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The Usury Issue in Public Utility Late Payment Charges

WARREN J. SAMUELS*

Notwithstanding the legislative and judicial trend toward greater protection for consumers, the late charge billing systems of public utilities have escaped consumer regulation. Consumer advocates have argued, inter alia, that the late payment charge is really a form of interest and therefore subject to statutory usury limitations. Courts and commissions have resisted this attack by classifying late charges in other ways, thereby increasing confusion among jurisdictions about the real nature of the late payment charge. The author proposes to unravel this complexity by examining and comparing the different judicial perceptions of the late payment charge, as well as by providing a comprehensive analysis of the interest classification.

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I. INTRODUCTION

In the past decade, consumers have shown an increasing willingness to challenge the legality of the techniques that public utilities have adopted to induce customers to pay their bills promptly.

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This article is the partial result of a comprehensive study of public utility late payment charge systems. The author is indebted to most of the state public service commissions, to numerous public utility companies, and to private and legal-aid attorneys for a variety of data and materials. He is also indebted to Harry M. Trebing for the benefits of frequent discussions.

These techniques include customer deposits, extra charges for late payment, and disconnection with a fee for reconnection. Although these techniques met with the approval of public service commissions even at the outset, consumers have secured important substantive and procedural rights *vis-a-vis* the utility companies before both the commissions and the courts.¹

The late payment charge has been the center of much litigation and many administrative actions challenging utility billing practices.² One controversial issue in the litigation and administrative actions has been whether state laws prohibiting usurious rates of interest or comparable charges apply to late payment charges. The attacks on late charges on usury grounds almost invariably have been unsuccessful. The decisions by commissions and by courts have, nonetheless, raised important analytical and jurisprudential questions, while evidencing the confusion of judges and commissioners about the functions of the late payment charge and of usury law.³

Three principal questions are crucial in determining whether a late payment charge will survive an attack under the usury laws. The first question is whether the late charge is an interest charge. If the late charge is interest, the court or commission must next decide whether the effective interest rate exceeds the limit in the applicable usury statute. A final question is whether a late charge that constitutes interest at a usurious rate nevertheless falls within

1. Michigan has perhaps the most advanced set of procedural safeguards for consumers. See MICHIGAN PUBLIC SERVICE COMMISSION, CONSUMER STANDARDS AND BILLING PRACTICES, Rules 460.2101-.2199 (1974). For a discussion of a possible constitutional source for procedural rights of utility customers, see Note, *Constitutional Safeguards for Public Utility Customers: Power to the People*, 48 N.Y.U. L. REV. 493 (1973). But cf. *Jackson v. Metropolitan Edison Co.*, 419 U.S. 345 (1974) (conduct of a privately owned but publicly regulated utility corporation is not state action).

2. See Note, *Determining the Reasonableness of Public Utility Late Charges*, 26 KAN. L. REV. 595 (1978). See generally Samuels, *Commentary: Utility Late Payment Charges*, 19 WAYNE L. REV. 1151 (1973).

3. See Sections III and IV *infra*. Confusion also surrounds the applicability of usury statutes to public utility bonds or debentures issued during periods of high bond rates. Some commentators have expressed concern that a utility issuing bonds at a competitive interest rate may subject its bondholders to civil and criminal penalties for usurious lending. These commentators suggest that the tortuous and subtle distinctions drawn by the courts among transactions in applying the usury laws may generate such uncertainty that investors will shy away from utility bonds. See, e.g., Blitz, *California Public Utilities and the Usury Law*, 50 L.A. B. BULL. 180 (1975).

The usury issue has also appeared in public utility law when utilities have argued that the interest they must pay on customer deposits is usurious; they simultaneously argue that the effective annual interest rate generated by a five percent nonrecurring late payment charge is not usurious. See 52 PA. CODE §§ 56.22, .57 (1979).

a statutory exemption from the usury laws.

This article will survey, interpret, and criticize recent developments in commission and court decisions regarding challenges on usury grounds to public utility charges for late payment. Following this introduction, Section II will review several recent leading cases, and Section III will discuss the nature of late payment charges. Section IV examines the availability of statutory usury exemptions for the late payment charge, while Section V discusses the calculation of the effective rate of interest represented by a particular late charge. Section VI sets forth some broad conclusions derived from this analysis of the application of usury law to the late charge.

Three matters require clarification at the outset. First, the revenue from late payment charges does not necessarily increase the profits of the utility companies. Late charges are a method of recouping the actual costs to the utility from late customer payments—the expenses of collection and the loss of working capital until the consumer pays the utility bill. Public utility regulators take account of these costs in calculating the rates utilities may charge to earn a permissible rate of return on the rate base. The regulators do not allow the utility to earn more than the set rate of return, whether the utility covers its costs of late payment with a separate late charge or simply includes the costs of late payment in its basic service charge. Regulatory lag, however, may allow the revenue from late charges to rise temporarily above the actual costs of late payment to the utility. Even when this happens, the extra profit the utility earns is small, for the total revenue a utility receives from late charges is typically an infinitesimal percentage of total revenues.⁴

The second point that will help clarify the discussion of late charges is that the utility companies use many terms, some of them misleading, to denote a late charge. For example, penalty charges, forfeited discounts, net-gross differentials, and finance charges are all charges for late payment. The terms “forfeited discount” and “net-gross differential” are particularly misleading. Under the “forfeited discount” or “net-gross” system, the net or lower amount is the amount that the utility charges for its gas or electric service. The gross amount is the net amount plus the late

4. See 1975 REPORT OF THE AD HOC COMMITTEE ON UTILITY BILLING PRACTICES, NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS [hereinafter cited as 1975 NARUC REPORT].

payment charge. There is no "discount" taken from the basic charge. Indeed, if the utility in fact discounted its bill for regular service and all customers took advantage of the discount, then the company would have inadequate revenue to meet its costs, given rate limitations. The "discount," therefore, is only an avoided late charge.⁵ In the following discussion, the terms "late payment charge" or "late charge" are used except when legal analysis requires the use of another term. The synonyms for a late charge are legally significant in the discussion of the status of the charges as interest, for utilities use these synonyms in part to encourage courts and commissions not to categorize late charges as interest.

The third point to keep in mind is that legal developments have severely compromised the integrity of the interest rate ceilings of usury statutes. In the contemporary United States economy, the vast majority of transactions involving interest fall under some exception to the usury limits, although other statutes often regulate interest rates in cases not covered by the usury law.⁶ The current weakness of the usury statutes in so many contexts makes ironic the use of usury law as a weapon to reform utility billing practices.

II. RECENT LEADING CASES

Three recent cases illustrate the typical approaches that courts and commissions have taken to analyze whether late charges are usurious interest. Although the decisions have followed different rationales, each case has reached the same result, concluding that a utility's late charges constitute not interest subject to usury laws, but a device to recover the costs incurred by the utility because of late payments.

In *Coffelt v. Arkansas Power & Light Co.*,⁷ a customer of a utility company brought a class action against it on behalf of all customers who bought electric power from the utility. The plaintiff alleged that the utility imposed late payment charges on its customers in violation of the state constitution's prohibition against usury.⁸ The trial court upheld the validity of the late charge, and

5. Samuels, *supra* note 2, at 1153-54; see 1972 REPORT OF THE AD HOC COMMITTEE ON UTILITY BILLING PRACTICES, NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS [hereinafter cited as 1972 NARUC REPORT].

6. See Section IV *infra*.

7. 248 Ark. 313, 451 S.W.2d 881 (1970).

8. ARK. CONST. art. 19, § 13. The statutes that implement this constitutional prohibition are 68 ARK. STAT. ANN. §§ 602, 603 (1979). The late payment charge in *Coffelt* was 8%

the Supreme Court of Arkansas affirmed.⁹

The utility company called its late payment charge a net-gross differential, but the supreme court did not find that term determinative of whether the charge was usurious. The court explained that "[w]e use the phrase 'late charge' merely for convenience. The practice has also been said to involve a discount for prompt payment, a penalty for tardy payment, a gross-net rate differential We are interested not in nomenclature but in the substantive nature of the charge."¹⁰ To determine the substantive nature of the charge, the court looked to the reasons given by the Arkansas Public Service Commission when it first authorized the late payment charge. The Commission authorized the charge solely as a device to ensure that late payers, rather than all utility customers, would bear the costs caused by the late payers. If the utility were to include the costs of late payment in its basic charge, those who paid their bills on time would suffer discrimination, because they would be paying for costs they had not created.¹¹ Adopting this reasoning, the supreme court concluded that the late payment charge was simply a device to allow the utility to recover the costs caused by late payers without discriminating against timely payers. The court decided that because the late charge was a cost recovery device it was not a charge for an extension of credit. The late charge was not interest and therefore could not be usurious.¹²

In *State ex rel. Guste v. Council of New Orleans*,¹³ the Attorney General of Louisiana brought suit against a utility company and the city council that regulated it. The attorney general, acting on behalf of customers of the utility, asserted that the late payment charge authorized by the city council and imposed by the

of the first \$15 of the net bill and 2% of the excess. The due and payable period (the period from the time the utility sends out its bill until the customer becomes liable for the late payment charge) was ten business days. 248 Ark. at 314, 451 S.W.2d at 882.

9. 248 Ark. 313, 451 S.W.2d 881. The plaintiff did not respond to the affidavits the utility presented with its motion for summary judgment, but instead rested solely on its verified complaint. The trial court and the Arkansas Supreme Court therefore accepted the facts established by the affidavits as controlling. *Id.* at 315-16, 451 S.W.2d at 883.

10. *Id.* at 314, 451 S.W.2d at 882.

11. *Id.* at 314-15, 451 S.W.2d at 882. When the Commission authorized the late charge, it required the utility to keep records of the actual costs that late payment caused the company. The Commission could then adjust the amount of the late charge so that it did not exceed the actual cost of late payment. *Id.* at 315, 451 S.W.2d at 883.

12. *Id.* at 316-17, 451 S.W.2d at 883-84. The court called the late payment charge "a practical method of preventing discrimination" among the customers of the utility. *Id.* at 317, 451 S.W.2d 883.

13. 297 So. 2d 518 (La. Ct. App. 1974), *rev'd*, 309 So. 2d 290 (La. 1975).

utility was usurious interest.¹⁴ The trial court found for the utility and city council. The Louisiana Court of Appeal for the Fourth Circuit reversed and held that the late charge was usurious. The Supreme Court of Louisiana again reversed and reinstated the trial court judgment for the defendants.¹⁵

The utility and city council made two arguments before the court of appeals that the late payment charge was not interest. They first argued, based on the reasoning of the court in *Coffelt*, that the late charge was a device to prevent rate discrimination by assessing the costs of late payment against those who paid their bills late. The court of appeals rejected this argument. The utility in *Guste*, unlike the utility in *Coffelt*, admitted that the late charge covered costs not ascribable to late paying customers, such as the cost of writing off uncollectible accounts. The court of appeals concluded that the late payment charge, far from being an antidiscriminatory device, was itself unjustly discriminatory.¹⁶ Because Louisiana public utility law forbade unjust and discriminatory rates, the court concluded that the late charge was "in fact not a utility rate."¹⁷

The second argument the defendants made before the court of appeals was that the late charge was a time-price differential rather than interest. They argued that the utility customers could choose to pay the "net" rate by paying on time or the "gross" rate by paying late; and that this choice was like the choice of a buyer of goods who chose to pay a higher "time" price to obtain credit rather than pay a lower cash price at once. Relying on the definition of interest in the Louisiana Civil Code, the court of appeals rejected the characterization of the late charge as a time-price differential. The Code defined interest as the "damages due for delay in the performance of an obligation to pay money."¹⁸ Such "damages," to the court, constituted a payment by the debtor for the use of money over the time of the delay in payment. The court distinguished interest payments for the use of money over time from an addition to the sales price of goods to cover credit that the

14. 297 So. 2d at 520. The late charge was 10% of the bill. The due and payable period was ten days. *Id.* at 519. The general interest rate ceiling in Louisiana was 8%. LA. CIV. CODE ANN. art. 2924 (West 1952 & Supp. 1980).

15. 309 So. 2d at 292.

16. 297 So. 2d at 523-24. The intermediate court asserted that "[t]here is no relationship between costs of uncollectible accounts and expenses related to past due accounts." *Id.* at 523.

17. *Id.* at 524.

18. LA. CIV. CODE ANN. art. 1935 (West 1977).

seller extended to the buyer.¹⁹ Here, the late charge was the same no matter how long after the due date the customer delayed payment; it did not depend on the amount of credit the utility was willing to extend to its customers. The court concluded that the late charge was a damage payment to the utility for the customer's delay, not an addition to the price of electrical service to cover credit extended to the customer. Under the Louisiana Civil Code, therefore, the late charge was interest.²⁰

Having found the late charge to be interest, the court of appeals easily concluded that the charge was usurious. The general Louisiana interest rate ceiling was eight percent. The effective rate of the late charge far exceeded that ceiling. The utility could not rely on a statutory exemption from interest rate ceilings for public utility rates²¹ because the court found the late charge was not a valid utility rate. The late charge was therefore usurious.²²

On appeal, the Supreme Court of Louisiana reversed the court of appeals and reinstated the trial court judgment for the defendants. The supreme court noted that the Louisiana usury statute²³ applied only to loans and not to "consumer credit sales."²⁴ The court then found that the provision of services by a utility was a consumer credit sale because it involved the sale of a commodity, electricity, to consumers. The general usury statute therefore did not apply to public utility charges.²⁵ The Louisiana Consumer Credit Act governed consumer credit sales, but it specifically exempted from its restrictions public utility rates regulated by a

19. 297 So. 2d at 525.

20. *Id.* The court found precedent for its distinction between damages for a delay in payment and a time-price differential in the case of *Dendinger, Inc. v. Emury & Eichhorn*, 12 La. App. 39, 124 So. 604 (1929). In *Dendinger*, a contract for the sale of lumber provided for a 10% addition to the sales price if the buyer did not pay by a certain date. The court characterized the additional charge, which was the same regardless of the length of time the buyer delayed payment, as a penalty. The court rejected the argument that the penalty was a time-price differential, and held that the penalty was an interest payment because it constituted damages for a delay in payment.

21. The Louisiana Unfair Trade Practices and Consumer Protection Act does not apply to public utility rates. LA. REV. STAT. ANN. § 51:1406(1) (West Supp. 1980). Public utility rates are also exempted from the interest ceilings of the Louisiana Consumer Credit Law. LA. REV. STAT. ANN. § 9:3512(3) (West Supp. IV 1980).

22. 297 So. 2d at 526. The court of appeals found that the city of New Orleans had exceeded its charter powers when it authorized the usurious late charge, and that it was bound by the decision against the utility. *Id.*

23. LA. CIV. CODE ANN. art. 2924 (West Supp. 1980).

24. 309 So. 2d 290, 296 (La. 1975).

25. *Id.*

state agency²⁶ or subdivision. Since a subdivision of the State of Louisiana, the Council of the City of New Orleans, regulated the rates of the defendant utility, the Consumer Credit Act was also inapplicable. Regulation of public utility rates thus rested solely with the Council.²⁷ The court apparently preferred that the agency charged by the legislature with regulating utility rates have unfettered control over those rates.

In *Delich v. Iowa Electric Light & Power Co.*,²⁸ the Iowa Commerce Commission rejected a usury attack on a late payment charge, relying on the statutory exemption argument successfully expounded in *Guste*. The Commission ultimately concluded that its jurisdiction over public utility rates was preemptive and that the usury statute was therefore inapplicable. In reaching this conclusion, the Commission considered the reach of Iowa's usury statute,²⁹ the Iowa Consumer Credit Code,³⁰ and the statutes vesting the Commission with regulatory authority over public utilities.³¹ The Commission first acknowledged that Iowa's general usury statute did not specifically exempt public utility rates from its operation.³² The Iowa Consumer Credit Code did, however, expressly exempt public utility rates regulated by state agencies.³³ The Commission then asserted that it had the statutory authority to regulate "all rates and charges of public utilities not specifically exempted."³⁴ Reading the Consumer Credit Code exemption to-

26. 9 LA. REV. STAT. ANN. § 3512(3) (West Supp. IV 1980).

27. 309 So. 2d at 296. Judicial review of ratemaking actions by administrative bodies such as the city council is confined to an inquiry into the "reasonableness" of the administrative action. The supreme court found that the late payment charge approved by the city council was nondiscriminatory and reasonable. The court reasoned that the revenue the utility received from the charges imposed on delinquent customers nearly equalled the total costs that the delinquent customers created. Because customers who paid on time caused neither the costs of late payment nor the costs of uncollectible accounts, it was reasonable for the city council to conclude that timely payers should not bear those costs. *Id.* at 294-95. *But cf.* *Kansas City Power & Light Co.*, 28 Pub. U. Rep. 4th 398, 435-36 (Mo. P.S.C. 1979) (late charge that includes the cost of uncollectible accounts discriminates against late payers and should be reduced to include only the costs of late payment).

28. 9 Pub. U. Rep. 4th 335 (Iowa Com. Comm'n 1975).

29. Iowa CODE § 535.2 (1975) (amended 1978 & 1979); *id.* § 535.4 (1975).

30. *Id.* §§ 537.1101-7103 (1975).

31. *Id.* § 490A.1-.27 (1975) (renumbered 1977 as §§ 476.1-.27).

32. 9 Pub. U. Rep. 4th at 337.

33. Iowa CODE § 537.1202(3) (1975). One might wonder whether the Consumer Credit Code exemption was logically necessary in light of the preemptive nature of the Iowa public utility rate regulation. If the Commission was correct in its interpretation of its own jurisdiction, then the Consumer Credit Code would be preempted along with the usury statute. *See* Section IV *infra*.

34. 9 Pub. U. Rep. 4th at 338. Iowa CODE § 490A.21 (1975) (renumbered 1977 as §

gether with the statute granting the Commission regulatory authority over public utilities, the Commission reasoned that the legislature intended late payment charges to be regulated under the statute specifically for public utilities rather than under the statutes on interest rates and credit transactions generally.³⁵ The Commission concluded that it had exclusive jurisdiction over public utility rates and that the usury statute was not applicable.³⁶

Although the statutory usury exemption found in *Delich* made it unnecessary for the Commission to analyze the nature of the late charge to see whether it was usurious, the Commission undertook such an analysis in dicta.³⁷ Interest, under Iowa law, was the consideration a debtor gave a creditor in return for "forbearance" by the creditor in collecting a debt.³⁸ The Commission noted that the utility's late charge was fixed and nonrecurring. The amount of the charge remained the same no matter how long the utility refrained from disconnecting service or suing the customer. Because the customer could not pay an additional late charge for additional forbearance, the Commission reasoned the late charge could not be consideration for forbearance by the utility in collecting its bill.³⁹ The Commission concluded that the late charge was therefore not an interest payment, but was simply a device by which the utility recovered the costs of late payment.⁴⁰

Coffelt, *Guste*, and *Delich* highlight the main analytical and legal issues raised in usury attacks on late payment charges. The decisions share important similarities. In all three cases, the highest court or agency to analyze the usury attack concluded that gen-

476.15) provides that the jurisdiction of the Iowa Commerce Commission over public utilities extends "to the full extent permitted by the constitution and laws of the United States."

35. 9 Pub. U. Rep. 4th at 337-40.

36. *Id.* at 338. A more recent case in which a court relied on a statutory exemption argument to find that a late charge was not usurious is *Jones v. Kansas Gas & Elec. Co.*, 222 Kan. 390, 565 P.2d 597 (1977). In *Jones*, the Kansas Supreme Court held that the Kansas Consumer Credit Code, KAN. STAT. ANN. §§ 16a-1-101 to -9-102 (1974 & Supp. 1979), preempted all other usury laws in the field of consumer transaction; that the sale of utility services was a consumer transaction; but that the Consumer Credit Code exempted regulated public utility rates from its restrictions. Public utility rates in Kansas were therefore to be regulated only by the utility commission. 222 Kan. at 397-98, 555 P.2d at 603-04. The court in *Jones*, like the supreme court in *Guste* and the Commission in *Delich*, upheld exclusive authority in the utility commissioners to regulate rates in any reasonable manner.

37. 9 Pub. U. Rep. 4th at 339.

38. *Id.* at 339-40, 343.

39. *Id.* at 341.

40. *Id.* at 341-42. *Cf. Guste*, 297 So. 2d at 518 (nonrecurring nature of the late charge made the charge more like interest, not less).

eral interest rate limitations do not apply to late charges and that utility regulators have exclusive responsibility for ensuring that utility rates, including late charges, are reasonable. In all three decisions, the court or agency decided that the late charge was not interest and that usury limitations therefore could not apply to the charge. In *Guste* and *Delich*, the Supreme Court of Louisiana and the Iowa Commerce Commission, respectively, held that statutory exemptions of utility rates from the consumer credit statutes imply an exemption for public utility rates from the general state usury law. In the final *Guste* decision, as in *Coffelt* and *Delich*, the court characterized the late charge as a device through which the utility could recover the costs of late payment from those who paid their bills late, thereby preventing the rate discrimination against timely payers that would result if they had to pay the utility for costs caused by late payers.

The *Coffelt*, *Guste*, and *Delich* cases raise the problems associated with the different perceptions of the late payment charge, as evidenced by the alternative rationales expounded by the courts and the Commission to reach the same result. These different perceptions of the purpose of the late payment charge, combined with the differences among state usury statutes, make it difficult to develop a uniform body of law on the issue of whether a late payment charge is usurious interest. The decisions give varying explanations of the analytical differences among a loan, an extension of credit, and an act of forbearance by a creditor utility for a mere delay by the customer in paying his bill.

The confusion in *Coffelt*, *Guste*, *Delich*, and subsequent cases leaves us with numerous questions for which there are no clear answers. In *Guste*, for example, the court drew a distinction between a charge for the use of money over time and an addition to the price of an item (a "time-price differential") because payment for the item is deferred over time. But the court never explained the analytical or economic differences between these two concepts. Still another example of the confusion generated by these decisions concerns the nonrecurring nature of late charges, insofar as they are distinguishable from credit charges. In *Delich*, the nonrecurrence of the late charge led the Commission to conclude that the charge was not interest. In *Guste*, however, the nonrecurring nature of the charge helped persuade the court of appeals that the late charge was interest. How may one reconcile these decisions? Further, even when a court decides that a late charge is interest, how should it calculate the effective rate of that interest?

In part, the thesis of this article is that the questions raised by the *Coffelt*, *Guste*, and *Delich* decisions have no absolute answers. The distinctions that courts and commissions use in discussing late charges may lack analytical legal content, but they do draw substance from the realm of policy. It is thus important to analyze the reasons behind the use of varying characterizations of the late charge.

III. THE NATURE OF THE LATE PAYMENT CHARGE

The most conspicuous feature of the controversy over the nature of the late payment charge is the enormous diversity of perceptions. However designated, the late payment charge is inherently complex and has multiple facets, each of which may be seen as independent and exclusive of the others. The charge may be identified alternatively as a cost recovery device, a penalty, a forfeited discount, an inducement to prompt payment, or a credit charge, as well as interest. Thus, even though the court in *Coffelt* could say that it was "interested not in nomenclature but in the substantive nature of the charge,"⁴¹ another court could advance the view that there is "nothing in this [imposition of a late charge] but the offer of a discount for prompt payment."⁴² Of the company respondents to an Edison Electric survey in 1974, thirty-five described their late payment charge as a penalty, eight as a discount for prompt payment, and seven as interest.⁴³ A company witness in a Maryland case argued that the charge was a cost recovery device and *not solely* interest.⁴⁴ Two spokesmen for one utility also differed, one saying that the late charge was a penalty and not a discount, the other saying that it was a discount for prompt payment.⁴⁵ The 1975 Report of the National Association of Regulatory Utility Commissioners (NARUC) Ad Hoc Committee on Utility Billing Practices states that a late charge is an inducement to

41. 248 Ark. 313, 314, 451 S.W.2d 881, 882 (1970).

42. *Central Hudson Gas & Elec. Corp. v. Napoletano*, 277 A.D. 441, 444, 101 N.Y.S.2d 57, 59 (1950).

43. Edison Electric Institute, Questionnaire Covering Electric Utility Billing Practices for Use in EEI Rate Research Committee Meeting at 2 (Apr. 22-23, 1974).

44. Brief for Joint Petitioners at 9, *People's Counsel & Legal Aid Bureau, Inc.*, No. 7163 (Md. P.S.C., brief dated Jan. 29, 1979) (quoting from Transcript at 690). The witness, Mr. Monte Edwards, counsel for the Washington Gas Light Company, stated that "to characterize it [the late payment charge] solely as interest earned by the utility I think is inappropriate in this proceeding." *Id.*

45. *Louisville Times*, Nov. 21, 1972, at 1, col. 1.

prompt payment,⁴⁶ rather than credit charge,⁴⁷ but also states it is a charge for the use of funds.⁴⁸ One can sympathize, then, with the former chairman of the District of Columbia Public Service Commission who, after concluding that a late payment charge was not interest and was not in violation of the credit laws, added that the proper classification of late payment charges is nevertheless "almost a metaphysical question . . . a pure question of judgment, and probably will have to be decided by the court."⁴⁹

Commissions as well as courts do reach decisions, of course, but those decisions involve quite diverse perceptions with both strengths and limitations. The requirements of legal decisionmaking in cases reaching determinate results upon stated grounds, however, have led to the adoption and defense of exclusive definitions of late payment charges, ignoring or rejecting other perceptions and conflicting lines of reasoning. An overwhelming number of commissions and courts perceive late charges as something other than interest.⁵⁰ This attitude by the decisionmakers apparently derives both from the strength of the noninterest perceptions and from the drawbacks of characterizing late charges as interest, particularly the decisionmakers' awareness that late charges identified as interest will likely fall within the reach of the usury statutes.

The interpretation offered here is that the late payment charge can be perceived within different categories; that a policy choice is necessary and implicit in the choice of any particular category in articulating a decision; and that there are positive elements as well as deficiencies in each perception.

A. *Cost Recovery and Allocation*

As *Coffelt*, *Guste*, and *Delich* suggest, the predominant view is that late charges function to recover and allocate costs of late payment to late payers and, therefore, are not interest.⁵¹ This view is

46. 1975 NARUC REPORT, *supra* note 4, at 3, 13, 21.

47. *Id.* at 9.

48. *Id.* at 4.

49. NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS, BULL. No. 24-1972 at 21 (June 12, 1972) [hereinafter cited as NARUC BULL. No. 24-1972].

50. Samuels, *supra* note 2, at 1160.

51. See, e.g., *Kansas Gas & Elec. Co.*, No. 96,137-U, slip op. at 6-7 (Kan. Corp. Comm'n Apr. 3, 1974); *Consumer Standards and Billing Practices for Residential Service*, slip op. at 10-11, 18 (Pa. P.U.C. Apr. 12, 1978); *Utah Power & Light Co.*, 19 Pub. U. Rep. 2d 369 (Utah P.S.C. 1937); *Investigation to Determine the Reasonableness of Certain Practices and Charges by Public Utilities*, No. 19589, slip op. at 20 (Va. Corp. Comm'n Jan. 10, 1977); *Brief for Wisconsin Power & Light Co.* at 3, *Investigation on Motion of the Commission*

not inaccurate. But, although courts and commissions have perceived the late charge as a simple antidiscriminatory device, there are complicating factors. First, the relationship between collection costs and the revenues from late charges varies with the collection policy. Perhaps half of the utility companies do not impose charges for late payment; and among those that do, both the amount of the charge⁵² and the time over which the costs are incurred vary considerably. One critical variable is the length of the due and payable period, a factor of considerable importance because it determines what constitutes a late payment. Although the due and payable period may be as short as ten or fifteen days, the overwhelming number of customers pay within one month without any collection activity by the utility company.⁵³

Second, the allocation of general costs to late payment is arbitrary. It is often a matter of historical policy. The utility's purpose

Relative to Whether the Present Deposit, Guarantee and Disconnect Rules Are Appropriate and Reasonable and as to Whether a Rule Should Be Promulgated Respecting Net and Gross Billing Practices of Public Utilities, No. 2-U-7720 (Wis. P.S.C. Apr. 6, 1976) [hereinafter cited as Wis. Billing Practices Investigation]; Memorandum from William Anderson to Commissioners and Commission Attorneys, North Carolina Utilities Commission at 2-6, The "Net and Gross" Billing Practice (December 22, 1970).

52. Typically, the level of the charge is not directly related to collection activity and costs. Answer of Kansas Gas & Electric Co. at 3, Kansas Gas & Elec. Co., No. 96,137-U.

53. Samuels, *supra* note 2, at 1158-59. In the case of a usury charge brought against the water department of the City of Cleveland, the city defended its policies in part on the ground that

[u]sury regulations were enacted to protect borrowers from extortion and unjust oppression by unscrupulous lender [*sic*]. Such regulations proceed on the assumption that a usurious loan is attributable to an imbalance in the relationship between the lender and the borrower and that the borrower's plight deprives him of the freedom to contract, placing him at the mercy of the lender . . . It is clear, initially, that such an inequity does not exist in the relationship between a municipally-owned utility and its customers.

Defendant's Motion for Summary Judgment at 4, *Benham v. City of Cleveland*, No. 914,017 (Ohio Cuyahoga County Ct. C.P. Feb. 3, 1977). In reply, the plaintiffs characterized the city's position as being "that, basically, the usury statute should not apply to it because the water company is run by 'nice people,'" and commented that "malice or vindictiveness is not an element of the offense of usury." Reply Brief to Defendant's Motion for Summary Judgment at 3, 4, *Benham v. City of Cleveland*, No. 914,017. The relevant point is that although the court held the city's late charge not to be usurious interest, it urged the City Council to lengthen the due and payable period because the people least able to afford the late charge were the ones most likely to suffer. Moreover, the court criticized the billing procedure for giving

the false impression of a discount if payment is made before the due date expires in fifteen (15) days. It is grossly misleading to the thousands of citizens of Cuyahoga County who have a right to rely on the City of Cleveland's representations. The billing procedure of the City of Cleveland's Water Division must be changed.

Benham v. City of Cleveland, No. 914,017, slip op. at 3.

in allocating general costs to the late payment charge is to have sufficient costs to offset revenues so that the utility can defend the amount of the charge against future challenge.⁵⁴ Utility companies also frequently and arbitrarily allocate the specific cost of uncollectible accounts to late payers generally,⁵⁵ failing to distinguish late payers from nonpayers. In addition, the companies often do not distinguish between late payers who pay only after collection action and those who pay on their own initiative.⁵⁶

Third, the loss of working capital is the principal if not sole cost to the utility of late payments during the precollection activity period. Interest is a logical device to recover the value of that loss and has been acknowledged as such by at least one company witness.⁵⁷ Two further complications arise. First, the effective annual rate calculable for late payment charges is often much higher than the actual market cost of working capital, even during periods of relatively high market interest rates. Second, the rate base often includes working capital, so that recovering the cost of working capital through late payment charges may permit double recovery. For this reason, working capital costs are sometimes excluded in estimating late payment costs.

Finally, it is questionable whether identifying the late charge as a method of recovering collection costs precludes its identification as interest. After all, banks and other institutions have collection and other operating costs that do not prevent the identification of their charges as interest. Moreover, utility collection costs

54. It should be noted that, in most cases, little if any cost information is available. Cost figures typically are estimates inasmuch as the Uniform System of Accounts neither requires nor permits the isolation of late payment costs.

55. Samuels, *supra* note 2, at 1155; 1972 NARUC REPORT, *supra* note 5, at 8, 10.

56. See *Jones v. Kansas Gas & Elec. Co.*, 222 Kan. 390, 400-02, 565 P.2d 597, 605-06 (1977); Samuels, *supra* note 2, at 1155-56.

It has been argued that bill collection activity is not the same thing as financing accounts receivable. See Transcript of May 5, 1975 Hearing, vol. VIII, at 1016, Wis. Billing Practices Investigation, *supra* note 51. It also has been argued that cost recovery is justified only when there have been special services, Plaintiff's Motion for Summary Judgment at 9, *Benham v. City of Cleveland*, No. 914,017, and that the late charge has no relation to the actual damages suffered by the company, Memorandum of Intervenor at 1, *Odell Smith*, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969). In an early case, the court held that a 10% late charge was a penalty for enforcing prompt payment or indemnifying for damage suffered from unpaid bills and that the only such damage allowed a creditor is legal interest. *Ford v. Vicksburg Waterworks Co.*, 102 Miss. 717, 59 So. 880 (1912), noted in Brief for the Attorney General of Kansas as Amicus Curiae at 6, *Jones v. Kansas Gas & Elec. Co.*, 222 Kan. 390, 400-02, 565 P.2d 597, 605-06 (1977).

57. Brief for Complainant at 20, *Kansas Gas & Elec. Co.*, No. 96,137-U (Kan. Corp. Comm'n Apr. 3, 1974) (quoting Transcript at 356, 527).

and late payment charges are for the most part independently determined through separate policy decisions.⁵⁸

In conclusion, the identification of the late payment charge as interest and its identification as a device for the recovery and allocation of cost are not mutually exclusive, because the charge is for the time-use of money. Thus, even though an emphasis on the interest categorization arguably ignores the recovery of collection expenses,⁵⁹ one can also argue that late payment charges constitute both interest and a means necessary to recover costs and induce prompt payment.⁶⁰

B. *Inducement to Promptness, "Penalty," and Other Perceptions of Late Charges*

Although the definition of late charges as a device for the recovery and allocation of cost predominates, four other perceptions are common: the forfeited discount, the net-gross rate, the inducement to prompt payment, and the penalty for late payment. One of them is fallacious, another is an exercise in studied ambiguity, and the other two have substantive meaning but remain controversial. Confusion pervades this issue, as advocates of each perception explicitly reject one or more of the other perceptions. One utility spokesman, for example, has characterized the late charge not as interest but as a penalty, while a staff member of a commission has argued that the late charge should not be considered a penalty but a forfeited discount.⁶¹

The conception of a forfeited discount is utterly fallacious. When there are two listed prices, the lower price reflects not a discount but the utility company's charge for its utility service; the higher price reflects the addition of a charge for late payment.⁶²

58. Samuels, *supra* note 2, at 1155.

59. Answer of Kansas Gas & Elec. Co. at 3, Kansas Gas & Elec. Co., No. 96,137-U.

60. See, e.g., Atlanta Gas Light Co., 17 Pub. U. Rep. 4th 421, 426 (Ga. P.S.C. 1976); Rule-Making Proceeding to Investigate and Promulgate Rules to Prohibit and to Establish Uniform Tariff Provisions for Billing of Customers of Electric, Telephone, Gas, Water and Sewer Utilities, No. M-100, SUB 39, slip op. at 6 (N.C. Util. Comm'n Nov. 24, 1972) [hereinafter cited as N.C. Uniform Billing Procedure Investigation].

61. NARUC BULL. No. 24-1972, *supra* note 49, at 20.

62. The ambiguity of such practice was noted in Plaintiff's Motion for Summary Judgment at 5-6, Benham v. City of Cleveland, No. 914,017 (Ohio Cuyahoga County Ct. C.P. Feb. 3, 1977):

Indeed, defendant's characterization of the late-payment charge as a 'discount' rather than a 'penalty' is refuted by a simple reading of the ordinance which effectuated the late payment charge. That ordinance provides, '[A]ll bills . . . not paid on or before the date shown on the bill . . . shall be *increased* by an

The idea that the late charge embodies the failure to take advantage of a discount is attractive to some persons and may motivate customers to pay promptly; it is nevertheless untrue. The concept's main historic advantage has been to improve public relations by avoiding the antagonistic designation of late charges as penalties or even as charges. This notion does, of course, place the moral blame on the customer for not paying on time. The very concept of a discount, however, may run afoul of statutory provisions that instruct commissions to make rules and regulations to prevent discounts.⁶³

The concept of net-gross rates shares with the notion of a forfeited discount the twin advantages of avoiding identification of the late charge as a penalty, which utility companies find conducive to the formation of a positive public image, and of avoiding identification of the charge as interest, which utility company executives and lawyers find desirable in light of the usury statutes. Utility companies developed the net-gross idea largely in response to the recognition of the fallacy of forfeited discounts, but it is the epitome of ambiguity. The customer's bill indicates a "gross" amount and a "net" amount, with no identification of the difference between them except that the gross amount is to be paid after the due and payable date.⁶⁴ The related characterization as a "discount for prompt payment" is no less fallacious than the less specific notions of a forfeited discount and a net-gross rate.⁶⁵

The notions of an inducement to prompt payment and a penalty for late payment more accurately characterize the nature of a late payment charge, because irrespective of how the charge is labeled, it is likely to motivate prompt payment and to be perceived as a penalty by the customer. The categorization as an inducement to prompt payment is controversial. The plaintiffs in one usury case argued that "the creation of incentive for prompt payment has never been recognized as a justification for imposition of exorbitant and usurious interest rates."⁶⁶ Intervenors challenging a net-

amount equal to three per cent (3%) of the bill.' Cleveland City Ordinances, Section 7.2112 (emphasis added). The impact of the ordinance is clear: it exacts a penalty for late payment of bills.

63. See, e.g., N.C. GEN. STAT. § 62-140(b)(2) (1975).

64. In some cases, the official tariffs on file at commission offices may speak of a late charge, penalty, or other term, but the bill rendered to customers merely lists net and gross amounts.

65. See 1975 NARUC REPORT, *supra* note 4, at 18. But see *Central Hudson Gas & Elec. Corp. v. Napoletano*, 277 A.D. 441, 444, 101 N.Y.S.2d 57, 59-60 (1950).

66. Plaintiff's Motion for Summary Judgment at 8, *Benham v. City of Cleveland*, No.

gross billing system in Arkansas quoted from a dissent by Justice Frankfurter: "[e]xactions for a breach of contract not giving rise to damages and merely serving as added pressure to carry out punctiliously the terms of a contract, are not enforced by the courts."⁶⁷ The intervenors added that although Justice Frankfurter expressed this view "in a dissent, it voices a generally held view that the providing of 'incentives' for prompt payment of debts should not be left up to private individuals or corporations."⁶⁸ Conversely, many utilities defend net-gross billing systems and favor the imposition of penalties and the allowance of discounts to secure the prompt payment of utility bills.⁶⁹

The attempt to justify late charges as a penalty is also controversial. Critics of late payment charges, for example, tend to characterize them as an inequitable punishment for poverty.⁷⁰ Utilities, on the other hand, argue that late payment charges are not interest but a legal penalty for delinquency.⁷¹ One company representative testified that the late charges are but a penalty for violating the terms under which service is provided.⁷² This latter argument is a

914,017.

67. Memorandum of Intervenors at 4, Odell Smith, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969) (quoting *Priebe & Sons, Inc. v. United States*, 332 U.S. 407, 417-18 (1947) (Frankfurter, J., dissenting)).

68. *Id.* Perhaps less significant than the dissent origin of the quotation from Justice Frankfurter is the fact that the object of attack was company tariff provisions previously approved by the state commission, lending to them the color of state action.

69. See, e.g., Brief for Wisconsin Power & Light Co. at 3, Wis. Billing Practices Investigation, *supra* note 51.

70. In Odell Smith, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969), a group of welfare recipients intervened in the Arkansas Public Service Commission's investigation of the petition by Arkansas Power & Light Co. for the imposition of a Gross-Net Billing Rider. The intervenors argued in part that the proposed late payment charge, or "penalty," could not be equitably justified, because late payment is "frequently a matter of hardship and involuntary delinquency." Memorandum of Intervenors at 4, Odell Smith, 78 Pub. U. Rep. 3d 317. In support of their argument, they noted that the welfare allowance for public utility charges is frequently less than what the recipient needs, and that the recipient receives the welfare check two weeks before the utility bill arrives. *Id.* at 4-5. The intervenors claimed that "[g]iven an already acute money shortage in these families, and the resulting inability to put aside an unknown amount of cash for two weeks to cover the utility bill, . . . welfare recipients will frequently be made to pay the requested penalty through no fault of their own *Id.* at 5.

When the poor and the elderly on fixed incomes do not pay their utility bills on time, it is often because of unemployment and poverty, not because of lack of incentive. Samuels, *supra* note 2, at 1159-60.

71. Memorandum Brief at 13-15, Odell Smith, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969).

72. Transcript of May 5, 1975 Hearing, vol. VIII, at 1095, Wis. Billing Practices Investigation, *supra* note 51. A Wisconsin Gas Company representative stated that "[t]he bill is unconditionally due on the due date" and "[t]he company does not permit late payments."

non sequitur, since the late charge—or penalty—is one of the terms under which service is provided.⁷³

However one characterizes late payment charges, the use of certain terms and not others is not necessarily dispositive of the “real nature” of the transaction. Thus, statements such as “[t]he existence of prompt payment discounts or late payment penalties may be taken as evidence of a desire to collect as promptly as possible, rather than to levy a charge for credit,”⁷⁴ merely beg the issue. This is precisely the point: Because public relations symbolism and semantics have little bearing on the substance of the transaction, the identification of late payment charges under one category does not preclude identification under others, including that of interest. Although the categories are self-justifying, and the decisions resting on specific categories are tautological, the differing perceptions still co-exist. The bogey, of course, is the interest category, on which the discussion will now focus.

C. *Interest*

Despite the overwhelming tendency of courts and commissions not to perceive late payment charges as interest, the factors and lines of reasoning they consider are diverse, often ambiguous, and sometimes internally conflicting. The recurring themes in any discussion of the nature of late payment charges include: late payment as a charge for the extension of credit; the conflict between the time-price and the time-use doctrines; the existence of forbearance in the late-charge system; the significance of the recurring or nonrecurring nature of the charge; and the argument that nonpayment, and thus exposure to the late charge, is within the control of the payor. In light of these diverse themes, both the identification of late charges as interest and the rejection of such an identification are at best subject to serious qualifications and require the exercise of arbitrary or partisan choice.

Id. It follows, according to such reasoning, that a revolving charge or installment plan cannot be considered a term within the service agreement offered to customers.

73. Late payment charges can also be analogized to liquidated damages clauses, which are void and unenforceable unless related to the actual damage suffered. See Memorandum of Intervenor at 4, Odell Smith, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969). In *Smith*, the intervenors concluded that the late charge (ten percent of the first \$15.00 of the bill, two percent of the excess) was regressive and unrelated to the costs created by late payment. *Id.* at 2, 5.

74. 1975 NARUC REPORT, *supra* note 4, at 9.

1. CHARGE FOR THE EXTENSION OF CREDIT

The specific substantive arguments against regarding late payment charges as interest are: (1) that there is no extension of credit, no loan, no specific payment for the use of money, no bill in the sense contemplated by the usury law; (2) that utility companies do not desire to extend credit; and (3) that such charges are the equivalent of a time-price differential and thus are not interest. Each of these arguments, on which the majority of rulings have been based, has been either compromised by statements and decisions to the contrary or severely weakened by countervailing lines of reasoning.

One recent example is the case of *Jones v. Kansas Gas & Electric Co.*⁷⁵ At the agency level, the Kansas Corporation Commission found that "the late payment charges do not constitute payment for the extension of credit . . . It follows, and the Commission so finds, that the late payment charges do not constitute interest . . ."⁷⁶ On appeal from a district court order affirming the decision of the Commission, the Supreme Court of Kansas agreed in part with the Commission and held that the late payment charges were not interest but penalty charges to induce prompt payment and defray collection costs. The court noted, however, that in testimony before the Commission a company witness referred to the late payment charge as an extension of credit.⁷⁷ The court concluded that since the utility did not incur any collection costs during the fifteen-day grace period for late payment charges, "[t]he penalty . . . should be limited to an amount which encourages prompt payment *and covers the cost of extending credit.*"⁷⁸ This result, of course, is totally inconsistent with the court's holding that late payment charges do not constitute interest payments if one includes in the definition of interest the notion of a charge for the extension of credit.

The *Jones* decision is not the sole illustration of the inherent compromises and ambiguities in reasoning that surround the issue of whether late payment charges involve an extension of credit. The 1972 NARUC Ad Hoc Committee on Billing Practices stated that a late payment charge is a credit or finance charge.⁷⁹ The

75. 222 Kan. 390, 565 P.2d 597 (1977).

76. *Kansas Gas & Elec. Co.*, No. 96,137-U, slip op. at 6 (Kan. Corp. Comm'n Apr. 3, 1974).

77. 222 Kan. at 395, 565 P.2d at 602.

78. *Id.* at 401-02, 565 P.2d at 606 (emphasis added).

79. 1972 NARUC REPORT, *supra* note 5, at 9.

North Carolina Utilities Commission adopted a one percent per month maximum rate as a charge for the extension of credit and found "late payment charges," "finance charges," and "service charges" synonymous with "interest."⁸⁰ An Iowa lower court wrote of a "delayed payment charge,"⁸¹ and the staff of the New York Public Service Commission referred to late payment charges as an extension of credit.⁸² Also, various plaintiffs and intervenors have attacked utility late payment charges in terms of credit extension⁸³ and credit sales contracts.⁸⁴ Conversely, several recent decisions have held that late charges are not interest, asserting that a late charge is not a payment for the use of money in the sense of a loan, as distinguished from a credit sale.⁸⁵ In at least one case, a commission determined that the late charge constituted neither a loan, nor the use of money, nor a credit sale, nor the extension of credit.⁸⁶

Are utility companies extending credit when they assess late charges? Utility spokesmen arguing against characterization as interest often deny that their business involves credit extension. When arguing for the approval of late charges, however, they often call attention to the credit extended during the month of service before billing and during the period between the billing date and the due and payable date. The 1975 NARUC Report emphasized inducement to promptness and rejected the credit-charge concept; nonetheless, the report referred to the late charge as a charge "for the use of funds."⁸⁷ The New York Commission has gone so far as

80. N.C. Uniform Billing Procedure Investigation, *supra* note 60, at 6, 8.

81. *State ex rel. Turner v. Town of LeGrand*, No. 32857, slip op. at 5 (Iowa Marshall County Dist. Ct. Jan. 3, 1978).

82. Energy Division Staff Memorandum to the New York Public Service Commission, at 15 (Apr. 26, 1974).

83. Brief for Joint Petitioners at 4, Peoples' Counsel & Legal Aid Bureau, Inc., No. 7163 (Md. P.S.C., brief filed Jan. 29, 1979).

84. Memorandum of Intervenors at 4, Odell Smith, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969).

85. *See, e.g., Ferguson v. Chattanooga Elec. Power Bd.*, 378 F. Supp. 787, 790 (E.D. Tenn. 1974).

Late charges can be defended against usury attack by two parallel arguments. One can argue that the charges are not interest either because there is no extension of credit, or because there is no loan. The distinction between a credit sale and a loan, and the question whether the nature of the charge for extended credit is the same for each, are key issues. But both forms of the use of money (credit extensions and loans) have been the definitional bases of both rejections and acceptances of the late charge as interest.

86. Consumer Standards and Billing Practices for Residential Service, slip op. at 10-11 (Pa. P.U.C. Apr. 12, 1978).

87. 1975 NARUC REPORT, *supra* note 4, at 4.

to conclude that, "[i]n essence, customers making late payments are receiving loans from the company" ⁸⁸ In other words, although some authorities refuse to identify late charges as interest on the ground that they involve neither an extension of credit, nor the use of money, nor a loan, other authorities have identified late charges as interest on precisely those grounds.

A related line of reasoning is that late charges are not interest subject to usury limitations because utility bills are not "bills" in the sense contemplated by the usury statutes, which are inapplicable to sales of services or products. One Ohio court held that the state statutes "limiting the rate of interest on bills do not use the term 'bill' in the sense of notices sent out on amounts owed for services rendered or products delivered, but only in the sense of an instrument of writing for the forbearance [*sic*] of payment of money at any future time." ⁸⁹ The relevant Ohio statute reads, in pertinent part:

[W]hen money becomes due and payable upon any bond, bill, note or other instrument of writing, upon any book account, or settlement between parties upon all verbal contracts entered into, and upon all judgments, decrees, and orders of any judicial tribunal for the payment of money arising out of a contract, or other transaction, the creditor is entitled to interest at a rate of six percent per annum, and no more. ⁹⁰

On the basis of this provision, the defendant utility argued that the city's billing procedure, especially its late charge provision, was not specifically enumerated and therefore was not within the ambit of the usury statute. ⁹¹ In response, the plaintiff suggested that the very language of that section, notably "when money becomes due and payable, upon any . . . book account," sufficed to bring a utility bill within the statute. ⁹² Similarly, apropos of *Jones*, ⁹³ the Kansas usury statute includes such language as "for money lent or money due on settlement of account" and "for payment due and withheld by an unreasonable and vexatious delay of payment or

88. Memorandum Approving Late Payment Charge at 5, Long Island Lighting Co., No. 27237 (N.Y. P.S.C. Sept. 14, 1977).

89. Benham v. City of Cleveland, No. 914,017, slip op. at 2-3 (Ohio Cuyahoga County Ct. C.P. Feb. 3, 1977).

90. OHIO REV. CODE ANN. § 1343.02 (Page 1979).

91. Defendant's Motion for Summary Judgment at 4-5, Benham v. City of Cleveland, No. 914,017.

92. Reply Brief to Defendant's Motion for Summary Judgment at 4, Benham v. City of Cleveland, No. 914,017.

93. 222 Kan. 390, 565 P.2d 597 (1977).

settlement of accounts."⁹⁴ Thus, even though utility bills are generally excluded from usury statutes, some consumers have persuasively stressed the *prima facie* applicability of the usury limitations to utility bills and charges for late payment by analogizing these charges to amounts due on accounts and to charges for credit.⁹⁵

For comparison, note that the Internal Revenue Service treats late payment charges of public utility companies as interest payments deductible for the customer.⁹⁶ For tax deduction purposes, interest is compensation allowed by law or fixed by the parties for the use, forbearance, or detention of money.⁹⁷ Under the Internal Revenue Code, "it is not necessary for the parties to a transaction to label a payment made for the use of money as interest for it to be so treated. The facts of the transaction control its character, not the terminology."⁹⁸ Moreover, "[t]he fact that the late-payment charge is a one-time charge does not preclude a finding that it is interest."⁹⁹ Finally, late charges are deductible as interest payments regardless of their use by the recipient to cover operating costs.¹⁰⁰

One reason why utilities do not perceive late payment charges as interest payments is that they do not see themselves as financial institutions. Utility representatives frequently argue that they have no desire to extend credit, that they are not in the loan or finance business, and that they do not use credit as a marketing tool.¹⁰¹ Analytically, the situation is more complex. The utility has made no prior payment to the customer, the repayment of which has been delayed, but prior delivery and consumption of utility services have taken place, and amounts on accounts are due, if not overdue. Alongside the cases of welfare families unable to pay

94. KAN. STAT. ANN. § 16-201 (1974).

95. See, e.g., Memorandum Approving Late Payment Charge, Long Island Lighting Co., No. 27237 (N.Y. P.S.C. Sept. 14, 1977); 1972 NARUC REPORT, *supra* note 5.

96. See generally Brief for Wisconsin Department of Justice at 4, Wis. Billing Practices Investigation, *supra* note 51; see also Transcript of Hearing at 464-67, Investigation by the Commission of Gas and Electric Tariffs Relative to (a) Waiver of Late Payment Charge After Due Date, (b) Amount, or Percentage, of Late Payment Charge, and (c) Customer Deposit Requirements, No. 6785 (Md. P.S.C., hearing on July 17, 1975) [hereinafter cited as Md. Late Payment Charge Investigation].

97. Fall River Elec. Light Co. v. Commissioner, 23 B.T.A. 168 (1931).

98. Rev. Rul. 72-315, 1972-1 C.B. 49, 50.

99. Rev. Rul. 74-187, 1974-1 C.B. 48.

100. [1979] STAND. FED. TAX REP. (CCH) ¶ 1420.103; see 1979 U.S. MASTER TAX GUIDE (CCH) § 1071.

101. Brief for Wisconsin Gas Co. at 4-5, Wis. Billing Practices Investigation, *supra* note 51.

monthly bills on time are the small businesses that finance their own working capital by paying the relatively low rates of late charges and thus avoid more expensive alternatives. Because the utility company has the option of disconnecting service immediately upon delinquency, the use of late charges as an intermediate step prior to disconnection indicates an institutional decision to permit late payment at a price, at least up to a point. Indeed, disconnections are relatively few in comparison to the percentage of delinquences and total customers. Insofar as the question of usury is concerned, the nebulous distinctions variously between a loan, an extension of credit, and a nonpayment of an amount owed are influenced by further distinctions between "financial" and "nonfinancial" institutions. The general demise of standard usury limits on finance charges of all types, however, largely eclipses such distinctions and considerations.

2. THE CONFLICT BETWEEN THE TIME-PRICE AND THE TIME-USE DOCTRINES

The time-price doctrine has rationalized the exclusion of a wide range of transactions from the reach of usury statutes. Under the time-price doctrine the seller may charge a credit price that is higher than the cash price. The credit price is the cash price plus the time-price differential. Typically, the time-price differential is regulated by other statutes that permit effective rates well in excess of the legal rate of interest allowed by the usury statutes.

It is implicit in the time-price doctrine that the extra amount charged is correlated with the passage of time. Whenever a differential amount of money is correlated with some measure of time, that differential is interest in the eye of the economist. Whenever a charge involves payment over time, it is interest. This is the *time-use* nature of interest, independent of whether there is a loan, an extension of credit, or a delayed payment for an amount due.

The necessary implication of this economic view of the time-price differential is that the adoption of the time-price doctrine excludes certain transactions from the reach of the usury statute. When a court holds that the time-price differential is not interest, it gives effect to a normative judgment to exclude these types of transactions. Such a holding is not based on the analytical or economic nature of interest¹⁰² as given by the time-use analysis. It fol-

102. Thus, the distinction drawn by the appellate court in *State ex rel. Guste v. Council of New Orleans*, 297 So. 2d 518 (La. Ct. App. 1974), *rev'd*, 309 So. 2d 290 (La. 1975), is

lows that plaintiffs who rely on the time-use analysis to assert that late charges are interest employ a limited argument. The legal treatment of late charges *vis-a-vis* the usury statute confronts an *ought* question. Because an *ought* cannot be deduced from an *is*, then even assuming the *is* status of the time-use analysis, legal decisionmaking still requires an additional normative premise, such as that provided by the time-price doctrine, which, unfortunately perhaps, leads to the opposite conclusion.

3. FORBEARANCE

The notion of forbearance figures prominently in the identification of late payment charges as interest. As with the issue of whether late payment charges involve an extension of credit, the question of forbearance evidences diverse and conflicting lines of reasoning. For the most part, decisions that find neither a loan nor an extension of credit in late-charge systems also find no forbearance from collection of a debt. This was the result in *Coffelt v. Arkansas Power & Light Co.*,¹⁰³ as well as that of the Kansas Corporation Commission in *Kansas Gas & Electric Co.*¹⁰⁴

The argument that late-charge billing systems are not usurious because they do not involve forbearance is superficially consistent with the general definition of usury. *Black's Law Dictionary* defines usury as an "illegal contract for a loan or forbearance of money, goods, or things in action, by which illegal interest is reserved"¹⁰⁵ and the taking, either directly or indirectly, of "a greater sum for the use of money than the lawful interest."¹⁰⁶ Although *Black's* notes that usury is the forbearance of a loan or of an existing indebtedness, at least one city has successfully defended a late-payment usury charge on the ground that forbearance applies only to a loan of money.¹⁰⁷ Another court, however, held that

[w]hen time is given to pay . . . an amount . . . greater than the cash price with legal interest, the result is an agreement for for-

without analytical foundation. See notes 16-20 and accompanying text *supra*.

103. 248 Ark. 313, 316-17, 451 S.W.2d 881, 883-84 (1970). Similarly, in *Ferguson v. Chattanooga Elec. Power Bd.*, 378 F. Supp. 787 (E.D. Tenn. 1974), the court held that the late charge was neither a payment for the use of money nor consideration for the creditor's forbearance. *Id.* at 790.

104. *Kansas Gas & Elec. Co.*, No. 96,137-U, slip op. at 6 (Kan. Corp. Comm'n Apr. 3, 1974).

105. *BLACK'S LAW DICTIONARY* 1714 (rev. 4th ed. 1968).

106. *Id.*

107. Defendant's Motion for Summary Judgment at 5-6, *Benham v. City of Cleveland*, No. 914,017 (Ohio Cuyahoga County Ct. C.P. Feb. 3, 1977).

bearance from demanding payment of an existing debt

Forbearance does not necessarily require an actual loan of money. It generally signifies the giving of time for the payment of a debt. In any transaction in which there is delay until final payment there is a forbearance as that term is used in the requirement for a finding of usury.¹⁰⁸

If, consistent with this opinion and *Black's*, one defines forbearance as an "[a]ct by which [a] creditor waits for payment of [a] debt due him by [the] debtor after it becomes due,"¹⁰⁹ then forbearance also applies to debts arising from transactions other than loans. Irrespective of which definition applies, however, courts and commissions may not find forbearance if they perceive the late payment charge as a method of recovering costs or inducing prompt payment.

The question of forbearance is involved analytically in the identification of late charges as interest. For late charges to be usurious, they must first be considered interest. One test of interest is forbearance.¹¹⁰ The immediate operative question, then, is whether forbearance is present. The answer seems to turn on the interpretation given to the billing and collection system as a whole, of which late charges are a part. This interpretation is a function of some combination of company and commission policy. One can argue, therefore, that there is no specific act of forbearance, since delay of further company collection activity is built into the system. One can also argue, however, that the built-in delay per se constitutes forbearance insofar as imposition and payment of late charges postpone the utility's "most effective collection technique,"¹¹¹ namely, disconnection. In addition, one can argue that there is forbearance of the legal option available to the company to bring suit in small claims court and perhaps even to perfect a lien on the customer's property.¹¹² One court has reasoned that

[e]ven the name used by the Ordinance [permitting late charges]

108. *State ex rel. Turner v. Younker Bros.*, 210 N.W.2d 550, 562 (Iowa 1973).

109. *BLACK'S LAW DICTIONARY* 1714 (rev. 4th ed. 1968).

110. In *Benham*, the court stated that the usury statute does "not use the term 'bill' in the sense of notices sent out on amounts owed for services rendered or products delivered, but only in the sense of an instrument of writing for the forbearance of payment of money at any future time." No. 914,017, slip op. at 2-3. The court held the statute did not apply to the city's late charge.

111. *State ex rel. Turner v. Town of LeGrand*, No. 32857, slip op. at 5 (Iowa Marshall County Dist. Ct. Jan. 3, 1978).

112. Brief of Joint Petitioners at 16, *People's Counsel & Legal Aid Bureau, Inc.*, No. 7163 (Md. P.S.C., brief filed Jan. 29, 1979).

itself is indicative of the forbearance inherent in the system. The Ordinance doesn't call it a "late payment charge," it calls it a "delayed payment charge." The clear implication is that a customer may "delay" his payment by paying the 10% fee for so "delaying."¹¹³

This court viewed the city's policy decision to include a late charge in its billing and collection system as constituting by itself a decision to delay and forbear.

Thus, there is obvious disagreement and confusion over the nature and reach of the forbearance requirement. Both the law and the facts on forbearance in late payment charges permit diverse and conflicting perceptions, lines of reasoning, and conclusions.

4. NONRECURRING AND RECURRING LATE CHARGES

Another line of reasoning for finding that late charges are not interest is that late charges are nonrecurring and therefore independent of the specific length of time during which payment is delayed. The charge is imposed but once and does not increase with the passage of time.¹¹⁴ It has been argued, however, that a nonrecurring late charge is interest because of forbearance, notwithstanding its invariability with time.¹¹⁵

More important for this discussion are the alternative rationales underlying the view that nonrecurring charges are not interest. First, there is the implication that if a nonrecurring charge is not interest, a recurring charge is interest. Indeed, commissions that adopt recurring late charges are more receptive to the idea that late charges are interest.¹¹⁶ Second, the implication that a recurring late charge is interest leads to the notion that a recurring charge is desirable; this notion is also supported by the recognition of the continuity and accumulation of working capital costs, which

113. *State ex rel. Turner v. Town of LeGrand*, No. 32857, slip op. at 5. The same implication appears to follow from the term "late payment charge."

114. Defendant's Motion for Summary Judgment at 5, *Benham v. City of Cleveland*, No. 914,017 (Ohio Cuyahoga County Ct. C.P. Feb. 3, 1977). "[O]nly the computations of effective interest," rather than "[t]he time of the payment after the due date," "determine the amount to be paid . . . [T]hough computations may create an effective rate of interest, the late charge, itself, is not legal interest, because the amount due does not increase as time passes." *Id.*, slip op. at 2. See also 1975 NARUC REPORT, *supra* note 4, at 3, 13-14, 21.

115. Reply Brief to Defendant's Motion for Summary Judgment at 5, 7, *Benham v. City of Cleveland*, No. 914,017.

116. *E.g.*, *State ex rel. Guste v. Council of New Orleans*, 309 So. 2d 290 (La. 1975); *Rangeley Power Co.*, 9 Pub. U. Rep. 4th 289 (Me. P.U.C. 1975); N.C. Uniform Billing Procedure Investigation, *supra* note 60.

are clearly interest. Conversely, the view that the late charge is *not* intended to be interest implies that the late charge should be collected only once.¹¹⁷

Utility billing and collection systems actually include late charges that are both recurring and nonrecurring. In this context, the perception that late charges are interest may justify a recurring or time-differentiated late charge, whereas the imposition of a non-recurring late charge may lead to the perception that late charges are not interest—a circular approach at best. The perception that late charges are not interest may lead utilities to impose a non-recurring late charge, and the practice can logically serve as “proof” that there is no interest either intended or actual. Conversely, the perception of late charges as interest may lead to the imposition of a recurring charge with the effect that the practice can serve as proof that they are interest. Whatever the requirements of logic, the predominant holdings seem to say that a non-recurring late charge is not interest.

5. CONSUMER CONTROL

A final line of reasoning used to argue that late charges are not interest is that payment of the late charge is within the control of the payor who, presumably, could pay by or on the due date.¹¹⁸ Although no decision appears to have turned on this argument, three points merit discussion. First, at issue is the nature of the system, not the consumer's options. Even though incurring an obligation to pay interest is always within the control of the payor, that factor alone does not conclusively rebut the interest identification and usury allegation. Second, the customer's delay does reduce the effective rate of interest in the case of the nonrecurring charge, because the flat-rate single charge applies to an increasing period of time.¹¹⁹ Third, the very lessening of the effective rate of interest implies that the nonrecurrence of the charge is dysfunctional in pressuring the customer to delay payment no further.¹²⁰

117. Written comments by Arkansas Consumer Research Regarding Issues Raised by the Commission's October 1977 Order at 11, Revised Rules and Regulations Governing Utility Service, No. U-2888 (Ark. P.S.C., comments dated Jan. 20, 1978); W. VA. PUBLIC SERVICE COMMISSION, RULES & REGULATIONS FOR THE GOVERNMENT OF WATER UTILITIES Rule 403.3 (1977).

118. Memorandum Brief at 13, 15, Odell Smith, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969); Transcript of Proceedings at 24-26, Benham v. City of Cleveland, No. 914,017 (Ohio Cuyahoga County Ct. C.P. Feb. 3, 1977).

119. Samuels, *supra* note 2, at 1156-57.

120. Direct Testimony and Exhibits of Dr. Frederick J. Wells, Appendix D to Com-

To argue, therefore, that the late charge is not interest because it is within the control of the payor emphasizes the customer's ability not only to avoid any late charge but also, by calculated delay, to take advantage of the nonrecurring nature of the charge. Thus, this argument indirectly and ironically makes the dysfunctional character of a nonrecurring late charge as an inducement to prompt payment a ground for not identifying the late charge as interest.

D. *Interest and Usury*

The predominant course of commission and court decisions has been to assert cost-recovery-and-allocation and promptness-inducement theories and to deny extension-of-credit, use-of-money, and forbearance arguments.¹²¹ A number of decisions, however, have found late payment charges to be interest. Two recent lower courts, moreover, in addition to the court of appeals in *Guste*, went one step further and found late payment charges to be usurious.¹²²

It is not surprising that private plaintiffs identify late charges as usurious interest in cases brought specifically on usury grounds,¹²³ but several state officials, including the state attorney general in *Guste*,¹²⁴ the attorney generals of Kansas¹²⁵ and Iowa,¹²⁶

plaint, *Sabur v. Commonwealth Edison Co.* (Ill. Com. Comm'n, filed June 28, 1974); Samuels, *supra* note 2, at 1155-56.

121. See cases cited note 109 *supra*. See also 1972 NARUC REPORT, *supra* note 5. In *Rangeley*, the Maine Commission held an eighteen percent per annum rate less appropriate than one percent per month. Also noteworthy is the Commission's condemnation of the company's extending interest-free loans to the owner and to other companies owned by him while the company was having financial difficulties. 9 Pub. U. Rep. 4th at 299.

Another argument that late charges are not interest, and therefore not usurious, is that payment of the late charge is within the control of the payor who, presumably, could pay by or on the due date. Memorandum Brief at 13, 15, Odell Smith, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969); Transcript of Proceedings at 24-26, *Benham v. City of Cleveland*, No. 914,017. It appears that the utility in *Guste* also made this argument. 297 So. 2d at 524. No decisions, however, appear to have turned on this argument.

Almost all recent usury cases have involved high nonrecurring rates; an exception is *State ex rel. Utilities Comm'n v. North Carolina Consumers Council, Inc.*, 18 N.C. App. 717, 198 S.E.2d 98 (1973) (the court followed *Coffelt* and upheld the North Carolina Commission's charge of one percent per month after a 25-day due and payable period).

122. *State ex rel. Turner v. Town of LeGrand*, No. 32857 (Iowa Marshall County Dist. Ct. Jan. 3, 1978); *State v. City of Altoona*, No. CE-7-3671 (Iowa Polk County Dist. Ct. 1977), *rev'd*, 274 N.W.2d 366 (Iowa 1979).

123. See, e.g., Memorandum of Intervenor at 3, Odell Smith, 78 Pub. U. Rep. 3d 317 (Ark. P.S.C. 1969); Plaintiff's Motion for Summary Judgment, *Benham v. City of Cleveland*, No. 914,017.

124. 297 So. 2d 518 (La. Ct. App. 1974).

125. *Kansas Gas & Elec. Co.*, No. 96, 137-U (Kan. Corp. Comm'n Apr. 3, 1974).

126. *State ex rel. Turner v. Younker Bros.*, 210 N.W.2d 550 (Iowa 1973). See also 1975 NARUC REPORT, *supra* note 4, at 17, 24.

and the Wisconsin Department of Justice,¹²⁷ also have argued that late charges constitute interest and are usurious. The 1972 NARUC Ad Hoc Committee Report stressed the interest nature of the late payment charge, despite not concluding that such a charge may be usurious.¹²⁸ One court acknowledged that "computations may create an effective rate of interest,"¹²⁹ although it refused to hold that late charges constituted legal interest. In a rulemaking decision, however, the Utah Commission not only required that late charges be expressed in annual percentage rates, but also referred to the late charges as finance charges.¹³⁰ Other commissions in Georgia,¹³¹ North Carolina,¹³² New York,¹³³ Connecticut,¹³⁴ and Maine¹³⁵ went even further and specifically identified late charges as interest.

Finally, in two separate actions, two Iowa district courts ruled that the late charges of two municipal utilities violated the usury statute.¹³⁶ In one, the court found that since anyone could assert a wish not to extend credit, such a defense would only permit "wholesale evasion of the Usury Statute," and that forbearance was present within the meaning of that statute.¹³⁷ It is important to note that the Iowa Supreme Court had previously negated the

127. Brief of the Wisconsin Department of Justice, Wis. Billing Practices Investigation, *supra* note 51.

128. 1972 NARUC REPORT, *supra* note 5.

129. *Benham v. City of Cleveland*, No. 914,017, slip op. at 2.

130. Proposed Residential Utility Service Regulations, *in re* the Adoption and Promulgation of Rules, Regulations and Standards of Service for Public Utilities Relating to Termination of Service for Non-Payment, Security Deposits, Billing Procedures, Complaints, and Information, No. A67-05-32 (Utah P.S.C.).

131. *Atlanta Gas Light Co.*, 17 Pub. U. Rep. 4th 421 (Ga. P.S.C. 1976).

132. N.C. Uniform Billing Procedure Investigation, *supra* note 60.

133. Memorandum Approving Late Payment Charge, Long Island Lighting Co., No. 27237 (N.Y. P.S.C. Sept. 14, 1977).

134. *Hartford Elec. Light Co.*, No. 11553 (Conn. P.U.C. Oct. 7, 1974) (approving 1% per month late payment charge for nonresidential customers); *Hartford Elec. Light Co.*, No. 760605 (Conn. P.U.C. Dec. 22, 1976) (terminating late payment charge applicable to commercial and industrial customers); *Hartford Elec. Light Co.*, No. 770320 (Conn. P.U.C. Oct. 25, 1977) (reinstating late payment charge for commercial and industrial customers). The same sequence characterizes commission decisions in *Connecticut Light & Power Co.*, No. 11552 (Conn. P.U.C. Oct. 7, 1974); *Connecticut Light & Power Co.*, No. 760604 (Conn. P.U.C. Dec. 22, 1976); *Connecticut Light & Power Co.*, No. 770319 (Conn. P.U.C. Oct. 25, 1977). See also *Southern Conn. Gas Co.*, No. 11731 (Conn. P.U.C. Nov. 28, 1975) (approving 1% per month late payment charge).

135. *Central Maine Power Co.*, 8 Pub. U. Rep. 4th 277 (Me. P.U.C. 1975).

136. *State ex rel. Turner v. Town of LeGrand*, No. 32857 (Iowa Marshall County Dist. Ct. Jan. 3, 1978); *State v. City of Altoona*, No. CE-7-3671 (Iowa Polk County Dist. Ct. 1977), *rev'd*, 274 N.W.2d 366 (Iowa 1979).

137. *State v. City of Altoona*, No. CE-7-3671, slip op. at 5.

time-price doctrine for retail sales.¹³⁸

IV. THE QUESTION OF STATUTORY EXEMPTION: POLITICS AND POLICY

The two Iowa district court cases discussed in the preceding paragraph arose from a somewhat anomalous situation. Chapter 537 of the Iowa Consumer Credit Code specifically exempts late payment charges from its eighteen percent per annum ceiling.¹³⁹ Such charges, however, are not explicitly exempted from the nine percent per annum ceiling imposed by the usury statute, chapter 535.¹⁴⁰ The differing treatments in chapters 535 and 537 permitted the specific holdings.¹⁴¹ The anomaly, which perhaps accounts for the unusual findings of usury in the Iowa cases, better illustrates the more general result, in which reliance upon one or another statutory exemption prevents a finding of usury.

Courts and commissions can avoid applying interest and credit rate ceilings to utility late payment charges by finding the late charges specifically exempted by statute. For example, public utilities are free from the restrictions of the Federal Truth in Lending Act because the Act specifically excludes "[t]ransactions under public utility tariffs, if . . . a State regulatory body regulates the charges for the public utility services involved [and] the charges for delayed payment"¹⁴² The Johnson Act withdraws federal court jurisdiction from cases involving state orders affecting public utility rates.¹⁴³

On the state level, some courts and commissions approach the usury issue in public utility late payment charges by looking to the relation of laws regulating interest and credit terms to public utility regulation in general. A Connecticut court, for example, ruled that the state truth in lending act "expressly exempts 'charges for delayed payment and any discount allowed for early payment' under utility rate schedules regulated by a state agency."¹⁴⁴ In

138. *State ex rel. Turner v. Younker Bros.*, 210 N.W.2d 550 (Iowa 1973).

139. IOWA CODE § 537.1202(3) (1975).

140. *Id.* § 535.4 (1975).

141. Letter from Maurice Van Nostrand, Chairman of the Iowa State Commerce Commission, to Dr. Warren J. Samuels (Feb. 13, 1978).

142. 15 U.S.C. § 1603(4) (1976); see *Ferguson v. Electric Power Bd.*, 378 F. Supp. 787, 790 (E.D. Tenn. 1974).

143. 28 U.S.C. § 1342 (1976); see *Tennyson v. Gas Serv. Co.*, 506 F.2d 1135, 1137 (10th Cir. 1974) (court held Johnson Act removed the district court's jurisdiction over an action challenging the legality of a utility late payment charge) (alternative holding).

144. *City of Hartford v. Hartford Elec. Light Co.*, No. 112008, slip op. at 19 (Conn.

State ex rel. Guste v. Council of New Orleans, the Supreme Court of Louisiana pointed out that the usury laws apply to loans, not to consumer credit sales, that the latter are governed by the state's consumer credit law, and that the consumer credit law exempts public utility rates regulated by other means.¹⁴⁵ In *Jones v. Kansas Gas & Electric Co.*,¹⁴⁶ the Supreme Court of Kansas held that since public utilities were regulated by state agencies vested with "the authority to supervise operation of the utility, subject to judicial review of the reasonableness of the rate,"¹⁴⁷ public utility late payment charges were exempt from the restrictions of the Kansas Uniform Consumer Credit Code.¹⁴⁸

Similarly, the Wisconsin Power & Light Company argued before the Wisconsin Public Service Commission that the Wisconsin Consumer Act specifically exempts from the scope of the Act "[c]harges for delayed payment and any discount allowed for early payment in transactions under public utility or common carrier tariffs if a subdivision or agency of this state or of the United States regulates such charges or discounts."¹⁴⁹ In reply to that defense, the Wisconsin Department of Justice argued that:

[i]t is true that the United States Congress and the Wisconsin Legislature have excluded public utility late payment charges from the application of Truth in Lending . . . and the Wisconsin Consumer Act . . . , but *only if* such charges are otherwise regulated by a governmental agency. The inference is clear that if the Public Service Commission does not intend to regulate the late payment charges of the public utilities, such charges will come within the purview of the laws which generally regulate the extension of consumer credit. Moreover, the applicability of Chapter [sic] 138, Wis. Stat., entitled Money and Rates of Inter-

Hartford County Ct. C.P. Mar. 29, 1976).

145. 309 So. 2d 290, 296 (La. 1975). The reasoning that late charges are excluded from the reach of statutes that otherwise would control them parallels the argument that company tariffs for late payment charges approved by regulatory commission rules are thereby exempt from other control. Thus, regulation per se prevents the utility from receiving greater profit than allowed by law, thereby negating the charge of usury. *Id.* The more general reasoning is that late charge provisions are within the category of regulated rates and therefore are not legal interest. *Ferguson v. Electric Power Bd.*, 378 F. Supp. 787, 789-90 (E.D. Tenn. 1974); *Central Hudson Gas & Elec. Corp. v. Napoletano*, 277 A.D. 441, 101 N.Y.S.2d 57 (1950); *Delich v. Iowa Elec. Light & Power Co.*, 9 Pub. U. Rep. 335, 341-42 (Iowa Com. Comm'n 1975).

146. 222 Kan. 390, 565 P.2d 597 (1977).

147. *Id.* at 397, 565 P.2d at 604.

148. KAN. STAT. ANN. §§ 16a-1-101 to -9-102 (1974 & Supp. 1979).

149. WIS. STAT. ANN. § 421.202(3) (West 1974) (amended 1975), *quoted in* Brief for Wisconsin Power and Light Co. at 2, Wis. Billing Practices Investigation, *supra* note 51.

est, to public utility net-gross charges remains an open and unresolved question.¹⁵⁰

But the Wisconsin Public Service Commission ignored this argument in its decision.¹⁵¹

The debate over the nature of late payment charges also raises a question about the relationship between municipal and state authority. In the Iowa cases, one district court stated that it opposed repeal of the usury statute by implication and that "[t]here seems nothing intrinsic in the grant of power over rates to the defendant City of Altoona, including late charges, as to require the partial nullification of the Usury Statute which has general application to all contracts, unless otherwise excepted by statute."¹⁵² The other Iowa district court emphasized that the authority of the city was not superior to that of the state.¹⁵³ In *Benham v. City of Cleveland*,¹⁵⁴ the court ignored the issue, even though it was elaborately debated in the briefs. The plaintiff argued that city authority in the area of utility regulation was subject to the general regulatory measures of the state under its police power. One of those regulatory measures was the usury statute.¹⁵⁵ The attorney for the defendant City of Cleveland argued the opposite view:

[A] municipal corporation is free to operate [a utility] without restrictions or qualifications by the General Assembly.

. . . .

If the usury statute were held applicable to the billing procedure, the effect of such applicability would be that the General Assembly would be preempting a municipality in a determination as to how that municipality can best further a very important interest.¹⁵⁶

Case law evidences the ability of the federal and state statu-

150. Brief for the Wisconsin Department of Justice at 5, Wis. Billing Practices Investigation, *supra* note 51.

151. Wis. Billing Practices Investigation, *supra* note 51.

152. State v. City of Altoona, No. CE-7-3671, slip op. at 7 (Iowa Polk County Dist. Ct. 1977), *rev'd*, 274 N.W.2d 366 (Iowa 1979).

153. State *ex rel.* Turner v. Town of LeGrand, No. 32857 (Iowa Marshall County Dist. Ct. Jan. 3, 1978).

154. No. 914,017 (Ohio Cuyahoga County Ct. C.P. Feb. 3, 1977).

A short time earlier, the Iowa Supreme Court had avoided the issue by holding that "the commission's jurisdiction should have been exhausted before this suit was brought." State *ex rel.* Turner v. Iowa Elec. Light & Power Co., 240 N.W.2d 912, 914 (Iowa 1976).

155. Plaintiff's Motion for Summary Judgment at 4, *Benham v. City of Cleveland*, No. 914,017.

156. Transcript of Proceedings at 15, 19-20, *Benham v. City of Cleveland*, No. 914,017.

tory exemptions to defend late payment charges against usury attacks. Some uncertainty remains, however, about the status of a municipality's rules as compared with a state's usury statute. This situation raises three interesting and important considerations. The first concerns the tendency of commissions and courts to deal directly with the substantive issues in face of the usually available and less demanding recourse to statutory exemptions as a decisional ground. This tendency is not of much present concern, since there appears to be a desire to settle the issues on the perceived legal merits. Secondly, the implication from these statutory exemptions is that late payment charges constitute interest and come within the ambit of the usury statutes. Indeed, as one Iowa district court concluded, "the matter of public utility late charges and discounts was thought to involve interest by the Iowa Legislature. It excepted such matters from coverage of the Consumer Credit Code The legislature did not then or otherwise except such from coverage under [Iowa's usury statute]."¹⁵⁷

Third, the foregoing implication relates to the role of politics and policy in the area of public utility late charges. The central point is that utility billing and collection systems are a matter of policy. It is perhaps likely that only half of the electric and gas utilities have late payment charges and that only one state in four

157. *State v. City of Altoona*, No. CE-7-3671, slip op. at 2 (Iowa Polk County Dist. Ct. 1977), *rev'd*, 274 N.W.2d 366 (Iowa 1979).

With respect to the *Jones* case, one commentator has written that:

[E]ven if the charges were interest, they would not be usurious. [The *Jones* court] noted that the Uniform Commercial Credit Code (U3C) and Truth in Lending Acts have displaced the usury statute for purposes of consumer transactions, which, the court suggested, include sales by utilities to consumers. The court then reasoned that because utility companies are expressly excluded from coverage by those two consumer protection laws, the companies may escape the coverage of the general usury statute as well. Thus, utility regulations appear to float in a statutory vacuum between consumer protection acts, from which they are exempt, and the state usury law, which the court concluded is inapplicable.

....
The exclusion of utility rates from the U3C would appear to throw them back into the field of general transactions that are subject to general laws. Section 16a-1-103 of the U3C, which makes general principles of law applicable '[u]nless displaced by the particular provisions of [the uniform consumer credit code],' supports that conclusion. Given that utility rates are excluded from the scope of consumer protection legislation, it seems illogical for the court to call on those acts to shelter the rates from scrutiny under the general usury statute.

... And even the conclusion that the Kansas Corporation Commission properly has exclusive power to regulate rates does not logically lead to the result that the Commission has the power to do so without reference to general statutes.

Note, *supra* note 2, at 599-600 (Footnotes omitted).

forbids such charges entirely.¹⁵⁸ Whether collection pressure through a charge for late payment is superior to the threat of disconnection is a matter of judgment;¹⁵⁹ and such judgment is a matter of policy for legislatures, commissions, and courts.

The legislative adoption of a late charge system, or, more correctly, of statutory provisions enabling the same, has been a matter of considerable political pressure and lobbying. A member of the Maryland House of Delegates remarked that "the late payment rates resulted from 'the heavy utility lobby in Maryland,'"¹⁶⁰ and a Maryland utility representative has argued that reform efforts in Maryland were due to political pressures from a liberal commission decision in the District of Columbia.¹⁶¹ In at least one instance, state regulatory commission rules governing late payment charges were "largely the result of negotiations between interested parties, including intervening consumer-interest groups."¹⁶² It is quite possible, therefore, that suits brought by several state attorney generals to challenge late payment charges under the usury statutes were motivated by a desire to fashion a pro-consumer public image with a view towards re-election.¹⁶³

Of more immediate importance is the reality that statutory exemptions have been the result of considerable political pressure. The activities of NARUC in support of the exemption of public utility late payment charges from the Federal Truth In Lending Act are a good example. In early 1972, both the president and the general counsel of NARUC lobbied against the proposal by Senator Lee Metcalf to delete the exemption.¹⁶⁴ They argued, *inter alia*, that the amendment would require utilities not only to comply with the Truth in Lending Act, but also to comply with the Fair

158. NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS, 1977 ANNUAL REPORT ON UTILITY AND CARRIER REGULATION 521-22, table 47(a); Samuels, *supra* note 2, at 1152.

159. Utah Power & Light Co., 19 Pub. U. Rep. 2d 369, 373 (Utah P.S.C. 1937).

160. NARUC BULL. No. 24-1972, *supra* note 49, at 21.

161. Transcript of Hearing at 393-94, Md. Late Payment Charge Investigation, *supra* note 96.

162. Letter from C. Burton Nelson, Chairman of the Illinois Commerce Commission, to Dr. Warren J. Samuels (Feb. 2, 1979).

In Missouri, the State Public Service Commission reached a compromise with utility companies on an earlier commission order dealing with billing practices after several companies filed a civil suit against the order. Letter from Charles J. Fraas, Jr., Chairman of the Missouri Public Service Commission, to Dr. Warren J. Samuels (Apr. 21, 1978).

163. Admittedly, this supposition is highly speculative. But it is one explanation for the suits brought under the aegis of the usury laws despite the overwhelmingly adverse case law.

164. 118 CONG. REC. 14831 (1972).

Credit Billing Act, thereby "wreaking havoc with practices required by the present regulators and ignoring present local practices which have wide consumer acceptance. . . . [S]uch a concentration of regulatory power in the Federal Government is unwarranted because such billing practices are now subject to comprehensive state regulation."¹⁶⁵ The NARUC position was apparently motivated chiefly by a desire to retain state regulatory jurisdiction and decisionmaking authority. Indeed, the NARUC Ad Hoc Committee on Utility Billing Practices forthrightly acknowledges that its initial creation and continuing existence is due to a "good faith" response to the effort to remove the public utility exemption, and claims credit for persuading Senator Metcalf to withdraw his amendment.¹⁶⁶ The irony of this episode is that the original NARUC committee reached substantive conclusions and policy recommendations that would have drastically revised utility late charge payment practices.¹⁶⁷ Their report had a negative effect on the 1972 convention and ultimately led to an expansion of the committee's membership and more conservative recommendations as a countermeasure. The original report characterized net-gross differentials as an interest charge for the extension of credit,¹⁶⁸ while the 1975 Report concluded that the differentials were an inducement to prompt payment.¹⁶⁹ The former view would have undercut the statutory exemption argument and reinforced the arguments in favor of usury control. Thus, even though both the 1972 and the 1975 Reports advocated a policy of full disclosure, the question of repeal of the statutory exemption now appears settled.

Public policy and law in this area are not solely matters of choice between perceptions embodied in legal semantics, but also consequences of political strategy and pressure. The law regulating public utility late payment charges and usury is clearly a matter of policy.

V. THE EFFECTIVE RATE OF INTEREST

The legal identification of the late payment charge as interest

165. Letter to Honorable John J. Sparkman, Chairman of the Committee on Banking, Housing & Urban Affairs, from Francis Riordan, President of the National Association of Regulatory Utility Commissioners (Mar. 14, 1972), *quoted in* 118 CONG. REC. 14831 (1972).

166. 1975 NARUC REPORT, *supra* note 4, at 1; 1972 NARUC REPORT, *supra* note 5, at 2 n.9.

167. 1972 NARUC REPORT, *supra* note 5, at 9-11.

168. *Id.*

169. 1975 NARUC REPORT, *supra* note 4, at 3.

poses only the first general problem in determining the applicability of the usury law. The second general problem is the calculation of a meaningful effective annual rate of interest for comparison with the limit imposed by the usury law. The calculation requires the solution of a number of problems.

For a recurring charge of one and one-half percent per month, the calculation of an effective annual rate is straightforward. One multiplies the monthly rate by the number of months in a year: one and one-half percent times twelve, or eighteen percent. Unlike a nonrecurring late charge, which commences with the passing of the due and payable period, the recurring charge becomes payable only when the customer fails to pay the past due bill by the billing date of the next bill; thus, no charge less than the monthly effective rate is calculable. The amount to be paid in late charges accumulates at an effective annual rate each month.

In comparison, a nonrecurring charge of five or ten percent can produce an extremely high effective annual rate, depending on how long payment is delayed. A five percent late charge paid after five, fifteen, or thirty days' delay yields effective annual rates of 360%, 120%, or 60%, respectively. The great majority of late payers do, however, remit within one month and thus face an effective annual rate of 120%, assuming a five percent late charge and a fifteen-day due and payable period.¹⁷⁰ Such rates are well above

170. See Samuels, *supra* note 2, at 1156-57.

The State of West Virginia provides that "[o]n all accounts not paid in full within twenty (20) days of the billing date, a ten percent (10%) penalty may be added to the net amount shown. This delayed payment penalty is not interest and is only to be collected once for each bill where it is appropriate." WEST VIRGINIA PUBLIC SERVICE COMMISSION, RULES AND REGULATIONS FOR THE GOVERNMENT OF WATER UTILITIES Rule 4.03(3) (1977). The recurring or nonrecurring character of the late charge is, however, ambiguous. In a recent case, the West Virginia Commission commented on the ten percent per month charge on unpaid water bills. The commission stated that "[a] delayed payment penalty is not supposed to be interest and is not supposed to be charged but once [*sic*]. Of course, if a second month's bill is also delinquent, a delayed payment penalty may be charged for that." The commission found that "[a] penalty of ten percent (10%) will be added to all bills not paid within fifteen (15) days of the date thereof." Jane Lew Water Comm'n, No. 7554 (W. Va. P.S.C. Apr. 30, 1973).

In comparison, the Wisconsin Commission has said:

A late payment differential has as its primary purpose the encouragement of prompt payment. An amount unpaid over two or more billing cycles should not bear two or more late payment charges on any one specific amount outstanding, as it is not the intended function of these charges to serve as interest on a loaned balance. It is reasonable that a late payment charge be applied only once on any given amount outstanding.

Slip op. at 5-6, Wis. Billing Practices Investigation, *supra* note 51. The more conventional device is a flat-rate late charge applied only once.

the rates contemplated by the usury statutes.

As has been illustrated, the effective annual rate decreases with the prolonging of customer delay. Not only is the nonrecurring nature of a late charge dysfunctional for pressuring the tardy payer to remit, but the effective annual rate will eventually fall below the ceiling rates of the usury statutes. A five percent charge, for example, yields an effective annual rate of ten percent when payment is delayed six months, but five percent when delayed one year. Such a decline affects relatively few late payers, however, because the utility will disconnect service and either collect reconnection fees or write off the late charge as an uncollectible.

A number of persons and groups have called for the disclosure of the effective annual rate for recurring and nonrecurring late charges. Calculation in the latter case is difficult because the effective annual rate varies with the period of delayed payment, whereas the recurring charge increases measurably over time at a constant annual rate. Empirical data on actual customer payment performance nevertheless enables the calculation of an approximate effective annual rate.¹⁷¹

Below are two tables that use data provided by two companies in response to a suit challenging their late payment practices.¹⁷² Each table assumes that late payment is on the last day of each period and, in the alternative, that late payment is on the midpoint date of each period. For each of these assumptions the effective annual rate is calculated using a flat-rate late charge of five percent with a twenty-day due and payable period for Company A, and a fifteen-day due and payable period for Company B. These rates are then weighted in accordance with the actual proportion of late payors for each indicated period. The actual averages of the weighted effective rates are 70.5% and 128.5% for Company A and 50.8% and 96.0% for Company B. The lower percentages apply to payments on the last day of each period and the higher percentages apply to payments on the midpoint date. These rates, of course, are clearly higher than those allowed by the state usury

171. 1972 NARUC REPORT, *supra* note 5, at 4.

172. Transcript of Hearing at 5-7, Md. Late Payment Charge Investigation, *supra* note 96.

statutes, which range from six to ten percent per annum.¹⁷³

TABLE

(Left column: assume payment on last day of period; right column: assume payment on mid-point date.)

<i>Company A</i>					Weighted Effective	
Days		Effective Rate (%)		Performance (%)	Annual Rate (%)	
0		—	—	59	—	—
20	10	90	180	18 (62%)	55.8	111.6
30	25	60	72	3 (10%)	6.0	7.2
40	35	45	51	2 (7%)	3.2	3.6
50	45	35	40	2 (7%)	2.5	2.8
60	55	30	33	3 (10%)	3.0	3.3
70	65	25	28	1 (3%)	.0075	.0084
					70.5%	128.5%
<i>Company B</i>						
0	0	—	—	79	—	—
29	15	60	120	15 (71%)	42.6	85.2
59	45	30	40	5 (24%)	7.2	9.6
89	75	20	24	1 (5%)	1.0	1.2
Over 90	—	(omit)	(omit)	0.2	(omit)	(omit)
					50.8%	96.0%

(Note: "Omit" lowers effective rate.)

VI. CONCLUSION

The purpose of this article is not to reform the law of usury, but rather to interpret and criticize the application of that law to public utility late charges. Several conclusions follow from the preceding discussion.

First, control of interest through usury law in the United States has generally been ineffective. The maximum lawful rates established by state usury laws have been widely compromised by other provisions, such as the time-price doctrine, which effectively exempt many transactions from the reach of the usury law. Consequently, usury law as applied to late charges, and perhaps in general, is confused and contradictory.

173. *Id.* at 6-7.

An interesting ambiguity is provided by MD. ANN. CODE art. 78, § 54C (Supp. 1980), which provides "that any additional charge shall not exceed five percent (5%) of the net part of the bill." A flat five percent charge without reference to *any period* is analytically meaningless. One could interpret it to impose a limit of either five percent per year or five percent per month. The Maryland Commission has regarded the five percent as an upper limit on a recurring charge, although it also has permitted flat rate charges of five percent (within each billing period), which may produce effective *annual* and *monthly* rates far in excess of five percent.

Second, there has been a renewed attack on public utility late charges on usury grounds during the last decade. This attack, however, has largely been unsuccessful. Reform has come through commission and court action lengthening the due and payable period, lowering the nonrecurring late charges, favoring recurring or time-differentiated late charges, and fostering the adoption of rules governing termination and disconnection procedures. Commissions and courts have also been persuaded of the validity of the time-use doctrine, the need to distinguish between classes of late payers, and the dysfunctional, if not discriminatory, nature of nonrecurring late charges. The combination of statutory exemptions and competing perceptions of late payment charges, however, is likely to preclude any change in the usury status of the late payment charge. The consumer movement, moreover, has not focused on reforming the law on late charges. To the extent that public-interest and legal-aid attorneys have been active in this area, their successes have come largely through commission complaints, intervention in rate cases, and litigation on grounds other than usury.

Finally, late charge systems, as well as the usury issue, rest on policy considerations. Rules, doctrines, and definitions are not the only means by which cases are decided; law is not only a system of abstract rights and reasoning, but also a system for the accommodation of selective perceptions and special interests.