. Co. v. Ferguson*, 561 S.W.2d 777, 787 (Tex. 1977).

255. See 1979 Tex. Sess. Law. Serv., ch. 281, § 1, at 604-05 (Vernon).

256. See footnotes 201, 217 *supra* and accompanying text.

257. TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971).

258. 483 S.W.2d 279 (Tex. Civ. App.—San Antonio 1972, writ *ref'd n.r.e.*).

259. *Id.* at 282.

260. See *First State Bank v. Miller*, 563 S.W.2d 572, 576-77 (Tex. 1978). The *Miller* holding that section (1) of article 5069-1.06 does not provide for recovery of interest paid was based upon noting that section (2) expressly so provides. *Id.*; see TEX. REV. CIV. STAT. ANN. art. 5069-1.06(1), (2) (Vernon 1971). See notes 246 & 247 *supra* for a discussion of the *Miller* case.

and a forfeiture of all of the principal.²⁶¹ If the debtor has made no principal payments, that amount is forfeited and the debt discharged. On the other hand, the amount of principal that has been paid by the debtor is refunded to him, and the balance is discharged.²⁶² In this manner the debtor receives the full penalty of twice the interest rate exacted, and receives or retains the entire principal obligation.²⁶³

Although the wording of subsection two was not changed by the legislature in 1979, the amendment to subsection one of the statute will alter the penalty provided by the former.²⁶⁴ This is so because the penalty recoverable under subsection two is in addition to that provided in subsection one.²⁶⁵ Consequently, after the effective date of the new statute, the penalty for exacting more than twice the allowable interest rate will be a forfeiture of all principal, all interest and other charges, reasonable attorney's fees, as well as three times the amount that the interest exacted exceeds the allowable rate.²⁶⁶

In *Houston Sash and Door Co. v. Heaner*²⁶⁷ the supreme court made it clear that the penalty for "double usury"²⁶⁸ is applicable to all of the various interest rates authorized by subtitle one of the credit code, and to the exceptions thereto.²⁶⁹ In the absence of an agreement to pay interest, the maximum legal rate applicable is six percent.²⁷⁰ In that case, if the creditor has charged twelve percent, he has charged twice the legal rate applicable and is liable for the penalty provided in subsection two.²⁷¹ Furthermore, if the parties are dealing on an open account without an agreement for interest, the creditor may impose no interest charges until January 1 following the date that the account was made, and may charge only six percent per annum thereafter.²⁷² In *Houston Sash* the court held that if the creditor in this position charges any interest during the calendar year

261. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971).

262. See *Johns v. Jaeb*, 518 S.W.2d 857, 861 (Tex. Civ. App.—Dallas 1974, no writ); *Texas Tool Traders v. W.E. Grace Mfg. Co.*, 488 S.W.2d 498, 504 (Tex. Civ. App.—Dallas 1972), *aff'd as modified sub nom. W.E. Grace Mfg. Co. v. Levin*, 506 S.W.2d 580 (Tex. 1974).

263. See *Johns v. Jaeb*, 518 S.W.2d 857, 861 (Tex. Civ. App.—Dallas 1974, no writ); TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971).

264. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971); 1979 Tex. Sess. Law. Serv., ch 281, § 1, at 604-05 (Vernon).

265. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06(2) (Vernon 1971). The statute is reprinted at footnote 214 *supra*.

266. See *id.*; 1979 Tex. Sess. Law Serv., ch. 281, § 1, at 604-05 (Vernon).

267. 577 S.W.2d 217 (Tex. 1979).

268. *Id.* at 221.

269. *Id.* at 220-21.

270. See TEX. REV. CIV. STAT. ANN. art. 5069-1.03 (Vernon 1971).

271. See *Heaner v. Houston Sash & Door Co.*, 560 S.W.2d 525, 526-27 (Tex. Civ. App.—Waco 1977), *rev'd in part*, 577 S.W.2d 217 (Tex. 1979); TEX. REV. CIV. STAT. ANN. art. 5069-1.03, .06 (Vernon 1971).

272. See TEX. REV. CIV. STAT. ANN. art. 5069-1.03 (Vernon 1971).

in which the account is made, that charge constitutes "double usury" since no interest is allowable during that period and any charge would be in excess of twice the legal rate.²⁷³

COMMON LAW REMEDIES

In Texas, the existence of statutory remedies does not exclude appropriate common law remedies for usury.²⁷⁴ A common law remedy appears to be available, for instance, as a supplement to the statutory remedies since article 5069-1.06(1), as construed, does not provide for a return of usurious interest already paid.²⁷⁵ As in the case of statutory remedies, a successful assertion of a common law remedy depends upon pleadings and proof of a party's right thereto.²⁷⁶

Application of Interest Payments to Principal

It is well settled that a debtor who has proven his right to usury penalties may elect to have those penalties applied to the reduction of the outstanding balance of principal for which he remains liable.²⁷⁷ If the debtor has voluntarily paid usurious interest,²⁷⁸ and part of the principal remains unpaid, the debtor may elect to apply the interest paid to the remaining balance of the principal.²⁷⁹ It has been stated, however, that the debtor

273. See *Houston Sash & Door Co. v. Heaner*, 577 S.W.2d 217, 221 (Tex. 1979).

274. See, e.g., *Irving Bank & Trust Co. v. Second Land Corp.*, 544 S.W.2d 684, 687 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.) (injunction); *Ferguson v. Tanner Dev. Co.*, 541 S.W.2d 483, 496 (Tex. Civ. App.—Houston [1st Dist.] 1976) (common law recovery of usury paid), *rev'd on other grounds*, 561 S.W.2d 777 (Tex. 1977); *Cherry v. Berg*, 508 S.W.2d 869, 875 (Tex. Civ. App.—Corpus Christi 1974, no writ) (cancellation of instruments).

275. See, e.g., *First State Bank v. Miller*, 563 S.W.2d 572, 577 (Tex. 1978); *Bexar Bldg. & Loan Ass'n v. Robinson*, 78 Tex. 163, 168-69, 14 S.W. 227, 227-28 (1890); *Ferguson v. Tanner Dev. Co.*, 541 S.W.2d 483, 495 (Tex. Civ. App.—Houston [1st Dist.] 1976), *rev'd on other grounds*, 561 S.W.2d 777 (Tex. 1977).

276. See *First State Bank v. Miller*, 563 S.W.2d 572, 576-77 (Tex. 1978); *Burnett v. James*, 564 S.W.2d 407, 409 (Tex. Civ. App.—Dallas 1978, writ disp'd); *Irving Bank & Trust Co. v. Second Land Corp.*, 544 S.W.2d 684, 687 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.).

277. See, e.g., *Adleson v. B.F. Dittmar Co.*, 124 Tex. 564, 568, 80 S.W.2d 939, 941 (1935); *Irving Bank & Trust Co. v. Second Land Corp.*, 544 S.W.2d 684, 688 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.); *Cherry v. Berg*, 508 S.W.2d 869, 874 (Tex. Civ. App.—Corpus Christi 1974, no writ).

278. See *Cherry v. Berg*, 508 S.W.2d 869, 877 (Tex. Civ. App.—Corpus Christi 1974, no writ); *Gulf Coast Inv. Corp. v. Prichard*, 438 S.W.2d 658, 660 (Tex. Civ. App.—Dallas), *writ ref'd n.r.e. per curiam*, 447 S.W.2d 676 (Tex. 1969). To voluntarily pay on a usurious contract means that the debtor did actually pay when, if he had chosen not to pay, he could not have been compelled to do so, since usurious contracts are unenforceable with regard to the interest. See *Palmetto Lumber Co. v. Gibbs*, 124 Tex. 615, 621, 80 S.W.2d 742, 745 (1935).

279. *Cherry v. Berg*, 508 S.W.2d 869, 877 (Tex. Civ. App.—Corpus Christi 1974, no writ); *Gulf Coast Inv. Corp. v. Prichard*, 438 S.W.2d 658, 660 (Tex. Civ. App.—Dallas), *writ ref'd n.r.e. per curiam*, 447 S.W.2d 676 (Tex. 1969).

may not have the benefit of both application of payments to principal and the statutory penalties for usury for the same interest payments.²⁸⁰ Since the statute of limitations runs only against affirmative actions to recovery of usury penalties,²⁸¹ limitations do not run against a defense of usury,²⁸² nor against the debtor's right to elect to have payments of usurious interest applied against the principal.²⁸³ Thus, when all of the payments are made within the limitations period the debtor should sue for usury penalties, and then have the full usury penalty applied against the outstanding principal. On the other hand, when some of the interest payments fall outside the limitations period, the debtor may elect to have those interest payments for which recovery of penalties is barred applied against the principal, and then may recover the penalty for those payments made within the limitations period.²⁸⁴ Should the interest payments, after application to principal, be sufficient to retire the entire principal debt, the debtor is not entitled to recover the excess interest paid.²⁸⁵

280. *Adleson v. B.F. Dittmar Co.*, 124 Tex. 564, 568, 80 S.W.2d 939, 941 (1935). This statement from *Adleson* may be the reason that the supreme court was reluctant to acknowledge the existence of a common law action for the recovery of usurious interest paid in *Miller*. See *First State Bank v. Miller*, 563 S.W.2d 572, 577 (Tex. 1978). In *Miller* the borrower received the full statutory penalties for usury, but the dissent contended that the recovery was not complete unless there was a refund of usurious interest paid prior to the imposition of the statutory penalty. *Id.* at 578-79. The majority declined to consider the issue of granting recovery of interest paid absent pleadings therefor. *Id.* at 577. Although *Adleson* was not cited in *Miller*, it is submitted that recovery of usurious interest paid and application of those payments to the reduction of principal are, in effect, almost identical concepts since in each case the payments are put to the debtor's benefit. Therefore, ultimate recognition by the courts of a common law action for recovery of usury paid in addition to the statutory remedy would effectively overrule the statement in *Adleson* that a debtor may not reduce the principal and recover the penalty on account of the same payments. Compare *Ferguson v. Tanner Dev. Co.*, 541 S.W.2d 483, 495 (Tex. Civ. App.—Houston [1st Dist.] 1976) (recognition of common law action to recover usury paid in addition to statutory penalty), *rev'd on other grounds*, 561 S.W.2d 777 (Tex. 1977) with *Cherry v. Berg*, 508 S.W.2d 869, 874 (Tex. Civ. App.—Corpus Christi 1974, no writ) (debtor may not recover penalties on and reduce principal with same interest payments).

281. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06(3) (Vernon 1971) (four year statute of limitations on actions to recover penalties).

282. See *Ware v. Paxton*, 266 S.W.2d 218, 228 (Tex. Civ. App.—Eastland 1954, writ ref'd n.r.e.); *Smith v. Mason*, 39 S.W. 188, 189 (Tex. Civ. App. 1897, no writ).

283. See *Adleson v. B.F. Dittmar Co.*, 124 Tex. 564, 568, 80 S.W.2d 939, 941 (1935).

284. See *id.* The debtor may also wish to apply interest payments to principal for another reason. If he is faced with foreclosure on land that has been put up as security, he may make such an election, and if the principal is thus discharged foreclosure would no longer be proper. See *Irving Bank & Trust Co. v. Second Land Corp.*, 544 S.W.2d 684, 688 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.); *Cherry v. Berg*, 508 S.W.2d 869, 875 (Tex. Civ. App.—Corpus Christi 1974, no writ).

285. See, e.g., *Cherry v. Berg*, 508 S.W.2d 869, 876-77 (Tex. Civ. App.—Corpus Christi 1974, no writ); *Eastern Mortgage & Sec. Co. v. Collins*, 118 S.W.2d 479, 481 (Tex. Civ. App.—Galveston 1938, writ ref'd); *Ingram v. Temple Trust Co.*, 108 S.W.2d 306, 309-10 (Tex.

Injunctions

The existence of a remedy at law is not a ground for denying injunctive relief "unless the legal remedy is as practical and efficient to the ends of justice as the equitable remedy."²⁸⁶ Thus an injunction is available in a suit for usury penalties to restrain the lender from collecting usurious interest,²⁸⁷ or to prevent foreclosure and sale under a deed of trust that secures a usurious agreement.²⁸⁸ The granting of an injunction is a matter of the trial court's discretion, and will not be reversed unless there is an abuse of discretion, or a failure to apply the law correctly to the facts.²⁸⁹ If injunctive

Civ. App.—Austin 1937), *aff'd sub nom.* Glenn v. Ingram, 133 Tex. 431, 126 S.W.2d 951 (1939).

286. Irving Bank & Trust Co. v. Second Land Corp., 544 S.W.2d 684, 688 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.); *see* Long v. Castaneda, 475 S.W.2d 578, 582 (Tex. Civ. App.—Corpus Christi 1971, writ ref'd n.r.e.).

287. *See* Gifford v. State, 229 S.W.2d 949, 952 (Tex. Civ. App.—El Paso 1950, no writ) (practice of usury destroys status quo created by law that is duty of the court to re-establish); Stinson v. King, 83 S.W.2d 398, 400-01 (Tex. Civ. App.—Dallas 1935, writ dismissed) (on motion for rehearing) (debtor entitled to injunction restraining lender or lender's employees from harassment by demanding payment of note).

288. *See, e.g.,* Yonack v. Emery, 13 S.W.2d 667, 669 (Tex. Comm'n App. 1929, judgment adopted); Irving Bank & Trust Co. v. Second Land Corp., 544 S.W.2d 684, 688 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.); Poff v. Rollinsford Sav. Bank, 105 S.W.2d 782, 783-84 (Tex. Civ. App.—Amarillo 1937, no writ). It is generally held that the borrower must offer to do equity by tendering payment of the outstanding balance of the principal for which he remains liable. He is not required to actually pay the sum over to the lender or into court, however, but only to offer to do so. *See* Yonack v. Emery, 13 S.W.2d 667, 669 (Tex. Comm'n App. 1929, judgment adopted) (prayer only for excess of penalties over principal sufficient offer to do equity); Poff v. Rollinsford Sav. Bank, 105 S.W.2d 782, 783-84 (Tex. Civ. App.—Amarillo 1937, no writ) (tender of legally due principal in pleading sufficient offer).

289. Riverdrive Mall, Inc. v. Larwin Mortgage Investors, 515 S.W.2d 5, 7 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.); *cf.* Irving Bank & Trust Co. v. Second Land Corp., 544 S.W.2d 684, 687 (Tex. Civ. App.—Dallas 1976, writ ref'd n.r.e.) (record must only show probable right to recovery and probable injury should injunction not be granted to support judge's exercise of discretion). A court of civil appeals also may issue a temporary injunction to protect its jurisdiction on an appeal from a denial of an injunction by the trial court. *See* Riverdrive Mall, Inc. v. Larwin Mortgage Investors, 515 S.W.2d 2, 4 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.). In *Ex parte Hughes* the supreme court held that usury laws create only private rights, and that since there were no constitutional or statutory provisions authorizing the state to enjoin usury, nor declaring it to be a nuisance, the state had no standing to seek an injunction. *See Ex parte Hughes*, 129 S.W.2d 270, 274 (Tex. 1939). The Consumer Credit Code now provides that the Consumer Credit Commissioner may seek to enjoin violations of the consumer provisions of the code. *See* TEX. REV. CIV. STAT. ANN. art. 5069-2.03(7) (Vernon 1971). It is arguable that the chapter one provision that "contracts for usury are contrary to public policy," would satisfy the requirements laid out in *Hughes* that there be some injury to the public at large, and that the state may now properly bring actions to enjoin usury under chapter one. *See Ex parte Hughes*, 129 S.W.2d 270, 274 (Tex. 1939); Watts v. Mann, 187 S.W.2d 917, 925 (Tex. Civ. App.—Austin 1945, writ ref'd); TEX. REV. CIV. STAT. ANN. art. 5069-1.02 (Vernon 1971).

relief is denied, the debtor is left with the remedy of a suit for statutory penalties.²⁹⁰ In cases in which real property is concerned, the existence of a cause of action for damages at law should not exclude equitable relief.²⁹¹ When a substantial claim of usury is asserted, as in *Irving Bank & Trust Co. v. Second Land Corp.*,²⁹² the trial judge may preserve the status quo by injunction until the net indebtedness is ascertained at trial.²⁹³ The *Irving* court held that the value of the land need not be proven to show irreparable injury, but that one need only show that denial of an injunction is likely to cause substantial losses that would not be remedied by money damages or statutory penalties.²⁹⁴ In *Irving* the borrowers sought to enjoin the lender from sale of the borrower's land that was subject to unpaid notes.²⁹⁵ The borrowers showed that if the land were to be sold, their partnership business of sand and gravel mining would be interrupted and their equity and source of materials would be lost — the losses of which could not be compensated for by usury penalties or money damages.²⁹⁶

DEFENSES

In any claim of usury, four elements must be shown:²⁹⁷ a loan or agree-

290. See *Riverdrive Mall, Inc. v. Larwin Mortgage Investors*, 515 S.W.2d 5, 9 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.). In *Riverdrive Mall* the court of civil appeals determined that the trial judge had not abused his discretion in denying an injunction to prevent a foreclosure sale. Although the court recognized that the plaintiffs had a colorable claim of usury and had offered to do equity by their petition, it nevertheless held that the court's decision was not an abuse of discretion. The court noted that the plaintiff was actually financially unable to tender payment of the principal to the defendant, and that construction of the mall had been delayed for several months, and would be further delayed by the granting of an injunction. *Id.* at 9.

291. See *Irving Bank & Trust Co. v. Second Land Corp.*, 544 S.W.2d 684, 688 (Tex. Civ. App.—Dallas 1974, writ ref'd n.r.e.).

292. 544 S.W.2d 684 (Tex. Civ. App.—Dallas 1974, writ ref'd n.r.e.).

293. *Id.* at 688. The court noted that the penalties for usury, when applied against the principal, could retire the indebtedness and thus prevent the foreclosure sought to be enjoined. *Id.* at 688. In that case, an injunction would appear to be a more practical remedy since a foreclosure and sale upon property securing a usurious, but delinquent note, is not a nullity. See *Graham & Locke Invs., Inc. v. Madison*, 295 S.W.2d 234, 245-46 (Tex. Civ. App.—Dallas 1956, writ ref'd n.r.e.). Furthermore, it has been noted that failure to pay usurious interest is not a default authorizing acceleration of maturity and foreclosure since an agreement to pay usury is illegal and unenforceable. See *Ferguson v. Tanner Dev. Co.*, 541 S.W.2d 483, 494 (Tex. Civ. App.—Houston [1st Dist.] 1976), *rev'd on other grounds*, 561 S.W.2d 777 (Tex. 1977).

294. See *Irving Bank & Trust Co. v. Second Land Corp.*, 544 S.W.2d 684, 688 (Tex. Civ. App.—Dallas 1974, writ ref'd n.r.e.).

295. *Id.* at 686.

296. *Id.* at 688.

297. *Maxwell v. Estate of Bankston*, 433 S.W.2d 229, 232 (Tex. Civ. App.—Texarkana 1968, no writ); *Campbell v. Osby*, 239 S.W. 332, 334 (Tex. Civ. App.—El Paso 1922, no writ).

ment to lend;²⁹⁸ an agreement to repay the principal absolutely;²⁹⁹ the exaction of a greater rate of interest than legally allowed for use of the loan;³⁰⁰ and the intent to violate the usury laws.³⁰¹ Since the presence of each of these elements is essential to establish usury, the absence of any of the four elements defeats the claim of usury.³⁰² Other possible defenses include mistake or error, estoppel, disclaimers and savings clauses, purging, and the statute of limitations.

Mistake or Accidental and Bona Fide Error

No penalty for usury is imposed under article 5069-1.06 when the violation results from an accidental and bona fide error,³⁰³ but few Texas courts have been willing to find such errors. In *Guetersloh v. C.I.T. Corp.*³⁰⁴ the court found that the lender intended the interest to be at a non-usurious rate and that the illegal rate actually charged was caused by an honest mistake in calculation.³⁰⁵ It was held that the *Guetersloh* trial court correctly reformed the note to comply with the parties' intended bargain.³⁰⁶

In other cases, the courts have been reluctant to find mistake or bona fide error.³⁰⁷ A lender will not be allowed to reform a note that is usurious

298. See *Maxwell v. Estate of Bankston*, 433 S.W.2d 229, 232 (Tex. Civ. App.—Texarkana 1968, no writ); *Campbell v. Osby*, 239 S.W. 332, 334 (Tex. Civ. App.—El Paso 1922, no writ).

299. See *Pansy Oil Co. v. Federal Oil Co.*, 91 S.W.2d 453, 455-56 (Tex. Civ. App.—Texarkana 1936, writ ref'd).

300. See *id.* at 456.

301. *Miller v. First State Bank*, 551 S.W.2d 89, 98 (Tex. Civ. App.—Fort Worth 1977), *aff'd as modified*, 563 S.W.2d 572 (Tex. 1978) (intent is intent to make bargain made, not intent to commit usury); *Ferguson v. Tanner Dev. Co.*, 541 S.W.2d 483, 492 (Tex. Civ. App.—Houston [1st Dist.] 1976) (subjective intent immaterial), *rev'd on other grounds*, 561 S.W.2d 777 (Tex. 1977).

302. See *Pansy Oil Co. v. Federal Oil Co.*, 91 S.W.2d 453, 455-56 (Tex. Civ. App.—Texarkana 1936, writ ref'd); *Campbell v. Osby*, 239 S.W. 332, 334 (Tex. Civ. App.—El Paso 1922, no writ).

303. TEX. REV. CIV. STAT. ANN. art. 5069-1.06 (Vernon 1971).

304. 451 S.W.2d 759 (Tex. Civ. App.—Amarillo 1970, writ ref'd n.r.e.).

305. *Id.* at 761. Not only was there an error in calculation, but the intent to exact usury was also absent. See *id.* at 761. Another recent case involving accidental and bona fide error was *Page v. Central Bank & Trust Co.*, 548 S.W.2d 802, 803 (Tex. Civ. App.—Eastland 1977, no writ).

306. *Guetersloh v. C.I.T. Corp.*, 451 S.W.2d 759, 761 (Tex. Civ. App.—Amarillo 1970, writ ref'd n.r.e.); see *Dewey v. American Nat'l Bank*, 382 S.W.2d 524, 527 (Tex. Civ. App.—Amarillo 1964, writ ref'd n.r.e.), *cert. denied*, 382 U.S. 821 (1965).

307. See, e.g., *O.R. Mitchell Motors, Inc. v. Bell*, 528 S.W.2d 856, 861 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.) (printer's error not bona fide error of defendant); *Johns v. Jaeb*, 518 S.W.2d 857, 860 (Tex. Civ. App.—Dallas 1974, no writ) (failure of attorney to advise not accidental and bona fide error); *Townsend v. Adler*, 510 S.W.2d 175, 176 (Tex. Civ. App.—Houston [14th Dist.] 1974, no writ) (if intent existed to make the bargain made, then not error).

on its face without first establishing mutual or unilateral mistake by pleading and proof.³⁰⁸ When a note is usurious on its face, there can be no implication that the usurious interest was the result of a bona fide error without evidence that an actual error was made.³⁰⁹ Unless there is evidence that either party was misled or was ignorant of the terms of the note, a mistake theory is not a good defense to a charge of usury.³¹⁰ When a lender receives usurious interest in an honest but mistaken belief about the particular circumstances of the loan transaction, he may use mistake as a successful defense.³¹¹ Ignorance of the law, however, is not bona fide error within the statute.³¹² Thus, while the general rule prevails that ignorance of the law is no defense, ignorance of the terms of a usurious agreement may be an acceptable defense.³¹³

Another situation, closely analogous to that of mistake arises when the interest exacted, though above the legal rate, is so minimally above the rate that the existence of usury is negated.³¹⁴ When the usury exacted is trivial, the courts generally apply the doctrine of *de minimis non curat*

308. See *Southwestern Inv. Co. v. Hockley County Seed & Delinting, Inc.*, 511 S.W.2d 724, 733 (Tex. Civ. App.—Amarillo), writ ref'd n.r.e. per curiam, 516 S.W.2d 136 (Tex. 1974).

309. *Wall v. East Tex. Teachers Credit Union*, 533 S.W.2d 918, 922 (Tex. 1976).

310. See *Freeman v. Hernandez*, 521 S.W.2d 108, 111 (Tex. Civ. App.—Dallas 1975, no writ).

311. Comment, *Lender Participation in Borrower's Venture: A Scheme to Receive Usurious Interest*, 8 Hous. L. Rev. 546, 566 (1971); see *Bank of United States v. Waggoner*, 34 U.S. (9 Pet.) 378, 399 (1835) (neither party intending usury, law will not infer it); *Abilene Christian College v. Wright*, 1 S.W.2d 720, 723 (Tex. Civ. App.—El Paso 1927, writ ref'd) (lender mistaken or misled in believing contract not usurious, thus no intent and no usury).

312. See *Johns v. Jaeb*, 518 S.W.2d 857, 860 (Tex. Civ. App.—Dallas 1974, no writ) (consulting attorney no relief to taint of usury); *Townsend v. Adler*, 510 S.W.2d 175, 176 (Tex. Civ. App.—Houston [14th Dist.] 1974, no writ) (ignorance of usury laws no excuse for intentional usurious bargain).

313. Compare *Johns v. Jaeb*, 518 S.W.2d 857, 860 (Tex. Civ. App.—Dallas 1974, no writ) (ignorance of law no excuse) and *Townsend v. Adler*, 510 S.W.2d 175, 176 (Tex. Civ. App.—Houston [14th Dist.] 1974, no writ) (no excuse for ignorance of law) with *Freeman v. Hernandez*, 521 S.W.2d 108, 111 (Tex. Civ. App.—Dallas 1975, no writ) (indicating that if ignorant about terms of note or misled, then mistake good defense) and *Southwestern Inv. Co. v. Hockley County Seed & Delinting, Inc.*, 511 S.W.2d 724, 733 (Tex. Civ. App.—Amarillo) (must establish mutual or unilateral mistake by proof and pleading for valid defense of mistake), writ ref'd n.r.e. per curiam, 516 S.W.2d 136 (Tex. 1974) and *Abilene Christian College v. Wright*, 1 S.W.2d 720, 723 (Tex. Civ. App.—El Paso 1927, writ ref'd) (lender misled about meaning of terms of contract).

314. See *Peightal v. Cotton States Bldg. Co.*, 61 S.W. 428, 432 (Tex. Civ. App. 1901, no writ).

Where the amount of interest taken above the legal rate is trivial, the maximum "De minimis non curat lex," is applicable. The taking of an insignificant amount would have a tendency rather to disprove than to prove usury; for any one intending to take more profit upon a loan of money than the law would hardly be content with an exceedingly small amount. *Webb, Usury*, §210.

Id. at 432.

lex.³¹⁵ Under this doctrine, the excess interest is simply disregarded.³¹⁶

Estoppel

Although estoppel is not usually an effective defense in usury cases,³¹⁷ it may be effective with evidence of deceitful conduct.³¹⁸ In *American Century Mortgage Investors v. Regional Center, Ltd.*³¹⁹ the borrower concealed from the lender the fact that the loan was made for the benefit of a partnership and not a corporation.³²⁰ The borrower was estopped from asserting the subterfuge to establish usury unless he could show that the lender had knowledge of or acted in the subterfuge.³²¹

Disclaimers and Savings Clauses

Although men are generally presumed to have the intent to obey the law unless the contrary is shown,³²² lenders may nevertheless attempt to protect themselves from usury charges by adding disclaimers and savings clauses to their contracts.³²³ Disclaimers state that the lender lacks the requisite intent to charge usurious rates.³²⁴ A mere disclaimer will not

315. "The law does not care for, or take notice of, very small or trifling matters." BLACK'S LAW DICTIONARY 482 (4th ed. 1951); see *Thornhill v. Sharpstown Dodge Sales, Inc.*, 546 S.W.2d 151, 152 (Tex. Civ. App.—Beaumont 1976, no writ); *Miller v. Gibraltar Sav. & Bldg. Ass'n*, 132 S.W.2d 606, 607 (Tex. Civ. App.—Beaumont 1969, writ dismissed judgment corrected).

316. *Thornhill v. Sharpstown Dodge Sales, Inc.*, 546 S.W.2d 151, 152 (Tex. Civ. App.—Beaumont 1976, no writ) (forty-two cents overcharge). See also *Morris v. Jordan Financial Corp.*, 564 S.W.2d 180, 183 (Tex. Civ. App.—Tyler 1978, no writ); *Anguiano v. Jim Walter Homes, Inc.*, 561 S.W.2d 249, 255 (Tex. Civ. App.—San Antonio 1978, writ refused n.r.e.).

317. See *Miller v. First State Bank*, 551 S.W.2d 89, 101 (Tex. Civ. App.—Fort Worth 1977), *aff'd as modified*, 563 S.W.2d 572 (Tex. 1978); *Western Guaranty Loan Co. v. Dean*, 309 S.W.2d 857, 863 (Tex. Civ. App.—Dallas 1957, writ refused n.r.e.).

318. See *Miller v. First State Bank*, 551 S.W.2d 89, 101 (Tex. Civ. App.—Fort Worth 1977), *aff'd as modified*, 563 S.W.2d 572 (Tex. 1978). The five elements of equitable estoppel are (1) misrepresentation or concealment of facts, (2) made with knowledge of the true facts, (3) to one ignorant of the truth, (4) with the intent that the innocent party should act on it, (5) and the innocent party must, in fact, act upon it. *Id.* at 101.

319. 529 S.W.2d 578 (Tex. Civ. App.—Dallas 1975, writ refused n.r.e.).

320. *Id.* at 583.

321. *Id.* at 583-85. In *O'Quinn v. Beanland* the borrower successfully avoided an obligation on a note on the ground of mental incompetency, thus losing his right to assert usury. *O'Quinn v. Beanland*, 540 S.W.2d 526, 528 (Tex. Civ. App.—San Antonio 1976, no writ).

322. *Miller v. First State Bank*, 551 S.W.2d 89, 95 (Tex. Civ. App.—Fort Worth 1977), *aff'd as modified*, 563 S.W.2d 572 (Tex. 1978); see *Hernandez v. United States Fin. Co.*, 441 S.W.2d 859, 862 (Tex. Civ. App.—Waco 1965, writ dismissed).

323. See *Nevels v. Harris*, 129 Tex. 190, 198, 102 S.W.2d 1046, 1050 (1937).

324. See *id.* at 198, 102 S.W.2d at 1050. The following are two examples of savings clauses found in notes for loans.

Short form savings clause:

relieve a usurious contract of usury,³²⁵ but a savings clause, in conjunction with a disclaimer can avoid usury.³²⁶ Savings clauses, an example of which is a clause allowing the "spreading" of interest over the entire term of the loan, may protect a lender from a charge of usury.³²⁷ Generally, a lender cannot write a usurious contract and then relieve himself of usury penalties by a clause disclaiming the intent "to do that which he had already done."³²⁸ If there is a savings clause providing that an otherwise usurious interest rate is to be spread over the entire term of the loan, usury may be avoided.³²⁹

The loan evidenced by this note has been made on the assumption that all scheduled payments will be made when due and in the event of accelerated maturity from any cause any interest paid on account of this loan in excess of the maximum lawful rate to the time of such maturity shall be considered for all purposes as payment of principal.

Long form savings clause [in pertinent part]:

This instrument shall be construed under the laws of the State of Texas, and the obligation of maker to make payments of additional interest as provided for in this note is expressly limited so that the aggregate amount of all the interest due and payable by maker on this note during any period of twelve (12) calendar months shall never exceed the highest rate allowed by the usury laws of the State of Texas as construed by courts having jurisdiction thereof; and if, at the time any such payment of additional interest is due and payable, the payment of such sum would make the total interest due and payable during the twelve (12) calendar month period ending upon such due date exceed the highest rate allowed by such usury laws as construed by courts having jurisdiction thereof, the amount so payable by maker shall be reduced to an amount which, together with all other interest due and payable during that period as provided for in this note, together with any other amount or charges allocable to such period which maker may become obligated to pay under this note, the deed of trust or other security instruments, or otherwise, in connection with the borrowing evidenced hereby, which might be construed or deemed to constitute 'interest,' does not exceed interest at the highest rate permitted by the usury laws of the State of Texas, all as construed by the courts having jurisdiction thereof, and, further, any payment made of additional interest in excess of such highest rate permitted by the usury laws of the State of Texas shall be considered as a mistake and the excess thereof over such highest rate shall be returned.

See STATE BAR OF TEXAS, LEGAL FORM MANUAL FOR REAL ESTATE TRANSACTIONS, *Deed of Trust*, § 7, at 7B (1976).

325. *Nevels v. Harris*, 129 Tex. 190, 198, 102 S.W.2d 1046, 1050 (1937); *Terry v. Teachworth*, 431 S.W.2d 918, 926 (Tex. Civ. App.—Houston [14th Dist.] 1968, writ ref'd n.r.e.).

326. See *Imperial Corp. of America v. Frenchman's Creek Corp.*, 453 F.2d 1338, 1343-45 (5th Cir. 1972); *Commerce Sav. Ass'n v. GGE Management Co.*, 539 S.W.2d 71, 81 (Tex. Civ. App.—Houston [1st Dist.]), *aff'd as modified*, 543 S.W.2d 862 (Tex. 1976).

327. See *Commerce Sav. Ass'n v. GGE Management Co.*, 539 S.W.2d 71, 81 (Tex. Civ. App.—Houston [1st Dist.]), *aff'd as modified*, 543 S.W.2d 862 (Tex. 1976). For a more complete explanation of "spreading," see generally *St. Claire, The Spreading of Interest Under the Actuarial Method*, 10 ST. MARY'S L.J. 753 (1979).

328. *Riverdrive Mall, Inc. v. Larwin Mortgage Investors*, 515 S.W.2d 5, 8 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.).

329. See *Imperial Corp. of America v. Frenchman's Creek Corp.*, 453 F.2d 1338, 1343-

Purging Usury by Compromise and Settlement, Release, Novation or Renewal

Simple renewal of an originally usurious contract cannot remove the taint of usury.³³⁰ The new note must be a novation or settlement of the old note by the parties supported by new consideration in order to purge the contract of usury.³³¹ Whether a new note is a novation or merely a renewal is a question of fact.³³² By abandoning the old debt and creating a new valid one in a compromise and settlement, the contract may be purged of usury.³³³ A release in a compromise and settlement agreement may be ineffective in eliminating usury, however, if the usurious charges are carried forward into the new agreement.³³⁴ Care should be taken to ascertain that the contract has been purged of usury. If charges are carried forward, new consideration should be clearly specified.³³⁵

LIMITATION OF ACTIONS

Under article 5069-1.06 of Texas Credit Code, a cause of action for usury arises when interest greater than the amount authorized is contracted for, charged, or received.³³⁶ All usury actions, however, must be brought within

45 (5th Cir. 1972) (spreading of front end interest by savings clause over term of loan prevented charge of usury); *Commerce Sav. Ass'n v. GGE Management Co.*, 539 S.W.2d 71, 81 (Tex. Civ. App.—Houston [1st Dist.]) (spreading by savings clause allowed to prevent usury), *aff'd as modified*, 543 S.W.2d 862 (Tex. 1976). *See also Tanner Dev. Co. v. Ferguson*, 561 S.W.2d 777, 786-87 (Tex. 1977) (on motion for rehearing). When the debtor had full use of the consideration in the form of real property, although one year's interest exceeded the legal rates, that amount may be spread avoiding usury. *Id.* at 786-87.

330. *See Commerce Trust Co. v. Ramp*, 135 Tex. 84, 89-90, 138 S.W.2d 531, 534 (1940). A unilateral election by the lender to treat interest paid as return of principal and to reduce interest to a legal amount to avoid usury penalties is not a permissible method of purging usurious contracts. *Hurley v. National Bank of Commerce*, 529 S.W.2d 788, 790 (Tex. Civ. App.—Dallas 1975, writ ref'd n.r.e.). Moreover, a usurious loan made under prior law cannot be purged of usury by subsequent renewals and extensions to come within the new statute and escape usury charge. *See Hockley County Seed & Delinting, Inc. v. Southwestern Inv. Co.*, 476 S.W.2d 38, 40-41 (Tex. Civ. App.—Amarillo), *on remand*, 511 S.W.2d 724 (Tex. Civ. App.—Amarillo), *writ ref'd n.r.e. per curiam*, 516 S.W.2d 136 (Tex. 1974).

331. *Commerce Trust Co. v. Ramp*, 135 Tex. 84, 90, 138 S.W.2d 531, 534 (1940); *see Cherry v. Berg*, 508 S.W.2d 869, 873 (Tex. Civ. App.—Corpus Christi 1974, no writ).

332. *Wallace v. D.H. Scott & Son*, 133 Tex. 293, 299, 127 S.W.2d 447, 450 (1939); *Cherry v. Berg*, 508 S.W.2d 869, 873 (Tex. Civ. App.—Corpus Christi 1974, no writ); *see Commerce Trust Co. v. Ramp*, 135 Tex. 84, 90, 138 S.W.2d 531, 534 (1940). The *Ramp* court stated that novation is the purging of an executory contract, in contrast to the release of liability for interest paid. *Id.* at 90, 138 S.W.2d at 534.

333. *Southwestern Inv. Co. v. Hockley County Seed & Delinting, Inc.*, 516 S.W.2d 136, 137 (Tex. 1974); *Commerce Trust Co. v. Ramp*, 135 Tex. 84, 90, 138 S.W.2d 531, 534 (1940).

334. *Skeen v. Slavik*, 555 S.W.2d 516, 521-22 (Tex. Civ. App.—Dallas 1977, writ ref'd n.r.e.).

335. *See id.* at 521-22.

336. *See TEX. REV. CIV. STAT. ANN.* art. 5069-1.06, §§ 1, 2 (Vernon 1971).

four years of the date the usurious charge was received or collected.³³⁷ No mention is made in the statute of the time the usurious interest was contracted for.³³⁸ The date of contracting, therefore, has no bearing upon the limitations period.³³⁹ An action for debt was brought by the plaintiff in *Joy v. Fidelity Finance Co.*³⁴⁰ to recover as penalties double the amount of usurious interest collected by the defendant on three notes totaling \$800. The defendant, among other defenses, pled that the then current two year statute of limitations had run on a portion of the cause of action.³⁴¹ The court of civil appeals agreed that the statute of limitations began to run on the date the usurious interest was paid, and barred the plaintiff's cause of action on six interest installments of \$12 each on which the period of limitations had run.³⁴² A new period of limitations begins running with each usurious interest payment since receipt of each constitutes a matured cause of action; affirmative action, if taken at all, must be asserted before the limitation period expires.³⁴³ The law will not create a new contract and

337. See *id.* § 3. It should be pointed out that for transactions under subchapter two of the credit code a different statute limits the time within which actions must be brought. Regulated loans, installment loans, retail installment sales, secondary mortgage loans and motor vehicle installment sales all are within the purview of article 5069-8.04, providing for a two and a four year statute of limitation, depending upon the circumstance. See *id.* art. 5069-8.04 (Vernon Supp. 1978-1979). See also *Schmid v. City Nat'l Bank*, 132 Tex. 115, 119, 114 S.W.2d 854, 856 (1938); *Rest Haven Cemetery v. Swilley*, 127 S.W.2d 996, 1001 (Tex. Civ. App.—Galveston 1939, writ dismissed judgment corrected); *Noble v. First State Bank*, 69 S.W.2d 1114, 1115 (Tex. Civ. App.—San Antonio 1934, writ dismissed); *Hampton v. Guaranty State Bldg. & Loan Ass'n*, 63 S.W.2d 873, 875 (Tex. Civ. App.—Amarillo 1933, no writ); *Joy v. Fidelity Fin. Co.*, 60 S.W.2d 1041, 1041 (Tex. Civ. App.—Dallas 1933, no writ); *Russ v. Motor Fin. Co.*, 55 S.W.2d 645, 647 (Tex. Civ. App.—Dallas 1932, no writ).

338. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06, § 3 (Vernon 1971).

339. See *id.* Thus, the limitations period may run far beyond four years from the date of contracting. For example, if the contract is entered into in 1970, under article 5069-1.06(1) or (2), a cause of action for usury exists at that time. If the first payment of interest is received in 1971, the statute of limitations begins to run at that time. With each collection or receipt of usurious interest, the statute of limitations begins regarding that payment. Thus, if the last payment of interest is made in 1978, the last date for a cause of action within the limitations period is 1982. This is twelve years from the time of contract in 1970. See *Hurley v. National Bank of Commerce*, 529 S.W.2d 788, 790 (Tex. Civ. App.—Dallas 1975, writ reversed n.r.e.) (limitations period runs on each payment from time made). See also *Adleson v. B.F. Dittmar Co.*, 124 Tex. 564, 568, 80 S.W.2d 939, 941 (1935); *United Fin. & Thrift Co. v. Farr*, 359 S.W.2d 219, 220 (Tex. Civ. App.—Dallas 1963, no writ); *Ware v. Paxton*, 352 S.W.2d 520, 522 (Tex. Civ. App.—Dallas 1961), *aff'd in part, ref'd in part*, 359 S.W.2d 897 (Tex. 1962).

340. 60 S.W.2d 1041 (Tex. Civ. App.—Dallas 1933, no writ).

341. *Id.*

342. *Id.* at 1041-42.

343. See *Hampton v. Guaranty State Bldg. & Loan Ass'n*, 63 S.W.2d 873, 875 (Tex. Civ. App.—Amarillo 1933, no writ) (appellant's theory that cause of action accrued not on payment of interest but on payment of entire debt rejected by court); *Russ v. Motor Fin. Co.*, 55 S.W.2d 645, 647 (Tex. Civ. App.—Dallas 1932, no writ) (amended pleading not substantially different from former pleading, therefore, cause not barred by statute of limitations).

extend the limitations period "for the sole purpose of creating a right to a penalty suit" for usury.³⁴⁴

The cause of action for the statutory penalty for usury arises when usurious interest is paid in advance, and not when the entire principal and interest are liquidated.³⁴⁵ It was pointed out in *Noble v. First State Bank*³⁴⁶ that the date of payment of usurious interest is not so simply ascertained. There was an exchange, in *Noble*, of a check, a deposit slip, and a note at the time the loan was made. The dissenting judge would have held that "when all matters of form and simulated transactions are brushed aside," the usurious interest was not paid until just before maturity of the note.³⁴⁷ Under this interpretation, the dissent contended that the borrower's claim should not have been barred by the statute of limitations.³⁴⁸ *Noble* illustrated first, that ascertainment of the date of payment on which the statute of limitations begins to run is often unclear and complicated. Second, it demonstrates that the attorney should consider all possible dates upon which the statute of limitations could have begun in order to prevent being barred from asserting a valid claim of usury.

When usury is pled as a defense to a contract sued upon, it is not an affirmative action to recover the statutory penalties and, therefore, the statute of limitations does not apply.³⁴⁹ This rule, however, holds true only when the defendant's answer claims usury as the only defense.³⁵⁰ In *Commerce Savings Ass'n v. GGE Management Co.*³⁵¹ the defendants filed verified answers in an action to recover on a promissory note, alleging the transaction to be usurious. Besides alleging usury as a defense, they affirmatively prayed for relief, counterclaiming for penalty interest, attorney's fees, and exemplary damages.³⁵² Since the defendant asserted affirmative claims along with the defense of usury, the four year statute of limitations was held to apply.³⁵³

344. *Hampton v. Guaranty State Bldg. & Loan Ass'n*, 63 S.W.2d 873, 875 (Tex. Civ. App.—Amarillo 1933, no writ).

345. See *Schmid v. City Nat'l Bank*, 94 S.W.2d 554, 555-56 (Tex. Civ. App.—Fort Worth, 1936), *aff'd*, 132 Tex. 115, 114 S.W.2d 854 (1938) (lender's demand that borrower pay \$3000, or ten percent before maturity held usurious).

346. 69 S.W.2d 1114, 1115 (Tex. Civ. App.—San Antonio 1934, writ *dism'd*) (dissenting opinion).

347. *Id.* at 1115.

348. *Id.* at 1115; see *Adleson v. B.F. Dittmar Co.*, 124 Tex. 564, 568, 80 S.W.2d 939, 940-42 (1935); *Cherry v. Berg*, 508 S.W.2d 869, 874 (Tex. Civ. App.—Corpus Christi 1974, no writ).

349. See *Bexar Bldg. & Loan Ass'n v. Robinson*, 78 Tex. 163, 168-69, 14 S.W. 227, 228 (1890); *Smith v. Mason*, 39 S.W. 188, 189 (Tex. Civ. App. 1897, no writ).

350. See *Bexar Bldg. & Loan Ass'n v. Robinson*, 78 Tex. 163, 168-69, 14 S.W. 227, 228 (1890); *Smith v. Mason*, 39 S.W. 188, 189 (Tex. Civ. App. 1897, no writ).

351. 539 S.W.2d 71, 74 (Tex. Civ. App.—Houston [1st Dist.]), *modified*, 543 S.W.2d 862 (Tex. 1976).

352. *Id.* at 75.

353. *Id.* at 76.

RIGHTS AND LIABILITIES OF THIRD PARTIES

A third party's rights or liabilities regarding usury claims or defenses are determined by his relationship to the parties directly involved in the transaction alleged to be usurious.³⁵⁴ Since article 5069-1.06 provides that penalties for usury shall be forfeited "to the obligor,"³⁵⁵ the courts have limited its applicability to the "immediate parties" to the transaction.³⁵⁶ Thus, in *Houston Sash and Door Co. v. Heaner*³⁵⁷ the supreme court held that an individual guarantor of a corporate debt could not interpose the usury defense to which the corporation was entitled.³⁵⁸ Although an earlier civil appeals case had held that "[a] surety or guarantor can assert any defense to a suit on a note available to the principal,"³⁵⁹ *Houston Sash* represents a unique case.³⁶⁰ In *Houston Sash* the guarantor had signed a written guaranty agreement that provided for interest, while the underlying obligation was an open account with no agreement for interest.³⁶¹ Although the usurious nature of the underlying agreement called for a forfeiture of principal as well as penalties for usury, the guarantor had waived any requirement of a judgment on the open account before enforcement of his guaranty.³⁶² He remained liable on his guaranty, and could not set up the defense of usury available on the underlying transaction that arose because of the absence of an agreement for interest, since his written guaranty agreement did provide for interest.³⁶³

A third party is thus obliged to show that his right to question a usurious contract is derived from the rights of a party to the contract.³⁶⁴ "Successors,

354. See, e.g., *Houston Furniture Distrib., Inc. v. Bank of Woodlake*, 562 S.W.2d 880, 884 (Tex. Civ. App.—Houston [1st Dist.] 1978, no writ) (liabilities); *Gubitosi v. Buddy Schoellkopf Prod., Inc.*, 545 S.W.2d 528, 534 (Tex. Civ. App.—Tyler 1976, no writ) (liabilities); *Micrea, Inc. v. Eureka Life Ins. Co. of America*, 534 S.W.2d 348, 354 (Tex. Civ. App.—Fort Worth 1976, writ ref'd n.r.e.) (rights); *Lydick v. Stamps*, 316 S.W.2d 107, 110 (Tex. Civ. App.—Fort Worth 1958, writ ref'd n.r.e.) (rights).

355. See TEX. REV. CIV. STAT. ANN. art. 5069-1.06 (Vernon 1971).

356. See *Houston Sash & Door Co. v. Heaner*, 577 S.W.2d 217, 222 (Tex. 1979); *Micrea, Inc. v. Eureka Life Ins. Co. of America*, 534 S.W.2d 348, 354 (Tex. Civ. App.—Fort Worth 1976, writ ref'd n.r.e.).

357. 577 S.W.2d 217 (Tex. 1979).

358. *Id.* at 222.

359. *Stephens v. First Bank & Trust*, 540 S.W.2d 572, 574 (Tex. Civ. App.—Waco 1976, writ ref'd n.r.e.).

360. See *Houston Sash & Door Co. v. Heaner*, 577 S.W.2d 217, 222 (Tex. 1979).

361. See *id.* at 218-19.

362. See *id.* at 221-22.

363. See *id.* at 221-22. It is questionable whether the court's conclusion would have been the same had the guarantee agreement not provided for interest. In that case, it would seem that the creditor would have made the same usurious demands against the guarantor as against the primary obligor. See *id.* at 221-22; *Stephens v. First Bank & Trust*, 540 S.W.2d 572, 574 (Tex. Civ. App.—Waco 1976, writ ref'd n.r.e.).

364. See *Micrea, Inc. v. Eureka Life Ins. Co. of America*, 534 S.W.2d 348, 354 (Tex. Civ.

guarantors, assignees or anyone" on behalf of a corporation are prohibited by article 1302-2.09 from the claim or defense of usury unless the corporation has the right.³⁶⁵ The term "guarantor" in article 1302-2.09 extends to guarantors of all kinds.³⁶⁶ For example, the president of a corporation, as corporate guarantor, cannot assert the defense of usury unless the corporation could do so.³⁶⁷ An individual guarantor of a corporate loan does not have a claim of usury under article 1302-2.09, even though he is primarily liable on the loan.³⁶⁸ To sue successfully on a claim of usury on a corporate loan, an individual must sue as a comaker with control over the corporate borrower.³⁶⁹

A guarantor or surety may be sued independently and separately on a debt and cannot assert usury when the party or corporation accommodated could not do so.³⁷⁰ A guarantor's liability on a debt is determined by the principal's liability, unless expressly limited or extended by agreement.³⁷¹ An agreement limiting the guarantor's liability to the remaining balance of the principal limits the guarantor's liability to that remainder plus the

App.—Fort Worth 1976, writ ref'd n.r.e.); *Lydick v. Stamps*, 316 S.W.2d 107, 110 (Tex. Civ. App.—Fort Worth 1958, writ ref'd n.r.e.). In a 1977 case, a bank, as assignee of a note by the maker, paid the payee allegedly usurious interest on behalf of the maker. Since no interest was paid on the bank's behalf, no cause of action accrued to it; the cause of action accrued to the maker of the note. *See Izaks v. National Bank of Commerce*, 547 S.W.2d 345, 350 (Tex. Civ. App.—Tyler 1977, no writ); *cf. Stephens v. First Bank & Trust*, 540 S.W.2d 572, 574 (Tex. Civ. App.—Waco 1976, writ ref'd n.r.e.) (surety or guarantor can assert any defense available to principal party in suit on note).

365. *See* TEX. REV. CIV. STAT. ANN. art. 1302-2.09 (Vernon Supp. 1963-1978); Dorsaneo, *Creditors Rights, Annual Survey of Texas Law*, 31 Sw. L.J. 213, 233 (1977).

366. *Hutchinson v. Commercial Trading Co.*, 427 F. Supp. 662, 667 (N.D. Tex. 1977); *see Universal Metals & Mach., Inc. v. Bohart*, 539 S.W.2d 874, 879 (Tex. 1976).

367. *See Loomis Land & Cattle Co. v. Diversified Mortgage Investors*, 533 S.W.2d 420, 425-26 (Tex. Civ. App.—Tyler 1976, writ ref'd n.r.e.); Dorsaneo, *Creditors Rights, Annual Survey of Texas Law*, 31 Sw. L.J. 213, 234 (1977).

368. *VIP Commercial Contractors v. Alkas*, 553 S.W.2d 656, 658 (Tex. Civ. App.—San Antonio 1977, no writ); *see* TEX. REV. CIV. STAT. ANN. art. 1302-2.09 (Vernon Supp. 1963-1978). Normally, loans involving individuals are limited to a ten percent maximum interest rate. *See id.* art. 5069-1.02 (Vernon 1971).

369. *See Sud v. Morris*, 492 S.W.2d 335, 337-38 (Tex. Civ. App.—Beaumont 1973, no writ); Dorsaneo, *Creditors Rights, Annual Survey of Texas Law*, 31 Sw. L.J. 213, 233-34 (1977).

370. *See, e.g., Hutchinson v. Commercial Trading Co.*, 427 F. Supp. 662, 667 (N.D. Tex. 1977); *Universal Metals & Mach., Inc. v. Bohart*, 539 S.W.2d 874, 879 (Tex. 1976); *Loomis Land & Cattle Co. v. Diversified Mortgage Investors*, 533 S.W.2d 420, 426 (Tex. Civ. App.—Tyler 1976, writ ref'd n.r.e.). A guaranty agreement may waive the legal requirement that a lender must first exhaust his rights against the maker of a note. *Hartnett v. Adams & Holmes Mortgage Co.*, 539 S.W.2d 181, 183 (Tex. Civ. App.—Texarkana 1976, no writ).

371. *Houston Furniture Distrib., Inc. v. Bank of Woodlake*, 562 S.W.2d 880, 884 (Tex. Civ. App.—Houston [1st Dist.] 1978, no writ); *Gubitosi v. Buddy Schoellkopf Prod., Inc.*, 545 S.W.2d 528, 534 (Tex. Civ. App.—Tyler 1976, no writ).

interest on the balance.³⁷² When the guarantor's agreement with the borrower does not indicate at what point a guarantor's liability arises, then the filing of the suit by the lender will operate as a demand on the guarantor.³⁷³ Guarantors, however, are not necessary parties to a suit for recovery of amounts owed even though it is alleged they paid part of the interest.³⁷⁴ In considering liabilities of third parties from the lender's view point, it is important to remember that assignees of lenders are charged with knowledge of the usurious nature of the contract and are liable for the statutory penalties.³⁷⁵

EXCEPTIONS TO THE USURY STATUTES

Corporations

In Texas, corporations are not governed by the maximum interest rate of ten percent.³⁷⁶ With certain exceptions "as otherwise fixed by law," article 5069-1.02 sets the maximum legal rate of interest at ten percent and provides that *all* usurious contracts are against public policy and are subject to the penalties in article 5069-1.06.³⁷⁷ One exception "otherwise fixed by law" is article 1302-2.09, which sets the maximum borrowing rate for corporations at one and one-half percent per month for loans over \$5000.³⁷⁸ Although article 1302-2.09 is not in the same subtitle as article 5069-1.06, the court in *Texas Tool Traders v. W.E. Grace Manufacturing Co.*³⁷⁹ held that the legislature intended that the penalties in article 5069-1.06 apply

372. *Commerce Sav. Ass'n v. GGE Management Co.*, 539 S.W.2d 71, 77 (Tex. Civ. App.—Houston [1st Dist.]) (limitation of liability also negated claim of usury), *modified and aff'd per curiam*, 543 S.W.2d 862 (Tex. 1976).

373. *See Hargis v. Radio Corp. of America*, 539 S.W.2d 230, 232-33 (Tex. Civ. App.—Austin 1976, no writ).

374. *Sud v. Morris*, 492 S.W.2d 335, 338 (Tex. Civ. App.—Beaumont 1973, no writ).

375. *See North Am. Acceptance Corp. v. Warren*, 451 S.W.2d 921, 925-26 (Tex. Civ. App.—Dallas 1970, writ ref'd n.r.e.); *Lydick v. Stamps*, 316 S.W.2d 107, 110 (Tex. Civ. App.—Fort Worth 1958, writ ref'd n.r.e.).

376. *See Sud v. Morris*, 492 S.W.2d 335, 337 (Tex. Civ. App.—Beaumont 1973, no writ). Compare TEX. REV. CIV. STAT. ANN. art. 1302-2.09 (Vernon Supp. 1963-1978) (corporate rate) with *id.* art. 5069-1.02 (Vernon 1971) (general interest rate).

377. *Texas Tool Traders v. W.E. Grace Mfg. Co.*, 488 S.W.2d 498, 502 (Tex. Civ. App.—Dallas 1972), *modified and aff'd sub nom.*, *W.E. Grace Mfg. Co. v. Levin*, 506 S.W.2d 580 (Tex. 1974); *see* TEX. REV. CIV. STAT. ANN. art. 5069-1.02, .06 (Vernon 1971); *cf. id.* art. 5069-8.01 to 8.06 (Vernon Supp. 1978-1979) (providing penalties for usurious violations of subtitle 2, article 5069, consumer credit section of code).

378. *See* TEX. REV. CIV. STAT. ANN. art. 1302-2.09 (Vernon Supp. 1963-1978). An eighteen percent annual interest rate has been discussed as equivalent to a one and one-half percent per month rate without regard to computation methods. *See Micrea, Inc. v. Eureka Life Ins. Co. of America*, 534 S.W.2d 348, 353 (Tex. Civ. App.—Fort Worth 1976, writ ref'd n.r.e.).

379. 488 S.W.2d 498 (Tex. Civ. App.—Dallas 1972), *modified and aff'd sub nom.* *W.E. Grace Mfg. Co. v. Levin*, 506 S.W.2d 580 (Tex. 1974).

to all transactions exceeding the maximum legal rate of interest whether under article 5069 or article 1302.³⁸⁰

Avoidance of the ten percent maximum legal interest rate for loans can be achieved by incorporation. Lenders may validly require borrowers to incorporate prior to entering into a loan agreement.³⁸¹ In *Skeen v. Glenn Justice Mortgage Co.*³⁸² the court held that a loan contract was not void or illegal even though the borrowing corporation was formed solely to qualify for the loan.³⁸³ Moreover, in *American Century Mortgage Investors v. Regional Center, Ltd.*³⁸⁴ the court noted that incorporation was demanded to comply with the usury laws, not to evade them.³⁸⁵ It could be argued, of course, that while complying with the law allowing corporations to borrow at one and one-half percent per month interest rates, the intent of forced incorporation is to avoid the ten percent per annum ceiling for non-corporate loans. Regardless of the logic in this argument, the courts in *Skeen* and *American Century* refused to recognize it.³⁸⁶

Texas has yet to deal adequately with two problems raised by forced incorporation. The first problem was pointed out in *Hutchinson v. Commercial Trading Co.*,³⁸⁷ in which the court hypothesized a circumstance in which an inexperienced borrower was forced to incorporate for a "personal and necessitous" loan by a lender in a superior bargaining position.³⁸⁸ The *Hutchinson* court concluded that this loan probably would be found to be usurious in Texas.³⁸⁹ To date, this conclusion has not been tested. The second problem involves the tax consequences of forming corporations solely for the purpose of borrowing.³⁹⁰ When a corporation carries on a

380. *Id.* at 502.

381. *See Hutchinson v. Commercial Trading Co.*, 427 F. Supp. 662, 666 (N.D. Tex. 1977); *Dicker v. Lomas & Nettleton Fin. Corp.*, 576 S.W.2d 672, 676 (Tex. Civ. App.—Texarkana 1978, no writ).

382. 526 S.W.2d 252 (Tex. Civ. App.—Dallas 1975, no writ).

383. *Id.* at 256; *see Houston Furniture Distrib., Inc. v. Bank of Woodlake*, 562 S.W.2d 880, 883 (Tex. Civ. App.—Houston [1st Dist.] 1978, no writ).

384. 529 S.W.2d 578 (Tex. Civ. App.—Dallas 1975, writ ref'd n.r.e.).

385. *Id.* at 582.

386. *See id.* at 582; *Skeen v. Glenn Justice Mortgage Co.*, 526 S.W.2d 252, 256 (Tex. Civ. App.—Dallas 1975, no writ).

387. 427 F. Supp. 662 (N.D. Tex. 1977).

388. *Id.* at 666; *see Heath & Bentley, Real Property, Annual Survey of Texas Law*, 32 Sw. L.J. 27, 80 (1978); 29 Sw. L.J. 959, 963-64 (1975).

389. *Hutchinson v. Commercial Trading Co.*, 427 F. Supp. 662, 666 (N.D. Tex. 1977); *see 418 Trading Corp. v. Oconefsky*, 234 N.Y.S.2d 747, 749 (Sup. Ct. 1962), *aff'd*, 240 N.Y.S.2d 956 (App. Div. 1963), *aff'd*, 198 N.E.2d 907, 249 N.Y.S.2d 246 (1964) (disregarded corporate exception to usury laws when individual incorporated for personal loan and lender had knowledge of this fact); 29 Sw. L.J. 959, 963-64 (1975) (Texas courts likely to find usury for public policy reasons when corporate loans for personal use).

390. *See generally* Comment, *Using a Dummy Corporate Borrower Creates Usury and Tax Difficulties*, 28 Sw. L.J. 437, 451-52 (1974).

business activity, such as borrowing, it cannot be considered a passive non-taxable entity.³⁹¹ Incorporation for borrowing purposes generally entails a greater taxation burden on the borrower.³⁹² Although extensive analysis of tax or other consequences of incorporation is beyond the scope of this paper, in looking to the corporate exception for borrowing relief, both the borrower and the lender should be aware of at least two possible problem areas — the tax consequences and the purpose for which the loan is made.³⁹³

Real Property Improvement

A 1975 addition to article 5069-1.07 provides that certain real estate loans of \$500,000 or more are to have the same maximum interest rates as corporate loans.³⁹⁴ Although the courts have not yet construed this subsection, several questions might be raised. It is unclear whether the reference to construction loans in 5069-1.07(b) means that the entire amount must be spent on land acquisition.³⁹⁵ To avoid a possible conflict with the statute, two separate loan transactions, one for construction and one for land acquisition, could be made; or perhaps the loan contract could specifically apportion the costs.³⁹⁶ Another question concerns the definition to be given "improved real property" as used in article 5069-1.07. Regulation 8.1A of the Texas Savings and Loan Commission defines "improved real estate" as (1) land where there is a permanent building, (2) land or site ready for

391. See *Moline Properties, Inc. v. Commissioner*, 445 F.2d 455, 457 (1st Cir. 1971).

392. See generally Comment, *Using a Dummy Corporate Borrower Creates Usury and Tax Difficulties*, 28 Sw. L.J. 437, 451-61 (1974). In this comment, the writer discusses at least one possible remedy—the corporate agent. See *id.* at 453-57.

393. See *id.* at 459-61.

394. TEX. REV. CIV. STAT. ANN. art. 5069-1.07(b) (Vernon Supp. 1978-1979) provides: (b) Notwithstanding any contrary provisions of the law, any person may agree to pay, and may pay pursuant to such an agreement, the same rate of interest as corporations (other than non-profit corporations) on any loan in the principal amount of \$500,000 or more, which is made for the purpose of interim financing for construction on real property or financing or refinancing of improved real property, and such a loan shall not be subject to the defense of usury unless it exceeds the maximum lawful interest rate for corporations (other than non-profit corporations).

Id. This article was amended in 1979, and many of the questions raised in the text have been clarified. See 1979 Tex. Sess. Law Serv., ch. 305, § 1, at 704 (Vernon). For a discussion of the amended statute, see Roberts, *The Revised Article 5069-1.07(b)*, 10 ST. MARY'S L.J. 699 (1979).

395. For a possibly analogous interpretation of a construction loan, refer to the Texas Uniform Commercial Code, § 9.313(a) (3), for a definition of a "construction mortgage" as used in section 9. The pertinent part reads "a mortgage is a 'construction mortgage' to the extent that it secures an obligation incurred for the construction of an improvement on land including the acquisition cost of the land, if the recorded writing so indicates." TEX. BUS. & COM. CODE ANN. § 9.313(a) (3) (Tex. UCC) (Vernon Supp. 1978-1979).

396. Oxford, *Usury Update*, 15 REAL EST., PROB. & TR. LAW NEWSLETTER 35 (Oct. 1977).

construction of such a building, (3) improved land which provides sufficient income to maintain the property and to retire the loans, and (4) land to be improved in either (1), (2) or (3).³⁹⁷ The National Bank Act Regulations also provide a definition of improved land.³⁹⁸ Whether or not real estate is improved has been left to the discretion of Texas courts in condemnation proceedings³⁹⁹ and may also be left to their discretion under article 5069-1.07. It has been noted that article 5069-1.07(b) is prospective and may not be effective for loans made prior to September 1, 1975, or for renewals of loans originally made prior to that date.⁴⁰⁰

Oil and Gas Exploration

Another new subsection of article 5069-1.07 has excepted loans exceeding \$500,000 for oil and gas exploration, development, and reworking of oil and gas wells.⁴⁰¹ Questions in this area will arise with respect to certain definitions of terms used in the statute, such as "exploration," "development," "indirect costs," and "working interest."⁴⁰² Another relevant question is how far beyond the wellhead phase financing can go under this subsection.⁴⁰³

Other New Exceptions

Two other new sections, article 5069-1.08 and 1.09, have been added as usury exceptions, but have not been construed by the courts.⁴⁰⁴ Article

397. *Id.* at 36.

398. 12 C.F.R. § 7.2020(b) (1978).

399. Oxford, *Usury Update*, 15 REAL EST. PROB. & TR. LAW NEWSLETTER 35, 37 (Oct. 1977); see *Texas Power & Light v. Lovinggood*, 389 S.W.2d 715, 717-18 (Tex. Civ. App.—Dallas 1965, no writ).

400. See Wallenstein & St. Claire, *Property, Annual Survey on Texas Law*, 30 Sw. L.J. 28, 45-46 (1976).

401. TEX. REV. CIV. STAT. ANN. art. 5069-1.07(c) (Vernon Supp. 1978-1979) provides: (c) Notwithstanding any contrary provisions of law, any person may agree to pay, and may pay pursuant to such an agreement, the same rate of interest as corporations (other than nonprofit corporations) on any loan in the principal amount of \$500,000 or more, which is made for the purpose of the payment of the direct or indirect costs of exploration for oil and gas, the development of oil and gas properties, or the reworking of oil or gas wells, provided that the value of the collateral securing such loans is reasonably estimated by the lender at the time of the making of the loan to be in excess of the amount of the loan. Such a loan shall not be subject to the defense of usury or the penalties for usury unless the interest rate exceeds the maximum lawful interest rate for corporations (other than nonprofit corporations).

Id.

402. See Oxford, *Usury Update*, 15 REAL EST., PROB. & TR. LAW NEWSLETTER 35, 39 (Oct. 1977).

403. *Id.* at 39.

404. See TEX. REV. CIV. STAT. ANN. art. 5069-1.08, .09 (Vernon Supp. 1978-1979).