

RULE OF 78

Barbara Curran's "Trends in Consumer Credit Legislation" defines the Rule of 78 as follows:

"The Rule of 78 is merely a mathematical formula for determining the amount of the charge to be allocated to each installment period. The amount of the charge to be allocated to any particular installment period bears the same relation to the aggregate charges computed for the entire loan as the number of installments scheduled to be paid on and after the expiration of such installment period bears to the sum of the numbers designating all of the installment payments contracted for. Thus the charge applicable to the third installment period of a 12-installment contract would be $10/78$ of the total charge.⁷⁸ The "10" represents the number of installments scheduled to be paid on and after the date the third installment period terminates, and the "78" represents the sum of the numbers of all the installments contracted for (i.e., $1+2+3+4+5+6+7+8+9+10+11+12=78$). Under the Rule of 78, $10/78$ of the total charge is earned during the third installment period.⁷⁹ The refund for a loan prepaid in full will equal the aggregate of the charges to be allocated for each installment period following the date of prepayment. In other words, if the borrower prepays the loan in full on the fourth installment due date, he is entitled to $36/78$ of the aggregate of

"TABLE II.—METHOD REFERRED TO IN NOTE 56 SUPRA (UNIFORM PAYMENTS OF PRINCIPAL AND INTEREST COMBINED BUT NOT ON BASIS OF PRECOMPUTATION)

"Balances	Interest	Principal	Total payment
\$300.00	\$6.00	\$47.56	\$53.56
252.44	5.05	48.51	53.56
203.93	4.08	49.48	53.56
145.45	3.09	50.47	53.56
103.98	2.08	51.48	53.56
52.50	1.05	52.50	53.55
-----	21.35	300.00	321.35

Id. at 205.

"Precomputation: Add the total of the Interest column under either Table I or II above to total of the Principal column and then divide by number of payments in the Total Payment column. For Table I, amount will be \$53.50; for Table II, \$53.558."

⁵⁰ If charges are computed monthly on the outstanding principal balance and if monthly installment payments of principal are to be equal in amount, then the total amount of each monthly installment payment (which includes the charge for credit) will be less than the amount of the total installment payment for the preceding month. Such is the case because the credit charge is computed on the basis of the outstanding principal which decreases as each monthly installment payment is made. Since the act does not require that installments of principal be equal in amount (only that no installment can be substantially greater than the preceding installment), small loan companies are able to devise repayment schedules which provide for installment payments which combine principal and charges but which are equal in amount (except for the last installment payment, which may be somewhat less than preceding installments) and which do not violate the maximum rate provisions of the law. See Ayres, *Installment Mathematics Handbook*, "Uniform Payments Under Small Loan Laws" 202-208 (1946). This method is not to be confused with "precomputation" described subsequently in the text. The two are distinguished in note 74 *infra* following the textual discussion of precomputation.

⁷⁸ Ayres, *op. cit. supra* note 74, at 160-170.

⁷⁹ It is to be noted that the third installment is due and payable at the *end* of the third installment period. That is, the first installment period runs from the date the loan is made to the date of the first scheduled installment payment, the second installment period runs from the date of the first scheduled installment payment to the date of the second scheduled installment period, etc.