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Louisiana Loan Laws

Herschel C. Adcock

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tled character of this area of the law by expressing no opinion as to whether insane persons are required to conform for their own protection to the standard of conduct which society demands of sane persons.²⁶

In those cases where the mentally ill plaintiff was under the care and control of a hospital at the time of the accident, the distinction between absolute insanity and less severe mental illness, as well as the disagreement as to its effect upon the degree of care expected of the plaintiff appears less significant.²⁷ These cases place considerable emphasis upon the special duty relationship formed and tend to require a lower standard of care from the patient for his own safety. However, since a hospital is not an insurer, the patient is always required to exercise whatever capacity he has for his own protection.²⁸ Other than this somewhat more liberal approach when the patient-plaintiff is under the care of a hospital, few generalizations can be deduced.

Thus, as the California Supreme Court expressed in the *Vistica* case, in perhaps too succinct a manner, the jury has the well-placed but difficult responsibility of weighing the patient's capacity to protect himself with the hospital's concomitant duty to guard the patient in determining the "responsible cause" of the accident.

Chester H. Budz, Jr.

LOUISIANA LOAN LAWS

We are living in a society geared to a "buy-now-pay-later" plan. Almost any consumer¹ can finance his goods and services over an extended monthly payment plan. The financing of goods and services is broadly categorized as consumer credit. The arrangement for extension of credit may be made by the consumer with the person or organization providing the goods or furnishing the services or with some other entity which advances the cash to the consumer to pay for such goods or services in return for the consumer's promise to repay the advance. Consumer

26. RESTATEMENT (SECOND) OF TORTS § 464, caveat (1965).

27. See *Lange v. United States*, 179 F. Supp. 777 (N.D.N.Y. 1960); *Emory Univ. v. Lee*, 97 Ga. App. 680, 104 S.E.2d 234 (1953); *Doty v. State*, 33 Misc. 2d 330, 226 N.Y.S.2d 901 (Ct. Cl. 1961).

28. *DeMartini v. Alexander Sanitarium, Inc.*, 192 Cal. App. 2d 442, 13 Cal. Rptr. 564 (1961).

1. Any person who acquires goods or services which he or his family will use primarily for purposes other than business or capital producing is, at least in relation to such goods or services, a consumer.

credit has skyrocketed from less than \$1 billion at the end of World War I to more than \$69 billion in 1963,² of which approximately one-third was granted by finance companies.³

Finance Company, Loan Company, and Small Loan Company are synonymous terms as understood by the average man. These lending institutions represent, perhaps, one of the most misunderstood industries known to our society. The purpose of this Note is to briefly explain the various statutes regulating interest charges on loans in Louisiana, to point out areas where Louisiana has failed to regulate interest, and to examine some problems emanating from our usury laws.

Louisiana Small Loan Act

The Louisiana Small Loan Act⁴ regulates the rate of interest that may be charged on loans not exceeding \$300.00. The Small Loan licensee may collect interest at a rate not exceeding 3½% a month on the principal not in excess of one hundred and fifty dollars, and at a rate not exceeding 2½% a month on the principal in excess of one hundred and fifty dollars up to a maximum of three hundred dollars. In less complex terms, the statute permits a lender to collect \$124.56 on a loan of \$100.00 provided the loan is paid out in twelve installments of \$10.38.⁵ Should the borrower fail to make the monthly installments and elect to pay a lump sum at the end of the year, he will owe \$142.00.⁶ On a loan of \$300.00, the borrower must repay \$366.96 in twelve monthly installments of \$30.58 or one lump sum of \$409.50 at the end of a year.⁷

In recent years there has been a gradual decrease in Small Loan volume.⁸ This decrease can be attributed primarily to two factors. The first and more obvious factor is that the borrower

2. B. CURRAN, TRENDS IN CONSUMER CREDIT LEGISLATION 1 n.2 (1965).

3. 50 FED. RESERVE BULL. 376 (1964). Sales finance companies comprise 25%, or \$13,523,000,000.00, and small loan companies 8.5%, or \$4,590,000,000.00.

4. LA. R.S. 6:571-93 (1950), *as amended*, La. Acts 1952, No. 169, § 1.

5. The Small Loan Law is based on twelve, thirty-day months, thus permitting the collection of five additional days interest.

6. The collection of \$142.00 for a loan of \$100.00 is why the label of "Forty-Two Percenters" has been placed on the Small Loan Companies.

7. These rates were obtained from a rate chart based on the Louisiana Small Loan Act and verified as correct by the State Banking Department.

8. 1966-1967 LA. STATE BANKING DEP'T 37TH BIENNIAL REPORT 79-80. As of December 31, 1967, there were 941 Small Loan companies licensed under the Louisiana Small Loan Act with assets of \$52,831,209.79. The total number of loans made during the calendar year ending December 31, 1967, numbered 262,620 with a total outlay of \$51,920,641.22. The number of Small Loan companies increased from 915 licensees in 1966 to 941 in 1967 while the number of loans made decreased from 268,639 in 1966 to 262,620 in 1967.

is no longer satisfied with a loan of \$300.00; he needs more money. Secondly, the lender is anxious to lend him more funds in order to "discount" the interest because loans in excess of \$300.00 are much more lucrative.

Motor Vehicle Loan Laws

Motor vehicle loans are regulated by the Motor Sales Finance⁹ and Direct Vehicle Loan Company¹⁰ acts.¹¹ The finance rates and provisions of these two acts are identical¹² except that the former applies when the vendor of a motor vehicle finances the sale and the latter applies when a lender places a chattel mortgage on a motor vehicle.

Finance charge limitations under these acts are even more complex than those under the Louisiana Small Loan Act. The rates are broken down into four classes, according to the age of the automobile.¹³ Class 1 applies to new motor vehicles and provides for a rate of $1\frac{1}{4}\%$ per month simple interest on the declining balance or \$8.30 per \$100.00 over a twelve-month installment period. Class 2 applies to used vehicles not more than two years old and provides for a rate of $1\frac{3}{4}\%$ per month simple interest on the declining balance or \$11.73 per \$100.00 over a twelve-month installment period. Class 3 applies to vehicles not in class 1 or 2 but not more than four years old and provides for a rate of $2\frac{1}{4}\%$ per month simple interest on the declining balance or \$15.22 per \$100.00 over a twelve-month installment period. Class 4 applies to all other motor vehicles not covered in classes 1, 2, or 3, and provides for a rate of $2\frac{1}{4}\%$ per month simple interest on

9. LA. R.S. 6:951-64 (1950), *as last amended*, La. Acts 1966, No. 515, § 1.

10. LA. R.S. 6:970-76 (1950) *as last amended*, La. Acts 1966, No. 515, § 2.

11. To date, the Louisiana Motor Vehicle Commission has issued a total of 553 licenses under the Motor Sales Finance Act and 145 licenses under the Direct Vehicle Loan Company Act. The Commission does not require a reporting by the licensees of the number of loans or the total volume of loans.

12. LA. R.S. 6:974 (Supp. 1968): "The provisions of R.S. 6:957, R.S. 6:958, and R.S. 6:959 also shall apply to any direct vehicle loan company and any direct vehicle loan."

13. LA. R.S. 6:957 (Supp. 1968). These rates are based on information received from the office of M. F. Holland, Executive Director of Motor Vehicle Commission, 234 Loyola Ave., New Orleans, La. The actual rates quoted are as follows:

Class 1	8.30997 per annum add on.
Class 2	11.73652 per annum add on.
Class 3	15.22088 per annum add on.
Class 4	15.22088 per annum add on, plus a flat charge of \$1.00 per month not to exceed twelve months.

The Motor Vehicle Commission employs investigators to visit and audit licensees. In addition to the investigators, the Commission also receives a microfilm on all automobile titles issued by the state so it may determine whether a mortgage has been recorded on the title.

the declining balance, plus a flat charge of \$1.00 per month up to a maximum of twelve months, or \$16.22 per \$100.00 over a twelve-month installment period.

The buyer or borrower has a right to prepay his loan and receive a refund of unearned interest.¹⁴ The amount of refund shall be at least 90% as great a proportion of the finance charge (after first deducting from such finance charge a charge of \$25.00) as the sum of the monthly time balance (beginning one month after the month in which prepayment is made) bears to the sum of all the monthly time balances under the schedule of payments in the contract; this method of refund upon prepayment is commonly referred to as the "Rule of 78" or the "Sum of the Digits" refund method.¹⁵ After the contract has run twelve months, the \$25.00 may not be deducted prior to computing the refund of unearned interest.¹⁶

Discount Loans

Loans in excess of \$300.00 made with security other than motor vehicles are commonly referred to as "discount" loans. The name is derived from a practice, sanctioned by our courts,¹⁷ adopted to avoid the Louisiana usury statute.¹⁸

The legal rate of interest that may be charged on loans in excess of \$300.00 is 8% per annum.¹⁹ However, if the lender pre-

14. LA. R.S. 6:958, *as amended*, La. Acts 1962, No. 139, § 1.

15. On a 24-month contract with an interest charge of \$300.00, the refund of unearned interest would be as follows:

If the contract is prepaid in the sixth month, the debtor is entitled to 90% of 57% of the interest charge (\$300) after first deducting \$25.00, or a total refund of \$128.25 ($\$300 - \$25 \times 57\% \times 90\% = \text{Refund}$).

If the contract is prepaid in the twelfth month, the debtor is entitled to 90% of 26% of the interest charge (\$300) after first deducting \$25, or a total refund of \$58.50 ($\$300 - \$25 \times 26\% \times 90\% = \text{Refund}$).

16. LA. R.S. 6:958 (1950), *as amended*, La. Acts 1962, No. 139 § 1.

17. Customer borrowed \$9,933.70 and executed promissory note for \$15,000.00, bearing 8% per annum interest from date until paid, payable in \$400.00 monthly installments. Interest on note "from date" was illegal but principal of \$15,000.00 was legal. *Mayfield v. Nunn*, 239 La. 1021, 121 So.2d 65 (1960).

"[P]arties would be permitted to recover usurious interest by merely capitalizing it with transactions foreign to the principal obligation and by this means circumventing the law." *Vosbein v. Leopold*, 230 La. 21, 28, 87 So.2d 715, 717 (1956).

A note acquired by a finance company at a discount of 11% on its face value, but conditioned to bear interest at 8% from maturity, "since it does not bear more than 8% interest after maturity it cannot be said to carry usurious interest." *General Securities Co. v. Jumonville*, 216 La. 681, 686, 44 So.2d 702, 703 (1950).

Customer borrowed \$2000.00 and executed note for \$3744.00. The court stated that there is no limit to the amount of capitalized interest which may be added to the principal on a note. *Clasen v. Excel Fin. Causeway, Inc.*, 170 So.2d 924 (La. App. 4th Cir. 1965).

18. LA. CIV. CODE art. 2924.

19. *Id.*

computes the interest and includes it in the face amount of the note, there is no limit to the amount of capitalized interest which may be charged and added to the principal of the note.²⁰ The lender may charge 8%, or he may charge 800%; as long as he includes the interest in the note, he is not guilty of usurious lending. The usury statute makes a nonsensical distinction between "interest" and "discount." However, in practical terms the result of both is the same; i.e., the borrower is paying a charge for the use of the money. The distinction is made according to the manner in which the lender constructs his note. If the lender draws the note for the exact amount of money borrowed, he may not collect interest at a rate in excess of 8% per annum. However, if the lender draws the face amount of the note for the amount of cash loaned plus interest and whatever "other charges" he chooses to add to the note, he is not charging interest but is charging discount and there is no ceiling on the amount of discount charged. The practice of lending money at exorbitant discount rates has been attacked in the courts to no avail.²¹ It seems clear that unless and until legislation is enacted to regulate the amount of interest that may be charged on discount loans, the courts must continue to sanction unconscionable and usurious lending practices.²²

20. *Vosbein v. Leopold*, 230 La. 21, 87 So.2d 715 (1956).

21. *Mayfield v. Nunn*, 239 La. 1021, 121 So.2d 65 (1960); *General Securities Co. v. Jumonville*, 216 La. 681, 44 So.2d 702 (1950); *Time Fin. Co. v. Louis*, 152 So.2d 248 (La. App. 4th Cir. 1963).

In *Clasen v. Excel Fin. Causeway, Inc.*, 170 So.2d 924, 925 n.3 (La. App. 4th Cir. 1965), the court permitted lender to recover the face amount of note and stated that there is no limit to amount of capitalized interest which may be added to the principle of a note and that a proportionate rebate of interest on a note paid prior to expiration of its full term is required only when prepayment was initiated by the creditor. The court commented on Louisiana Civil Code Article 2924: "In this connection we might add that the development of the law of usury in Louisiana has been slow and unsatisfactory. The innumerable statutes that were passed and made a part of this article of the Code have unnecessarily complicated the subject. It appears that many of the cases emanating from our appellate courts are in error in their conclusions relative to usury. In any event, a statute should be enacted placing a maximum on the charge for the use of money to cover discount and capitalized interest, and it should be written so that its meaning is crystal clear."

In *Williams v. Alphonse Mortgage Co.*, 144 So.2d 600, 602 (La. App. 4th Cir. 1962), the court stated: "Counsel for appellant would point out that the rate of interest exacted by the defendant was exorbitant and unconscionable. From this, we would conclude we are urged to consider the inequity of the situation from her standpoint and, on the basis of equity, to grant her relief. However, 'The distinction of laws into odious laws and laws entitled to favor, with a view of narrowing or extending their construction, cannot be made by those whose duty it is to interpret them.' (LA. CIV. CODE art. 20).

"In civil matters, it is only in the absence of expressed law that the courts may provide and decide according to equity. (LA. CIV. CODE art. 21).

"In the instant case, the law is expressed; the jurisprudence is in accord therewith."

22. Numerous attempts have been made to pass laws regulating discount and

The practice of charging exorbitant interest rates on discount loans is only a small portion of the story. As often happens, the borrower is unable to pay his installments promptly each month and must make arrangements to postpone the past due payment. He is often willing to pay the lender an "extension fee" or "late charge" in order to delay legal action. Although cases²³ have held that these charges are tantamount to interest payments and are usurious if they exceed the maximum legal rate of 8% per annum, the common practice among some finance companies is to charge what the traffic will bear. The borrower is either unaware that he is paying an illegal amount of interest or simply submits to the charge in order to receive the service.²⁴

Another area of the discount loan business costly to the borrower is prepayment of his loan. Suppose the borrower signs a note for \$1,000.00, including capitalized interest of \$400.00, repayable in twenty-four monthly installments; the borrower decides the next day he does not need the money and attempts to prepay the loan. Our courts have taken the position that the payment of a note can be made before maturity only by consent of both debtor and creditor.²⁵ Therefore, the borrower has no right to demand a refund of unearned interest and must pay the face amount of the note. The result is different, however, if the creditor elects to accelerate maturity. The leading case of *Berger v. DeSalvo*²⁶ held that the holder of the note must give a pro rata

interest without attaining final approval. The most recent attempt was defeated by the House of Representatives in the Special Session of 1968. This attempt followed Louisiana House Bill No. 556 (hereafter La. H.B. 556) which was vetoed by the governor on June 29, 1968. The governor stated in vetoing the bill: "No person has any business borrowing money if he has to pay the interest rates which this bill allows." This statement seems inappropriate because, at the present time, interest rates are not regulated, and this bill would have placed a ceiling on the amount of interest that could be charged. Without this bill, the loan sharks can continue to thrive and charge whatever rate they can extract. The maximum rate that could have been charged under this bill amounted to approximately \$20.00 per \$100.00. The bill had passed the House of Representatives by a vote of 97-0 and the Senate by a margin of 30-4. The State of Louisiana lost a much needed law in this veto.

23. *Chadwick v. Menard*, 104 La. 38, 28 So. 933 (1900); *Consolidated Loans, Inc. v. Smith*, 190 So.2d 522 (La. App. 1st Cir. 1966).

24. La. H.B. 556 would regulate extension fees, but the rate is far in excess of the now legal 8% per annum.

25. *In re Liquidation of Hibernia Bank & Trust Co.*, 189 La. 813, 817, 180 So. 646, 647 (1938). "[T]he maker of a note has no right to pay the same before maturity without the consent of the holder."

In *State v. Ratzbrug*, 215 La. 295, 298, 40 So.2d 395, 396 (1949), the court stated: "Under the provisions of Article 1945 of the Revised Civil Code parties are governed by their legal agreements and the courts are bound to give legal effect to the contracts according to the true intent of the parties, which intent is to be determined by the words used in the contracts."

Garrison v. Hebert, 144 So.2d 916 (La. App. 4th Cir. 1962).

26. 156 So.2d 323 (La. App. 4th Cir. 1963), *cert. denied*.

refund of unearned interest if he elects to demand a payoff prior to maturity. In *Berger*, the defendant signed a note for \$13,000.00, of which \$3,000.00 was capitalized interest, on May 6, 1959, to be repaid in installments over a two-year period. The note provided for acceleration of maturity of the entire note at the holder's option for failure to pay any installment punctually, and provided for 8% interest per annum from the accelerated maturity date. The borrower failed to pay the first installment when due; and the holder elected to treat the entire balance as mature and due upon demand. The defendant had only six months' use of the \$10,000.00 prior to the holder's decision to exercise his option to accelerate the balance. The court, relying on an old case,²⁷ held that the holder must return the capitalized interest unearned on the acceleration date.²⁸ By comparison, the same court held in another case²⁹ that when the maker elects to prepay the note, there is no right to demand a refund of the unearned interest. The court stated:

"[I]t appears to be well settled in the jurisprudence that a holder of a promissory note may collect the face of the note, notwithstanding that such note may include a greater discount than 8% per annum, provided that such note does not bear a greater rate of interest than 8% per annum after maturity."³⁰

The distinction here is: if the holder of the note elects to mature the note, he must refund a pro rata amount of the unearned interest; but if the maker decides to prepay the note, he has no right to demand refund of this same unearned interest.³¹

27. *Williams' Heirs v. Douglass*, 47 La. Ann. 1277, 17 So. 805 (1895).

28. La. H.B. 556 would have required the creditor to refund unearned interest except in situations where the creditor sues for the balance. The refund method was identical to the method used in the Motor Vehicle Sales Finance Act (La. R.S. 6:958), as amended, La. Acts 1962, No. 139, § 1) and the Direct Vehicle Loan Companies Act (La. R.S. 6:974 (Supp. 1968)).

The governor, in his veto message, objected to the provision, because it would in effect overrule *Berger* by permitting recovery of the entire note with no rebate when the creditor elects to accelerate maturity by filing suit. This provision does seem to be inequitable since it would encourage some to file suit on a note in order to get around the rebate statute.

29. *Williams v. Alphonse Mortgage Co.*, 144 So.2d 600 (La. App. 4th Cir. 1962).

30. *Id.* at 602.

31. *Gulf Acceptance Loan Corp. v. Demas*, 205 So.2d 855 (La. App. 4th Cir. 1968). Defendant borrowed \$650 from plaintiff on November 15, 1966, and executed a promissory note for \$977.70 to be repaid over a period of thirty monthly installments. Defendant defaulted on his first payment and suit was filed on January 24, 1967. A demand was made for the entire \$977.70 plus attorney fees of 8% per annum interest from date of default. Defendant did not contest the suit, a default judgment was entered and time for appeal passed. In denying a rebate and unearned interest, the court recognized the right to a refund but the right was lost when the defendant failed to plead the point and let his appeal time pass.

Credit Sales

Credit sales³² are of equal concern to the consuming public. Buying on the installment plan has become a way of life for most Americans. The poor are especially vulnerable to installment buying and are seldom concerned with carrying charges. At the present time, credit sales are exempt from Louisiana's usury laws.³³

A very important but usually unnoticed characteristic of the installment sale is that very often a finance charge is included in the cash price. The merchant is not required to state his cost of the merchandise; therefore, the consumer is unaware of the time-price differential. In regard to the retail merchant who sells his merchandise on time, four serious questions need to be considered: (1) Should he be required to disclose in writing the amount and nature of all charges; (2) Should his retail price be regulated; (3) Should he be required to refund unearned interest when the purchaser prepays his account; and (4) Should he be required to subtract the time-price differential when the customer pays cash.³⁴ Grievous evils exist in the field of credit sales. The merchant is permitted to "mark-up" his merchandise with no limitation and then charge a time-price differential that is not regulated. Very often the merchant sells the sales contract to a finance company at a discounted rate. In most instances³⁵ the finance company becomes a holder in due course obviating the personal defense of redhibition due to defective merchandise.³⁶

32. See generally Comment, 24 LA. L. REV. 822 (1964), containing an in-depth discussion of usury as it relates to credit sales.

33. In *Motes v. Van Wagner*, 188 So.2d 704, 705 (La. App. 4th Cir. 1966), the court stated: "Civil Code art. 2924 does not apply to a bona fide credit sale of property; in the absence of fraud or intention to defeat the law relative to usury, a vendor and a purchaser may validly agree on a credit price in excess of the cash price for the same article, even though the added price for the credit sale over the cash price exceeds the legal interest rate." See *Mills v. Crocker*, 9 La. Ann. 334 (1854).

34. La. H.B. 556 did not contain a provision to regulate interest on credit sales. This writer submits that any legislation directed at regulation of discount and interest on loans should also include regulation of discount, interest, and carrying charges on credit sales.

35. See LA. R.S. 7:51-59 (1950).

36. Credit transactions between sellers and lenders and buyers and borrowers are to be regulated by the new Consumer Credit Protection Act, more commonly known as Truth-in-Lending. The following statement appeared in the June 1968 issue of *Louisiana Consumer*: "A major victory for consumers was won with the passage by both houses of Congress of the Federal Truth in Lending Act on April 22, 1968. The act was signed into law by the President on April 29, 1968, and most of its provisions will become effective on July 1, 1969.

"The most significant feature of the new law is the provisions which require lenders and retail creditors to provide their customers full, honest and comparable information about the cost of credit. In particular, the act requires that consumers be told the effective annual rate of interest they are being charged, thus

Conclusion

The future of the loan industry in Louisiana is uncertain. Almost everyone agrees that finance companies are necessary, but they disagree as to rates, pre-payment refunds, collection methods, and miscellaneous charges. What effect, if any, the federal *Truth-in-Lending Act*³⁷ will have on loan companies is unknown. The Act does not contain rate controls nor does it provide for a refund of unearned interest.³⁸

There may, however, be hope for the unwary borrower should Louisiana adopt the Uniform Commercial Code.³⁹ The UCC has a provision⁴⁰ that could enable the court to find as a matter of law that the discounting of exorbitant interest is unconscionable and thereby take appropriate action. The outcome of the court's finding would depend entirely upon their definition of the term "unconscionable." The UCC does not attempt to define the term, thus leaving much discretion in the courts.

Herschel C. Adcock

MANDAMUS—COMPELLING AN OFFICIAL TO PERFORM
DISCRETIONARY DUTY

Plaintiffs, desiring to complete a course in barber college, were unable to fulfill the requirements within the time allotted by law¹ and sought an extension from the Louisiana State Board of Barber Examiners. The Board, "in its discretion,"² refused to allow the requested extension and plaintiffs brought

enabling them, for the first time in most states, to actually have a meaningful opportunity to shop for the best credit buy."

37. 15 U.S.C. §§ 1601-1677 (1968).

38. A bill such as La. H.B. 556, even though it contained some inequitable provisions, would have been a welcome relief.

39. Louisiana is the only state that has not adopted the Uniform Commercial Code; however, the Louisiana Law Institute is presently studying the UCC with an eye toward its possible adoption by Louisiana.

40. UNIFORM COMMERCIAL CODE § 2-302: "(1) If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

"(2) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination."

1. LA. R. S. 36:363 (1950).

2. *Id.* 36:366 gives the Board the power to extend the time permitted for completion of the required course. To give, or not to give, an extension is within the Board's discretion, but it may only grant an extension upon a showing of good cause.