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State-Imposed Interest Rate Ceilings and the Home Equity Loan Scandal in Georgia

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STATE-IMPOSED INTEREST RATE CEILINGS AND
THE HOME EQUITY LOAN SCANDAL IN GEORGIA

>This bond doth give thee here no jot of blood;
The words expressly are “a pound of flesh.”

INTRODUCTION

This Note discusses the history and legal issues of the home equity loan scandal that occurred in Georgia in the late 1980s and claimed widespread public and official attention in Georgia in the early 1990s. Part I summarizes the history of the scandal and its aftermath. Part II outlines the development of usury law in the United States. Part III discusses policy considerations affecting state regulation of interest rate ceilings. Part IV discusses mortgage loan deregulation in Georgia in the 1980s. Part V describes current Georgia usury law as it applies to mortgage loans. Part VI discusses significant Georgia cases of the 1980s and 1990s in which borrowers urged state and federal courts to provide relief from predatory high-interest-rate home equity loans. Finally, Part VII summarizes legislative action taken by the Georgia General Assembly in response to the

2. An “equity loan” is defined as a “line of credit made available by banks to homeowners with the extent of such credit based on, and secured with, built-up equity in borrower’s home.” BLACK’S LAW DICTIONARY 541 (6th ed. 1990). E.g., Shelley Emlyn, House Sets Hearings on Interest Caps: Home-Equity Loan Action Long Overdue, Critics Say, ATLANTA CONST., Sept. 6, 1993, at B1 (using the term “home-equity loan”). The term “second mortgage loan” is sometimes used to mean essentially the same thing as a home equity loan. E.g., Dwight Golann, Consumer Financial Services Litigation: Major Judgments and ADR Responses, 48 BUS. LAW. 1141, 1147 (1993) (using the term “second-mortgage loans” to describe the same type of loan). However, technically a “second mortgage” is simply the second of a series of mortgages. BLACK’S LAW DICTIONARY 1011 (6th ed. 1990). Georgia law regulating mortgage lenders employs the more generic term “mortgage loan,” defining it as “a loan made to a natural person which loan is secured by a deed to secure debt, security deed, mortgage, or deed of trust upon any interest in one-to-four family residential property located in Georgia, regardless of where made, including the renewal or refinancing of any such loan.” See O.C.G.A. § 7-1-1000(9) (Supp. 1994).
scandal, especially the 1993 Act regulating mortgage brokers and mortgage lenders.  

I. THE HOME EQUITY LOAN SCANDAL IN GEORGIA

In the 1980s a number of factors combined to attract into Georgia, as well as into several other states, dishonest finance companies that carried on a scheme of quasi-legal loansharking based on home equity loans. These factors included: (1) a general rise in residential property values; (2) a large number of financially unsophisticated homeowners who over the years had acquired substantial equities in their homes; (3) a lending environment in which many African-American homeowners did not or could not obtain loans from conventional lenders; (4) widespread federal and state elimination of interest rate ceilings; and (5) lax regulation of second mortgage lending.

The scheme usually involved enticing a financially unsophisticated homeowner, frequently an elderly African-American man or woman, into committing his or her home as security for a high-fee, high-interest-rate home repair loan with payments higher than the homeowners could afford to pay.

5. See Golann, supra note 2, at 1146-47; Michael Hudson, Loan Scams that Prey on the Poor, BUS. & SOC’Y REV., Winter 1993, at 11, 12; Vejnoska, supra note 3. The scam also developed in New York, Chicago, Boston, Los Angeles, Virginia, and Alabama. Golann, supra note 2, at 1146; Hudson, supra, at 12, 14.
6. KEVIN W. BROWN & KATHLEEN E. KEEST, USURY AND CONSUMER CREDIT REGULATION § 2.3.3.6. (The Consumer Credit and Sales Legal Practices Series, 1987).
7. Vejnoska, supra note 3.
8. See Hudson, supra note 5, at 12; Vejnoska, supra note 3.
9. BROWN & KEEST, supra note 6, § 2.4.1; see infra Part IV.
10. See Vejnoska, supra note 3.
11. Id.; see also Hudson, supra note 5, at 11-12. Mrs. Lillie Mae Starr was the named plaintiff in the Starr v. Fleet Finance, Inc. class action suit. Complaint for Preliminary Injunction, Final Injunction and for Declaratory Relief, Starr v. Fleet Finance, Inc. (Cobb Co. Super. Ct. filed Apr. 3, 1992) (No. 9212314-06); Jill Vejnoska, Judge OKs Class Action Against Fleet: Borrowers Suing Firm Over Lending Practices, ATLANTA J., Dec. 15, 1992, at E1. Mrs. Starr, a sixty-two-year-old grandmother who owned a $40,000 home in Smyrna, Ga., responded to a television advertisement from a home repair company and was persuaded by the company’s sales representative to pay the company $5000 to replace the drafty windows in her house. Vejnoska, supra note 3. Mrs. Starr took out a loan from a local finance company for $9200, $4200 of which was a loan origination fee, and pledged her home as security for the loan; this loan had an annual percentage rate (APR) of 23.3% and required Mrs. Starr to pay back $19,420.56 over nine years. See id. Fleet bought the loan from the local finance company on the secondary mortgage market. Id. When Mrs. Starr fell behind after
Over a period of years, victims alleged, the holder of the loan would wring all financial resources from the homeowner by allowing a homeowner who was behind in monthly payments to refinance the loan for an even higher face value, adding on expensive refinancing fees.\textsuperscript{12} When the homeowner's debt equaled the value of the home and the homeowner no longer could manage to make the monthly payments, the holder of the loan would foreclose on the property.\textsuperscript{13}

Two types of lenders allegedly were involved in these practices: smaller finance companies that made the loans\textsuperscript{14} and larger finance companies that purchased the loans from the smaller companies and handled debt collection and foreclosures.\textsuperscript{15} Allegedly, the larger finance companies made funds available in advance to the smaller finance companies knowing that the funds would be used for these high-priced, high-risk loans.\textsuperscript{16} In particular, advocates for borrowers in Georgia focused their attention on Fleet Finance, Inc. (Fleet), a finance company that in 1992 made and purchased more home equity loans in Georgia than any other single lender.\textsuperscript{17} Fleet acknowledged that it had purchased loans in the secondary mortgage market,\textsuperscript{18} but "vehemently disagree[d] with [the newspaper's] characterization of Fleet Finance as 'an unscrupulous company' that [had] a 'reputation for bilking poor people.'"\textsuperscript{19}

\begin{flushleft}
\textsuperscript{12} See Vejnoska, supra note 11.
\textsuperscript{13} See id.
\textsuperscript{14} See id.; Golann, supra note 2, at 1147.
\textsuperscript{15} See Vejnoska, supra note 3; Golann, supra note 2, at 1147.
\textsuperscript{16} Golann, supra note 2, at 1147.
\textsuperscript{17} Vejnoska, supra note 3. Fleet Finance, Inc., is an Atlanta-based subsidiary of the largest financial institution in New England, Fleet Financial Group, which is based in Providence, Rhode Island. Rodney Ho, Closing a Chapter at Fleet Finance, ATLANTA CONST., Aug. 23, 1994, at D1; Hudson, supra note 5, at 12.
\textsuperscript{18} Harold Owens, Fleet Finance: Why Blame Lone Company?, ATLANTA CONST., Mar. 3, 1993, at A13. Mr. Owens, at the time, was chief operating officer of Fleet Finance, Inc. Id.
\textsuperscript{19} John R. Strickland, A Word from Fleet Finance, ATLANTA CONST., Oct. 20, 1992, at A19 (letter to the editor). At the time Mr. Strickland wrote this letter to the editor, he was president and CEO of Fleet Finance, Inc. Id.
\end{flushleft}
Pursuant to Code section 7-4-18(a), which sets a maximum legal interest rate ceiling of 5% simple interest per month, equivalent to 60% interest per year, some borrowers asserted usury claims against these lenders. Borrowers' advocates argued in state and federal courts that the loan origination fees and discount points paid by the borrower to the lender at the loan closing should be reckoned as interest paid in the first month of the loan; thus, the interest rate of the loans exceeded the legal maximum of 5% simple interest per month. These arguments were ultimately unsuccessful. In 1993 the Supreme Court of Georgia held that front end finance charges could not be attributed as interest on the first month of the loan.

As more facts about the scandal came to light, the outrage of Georgia citizens, officials, and lawmakers sparked attempts for a statewide remedy. In 1992, after the Georgia Office of Consumer Affairs had received complaints of "various types of misrepresentations" by Fleet to borrowers over a period of months, the Georgia Office of Consumer Affairs and the Attorney General's office conducted an investigation of Fleet. In 1993, the investigation resulted in "[t]he state [finding] Fleet guilty of three violations of Georgia's Fair Business Practices Act."
Fleet contested the findings of civil wrongdoing, but agreed to a settlement under which it would pay up to $115 million in damages. However, the settlement did not totally remedy the damage caused by predatory loans.

In 1993, the Georgia General Assembly enacted legislation under which the Department of Banking and Finance (the Department) monitors lending practices of mortgage lenders and mortgage brokers doing business in Georgia. However, the General Assembly declined to enact a bill in 1993 or 1994 that would have created a floating interest rate ceiling for home equity loans much lower than the current ceiling of 5% simple interest per month, which is equivalent to 60% per year.

In the pivotal case of Fleet Finance, Inc. v. Jones in 1993, the Supreme Court of Georgia rejected the borrowers’ argument that the home equity loans in question were made usurious by the lenders’ collection of costly loan origination fees in the first month of the loan. Although the court condemned Fleet’s aggressive lending practices, the court pointed out that the interest rate reform sought by the borrowers, a lower interest rate ceiling for mortgage loans, must come from the legislature. Finally, in 1993 Fleet settled two class action lawsuits, Alexander v. Fleet Finance, Inc. and Starr v. Fleet
Finance, Inc., for large amounts of money and also settled dozens of lawsuits brought on behalf of individual borrowers by the Atlanta Legal Aid Society.

Fleet continued to maintain that it had not bought loans with the intention of foreclosing on them, but admitted that its policy in the 1980s of buying third-party mortgages with "aggressive" terms had caused problems. After coming under new management, Fleet stopped buying third-party mortgage loans, agreed to settlements with the class action plaintiffs, voluntarily provided home improvement assistance to some victims of the scams, initiated a community service program, and looked forward to putting the scandal behind it and doing business in Georgia as a respected lender.

II. DEVELOPMENT OF USURY LAW IN THE UNITED STATES

Usury is defined as charging a higher rate of interest than is allowed by law. The elements of usury are: (1) a loan or forbearance of money; (2) an obligation to repay the principal; (3)
the charging of a higher rate of interest than is permitted by law; and (4) some level of intent to charge an illegal interest rate.47

Charging interest is an age-old practice that societies throughout history have tolerated in some circumstances and prohibited in others, reflecting a continuing tension between the recognition that credit is essential to commerce and a belief that interest taking is predatory and immoral.48 The American colonies adopted the English practice of enacting a "general" usury law that simply set a maximum interest rate for all types of loans.49 These laws were for many decades the only statutes regulating interest rates in the United States.50 In the early twentieth century, states began to enact "special" usury laws51 aimed at overcoming "problems associated with a particular type of creditor . . . [or] transaction."52

The earliest special usury laws were the small loan laws, aimed at foiling the widespread practice of loansharking.53 Prior to these acts, "consumer loans" usually were available only from loansharks at extremely high rates of interest because it was not profitable for reputable lenders to make small loans to individuals.54 Small loan laws licensed a new class of lenders to make loans to individuals at higher rates of interest than the ceiling set by the general usury statute in compensation for adhering to statutory requirements as to interest rates, security for loans, and methods of loan collecting.55 In time, state special usury laws came to regulate many types of credit transactions,
including bank installment loans, retail installment loans, insurance premium financing, second mortgages, and credit card sales.\textsuperscript{56}

The proliferation of special usury laws within each individual state has resulted in "highly fragmented" state regulation of credit transactions.\textsuperscript{57} A number of states have achieved a degree of uniformity by adopting the Uniform Consumer Credit Code (UCCC) in some form.\textsuperscript{58} But even in these states, the recurring need to correct a specific problem associated with a particular type of loan or creditor prevents entirely uniform treatment of credit transactions.\textsuperscript{59} Statutory usury law today is a "patchwork" of surviving state general usury statutes, various state special usury statutes, and federal laws supplementing or partially preempting state laws.\textsuperscript{60}

\textbf{III. POLICIES AFFECTING STATE INTEREST RATE CeILINGS}

The primary purpose of an interest rate ceiling for consumer loans is to limit the financial loss that an unwise or desperate borrower may suffer at the hands of a predatory lender.\textsuperscript{61} Consumers arguably need this protection because lenders typically have much greater bargaining power than consumers.\textsuperscript{62} Loan agreements are adhesion contracts created by lenders with terms over which borrowers have little control.\textsuperscript{63} In the "classic" usury case, a borrower enters into an unequal loan contract out of desperation, perhaps to get money to pay already pressing debts.\textsuperscript{64} However, a loan contract may be so difficult for the average loan applicant to comprehend that the borrower is potentially in an unequal a position as the "classic desperate borrower."\textsuperscript{65}

\begin{footnotesize}
\begin{enumerate}
\item \textit{Id.} \S 2.2.3 to 2.3.3.7.
\item \textit{Id.} \S 2.3.3.
\item \textit{Id.} \S 2.3.3.9.
\item See \textit{id.} \S 2.3.3.
\item \textit{Id.} \S 2.1; \textit{CRANDALL ET AL., supra note 46, \S 3.01[1].}
\item \textit{BROWN \& KEEST, supra note 6, \S 1.2; see Note, \textit{Developments in Georgia Law: Debtor-Creditor Rights, 12 Ga. L. REV. 814, 919 (1978).}}
\item \textit{BROWN \& KEEST, supra note 6, \S 1.2.}
\item See \textit{id.}
\item \textit{Id.} \S 1.2; \textit{SIDNEY L. MOORE, JR., CONSUMER CREDIT DEFENSE IN GEORGIA 1 (Center for Continuing Legal Education Publication No. 168, 1989); George J. Wallace, Remarks at 1981 ABA Annual Meeting (Aug. 11, 1981), in \textit{Federal Pre-emption of State Usury Laws, 37 BUS. LAW. 747, 779, 792 (William M. Burke ed., 1982)}}
\end{enumerate}
\end{footnotesize}
Arguably, the danger of predatory lending is greater when (1) no interest rate ceiling exists, or an existing interest rate ceiling is set far above actual market interest rates; and (2) lending practices are unregulated. In a credit environment without some limit on lending rates and practices, lenders may easily profiteer against consumer borrowers. Moreover, usury ceilings may discourage predatory lenders from operating in a state because of its impact on their potential profits. An interest rate ceiling is ineffectual at discouraging predatory lending if the ceiling is so far above the current market interest rate that it cannot influence the behavior of lenders. Georgia's current rate ceiling of 5% simple interest per month is so much higher than historical market interest rates that it did little to restrain predatory lending during the state's home equity loan scandal.

On the other hand, a state-imposed fixed interest rate ceiling can create difficulties if market interest rates reach or exceed the fixed ceiling, as occurred in the United States in the late 1970s and early 1980s. Lenders operating in such an environment
may decrease the number of issued loans making it more difficult for consumers to obtain credit.\textsuperscript{73}

A potential solution to this problem is the adoption of a floating interest rate ceiling, which some states already use.\textsuperscript{74} A floating interest rate ceiling is set at some fixed level above a regulatory or market interest rate and is re-adjusted periodically if the base rate changes.\textsuperscript{75} As market interest rates rise or fall, the floating rate ceiling allows a consistent margin between the cost of funds and the legally allowable loan interest rate.

Opponents of interest rate ceilings further argue that an interest rate ceiling, by restricting a lender's opportunity to make a profit, influences the lender not to lend money to consumers who are higher credit risks.\textsuperscript{76} By contrast proponents argue that the number of consumers actually unable to get credit is "very low" and is relatively insignificant compared to the great number of consumers who pay higher prices for loans when no effective interest rate ceiling exists.\textsuperscript{77} Moreover, interest rate ceilings screen out predatory lenders who "often leave a trail of legal havoc and misery for both their borrowers and investors."\textsuperscript{78}

\textsuperscript{73} BROWN & KEEST, supra note 6, § 2.4.1.
\textsuperscript{74} CRANDALL ET AL., supra note 46, ¶ 3.01[3][c][iii]. For example, in 1993 Arkansas' current interest rate for consumer loans and credit sales was the lesser of 17% or the discount rate plus 5%. KEVIN W. BROWN & KATHLEEN E. KEEST, USURY AND CONSUMER CREDIT REGULATION, app. B (The Consumer Credit and Sales Legal Practice Series, Supp. 1993) (listing state lending statutes for all the states).

\textsuperscript{75} See, e.g., CRANDALL ET AL., supra note 46, ¶ 3.01[3][b][i]. The alternative federal rate allowed to national banks is 1% over the "discount rate on ninety-day commercial paper in the Federal Reserve bank in the Federal Reserve district where the bank is located." Id. (quoting 12 U.S.C. § 85 (1988)).

\textsuperscript{76} BROWN & KEEST, supra note 6, § 2.4.1. Rep. Clinton Oliver noted: "We're very concerned about having a good market for consumers, but consumers can't be served if companies can't make a profit here and move elsewhere..." Shelley Emling, Legislature '94, Home-Equity Loan Bill Stalls, ATLANTA CONST., Feb. 1, 1994, at C6 [hereinafter Emling, Home-Equity Loan Bill Stalls]. An attorney representing mortgage brokers in a House committee hearing argued that if companies find Georgia laws too restrictive, they will take their business elsewhere. Shelley Emling, Lawmakers Say 'Facts' Needed on Equity Loans, ATLANTA CONST., Sept. 17, 1993, at G3 [hereinafter Emling, 'Facts' Needed]. Harold Owens, the then-chief operating officer of Fleet, asserted that the "consumer-finance industry provides a critical source of credit to millions of low-and moderate-income people disqualified by major banks from receiving... credit." Owens, supra note 18.

\textsuperscript{77} BROWN & KEEST, supra note 6, § 2.4.1.
\textsuperscript{78} Id.
Finally, opponents of interest rate ceilings argue that fraud and consumer protection laws are a better solution than an interest rate ceiling because such laws will weed out predatory lenders without affecting the entire lending industry. Proponents counter by arguing that an interest rate ceiling is significantly more effective than these laws because an interest rate ceiling prevents injury to consumers by keeping predatory lenders out of the state.

IV. DEREGULATION OF MORTGAGE LOANS IN GEORGIA IN THE 1980S

The United States economy of the late 1970s and early 1980s created a credit crunch in which short term commercial interest rates rose until they approached or exceeded the fixed interest rate ceilings then imposed by many states. As a result, lenders who made medium-term and long-term business or consumer loans found their ability to make a profit squeezed between their higher cost of obtaining funds and the static maximum interest rate at which states allowed them to make loans to their customers. Urged by lenders to take action and fearing serious consequences to the economy, the federal government and a number of state governments responded with legislation eliminating many restrictions on interest rates.

The federal Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA) preempted state laws restricting interest rates in three areas: loans secured by a first lien on real estate; business and agricultural loans over

79. Id.; see, e.g., Emling, supra note 2. Rep. Clinton Oliver, Chairman of the House Banks and Banking Committee, stated that a recently enacted statute providing for monitoring of mortgage brokers and mortgage lenders eliminated any need for a floating-interest rate ceiling bill. Id.

80. Brown & Keest, supra note 6, § 2.4.1. The settlements resulting from the Attorney General’s investigation into the lending practices of Fleet did not fully compensate the victims and did not reach all victims because of a two-year statute of limitations. Emling, supra note 29.

81. Brown & Keest, supra note 6, § 2.4.1; see Galchus et al., supra note 72, at 706, 708, 713 (referring to the effect in Arkansas).

82. Brown & Keest, supra note 6, § 2.4.1; Galchus, supra note 72, at 702.

83. Brown & Keest, supra note 6, § 2.4.1.


85. See generally Brown & Keest, supra note 74, § 3.2.2.

$1000 (this was a temporary measure expiring after three years),\textsuperscript{87} and, loans made by some types of federally insured lenders.\textsuperscript{88} However, states were permitted to opt out of parts of these restrictions.\textsuperscript{89} Thus, although the states found their interest rate restrictions preempted in these three areas, states could nevertheless reassert many of their restrictions by enacting positive legislation.\textsuperscript{90} Sixteen states and territories, including Georgia,\textsuperscript{91} opted out of DIDMCA in some way.\textsuperscript{92}

The federal Alternative Mortgage Transactions Parity Act of 1982\textsuperscript{93} (AMTPA), enacted as part of the Garn-St. Germain Depository Institutions Act of 1982,\textsuperscript{94} dealt with types of loans rather than with interest rates.\textsuperscript{95} This Act preempted state laws restricting “creative” methods of home financing such as variable interest rates, balloon financing, and negative amortization.\textsuperscript{96} Like DIDMCA, AMTPA also contained an opt-out provision,\textsuperscript{97} which only five states exercised. Georgia did not opt out of AMTPA.\textsuperscript{98}

\textsuperscript{87} Id. § 86a (repealed Apr. 1, 1983 pursuant to Pub. L. No. 96-221, § 512. 94 Stat. 132) (temporarily preempting, until April 1, 1983, state interest rate restrictions on agricultural and business loans over $1000 and allowing lenders instead to charge the alternative federal rate).

\textsuperscript{88} Id. § 1831d(a) (1988 & Supp. V 1993) (extending lending privileges of state-chartered federally insured banks); id. § 1785(g) (1988) (extending lending privileges of federal credit unions); id. § 1730g(a) (repealed by Act of Aug. 9, 1989, Pub. L. No. 101-73, 103 Stat. 363) (extending lending privileges of federal savings and loans). See generally BROWN & KEEST, supra note 74, § 3.2.2.

\textsuperscript{89} 12 U.S.C. § 1735f-7a(b)(2) (1988) (permitting state to opt out of mortgage loan interest rate provisions); id. § 1735f-7a(b)(4) (permitting state to opt out of mortgage loan charge provisions); BROWN & KEEST, supra note 74, § 3.2.2.

\textsuperscript{90} BROWN & KEEST, supra note 74, § 3.2.2.4.

\textsuperscript{91} O.C.G.A. § 7-4-20(1) (1989) (opting out of provision preempting interest rate restrictions on loans secured by a first lien mortgage by certain classes of lenders); id. § 7-4-20(2) (opting out of provision preempting interest rate restrictions on agricultural and business loans over $1000). The Georgia General Assembly’s response to DIDMCA is discussed at infra notes 100-93 and accompanying text.

\textsuperscript{92} BROWN & KEEST, supra note 74, § 3.2.2.4. The states and territory are Colorado, Georgia, Hawaii, Idaho, Iowa, Kansas, Maine, Massachusetts, Minnesota, Nebraska, Nevada, North Carolina, Puerto Rico, South Carolina, South Dakota, and Wisconsin. Id.


\textsuperscript{95} BROWN & KEEST, supra note 74, § 3.3.1.1.

\textsuperscript{96} Id.


\textsuperscript{98} See BROWN & KEEST, supra note 74, § 3.3.1.1 n.251.
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As a result of these federal statutes and their opt-out provisions, state legislatures “were forced to consider the role that usury statutes should play, if any, in a modern economy.” The 1983 Georgia General Assembly responded by simplifying Georgia’s general usury laws by retaining a very high overall ceiling on interest rates, and by doing away with fixed interest rate ceilings for certain types of loans.

First, the 1983 General Assembly simplified the general usury law by classifying all loans, other than those covered by the special usury statutes, into three categories depending on loan amount. However, the 1983 General Assembly retained Code section 7-4-18, which is a criminal usury statute that makes it a misdemeanor to charge more than 5% simple interest per month, equivalent to 60% simple interest per year. In addition, the 1983 General Assembly repealed article 2 of chapter 4 of title 7, which was a special usury statute regulating residential second mortgages. This statute had restricted the interest rate for residential second mortgages to a fixed ceiling of 9%, with finance charges not to exceed 10% of the principal. This statute also limited late charges on monthly payments to 5% of the monthly payment and restricted charges for term life and

99. BROWN & KEEST, supra note 6, § 2.4.1. Several states have “reasserted their control over real estate transactions,” enacting special statutes establishing a floating interest rate ceiling for real estate loans. CRANDALL ET AL., supra note 46, § 3.01[3][c]. Other states have “effectively repealed their usury laws.” Id. at § 3.01[3][c][iii].


102. See id. § 7-4-20; see also infra notes 105-14 and accompanying text.

103. O.C.G.A. § 7-4-2(a)(1) (1989); see also infra Part V.

104. O.C.G.A. § 7-4-18 (1989). The 1983 General Assembly actually strengthened this Code section by adding subsection (c) which provides that nothing in the newly rewritten O.C.G.A. §§ 7-4-2 and 7-4-3 “shall be construed to amend or modify the provisions of this Code section.” 1983 Ga. Laws 1146, § 5.


106. 1982 Ga. Laws 574 (formerly found at O.C.G.A. §§ 7-4-29 to -36 (1982)).

107. 1980 Ga. Laws 511, 513 (formerly found at O.C.G.A. § 7-4-32(d) (1982)). This section required that interest on such loans be calculated in accordance with the provisions of O.C.G.A. § 7-4-4. Id. O.C.G.A. § 7-4-4 had set a maximum interest rate of 9% for installment loans. 1980 Ga. Laws 514, 515 (formerly found at O.C.G.A. § 7-4-4 (1982)).

108. 1986 Ga. Laws 574, 575 (formerly found at O.C.G.A. § 7-4-31 (1982)).

109. Id. at 576 (formerly found at O.C.G.A. § 7-4-32(b) (1982)).
disability insurance to a percentage set by the Insurance Commissioner.\textsuperscript{110} With the repeal of this statute, the only Georgia statute limiting interest rates on home equity loans was the criminal usury statute's limitation of 5% simple interest per month.\textsuperscript{111} Finally, the General Assembly eliminated a number of other provisions that had imposed low fixed-rate interest ceilings, including a civil usury statute section that had set the maximum interest rate for loans in general to 10.5% per year,\textsuperscript{112} a floating interest rate ceiling on real estate loans,\textsuperscript{113} and a 9% interest rate ceiling for installment loans.\textsuperscript{114} Thus, the 1983 General Assembly seemed to be willing to permit interest rates in general to be set by market forces rather than by legislative prescription.\textsuperscript{115}

Compared to DIDMCA, the actions of the 1983 General Assembly seemed to go further than the federal law in removing restrictions on interest rates. First, the 1983 General Assembly opted Georgia out of the DIDMCA provision preempting state interest rate restrictions on agricultural and business loans over $1000 for three years.\textsuperscript{116} While the General Assembly thus rejected a temporary federal elimination of interest rate ceilings on commercial loans of more than $1000, the General Assembly enacted a permanent system that in effect eliminated interest rate ceilings on all types of loans of more than $3000\textsuperscript{117} so long as the interest rate did not exceed the 5% per month ceiling imposed by the criminal usury statute.\textsuperscript{118}

Second, the DIDMCA provision affecting loans by depository institutions\textsuperscript{119} extended the same interest rate privileges that

\textsuperscript{110} Id. (formerly found at O.C.G.A. § 7-4-32(a) (1982)).

\textsuperscript{111} See O.C.G.A. § 7-4-18(a) (1989).


\textsuperscript{113} 1979 Ga. Laws 357, 359 (formerly found at O.C.G.A. § 7-4-3(a) (1982)); see 1983 Ga. Laws 1146, 1148 (repealing old O.C.G.A. § 7-4-3 (1982)).

\textsuperscript{114} 1980 Ga. Laws 514, 515 (formerly found at O.C.G.A. § 7-4-4 (1982)); see 1983 Ga. Laws 1146, 1150 (repealing old O.C.G.A. § 7-4-4 (1982)).

\textsuperscript{115} See Fleet Case Shows Need For Rate Caps, supra note 66.

\textsuperscript{116} O.C.G.A. § 7-4-20(2) (1982); see 12 U.S.C. § 86a (1982).

\textsuperscript{117} O.C.G.A. § 7-4-2(a)(1)(A) (1989). Under the 1983 classification of general loans into three types depending on amount, parties may "establish by written contract any rate of interest, expressed in simple interest terms" for loans between $5000 and $250,000. Id. § 7-4-2(a)(1). For loans of $3000 or less the interest rate must be 16% or less, unless the loan is made under a special usury statute. Id. § 7-4-2(a)(2) to (6); see infra Part V.

\textsuperscript{118} See O.C.G.A. § 7-4-18(a) (1989).

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had long been only the privilege of national banks to many federally insured depository institutions:120 the higher of either the state’s most favored lender rate121 for the type of loan in question or the alternative federal rate.122 The 1983 Georgia General Assembly did not opt out of this provision, but nonetheless went further toward deregulation by repealing Georgia’s 9% rate ceiling for second mortgages123 and its floating rate for first mortgages issued by nonfederally insured lenders.124 This legislative action left interest rates for mortgage loans limited only by the 5% simple interest per month ceiling imposed by the criminal usury statute.125 Also, this interest rate ceiling applied to all mortgage lenders in Georgia, not just to many federally insured lenders.126

Third, the DIDMCA provision preempting state restrictions on loans secured by first liens on real estate127 preempted, for certain specified lenders or types of loans,128 any state

120. Id. § 1785(g) (1988) (affecting federal credit unions); id. § 1730g(a) (repealed 1989) (affecting federal savings and loans).
121. Id. § 85 (1988); see BROWN & KEEST, supra note 74, § 3.2.2.1; CRANDALL ET AL., supra note 46, ¶ 3.01[3][b][i].
122. CRANDALL ET AL., supra note 46, ¶ 3.01[3][b][i]. The “most favored lender” rate is the highest rate that the state in which the lender is located allows any lender to charge for a loan of the same type. Id. DIDMCA did not specifically give lenders the privilege to charge this rate; the privilege has been added by interpretation. BROWN & KEEST, supra note 74, § 3.2.2.1.
123. CRANDALL ET AL., supra note 46, ¶ 3.01[3][b][i]. The alternative federal rate is 1% above the discount rate on ninety-day commercial paper held by the Federal Reserve bank in the Federal Reserve district where the national bank or other institution is located. Id.
124. 1980 Ga. Laws 511, 513 (formerly found at O.C.G.A. § 7-4-32(d) (1982)). This section required that interest on such loans be calculated in accordance with the provisions of O.C.G.A. § 7-4-4. Id. O.C.G.A. § 7-4-4 set a maximum interest rate of 9% for installment loans. 1980 Ga. Laws 514, 515 (formerly found at O.C.G.A. § 7-4-4 (1982)).
125. 1979 Ga. Laws 357, 359 (formerly found at O.C.G.A. § 7-4-3(a) (1982)).
126. See id. § 7-4-18. See id. § 7-4-18.
128. Id. § 1735f-7a(1)(C) (incorporating by reference id. § 1735f-5(b)). These lenders are from certain specified lenders or types of loans,128 any state chartered banks); id. § 1785(g) (1988) (affecting federal credit unions); id. § 1730g(a) (repealed 1989) (affecting federal savings and loans).
restrictions on "the rate or amount of interest, discount points, finance charges, or other charges"\(^{129}\) for loans secured by a first lien on residential real property, on a residential cooperative corporation, or on a residential manufactured home.\(^{130}\) Although the 1983 General Assembly opted Georgia out of this federal provision,\(^{131}\) the General Assembly's repeal of the floating interest rate for first mortgages made by nonfederally insured lenders left such loans to be limited only by the criminal usury statute's limit of 5% simple interest per month.\(^{132}\) The result was an interest rate ceiling far above the market interest rates.\(^{133}\)

V. GEORGIA GENERAL USURY LAW AS APPLICABLE TO MORTGAGE LOANS

Chapter 4 of title 7 of the Georgia Code contains the general statutory usury law of Georgia.\(^{134}\) Code sections 7-4-1, -2, -10, and -18 apply to interest rates for all types of loans and thus are of significance to mortgage loans.\(^{135}\) Also, Code section 7-4-21 bars class action suits for usury on loans secured by real estate.\(^{136}\) In 1993 the General Assembly enacted special usury legislation providing for regulation of mortgage lenders,\(^{137}\) which is discussed in Part VII.

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130. Id. § 1735f-7a(a)(1)(A). States could opt out of the preemption of restrictions on interest rates before April 1, 1983. Id. § 1735f-7a(b)(2). States could and still may at any time opt out of the preemption of restrictions on discount points and finance charges. Id. § 1735f-7a(b)(4).
132. See id. § 7-4-18(a); 1983 Ga. Laws 1146, 1148 (repealing 1979 Ga. Laws 356 (formerly found at O.C.G.A. § 7-4-3 (1982))).
133. Compare Georgia's maximum 60% interest rate ceiling with an interest rate of approximately 20% in the 1970s and 1980s that was considered by the federal government to be extremely high. See BROWN & KEEST, supra note 6, § 2.4.1. See generally Fleet Case Shows Need for Rate Caps, supra note 66 (arguing that abusive loans are "predictable in a state that allows lenders to charge up to 60 percent interest on loans").
136. Id. § 7-4-21.
137. Id. §§ 7-1-1000 to -1021.
Code section 7-4-1 defines usury as "reserving and taking or contracting to reserve and take, either directly or indirectly, a greater sum for the use of money than the lawful interest." The civil penalty for usury in Georgia, specified by Code section 7-4-10, is that the user must forfeit all interest on the loan, including both usurious and non-usurious interest, but may still collect any unpaid principal.

Code section 7-4-18 specifies an additional criminal penalty for usury when the usury is egregious, making it a misdemeanor to charge more than 5% simple interest per month. The Supreme Court of Georgia has ruled that the penalty for violating this provision is the loss of all interest with the ability to collect unpaid principal—the same penalty as the civil penalty set by Code section 7-4-10.

Code section 7-4-2, the primary civil usury section, specifies the maximum interest rates for loans in general and divides loans into three classes based on loan amount. For loans up to $3000, the maximum interest rate is 16% simple interest, unless the loan is made "pursuant to another law", that is, pursuant to one of the special usury statutes listed in Code section 7-4-2(c). For loans above $250,000, the parties "may

138. Id. § 7-4-1.
139. Id. § 7-4-10(a). State penalties for usury range from forfeiture of only the usurious interest to forfeiture of both principal and interest plus payment of statutory penalties. BROWN & KEEST, supra note 6, § 9.41.1.
140. O.C.G.A. § 7-4-18 (1989); see, e.g., Wall v. Lewis, 16 S.E.2d 430, 431 (Ga. 1941) (holding that the legislature's purpose in enacting the statute was "to condemn usury, and when usury reached such proportions as more than five per cent per month, to enhance the existing penalties of civil forfeitures by adding the criminal penalty of misdemeanor, which would attach and apply to the person of the usurer").
143. O.C.G.A. § 7-4-2(a) (1989).
144. Id. § 7-4-2(a)(2).
145. Hilary P. Jordan, Georgia Interest and Usury Issues in Secured Financing 84-14 (Institute of Continuing Legal Education in Georgia, Publication No. 890804, 1989). "These special statutes generally apply to consumer credit transactions only and permit interest and other finance charge yields on credit transactions involving generally $3,000 or less that in some cases are substantially higher than the 16.5% simple interest rate prescribed for such transactions by O.C.G.A. § 7-4-2(a)(2)." Id. O.C.G.A. § 7-4-2(c) states that "nothing contained in this Code section [7-4-2] shall be construed to amend or modify the provisions of [the special statutes listed]." O.C.G.A. § 7-4-2(c) (1989). Thus, the 16% simple interest limit of 7-4-2(a)(2) does not apply to the special usury statutes. Jordan, supra. The following statutes are listed in O.C.G.A. § 7-4-2(c): the Georgia Industrial Loan Act (O.C.G.A. §§ 7-3-1 to -29 (1989 &
establish by written contract any rate of interest,"¹⁴⁶ apparently subject to the 5% per month simple interest ceiling set by Code section 7-4-18.¹⁴⁷

For loans between $3000 and $250,000, "the parties may establish by written contract any rate of interest, expressed in simple interest terms,"¹⁴⁸ subject to the ceiling of 5% per month imposed by Code section 7-4-18.¹⁴⁹

Subsection (a)(3) provides definitions of principal and interest that are extremely flexible: “principal” means “such charges to which the parties may agree,” while “interest” is “a charge for the use of money computed over the term of the contract at the rate stated in the contract or precomputed at a stated rate on the scheduled principal balance or computed in any other way or any other form.”¹⁵⁰ This flexibility of definition is significant because the formula used to calculate the actual interest rate of a loan, as a step in determining whether a loan is usurious, is the standard formula: Rate = Interest/(Principal x Time).¹⁵¹ For example, characterizing a loan origination fee as a component of Interest as opposed to treating it as a component of Principle increases the resulting actual Rate of interest.¹⁵²

¹⁴⁷ Grice & Blumen, supra note 134, at 299; see O.C.G.A. § 7-4-18(a) (1969).
¹⁴⁹ See id. § 7-4-2(a)(1)(A) (stating that the parties may contract in writing for any rate of interest “[notwithstanding the provisions of other laws to the contrary, except Code Section 7-4-18]” (emphasis added)); see Grice & Blumen, supra note 135, at 299.
¹⁵¹ See CRANDALL ET AL., supra note 46, ¶ 3.01[4] (observing that in states without a comprehensive usury code such as the Uniform Consumer Credit Code, statutory or regulatory definitions of interest tend to be “sketchy”). Commonly any “general ‘service’ or other charge” is treated as interest. Id. But any fee excluded from interest by statute or used to reimburse the lender for expenditures (e.g., attorney fees) is treated as principal. Id. If the statutory definition does not clearly identify a fee as interest then “case law must be consulted.” Id.; see also BROWN & KEEST, supra note 6, § 4.2.1. The authors present the formula as I = P x R x T, or Interest = Principal x Rate x Time. BROWN & KEEST, supra note 6, § 4.2.1. “Interest” and “Principal” are dollar amounts, “Time” is the term of the loan in months or years. Id. To derive the formula for the interest rate R, divide both sides of the first equation by (P x T) and obtain the formula: Rate = Interest/(Principal x Time).
¹⁵² See CRANDALL ET AL., supra note 46, ¶ 3.01[4]. For example, in Norris v. Sigler

http://readingroom.law.gsu.edu/gsulr/vol11/iss3/5
Subsection (a)(3) of Code section 7-4-2 further provides that discount points and loan origination fees in loans secured by an interest in real estate "shall not be considered interest and shall not be taken into consideration in the calculation of interest." However, the Supreme Court of Georgia has held that this language does not apply to the criminal usury statute of Code section 7-4-18; in determining whether that Code section applies, a court must treat discount points and loan origination fees as interest.

Subsection (b) of Code section 7-4-2 deals with acceleration of the maturity of a loan and prepayment penalties. Subsection (b)(1) provides that upon acceleration the lender must rebate to the borrower any "unearned interest" that if retained by the lender would result in the borrower paying a higher rate of interest than is specified by the loan contract. Subsection (b)(2) provides that a lender may not exact prepayment penalties unless such penalties are stipulated in the contract.

Finally, Code section 7-4-21 prohibits any class action suit for usury based on "any loan secured by an interest in real estate," thus preventing a group of aggrieved borrowers from combining to sue a lender. Although the constitutionality of this section under the Georgia Constitution was raised in Fleet Finance, Inc. v. Jones, the court did not reach the issue.

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*Daisy Corp.*, the court rejected the lender's argument that a $5800 loan origination fee should be treated as principal and instead held that it was to be treated as interest. 392 S.E.2d 242, 243 (Ga. 1990). The court's calculation of the actual interest rate can be summarized as follows:

\[
\text{Rate} = \frac{\text{Interest}}{\text{Principal} \times \text{Time}}
\]

\[
\text{Rate} = \frac{\$14043.14}{($6510.50 \times 36 \text{ months})} = 5.99\% \text{ per month.}
\]

*Id.* at 244. Thus the loan exceeded the interest rate ceiling of 5% simple interest per month set by O.C.G.A. § 7-4-18 (1989). *Id.* Treating the $5800 loan origination fee as principal would have resulted in the following calculation:

\[
\text{Rate} = \frac{\text{Interest}}{\text{Principal} \times \text{Time}}
\]

\[
\text{Rate} = \frac{\$9243.14}{($12310.50 \times 36 \text{ months})} = 1.86\% \text{ per month.}
\]

154. Norris, 392 S.E.2d at 243-44.
155. O.C.G.A. § 7-4-2(b) (1989).
156. *Id.* § 7-4-2(b)(1).
157. *Id.* § 7-4-2(b)(2).
158. *Id.* § 7-4-21.
159. 430 S.E.2d 352, 354 (Ga. 1993).
VI. JUDICIAL ACTION: SIGNIFICANT GEORGIA CASES

This Part surveys a sequence of cases in state and federal courts in Georgia in the early 1990s that addressed Code section 7-4-18, the criminal usury statute setting the maximum interest rate for a general loan to 5% simple interest per month.160 In each of these cases the borrower asserted usury claims against the lender who had already foreclosed, or was threatening to foreclose, on residential property that the borrower had pledged as security for a home equity loan.161

Determining whether charging a higher rate of interest is permitted by law requires two steps: (1) determining the maximum interest rate permitted by law, which depends on the particular federal or state statute governing the loan in question; and (2) determining the actual rate of interest charged in the loan.162

In all of these cases advocates for the borrower argued that the loan was usurious if the “points” charged by the lender were properly reckoned in the usury calculation.163 Points, also termed discount points, loan origination fee, or loan fee, are not payments made to the lender to recompense the lender for any expense or service on his part in making the loan, but rather are an additional finance charge that the lender collects from the borrower at the outset of the loan period.164 In each case, the lender included the points in the face amount of the loan; that is,

160. O.C.G.A. § 7-4-18 (1989). This Code section reads in relevant part:
   Any person, company, or corporation who shall reserve, charge, or take for any loan or advance of money, or forbearance to enforce the collection of any sum of money, any rate of interest greater than 5 percent per month, either directly or indirectly, by way of commission for advances, discount, exchange, or the purchase of salary or wages; by notarial or other fees; or by any contract, contrivance, or device whatsoever shall be guilty of a misdemeanor. . . .
   Id. § 7-4-18(a).

161. See, e.g., Fleet, 430 S.E.2d at 353 (involving borrowers who asked court to enjoin lender from foreclosing on properties on the basis that the loans were usurious); Norris v. Sigler Daisy Corp., 392 S.E.2d. 242, 243 (Ga. 1989) (involving the foreclosure of a real estate deed given by the borrower to secure a loan).

162. CRANDALL ET AL., supra note 46, ¶ 3.01[2]. See id. ¶ 3.01[3][a]-[c] for a more detailed analysis of these two steps.

163. See, e.g., Fleet Fin., Inc. v. Jones, 430 S.E.2d 352, 357 (Ga. 1993) (rejecting borrowers’ argument that loan origination fees and discount points should be treated as interest paid in the first month of the loan); Norris v. Sigler Daisy Corp., 392 S.E.2d. 242, 243 (Ga. 1990). See generally BROWN & KEEST, supra note 6, § 4.2.3.7.

164. BROWN & KEEST, supra note 6, § 4.2.3.7.
the face amount of the loan included two components: (1) points, which were retained by the lender; and (2) the funds disbursed to the borrower. The value of the points was considerable, amounting to 20% or more of the face value of the loan.

First, borrowers argued that in the calculation of whether a loan is usurious, points should be treated as interest. The Supreme Court of Georgia approved this interpretation of Code section 7-4-18 in 1990 in Norris v. Sigler Daisy Corp. The court held that the lender’s “origination fee” fell within the statute's definition of usury as a charge for a loan of “‘any rate of interest greater than 5 percent per month, [charged] either directly or indirectly . . . or by any contract, contrivance, or device whatsoever.'” Thus, Norris somewhat constrained the “bite” of high interest loans by obliging a lender to keep the lender's total finance charges, including both interest and points, from exceeding the legal maximum of 5% simple interest per month.

The borrowers’ second argument was two-pronged: (1) points should be reckoned as interest occurring in the first month of the loan; and (2) if the first month’s interest on the loan, including points, is greater than the statutory maximum of 5% per month, the loan should be considered usurious, even if all monthly payments after the first are less than 5% per month. Although this argument prevailed for a time in

165. See, e.g., Fleet, 430 S.E.2d at 352, 354 (observing that discount fees and loan origination fees were deducted from the face amounts of the loans, and the remainder was disbursed to the borrowers); Norris, 392 S.E.2d. at 243-44 (noting that face amount of the loan included $5800 loan origination fee that the lender did not disburse to the borrower); see also BROWN & KEEST, supra note 6, § 4.2.3.7 (stating that “points are usually treated as a discount which reduces the amount of loan proceeds that the borrower receives” (footnote omitted)).
166. See, e.g., Fleet, 430 S.E.2d at 354 (noting that loan origination fees ranged from 22% to 27% of the principal); Norris, 392 S.E.2d. at 243-44 (noting that face amount of the loan was $12,310.50, of which $5800 was a loan origination fee).
167. E.g., Norris, 392 S.E.2d. at 243.
168. Id.
169. Id. (quoting O.C.G.A. § 7-4-18(a) (1989)). For the court’s calculations in Norris, see supra note 152.
171. See, e.g., Fleet Fin., Inc. v. Jones, 430 S.E.2d 352, 354 (Ga. 1993). Borrowers argued that the points were paid in the first month of the loan at the loan closing. Id. Points were not refundable or rebateable even if the borrower repaid the loan immediately. Id. Therefore, borrowers argued, the points should be treated as interest occurring in the first month of the loan. Id.
federal district court in the Southern District of Georgia,173 the Supreme Court of Georgia ultimately rejected this argument in 1993 in Fleet Finance, Inc. v. Jones.174

In the loans in question in Fleet Finance, Inc. v. Jones, 22% to 27% of the face amount of the loans consisted of up-front points paid at closing.175 The lender withheld these points from the face amount of the loan and disbursed the remainder to the borrowers.176 These points were nonrefundable and nonrebateable.177 However, the average monthly interest rate for these loans did not exceed the statutory ceiling of 5% per month, even though points were treated as interest as required by Norris v. Sigler Daisy Corp.178

In Fleet Finance, Inc. v. Jones, borrowers argued that, since the points were collected in the first month of the loan and were nonrefundable, these points should be treated as interest paid in the first month of the loan.179 Calculating interest for the first month in this way resulted in an interest rate of more than 5% for the first month of the loan, even though the interest paid in each of the other months of the loan was less than 5% per month.180 Borrowers argued that this high payment of interest

174. Fleet, 430 S.E.2d at 364.
175. Id.
176. Id.
177. Id.
178. Id. (referring to Norris v. Sigler Daisy Corp., 392 S.E.2d 242, 243-44 (Ga. 1989)).
179. Id.
180. See id. The Fleet court calculated that the interest rate for the loan made to plaintiff Jones was 1.57% simple interest per month if the total upfront charges and the interest were spread over the entire term of the loan. Id. But, if the upfront points were treated as interest paid in the first month of the loan, the interest rate
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in the first month of the loan made the loans usurious under Code section 7-4-18.181

In its briefs, Fleet countered the “first month’s fees” argument advanced by borrowers with the argument that points should be treated according to the doctrine of “spreading.”182 Spreading is a technique generally used by courts in determining whether a loan is usurious and consists simply of averaging all the finance charges over the entire term of the loan.183 Under this method, even if the interest paid in one particular month of a loan exceeds the usury ceiling, the loan is not usurious so long as the average interest rate per time period does not exceed the interest ceiling.184

Although the Supreme Court of Georgia did not use the term spreading in its opinion, the court agreed with Fleet, holding that the total interest must be averaged over the entire term of the loan when calculating whether a loan is usurious under Code section 7-4-18.185 The court reasoned that the entire term of the loan is the basis of several provisions integral to a loan agreement, and therefore, it is reasonable to use the entire term of the loan to measure the interest rate as well.186 The court also cited cases from other states in which courts have held that the total interest should be calculated based on the entire term of the loan.187 The court noted that the borrowers’ real concern

in the first month was 23% simple interest for that month, far above the statutory ceiling of 5% simple interest per month. Id.

181. Id.
182. Supplemental Brief for Appellants at 19, Fleet Fin., Inc. v. Jones, 430 S.E.2d 352 (Ga. 1993) (No. S93A0815). Fleet asserted that the spreading method “is consistent with commercial and economic reality.” Id. at 17. Fleet argued that: (1) points deducted at closing are an integral part of the finance charges, which are repaid over the entire term of the loan; (2) a federal standard requires accountants to treat points as spread over the term of the loan; and (3) the method of calculating interest urged by plaintiffs would make many loans illegal because of the amount of points charged. Id. at 16-23.
183. BROWN & KEEST, supra note 6, § 4.2.3.6.
184. Id. Fleet further argued that in Norris v. Sigler Daisy Corp. the Supreme Court of Georgia had used the spreading method because the court had averaged the sum of all the finance charges, including the up-front points, over the entire term of the loan. Brief of Appellants at 20-22, Fleet Fin., Inc. v. Jones, 430 S.E.2d 352 (Ga. 1993) (No. S93A0815); see Norris v. Sigler Daisy Corp., 392 S.E.2d 242, 243-44 (Ga. 1990). In Fleet the court held that it was not bound by the calculation used in Norris. Fleet, 430 S.E.2d at 355.
185. Fleet, 430 S.E.2d at 357.
186. Id. at 356.
187. Id.; see French v. Mortgage Guarantee Co., 104 P.2d 655, 657-59 (Cal. 1940);
was “not so much with spreading points and origination fees but with the fact that § 7-4-18 does not regulate points and permits 60% interest a year.” However, the court noted that borrowers should seek a remedy to this concern through the legislature.

VII. LEGISLATIVE ACTION: RESPONSE OF THE GEORGIA GENERAL ASSEMBLY

In response to widespread concern over home equity loan abuses, the 1993 Georgia General Assembly enacted strong consumer protection legislation regulating home equity lending practices. However, the General Assembly failed to approve a bill that would have set a floating interest rate ceiling for home equity loans.

The new regulatory scheme, as amended in 1994, comprising new Code sections 7-1-1000 to -1021, provides for the licensing and regulation of mortgage lenders and mortgage brokers doing business in Georgia. The statute, based in part on home equity loan acts in other states, prohibits abusive mortgage loan practices and authorizes the Department of Banking


188. Fleet, 430 S.E.2d at 357.
189. Id.
190. See Vejnoska, Lawmakers Call for Hearings on Fleet, supra note 25, at D2; Vejnoska, Legislators Urged to Cap Equity Loan Interest Rates, supra note 25, at C6; Vejnoska, supra note 71.
192. See SB 105 (SCSFA), 1993 Ga. Gen. Assem.; see also supra Part III.
193. O.C.G.A. §§ 7-1-1000 to -1021 (Supp. 1994); see also Ben Smith III, House OKs Licensing Mortgage Companies, ATLANTA CONST., Feb. 12, 1993, at E3. See generally Legislative Review, 10 GA. ST. U. L. REV. 11 (1993) [hereinafter Legislative Review 1993]; Legislative Review, 11 GA. ST. U. L. REV. 41 (1994) [hereinafter Legislative Review 1994]. A mortgage lender is defined as “any person who directly or indirectly makes, originates, or purchases mortgage loans or who services mortgage loans.” O.C.G.A. § 7-1-1000(8) (Supp. 1994). A mortgage broker is defined as any person who directly or indirectly solicits, processes, places, or negotiates mortgage loans for others, or offers to solicit, process, place, or negotiate mortgage loans for others or who closes mortgage loans which may be in the mortgage broker’s own name with funds provided by others and which loans are assigned within 24 hours of the funding of the loans to the mortgage lenders providing the funding of such loans.

Id. § 7-1-1000(7).
and Finance (the Department) to monitor certain mortgage lenders and brokers and enforce the provisions of the statute. The legislation delineates two classes of mortgage lenders and mortgage brokers who are subject to its provisions: (1) licensees and (2) persons exempted from licensing, some of whom must register with the Department and who are therefore termed registrants. Exempt persons include: state chartered or federally chartered banks, savings institutions, building and loan associations, and credit unions whose deposits are federally insured; lenders already regulated by the Department, such as Georgia banks and bank holding companies; and several other groups, such as Georgia and federal government agencies. However, federally insured organizations and those organizations already regulated by the Department, which are exempt from licensing but comprise the class of registrants, must provide prescribed information. Licensees, who are closely monitored under the statute, comprise all other mortgage lending institutions whose deposits are not federally insured, including out-of-state, state-chartered banks, savings institutions, building and loan associations, and credit unions.

Both exempt persons and licensees are subject to Code section 7-1-1013, which specifies lending practices that are fraudulent or predatory. As to enforcement of the legislation, the

196. See, e.g., id. § 7-1-1009 (permitting the Department to examine the records of those lenders and brokers licensed under the statute).
197. See, e.g., id. §§ 7-1-1017 to -1018 (authorizing Department to revoke or suspend licenses and issue cease and desist orders).
198. Id. § 7-1-1002(1)-(2).
199. Id. § 7-1-1001(a)(1).
200. Id. § 7-1-1001(a)(2); see id. § 7-1-64(a) (1989) (authorizing the Department to examine financial institutions); id. § 7-1-4(21) (Supp. 1994) (defining “financial institutions” to include banks).
201. Id. § 7-4-1001(a)(3)-(13).
202. Id. § 7-1-1001(b). For example, the statute calls for the registrant’s business address and phone number. Id.
203. See, e.g., id. §§ 7-1-1002, -1004 to -1006.
204. Id. § 7-1-1001(a)-(b). Lenders who must apply for licenses are those lenders not already identified as exempt persons. Id. These lenders must apply for and be approved for a license to do business in Georgia. Id. §§ 7-1-1002(1), -1003(a).
205. Id. § 7-1-1013. The prohibited acts include making false promises or misrepresentations that might influence a borrower to take a mortgage loan; misrepresenting the conditions of a transaction; failing to disburse funds in accordance with a written agreement; “improperly refus[ing] to issue a satisfaction of a mortgage loan”; wrongfully withholding or misusing money or other property
Department is authorized to impose administrative fines. These fines are an important means of enforcement, because fines are procedurally simple for the Department to initiate. Additionally, the Department may suspend, revoke, or fail to renew a license or registration. The Department may issue a cease and desist order, seek a court order (requested via the Attorney General’s office), or impose a civil penalty of up to $1000 per day upon licensees. Violation of the statute is a misdemeanor, punishable by imprisonment or fine, and any licensee, registrant, or exempt person, or any of their members, officers, agents, or employees may be punished. The effectiveness of this new legislation regulating home equity loans will depend on the firmness with which the Department enforces it because many provisions of the statute authorize the Department to write regulations or make decisions as to implementation.

belonging to the borrower; committing a fraud or any other practice that is not in good faith and fair dealing; fraudulently underwriting a mortgage; leaving blank spaces in a loan document to be filled out after the borrower has signed it; making a mortgage loan with intent to foreclose; and using extortion to collect a payment from a borrower. id. 206. Id. § 7-1-1018(f).
208. O.C.G.A. § 7-1-1017 (Supp. 1994).
209. Id. § 7-1-1018.
210. Id. § 7-1-1019.
211. See id. § 7-1-1012 (authorizing Department to “make reasonable rules and regulations, not inconsistent with law, for the enforcement of this article”); id. § 7-1-1014 (enacting regulations concerning loan disclosures to consumers); id. § 7-1-1015 (enacting rules as to escrow accounts); id. § 7-1-1016 (enacting regulations as to advertising); id. § 7-1-1017(a)-(c) (determining whether to suspend a license or registration, subject to judicial review); id. § 7-1-1018(c) (determining amount of civil penalty, but not to exceed $1000 per day); id. § 7-1-1018(f) (determining amount of administrative fines); id. § 7-1-1021 (authorizing enactment of regulations concerning lock-in agreements and commitment agreements). The Department has implemented regulations in a number of areas under the authority granted by the statute. Telephone Interview with Leslie A. Bechtel, Deputy Commissioner for Legal Affairs, Georgia Department of Banking and Finance (Mar. 14, 1995). Currently the Department has regulations in these areas: (1) license fees and supervision fees ($250 fee for investigation upon initial application for a license, and an annual fee of $400 for mortgage brokers or $800 for mortgage lenders, proceeds going to the State of Georgia); (2) examination and investigation fees (a $6.50 per-loan tax paid by the borrower at loan closing, proceeds going to the State of Georgia); (3) disclosure requirements (disclosures to be made to the borrower by the mortgage broker or lender at or before loan closing regarding finance charges and the risk of foreclosure upon default); (4) advertising requirements (ads must state that licensee is licensed by the State of Georgia); (5) recordkeeping requirements (records used to determine
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In enacting new Code sections 7-1-1000 to -1021, the General Assembly showed that it was ready to regulate problem areas in consumer lending. However, the General Assembly also demonstrated an aversion to interest rate ceilings by rejecting SB 105, a bill that would have set a floating interest rate ceiling for home equity loans. SB 105 passed the Senate in 1993 but failed to clear the House Committee on Banks and Banking.
in both 1993\textsuperscript{215} and 1994\textsuperscript{216} SB 105 would have set the maximum permissible interest rate on home equity loans to a floating rate of 11\% over the current federal prime rate.\textsuperscript{217} Opponents of the bill argued that passage of the bill would deprive low-income consumers of credit\textsuperscript{218} and was unnecessary because of the enactment of Code sections 7-1-1000 to -1021.\textsuperscript{219}

**CONCLUSION**

Both the absence of an effective interest rate ceiling and lax regulation of mortgage loans were factors that contributed to the severity of the home equity loan scandal in Georgia. The correction of either one of these deficiencies might have significantly limited the damage the predatory scheme caused to low-income borrowers.

Proponents of interest rate ceilings regard a ceiling as a reasonable tool to restrain overreaching by lenders, who hold a much more powerful bargaining position than borrowers. By contrast, opponents of interest rate ceilings regard a ceiling as, at best, a necessary element of a criminal statute, set up to discourage the most egregious offenses and placed so high that it will probably never influence the ordinary business of lending.\textsuperscript{220}

The substantial deregulation of interest rates by the 1983 Georgia General Assembly and the hostility of the 1993 and 1994 Georgia General Assemblies toward SB 105 was perhaps an overreaction to the powerlessness that the lending industry felt during the late 1970s when high market interest rates pushed against low state-imposed, fixed-rate interest ceilings.

The history of usury law in the United States demonstrates that interest rate ceilings developed as a prerogative of the

\textsuperscript{215} Final Composite Status Sheet, Mar. 23, 1993; see also Emling, supra note 2; Emling, *Facts* Needed, supra note 76.

\textsuperscript{216} Final Composite Status Sheet, Mar. 23, 1993; see also Emling, *Home-Equity Loan Bill Stalls*, supra note 76.


\textsuperscript{218} See supra note 76 and accompanying text.

\textsuperscript{219} See Emling, supra note 2 (reporting that Rep. Clinton Oliver stated that SB 105 “may not be necessary” because home equity lenders are regulated under the new O.C.G.A. §§ 7-1-1000 to -1021; O.C.G.A. §§ 7-1-1000 to -1021 (Supp. 1994).

\textsuperscript{220} “Georgia’s criminal usury statute is not designed to set fair interest rates on loans” but rather to “enhance the civil penalties in only the most egregious cases” of usury. Johnson v. Fleet Fin., Inc., 785 F. Supp. 1003, 1008 (S.D. Ga. 1992) (citing Wall v. Lewis, 16 S.E.2d 430, 431 (Ga. 1941)).
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legislature. The sequence of home equity loan cases in Georgia in the early 1990s was an unsuccessful effort by borrowers' advocates to persuade the courts to encroach upon the legislative prerogative of setting interest rate ceilings. However, by focusing public attention on the injury caused by overreaching lenders under existing law, these cases may have contributed to the General Assembly's adoption of the legislation regulating mortgage lenders and mortgage brokers doing business in Georgia. This enactment is typical "special" usury legislation because it aims solely at correcting an existing problem associated with a particular type of loan or group of lenders.

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