

THE C & D NEWSLETTER



CITRON & DEUTSCH
A LAW CORPORATION

Published by:
RICHARD K. CITRON
DAVID R. DEUTSCH
MICHELLE LeCOLST-JOHNSTON
Attorneys

CALIFORNIA USURY LAW

California's usury law regulates the maximum amount of interest which may be charged on any loan or forbearance of money. This Newsletter shall discuss the permitted rate of interest on various types of loans, which lenders and transactions are exempt from the usury law, and the penalties for making a usurious loan.

Permitted Interest Rate. The maximum interest rate permitted on loans used primarily for personal, family or household purposes is 10% per annum. The maximum interest rate on loans used for business and all other purposes is the higher of 10% per annum, or 5% per annum plus the interest rate established by the Federal Reserve Bank of San Francisco on the 25th day of the month preceding the earlier of the date of execution of the contract to make the loan or the date of making of the loan. On October 25th, Federal Reserve Bank interest rate was 7%.

Exempt Lenders. The following lenders are exempt from the usury law: (a) banks; (b) savings and loan associations; (c) industrial loan associations; (d) credit unions; (e) personal property brokers; (f) licensed pawnbrokers; (g) nonprofit cooperative agricultural associations; and (h) pension funds or retirement systems subject to the federal Employee Retirement Income Security Act of 1974.

Exempt Transactions. A loan made or arranged by a licensed real estate broker and secured in whole or in part by a lien on real property is exempt from the usury law. Similarly, a shared appreciation loan (i.e., one in which the lender receives a part of the appreciated value of the property securing the loan) is also exempt from the usury law. Since usury only exists where there is a borrowing or lending or forbearance of money, there can be no usury in a bona fide sale where the seller offers property at a certain price for cash or at a much higher price on credit. This is sometimes referred to as the "time-price doctrine." The "hazard rule" exception to usury provides that where repayment of the principal sum or the interest is subject to a business contingency of profits being earned, there is no usury as long as the parties are contracting in good faith and without intent to evade the usury law.

Penalties for a Usurious Loan. The effect of a usurious loan is to render the usurious interest provision void, resulting in a loan payable at maturity without interest. If the usurious interest has already been collected, the borrower may recover three times the amount of the usurious interest. The statute of limitations to recover treble damages is one year from the date of payment of the usurious interest; however, the borrower may still recover the actual interest paid within two years. In addition, if the lender sues on the indebtedness, all usurious payments may be set off in reduction of the principal, without regard to any statute of limitations.

Conclusion. Each of the fifty states has a usury law, and no two usury laws are identical. California's usury law, which is summarized in this Newsletter, appears simple but is full of traps for the unwary. For example, is it usurious if the borrower pays the lender points, bonuses, commissions, origination fees or closing fees in addition to the stated interest rate? Can a prepayment penalty be considered a usurious payment? How about transactions between a lender in one state and a borrower in another state where the loan would be usurious in the borrower's state but not in the lender's state? Because the usury issue in specific situations may not be apparent on the face of the loan, it is important to consult an attorney whenever there is a question as to whether the transaction may be usurious.

This complimentary newsletter is intended to provide general information. Because of the complexities and constant changes in the law, it is important to seek professional advice before acting on any of the matters covered herein.