



STATE OF TEXAS

OFFICE OF CONSUMER CREDIT COMMISSIONER

SAM KELLEY, Commissioner

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December 4, 1981 No. 81-29

Mr. Jeffrey J. Tompkins
Walsh, Squires, Tompkins & McCullough
Attorneys at Law
4200 Westheimer, Suite 130
Houston, Texas 77027

Dear Mr. Tompkins:

This is to acknowledge receipt of your letter dated August 10, 1981 concerning the propriety of the assessment of additional interest for default on loans made pursuant to Chapter 5, Article 5069, V.T.C.S.

I would first like to make some observations concerning a few points you make in your letter. On the first page of your letter, you stated that "...the type of loan covered under Chapter 5 has traditionally been associated with simple interest rates, i.e. loans secured by real property." I would at least partially disagree since Chapter 5 loans have always been limited to precomputed loans and simple interest loans were not authorized under Chapter 5 until May 8, 1981, the effective date of H.B. 1228. Also, the historic concept of allowing additional interest for default on precomputed loans has been that in the event the debtor does not pay an installment as scheduled, the lender does not earn additional interest for late payment unless the lender is allowed to assess some sort of default charge for late payment. The additional interest for default allowed by the various Chapters of the Credit Code have never had any bearing on the contract interest rate on pre-computed transactions. They have always been "in addition" to the add-on rates authorized by the various Chapters since, as stated before, the lender does not realize any additional interest earnings when a scheduled installment is not timely made. Also, I think the general provisions of the Texas Savings and Loan Act have no bearing on what may or may not be charged on a Chapter 5 loan. The Legislature has enacted a specific statute (Chapter 5) relating to a specific type of loan (secondary mortgage loan), and the provisions of the specific statute would control as to what charges could be assessed on loans made pursuant to that Chapter.

In Letter Interpretation No. 81-5, dated June 12, 1981, I made the statement that the position of this Office is that the default and deferment charges set out in Chapter 5 should not be assessed on an interest bearing loan made pursuant to Chapter 5. Our basic approach has always been that on an interest bearing transaction the lender continues to earn daily interest on the unpaid principal sum owed for the time during which the scheduled payment is not made, and it would not be proper for the debtor to have to pay daily interest earnings as well as additional interest for default for the same period of time.

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I now realize that my concept of interest bearing loans is not the same as that of simple interest loans as viewed by many people in the savings and loan and banking industry. When I speak of interest bearing transactions, as previously indicated, I am speaking of loans wherein the lender continues to realize daily interest earnings on unpaid principal amounts outstanding when an installment(s) is not paid as scheduled, such as a typical bank credit card account. When some lenders designate a loan as being a "simple interest" transaction, it may very well not be a true interest bearing loan. For example, I understand that many lenders wish to establish Chapter 5 "simple interest" loans so as to amortize the total interest over the life of the loan based on the assumption that all payments will be paid on the scheduled due date and that interest will be accrued based on this assumption. If a loan is established in this manner, in the event a scheduled payment is not timely made, the lender does not earn any additional interest on the unpaid principal for the period for which the payment is late. I suppose this type of loan is something of a "hybrid" somewhere in between the standard precomputed, add-on type of transaction and a true interest bearing loan. In any event, I am of the opinion that if a loan is structured so that it is not a true interest bearing transaction and if the lender does not earn additional interest on the unpaid principal balance when a payment is not made as scheduled, the additional interest for default authorized by Chapter 5 may be assessed in the event of late payment if the contract so provides.

Sincerely yours,



Sam Kelley
Consumer Credit Commissioner