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Office of  
Consumer  
Credit  
Commissioner

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Leslie L. Pettijohn  
Commissioner

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2601 N Lamar Blvd  
Austin, TX 78705  
[www.occc.state.tx.us](http://www.occc.state.tx.us)

512-936-7600  
Fax: 512-936-7610  
Consumer Helpline: 800-538-1579

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October 20, 1999

Karen Neeley  
General Counsel  
Independent Bankers Association of Texas  
408 W. 14<sup>th</sup> St.  
Austin, TX 78701

Dear Ms. Neeley:

You have inquired concerning several recent legislative enactments that affect the Texas Credit Title of the Finance Code. As you know, these provisions became effective September 1, 1999.

**Financing Administrative Fees.** Your first issue concerns the amendment to the definition of the interest computation methods in Section 342.002. The amendment corrected an error where previously the statute provided that the daily rate was applied to the unpaid balance of the amount financed. Now the statute reads that the daily rate is applied to the unpaid balance of the "principal amount." The significance of this change was intended to make the definitions more technically accurate when encountering secondary mortgage loans that include financed points. The financing of points has been acknowledged and authorized by Finance Commission rule, Texas case law, and OCCC interpretation letter.

Your concern is whether this amendment permits interest to be accrued upon an administrative fee that is financed. The authorization for the administrative fee in Chapter 342 is an authorization for additional interest of \$25 above that already permitted by Chapter 342. Chapter 342, nor any Finance Commission rule, authorizes the accrual of additional interest upon this additional interest charge. This may be an area that we will look at more closely, but it is not my opinion that, at this time, the definitional change authorizes the charging of additional interest upon the administrative fee. If you have further thoughts and arguments on this matter, I would be interested in hearing them.

**Late charge - Single Pay Notes & Balloon Notes.** The analysis of single pay notes and balloon notes raises very interesting questions. It seems that in both of the cases one must first look to the maturity of the contract. In a single pay transaction by the

Karen Neeley  
October 20, 1999  
Page 2

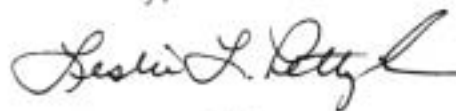
terms of the contract when the single payment or installment is due, the note is then mature. Since it is mature, then post-maturity interest would be the appropriate charge. I believe in certain situations a lender who tries to impose a late charge on a single pay loan may well run afoul of the usury limitations. Similarly in most contracts with balloon notes, the balloon occurs at the maturity of the note. In these cases, it would also be appropriate to charge post-maturity interest.

**Late charge - Unregulated loans.** Consumer loans with a rate of interest of 10% or less are not subject to Chapter 342. However, I believe it would be permissible for an authorized lender to choose to employ the provisions of chapter 342 on both loans above 10% and below 10%. A consumer is not likely to be harmed in any way by a lender who chooses to do this. It is important, though, to consider the impact of single pay notes as discussed above. In certain situations if late charges are applied, these may create potential usury violations.

**Deferment charge.** A deferment charge is essentially the interest charge associated with the balance on account without any payment for the reduction in principal. If contracted for, on a regular transaction that employs the true daily earnings method, a lender may collect an associated charge for the accrued interest for the month in which no principal reduction is made. The statute recognizes a deferment charge for regular transactions that are precomputed or that use the scheduled installment earnings method. The statute then provides for irregular transactions in sec. 342.206 which, essentially, was everything else. I believe it would be permissible to use the true daily earnings method for a period of deferring a principal payment. The concept of a payment moving to the end of the contract is more semantics than actuality. Since the lender is assessing charges on a true daily earnings basis, the lender is compensated at a daily rate for the outstanding unpaid balance.

I apologize for the delay in our response. I hope this information will be helpful to your members.

Sincerely,



Leslie L. Pettijohn