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Interest Rates Allowable

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5

Interest Rates Allowable

Ballot Title

INTEREST RATES ALLOWABLE. LEGISLATIVE CONSTITUTIONAL AMENDMENT. Except as to specified exempt lenders, such as banks, credit unions and savings and loan associations, the Constitution permits interest charges of no more than 10% per annum. This amendment would retain the 10% limit on loans made primarily for personal, family or household purposes but would, as to other loans by nonexempt lenders, increase the maximum permissible rate of interest to the higher of (a) 10% or (b) 7% plus the prevailing rate currently charged by the Federal Reserve Bank of San Francisco for monies advanced to member banks. Financial impact: No fiscal effect on state or local government.

FINAL VOTE CAST BY LEGISLATURE ON SCA 40 (PROPOSITION 5)

Assembly—Ayes, 55
Noes, 11

Senate—Ayes, 28
Noes, 5

Analysis by Legislative Analyst

PROPOSAL:

Every lender of money, unless specifically exempted by the Constitution, is prohibited from charging interest of more than 10 percent per year on any loan. Savings and loan associations, state and national banks, industrial loan companies, credit unions, pawnbrokers, personal property brokers and agricultural cooperatives are specifically exempted from the above provision.

This proposition provides that the 10 percent per year interest limitation on nonexempt lenders, such as individuals, insurance companies and mortgage banks,

only applies to loans for personal, family, or household purposes. On other loans these nonexempt lenders would be permitted to charge an interest rate that is the higher of (1) 10 percent per year or (2) seven percent plus the prevailing rate charged to member banks for monies advanced by the Federal Reserve Bank of San Francisco. In June 1976, the Federal Reserve rate was 5½ percent, which added to the seven percent, would total 12½ percent.

FISCAL EFFECT:

The proposition has no fiscal effect on state or local governments.

Text of Proposed Law

This amendment proposed by Senate Constitutional Amendment 40 (Statutes of 1976, Resolution Chapter 53) expressly amends an existing section of the Constitution; therefore, existing provisions proposed to be deleted are printed in ~~strikeout type~~ and new provisions to be inserted or added are printed in *italic type* to indicate that they are new.

PROPOSED AMENDMENT TO ARTICLE XV

SECTION 1. The rate of interest upon the loan or forbearance of any money, goods or things in action, or on accounts after demand or judgment rendered in any court of the State, shall be 7 per cent per annum but it shall be competent for the parties to any loan or forbearance of any money, goods or things in action to contract in writing for a rate of interest :

(1) *For any loan or forbearance of any money, goods or things in action, if the money, goods or things in action are for use primarily for personal, family or household purposes, at a rate not exceeding 10 percent per annum, or*

(2) *For any loan or forbearance of any money, goods or things in action for any use other than specified in paragraph (1), at a rate not exceeding the higher of (a) 0 percent per annum or (b) 7 percent per annum plus the rate prevailing on the 25th day of the month preceding the earlier of (i) the date of execution of the contract to make the loan or forbearance, or (ii) the date of making the loan or forbearance established by the Federal Reserve Bank of San Francisco on advances to member banks under Sections 13 and 13a of the Federal Reserve Act as now in effect or hereafter from time to time amended (or if there is no such single determinable rate for advances, the closest counterpart of such rate as shall be designated by the Superintendent of Banks of the State of California unless some other person or agency is delegated such authority by the Legislature) not exceeding 10 per cent per annum .*

No person, association, copartnership or corporation shall by charging any fee, bonus, commission, discount or other compensation receive from a borrower more than ~~10 per cent~~ *the amount of interest per annum allowed by this section* upon any loan or forbearance of any money, goods or things in action.

However, none of the above restrictions shall apply to any building and loan association as defined in and

which is operated under that certain act known as the "Building and Loan Association Act," approved May 5, 1931, as amended, or to any corporation incorporated in the manner prescribed in and operating under that certain act entitled "An act defining industrial loan companies, providing for their incorporation, powers and supervision," approved May 18, 1917, as amended, or any corporation incorporated in the manner prescribed in and operating under that certain act entitled "An act defining credit unions, providing for their incorporation, powers, management and supervision," approved March 31, 1927, as amended or any duly licensed pawnbroker or personal property broker, or any bank as defined in and operating under that certain act known as the "Bank Act," approved March 1, 1909, as amended, or any bank created and operating under and pursuant to any laws of this State or of the United States of America or any nonprofit cooperative association organized under Chapter 1 (commencing with Section 54001) of Division 20 of the Food and Agricultural Code in loaning or advancing money in connection with any activity mentioned in said title or any corporation, association, syndicate, joint stock company, or partnership engaged exclusively in the business of marketing agricultural, horticultural, viticultural, dairy, live stock, poultry and bee products on a cooperative nonprofit basis in loaning or advancing money to the members thereof or in connection with any such business or any corporation securing money or credit from any Federal intermediate credit bank, organized and existing pursuant to the provisions of an act of Congress entitled "Agricultural Credits Act of 1923," as amended in loaning or advancing credit so secured, nor shall any such charge of any said exempted classes of persons be considered in any action or for any purpose as increasing or affecting or as connected with the rate of interest hereinbefore fixed. The Legislature may from time to time prescribe the maximum rate per annum of, or provide for the supervision, or the filing of a schedule of, or in any manner fix, regulate or limit, the fees, bonus, commissions, discounts or other compensation which all or any of the said exempted classes of persons may charge or receive from a borrower in connection with any loan or forbearance of any money, goods or things in action.

The provisions of this section shall supersede all provisions of this Constitution and laws enacted thereunder in conflict therewith.

Argument in Favor of Proposition 5

Proposition 5 is vitally needed to help ensure a healthy state economy, able to meet the needs of California's citizens.

Proposition 5 will better enable businesses in our state to borrow funds for normal growth and expansion by reforming the present outdated and unrealistic 42 year old limitation on business loan interest rates.

While Proposition 5 reforms the rate of interest on business loans, it is carefully written so that it cannot affect existing interest rate laws now protecting consumers. That is why Proposition 5 was not opposed by any consumer groups when the Legislature held public hearings on the measure.

This Constitutional Amendment is supported by labor organizations, chambers of commerce, civic and community organizations, ethnic minorities and consumer-minded citizens . . . all of whom want a healthy growing economy in California.

Proposition 5 will place a more realistic limitation on the interest rate that can be charged on funds borrowed by business firms in California. The present limitation, which is the lowest in the nation, has had the unintended and undesirable effect of handcuffing business' ability to finance expansion and generate new jobs.

At present, under the outdated provision in the State Constitution, the highest interest rate that can be charged on money borrowed by business firms in California is 10 percent. Unfortunately, during periods of high inflation, certain lenders can receive a better return for their money by investing it in businesses in other states, where rate limitations have been reformed

and updated. The consequence is that California investment funds flow to other states, thereby depriving California business of the funds needed to create jobs and build new plants and equipment.

According to recent studies, the existing interest rate limitation on business loans has cost California hundreds of millions of dollars over the past two years. Or, viewed another way, it has cost California some 20,000 new jobs.

The new business loan interest rate proposed by this Proposition will be limited to the existing legal ceiling of 10 percent, except that in very inflationary periods the limit will be 7 percent, plus the prevailing interest rate charged banks that now borrow money from the Federal Reserve Bank of San Francisco.

In other words, a YES vote on Proposition 5 will establish a flexible, realistic interest rate limitation on business loans.

It will not, directly or indirectly, raise the rate of interest allowed on consumer loans.

A YES vote makes good economic sense—and good common sense.

LEO T. McCARTHY

Speaker of the Assembly, 18th District

HOUSTON I. FLOURNOY

Dean, Center for Public Affairs, University of Southern California

JAMES S. LEE

President, State Building and Construction Trades Council of California

Rebuttal to Argument in Favor of Proposition 5

In 1934 the California Constitution was changed giving Californians greater protection against usury. The same tight economy that prompted these safeguards then exists today. These safeguards are for your protection and should NOT be removed.

First, Proposition 5 will hurt the consumer loan market. Not only will this measure virtually dry up the consumer loan market by funneling available money to big business, it can also increase the cost of some consumer loans by boosting interest rates above the current 10% maximum. Under this measure, loans used partially, but not primarily, for household, personal or family needs could carry interest rates of 15 or 16 percent!

Second, Proposition 5 was sponsored initially by utility companies. They wanted more money available to them and were willing to pay higher interest rates to get it. If it costs public utilities and other businesses more money to borrow money they will pass their increased costs on to you. Expect higher utility bills and prices if Proposition 5 passes.

Finally, jobs are created and sustained by public demand for goods and services. If products and services become so expensive we cannot afford them, the demand for goods and services decreases. If fewer goods and services are bought, fewer people are required to produce and maintain them. This will eliminate thousands of jobs.

In 1974 and again in June, 1976 California voters rejected measures similar to Proposition 5. We again ask that you protect yourself, your pocketbook and your job. Vote NO on Proposition 5.

BOB WILSON

*Member of the Assembly, 77th District
Chairman, Committee on Governmental Organization*

JOHN J. MILLER

*Member of the Assembly, 13th District
Chairman, Committee on Judiciary*

OMER L. RAINS

*Member of the Senate, 18th District
Chairman, Committee on Elections and Reapportionment*

Argument Against Proposition 5

In the June, 1976 Primary Election, more than 56 percent of California voters rejected an effort to increase interest rates by changing a portion of the California Constitution that has protected the voters for more than 40 years. The voters in June clearly said **NO** to Proposition 12 which is identical to this proposition. We again ask that you vote **NO**.

Proposition 5 would boost interest rates on certain loans above the current 10 percent maximum. The maximum under this measure would be flexible depending on prevailing interest rates. If this measure had been law in August, 1974 the interest rate would have been 15 percent!

We are in a time of tight money. If higher interest rates can be charged on loans to businesses and corporations than can be charged to consumers, more money will be loaned to corporations. This will siphon money from the consumer loan market virtually drying it up. Proposition 5 would have a disastrous effect on the consumer loan market.

Also, contrary to what supporters of this proposition would have you believe, consumer loans could be

affected by these higher interest rates. Only loans used "primarily" for household, family or personal needs would be exempt. If you borrow money and 49 percent of it is used for household needs, but 51 percent is for some other purpose, you could be hit with interest rates as high as 15 or 16 percent.

Proposition 5 clearly means higher costs, tighter money and a weakening of California's usury laws. Twice before California voters have rejected a similar proposal. California voters should again say **NO** to higher interest rates. Vote **NO** on Proposition 5.

BOB WILSON

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Rebuttal to Argument Against Proposition 5

Despite misleading arguments to the contrary, Proposition 5 was written to accomplish one vitally necessary purpose: To enable California businesses, small and large, to borrow money for plant and equipment expansion from out-of-state banks, insurance companies, mortgage companies, and pension trusts at competitive, nationally-set interest rates during periods of high inflation.

Opponents say Proposition 5 would mean higher costs and higher interest rates for consumers and would dry up the consumer loan market. This is untrue. Proposition 5 does not raise or lower interest rates now charged by California banks, savings and loans, retailers, and consumer loan companies.

Proposition 5 applies only to interest rates charged on business loans. The measure clearly states, "for non-personal . . . non-family and non-household purposes." Proposition 5 will have no effect on interest rates now paid by consumers and home owners. It will not mean higher consumer interest rates.

Proposition 5 is needed because the existing,

outdated ceiling on business loan interest rates has cost California hundreds of millions of dollars and 20,000 new jobs over the past two years. In fact, Proposition 5 will mean needed business projects are not canceled or built later at a higher cost to consumers.

Proposition 5 simply places California on a more equal, competitive footing with neighboring states.

Passage of Proposition 5 will help stimulate a healthy economy and keep California investment funds at home.

We urge you to vote **YES** on Proposition 5.

LEO T. McCARTHY

Speaker of the Assembly, 18th District

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