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Texas Supreme Court Issues New Interpretation of Texas Usury Law

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On May 23, the Texas Supreme Court issued an opinion holding that in determining whether a commercial loan is usurious under Texas state law, the “actuarial method” must be employed. This requires the applicable amount of interest to be calculated using the loan’s declining principal balance on a monthly basis, rather than always using the original principal balance of the loan. This decision was in response to a question posed to the 5th Circuit Court of Appeals regarding a dispute over usurious interest charges.

Prior to 1997, there had been no reference to the actuarial method in the Texas usury statute, but the law was amended in 1997 to require use of the actuarial method in determining the amount of interest that could be assessed without violating the law. The Texas Supreme Court also pointed out that a loan is not deemed usurious when the interest exceeds the maximum amount allowed by law (28 percent per year for commercial loans in Texas), but instead when the loan’s interest is spread out over the contract’s entire term. This would allocate the total interest provided for a loan agreement over the loan’s full term. In this case, the difference between the permissible interest using the interpretation urged by the defendant lender over the life of the loan and the interpretation urged by the plaintiff borrower (ultimately accepted by the court) was over $100,000.

Putting It Into Practice: Commercial lenders in Texas should follow the statute and use the actuarial method to calculate the amount of interest the lender is permitted to collect over the life of the loan without the loan being deemed usurious. While the actuarial method is not defined in the Texas Finance Code, it does have a common definition provided by the Texas Banking Department and in the federal Truth in Lending Act, as well as by Black’s Law Dictionary.

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