RLSS Interest Calculation Methods: How They Work and How to Edit

When a new loan is entered into the RLSS system, there are entries made that determine the method to be used when the interest for that loan is calculated. The method can be either daily or amortized, and is a required field, meaning a selection must be made before the Loan Master file can be saved. If daily interest is chosen, you must also indicate whether the interest is to be calculated on 360 or 365 days per year. The method used by the majority of GMS clients is daily, but the choice is dictated by your loan closing documents. Since closing documents are legally binding, we suggest you talk to your auditor or attorney before changing the method of calculation.

When posting repayments in Loan Activity, the interest is calculated as follows:

<u>Daily Interest</u>: The loan balance multiplied by the interest rate and then divided by either 360 or 365 (as entered in the loan master file) will determine a daily interest amount. The daily interest amount is then multiplied by the days that have elapsed since the most recent activity was recorded as determined by the activity date.

<u>Amortized Loans</u>: The loan balance is multiplied by the interest rate to determine an annual interest amount. The annual interest amount is then divided by the payment frequency (number of payments expected in a year, usually 12) to determine the amount of interest to be allocated to the repayment being posted.

Circumstances may result in the need to change a loan's terms. One change might be the way interest is calculated. For example, some agencies have closing documents that allow them to switch from amortized to daily when the loan becomes delinquent. There are also times a loan is switched from daily interest calculation to following an amortization schedule.

Whether the loan is being switched from daily to amortized or vice versa, it is important to determine 1) the date of the change, and 2) what is to happen to any interest due on the loan as of that date. The Features menu includes Loan Payoff which can be printed to show how much interest is due. Use the date of the method change as the payoff date, and review the interest fields on the report. "Past Due Accrued Interest" reflects interest that is currently a part of the loan history, and "Additional Accrued Interest" reflects interest that has accrued since the last activity was posted. Knowing how much interest is due may assist with the decision as to whether or not to accrue it for collection at a later time.

If the decision is to <u>not collect accrued interest</u>, take the following steps:

Using Loan Activity, *Adjustments*, enter a repayment. Use the date of the interest calculation change as the activity date, and enter zero as the activity total. Leave all other fields as zero. This entry should have no impact on the loan balance.

Edit/Save the Loan Master file, Loan Terms tab, to reflect the new interest calculation.

Note: If there is accrued interest outstanding on the loan history which is not to be collected, an adjusting entry is required to clear that interest. Please refer to Help, GMS Help, Loan Activity, Handling Special Situations, Adjusting Accrued Interest for instructions on making this entry.

If the decision is to <u>collect accrued interest</u>, take the following steps:

<u>Daily Interest loan being switched to Amortized:</u>

1. Using Loan Activity, enter a Repayment. Use the date of the interest calculation change as the activity date, and enter zero as the activity total. This entry should have no impact on the loan balance. However, you will see a positive amount in the "accrued interest" field. This reflects the interest that has accrued on a daily basis from the last recorded activity date to the date used for this activity. Once the entry is saved, this accrued interest will be a part of the loan's history and will be collected automatically from future repayments.
2. Edit/Save the Loan Master file, Loan Terms tab to reflect the new interest calculation.

<u>Amortized loan being switched to Daily Interest:</u>

1. Using Loan Activity, *Adjustments*, enter a repayment. Use the date of the interest calculation change as the activity date, and enter zero as the activity total. Manually enter the amount listed as "additional accrued interest" from the Loan Payoff report (see above) under both "current interest" and "accrued interest". This entry should have no impact on the loan balance. Once the entry is saved, this accrued interest will be a part of the loan's history and will be collected automatically from future repayments.

2. Edit/Save the Loan Master file, Loan Terms tab, to reflect the new interest calculation.

Regardless of the entry being made, please pay close attention to the "new paid-thru date" and the "next payment due" fields and be certain they are accurate before saving the entry. Sometimes terms change as part of a work-out agreement, and that agreement may also affect these dates. Remember, "next payment due' determines when a loan appears as delinquent on reports. These entries are necessary to have a record in the loan history that reflects the date of the interest calculation change and to allow interest to be collected accurately from subsequently recorded activity.