1676.

FINANCE COMPANY—LOANING MONEY—PROFITSHARING CERTIFICATES—LICENSE UNDER SECTION 6346-1, GENERAL CODE, WHEN.

SYLLABUS:

A finance company engaged in the business of loaning money, which requires as a consideration for such loan that the borrower purchase certain profit sharing certificates at a stipulated price, is required to obtain a license under the provisions of Section 6346-1, General Code, where such finance company may benefit to the extent of the price paid for such certificates, which price, when added to the interest already paid by the borrower for the loan, would exceed eight per centum per annum.

COLUMBUS, OHIO, December 23, 1937.

HON. DAN T. MOORE, *Chief, Division of Securities, Columbus, Ohio.*

DEAR SIR: This will acknowledge receipt of your letter of recent date requesting my opinion as to the applicability of the provisions of Sections 6346-1, et seq., General Code, to a finance company which has adopted a certain plan in connection with its loan transactions. The plan briefly is as follows:

The finance company engaged in the business of making loans, as a part of the loan transaction, requires the borrower to purchase a book of profit sharing certificates at a stipulated price which is less than the face value of such certificates. The face value of the certificates and the cost price thereof vary with the amount of the loan. The purchase of such profit sharing certificates is evidenced by a written instrument wherein provision is made for the cash redemption of such certificates at the cost price thereof with interest at the rate of 6% per annum. The redemption privilege is limited to the unused profit sharing certificates issued in connection with the last loan transaction by and between the original purchaser of such certificates and the finance company. The original purchaser of a subsequent holder of the profit sharing certificates may use such certificates as 15% of the retail purchase price of produce, meats, general grocery merchandise, and other related articles sold at a store owned and operated by the finance company. The merchandise sold in this store is at prices comparable to prevailing competitive prices of merchandise of the same character and quality. The loan transaction is evidenced by a note, the principal amount of which is determined by adding the cost of the profit sharing certificates and the net amount of

cash received by the borrower. Such notes bear interest at the rate of one-half of one per cent per month on the unpaid balance.

The question presented in your letter is whether or not the sale of the profit sharing certificates in connection with a loan transaction constitutes a charge for the loan within the purview of Sections 6346-1, et seq., General Code, which charge shall be considered along with the rate of interest in determining whether or not the total charges exceed 8% per annum, thus requiring a license as provided in the above mentioned sections.

Section 6346-1, General Code, provides as follows:

> "It shall be unlawful for any person, firm, partnership, association or corporation, to engage, or continue, in the business of making loans, on plain, endorsed, or guaranteed notes, or due-bills, or otherwise, or upon the mortgage or pledge of chattels or personal property of any kind, or of purchasing or making loans on salaries or wage earnings, or of furnishing guarantee or security in connection with any loan or purchase, as aforesaid, at a charge or rate of interest in excess of eight per centum per annum, including all charges, without first having obtained a license so to do from the commissioner of securities and otherwise complying with the provisions of this chapter."

There are numerous conflicting authorities on the question as to whether or not a contract is usurious when a company loaning money to a borrower compels such borrower in connection with the loan to enter into some collateral agreement to purchase merchandise of the lender. The willingness of a borrower to concede to demands made of him in order to obtain temporary relief from financial embarrassment has resulted in many devices to evade the usury laws. The courts in such cases have been compelled to look beyond the form of the transaction and have laid down as a universal rule that the mere form is immaterial but that it is the substance which must be considered. 40 O. Jur. 833. It seems that the test applied by the courts in order to determine whether or not a contract similar to the one outlined in your letter is usurious, is the price paid by the borrower for the lender's property. If the price for such property is exorbitant, the contract is usurious; otherwise, it is not. In 40 O. Jur. 849, the following text appears with numerous authorities cited:

> "There is a conflict of authority on the question whether a lender, as a condition of the loan, may stipulate for some collateral advantage additional to the legal rate of interest, as, for

> instance, that the borrower should secure the payment of a debt due the lender from a third person. In some jurisdictions the question is answered in the affirmative, and it is held in Ohio, as well as generally, that the circumstance that the lender refused to make the loan unless the borrower would enter into another contract, which, apart from and unconnected with the lending, would be fair and legal, does not render the agreement for the loan usurious. But the rule is universal that the courts will not hesitate to declare usurious a contract for a loan at legal interest which secures to the lender a collateral advantage, where the stipulation is made purely to evade the laws against usury, as where the borrower is required to buy a piece of land from the lender at an exorbitant price, or to give a note to secure a loan of gold at a higher rate than the market price, in addition to legal interest."

The Supreme Court in *Life Insurance Co.* vs. *Hilliard,* 63 O. S. 478, has recognized the principle that where a borrower in order to make a loan must enter into a collateral contract to purchase the lender's property at an exorbitant price resulting in the lender receiving more than the legal rate of interest, the contract may be usurious. The court said at page 494:

> "Decisions are not lacking, and many are cited, to the effect that where the borrower is induced to make with the lender some unusual and unfair additional contract, as to buy a piece of land from the lender at an exorbitant price, or give a note to secure a loan of gold at a higher rate than the market value in addition to legal interest, the contract will be held usurious."

However, in this case the court concluded that a contract entered into by and between a life insurance company and a borrower of money whereby as a condition precedent to making the loan the borrower was required to take out a policy with the company, was not usurious by reason of the fact that the policy was actually issued at the same rate and on the same conditions as policies issued to non-borrowers. The transaction, no doubt, would have been declared to be usurious if the premium paid for the policy were exorbitant.

It might be contended that under the holding of the Supreme Court in the case of *Life Insurance Co.* vs. *Hilliard,* supra, the transaction under consideration would not be usurious for the reason that the price charged by the finance company for the profit sharing certificates is not exorbitant. However, a careful analysis of the entire contract involved in this

opinion reveals certain provisions which distinguish the transaction under consideration from the one considered by the court in the Hilliard case. While it is true that a borrower may redeem the profit sharing certificates within one year at the cost price thereof with interest at the rate of 6% per annum, yet this privilege of redemption is limited to the unused profit sharing certificates issued in connection with the last loan transaction. It is conceivable that a person may borrow from the finance company several times during the course of a year. In such an event, the borrower forfeits under the contract the right to redeem all profit sharing certificates purchased by him in connection with the loan transaction with the exception of those profit sharing certificates acquired by him in the last transaction. It is conceivable also that a borrower may not exercise the privilege of redemption of the certificates or that such certificates may be misplaced or lost by the borrower. In such events, the finance company would benefit to the extent of the price paid by the borrower for the profit sharing certificates, which price, when added to the interest already paid by the borrower for the loan, would exceed 8% per annum. In view of the above, it would seem that the transaction is a device to evade the usury laws.

In Opinions of the Attorney General for 1930, Vol. III, page 1948, a similar question was considered. The then Attorney General held as set forth in the syllabus:

> "When a jewelry store is engaged in the business of selling jewelry and loaning money, and the consideration for making loans is two fold, first, that the borrower pay interest at the rate of eight per centum per annum, and, second, that the borrower purchase jewelry from the lender, such jewelry store should comply with the provisions of the Chattel Loan Act, as contained in Sections 6346-1, et seq., General Code."

The facts under consideration in the above mentioned opinion indicated that the profit on the sale of the jewelry was from 300 to 600%. Thus, the conclusion reached in that opinion is in accord with the reasoning of the Supreme Court of Ohio in the case of *Life Insurance Co.* vs. *Hilliard,* supra. The Attorney General, however, in the foregoing opinion went one step further and concluded that even though the price charged by the jewelry company for its merchandise was not exorbitant, the transaction would be usurious if it were a device on the part of the jewelry company to evade the usury laws. Thus, at page 1951 of the above mentioned opinion appears the following language:

> "It is my opinion, however, that in the event a customer of a jewelry store should make a bona fide loan from such store

at a rate of interest not exceeding 8% per annum, including any charges connected with such loan, such interest is not usurious providing the purchase of jewelry is not part of the consideration for the loan. If, however, such jewelry store in connection with its business of loaning money requires, as part of the consideration for making a loan, that the borrower purchase an article of jewelry from such store at an exorbitant price in addition to requiring the borrower to pay interest on the loan at the rate of 8% per annum, undoubtedly such a transaction is usurious in the absence of compliance with the provisions of the Chattel Loan Act. Even under such circumstances if the article of jewelry which the borrower is compelled to purchase in order to obtain temporary relief from financial embarrassment and pressure, is sold at the usual market price for such an article, I am inclined to the view that such a transaction may very properly be held to be nothing more nor less than a device on the part of the lender to evade the usury laws."

In view of the above, it is my opinion that a finance company engaged in the business of loaning money, which requires as a consideration for such loan that the borrower purchase certain profit sharing certificates at a stipulated price, is required to obtain a license under the provisions of Section 6346-1, General Code, where such finance company may benefit to the extent of the price paid for such certificates, which price, when added to the interest already paid by the borrower for the loan, would exceed eight per centum per annum.

Respectfully,

HERBERT S. DUFFY,

Attorney General.

1677.

APPROVAL—LEASE OF RESERVOIR LAND TO CHARLES BRISTON OF COLUMBUS, OHIO, EXECUTED BY THE STATE OF OHIO THROUGH THE CONSERVATION COMMISSIONER.

COLUMBUS, OHIO, December 23, 1937.

HON. L. WOODDELL, *Conservation Commissioner, Columbus, Ohio.*

DEAR SIR: I am in receipt of your letter of recent date, submitting for my examination and approval a certain reservoir land lease in trip-