HUMIKO KINGZIO, ANTONIO MARBOU and EICHI MOBE, on behalf of themselves and other similarly situated and injured persons, Plaintiffs

v.

THE BANK OF HAWAII, KOROR BRANCH, Defendant

Civil Action No. 569

Trial Division of the High Court

Palau District

October 4, 1973

Class action alleging usury in bank loans. The Trial Division of the High Court, D. Kelly Turner, Associate Justice, held that "add on" method of computing interest on loans made by bank sued by borrowers who claimed usurious interest was charged, was in violation of usury statute limiting interest to one percent per month on the balance due, where the interest for each month's payment was calculated on the entire amount of the loan without taking into account the diminishing balance due.

1. **Civil Procedure—Class Actions—Maintainability**

   The hearing of a motion for summary judgment in favor of persons bringing a class action constitutes a determination by the court that the action is maintainable, and neither the territory nor federal rules require a prior determination that a class action is maintainable. (Rules Civil Procedure, Rule 5)

2. **Contracts—Usury**

   "Add on" method of computing interest on loans made by bank sued by borrowers who claimed usurious interest was charged, was in violation of usury statute limiting interest to one percent per month on the balance due, where the interest for each month's payment was calculated on the entire amount of the loan without taking into account the diminishing balance due. (33 TTC § 251)

3. **Evidence—Best Evidence**

   Where bank's loan records conflicted with deposition of bank officer, court must, in deciding motion for summary judgment, accept the records, not what officer said about the loans.

4. **Contracts—Usury**

   Interest is not an element of usury. (33 TTC § 251)

5. **Contracts—Usury**

   Bank intended the consequences of its acts in making usurious loans; its collection of usurious interest was the intended result. (33 TTC § 251)

6. Contracts—Usury

A right of action created by statute need not exist before usurious interest can be recovered, and where statute only allows the usurious interest as an offsetting credit when a borrower sues a lender, borrower may sue at common law for recovery of usurious interest. (33 TTC §§ 251, 252)

7. Contracts—Usury

Usury, being a criminal offense, is against public policy, and thus a usurious loan is a contract which will not be enforced; so that plaintiffs to whom bank made loans at usurious rates were entitled to recover all interest paid, since one may sue to recover that which was paid under an unenforceable contract. (33 TTC §§ 251–253)

Counsel for Plaintiffs: DENNIS F. OLSEN and DONALD JUNEAU
Micronesian Legal Services Corporation
Counsel for Defendants: CRAIN, RATHBUM & SHOECRAFT by
ROBERT K. SHOECRAFT

TURNER, *Associate Justice*

This was a class action brought pursuant to Trust Territory Rule 5, Rules of Civil Procedure, by the plaintiffs in behalf of themselves and all other persons in the Palau District who having obtained loans from the defendant bank paid allegedly usurious interest thereon. The record shows the bank made 2034 loans from the enactment of the usury statutes, February 15, 1965, to June 22, 1972, at which time, after the complaint had been filed, the bank changed its method of calculating and charging interest. Of the loans made, 1,234 were for more than $300.00. The interest on such loans is limited to one percent per month "on the balance due." 33 TTC § 251.

Payments made "by way of usurious interest" are to be credited as payments on the principal, 33 TTC § 252, and receipt of interest in excess of two percent per month on any loan amount is punishable as a criminal offense upon conviction. 33 TTC § 253.

The Trust Territory statute, like many in the United States, makes no mention of recovery of usurious interest paid, thus limiting its effect to an offsetting credit when the lender sues the borrower upon default of principal and interest payments. The common law rule is that the borrower is entitled to recover when the interest has been fully paid before suit is brought and there is no statutory provision for recovery of interest paid. In specific point is *Lee v. Hillman*, (Wash.), 133 P. 583:—

"Our statute contains no express provision relating to the right of the payer of usurious interest to maintain such an action . . . it has been uniformly held in this jurisdiction that usurious interest could at common law be recovered back in an action brought for that purpose."

The subject is extensively annotated in 59 A.L.R.2d 522, "*Right* in *Absence* of *Statute Expressly So Providing* to *Recover Back Usurious Payments.*" The annotation says:—

"It has been universally held, where statutes forbid the taking of excessive interest, and punish a violation of their provisions by the infliction of fines, penalties, or forfeitures upon the person who takes it, that the person who pays the same may, independently of the remedies afforded by the statutes, maintain an action for money had and received, at the common law, to recover back the money so paid."

The defendant cites an early California Case to the effect recovery of usurious interest may not be obtained. *Willox v. Edwards*, 123 P. 276. This case related to recovery of money under a state constitutional provision pertaining to the illegal sale of securities. It is not in point on the issue of recovery of usurious interest.

Whatever doubt the cited case may have raised as to the California law is removed without reference to defendant's cited decision by the opinion in *Stock v. Meek*, 221 P.2d 15, 20:—

"Borrowers may therefor bring an action for money had and received to recover usurious interest paid within two years of the suit."

Plaintiffs' filed motion for summary judgment to recover the loan interest paid by plaintiffs and for all other borrowers whom they represented. The motion was based upon the pleadings, the deposition and exhibit obtained from the Koror manager of the defendant bank and the affidavits filed in behalf of the parties. The motion stated the appropriate grounds for summary judgment, that there was no genuine issue as to any material fact and that the plaintiffs were entitled to a judgment as a matter of law. Summary Judgment is provided for under Rule 56, Federal Rules of Civil Procedure, which is made applicable to an appropriate case by Trust Territory Rule 8, Rules of Civil Procedure.

Summary Judgment was held to be available as a matter of law when no factual issue was raised in the appellate division case, *Guerrero Family Inc. v. Micronesian Line Inc.*, 5 T.T.R. 87. Federal rule 56(c) specifies the requirement for a summary judgment decision.

Defendant bank resisted the motion for Summary Judgment on both procedural and substantive grounds. Defendant proposed a curious procedural defense, asserting that the general denial answer to the complaint, i.e., "Defendant demands trial," placed the propriety of a class action in issue. Defendant relied upon its interpretation of Trust Territory Rule 5 and Rule 23, Federal Rules of Civil Procedure, which it suggests governs the proceedings. Defendant claims judgment would be premature because the Court had not heard and determined that a class action is "properly maintainable, with notice to the members of the class, who may or may not wish to be represented." The argument, without supporting authority, raises two procedural

points, both of which are contrary to Federal decisions dealing with Rule 23.

Trust Territory Rule 5 requires the class be "so numerous as to make it impracticable to bring them all before the court." Since defendant's evidence, given in deposition, shows a minimum of 1,234 borrowers of more than $300.00 each, the first requirement of the rule is met.

[1] The second requirement is that the representative of the class will insure adequate representation of all. The question of law—did the bank's method of charging interest result in a usurious exaction—is common to all of the class and a decision for the named plaintiffs is necessarily binding upon all borrowers represented. This common question of fact and law also meets the requirements of the Federal rule. Neither the Trust Territory, nor Federal rules make mandatory a hearing and a court determination that the class action is "maintainable" and that notice be given to the class. Hearing a motion for summary judgment constitutes a determination by the court the action is maintainable. As to notice it was held in *Eisen v. Carlisle and Jacquelin*, 52 F.R.D. 253, 266:—

> "Consequently, where a class consists of a large number of claimants with relatively small individual claims, notice to individual class members, as a legal and practical matter, becomes less important and need not be unduly emphasized or required."

Also, see, *Koehler v. Ogilvie*, 53 F.R.D. 98. *Zachary v. Chase Manhattan Bank*, 52 F.R.D. 532.

The substantive issue raised is whether there is a conflict of facts and whether as a matter of law the plaintiffs should prevail. As to disputed facts, defendants' general denial does not raise an issue of fact. It has been said in many decisions the court may pierce the pleadings to determine from depositions and affidavits whether issues of material facts actually exist. *Smoot v. Chicago R.I. & P.R.*

Co., 378 F.2d 879. *Zachry Co. v. O'Brien*, 378 F.2d 423. *Duarte v. Bank of Hawaii*, 287 F.2d 51, 53.

Pleadings alone do not determine whether there is an issue. The Federal Court said in *Byrnes v. Mutual Life*, 217 F.2d 497, 500:—

". . . resort is had to extrinsic facts through affidavits, admissions, and the like in order to find out if there is a real issue. This implies such a finding will be made despite the fact the pleadings as they stand present such issue."

Defendant insists, however, that the two affidavits which "explain" the bank's method of calculating interest precludes summary judgment. The bank's argument is not tenable. The basis of the contention is that the affidavit of plaintiffs' witness explaining the bank's method of calculating interest involves "expert testimony" and is therefor to be tested on cross-examination. Defendant also urges that the affidavit of the vice-president of the defendant bank which also "explains" the bank's method of charging interest is "contradictory" to that of plaintiffs' witness. If these two affidavits were, in fact, expert opinion neither one could be employed because when an expert opinion is offered, the jury or trier of fact may substitute its opinion for that of the expert. Neither of these affidavits are based on "expert opinion" in the legal sense. They both explain mathematical calculations and both reach the same factual result, with conflicting conclusions. The plaintiffs' accountant's affidavits concludes: "every loan made by the defendant bank recorded in said bank records exceeds this rate of interest. (Referring to the rate in 33 TTC § 251.)

The bank officer's affidavit argue there has been "compliance with the usury law" for loans of $300.00 or less but makes no conclusion as to the 1,234 loans in excess of $300.00. The banker did say:—

"in April, 1972, the bank voluntarily put into effect in its Micronesian branches a rate chart which would insure that all interest

charges would be in compliance with Title 33, Section 251 of the Trust Territory Code."

Plaintiffs' counsel notes the suit was filed April 21, 1972, and it was in that month the bank "voluntarily put into effect a rate chart which would insure that all interest charges would be in compliance" with the usury provision of the Code. The plaintiffs' conclusion seems inescapable:—

"The Bank thus explicitly admits that it has been consistently charging usurious interest prior to April, 1972, the plaintiffs' sole factual assertion."

[2] Without resorting to the conclusions of either plaintiff or defendant from the explanation of the method of calculating interest given in both plaintiff and defendant's exhibits, it is apparent to the court the bank's so-called "block/add on interest rate" is, as a matter of law, usurious for all loans payable monthly for an amount exceeding $300.00 at a rate in excess of 1 percent per month. The explanation given by the two affidavits of the method of calculating interest is the same, except the bank illustrates by an example of a loan of less than $300.00 for a one-year period at a rate of 10 percent, which computed as "add/on" is an annual percentage rate of 17.97 percent which is not usurious because the statute allows a rate of 2 percent per month for loans of $300.00 or under which is at an annual rate of 24 percent.

[3] The defendant officer's deposition and the loan records, attached as an exhibit to the branch manager's affidavit, are in conflict. The court must accept the bank's loan record, not what the defendant's officer says about its loans.

The so-called "add/on" calculation method has uniformly been held to be usurious when interest is calculated on the entire amount of the loan without taking into considera-

tion the diminishing balance due. The method is explained with illustrations from cases in an annotation at 57 A.L.R.2d 630, Usury—Interest in Advance. The bank loan records show all loans from February, 1965, when the usury statute became effective until April, 1972, when the method of calculating was changed, that the "amount of the loan" payable in installments includes interest which is then withheld as shown by the "net amount advanced" column.

The annotation points out at 57 A.L.R.2d 663, Sec. 10:—

> "As respects notes providing for the repayment of principal in installments, usury has resulted where the interest was deducted or taken in advance and computed as though the entire principal were to remain outstanding until the due date of the last installment, or otherwise not making proper allowance for the fact that the principal was being reduced during the period of the loan, requiring a proportionate reduction in the sum representing interest."

The court will not examine and comment on all of the loans disclosed by the bank records attached to the deposition. The first loan, made February 23, 1965, loan No. 39, at 7 percent per annum, interest for six months in the amount of $500.00, labeled by the bank as "net amount advanced," and the "amount of loan" of $517.50 illustrates the foregoing annotation statement. Six monthly payments of the loan and interest "added on" are $86.25 each. Six payments of the loan itself of $500.00 (regardless of how the bank labels it) are $83.33 each. On the monthly payments of $86.25, the bank is collecting $2.92 interest whereas under the statute, the bank is entitled to collect only 1 percent of the "balance due." The difference, in excess of the statutory limit is $2.09 for the six months as also is interest collected at the monthly amount of $2.92 in excess of 1 percent of the balance due after the third month.

The two decisions following illustrate the necessity of declaring the interest "add/on" method followed by the bank to be usurious under 33 TTC § 251 limiting interest to 1 percent of the "balance due."

In *Hallamon v. First State Bank of Stroud*, 389 P.2d 352, 355, the court said:—

". . . where the principal of a loan and interest thereon are payable in installments at specified intervals within the full loan period, and the interest is computed in such a manner that allowance has not been made for the reduction of the principal by reason of the installment payments, if such interest computed on the balance of the principal after each of the installments are paid, such plan is usurious."

Also in *Hayden v. Randles*, 80 P.2d 235, the court said:—

"When a note payable over a period of time, in installments, and interest at the highest contract rate is computed on the full amount without reduction thereof on account of partial payments, the plan results in the collection of usury."

[4] An examination of the bank's affidavit shows that these propositions of law are not disputed. What the bank's counsel did argue was that there is no usury without intent and that there is no right of action under the Trust Territory statutes to recover back usurious interest paid. The statutes only provide for offsetting credit of the usurious interest when the lender sues the borrower. Both propositions are contrary to the law.

In support of the theory intent must appear before usury can be found defendant cites an Arizona decision which does not so hold. That specific intent must be found is not the law in Arizona or elsewhere.

A recent pronouncement in Arizona is found in *Grady v. Price*, (1963) 383 P.2d 173, 176, where the court said:—

"Appellants argue that appellees failed to prove their intent to violate the usury statute. It is not necessary to show that the

appellants were conscious of the illegality of the transaction. 'It is sufficient (to show) that the loan contract unequivocally calls for an excessive rate of return on the indebtedness. In such case, the intent to exact usury is presumed.' *Britz v. Kinsvater*, 351 P.2d 986, 991."

In the case cited by defendant in support of the proposition intent must be found, *Houchard v. Berman*, 290 P.2d 735, 937, the court said:—

"If the face of the contract reflects a usurious charge, the intent will be presumed."

The court also said payment of interest in advance at the maximum rate "would be an usurious agreement, *Fagerberg v. Denny*, 112 P.2d 578, which renders all interest subject to forfeiture."

What misled defense counsel in the present case was that the Arizona Court held that the record in *Houchard* did not disclose whether or not the interest should be paid in advance. The record is clear in the present case that the Bank of Hawaii received (by withholding at the outset) all interest at the specified rate on the amount of the loan without any adjustment for the declining balance.

The Arizona rule is found in California also. In *Denny v. Hartley*, 315 P.2d 893, 895, the court said:—

"It is the rule, and has been so held many times in this state, that intent to execute a usurious rate of interest is conclusively presumed from a note or instrument which clearly shows on its face that it is usurious, and no evidence of intent or lack of such intent is required."

[5] The court holds the bank intended the consequence of its act. Its collection of usurious interest was the intended result. Any other intent is immaterial. *Thomas v. Hunt*, 269 P.2d 12, 16, and *Martin v. Kerchler*, 299 P. 52.

[6] Finally, the defendant's argument that without a right of action created by statute usurious interest may not be recovered. The law is to the contrary as demon-

strated in *Stock v. Meek*, supra, and in *Taylor v. Budd*, 18 P.2d 333, in which the court said that treble interest paid was recoverable under the statute for the year preceding the action, but prior to that, without benefit of statute. The court held:—

"The penalty of treble interest specified in the act has been held in this state to be cumulative, and not to abrogate the common-law remedy to recover money paid under illegal provisions of a contract."

[7] Having concluded the bank's loan to be usurious and that the plaintiffs may recover, the question remaining is how much of the interest paid are they entitled to recover. By our statutes usury is a criminal offense and is therefor against public policy. The contract for interest entered into between the bank and the borrower contravened public policy. Courts do not enforce contracts against public policy. This court so held in *Mongami v. Melekeok Municipality*, 4 T.T.R. 217. A suit to recover that which was obtained under an unenforceable contract is valid. Plaintiffs are entitled to recover all interest paid pursuant to the contract.

The rule allowing recovery of all interest paid is supported by substantial authority. The subject is annotated at 59 A.L.R.2d 522, 527, Sec. 3. The California rule that all interest paid under a usurious and therefor void contract is recoverable is set forth in *Westman v. Dye*, 4 P.2d 134; *Taylor v. Budd*, supra; *Stock v. Meek*, supra; *Goodwin v. Alston*, 250 P.2d 722; *Douglas v. Klopper*, 288 P. 36; and *Laypert v. Rieder*, 94 P.2d 96.

Ordered, adjudged and decreed:—

1. Plaintiff Kingzio shall have and recover from the defendant the sum of $240.00 together with interest thereon at the rate of 6 percent per annum from April 21, 1972, until paid.

2. Plaintiff Mobel shall have and recover from the defendant the sum of $48.00 together with interest thereon at the rate of 6 percent per annum from April 21, 1972, until paid.

3. That all members of the class represented by plaintiffs, upon making claim therefor as hereinafter provided, shall recover from defendant all interest collected by defendant from claimant borrowers on loans exceeding the sum of $300.00, payable in installments on which interest of more than 1 percent per month on the balance was collected by the defendant.

4. Defendant shall forthwith furnish plaintiffs' attorneys, the names, addresses, and interest collected from all borrowers on installment loans in excess of $300.00 made from February 15, 1965, to date on which interest charged and collected was more than 1 percent per month on the balance due.

5. Plaintiffs' attorneys shall forthwith notify by mail, messenger, or radio broadcast over Koror radio, all borrowers, as above described, from defendant of the judgment entered herein and of their entitlement to recover interest paid upon filing their claim under oath with plaintiffs' attorneys or the Clerk of Courts. Notification of the Judgment shall be in Palauan and English as follows:—

PALAU DISTRICT — CIVIL ACTION NO. 569

HUMIKO KINGZIO, et al.,
Plaintiffs,
vs.
THE BANK OF HAWAII,
KOROR BRANCH,
Defendant.

NOTICE OF JUDGMENT

To: (Name and address of Member of class)
You are hereby notified that judgment has been entered against the defendant in the above entitled action. Under the terms of the judgment, the defendant bank is required to reimburse all interest it has collected from each of its borrowers of more than $300.00, which loan was payable in installments with interest at a rate in excess of 1 percent per month. The bank's records indicate you were one of its borrowers during the period from February 15,

1965, to date of judgment, and accordingly you are notified of your possible entitlement to recover interest paid by you subject to making claim therefor.

You, your estate or representative must, within six months from October 15, 1973, file your claim under oath for recovery of interest paid. The claim shall be made through the offices of plaintiffs' attorneys, Micronesian Legal Services Corporation, Koror, Palau, or through the Clerk of Courts at the courthouse, Koror, Palau.

Clerk of Courts

6. Plaintiffs shall recover their costs in accordance with law, including costs of notification of members of the plaintiffs class, upon filing claim.

RICHARD L. CHRISTENSEN, Plaintiff

v.

MICRONESIAN OCCUPATIONAL CENTER, Defendant

Civil Action No. 38-73

Trial Division of the High Court

Palau District

October 17, 1973

Complaint by employee dismissed from government position. The Trial Division of the High Court, D. Kelly Turner, Associate Justice, held that when a government agency undertakes to follow regulations, whether or not it is required to adhere to them, they must be strictly observed.

1. Civil Procedure—Captions

Under the rule that it is immaterial what a pleading is labeled, for the court must give effect to its substance, motion to dismiss which was actually an answer in which the prayer asked for dismissal for failure to state a cause of action would be considered as such; and the case thus being at issue by complaint and answer, court could consider plaintiff's motion for summary judgment and defendant could not successfully claim the motion was not timely in view of his "motion to dismiss".

2. Judgments—Summary Judgment—Issues

Where there was no material issue of fact to be tried, summary judgment was appropriate.