

FINANCIAL INSTITUTIONS, DEPARTMENT OF: Conditional sales contract, deduction on account of prepayment. Prepayment deduction, method of computing same. Finance company, duty of when properly requested to give statement of amount due on prepayment of conditional sales contract.

October 6, 1937.

Hon. R. A. McKinley,
Director, Department of Financial Institutions,
Indianapolis, Indiana.

Dear Sir:

I have before me your letter submitting for an official opinion certain questions which have arisen in the administration of chapter 231 of the Acts of 1935, usually referred to as the Retail Installment Sales Act. The questions submitted are as follows:

"1. On a conditional sales contract on which there is a prepayment made by another finance company, can the finance company holding the contract quote to this company the net pay-off figure which takes into consideration rebate for prepayment and the discount for cancellation of the insurance policy?

"2. Is it necessary for a finance company to notify the customer in any way that this is being done? Does the rebate for the insurance have to go direct to the customer?

"3. In calculating discount for prepayment on a conditional sales contract, does the finance company begin figuring a discount on the installment that matures less than thirty days from the time the contract is paid in full?

"4. In the event of a conditional sales contract signed with recourse or with repurchase by a dealer, is the finance company permitted to give the dealer the full consideration for both prepayment of the account and the unearned premium of insurance in the event of a repossession and payoff?"

The above questions require a consideration of the provisions of section 6 of the Act, which provides in part as follows:

“Every retail buyer shall have the right, at any time, to pay the then unpaid time balance owed on any retail installment contract, whether then due or not, and upon payment thereof, any holder of the retail installment contract shall reduce the amount of the then unpaid time balance by the amount fixed and determined in accordance with the regulations of the department in force as of the date of the making of the particular retail installment contract and applicable to such cases. The reduction herein authorized may be known as a discount and every retail buyer, upon full prepayment of any unpaid time balance owed by him on any retail installment contract, shall receive the discount but only in the amount, at the times and upon the conditions provided herein. The department shall and is hereby authorized to fix and determine the amount of any discount to be given for prepayment as in this section authorized but no such discount shall be for an amount in excess of the amount of the finance charge on any particular retail installment contract.”

Acts of 1935, p. 1211.

Your first question seems to lack somewhat in clarity of statement, but I am advised orally that it has to do with a situation represented by the following or similar statement of facts, viz:

“S,” representing the retail seller, sells merchandise to “B,” representing the retail buyer, on a conditional sales contract, the conditions surrounding the sale being such as to bring the transaction within the Retail Installment Sales Act. “S” thereupon assigns the contract to “F,” which is a finance company, licensed under the Act. “B” desiring to refinance the transaction, contacts a small loan company, or other company willing to loan to him sufficient money to pay off the conditional sales contract. The transaction, however, in behalf of “B” is negotiated by the small loan company, or other company loaning him the money, and your question is this: When the small loan company or other company making the loan applies to the finance company for a statement of the balance due on the contract, should such finance company, represented by “F,” quote to the small loan company the net pay-off figure which takes into consideration the rebate for prepayment and

the discount for cancellation of the insurance policy, or should such finance company quote to the small loan company the gross amount required to pay off the contract without deducting the rebate for prepayment or the discount for cancellation of the insurance policy?

I think the answer to this question is very apparent from a consideration of section 6 of the Act already referred to. When the retail buyer personally prepays his contract, he is clearly entitled to the deduction provided in such cases in accordance with the rules and regulations of the department. This includes the return premium upon the cancellation of any insurance policy the cost of which was charged to the retail buyer.

See Opinions of Attorney General of 1936, page 335.

It seems to me to be almost self-evident, therefore, that if the retail buyer is entitled to this rebate upon prepayment, when he makes the prepayment himself, he would likewise be entitled to it when the prepayment is actually made by a small loan company, or other company from which he is borrowing the money with which he might personally do so. The fact that he is borrowing money from a small loan company with which to make the prepayment would not entitle the small loan company to add this rebate to the principal of any note which was being given in consideration of the prepayment of the amount due on the conditional sales contract, since to do so would operate to indicate a larger loan of money than actually occurred. It should be remembered in this connection that the loaning of money by a small loan company under the conditions above set out is not a transaction covered by the Retail Installment Sales Act. It is not a continuation of the original contract, nor does it operate as a new contract under the Retail Installment Sales Act whereby the prepayment privilege and deduction therefor is guaranteed to the retail buyer. The second transaction above described is a simple loan of money and the only question involved is the question as to how much money is loaned. In my opinion, it would be the duty of the finance company, represented by "F," in the above case, in quoting the amount required to pay off the contract to report the net amount after the deduction of the discount allowed for a prepayment and the deduction of the

cancellation value of the insurance policy. If that net amount is all the finance company receives, its relationship to the retail buyer upon such receipt would be at an end. However, if it does quote the gross amount without these deductions and receives in any method such gross amount, it would undoubtedly owe the retail buyer the amount of the deduction, which is required under the rules and regulations of the department to be made in the case of a prepayment.

Your second question refers to the first and inquires first, whether it is necessary for a finance company to notify the customer in any way that this is being done. This question likewise is not clear, but I am advised that the intention is to ask whether the finance company should notify the customer, referring to the retail buyer, as to the amount which it is quoting to the other company as being due on the contract. I do not think the Act itself actually covers this question, but the department, of course, is authorized to go into the subject and if it finds that a licensee under such circumstances is quoting a gross amount without the deduction and without paying the proper rebate to the retail buyer, such company would be violating the Act. Generally speaking, I would say that the finance company should notify the retail buyer as to what is being done, although I doubt whether there can be said to be an actual legal liability to do so. There is a legal liability on the finance company, however, to pay the rebate to the retail buyer if it collects in any way the gross amount from the other loan company. The second part of your second question is: "Does the rebate for the insurance have to go direct to the customer?" This has already been answered.

See Opinions of Attorney General of 1936, page 335.

Reasons for the conclusion are stated in the previous opinion. It is sufficient at this time in answer to this question to simply state that it is answered in the affirmative.

The answer to your third question may, generally speaking, be controlled by the rules of the department. However, I may say that the basis for figuring a discount on account of the prepayment of the balance due is doubtless the value of the use of the money remaining from time to time due and unpaid. Assuming, therefore, that an offer to prepay is during the last thirty-day period of the contract, the interest on the unpaid

balance could not, I think, be computed for a longer period of time than the difference between the expiration date of the contract and the date of the offer of prepayment. In other words, assuming as a concrete example that payments are required to be made monthly and that the last payment is due on December 1, 1937; assuming further that an offer to prepay is made on the 28th of October, 1937; the unpaid balance would be the total of the November 1 and December 1 payments, but the value of the use of that money would not be computed upon its use for a full two months. Obviously, as to the last payment, it would be computed upon its use for one month, the month of November. As to the November payment, it would be computed, if taken into consideration at all, only for the period of three days.

Referring now to your fourth question, it is based upon a conditional sales contract wherein the assignment of the contract is with recourse upon the dealer or with a repurchase agreement by the dealer. That is, the dealer agrees that if the buyer does not pay the contract out in full, he will pay it, or will repurchase the contract from the finance company for the remainder of the unpaid balance. The procedure in this case involves repossession of the specific goods involved in the contract by the finance company where the assignment is with recourse, and the turning of the specific goods back to the seller upon the payment of the amount due. In the case of an assignment with an agreement to repurchase by the dealer, the procedure involves the prepaying of the contract by the dealer who would then have the right to obtain repossession of the specific goods from the buyer. In either event, I think the dealer would ordinarily be entitled to the full consideration for both the prepayment of the account and the unearned premium for insurance. It is sufficient to say, however, that the defaulting buyer would not be entitled to such rebate.

BOYS' SCHOOL, INDIANA: Requirements for commitment.

October 7, 1937.

Dr. E. M. Dill, Superintendent,
Indiana Boys' School,
Plainfield, Indiana.

Dear Sir:

This will acknowledge receipt of your letter of October 6 containing the following questions: