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Semi-Monthly Payments: Impact to APR

THOUGHT LEADERSHIP

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Semi-Monthly APR

Thought Leadership

Lenders Aiming to Serve Their Customers Using Semi-Monthly Payment Products May Encounter Implementation Challenges

Regulations provide general guidance (not specifics) regarding calculations

Lenders typically look to maximize business opportunities, including adapting to their customers' needs for repayment of various loan products.

A prevalent trend seen today within the consumer lending industry is that of creditors matching repayment terms with a consumer's employment payroll schedule. From a business practice standpoint – it makes a lot of sense. If payments are scheduled on the same date the consumer gets paid, the chances of the desired availability of funds rises dramatically.

Appendix J to Regulation Z

When coupled with automated/scheduled payment arrangements through a checking or savings account, the probability of timely payments is high.

Weekly and Bi-weekly payment schedules are quite straight forward, occurring every 7 and 14 days, respectively.

However, all payroll plans are not created equal. Complexity can surface when consumer payroll is scheduled based on semi-monthly payments.

The business concept of when payments are due twice in a given month **may or may not coincide with the rather esoteric construction of Lending Regulatory rules in Appendix J to Regulation Z** for computing an accurate Annual Percentage Rate.

It is continual challenge within consumer lending mathematics to "standardize" time periods with a Gregorian calendar that contains 12 months of varying lengths within 365 calendar days in a year. Leap years further add to the challenges / complexities.

Parameters & data can be problematic, including:

- Repayment dates of the 1st & 15th
- Repayment dates after the 15th of the month couple with a payment due on the last day of each month
- A contract date originating in a non-30-day month that is between the two designated repayment dates

Combined with the practical workings of popular APR validation programs that make the lender declare the unit-period prior to calculating a value, the potential exists to have a host of varying numbers vying for the designation of the "right" APR for a given semi-monthly transaction. To be clear – **this is a two-step process**; first determining the unit-period and then computing the APR accurately using that unit-period.

A number of approaches have been observed over the years, from payments due every 15 days to any two designated dates as long as they are the same each month. **It's hard to ascertain where the latter methodology begins and ends.**

Does this approach mean payments due on the 10th and last day of each month qualify as semi-monthly unit periods according to Appendix J? **Many observers don't think so**…but sometimes it's not necessarily the framework in error, it's the implementation.

The Pathway Ahead

It's a safe assumption to make that the vast majority of employers do not consult Regulation Z before deciding how to pay their employees. From their business perspective, they employ a semi-monthly payroll schedule.

Whether or not that common payroll method translates into a lender's proper Reg. Z semi-monthly APR disclosure requires **careful examination**.

In a number of cases, t**he lender's best solution resides with a third-party computational specialist partner** who can provide their expertise and guidance to navigate through the semi-monthly payment implementation within their organization.

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