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Usury's Intent Requirement: Should There Be a Good Faith Defense?

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COMMENTS

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I INTRODUCTION

Credit crunches during the 1970's and 1980's revitalized commentary on the subject of usury—the unlawful taking of excessive interest for a loan or for forbearance of money owed. As market interest rates rose above usury rates, academics and legislators widely debated usury law changes that would accommodate both higher interest rates and alternative loan instruments.[1] Commentators advocating abolition of usury laws have also published extensively.[2]

The elements of usury, however, have received little attention. This comment discusses the intent element in a transaction

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1. Federal legislators responded to interest rate pressures by passing the Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stat. 132, *as amended by* Housing and Community Development Act of 1980, Pub. L. No. 96-399, § 324, 94 Stat. 1614, 1647-48. Commentary on the legislation is abundant. *See, e.g.*, Burke, *The New Federal Usury Law*, 36 BUS. LAW. 1237 (1981); Climo & Evans, *Interest Rate Deregulation*, 37 BUS. LAW. 1381 (1982); Farabee & Dodds, *Recent State and Federal Developments in Interest Rate Regulation*, 44 TEX. B.J. 879 (1981); Comment, *The Depository Institutions Deregulation and Monetary Control Act of 1980 and Its Effect on the Mortgage Market*, 1981 ARIZ. ST. L.J. 211.

2. *See, e.g.*, Crafton, *An Empirical Test of the Effect of Usury Laws*, 23 J.L. & ECON. 135 (1980); Rhodes, *The Literary Case for Repeal of the Usury Laws*, 35 PERS. FIN. L.Q. REP. 183 (1981); Note, *Usury Legislation—Its Effects on the Economy and a Proposal for Reform*, 33 VAND. L. REV. 199 (1980). One state legislator articulated most of the arguments against usury laws more than a century ago:

> I shall vote for the repeal of the usury laws, because I do not think they aid the borrower, but rather bring him to a worse condition than he would be in, in an open market. They have balked the humane purposes that gave them life. I vote for their repeal, because I think them in violation of the immutable laws of trade, and therefore necessarily leading to evil; because they are of no effect when the market rate is equal to or below the legal rate, and, when it is above, tend to frighten away capital, induce chicanery, circumventions, frauds and go-betweens, and to introduce the borrower to the worst class of lenders.

Rhodes, *supra*, at 186 (quoting REPORT OF PROCEEDINGS OF HOUSE OF REPRESENTATIVES OF MASSACHUSETTS (Feb. 14, 1867)).

usurious on its face.[3] States retaining usury laws[4] agree that a lender must have specific intent before he can be liable for usury. With few exceptions,[5] the intent required is not an intent to violate the usury statute, but specific intent to make the bargain made and to receive the interest rate received.[6] The consequence of this objective standard is that the intent requirement is generally meaningless,[7] preventing liability only if clerical error has occurred.

This comment advocates an alternative definition for usurious intent, one similar to Florida's intent requirement. This alternative approach considers whether the transaction was made in good faith. Focusing on good faith is preferable because the current standard of intent imposes usury too harshly and applies to transactions not requiring usury protection. Furthermore, because this alternative definition consolidates several doctrines applicable to usury, lenders will no longer need to rely on the doctrine of estoppel to prevent fraudulent borrowers from asserting the usury defense.

II. Harsh Consequences of Usury's Intent Requirement

Several recent cases highlight the inadequacy of usury's intent requirement. In these cases, the lender was liable for usury

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3. If a contract on its face imports usury, wrongful intent is implied. The only intent required is the intent to make a bargain. If a contract is not usurious on its face, then courts examine the form of a transaction to see if intent to circumvent the usury statutes exists. The requisite intent is the intent to evade the laws. 47 C.J.S. *Interest & Usury* § 120 (1982). This comment discusses intent when usury appears on the face of a transaction.

4. At least six states now statutorily allow parties to agree to any rate of interest. Those states are Arizona, Ariz. Rev. Stat. Ann. § 44-1201 (Supp. 1985), Massachusetts, Mass. Gen. Laws Ann. ch. 107, § 3 (West 1958), Nevada, Nev. Rev. Stat. § 99.050 (1984), New Hampshire, N.H. Rev. Stat. Ann. § 336:1 (1984), New Mexico, N.M. Stat. Ann. § 56-8-11.1 (Supp. 1985), and Utah, Utah Code Ann. § 70C-2-101 (Supp. 1985). Idaho, Maine, and Wisconsin effectively have eliminated usury restrictions by repealing their usury statute or by greatly limiting the stetute'e application. *See* 1 Consumer Cred. Guide (CCH) ¶ 510 (1985).

5. The general rule in Florida is that a lender must act in bad faith to be liable for usury. *See infra* text accompanying notes 20-26. Likewise, a few North Carolina cases require the lender to have "corrupt intent" and act in bad faith. Clarkson v. Finance Co. of Am., 328 F.2d 404, 407 (4th Cir. 1964); Bundy v. Commercial Credit Co., 200 N.C. 511, 157 S.E. 860 (1931).

6. *See supra* note 3.

7. "Where the agreement is clearly usurious on its face, the intention to violate the law is 'conclusively presumed.'" Lowell, *A Current Analysis of the Usury Laws: A National View*, 8 San Diego L. Rev. 193, 218 (1971).

even though the borrower had initiated the transaction and the lender's intent was to accommodate the borrower.

A. The Ford Motor *Case*

In *Ford Motor Credit Co. v. Hutcherson*,[8] Hutcherson purchased a Lincoln Mark V automobile on a level payment installment sales contract that financed $12,700 at 10% per annum, payable in 48 equal monthly installments of $322.09. Ford's original contract was not usurious.[9] However, at Hutcherson's request, a Ford clerk changed the date of Hutcherson's first payment to the 10th of the month instead of the 17th. The term of the loan thus became seven days less than four years, and the loan became usurious under the "exact day interest" method.[10] The revised contract was not usurious under the "banker's interest" method.[11] Hutcherson tendered his first payment under protest claiming that the contract was usurious. Ford offered a check to cover the excess finance charge, which Hutcherson refused to accept. He made two more payments under protest and then stopped payment altogether. When Ford filed suit to replevy the automobile, Hutcherson pleaded usury. The trial court found the contract usurious, and the Arkansas Supreme Court affirmed. Under Arkansas law the sales contract was declared void and Hutcherson retained his new car without having to make further payments.

The Arkansas Supreme Court noted that the circumstances of the case were "suspicious."[12] Hutcherson had worked for eight years as an assistant bank examiner. Two months before purchasing the car he attended a seminar on the subject of checking the accuracy of annual percentage rates on consumer loans. He was aware of the Arkansas usury law. Also, Ford's clerk altered the payment date at Hutcherson's request; the

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8. 277 Ark. 102, 640 S.W.2d 96 (1982).

9. *Id.* at 107, 640 S.W.2d at 99.

10. *Id.* at 104-05, 640 S.W.2d at 98. Exact day interest is the method that counts each day in the interest period. The basis year to compute interest is 365 or 366 days. Using exact day interest, Hutcherson would have paid $25.88 in usurious interest.

11. *Id.* at 105, 640 S.W.2d at 98. "Banker's interest has a basis year of 360 days but interest is charged on the exact number of calendar days in the interest period. . . . Thus in any period the interest computed equals 365/360 more than the stated annual interest rate." *Id.* at 105-06, 640 S.W.2d at 98. Since Ford used an ordinary interest table to calculate this particular loan, the court did not consider Ford's argument that the loan was not usurious using banker's interest. *Id.* at 106, 640 S.W.2d at 98.

12. *Id.* at 108, 640 S.W.2d at 99.

clerk was completely unaware that this slight change would void the transaction. Nevertheless, the court stated that "the intent required is the intent to charge a certain amount and . . . if the amount exceeds 10%, there was an intent to charge a usurious rate of interest."[13]

The decision's blatant inequities did not go unnoticed. Three dissenting judges argued that "[w]here intent is lacking and it is clear that no systematic pattern is being practiced to circumvent our usury laws . . . it is wrong to impose the highly punitive result that enables a borrower to drive away in a $12,700 automobile."[14]

B. The Parkway Highlands *Case*

In *Parkway Highlands Development Co. v. Estate of Allan*[15] the objective definition of intent led to a particularly perverse result. Parkway was purchasing land in California from Allan, an elderly widow with only a marginal understanding of financial matters. Parkway was unable to make payments and Allan was prepared to begin foreclosure proceedings. However, Parkway offered Allan $25,000 and an additional note for $75,000 if she would give Parkway another ninety days. Parkway needed the ninety days to complete a sale of the property to real estate developers at a price providing a huge profit to Parkway, a fact known by Allan. Neither Parkway nor Allan knew that the $100,000 in return for an extension constituted forbearance in violation of California's usury statute.[16] Allan and her attorney agreed to postpone proceedings since she did not want the property returned and had no desire to foreclose.

The additional ninety days enabled Parkway to sell the property and reap a tremendous profit. Then, having been informed that the $100,000 given to Allan was usurious, Parkway filed a usury action against Allan and her attorney ten days after escrow closed, seeking a return of all interest paid, treble damages, and prejudgment interest, based on California law.[17] Since

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13. *Id.* at 106, 640 S.W.2d at 99 (citation omitted).

14. *Id.* at 112, 640 S.W.2d at 102 (Hays, J., dissenting).

15. 1 Civ. No. 54664 (Cal. Ct. App. Oct. 25, 1983) (unpublished opinion and therefore not precedent).

16. *Id.* at 11. The total paid by Parkway to Allan was $100,993.75 on an unpaid balance of $561,013.61. The rate of interest for forbearance was therefore 76% per annum. *Id.*

17. "In a transaction which is usurious from its inception, *all* interest paid under the

Parkway did not know the $100,000 constituted usury when it suggested the payment to Allan, and since Allan did indeed intend to accept the $100,000, the jury found for Parkway, although the judge only granted return of the $100,000.

Parkway, like *Ford Motor,* illustrates the problems with usury's objective intent requirement. Loaning money or forbearing on a debt is not inherently wrong. Indeed, there are beneficial social consequences. Also, the borrower frequently instigates usury and the lender does not realize that the loan may be usurious. Thus, usury laws often mock equity by condemning a lender who intended to help the borrower. In some unjust situations, the doctrine of estoppel bars usury action.[18] However, as discussed below,[19] estoppel is an inappropriate vehicle for handling this problem.

III. Florida's Good Faith Defense

Florida has not adopted the doctrine that usury requires only the intent to make the bargain. Rather, Florida courts hold that the lender must have "corrupt" intent or act in bad faith.[20]

Numerous Florida cases have addressed the intent requirement.[21] The most significant case, *Dixon v. Sharp,*[22] is factually similar to *Parkway.* Borrower Sharp contracted to purchase real property. Sharp asked Dixon, a real estate salesman, to loan him $10,000 to complete the sale. Dixon did not have the money, but at Sharp's insistence agreed to pledge stock at a bank in order to obtain the funds. Sharp induced Dixon to do this by offering a $700 bonus. Dixon and his wife suggested that they and Sharp obtain legal advice, but Sharp said that would be unnecessary. When Sharp failed to repay the $10,000, or the $700 bonus, the Dixons instituted suit for the note's face value. Sharp counter-

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agreement may be recovered." *Id.* at 21. Prejudgment interest may be awarded in the discretion of the jury in an action for breach of an obligation not arising from contract and in every case of oppression, fraud, or malice. Cal. Civil Code § 3288 (West 1970). "[T]he granting of treble damages is discretionary with the trial court and depends upon the relative guilt of the parties . . . ." Golden State Lanes v. Fox, 232 Cal. App. 2d 135, 142, 42 Cal. Rptr. 568, 572 (1965).

18. *See* Annot., 16 A.L.R.3d 510 (1967).

19. *See infra* notes 41-52 and accompanying text.

20. *See* River Hills, Inc. v. Edwards, 190 So. 2d 415, 423 (Fla. Dist. Ct. App. 1966). North Carolina has an analogous standard, although recent case law is sparse. *See supra* note 5.

21. *See, e.g., River Hills,* 190 So. 2d at 415; Stewart v. Nangle, 103 So. 2d 649 (Fla. Dist. Ct. App. 1958); Chandler v. Kendrick, 108 Fla. 450, 146 So. 551 (1933).

22. 276 So. 2d 817 (Fla. 1973).

claimed and charged usury as an affirmative defense. The trial court held that the agreement was not usurious, but Sharp appealed. The appellate court remanded the case to the trial court, which entered judgment for Sharp. Judgment was affirmed by the appellate court.[23]

The Florida Supreme Court reversed, holding that the Dixons lacked corrupt intent. "The difference between a lawful transaction and usurious one," the court stated, "is *the difference between 'good faith' and 'bad faith.'*"[24] The purpose of usury statutes is "to bind the power of creditors over necessitous debtors and prevent them from extorting harsh and undue terms in the making of loans."[25] Therefore, only lenders acting in bad faith fall within the statute's scope. "To work a forfeiture under the statute the principal must knowingly and willfully charge or accept more than the amount of interest prohibited."[26]

Had Florida's definition of intent been applied in either *Ford Motor* or *Parkway,* different results would have been reached because neither the Ford clerk nor Allan acted in bad faith.

IV. Analysis of the Intent Requirement

A. *Inadequacy of Arguments Supporting the Objective Intent Requirement*

Two reasons have been proffered for applying an objective intent requirement. The first reason is that the law should not encourage ignorance, and ignorance of the law should not be a defense. "Ignorance of the law is generally no excuse in usury cases, and where a transaction unmistakably a loan is made for a rate of interest exceeding that permitted by law, it seems that logically the transaction would necessarily be usurious."[27] The *Dixon* dissent argued that "[a]ll citizens are presumed to know the law. . . . Ignorance of the law is no excuse for . . . misconduct."[28] The second reason is that the objective test "saves the usury plaintiff from an almost impossible burden [of proof]."[29]

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23. *Id.* at 818-19.

24. *Id.* at 821 (quoting *River Hills,* 190 So. 2d at 423) (emphasis in original).

25. *Id.* at 820 (quoting *Chandler,* 108 Fla. at 452, 146 So. at 552).

26. *Id.* at 820 (citations omitted).

27. 14 S. Williston, A Treatise on the Law of Contracts § 1698 (W. Jaeger 3d ed. 1972) (footnotes omitted).

28. *Dixon,* 276 So. 2d at 823 (Boyd, J., dissenting).

29. M. Leymaster, Consumer Usury and Credit Overcharges 18 (Supp. 1984).

1. Should ignorance be an excuse?

The doctrine that all citizens are presumed to know the law is indefensible in the context of usury. Never easily understood, usury laws have changed so rapidly within the past ten years that lawyers or experienced bankers can no longer safely be presumed to know the law. State statutes have created diverse usury exemptions,[30] federal law now preempts state law on many loans,[31] several states have eliminated usury ceilings altogether,[32] and other states have adopted floating usury rates requiring the lender to monitor an economic indicator to determine the legal rate of interest.[33] While all citizens may he expected to know speed limits or rules applicable to gun registration, it is absurd to expect or presume that every widow with extra cash will know current usury rates. Since loaning money is not inherently wrong, many people are unaware of usury laws altogether.

Furthermore, the purpose of usury laws implies that a person ignorant of the law should not be charged with usury. In California the purpose is "to penalize sharp operators taking advantage of unwary and necessitous horrowers."[34] In Illinois the purpose is "to protect the necessitous borrower from the unscru-

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30. For example, California exempts savings and loan associations, credit unions, pawn brokers, real estate brokers, and agricultural corporations, among others, from any restrictions. CAL. CONST. Art. XV § 1 (West Supp. 1985). New York, like many states, bars corporations from interposing the defense of usury, N.Y. GEN. OBLIG. LAW § 5-521 (McKinney 1978), and exempts all loans or forbearances in the amount of $250,000 or more, except those secured primarily by a one- or two-family residence. N.Y. GEN. OBLIG. LAW § 5-501 (McKinney Supp. 1984). An exhaustive list of distinct state exemptions is too vast to state here.

31. The Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stet. 132, *as amended by* Housing and Community Development Act of 1980, Pub. L. No. 96-399, § 324, 94 Stat. 1614, 1647-648, preempts state law on loans secured by first liens on residential real property, first liens on stock in residential cooperative housing corporations, or first liens on residential manufactured homes if the loans are made by certain types of financial institutions or by an individual financing the sale of his principal residence. Stete laws limiting interest rates paid on deposits are preempted, as are etate laws on business and agricultural loans of more than $1,000. Other transactions come under federal law as well. For a general discussion of federal preemption, see PRACTISING LAW INSTITUTE, USURY LAWS 257-72 (1982).

32. *See supra* note 4.

33. The number of states that use a floating usury rate is growing rapidly. These states include Alabama, Montana, New York, North Dakota, Rhode Island, Texas, and Washington. *See* 1 CONSUMER CRED. GUIDE (CCH) ¶ 510 (1985). Generally, a floating usury rate is pegged a few percentage points above an interest rate indicator such as the Federal Reserve Bank's discount rate, the commercial bank prime rate, or long-term government bond rates.

34. White v. Seitzman, 230 Cal. App. 2d 756, 761, 41 Cal. Rptr. 359, 362 (1964).

pulous lender."[35] Most other states have expressed similar purposes.[36] Therefore, since the "sharp operator" and "unscrupulous lender" are the targets of usury laws, and not the honest clerk or widow, good faith should be a defense. A standard of intent based upon good faith would catch sharp operators while disregarding those whom usury laws are not designed to catch.

2. *The burden of proof*

The argument that proving bad faith would be almost impossible has been mentioned infrequently.[37] It should not be a pressing concern because the borrower who has to prove usury is usually in an excellent position to testify about the lender's intent. The borrower could testify as to his necessitous situation, and he would know whether the lender's bargaining position had been inflexible and harsh, instead of accommodating.

Few courts, if any, have expressed much concern with burdens of proof. A legislature or court concerned with this problem could solve it by creating a presumption of bad faith upon a showing of usury. The lender then would have the opportunity to rebut that presumption by presenting evidence of his good faith. Shifting the burden of proof to the lender would mitigate the borrower's obstacle of proving bad faith.

B. Proper Construction of Usury Statutes

The most important argument in support of altering the intent requirement is that usury laws are penal and should be strictly construed.[38] *Ford Motor* and *Parkway* intolerably impose penalties for acts that legislatures did not intend to forbid. Courts "must give the [usury] statute a reasonable construction that comports with the underlying legislative intent."[39] Legislative intent is not to void every transaction violating maximum interest rates, as demonstrated by numerous usury exemptions.[40]

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35. Cohn v. Receivables Fin. Co., 123 Ill. App. 2d 224, 228, 260 N.E.2d 67, 69 (1970).

36. *See* 47 C.J.S. *Interest & Usury* § 88 (1982).

37. The author found no cases analyzing this issue. The source of this argument, therefore, is M. LEYMASTER, *supra* note 29.

38. Dobie v. Livengood, 12 Ill. App. 2d 343, 351, 139 N.E.2d 599, 603 (1957) ("Because the defense of usurious interest is in the nature of a penal action, the usury must be proved by a clear preponderance of the evidence.").

39. Alamo Lumber Co. v. Gold, 661 S.W.2d 926, 930 (Tex. 1983) (Barrow, J., dissenting) (citation omitted).

40. *See supra* note 30.

Given the penal nature of usury, the objective requirement of intent is a shortcut to proof that ought not be allowed.

Since the legislative purpose of usury is to guard against sharp operators, usury's intent requirement should be construed so that it applies only to such people and not to good faith lenders. Because objective intent requirements can lead to harsh results, and because a lesser intent requirement would satisfy usury objectives, the intent requirement should be changed.

V. The Doctrine of Estoppel

To prevent some injustices resulting from usury's harsh intent requirement, most jurisdictions hold that a borrower's initiation of, or fraud contributing to, a usurious transaction estops the borrower from claiming the usury defense.[41] The reason for this view is that granting a usury defense permits the borrower to take advantage of his own wrong.[42]

The doctrine of estoppel mitigates the harsh intent requirement in some situations, but as *Ford Motor* and *Parkway* demonstrate, estoppel does not apply in all situations needing correction. Indeed, most cases invoking estoppel involve a fiduciary relationship between the lender or borrower, or a situation in which the borrower knew the transaction was usurious and therefore committed fraud on the lender.[43]

Use of estoppel frequently leads to good results and prevents much injustice.[44] However, the doctrine is inappropriate in the context of usury. First, it bars usury actions that should he permitted; second, it fails to prevent usury actions that should be barred, as in *Ford Motor* and *Parkway*.

By focusing almost entirely on the borrower's acts and intentions rather than the lender's, the doctrine of estoppel fails to recognize that the purpose of usury laws is to protect necessitous borrowers from unscrupulous lenders or sharp operators.[45] Borrowers almost always initiate loan transactions.[46] In particular,

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41. Annot., *supra* note 18, at 512-13.

42. *Id.* at 513-14.

43. *See generally* Liebergesell v. Evans, 23 Wash. App. 357, 363, 597 P.2d 908, 912 (1979), *rev'd on other grounds*, 93 Wash. 2d 881, 613 P.2d 1170 (1980).

44. *See, e.g.*, Buck v. Dahlgren, 23 Cal. App. 3d 779, 100 Cal. Rptr. 462 (1972); Holt v. Rickett, 143 Ga. App. 337, 238 S.E.2d 706 (1977); Liebergesell v. Evans, 93 Wash. 2d 881, 613 P.2d 1170 (1980).

45. *See supra* notes 34-36 and accompanying text.

46. Annot., *supra* note 18, at 512 ("[T]he first step leading to the making of a loan is usually taken by the borrower . . . .").

borrowers in financial trouble are especially "necessitous" and are the borrowers most likely to insert the usurious element into a transaction since a borrower willing to pay usurious interest rates probably could not obtain credit at prevailing legal rates of interest. As one court said, "[t]he usury rule . . . is made for the beneficial purpose of protecting the necessitous debtor against extortion which he is *practically helpless to resist.*"[47]

Estoppel, therefore, which bars usury actions by borrowers who insert usury into a transaction, serves to thwart the purpose of usury laws. Since necessitous borrowers are willing to borrow at any cost, estoppel keeps them from resorting to usury laws for their defense. For that reason, the key factor should not be whether the borrower initiated the usurious transaction or whether the borrower knew that the transaction was usurious, but whether the lender acted unscrupulously in accepting the borrower's offer. Courts should focus on the lender's knowledge or bad faith, not the borrower's actions. By examining the lender's intent, the purpose of usury laws can be satisfied and protected.

Rogus v. Continental Illinois National Bank & Trust Co.[48] is illustrative. Rogus, the lender, was introduced to David Shandling, the borrower, through a mutual friend. Shandling wished to borrow $18,000 in order to participate in two business deals. Shandling sought out the lender and offered to pay a full year's interest for a three-month loan. Shandling later died and was represented by his executor, Continental. When Rogus attempted to enforce his note, Continental alleged usury. However, the Illinois appellate court ruled that Continental was estopped from claiming usury since Shandling had initiated the transaction. "[A] horrower who initiates a usurious transaction is estopped from setting up the defense of usury. . . . [T]he decedent voluntarily offered to pay a year's interest on a three month loan. It was he who initiated the terms, and not the lender."[49]

The court completely ignored any knowledge or intent that Rogus, the lender, may have had. It can be inferred, although it is not expressly stated, that Rogus had some experience with fi-

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47. Howes v. Curtis, 104 Idaho 563, 566, 661 P.2d 729, 732 (1983) (quoting Freedman v. Hendershott, 77 Idaho 213, 219, 290 P.2d 738, 741 (1955)) (emphasis added).

48. 4 Ill. App. 3d 557, 281 N.E.2d 346 (1972).

49. *Id.* at 560, 281 N.E.2d at 348 (citation omitted).

nancial matters.[50] Furthermore, Rogus arguably was unscrupulous simply because he so readily agreed to accept a full year's interest on a three-month loan. Since necessitous borrowers like Shandling often seek out loans, the *Rogus* fact pattern is very close to the situation contemplated by states enacting usury laws. Thus, the court should have examined Rogus' intent. *Rogus* illustrates why estoppel is inappropriate for many usury cases.

In some states a much higher standard must be met before a borrower is estopped from claiming usury. In Washington the lender must reasonably have relied on the borrower's greater knowledge.[51] In California the borrower must actually work a fraud before he is estopped.[52] As demonstrated earlier, however, this standard is also inappropriate because it goes too far in the other direction. When the borrower is required to have knowledge that the loan is usurious, fact patterns develop similar to those in *Ford Motor* and *Parkway* in which transactions were held to be usurious even though the lender acted in good faith. Hence, the court should look exclusively to the lender's intent and ignore the borrower's intent.

VI. The Proper Level of Intent

Usury should apply only to unscrupulous lenders or sharp

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50. Rogus and decedent did not know each other. When they met, on July 29, 1969, at the company's personnel office, Grant introduced decedent to Rogus stating, 'This is . . . the fellow who wants to borrow the money. . . . You work out the deal with him now.' The decedent said he would pay a full year's interest at 7% for a few months' use of the money. He brought with him a judgment note signed by him in the amount of $18,000 dated July 29, 1969, with interest at 7% after maturity, and two post-dated checks, one in the sum of $15,000 and one in the sum of $3,000, which represented payment of the note. . . . Then Rogus called in Michael Rosinia, Vice President of Personnel for Blackstone, who brought in $18,000 in cash. . . . Rogus gave the decedent $18,000 in cash . . . .

Id. at 559, 281 N.E.2d at 347-48.

51. *See* Liebergesell v. Evans, 93 Wash. 2d 881, 613 P.2d 1170 (1980) (estoppel appropriate when the lender properly and reasonably relied on the knowledge and experience of the borrower).

52. [E]stoppel does not arise simply because the borrower knew of the usurious nature of the transaction, took the initiative in seeking the loan and paid usurious interest without protest. However, in the present case the borrower . . . went one important step further. He devised the means whereby the fraud on the statute was accomplished.

White v. Seitzman, 230 Cal. App. 2d 756, 762, 41 Cal. Rptr. 359, 363 (1964); *see also* Buck v. Dahlgren, 23 Cal. App. 3d 779, 788, 100 Cal. Rptr. 462, 468 (1972).

operators, not to good faith lenders. The court should inquire whether the lender acted in good faith. This subjective standard allows the jury ample latitude to examine all facts and circumstances of a transaction and then to decide whether usury objectives would be satisfied. The jury would examine the transaction's purpose and its effects upon the parties. The good faith standard allows for excusable neglect, as in *Ford Motor*, and for transactions advantageous to the borrower, as in *Parkway*.

The effect of a good faith standard on institutional lenders does present special problems. Institutional lenders are aware of usury laws and have resources to investigate whether a transaction is usurious. Therefore a higher standard of good faith should apply to institutional lenders. *Ford Motor* is illustrative. If the contract had initially been usurious, Ford Motor Credit Company should have been liable because it should know the usury laws. Only the very unique circumstances of the case elevated Ford's intent to "good faith." Whether an institutional lender acted in good faith would be a jury question only when such unique circumstances are present.

Furthermore, an institutional lender is arguably not acting in bad faith when it charges usurious interest to a horrower who is a bad credit risk. While this argument has appeal, it effectively emasculates the usury laws. If a borrower is a good credit risk, he can obtain credit at prevailing nonusurious rates. An institutional lender has incentive to charge a usurious interest rate only when the borrower is a poor risk. If such a transaction were immune from usury laws, then the laws would be effectively meaningless. If a state finds this result desirable, it should eliminate its usury laws instead of adopting a good faith defense.

It is to society's advantage to limit restrictions on available credit.[53] A good faith defense to a usury charge fosters transactions that are beneficial while discouraging those that are not. Economic arguments against interest rate restrictions are legion.[54] Usury prohibitions do not fulfill an economic purpose but

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53. Usury laws are generally disliked by economic theorists. Paternalistic in nature, usury laws put restrictions on credit that keep borrowers and lenders apart; hence, they restrict savings and investment. Jeremy Bentham first articulated the economic rationale against usury in the late 1700's. Bentham, *Defence of Usury*, in 3 THE WORKS OF JEREMY BENTHAM (1962). For economic arguments against usury, see, *e.g.*, Boyes & Roberts, *Economic Effects of Usury Laws in Arizona*, 1981 ARIZ. ST. L.J. 35; Crafton, *supra* note 2; Ostas, *Effects of Usury Ceilings in the Mortgage Market*, 31 J. FIN. 821 (1976); Note, *supra* note 2.

54. *See supra* note 53.

instead fulfill a social purpose that took root in Old Testament times.[55] At a minimum, a good faith agreement found to be usurious should not be void. Rather, remedies should be limited to the return of usurious interest paid.

VII. Conclusion

The current objective requirement of usurious intent too frequently leads to harsb results. The doctrine of estoppel, while at times effective in mitigating harsh results, is imperfect, too concerned with the borrower's intent, and fails to bar all inequitable results. Objectives of usury laws can be satisfied by granting a good faith defense to usury charges. A good faith standard fosters transactions that benefit borrowers, lenders, and society. It also prohibits transactions that society finds objectionable. Finally, the good faith standard effectively limits usury's scope to those transactions in which weak and necessitous borrowers are at the mercy of unscrupulous lenders, thereby fulfilling legislative objectives.

Todd F. Maynes

55. Long, *Trends in Usury Legislation—Current Interest Overdue*, 34 U. Miami L. Rev. 325, 325-27 (1980); *Ezekiel* 18:13 (King James) ("Hath given forth upon usury, and hath taken increase: shall he then live? he shall not live: he hath done all these abominations; he shall surely die; his blood shall he upon him.").