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Administrative Interpretation No. 3.508-7702

A YEAR FOR PURPOSES OF DETERMINING MAXIMUM ALLOWABLE LOAN FINANCE CHARGES FOR SUPERVISED LOANS UNDER SECTION 3.508 AS WELL AS FOR DISCLOSING THE ANNUAL PERCENTAGE RATE IS A CALENDAR YEAR

You have asked whether the loan finance charges allowable under Section 3.508(2) should be calculated on the basis of a 360-day "year" or on the basis of a 365-day year and whether a supervised lender may use either basis as long as it discloses the actual yield as an annual percentage rate.

Speaking in terms of a 360-day "year" only leads to confusion. A calendar year has 365 days (or 366 days if it is a leap year). As commonly understood, the terms "per year," "per annum," and "annual" refer to a 365-day year.

In 1974 the United States Court of Appeals for the Ninth Circuit held that an Oregon bank violated Oregon's usury law and the National Bank Act [12 U.S.C.A. §§85, 86] by computing interest at the maximum legal rate based on 360 days when that method produced a higher yield than using a method based on a calendar year of 365 days. <u>American Timber & Trading Co. v. First National Bank of Oregon</u>, 511 F. 2d 980 (9th Cir. 1974), cert. den. 421 U.S. 921, 95 S. Ct. 1588, 43 L.Ed. 2d 789 (1975). The Court said that "per annum" means literally "by the year" and a 365-day year is intended unless that term has been otherwise construed by court decision. 511 F. 2d 980, 983. The bank was found in violation of federal banking law not only for charging excessive interest but also for <u>knowingly</u> charging excessive interest.

More recently the California Supreme Court enjoined a bank from advertising "per annum" rates based on a 360-day "year." <u>Chern v. Bank of America</u>, 544 P.2d 1310, 127 Cal. Rptr. 110 (1976). Such advertising was found likely to mislead and deceive a bank's potential borrowers and accordingly was held to be in violation of the State's false and misleading advertising law.

Consumer Protection Code Section 3.301 [S.C. Code Ann. §8-800.261(1975 Cum. Supp.)] incorporates by reference the Federal Truth in Lending Act [15 U.S.C. §§1601 <u>et seq.</u>].

The Truth in Lending Act requires disclosure of the finance charge as a dollar amount and also as an annual percentage rate. The annual percentage rate is that nominal annual percentage rate determined in accordance with the actuarial method of computation so that it may be disclosed with an accuracy at least to the nearest quarter of one percent. Federal Reserve Board Regulation Z Section 226.5(b)(1). The rate which must be disclosed under the federal law and regulation is the actual yield which the loan will produce over a 365-day year. Federal Reserve Board Letter No. 181, November 24, 1969 [5 CCH Consumer Credit Guide ¶31,184].

Subsection (2) of Section 3.508 provides that the loan finance charge, calculated according to the actuarial method, may not exceed the greater of either the composite rate per year as set forth in item (a) or the flat rate of 18% per year as set forth in item (b). The percentage rate "per year" for purposes of determining maximum charges for supervised loans is calculated on the basis of a 365-day year as is the annual percentage rate which is required to be disclosed to the consumer under the Truth in Lending provisions of the Consumer Protection Code.

Some confusion apparently has resulted from language contained in Subsection (4) of Section 3.508 which states in part:

> The term of a loan for the purposes of this section commences on the date the loan is made. Differences in the lengths of months are disregarded and a day may be counted as 1/30th of a month.... [A] part of a month in excess of 15 days may be treated as a full month if periods of 15 days or less are disregarded and that procedure is not consistently used to obtain a greater yield than would otherwise be permitted.

That subsection does not affect the length of a year for purposes of determining maximum allowable charges or calculating the annual percentage rate of the finance charge for supervised loans but instead provides a convenient method for handling periods of time which involve a part of a month rather than an entire month.

It should be pointed out that this interpretation is limited to the specific question asked and has no bearing on the method of contracting for the finance charge. Subsection (3) of Section 3.508 provides:

> This section does not limit or restrict the manner of contracting for the loan finance charge, whether by way of add-on, discount, or otherwise, so long as the <u>rate</u> of the loan finance charge <u>does not exceed that permitted</u> by this section.... (Emphasis added)

In summary, it is the opinion of this Department that rates of finance charges for supervised loans under Section 3.508 for both disclosure and maximum charge purposes must be based on a calendar year.

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