

Insights

January Hoosier Banker: Compliance Connection with Partner Brett Ashton

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Question 1: Indiana law provides for a \$50 loan origination fee that is earned at closing; however, if that amount is financed into the principal loan amount, are we still in compliance if we assess interest on the larger loan amount?

Answer: Most likely, yes. Interest can be collected on a loan amount that includes the loan origination fee, as long as it does not exceed the statutory finance charge limits¹ provided by the Indiana Uniform Consumer Credit Code (IUCCC or "the Act"). Indiana Code §24-4.5-3-201(8) provides, "Except as provided in subsection (7), in addition to the loan finance charge provided for in this section and to any other charges and fees permitted by this chapter, the lender may contract for and receive a loan origination fee of not more than fifty dollars (\$50)." This fee is not subject to refund or rebate and, in the event a borrower chooses to refinance its loan with the same lender, may be further limited depending on the timing of the refinance.² The loan origination fee is a prepaid finance charge for disclosure purposes under the Federal Truth in Lending Act (TILA) and Regulation Z. The loan origination fee must be deducted from the loan amount to arrive at the amount financed, which is the same as "principal" as defined in the IUCCC. "Amount financed" is a key term in the correct calculation of the finance charge and corresponding annual percentage rate. A creditor who correctly calculates the amount financed/ principal of the agreement by deducting the loan origination fee from the loan amount will be in compliance with the IUCCC if it finances the loan origination fee, unless inclusion of the fee causes the loan to exceed the maximum permissible finance charge under the Act.

Question 2: My bank currently charges more than \$50 for a loan origination fee – are we out of compliance?

Answer: Not necessarily. While the Indiana Uniform Consumer Credit Code provides that a lender may charge a \$50 loan origination fee that will be considered earned at closing, if your bank charges a higher fee, you will still be in compliance as long as you are calculating the finance charge correctly, not exceeding the maximum permissible finance charge as discussed above, and rebating the correct amount of the fee in the event of prepayment.³ A creditor charging a loan origination fee in excess of \$50 must contract for any amounts in excess of \$50 to be subject to refund upon prepayment in full. Additionally, accurate prepayment disclosures must be provided under

Section 1026.18(k) of Regulation Z. An alternative to a loan origination fee in excess of \$50 is to have a separate prepaid finance charge. This separate charge must comply with all provisions of IC 24-4.5, including maximum rate and possible rebate upon prepayment, as outlined in IC 24-4.5-3-209(2).

¹Ind. Code § 24-4.5-3-201 provides a lender may contract for a loan finance charge, calculated according to the actuarial method, not exceeding 25 percent per year on the unpaid balances of the principal. Ind. Code § 24-4.5-3-508 provides a lender may contract for and receive a loan finance charge calculated according to the actuarial method, which may not exceed the equivalent of the greater of: (1) 36 percent per year on that part of the unpaid balances of the principal which is \$2,000 or less; (2) 21 percent per year on that part of the unpaid balances of the principal which is more than 2,000 but does not exceed 4,000; and (3) 15 percent per year on that part of the unpaid balances of the principal which is more than \$4,000, or 25 percent per year on the unpaid balances of the principal. ² See Ind. Code § 24-4.5-3-201(9)(10). ³ See Ind. Code § 24-4.5-3-209.

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