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**CONSUMER CREDIT DIVISION
ADVISORY LETTER 2020-01
June 15, 2020**

TO: Creditors who engage in consumer credit transactions under chapter 2, or consumer loans under chapter 3 of the IUCCC (collectively, “Creditors”)

FROM: Lyndsay H. Miller, Deputy Director of Consumer Credit

RE: **SEA 395 - Precomputed Consumer Credit/Loan Transactions Prohibited eff. July 1, 2020; New tiered nonrefundable prepaid finance charges permitted with “hard cap” for consumer credit transactions not secured by an interest in land (Depository institutions partially exempted)**

This Advisory is being issued by the Consumer Credit Division of the Indiana Department of Financial Institutions (“DFI”) regarding a number of significant upcoming law changes as a result of SEA 395’s enactment. First, SEA 395 places a “hard cap” on prepaid finance charges. For non-depository Creditors, all prepaid finance charges will be nonrefundable based on a new tiered scale. As of July 1, 2020, any prepaid finance charges imposed in excess of the maximums permitted within the tiers, that prior law would have allowed as refundable upon a consumer’s prepayment, are no longer permitted on new agreements. In addition, this advisory is also to alert Creditors who currently engage in precomputed credit or loan transactions that effective July 1, 2020, precomputed transactions are prohibited by law.

The following provides an overview concerning these changes as a result of [SEA 395](#) (General Assembly, 2020).

2020 legislative changes as a result of SEA 395 and affected statutes

1. **New tiered nonrefundable prepaid finance charges.** Up to and including June 30, 2020, only consumer lenders (chapter 3 of the Uniform Consumer Credit Code, or “UCCC”) are permitted to charge up to a \$50 nonrefundable prepaid finance charge on a given consumer loan transaction that is not secured by an interest in land; see generally [Ind. Code §24-4.5-3-201\(8\)\(b\) and 508\(8\)](#). Sellers under chapter 2 of the UCCC do not have a comparable provision, and all prepaid finance charges are considered subject to refund at the time of a consumer’s prepayment.

As a result of SEA 395, on and after July 1, 2020, in addition to the credit service or finance charge permitted by Ind. Code §24-4.5-2-201(2), Ind. Code §24-4.5-3-201, or Ind. Code §24-4.5-3-508, and any other authorized charges permitted by law (generally, “permitted additional charges”), an agreement for a closed-end consumer credit sale, a consumer loan, and/or a supervised loan including a revolving loan allows a seller (chapter 2) or

lender (chapter 3) to contract for and receive a nonrefundable prepaid finance charge based on a new tiered scale, similar to the current finance charge tiered rate structure as long as the total finance charge remains within the confines of the loansharking cap (72% per year) at the time the credit sale or loan is consummated.

The new tiered structure permits a Creditor to impose the following prepaid finance charges on an amount financed (under chapter 2) or principal amount (under chapter 3) of a given closed-end consumer credit transaction or consumer loan (*in all cases, the amount referenced is exclusive of prepaid finance charges*):

- \$75 maximum for a credit sale/loan amount of \$2,000 or less;
- \$150 maximum for a credit sale/loan amount for more than \$2,000 and up to \$4,000;
- \$200 maximum for a credit sale/loan amount above \$4,000.

For non-depository Creditors, the new law also creates a “hard cap” for the nonrefundable fee, in that it now prohibits any additional amount of prepaid finance charges, even if refundable, above the new maximum amounts permitted within the tier. For example, if a seller imposes a \$75 nonrefundable prepaid finance charge on a \$1,000 retail installment contract, the seller may not also charge a \$5 refundable prepaid finance charge; the prepaid finance charge in its entirety must not exceed the maximum amounts permitted under the tier.

The new tiered nonrefundable prepaid finance charge will now be permitted for Creditors under chapter 2 of the UCCC (extenders of consumer credit – ie, auto dealers, retailers, etc) as a new charge. For Creditors under chapter 3 of the UCCC (traditional lenders – ie, licensed finance companies, state chartered banks and credit unions), the previously permissible maximum nonrefundable prepaid finance charge of \$50 will now increase to the maximum amounts permitted by the tiers.

Depositories are exempt from the “hard cap” and may continue to charge a refundable portion of a prepaid finance charge in an amount above the nonrefundable prepaid finance charge subject to the limitations provided in the new tiers, so long as:

- 1) the refundable portion of the prepaid finance charge imposed is tested upon prepayment by a consumer for whether or not a refund is due;
- 2) the total finance charge contracted for at the time the loan is consummated does not exceed the maximum permitted by Ind. Code. §24-4.5-3-508; and
- 3) the total finance charge remains within the confines of the loansharking cap (72%) at the time the loan is consummated; both the refundable and nonrefundable portions of the prepaid finance charge must be included for testing purposes (*see also the Department’s Loansharking Advisory, [Advisory Letter 2017-02](#)*).

The exemption of depositories from the “hard cap” is not a flow through exemption. For example, if a depository has an indirect lending relationship with a new auto dealer, as the original creditor the auto dealer is subject to limitations of the hard cap imposed by the tiers. Even though a depository has an agreement to purchase the retail installment agreement from the auto dealer, the depository may not require, nor may the auto dealer charge, a prepaid finance charge above the nonrefundable amounts permitted by the tiers. Should an auto dealer charge a nonrefundable prepaid finance charge as part of the credit transaction within the limitations of the tiers, the auto dealer and depository may agree between themselves as to how to share the charge.

By way of example, an auto dealer has a relationship with XYZ bank where the bank agrees to purchase and take assignment of retail installment agreements entered into with certain eligible customers. A customer enters into a retail installment agreement for purchase of the vehicle with the auto dealer for \$27,000. The auto dealer

imposes a nonrefundable prepaid finance charge of \$200. The auto dealer then assigns the agreement to the bank. The auto dealer may agree with the bank to retain a portion of the \$200, keep all of the \$200, or turn over the \$200 in its entirety to the bank.

First lien mortgage loans extended by Licensed Mortgage Lenders or Depositories are not subject to the nonrefundable prepaid finance charge limitations.

2. Prohibition on Precomputed Transactions. Up to and including June 30, 2020, [Ind. Code §§ 24-4.5-2-201, 3-201 and 3-508](#) permit Creditors to engage in precomputed credit and loan transactions. Further, corresponding statutes [Ind. Code §24-4.5-2-210](#) and [Ind. Code §24-4.5-3-210](#) prescribe the manner in which a rebate must be made, should a consumer prepay a precomputed credit or loan obligation prior to maturity. Upon prepayment in full of the unpaid balance of a precomputed consumer credit sale or consumer loan, or a refinancing or consolidation thereof, a consumer is entitled to a rebate of the unearned finance charge as required by [Ind. Code §24-4.5-2-210](#) and [Ind. Code §24-4.5-3-210](#).

A precomputed transaction entered into on or before June 30, 2020, will generally continue to be recognized as valid when made through maturity (so long as such a transaction was otherwise made in compliance with applicable state and federal laws, ie, a “valid precomputed transaction”). Precomputed transactions entered into on or before June 30, 2020 will continue to be reviewed during scheduled compliance examinations. Creditors are expected to continue to undertake the statutory rebate calculation on existing precomputed loans at the time a consumer prepays a valid precomputed transaction.

Effective July 1, 2020, precomputed transactions are prohibited by law. Chapter 2 (Consumer Credit) and Chapter 3 (Consumer Loans) of the Uniform Consumer Credit Code permit a number of alternative computation methods; the UCCC’s actuarial method is equivalent to what is commonly referred to as “simple interest.”

There are at least two (2) acceptable methods of computing time under the UCCC in charging for the period of time between payments. These are the "**actual days method**" and the "**calendar month method**."

Historically, DFI has taken no issue with a wide variety of other accrual methods for assessing a daily rate, including commonly used accrual methods on either a 365 or 360 day year, known as the "**365 day method**" and the "**360 day method**." These methods are more fully described below. These methods are by no means exclusive; however, these approaches represent the most commonly used accrual methods observed. Should a Creditor consider use of another method, such Creditor is encouraged to contact the DFI for review and guidance. Generally, the DFI will not take issue with a Creditor’s accrual method so long as the effective yield does not exceed the contractual provisions.

365 DAY METHOD:

In application, this method results in a creditor applying a daily rate of charge determined by dividing a permissible annual rate of charge by **365** and then applying that rate over the actual number of days elapsed.

Example: Assume a (note) rate of 21% and a principal balance of \$10,000

July 25 to September 3, 2019 = 40 days

.21 / 365 x 40 x \$10,000 = \$230.14

February 15 to April 2, 2019 = 46 days

.21 / 365 x 46 x \$10,000 = \$264.66

February 8 to March 4, 2019 = 24 days

$.21 / 365 \times 24 \times \$10,000$ = \$138.08

March 4 to April 1, 2019 = 28 days

$.21 / 365 \times 28 \times \$10,000$ = \$161.10

CALENDAR MONTH METHOD:

The UCCC¹ permits a creditor to disregard differences in the lengths of months and authorizes the treatment of a day as **1/30th of a month**. Thus, a month would be considered as that period of time extending from a given date in one month to the like date in the next succeeding month and if there is no such like date, then to the last day of that succeeding month. In dealing with periods of time other than a month, the UCCC permits a creditor to treat such periods by considering each day as 1/30th of a month.

The calendar month method permits a Creditor to treat each elapsed day as a day, but since a Creditor may not earn for both the first and last day in any given period of time, the UCCC will only allow interest to be earned through the day prior to the day on which an interest earned computation is made. Since the UCCC permits a Creditor to treat a day as 1/30th of a month, for purposes of computing interest, the creditor may apply 1/30th of the monthly rate of charge for each day in any irregular period over which he computes interest. When a calendar month has elapsed, there is no necessity for consideration of elapsed days in that the UCCC provides that differences in lengths of months may be disregarded; and therefore, a creditor may charge 1/12th of the annual rate of charge for that period.

Example: Assume a (note) rate of 21% and a principal balance of \$10,000

July 25 to September 3, 2019:

July 25 to August 25 = 1 calendar month

$.21 / 12 \times \$10,000$ = \$175.00

August 25 to September 3 = 9 actual days

$(.21 / 12) \times 1/30 \times 9 \times \$10,000$ = \$52.50

$\$175.00 + \$ 52.50$ = \$227.50

February 15 to April 2, 2019:

February 15 to March 15 = 1 calendar month

$.21 / 12 \times \$10,000$ = \$175.00

March 15 to April 2 = 18 actual days

$(.21 / 12) \times 1/30 \times 18 \times \$10,000$ = \$105.00

$\$175.00 + \105.00 = \$280.00

¹ Ind. Code § 24-4.5-2-201, Ind. Code § 24-4.5-3-201, and Ind. Code § 24-4.5-3-508

February 8 to March 4, 2019:

February 8 to March 4 = 24 actual days

$$(.21 / 12) \times 1/30 \times 24 \times \$10,000 = \$140.00$$

March 4 to April 1, 2019:

March 4 to April 1 = 28 actual days

$$(.21 / 12) \times 1/30 \times 28 \times \$10,000 = \$163.33$$

360 DAY METHOD:

Under this method, the Creditor applies a daily rate of charge, determined by dividing a permissible annual rate of charge by **360**, to the number of days elapsed, **counting each month as having 30 days**. Therefore, the 31st day of months having 31 days may be disregarded and one or two days are to be added to the month of February.

Examples: Assume a (note) rate of 21% and a principal balance of \$10,000

July 25 to September 3, 2019:

July = 5 days

August = 30 days

September = 3 days

38 days

$$.21 / 360 \times 38 \times \$10,000 = \$221.67$$

February 15 to April 2, 2019:

February = 15 days

March = 30 days

April = 2 days

47 days

$$.21 / 360 \times 47 \times \$10,000 = \$274.17$$

February 8 to March 4, 2019:

February = 22 days

March = 4 days

26 days

$$.21 / 360 \times 26 \times \$10,000 = \$151.67$$

March 4 to April 1, 2019:

March = 26 days

April = 1 day

27 days

$$.21 / 360 \times 27 \times \$10,000 = \$157.50$$

DFI Administration

On or after July 1, 2020:

1. There is a “hard cap” on permitted prepaid finance charges. For non-depository Creditors, the total permitted prepaid finance charge is limited to the maximum amount reflected in the new tiers set out in statute. Any prepaid finance charge imposed above the amount permitted by the tiers will be prohibited by law and subject to refund. As a result of the nature of the prohibition, should a Creditor continue to enter into transactions that include prepaid finance charges that otherwise exceed the maximum amounts permitted within the tier on or after July 1, 2020, the imposition of civil penalties within the limitations permitted by law will be considered.

2. New precomputed credit or loan transactions are prohibited by law. In most instances, should a Creditor enter into a precomputed transaction on or after July 1, 2020, DFI may recast the transaction to conform to the newly permitted limitations under chapters 2 and 3 of the UCCC, as well as require refunds of associated overcharges. As a result of the nature of the prohibition, should a Creditor continue to enter into precomputed transactions on or after July 1, 2020, the imposition of civil penalties within the limitations permitted by law will be considered.

3. Powers of the Department. Should a Creditor’s accrual method be made for the purpose of circumventing the new laws and prohibitions implemented by SEA 395, the Director may, after meeting certain procedural notice requirements, conform the credit service and/or finance charge (as applicable) to the limitations set forth by law, including but not limited to requiring any overcharges be refunded to a consumer. See generally SEA 395 [IC 24-4.5-2-201(12); IC 24-4.5-3-201(11)]. This power will be exercised judiciously and only in circumstances where the Director determines a Creditor’s particular method clearly demonstrates an intention to evade the limitations of the law.

Requests to DFI for further assistance and guidance

We recognize that for some Creditors, these law changes may necessitate a dramatic shift from its current business model. We are committed to assisting our licensed and regulated businesses with the help you may need in order to accommodate these new law changes. We are available to you as a resource, and would offer to assist you by discussing your proposed accrual method, discussing your intentions of imposing a new or revised nonrefundable prepaid finance charge, and reviewing any sample documents ahead of the impending law changes discussed above.

For additional guidance, please also see the complementary Q&A published along with this guidance reflecting a number of questions and answers we have received regarding the above changes.

Should you have any questions regarding the above, please contact: Deputy Director Lyndsay Miller, at lmiller@dfi.in.gov or 317.232.3961.

To request assistance, guidance, ask questions concerning accrual methods, or to request a review of sample documents, please contact: Scott Imbus, Division Supervisor – Consumer Credit, at: simbus@dfi.in.gov or 317.453.2179.

Disclaimer:

This Advisory Letter is applicable to all Creditors subject to Chapter 2 and Chapter 3 of the UCCC and is in effect unless later amended or withdrawn. This letter is intended to provide a clarification of existing Department policy and interpretation and is not a substitute for advice from a Creditor's legal counsel. Although the Department may not require refunds in all circumstances, this does not relieve the Creditor of possible civil liability.

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