Approved Clyde Graeber 2-15-90
Date

MINUTES OF THE HOUSE COMMITTEE ON Commercial and Financial Institutions.

The meeting was called to order by Representative Clyde D. Graeber at
Chairperson

3:30 ~~a~~m./p.m. on February 1, 19 90 in room 527-S of the Capitol.

All members were present except: Representatives Teagarden and Wilbert, Excused.

Committee staff present: Bill Wolff, Research Department
Bruce Kinzie, Revisor of Statutes
June Evans, Secretary

Conferees appearing before the committee: James Turner, President, Kansas-Nebraska League of Savings Institutions
Representative Frank Buehler, Vice Chairperson, Rules and Regulations Committee
Stanley Lind, Counsel and Secretary, Kansas Association of Financial Services
Dick Brock, Adm. Asst., KS Insurance Dept.

Representative King moved and Representative Johnson seconded the minutes of the January 25th meeting be approved. There was no discussion and the motion carried.

The Chairman opened the hearing on HB 2633.

James Turner, President, Kansas-Nebraska League of Savings Institutions, was the first conferee, speaking in support of HB 2633 which would grant authority for state-chartered savings and loan associations to offer demand deposit accounts. This authority was granted to federal savings and loan associations in the FIRREA law.

This bill would grant conformity between state-chartered and federally-chartered institutions and would request the committee's earliest attention to reporting the bill favorably for passage and placing the measure on the consent calendar. (See Attachment #1).

The hearing was closed on HB 2633.

The Chairman opened the hearing on HB 2651.

Representative Frank Buehler, Vice Chairman, Rules and Regulations Committee, stated the Rules and Regulations Committee was requested to review and make determination if they liked the bill or didn't like it; the Committee cannot change, or introduce legislation.

The Rules and Regulations Committee recommends that he be changed to the Commissioner and add "The Rule of 78or sum of the digits shall not be an acceptable method of computing a refund or credit of consumer credit premiums. (See Attachment #2).

The next conferee was Dick Brock, Administrative Assistant, Kansas Insurance Department, stating last summer in updating the regulations, they found a not in the regulations that was in error. A hearing was scheduled and the Consumer Credit Commissioneer should do the same so could not be calculated by the Rule of 78s. The Department asked the Commissioner to write a letter and she did so. Following the hearing on regulations and bearing in mind changes were disseminated and had much protest. The Consumer Credit Commissioner suggested we made change and mention others did not want to change. The Insurance Department is neutral.

The next conferee was Stanley Lind, Counsel and Secretary, Kansas Association of Financial Services,opposing change of legislation, stating it would be wrong and unfair to abolish the Rule of 78's in computing credit insurance refunds which would force the use of the pro-rated method. (See Attachment #3)

The Chairman asked Mr. Lind if other states had abolished the Rule of 78's and Mr. Lind replied, not to his knowledge.

The hearing was closed and the meeting adjourned at 4:30 P.M.

Date: 2-1-90

GUEST REGISTER

COMMERCIAL AND FINANCIAL INSTITUTIONS

NAME	ORGANIZATION	ADDRESS
Stan Lind	Kans. Assn. of Financial Services	Kans. City, Ks.
JEFF SONNICH	KNLSI	TOPEKA
Chuck Stones	KBA	"
Jan Turner	KNLSI	Topeka
David Douglass	Kansas S+L Dept	TOPEKA
Tony Humphrey	KMHA	Topeka
Dick Brock	Ins Dept	"

Kansas-Nebraska League of Savings Institutions

James R. Turner, President

Suite 512
700 Kansas Avenue
Topeka, Kansas 66603
(913) 232-8215

February 1, 1990

TO: HOUSE COMMITTEE ON COMMERCIAL AND FINANCIAL INSTITUTIONS
FROM: JIM TURNER, KNLSI
RE: H.B. 2633 (DEMAND DEPOSIT ACCOUNTS)

The Kansas-Nebraska League of Savings Institutions appreciates the opportunity to appear before the House Committee on Commercial and Financial Institutions in support of H.B. 2633 which would grant authority for state-chartered savings and loan associations to offer demand deposit accounts. This authority was granted to Federal Savings and Loans in the 400-page FIRREA law.

House Bill No. 2633 would change current law as follows:

1. Section 1, lines 23-27, deletes the existing restriction that state chartered associations may only accept demand accounts from customers that have a business, corporate, commercial or agricultural relationship with the association. This bill allows state chartered associations to accept demand accounts from any customer.

2. Section 1, lines 30-35, deletes the existing restrictions on demand accounts referred to above and the restriction that state chartered associations may not pay interest on a demand account.

3. Section 1, lines 40-43 on page 1, and lines 1-8 on page 2, deletes existing restrictions on the term for savings accounts and advance notice and priority rules on accounts withdrawn. These provisions are now covered in the new language set forth in Section 1, page 3, lines 1-35, to be consistent with the restrictions applicable to federal associations in FIRREA.

4. Section 1, lines 24-27 on page 2, deletes the existing negotiable order of withdrawal accounts restrictions by allowing such accounts to be accepted from all customers.

5. Section 1, lines 1-35 on page 3, adds the specific demand account authorities granted to federal associations by FIRREA.

The bill would grant conformity between state-chartered and federally-chartered institutions and we would request the committee's earliest attention to reporting the bill favorably for passage and placing the measure on the consent calendar.

James R. Turner, President

JRT:bw

Atch #1

When you borrow from a bank or other lender, you usually arrange to repay the loan with interest by a specific date in a number of equal installments.

Repaying It Early

But after several payments, you may decide to repay the entire loan earlier than originally scheduled. You ask the creditor for a payoff figure. You may be disappointed to learn that the balance due is higher than you anticipated.

Why is it higher? Perhaps because you thought the interest on the amount borrowed was divided evenly over the number of payments you agreed to make. Thus, you may have believed that if you paid the loan in 10 months instead of 30 you would owe only one-third as much interest.

This is not the way creditors compute interest, however.

The Rule of 78's

Creditors use tables based on a mathematical formula called "The Rule of 78's" - or sometimes "The Sum of the Digits" - to determine how much interest you have paid at any point in a loan. This formula takes into consideration the fact that you pay more interest in the beginning of a loan when you have the use of more of the money, and you pay less and less interest as the debt is reduced. Because each payment is the same size, the part going to pay back the amount borrowed increases as the part representing interest decreases.

When you decide to pay off a loan early, the creditor uses The Rule of 78's to determine your "rebate" - the portion of the total interest charge you won't have to pay.

The Rule is recognized as a practical way to calculate rebates of interest. There are other methods, but this one is widely used, and it is reflected in a number of state lending laws.

Reminders

The final payoff figure on your loan depends primarily on the original time to maturity, but it may be affected by other factors, such as variances in the payment schedule or a lag between the date of calculation and the date of payment.

Keep in mind that paying off a loan in, say, 15 months instead of 30 as originally planned will not produce a saving of one-half of the interest.

You may, however, be entitled to a rebate of certain other charges when you prepay a loan, such as part of a premium for credit insurance.

Finally, the Truth in Lending law requires that your creditor disclose how interest will be computed if you pay the debt in full before maturity. Look for the prepayment disclosure before you sign a loan agreement. Ask for an explanation of anything you do not understand.

HOW TO USE THE RULE OF 78's

The first step is to add up all the digits for the number of payments scheduled to be made. For a 12-installment loan, add the digits from 1 through 12:

$$1+2+3+4+5+6+7+8+9+10+11+12 = 78$$

The answer is "the sum of the digits" and explains how the rule was named. One might say the total interest is divided into 78 parts for payment over the term of the loan.

To add all the numbers in a series of payments is rather tedious. One can arrive at the answer quickly by using this formula:

$$\frac{N}{2} \times (N+1)$$

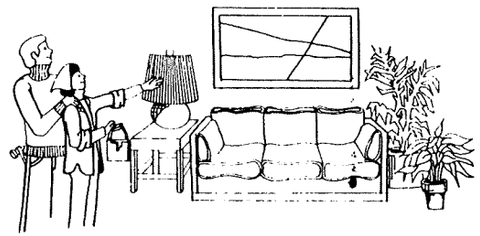
N is the number of payments. In a 12-month loan, it looks like this:

$$\frac{12}{2} \times (12+1) = 6 \times 13 = 78$$

In the first month, before making any payments, the borrower has the use of the whole amount borrowed and therefore pays 12/78's of the total interest in the first payment; in the second month, he still has the use of 11 parts of the loan and pays 11/78's of the interest; in the third, 10/78's; and so on down to the final installment, 1/78.

A Loan for Ann and Dan

Let us suppose that Ann and Dan Adams borrow $3,000 from the Second Street National Bank to redecorate their home. Interest comes to $225, and the total of $3,225 is to be paid in 15 equal installments of $215.



Using the Rule of 78's, we can determine how much of each installment represents interest. We add all the digits from 1 through 15:

$$\frac{15}{2} \times (15+1) = 7.5 \times 16 = 120$$

The first payment will include 15 parts of the total interest, or 15/120's; the second, 14/120's; and so on.

Notice in the following table that the interest decreases with each payment and the repayment of the amount borrowed increases with each payment.

DEPARTMENT OF CONSUMER AFFAIRS
FEDERAL RESERVE BANK OF PHILADELPHIA

Pay't No.	Interest	Reduction of Debt	Total Pay't
1	$ 28.13	$ 186.87	$ 215.00
2	26.25	188.75	215.00
3	24.37	190.63	215.00
4	22.50	192.50	215.00
5	20.63	194.37	215.00
6	18.75	196.25	215.00
7	16.87	198.13	215.00
8	15.00	200.00	215.00
9	13.13	201.87	215.00
10	11.25	203.75	215.00
11	9.37	205.63	215.00
12	7.50	207.50	215.00
13	5.63	209.37	215.00
14	3.75	211.25	215.00
15	1.87	213.13	215.00
	$225.00	$3,000.00	$3,225.00

How Much Is the Rebate?

Now let's assume Ann and Dan want to pay off the loan with the fifth payment. We know the total interest is divided into 120 parts. To find out how many parts will be rebated, we add up the digits for the remaining 10 installments which will be prepaid:

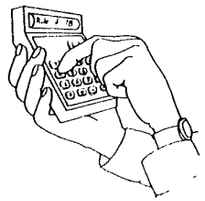
$$\frac{10}{2} \times (10+1) = 5 \times 11 = 55$$

Now we know that 55/120's of the interest will be deducted as a rebate; it amounts to $103.12.

$$\frac{55}{120} \times \$225 = \frac{12375}{120} = \$103.12$$

We see that Ann and Dan do not save two-thirds of the interest (which would be $150.00) by paying off the loan in one-third of the time. But the earlier they repay the loan the higher the percentage of interest they do save.

Check It Out



Perhaps you would like to try using The Rule of 78's. Here is a problem for you. Assume that Ann and Dan pay off their loan at Second Street National Bank with the eleventh payment. How much interest will they save? Remember that the interest over 15 months is divided into 120 parts, and you need to know the number of payments that will be prepaid. Fill in the blanks.

$$\frac{N}{2} \times (N+1) = \frac{\_\_}{2} \times (\_\_+1) = \_\_ \times \_\_ = \_\_.$$

Now multiply the rebate fraction by the total amount of interest on the loan:

_____ x $ ____ = $____ rebate

Your answers should be as follows:

$$\frac{4}{2} \times (4+1) = 2 \times 5 = 10$$

$$\frac{10}{120} \times \$225 = \frac{2250}{120} = \$18.75$$

Other pamphlets available include:

- How to Establish and Use Credit
- Your Credit Rating
- How the New Equal Credit Opportunity Act Affects You
- The Equal Credit Opportunity Act and...Age
- The Equal Credit Opportunity Act and...Women
- The Equal Credit Opportunity Act and...Doctors, Lawyers, Small Retailers
- The Equal Credit Opportunity Act and...Credit Rights in Housing
- Fair Credit Billing
- Truth in Leasing
- The Fair Debt Collection Practices Act
- If You Use a Credit Card

For further information or copies of pamphlets, you may write or call:

Department of Consumer Affairs
Federal Reserve Bank of Philadelphia
P. O. Box 66
Philadelphia, Pennsylvania 19105

Telephone (215) 574-6116

Rev. 4-79

THE RULE OF 78's

or What May Happen When You Pay Off a Loan Early

DEPARTMENT OF CONSUMER AFFAIRS
FEDERAL RESERVE BANK OF PHILADELPHIA

1. The present premium for level term credit life insurance is $1.20 per $100 for 12 months. Level term credit life insurance can only be sold on a single payment loan where the amount owed on the loan is the same for each month of the loan contract. Likewise, a credit life policy sold in conjunction with a single payment loan will insure the same amount each month and is therefore referred to as a "level term" policy.

To illustrate: Assume a $1200 single payment loan for 12 months covered by a $1200 level term credit life policy. The premium would be calculated as follows:

2. ° $1.20 premium per $100 insurance for 12 months = $1.20 x 12 months = $14.40.
   ° Stated on a monthly basis, the calculation -is- $1.20 premium ÷ 12 months = .10 per month per $100 insurance.

3. A table of the above premium charges appears as follows:

(1) Month of Ins. Policy	(2) Ins. Premium per $100 per month	(3) No. of $100's Covered Monthly	(4) Total Monthly Insurance Premium [Col. #2 x Col. #3]
1st	.10	12 x ($100)	$ 1.20
2nd	.10	12 x ($100)	1.20
3rd	.10	12 x ($100)	1.20
4th	.10	12 x ($100)	1.20
5th	.10	12 x ($100)	1.20
6th	.10	12 x ($100)	1.20
7th	.10	12 x ($100)	1.20
8th	.10	12 x ($100)	1.20
9th	.10	12 x ($100)	1.20
10th	.10	12 x ($100)	1.20
11th	.10	12 x ($100)	1.20
12th	.10	12 x ($100)	1.20
		Total Premium:	$14.40

4. By regulation, the refund on all level term policies are calculated by the pro-rate method which means to divide the total premium by the number of months of the policy and multiply that result by the number of months yet to be used of the policy. For example:

Assume the policy shown in the above table was terminated at the end of the 6th month. There would be six months not used by the policy. The calculation would be as follows:

° Total premium ÷ No. of Months in Policy = $14.40 ÷ 12 = $1.20 = premium per month.

° Premium per month x number of unused months = $1.20 x 6 = $7.20 = amount of premium to be refunded.

Atch #3

Decreasing Term Credit Life Insurance

1. Decreasing term credit life insurance is that coverage issued when an instalment loan is made which will have a balance which decreases each month because each month a payment is made. To illustrate: Assume a $1200 monthly instalment loan repayable in 12 equal payments of $100 which is covered by credit life insurance on the decreasing balance. Both the loan balance and the insurance coverage is reduced each month.

2. The same insurance premium for credit life is charged for decreasing term insurance as is charged for level term insurance, namely, .10 per $100 per month. However, there is an additional factor to consider on decreasing term insurance, namely, the amount of insurance coverage decreases each month so that the resultant dollar cost to the insured borrower is less than the cost of level term insurance.

3. To illustrate, using the above described $1200 instalment loan, we would have the following:

(1) No. of Months	(2) Balance Owed	(3) No. of $100's Covered During the Month	(4) Ins. Premium Per $100 Per Month	(5) Total Monthly Insurance Premium (Col. #3 x Co.. #4
1	$1200	12	.10	$1.20
2	1100	11	.10	1.10
3	1000	10	.10	1.00
4	900	9	.10	.90
5	800	8	.10	.80
6	700	7	.10	.70
7	600	6	.10	.60
8	500	5	.10	.50
9	400	4	.10	.40
10	300	3	.10	.30
11	200	2	.10	.20
12	100	1	.10	.10

Total No. of $100's covered: 78

Total Premium: $7.80

4. For ease of computation, decreasing term insurance premium rates are expressed at $.65 per $100 per month for one year. This may be seen for the following:

- $7.80 Total Premium for 12 months ÷ by 12 months = 7.80 ÷ 12 = .65
- A premium on a $1200 monthly instalment loan for 12 months would be calculated as follows:

  (12 months x .65 per $100 per year = $7.80 instead of using the table shown above.)

5. Rule of 78's: By looking at the above table and specifically at columns numbered (3) and (5)), one can see that the total of these columns are 78 and 7.80 respectively. By dropping the decimal and the zeros in column #5, the result is 78. It is from this that the name, Rule of 78's is derived.

6. Refunds: Since the total premium in the above table was calculated on the decreasing term balance so that the premium per month is reduced each month, under present regulation, the refund of any unearned premium is calculated on the same basis.

By adding the dollar amount for each month's premium charge the total comes to $7.80. If the policy is cancelled at the end of six months, it is seen from the above table that the premium for the first six months has been earned, namely, $1.20 + 1.10 + 1.00 + .90 + .80 + .70 = $5.70. That the amount of the earned premium is:

- $\frac{5.70}{7.80} = .7308$ of the total premium, or
- 7.80 x .7308 = $5.70

It is to be further seen that the unearned premium is the total of the last six months, which are: $.60 + .50 + .40 + .30 + .20 + .10 = $2.10.

Expressed as the Rule of 78's:

- $\frac{2.10}{7.80} = .2693$ or
- 7.80 x .2693 = $2.10

CONCLUSION: The foregoing explains why it would be wrong and unfair to abolish the Rule of 78's in computing credit insurance refunds - which would force the use of the pro-rate method.

Submitted by:

Stanley L. Lind
Counsel & Secretary
Kansas Assn. of Financial Services