



IRVIN D. PARKER
ADMINISTRATOR
AND
CONSUMER ADVOCATE

The State of South Carolina
Department of Consumer Affairs

2221 DEVINE STREET
P.O. BOX 5757
COLUMBIA, S.C. 29250

April 20, 1981

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Declaratory Ruling No. 2.605-8102 Isle of Palms Beach and Racquet Club Company, Inc.

ISLE OF PALMS BEACH AND RACQUET CLUB COMPANY, INC. MAKES SECURED SALES OF LOTS OTHER THAN CONSUMER CREDIT SALES WHICH MAY BE MADE AT ANY RATE CONTRACTED FOR BY THE PARTIES, INCLUDING A REASONABLE ANNUAL ADJUSTMENT TIED TO AN OUTSIDE INDEX.

In accordance with Regulation 28-24 of the Administrator of the Department of Consumer Affairs, you have petitioned for a declaratory ruling on the applicability of Consumer Protection Code Section 37-2-605 (1976) to sales of residential lots by the Isle of Palms Beach and Racquet Club Company, Inc. ("Beach and Racquet Club"). CPC §37-6-409 (1976).

The Beach and Racquet Club is a South Carolina corporation that is developing land which it owns in fee simple on the Isle of Palms. The Beach and Racquet Club sells finished residential lots to the general public as well as tracts of land for development, the latter not being pertinent to the ruling.

The Beach and Racquet Club proposes to offer lots for sale to the general public and accept for a portion of the sales price a note secured by a first lien on the property sold generally on terms and conditions stated in the petition including those with regard to the rate of interest as follows: "The interest rate to be computed at 12% per annum for the first year and at the end of the first year and thereafter the interest rate to be adjusted each year on the anniversary date of the note to the prime rate as set forth by the South Carolina National Bank; with the proviso that the rate charged may not increase or decrease more than 4% per annum." The monthly payments would be adjusted annually to reflect the increase or decrease in the interest rate.

Consumer Protection Code Section 37-2-605 (1976) provides:

With respect to a sale other than a consumer credit sale, the parties may contract for the payment by the buyer of any credit service charge.

TELEPHONES (AREA CODE 803)

ADMINISTRATION
758-3017

CONSUMER COMPLAINTS
758-2040
WATTS 1-800-922-1594

PUBLIC INFORMATION
758-7546

NOTIFICATION
758-8587

CONSUMER ADVOCACY
758-8996

Although some, and probably most, of the residential lot sales will have the elements of a consumer credit sale in subsection (1) of Consumer Protection Code Section 37-2-104 (1976), even those sales will not be consumer credit sales unless the parties subject such a sale to the Consumer Protection Code by agreement because subsection (2) of Section 37-2-104 (Cum. Supp. 1980) provides:

Unless the sale is made subject to this title by agreement (§37-2-601), "consumer credit sale" does not include...

- (b) a sale of an interest in land if the debt is primarily secured by a first lien which is a purchase money security interest in land.

It is the opinion of this Department that the Beach and Racquet Club would be making sales other than consumer credit sales when it sells residential lots in the manner and on the terms and conditions in your petition. This is assuming that these are bona fide sales and not transactions structured with the intention or purpose of defeating the usury laws. See Declaratory Ruling No. 2.605-8001 Litchfield-by-the-Sea, Inc. of January 17, 1980 headed "Litchfield-by-the-Sea, Inc. is not engaged in the business of making consumer credit transactions when it finances sales of condominiums it constructs and sells, secured by first mortgages on those condominiums, and is subject to §2.605" at page 3. A bona fide credit sale that is not a consumer credit sale is governed by Consumer Protection Code Section 37-2-605 quoted above which permits the parties to agree to any credit service charge which includes interest. See Administrative Interpretation No. 2.605-8005 of May 14, 1980 headed "Homeowner and buyer may contract for any credit service charge in connection with credit sale of residence secured by first mortgage on that residence." Not only is there no limit on the amount of credit service charge that may be contracted for by the parties in a sale other than a consumer credit sale, neither is there a limitation on the manner in which that charge may be determined or paid. Thus, Consumer Protection Code Section 37-2-605 does not prohibit variable rate credit sales and there is no other law or regulation of which we are aware that prohibits variable rate or variable payment credit sales.

South Carolina law does prohibit or limit some variable interest rate loans. For instance, Act No. 7 of 1979, as amended, extended by Act No. 6 of 1981 (R 16, H2164) until June 30, 1985, provides that some first mortgage real estate loans of \$100,000.00 or less be made at a fixed interest rate or that act will not apply. But see §2 of Act No. ___ of 1981 (R59, H2172) adding exceptions to the general rule effective April 8, 1981. Likewise, Section 34-31-90(2) (Cum. Supp. 1980) declares the public policy of South Carolina that mortgage loans of \$100,000.00 or less may not have their interest rate raised more than 1% above the initial rate over the life of the mortgage and then only if agreed to by

the borrower. But see Act No. ___ of 1981 (R59, H2172) adding exceptions to the general rule. While we have determined that Section 34-31-90(2) will apply to real estate mortgage loans made under the Consumer Protection Code [see Administrative Interpretation No. 1.108-8017 of December 19, 1980 headed "Variable rate loans are not prohibited by Consumer Protection Code but increase in rate on mortgage loans may be limited to 1% by §34-31-90(2)" and Op. Att'y Gen. No. 81-_____ of April 7, 1981 on § 34-31-90(2)], in our opinion that section does not apply to bona fide sales whether they are consumer credit or other sales, nor does Act No. 7 of 1979 apply to any bona fide sales.

Although the Beach and Racquet Club's sales are not consumer credit sales for purposes of the Consumer Protection Code generally, note that for purposes of some debtors' remedies including civil liability for violation of disclosure provisions, these transactions will be considered to be consumer credit sales. CPC §37-5-201 (Cum. Supp. 1980). Besides being subject to disclosure requirements of the Federal Truth in Lending Act and Consumer Protection Code, sellers contemplating variable rate transactions are encouraged, because of the novelty of these types of transactions involving consumers, to provide reasonable terms and conditions including variation that is tied to an index or rate outside the seller's control and that will not increase finance charges unreasonably with regard to the frequency of the increase, the maximum increase at any one time and the maximum increase over the term of the transaction. Although there are apparently no statutes or regulations directly applicable to the variable aspect of such sale transactions, restrictions on similar loan transactions could be used for guidance on the question of reasonableness. See e.g., Federal Home Loan Bank Board regulations for federally chartered savings and loan associations (12 C.F.R. §545.6-4) and South Carolina Board of Financial Institutions Regulation 15-34 for State chartered savings and loan associations (State Register dated February 20, 1981, p.45).

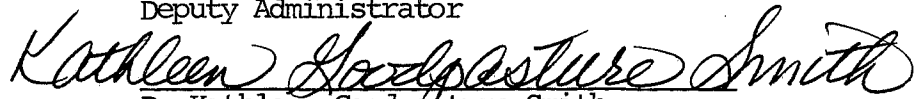
Because of South Carolina's public policy against certain types of variable rate loans, and restrictions on permitted variable rate loans, sellers should assure that their variable rate sale terms are reasonable and that potential increases in rates and charges are fully disclosed to consumers. The Department of Consumer Affairs will be monitoring developments in this area, being mindful of our responsibilities to recommend legislation to promote the protection of legitimate interests of consumers. CPC §37-6-117(g) (1976).

In summary, it is the opinion of this Department that the Beach and Racquet Club may make bona fide financed sales of residential lots secured by first liens on those lots at any rate of credit service charge contracted for by the buyer and seller, including a reasonable

Declaratory Ruling No. 2.605-8102
April 20, 1981
Page 4

variable feature, under the authority of Consumer Protection Code
Section 37-2-605 unless or until laws or regulations restricting
variable rates are made applicable to sales.

Roy C. Harms
Deputy Administrator

A handwritten signature in cursive script that reads "Kathleen Goodpasture Smith". The signature is written in dark ink and is positioned above the typed name of the same individual.

By Kathleen Goodpasture Smith
Counsel to the Administrator

KGS/sls