DATE: 09-10-90

CITATION: VAOPGCPREC 91-90
Vet. Aff. Op. Gen. Couns. Prec. 91-90

TEXT:

Interest Rate Limitation under Soldiers' and Sailors' Civil Relief Act

QUESTION PRESENTED:

Does an interest rate reduction applied to an existing VA guaranteed loan by operation of law under the provisions of the Soldiers' and Sailors' Civil Relief Act affect the VA liability when a claim under a VA loan guaranty is filed?

COMMENTS:

1. Due to the current situation involving the mobilization of U.S. forces for deployment, a number of reservists have been activated, thereby possibly meeting the basic requirements for eligibility of certain benefits provided under the provisions of the Soldiers' and Sailors' Civil Relief Act of 1940, as amended, 50 U.S.C. App. 510 et. seq. (the Act).

2. The particular provision of the Act with which you are concerned relates to the maximum rate of interest which may be assessed on an obligation incurred prior to the person's military service during the period of military service. Appendix 526 of title 50, United States Code, provides, in part, that " no obligation or liability bearing interest at a rate in excess of 6 per centum per annum incurred by a person in military service prior to his entry into such service shall, during any part of the period of military service ... bear interest at a rate in excess of 6 per centum per annum...." When the rate is reduced pursuant to the Act, an issue which naturally follows relates to whether a holder of a loan would have recourse for the recovery of the interest difference between the contract rate and the maximum rate permissible under the Soldiers' and Sailors' Civil Relief Act (lost interest) by including such lost interest in a loan guaranty claim either prior to loan termination or after termination if the mortgagor defaults.

3. Under the current VA statute, the Secretary of Veterans Affairs may pay a claim under the VA loan guaranty only after certain conditions have been met. The conditions are that the loan must be in default, the value of the property must have been determined, and a liquidation sale must have been held. 38 U.S.C. § 1832. Subsequently, the amount which may be paid on the claim is based on the total indebtedness as compared to the value of the property. Total indebtedness is defined as "the amount equal to the total of (i) the unpaid principal of the loan, (ii) the interest on the loan as of the date applicable under paragraph (10) of this subsection, and (iii) such reasonably necessary and proper charges ... associated with liquidation of the loan...." 38 U.S.C. § 1832(c)(1)(D). The interest due on the loan which is included as part of the

total indebtedness is computed as of a cutoff date which is generally the liquidation sale date.

4. Accordingly, based on the provisions of existing law, a loan guaranty claim may only be paid after liquidation has occurred. The liquidation could be in the form of a sale or the acceptance of a transfer in lieu of foreclosure. This provision thus effectively precludes a lender from filing a claim with VA prior to termination of the loan. As long as the loan is current and has not been terminated, the lender may not file a claim under the VA loan guaranty in order to attempt to recover any of the lost interest.

5. The VA statute further provides that the amount of the claim which VA may pay to a holder after loan termination is based on the difference between the debtor's total indebtedness at the time of the foreclosure and the value of the property as determined by VA. The primary issue in this instance is whether the lost interest which has not been paid by the mortgagor may be included in the claim filed with VA.

6. Generally, the liability of the guarantor will not exceed the liability of the principal debtor as to the principal indebtedness. 38 Am.Jur.2d, Guaranty § 73. Therefore, if the debtor is not obligated to pay interest at a rate in excess of 6 percent, VA as guarantor likewise would not be obligated to include, in the total indebtedness subject to the VA guaranty, interest on the obligation in excess of 6 percent. Of course, the guarantor may elect to retain absolute guaranty liability regardless of what happens to the principal obligation by including provisions to that effect in the loan guaranty contract. Id. § 79.

7. Our review of the VA loan guaranty contract, which consists of the VA statute and regulations, does not reflect any provision which would provide for a deviation from the general legal principle recited above. VA's intent to apply this general principle to its loan guaranty contract is clearly demonstrated by the existing VA regulation which provides that the release of personal liability of an obligor without the prior consent of the Secretary releases the VA of its loan guaranty liability. 38 C.F.R. § 36.4324(f). Thus, the VA liability on its guaranty is generally measured by the debtor's preforeclosure obligation.

8. The Act is specific and prohibits an assessment of interest at a rate greater than 6 percent per annum during the person's period of military service. Unless otherwise permitted by a court of competent jurisdiction, the rate of interest is reduced. The issue which must be addressed at this point is whether the interest rate reduction provision of the Act reduces the debtor's obligation or if it only defers the payment of interest in excess of the statutory rate until the period of military service is terminated. As indicated, the language in the Act is clear and unambiguous and limits the interest rate that may be assessed on the outstanding obligation during the period of military service. Unlike other provisions in the Act which permit the modification of payments on mortgages and which specifically provide that the deferred amounts will be repaid upon release from military service, no such provision exists as to this particular section. It is, therefore, clear that upon modification of the interest rate the servicemember's interest liability is reduced and that, when computing the debtor's total indebtedness, the

interest portion on the underlying principal obligation will be determined accordingly.

HELD:

a. Claims under the VA loan guaranty may only be filed after liquidation has occurred or after a conveyance in lieu of foreclosure has been approved by VA and completed. At that time, based on the remaining outstanding indebtedness, a claim may be paid. If during the term of the loan the interest rate on the loan has been reduced pursuant to the terms of the Soldiers' and Sailors' Civil Relief Act, the total indebtedness for purposes of accounting with VA may not include any of the lost interest.

b. VA, however, pursuant to properly promulgated regulations, may modify the terms of its loan guaranty contract and agree to be liable to a holder to a greater degree than the original debtor in situations where a debtor's total indebtedness has been affected by the Soldiers' and Sailors' Civil Relief Act. A modification of this nature would not be without precedent as a similar modification to the VA loan guaranty contract has been adopted pursuant to 38 U.S.C. § 1832(c)(10)(D). The modification permits the filing of an increased loan guaranty claim to include additional accrued interest in any case where an excessive delay in the liquidation sale of the property has been caused by VA.

VETERANS ADMINISTRATION GENERAL COUNSEL
Vet. Aff. Op. Gen. Couns. Prec. 91-90