



DEPARTMENT OF BUSINESS, OCCUPATIONAL AND PROFESSIONAL REGULATION
BUREAU OF CONSUMER CREDIT PROTECTION
(207)289-3731

ADVISORY RULING #81
OCTOBER 1, 1985

October 1, 1985

Re: Late charges in consumer credit transactions in which no finance charge is imposed

A creditor has inquired whether or not the Maine Consumer Credit Code prohibits or limits the assessment of late charges in consumer credit transactions in which no finance charge has been imposed.

Such charges are authorized under §2-502 as delinquency charges and are limited to the extent specified under that section. A discussion of the analysis leading to this conclusion follows.

The party requesting this Advisory Ruling is a dentist. Once services have been rendered the dentist enters into repayment agreements with his patients that spread payments over a reasonable period of time to accommodate each patient's budgetary situation. No finance charge is assessed for the privilege of making delayed payments. In many cases, however, full repayment will require more than four installment payments. In such cases the dentist acknowledges that the transactions are consumer credit sales (making him a creditor) under the Code (See §1-301(11): "...a sale of services...which is payable in more than four installments"), and truth-in-lending disclosures are provided showing a 0% APR and \$0 Finance Charge. For those patients who do not follow the repayment schedule the dentist (hereafter "creditor") would like to impose late charges to spur payment and reduce overall accounts receivable.

As a preliminary matter, and at the risk of stating the obvious, it should be noted that for those transactions with four or fewer installments, the dentist is not a creditor nor are the transactions covered by the Code. Consequently, any late charge contracted for can be imposed, provided certain other reasonable collection efforts have been initiated. (See AR # 58; Regulation Z-2 §226.4(c)(2) and the Commentary thereto.)

With regard to those transactions covered by the Code, the ability to impose late charges, and the amount of such charges, is limited. Although the term "late charge" is not defined in the Code, it is clear late charge-type payments are contemplated and are distinct from finance charges. "Charges as a result of default" and "delinquency charges" are among the types of late payment charges excluded from the definition of "finance charge" (§1-301(19)(B)(i)). The only sections expressly referencing such charges, and authorizing them, are §§2-502 and 2-503, with §2-502 being the only relevant section for purposes of this analysis.

Although §2-502 ostensibly addresses the issue of late charges in "precomputed" transactions and consumer leases, its overall purpose is to address all consumer credit transactions

with fixed yields in which late payments occur. This is revealed by an analysis of §2-502's operation and legislative amendment to it.

As originally enacted, §2-502 permitted a creditor to assess "delinquency charges" in "precomputed transactions" only, provided such charges had been contracted for and payment was more than 15 days late. A "precomputed" transaction is one in which the debt is expressed as the sum of the amount financed and the finance charge computed in advance (§1-301(31)). Late charges were allowed in such transactions because the transaction was entered into on the assumption all payments would be made as agreed, and if they were not it would be unfair to allow longer use of the creditor's money by the consumer without compensation. (Simple interest transactions, on the other hand, were not included in §2-502: creditors in such transactions are already compensated for the longer use of their money by virtue of the fact that the finance charge continues to accumulate until the obligation is repaid.)

In 1981 the logic of §2-502 was extended by the Legislature to consumer leases, transactions which have no overt finance charge but which provide a fixed yield and are based on the assumption that the repayment schedule will be adhered to. (P.L. 1981, c. 293, §2.) When a lessee is slow in paying, the lessor is denied the bargained for return on his money just as is the creditor in a precomputed transaction.

In making this change the Legislature recognized the unfairness of not allowing creditors or lessors in fixed yield transactions to recover something for the unanticipated longer use of their money, or, stated from the other perspective, of allowing slow payers to, in effect, enjoy a lower finance charge than customers who pay on time.

Considered in that light, transactions that involve no finance charges but which are consumer credit transactions simply because of their repayment schedule, are deserving of §2-502 coverage when payment is not made as agreed.

Beside its inherent logic, this argument is further bolstered by another fact. The Code is to be liberally construed and applied to promote its underlying purposes, one of which is the development of fair and economically sound credit practices (§1-102). Clearly, in the instant case, if no late charge was allowed the creditor might be forced to abandon his favorable credit policy to most consumers because of a few delinquents and impose finance charges on all accounts or raise prices on all services. Such a development could hardly be characterized as a positive development for the majority of consumers involved. Despite its certainty of legislative intent in this issue, the Bureau intends to seek legislative ratification of this position and appropriate amendment of §2-502 in the next legislative session.

While §2-502 does provide an avenue for late charges to be assessed, creditors are reminded that the conditions established in that section must still be respected with regard to the amount, timing and frequency of such assessments:

1. the possibility of late charges must be contracted for;
2. late charges may not exceed 5% of the installment amount or \$5 (now \$11.50 by virtue of adjustments in dollar amounts, §1-106) whichever is less;

3. payments must be more than 15 days late before late charges can be imposed; and
4. late charges may be assessed only once per late installment (i.e., no pyramiding).

/s/ Robert A. Burgess
Robert A. Burgess
Superintendent

RAB:as