RULES and REGULATIONS
FEDERAL RESERVE SYSTEM
12 CFR Part 226
[Reg. Z; Docket No. R-0288]
Truth in Lending; Revised Regulation Z
Tuesday, April 7, 1981

***20848** AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board is adopting a complete revision of its Regulation Z (Truth in Lending). The revision implements the Truth in Lending Simplification and Reform Act (Title VI of the Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. 96-221) and substantially alters the requirements and the structure of the current regulation. Within the last year, the Board has twice published proposed revisions of the regulation (45 FR 29702, May 5, 1980, and 45 FR 80648, December 5, 1980) and received more than 1000 comments on those proposals.

The new regulation becomes effective on April 1, 1981, but creditors have the option of continuing to comply with current Regulation Z until March 31, 1982. Beginning April 1, 1982, creditors subject to Regulation Z must comply with the revised regulation.

The Board has consolidated the consumer leasing provisions contained in current Regulation Z and is publishing them as a separate regulation (Regulation M, 12 CFR 213) published elsewhere in this issue.

EFFECTIVE DATE: April 1, 1981, but compliance optional until April 1, 1982.

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SUPPLEMENTARY INFORMATION:

(1) General. In March 1980, Congress adopted the Truth in Lending Simplification and Reform Act (Title VI of the Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. 96-221). Although the act has been revised several times since its adoption in 1968, the Simplification Act marked the first concerted effort by Congress, partly on the basis of recommendations from the Federal Reserve Board, to reduce federal Truth in Lending requirements. Among its major provisions are (1) a significant reduction in consumer credit disclosures, particularly in closed-end transactions, (2) reimbursement requirements for certain cost understatements, (3) a decrease in civil liability for violations, and (4) revisions in the act's application to real estate transactions.

Following the enactment of the revised statute, the Board twice published proposed revisions of Regulation Z. The first proposal was published on May 5, 1980 (45 FR 29702) and incorporated changes mandated by the revised act, as well as a number of substantive and structural changes from the current regulation. After analysis of more than 500 comments on that proposal, the Board published a second revised regulation for comment on December 5, 1980 (45 FR 80648), which proposed further substantive changes. The Board received approximately 530 comments on the second proposal. (Copies of these comments are available through the Office of the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C.)

The revised act and regulation reflect a growing concern in Congress and elsewhere that Truth in Lending has not completely fulfilled its original purposes. In the last decade, surveys indicate that Truth in Lending has heightened consumers' awareness and understanding of the cost and terms of consumer credit transactions. During the same period, however, it has become increasingly evident that the act has imposed highly complex and technical requirements on creditors, produced disclosures that sometimes obscured the important information to consumers, and generated costly and burdensome litigation over technical interpretations of the regulation.

The revised regulation addresses these concerns in its emphasis on disclosure of essential credit information in a straightforward manner, and on reduction in the number of technical disclosure burdens placed on creditors. The regulation's focus on simplified disclosure of material terms should benefit consumers by providing a more useful basis for credit decisions, and creditors by reducing the difficulty of compliance.

An official commentary to the regulation, to be published in the near future, will incorporate those Board and staff interpretations previously issued on current Regulation Z that remain applicable to the new regulation. The commentary, which will be issued in the form of an official staff interpretation, will provide additional guidance regarding application of the regulation and will incorporate some of the detailed material from the current regulation.

One major change in the revised regulation, not reflected in the earlier proposals, is the deletion of the requirements relating to consumer leases. The Consumer Leasing Act was adopted by Congress in 1976 as an amendment to the Truth in Lending Act, and the Board's regulations to implement the leasing provisions have until now been incorporated into Regulation Z. Because they are unrelated to the basic credit orientation of the regulation and are relevant to comparatively few institutions, the leasing provisions have been placed in a separate Regulation M. The new regulation, which makes no substantive change in the leasing requirements of the current regulation, is also being adopted at this time and appears elsewhere in this publication. Regulation M incorporates the leasing forms that now appear in Board Interpretation §§ 226.1501, 226.1502, and 226.1503.

As in the earlier proposals, the regulation is divided into subparts, with Subpart B addressing open-end credit and Subpart C containing rules for closed-end credit. Subparts A and D reflect general provisions of the regulation that relate to both open-end and closed-end credit. The appendices following Subpart D are formally a part of the regulation and contain a variety of technical material, specialized rules and procedures, as well as the model forms and clauses for compliance with the regulation. Supplement I to current Regulation Z, which sets forth equations and instructions for calculating the annual percentage rate, has been redesignated as Appendix J, but is otherwise substantially unchanged.

The new act becomes effective on April 1, 1982, but requires the Board to ***20849** adopt final rules implementing the act by April 1, 1981. In order to provide an adequate transition period during which creditors may begin adjusting their forms and procedures to the new rules, creditors have the option for the intervening year of complying with either the current regulation or the revised regulation. By April 1, 1982, creditors must be in compliance with the revised regulation. Creditors may begin complying with the revised regulation as soon as they are able, but they are not required to do so unit April 1, 1982. A creditor may wish to convert its entire operation to the new requirements at one time or it may prefer to phase in the new requirements over time, for example, by converting to the new rules by category of transaction, by branches or offices, or even by transaction. Any of these approaches is acceptable. In addition, a creditor may choose to follow the revised regulation's rules on credit advertising and the right of rescission even though it has not yet converted its other operations to the new regulation.

In addition to the new provisions on how to make disclosures, the revised regulation contains a number of new rules regarding coverage. A creditor may use the new coverage rules to make the determination as to whether a particular transaction or the creditor itself is covered by Regulation Z. For example, layaway plans are not subject to the new regulation, nor are oral agreements, payable in more than four installments if there is no finance charge. These provisions may be relied on even if a person is using the current regulation for its other operations. Similarly, a person may use the 25 transactions per year rule of the creditor definition to decide whether or not it is subject to the regulation.

Creditors may not, however, "mix and match" requirements from the current and the revised regulations in making the disclosures for a single transaction. For example, all of the disclosures for a closed-end credit transaction must be made in accordance with the current regulation or all of them must be made in accordance with the revised regulation. Similarly, an open-end creditor must comply either with all the current rules or with all the revised rules for any individual account. (Of course, periodic statements may be made under the new requirements even though the initial disclosures were made under the old.) A creditor may avail itself of the new tolerances only if it complies with the revised regulation.

The Board and staff interpretations that have been issued under the current regulation will continue to be effective until April 1, 1982, for those creditors complying with the current regulation. Those interpretations and letters will be revoked as of that date.

The Board hopes these rules will provide for a simple, orderly transition from old to new rules with a minimum of disruption and inconvenience.

Five states have been granted exemptions from current Regulation Z. Those exemptions--to Connecticut, Maine, Massachusetts, Oklahoma, and Wyoming-- do not expire until April 1, 1982.

(2) Section-by-section analysis. Set forth below is a section-by-section analysis of the revised regulation, followed by the text of the regulation. In the discussion of the provisions, the regulation as it existed prior to this Board action is referred to as the "current" regulation; the regulation as modified by this action is referred to as the "revised" regulation.

§ 226.1 Authority, purpose, coverage, organization, enforcement and liability.

This section restates the authority and purpose provisions now contained in § 226.1(a) of the current regulation, and describes the coverage of the regulation. It also explains the reorganization of the regulation into four major subparts, and directs attention to the shifting of certain material from the regulatory text into appendices and a commentary to be produced in the near future.

The leasing provisions have been removed from Regulation Z and are being issued as a separate regulation, Regulation M. The Board believes that since consumer leasing is engaged in by such a small proportion of the people covered by Regulation Z, it makes more sense to provide the requirements separately. The separation of leasing from credit is aimed at making both regulations easier to use.

This section reflects some minor editorial changes from the December proposal. A footnote has been added to clarify that credit is "regularly" offered only if it meets the specific standards set out in the definition of creditor. In paragraph (c)(1)(iii) the word "payable" replaces the word "repayable" to more clearly apply to sales as well as loans. The list of enforcement agencies has been added to the enumeration of the contents of the appendices in paragraph (d)(6). However, the detailed description of the appendices has been deleted so that if appendices are added later, such additions will not require amendments to this section.

The foreign application of Regulation Z was a concern to some commenters, particularly with regard to credit cards. The commentary will clarify the Board's position that if an account is located in the U.S. and credit is extended to a U.S. resident, the transaction is subject to Regulation Z. This will be the case whether or not the transaction takes place in the U.S. and whether or not the extender of credit is chartered in the United States or a foreign country.

Paragraph (e) of the revised regulation refers to the various civil and criminal liability provisions of the act. It does not describe the content of those provisions as does § 226.1(c) of the current regulation; it is meant merely as an easy cross-reference to the applicable provisions of the act. The reference has been expanded from that in the December proposal to include § 113.

§ 226.2 Definitions and rules of construction.

Section 226.2 is organized in two paragraphs: § 226.2(a), which contains in alphabetical order the definitions that apply to the regulation, and § 226.2(b), which contains the rules of construction. The leasing provisions have been removed from the revised regulation and incorporated into a separate regulation, new Regulation M; therefore, all references to leases have been deleted from this section. Section 226.2 incorporates virtually all of the defined terms used in current Regulation Z and all of the terms defined in the December proposal, with the exception of "personal property" which has been eliminated because its definition relates primarily to leases.

(a) Definitions.

Act. This definition cites the original and the amended statutes and corresponds to § 226.2(b) of the current regulation. This term was a rule of construction in the December proposal.

Advertisement. This definition describes the advertisements that are subject to §§ 226.16 or 226.24. It is based on § 226.2(d) of the current regulation.

The definition has been slightly revised from that in the December proposal. The phrase "is designed to promote" has been replaced by the word "promotes," a more direct way of expressing the idea intended.

Two additional things should be noted about advertisements. First, the definition continues to exclude direct personal contact, such as follow-up letters and cost estimates for individual consumers. Second, all persons, not only creditors, must comply with the advertising requirements of §§ 226.16 and 226.24.

Arranger of credit. This definition is based on amended § 103(f) of the act, which includes in the definition of ***20850** "creditor" persons in the business of arranging credit under certain limited circumstances. The scope of the definition is narrower than § 226.2(h) of the current regulation, because it includes only professional arrangers acting on behalf of primary lenders who do not themselves fit the definition of "creditor." To fall within this definition, a person must arrange for extensions of consumer credit (that is, credit subject to a finance charge or payable by written agreement in more than four installments) by non-creditors more than the specified number of times a year. Footnote 2 sets forth the numerical standards, which are the same as those used in the definition of "creditor," discussed below. The first part of the definition has been redrafted to clarify that the numerical standard applies only to the instances in which credit arranged is in fact extended and not to instances in which credit is offered but not accepted.

Billing cycle or cycle, which corresponds to § 226.2(i) of the current regulation, is unchanged from the December proposal. The definition incorporates a longstanding staff position that these cycles must be no longer than a quarter of a year.

The revised regulation differs from the current regulation in that it also requires periodic statement cycles to be equal, whereas the current regulation only sets forth the rule for when such cycles may be considered equal for computation and disclosure purposes. The requirement that cycles be of equal intervals is intended both to facilitate accurate disclosures and to ensure the furnishing of statements on a regular basis.

The revised regulation retains the provision allowing a creditor to consider as equal the intervals at which statements are sent, unless a particular statement date varies by more than four days from the regular date used by the creditor. In addition, the revised definition allows greater flexibility than the current one by permitting a creditor that uses regular statement days (such as the third Thursday of every month) to measure its four-day variance from that day, rather than from the date on which it falls.

The Board notes that the revised definition refers to both "billing cycle" and "cycle," in light of the fact that many creditors do not bill in the traditional sense, but rather send statements of the account to consumers. No substantive change is intended by this addition.

Board. This definition is virtually identical to § 103(b) of the act and § 226.2(k) of the current regulation. It is defined here to avoid needless repetition elsewhere in the regulation.

Business day. This definition is based on the combination of footnote 14 to § 226.9 of the current regulation and the definition of "business day" in the December proposal.

This definition provides a general rule applicable to most sections of the regulation and a special rule applicable only to the provisions on the right of rescission. The general rule, based on a creditor's normal operating schedule, is identical to the December proposal. It is substantially similar to its counterpart in Regulation E, which implements the Electronic Fund Transfer Act. The rule for transactions subject to the right of rescission is virtually identical to footnote 14 to § 226.9 of the current regulation. The Board believes, based on the comments, that transactions subject to the right of rescission need a more definite and uniform business day definition and that a separate definition for those cases is justified. Thus, it has adopted this two-tiered definition.

Card issuer. The definition of card issuer is unchanged from the December proposal and § 226.2(l) of the current regulation.

Cardholder. This definition differs in structure, but not in scope, from § 226.2(m) of the current regulation. The current regulation provides that a "cardholder" means any person to whom a credit card is issued for any purpose. Because of limitations set forth elsewhere in the act and regulation, however, general coverage is in fact restricted to natural persons who are issued the cards for consumer credit purposes. Other persons to whom cards are issued and cards issued for non-consumer credit purposes are covered only by the provisions regarding credit card issuance and liability. The revised definition reflects this distinction, as did the December proposal, and makes clear that a natural person guaranteeing a business credit card is not a cardholder except for the limited purposes of § 226.12 (a) and (b).

The revised regulation differs from the December proposal by deleting language tying coverage as a cardholder to whether the card was issued at the request of that person. Guidance on credit card issuance appears in § 226.12(a) and the accompanying material.

Cash price. This definition is based on § 226.2(n) of the current regulation. The statement that charges imposed equally in cash and credit transactions are included has been deleted from the definition since it essentially repeats the sense of the first sentence. This item is no longer a required disclosure, as it is in the current regulation.

The definition has been revised from the December proposal. The language "at the creditor's option" has been added to the second sentence to stress the permissive nature of the rule regarding what can be included in the cash price. The word "optional" has been deleted from the phrase "optional accessories" as unnecessary; and no change in meaning is intended.

The Board has received numerous questions regarding the proper treatment of rebates, both manufacturer's and seller's, in credit sale transactions. The Board believes that a uniform rule regarding their treatment for Truth in Lending purposes is neither desirable nor feasible. This represents a change from the staff's position under the current regulation that rebates had to be disclosed in a particular manner. This means that rebates need not be reflected in the Truth in Lending disclosures, and if they are reflected, the creditor may treat them in any manner.

Closed-end credit. This definition has no counterpart in the current regulation. However, it has long been unofficially used to describe the type of credit referred to in the act as "other than open-end." The definition is identical to the one in the December proposal. Subpart C contains the substantive rules that apply to closed-end credit transactions.

Consumer. This definition is based partly on the statutory definition in § 103(h) and partly on the definition of "customer" in § 226.2(u) of the current regulation.

The definition has been significantly revised from the December proposal.

It provides a general rule for most sections of the regulation and a special rule applicable only to the provisions on the right of rescission. The general rule significantly reduces the scope of the definition from that in the current regulation and December proposal; it includes only cardholders and natural persons to whom consumer credit is offered or extended. This means that persons such as endorsers, guarantors or sureties are no longer "consumers" for purposes of the general rule.

The special rule for rescission, however, broadens the definition to include any natural person (such as a guarantor, surety, or a person who is not liable on the credit obligation) when that person's home is subject to the risk of loss. That person has the right to receive the material disclosures and the notice of the right to rescind and may rescind the transaction.

***20851** There is one exception to the rule that a consumer must be either a natural person or a cardholder. Credit extended to land trusts, as described in the material accompanying § 226.3 of this regulation, is considered consumer credit extended to a consumer for Truth in Lending purposes.

Consumer credit. This definition is based on § 226.2(p) of the current regulation, and is identical to the December proposal.

Consummation. This definition is based on § 226.2(kk) of the current regulation, which defines consummation in terms of the creation of a contractual relationship, and is the same as that in the December proposal. As before, state law determines when the contractual obligation arises, but the revised definition focuses on when the consumer becomes obligated.

This definition is a significant departure from longstanding staff interpretations of the current regulation that had added the concept of "economic coercion" to the test of when consummation occurs. Under the revised definition, consummation occurs only when the consumer becomes contractually obligated on the credit transaction. The time at which a consumer becomes contractually obligated on a purchase does not determine when consummation occurs for Truth in Lending purposes, as long as there is no credit obligation. For example, when a consumer pays a nonrefundable deposit to purchase an automobile, a sales contract may have arisen. However, consummation for Truth in Lending purposes does not occur unless the consumer also contracts for financing at that time.

Credit. This definition is based on § 103(e) of the act and § 226.2(q) of the current regulation. It is identical to the one in the December proposal. The regulatory definition may be difficult to apply in particular fact situations, and the Board therefore offers the following guidance, which will also be incorporated into the commentary.

In the Board's view, layaway plans are not extensions of credit, unless the consumer is contractually obligated to continue making payments. Whether the consumer is so obligated is a matter to be determined under state law. The fact that the consumer is not entitled to a refund of any amounts paid towards the cash price of the merchandise does not bring layaways within the regulation. This position on entitlement to a refund is contrary to current Board Interpretation § 226.201.

Certain transactions do not involve the voluntary incurring of debt; others do not involve the right to defer a debt. Tax liens, tax assessments and court judgments (including reaffirmations of a debt discharged in bankruptcy, if approved by a court) fall into this category and are therefore not covered by the regulation. However, third-party financing of such obligations (for example, obtaining a bank loan to pay off a tax lien) would constitute credit for Truth in Lending purposes.

If the consumer's payments generally parallel the value received from the other party, with no continuing obligation to make payments, the Board does not view this as an extension of credit. For example, certain insurance premium plans involve payment in installments; each installment represents payment for insurance for a certain future period of time. If the consumer fails to make a payment, coverage is not provided for that period. There is in this case no obligation for the consumer to continue making payments. Similarly, in a home improvement transaction involving progress payments, the consumer simply pays the value of work completed as the work progresses, with no contractual obligation to continue payments. Thus, these types of transactions are not covered by the regulation.

Certain types of loans are not viewed as extensions of credit. For example, where the consumer borrows money against the accrued cash value of an insurance policy, credit has not been extended because the consumer is, in effect, only using the consumer's own money.

Issuance of letters of credit and execution of option contracts are not extensions of credit, although there may be an extension of credit when the letter of credit is presented for payment or the option is exercised, if there is a deferral of the payment of a debt at that time.

In the December proposal the Board suggested that pawn shop transactions not be viewed as credit extensions. The Board now believes that these types of transactions are credit extensions for Truth in Lending purposes. This approach is consistent with staff interpretations of the current regulation.

Credit card. This definition corresponds to § 226.2(r) of the current regulation with only minor editorial changes. The revised regulation differs from the December proposal since it returns to the current regulation's language that a credit card is a "single" credit device. This was done simply as a clarification and no substantive change is intended.

Credit sale. This definition is based on § 103(g) of the act and § 226.2(t) of the current regulation. It is similar to that in the December proposal, except that "total value" replaces "aggregate value" in paragraph (a)(16)(i) and parentheses have been added to paragraph (a)(16)(ii) to improve readability.

Creditor. This definition is based on amended § 103(f) of the act, and is revised from § 226.2(s), its counterpart in the current regulation.

The definition retains in paragraph (a)(17)(i) the "regularly extends" standard found in the current regulation. However, new footnote 3 defines "regularly" by reference to the frequency with which credit is extended. The numerical tests are similar to those in the December proposal, but they have been revised to include persons who meet the numerical test in the current year even if they did not meet it in the preceding year.

For example, if a business begins in 1981 and extends unsecured consumer credit 20 times, it is not a creditor for purposes of the regulation in 1981.

However, if it extends consumer credit 75 times in 1982, it becomes a creditor for Truth in Lending purposes after the 25th extension of credit. On the other hand, if a person extends consumer credit 26 times in 1981, then it is a creditor for Truth in Lending purposes for all extensions of consumer credit in 1982. The Board believes these numerical tests will be most useful in cases when a person does not extend credit as part of its primary business and therefore is genuinely unsure whether it is a "creditor" for Truth in Lending purposes.

The definition has also been revised to require, if there is no finance charge, that there be a written agreement to pay in more than four installments, in order for a person offering credit to be considered a creditor. This is narrower than in the current regulation, which covers both oral and written agreements. Whenever a finance charge is imposed, of course, the transaction would come within the regulation's coverage whether or not there is a written agreement. This is consistent with the approach taken in the current regulation.

The requirement in paragraph (a)(17)(i)(B) that, for a person to be a creditor, the obligation must be initially payable on its face to that person, is new; it implements amended § 103(f) of the act.

Paragraph (a)(17)(ii) implements amended § 103(f) of the act and is identical to its counterpart in the December proposal.

Paragraph (a)(17)(iii) of the definition, which extends the coverage of certain provisions of the regulation to persons ***20852** who honor credit cards, is substantively unchanged from the current regulation.

Paragraphs (a)(17) (iv) and (v) of the definition impose certain creditor responsibilities on card issuers. Although the provision has been reorganized from the current regulation, the Board intends no substantive difference in coverage between the current and the revised regulations.

Paragraph (a)(17)(iv) provides that card issuers are creditors for purposes of Subpart B if they extend open-end credit or consumer credit not involving either a finance charge or a written agreement to pay in more than four installments. As all disclosures are to be made only as applicable, a card issuer that extends consumer credit without a finance charge would, of course, omit finance charge disclosures. Other general provisions of the regulation regarding such areas as scope, definitions, Spanish language disclosures, record retention, and use of model forms also apply.

Paragraph (a)(17)(v) applies to a card issuer extending consumer credit that does not meet the test for open-end credit. This paragraph corresponds to § 226.8(q) of the current regulation, which imposes certain open-end disclosures and error resolution responsibilities on credit card issuers, even though they are also fully subject to the closed-end credit requirements. The parenthetical is intended to make clear that such a card issuer need not make both open- and closed-end finance charge disclosures, and is subject to the closed-end, rather than the open-end, rescission provision.

Downpayment. This definition is a new one that has no statutory counterpart. The definition has been revised from the December proposal by deleting the reference to the amount financed and payment schedule. This change was made merely to streamline the definition.

The second portion of the definition deals with deferred portions of the downpayment, often referred to as "pick-up payments." It permits pick-up payments to be treated as part of the downpayment and excluded from the amount financed, as does Board Interpretation § 226.504 of the current regulation. The revised regulation, however, does not require creditors to reflect the deferred amount in the payment schedule.

Thus, the creditor has several options available concerning the treatment of pick-up payments. For example, when the pick-up payment is treated as part of the downpayment: (1) it is not included in the amount financed; and (2) it may but need not be reflected in the payment schedule. On the other hand, when the pick-up payment does not meet the definition (for example, if it is payable after the second scheduled payment) or when the creditor chooses not to treat it as part of the downpayment: (1) it must be included in the amount financed; and (2) it must be reflected in the payment schedule. However the pick-up payment is treated, the total of payments must equal the sum of the payments disclosed.

Dwelling. This definition implements new § 103(v) of the act. The definition is broader than its counterpart in § 226.2(v) of the current regulation in that it includes mobile homes and cooperatives, as well as other residential units. The definition continues to exclude from its scope structures that are not used as residences.

Open-end credit. This definition, which corresponds to § 226.2(x) of the current regulation, implements the amended § 103(i) of the act. The provision differs significantly from the current regulation, as discussed below. Although the definition is substantively unchanged from the December proposal, major editorial changes have been made.

The current regulation, and the December proposal, provide in part that open-end credit is credit extended on an account pursuant to a plan. A number of commenters, particularly credit unions, asked for further guidance on whether a program offering a number of different credit features could be considered one open-end credit account. Under many of these programs, each consumer is deemed to have a single "account" with the institution that could be accessed repeatedly via a number of sub-accounts established for the different program features and rate structures. Some individual features of the program could be used repeatedly (for example, an overdraft) whereas others might be used infrequently (such as the part of the credit line available for credit secured by an automobile). If the program as a whole has prescribed terms and otherwise meets the open end-credit definition, the Board believes that such a program could be considered a single multi-featured account. To help alleviate confusion caused by the use of the term "account," the revised regulation has deleted the reference to "account" found in both the current regulation and the December proposal, and instead uses the statutory language that refers to open-end credit "plans."

Paragraph (a)(20)(i) of the definition provides that the creditor must reasonably contemplate repeated transactions on the plan. This is unchanged from the December proposal and reflects an amendment to § 103(i) of the act. This part of the open-end credit definition replaces the current regulatory requirement that the terms of the plan provide for credit transactions "from time to time." The current regulatory requirement that the creditor reasonably contemplate multiple transactions was intended, according to the Senate Report on S. 108, to curb the use of spurious open-end credit plans.

In particular, the committee expressed the belief that consumers should receive essential cost disclosures, such as the total finance charge and the total of payments, when a creditor makes what is likely to be a one-time credit extension. A number of commenters asked for guidelines on determining when a creditor may be said to contemplate such repeated credit extensions. The Board believes that this is a question of fact to be decided in the context of the creditor's type of business, and the creditor's relationship with a consumer. For example, as discussed in the notice accompanying the December proposal, it would be more reasonable for a thrift institution chartered for the benefit of its members to contemplate repeated transactions with a member, than for an aluminum siding dealer to make the same assumption about its customers. Similarly, it would be more reasonable for a bank to contemplate repeated transactions when it makes a purchase money loan for an automobile to be used by the consumer to further secure an open-end line than it would be for an automobile dealer to sell a car under open-end plan.

The current regulation requires that the consumer have the privilege of paying the balance in full or in installments. The revised regulation deletes this test. The Board believes that a plan in which purchases are contemplated from time to time, with finance charges imposed on the outstanding unpaid balance, would qualify as open-end credit, even though full payment is required at the end of each month. The December proposal contained a modified version of the current provision, setting forth the test that the consumer must be given the privilege of paying the balance in full at any time without penalty. The Board solicited comment on the need for this test, in light of the fact that the definition requires calculation of the finance charge on the basis of the outstanding unpaid balance, thus already distinguishing open-end plans from plans involving precomputed finance charges. While a few ***20853** commenters believed that the language provided a useful distinction from closed-end credit, the majority of commenters on this section felt that the provision should be deleted.

Paragraph (a)(20)(ii) of the revised regulation, regarding the computation of finance charges, is unchanged from the current regulation and the December proposal.

Paragraph (a)(20)(iii) of the revised regulation, which was paragraph (4) of the December proposal, has no counterpart in the current regulation but does not substantively alter the open-end credit definition from the current definition. This factor is intended to assist creditors in distinguishing open-end credit from a series of advances made pursuant to a loan commitment. Under such a commitment, for example, a creditor might agree to lend a total of $10,000 in a series of advances as needed by the consumer. When a consumer has borrowed the full $10,000, no more money is advanced under that particular agreement even if there has been a repayment of a portion of the debt. Such a commitment would be considered closed-end credit. This paragraph has been editorially revised from the December proposal in response to commenters' concerns. The language providing that the amount of credit is "replenished to the extent that the consumer repays on the outstanding balance" has been replaced by "is generally made available to the consumer to the extent that the consumer repays the outstanding balance." By this language the Board intends to make clear that the creditor may make allowance for reductions in the credit line or refuse to extend credit in a particular case due to changes in the economy, the creditor's financial condition, or a change in the borrower's creditworthiness. While the consumer should have a reasonable expectation of obtaining credit as long as the account remains current and within any present credit limits, an extension need not be an absolute right in order for the plan to be considered open-end credit.

The Board also notes that the revised regulation differs from the current regulation in deleting the per se exclusion from open-end credit of negotiated advances under an open-end real estate mortgage or a letter of credit.

Periodic rate. The definition of periodic rate in the revised regulation combines two definitions from the current regulation: § 226.2(z) ("period") and § 226.2(aa) ("periodic rate"). The definition differs from § 226.2(aa) of the current regulation, as well as from the December proposal, in deleting the requirement that the rate be expressed as a percentage of the finance charge imposed against the balance for a particular period. The Board believes that a creditor may express the rate either as a percentage or as a decimal equivalent. Of course, the annual percentage rate derived from the periodic rate must always be expressed as a percentage.

As is the case under § 226.2(aa) of the current regulation, a creditor may use any subdivision of a year in disclosing and applying its rate, as long as it does so within the degree of accuracy required in the regulation. Some creditors use 1/360th of a year as a period for which a rate is applied, for example they may disclose this rate as a "daily" periodic rate, without further explanation, as long as it is in fact only applied 360 days per year. In contrast, if a creditor discloses a rate based on

1/360th of a year but applies it for 365 days, the creditor would have to note that fact and, of course, disclose the true annual percentage rate.

Person. This definition combines the definitions of "organization" and "person" found in § 103(c) and (d) of the act and § 226.2(y) and (bb) of the current regulation. The definition is identical to the one in the December proposal. The list of types of organizations is only illustrative and is not intended to be all-inclusive.

Prepaid finance charge. This definition is based on § 226.8(e)(1) of the current regulation. It is like the definition in the December proposal, except that it uses "proceeds" instead of "principal" to parallel more closely the language of amended § 128(a)(2) of the act.

The term does not include precomputed finance charges such as add-on and discount interest. The rule that these are not prepaid finance charges replaces the permissive rule in Board Interpretation § 226.819 of the current regulation.

Regular price. The definition of regular price, found in § 226.2(tt) of the current regulation, has been deleted. The definition is unnecessary as part of the revised regulation since the detailed provisions concerning certain cash discounts found in § 226.4(i) of the current regulation have been deleted. Instead, § 226.4(c)(8) of the revised regulation merely refers to § 167(b) of the act for details about which cash discounts may be excluded from the finance charge. Any discussion of the "regular price" of a property or service would be included in the commentary to § 226.4(c)(8).

Required deposit balance. Although this section does not define this term, required deposits must be disclosed in closed-end credit transactions under § 226.18(r). See further discussion below.

Residential mortgage transaction. This definition is based on new § 103(w) of the act and has no counterpart in the current regulation. The definition is the same as that in the December proposal except that the word "principal" has been added to modify "the consumer's dwelling." This change limits the scope of the definition by excluding vacation for temporary dwellings, a limitation the Board believes is consistent with the Congress' intent in treating residential mortgages differently from other transactions. Thus, various of the regulation's special rules--such as the disclosure of the creditor's assumption policy in § 226.18(q) and the early disclosure requirements in § 226.19-- apply only to transactions involving the acquisition of the consumer's principal dwelling.

Security interest. This definition is based on § 226.2(gg) of the current regulation, but is much narrower. The revised definition lists a number of interests that have been considered security interests under the current regulation but no longer will be, such as interests in after-acquired property. It also eliminates disclosure of interests that arise solely by operation of law, although such interests may still trigger the right of rescission.

One change from the definition in the December proposal is the addition of the word "solely" to the phrase "by operation of law" in the last two sentences. The effect of this change is to clarify that if an interest (such as a right of setoff) arises both by contract and by operation of law, it is a security interest to be disclosed.

Finally, it should be noted that there is a difference between an incidental interest and an interest that is the essence of the transaction. For example, when an automobile is financed, the insurance proceeds are incidental to the primary security interest, the automobile. The creditor's interest in such insurance would not be a security interest under the regulation. On the other hand, when the credit transaction is the financing of an insurance policy, the creditor's interest in that policy is just like a purchase money security interest and would be disclosed as a security interest.

State. This definition is identical to § 103(r) of the act and § 226.2(hh) of the current regulation.

(b) Rules of construction. Section 226.2(b) contains rules of construction that are intended to assist in understanding the regulatory language and to permit abbreviated references in ***20854** the text of the regulation. They are based on § 226.2 of the current regulation, with the addition of rules about singular and plural forms, the status of footnotes, and reference to state law for words not defined. The reference to the status of catchlines and captions has been eliminated as unnecessary. References to leasing have been deleted and the explanation of "act" has been made a definition in paragraph (a).

§ 226.3 Exempt transactions.

This section provides for the exemption of several types of transactions from the regulation. There has been little change from the December proposal other than minor editorial changes.

The new provision is basically the same as that in the current regulation.

It reflects the total exemption of agricultural credit. An agricultural purpose is defined the same way as in the current regulation, but it also includes the acquisition of real property (including real property with a dwelling), personal property, and services, if the acquisition is used primarily in any of the specified activities.

The business credit exemption has been qualified to clarify that several credit card provisions do apply to business credit. Although business and commercial purposes are not defined in the regulation, more specific guidance in the area of rental property will be provided in the commentary. The approach taken in current Board Interpretation § 226.302, which defines certain credit for multiple-unit dwellings as business credit, will be adopted and expanded. If the property (regardless of the number of units) is not owner-occupied and is not expected to be owner-occupied within a year, the credit will be deemed to be for business purposes. Where the property contains three or more units, the credit will also be deemed to be for business or commercial purposes, even if one or more of the units is or will be owner-occupied. The Board hopes that this more precise test will simplify the determination of whether transactions are subject to the regulation's requirements.

An editorial change was made to § 226.3(a)(2) of the December proposal. The word "organizations" has been replaced by the phrase "person other than a natural person." This change was made to avoid the use of a term that is not defined in the regulation. Note that the definition of "person" includes organizations. There was also a minor change to § 226.3(b) of the December proposal. The word "a" before the word "dwelling" has been replaced with the word "the" to reflect the statutory language and to clarify that only one dwelling can be a consumer's principal dwelling.

The addition of the parenthetical, "(including extensions of such facilities)" expands the coverage of the public utility exemption in revised § 226.3(c). The result is a departure both from the current regulation and the December proposal. It addresses the case where utility service is to be extended into a new area not already served, and the customers who request the extension are required to pay for some or all of the transmission equipment needed. Such equipment may include pipes and wires, conduits and poles, metering equipment and transformers. The Board believes that such extensions of public utility services should be exempt because they are analogous to the exempt services. This section makes it clear, however, that an extension of credit by a public utility for the purchase of appliances such as telephones or home improvements is not exempt. These extensions of credit are closer to the typical credit transaction covered by Regulation Z.

The exemption for securities transactions in the current regulation has been expanded to also apply to commodities transactions with a broker-dealer registered with the Commodity Futures Trading Commission.

The regulation provides a new exemption for home fuel budget plans in which the fuel dealer estimates the total cost for the season, bills the consumer for an average monthly payment, and makes an adjustment in the final payment for any difference between the estimated and the actual cost of the fuel. Fuel is delivered as needed, no finance charge is assessed, and the customer may withdraw from the plan at any time. These plans are not subject to the revised regulation, even if they involve a charge to cover billing costs.

The Board received comment requesting an exemption for hospital credit.

Although such an exemption has not been adopted, the Board notes that if hospitals do not impose a finance charge, They are subject to the revised regulation only if they have written agreements specifically contemplating that the bill will be payable in more than four installments. This means that if the hospital makes informal oral agreements, it is not subject to the regulation.

A question was also raised in the comments as to whether credit extended to a land trust is organizational credit and therefore exempt from the regulation under revised § 226.3(a)(2). In some jurisdictions, a bank financing a residential real estate transaction for a customer (a natural person) uses a land trust mechanism. Title to the property is conveyed into the land trust for which the bank itself is trustee. The underlying installment note is executed by the bank in its capacity as trustee and payment is secured by a trust deed, reflecting title in the bank as trustee. In some instances, the bank customer executes a personal guarantee of the indebtedness. The note indicates that it is payable only out of the property specifically described in the trust deed and that the trustee has no personal liability on the note. The Board believes that such transactions should be subject to the regulation's disclosure requirements since in substance (if not in form) consumer credit is being extended.

In the December proposal, the Board solicited comment on the necessity of an exemption for trusts that extend credit. After careful consideration, the Board has decided that although an outright exemption is not appropriate, each trust should be treated as a separate entity for purposes of determining whether it is a "creditor." In other words, if an individual trust extends credit frequently enough to meet the numerical standard set out in the definition of "creditor," then all the required disclosures must be made. Furthermore, the trustee will be considered to be the same person as the trust and therefore the trustee does not meet the definition of "arranger."

§ 226.4 Finance charge.

Section 226.4 provides rules for determining the finance charge in open-end and closed-end credit transactions. A few substantive changes have been made and the format is quite different from § 226.4 of the current regulation. The format was changed in order to make the treatment of various items clearer and easier to understand. For example, in the current regulation, the procedures for excluding insurance premiums from the finance charge were included with the examples of charges that would normally constitute part of the finance charge. In the revised regulation, the procedures are set forth in their own paragraph, paragraph (d). There have also been several substantive changes from the December proposal.

(a) Definition. Section 226.4(a) corresponds to the first paragraph of § 226.4(a) of the current regulation. It reflects the amendment to § 106 of the act that states explicity that charges imposed uniformly in cash and credit ***20855** transactions, such as sales taxes or license or registration fees, are not within the scope of the finance charge definition.

The finance charge tolerance proposed in the December proposal has been deleted from this section. A specific dollar tolerance for the finance charge (with the amount depending on the size of the transaction) has been provided for closed-end transactions, and is contained in a footnote to § 226.18(d) of the revised regulation.

Section 226.8(o) of the current regulation treats as a finance charge a discount offered for prompt payment of a credit sale. This is not the case in the revised regulation. A creditor should now compare cash and credit transactions to determine whether a discount is a finance charge.

(b) Examples of finance charges. The introductory sentence to § 226.4(b) has been changed from the December proposal. The change was made to draw attention to the fact that the examples of items that would be considered finance charges in paragraph (b), may nevertheless be excludable from the finance charge under paragraphs (c), (d), or (e).

Section 226.4(b) reflects one substantive change from the December proposal, the deletion of application fees. Application fees are now addressed in § 226.4(c)(1), which states that they are not finance charges, provided they are charged to all applicants, whether or not credit is actually extended.

Section 226.4(b) corresponds to the list of examples of finance charges in § 226.4(a) (1) through (8) of the current regulation. Assumption fees imposed upon the consumer assuming a loan at the time of the assumption have been added to the list.

Paragraph (b)(9) of the revised regulation does not have a corresponding provision in the current regulation. This paragraph provides that any discount given to induce payment by a means other than by use of credit is a finance charge. One exception to this general rule is found in § 226.4(c)(8) of the revised regulation, addressing certain discounts.

(c) Charges excluded from the finance charge. Section 226.4(c) corresponds to § 226.4 (c), (d), and (e) of the current regulation, with some substantive changes.

Paragraph (c)(1), excluding application fees from the finance charge, is new. Application fees were included in the finance charge in the December proposal, but the revised regulation excludes them if the application fees are charged to all applicants, whether or not credit is actually extended.

Paragraph (c)(2) corresponds to § 226.4(c) of the current regulation, but adds one item to the list. The revised regulation specifically excludes charges for exceeding a credit limit from the finance charge. Although the regulation does not spell out what is "a charge for actual unanticipated late payment," the commentary to the revised regulation will provide guidance on this point. It should be noted, however, that the approach taken in current Board Interpretation § 226.401 will not be considered dispositive of the question. All of the circumstances surrounding the charge (for example, the terms of the plan involved and the action taken by the creditor with respect to accounts that are delinquent) must be considered. This means that a failure to terminate credit privileges while imposing a late payment charge will not automatically cause the late payment charge to be a finance charge.

Paragraph (c)(3) corresponds to § 226.4(d) of the current regulation, with only a few minor editorial changes. The term "bank" was changed to "financial institution" and the term "checks" was changed to "item" to reflect the ability of other financial institutions, such as savings and loan associations, to pay items that are similar to checks, such as negotiable orders of withdrawal, and create an overdraft on an account. The phrase "which overdraw or increase an overdraft" in the current regulation has been shortened to "that overdraws." No substantive change is intended; the provision continues to cover charges for paying the item that initially overdraws an account and for paying subsequent items while the account is overdrawn.

Although this provision reflects the position in the current regulation as to when such a charge constitutes a finance charge, it represents a change from the December proposal. The reference to an item that "inadvertently" overdraws an account has been deleted. The question of inadvertence is no longer relevant since the revised regulation excludes overdraft charges from the finance charge unless there is an agreement in writing to pay items and impose a charge. Although the reference to agreements in writing is a change from the December proposal, it is the position taken in the current regulation.

Paragraph (c)(4) excludes participation fees from the finance charge, which is the result under current Board Interpretation § 226.407.

Paragraph (c)(5), excluding seller's points from the finance charge, has no counterpart in the current regulation. It reflects a new position by the Board with respect to seller's points and is a departure from current Board Interpretation § 226.406. Although seller's points may have an indirect effect on the cost of credit to the borrower (if they are passed on indirectly in the form of a higher sales price), a uniform rule regarding these charges is desirable. As a result, the Board has concluded that seller's points should be excluded from the finance charge in all cases.

Paragraph (c)(6) has been added to incorporate the substance of proposed Board Interpretation § 226.408 to the current regulation. Certain federal and state laws mandate a percentage differential between the interest rates on a time deposit and a loan secured by such deposits. This may result in the consumer forfeiting some of the interest that otherwise would be earned, on the deposit. This paragraph provides that the lost interest need not be included in the finance charge in such transactions. The provision is limited to those situations where the interest reduction is required by law. The provision contained in the December proposal was not so limited.

Paragraph (c)(7) reflects § 226.4(e) of the current regulation. The introduction expands the statutory language regarding the types of transactions to which the exceptions apply, by the addition of the phrase "or a residential mortgage transaction." This would include certain mobile home transactions and similar credit extensions which are functionally the same as real estate transactions, even if state law characterizes the property as personalty. In the Board's view, this expansion carries out the congressional intent to treat mobile home transactions and similar types of credit extensions in the same manner as traditional realty transactions. Paragraph (c)(7) adds reconveyance document preparation fees to the list contained in paragraph (e)(2) of the current regulation and clarifies that the escrow account exception only applies to items that would not otherwise be finance charges.

Paragraph (c)(8) corresponds to § 226.4(i) of the current regulation and § 226.4(f) of the December proposal. It excludes from the finance charge certain discounts offered to induce payment by cash, check, or other means, as provided in § 167(b) of the act. Since this provision provides for an exclusion from the finance charge similar to the others listed in paragraph (c), it has been incorporated here rather than in its own paragraph.

***20856** The provision merely refers to § 167(b) of the act and replaces the material found in § 226.4(i) of the current regulation and § 226.4(f) of the December proposal. On February 24, 1981, the House passed H.R. 31, a bill that would amend § 167(b) of the act and, as a result, require changes in any Regulation Z provision implementing the statutory requirements for excluding certain discounts from the finance charge. On March 12, 1981, the Senate passed a bill similar to H.R. 31. Since final action by the Congress appears imminent, the provision in the revised regulation refers to § 167(b) of the act for details concerning what discounts are in fact excludable from the finance charge. The commentary will contain further explanatory material.

(d) Insurance. This paragraph sets forth the procedures for excluding credit life and property insurance premiums from the finance charge. It is based on § 226.4(a) (5) and (6) of the current regulation, but the procedures are changed in several respects. Note that the rules regarding the location of the disclosures called for by this paragraph in closed-end credit transactions are found in § 226.17 of the revised regulation.

Paragraph (d)(1) deals with credit life, accident, health and loss-of-income insurance (credit insurance) and it relaxes several of the requirements found in § 226.4(a)(5) of the current regulation. For example, it permits disclosure of the amount of the insurance premium on a unit-cost basis in certain closed-end credit transactions, in addition to open-end credit transactions where it has long been used.

The December proposal would have permitted the use of unit-cost disclosure in all types of transactions. However, because of the concern expressed by commenters (both creditors and consumers) and the lack of evidence that such a provision is needed in most closed-end credit transactions, the revised regulation restricts the use of unit-cost disclosures. The use of unit-cost disclosures is now limited to open-end credit transactions, closed-end credit transactions by mail or telephone, and certain closed-end credit transactions with a particular type of insurance plan. This last category includes a credit extension that exceeds, in whole or in part, the total indebtedness subject to coverage under an insurance plan. For example, a consumer who currently has an indebtedness of $8,000, subject to a plan of insurance coverage with a $10,000 maximum, may request that a new $4,000 loan be covered by the same credit life insurance plan. Since the $4,000 loan exceeds, in part, the maximum amount of indebtedness that can be covered by the plan, the creditor in such a case could properly give the insurance cost disclosures for the $4,000 loan on a unit-cost basis.

Another change from the current regulation concerns the signature requirements. Any consumer, whether or not an insured party, may sign the statement indicating a desire for the insurance. The words "or initials" have been added to make clear that either a signature or initials will satisfy the requirement.

Finally, the requirement in the current regulation that the insurance authorization be dated has been deleted.

Paragraph (d)(2) reflects the procedures for excluding property insurance premiums from the finance charge and is essentially the same as § 226.4(a)(6) of the current regulation. The language in the first sentence of paragraph (d)(2) differs from that found in the December proposal, which referred to "the property securing the obligation"; it reflects the language in the current regulation and in § 106(c) of the act. Paragraph (d)(2)(i) rephrases the current regulation's requirement that the customer have a choice as to the insurer, but no substantive change is intended. The requirement that property insurance disclosures be in a "clear, conspicuous, and specific statement" has been deleted since all disclosures are subject to the requirement of being clear and conspicuous. As in the December proposal, footnote 6 incorporates the substance of current Board Interpretation § 226.404, which permits vendor's single interest insurance to be excluded from the finance charge in the same manner as normal property insurance if the insurer waives all right of subrogation against the consumer.

(e) Certain security interest charges. Section 226.4(e) reflects § 226.4(b) of the current regulation, with only minor changes. The caption has been changed in an effort to more accurately reflect the coverage of this paragraph, which addresses only costs associated with security interests. The phrase "taxes and" has been added to paragraph (e)(1) to clarify that the types of charges described in that paragraph may include taxes as well as fees. The charges described in paragraph (e)(1) may be aggregated for disclosure purposes, rather than itemized according to the specific fees and taxes imposed. For purposes of closed-end credit disclosures, § 226.17 permits creditors to itemize these charges either separately or with the segregated disclosures.

Section 226.4(b) (3) and (4) of the current regulation has been deleted in the revised regulation to reflect the amendments to § 106 (a) and (d) of the act. These charges will now be judged by the general rule of § 226.4(a) to determine whether they are finance charges.

(f) Prohibited offsets. This paragraph is substantively the same as § 226.4(f) of the current regulation and § 226.4(g) of the December proposal.

SUBPART B--OPEN-END CREDIT

Sections 226.5 through 226.16 deal with the disclosure and procedure requirements for open-end credit plans.

§ 226.5 General disclosure requirements.

This section sets forth all of the general rules for open-end credit disclosures. It corresponds to § 226.5 of the December proposal, and to portions of §§ 226.6 and 226.7 of the current regulation.

Section 226.5(a) deals with the form of disclosures. Paragraph (a)(1) requires that open-end credit disclosures be made clearly and conspicuously. The December proposal required that all disclosures be in writing. The revised regulation provides one exception: the disclosure required by § 226.9(d) of certain finance charges imposed at the time a transaction takes place may be made orally or in writing. The December proposal also required that all disclosures be given in a form the consumer could keep. The revised regulation continues this general requirement, but provides that information about § 226.10 payment requirements and the alternative summary billing rights statement permitted by § 226.9(a) need not be in a form that the consumer can keep. The creditor may, for example, place this information on the payment stub portion of the periodic statement. The Board believes that this will ease the space limitation problem on periodic statements.

12 CFR § 226.7
12 CFR § 226.5

The current regulation requires (as did the December proposal) that the terms "finance charge" and "annual percentage rate" be disclosed more conspicuously in certain circumstances than other "required terminology." In December the Board solicited comment on whether it should delete the regulatory requirement that certain terminology be used on periodic statements. In response to comments and in light of the fact that the statute does not require the use of specific terminology, the revised regulation no ***20857** longer requires the use of specific terminology (see § 226.7). This deletion does not extend to the required terms, "finance charge" and "annual percentage rate." In light of this change, § 226.5(a)(2) requires that the terms "finance charge" and " annual percentage rate" be disclosed more conspicuously than other "required disclosures."

Section 226.5(a) also differs from the current regulation by increasing the flexibility with which a creditor may design initial disclosure statements and periodic statements. Section 226.6(a) of the current regulation requires that disclosures of numerical amounts and percentages be stated in figures and be in specified type sizes or be legibly handwritten. It further provides that disclosures be made "clearly, conspicuously, and in meaningful sequence." The revised regulation retains the standard that disclosures be made clearly and conspicuously, but deletes the sequence and type size requirements as being unnecessary in light of the general rule.

The revised regulation also deletes the separate rules set forth in current § 226.6(c) covering the use of additional information on the initial disclosure or periodic statements. The Board believes that additional information may be included on the statements, and its use will be adequately regulated by the general requirement that all open-end Truth in Lending disclosures be made clearly and conspicuously.

The current § 226.7(a) requires that the initial disclosures be made in a "single written statement." The revised regulation deletes this language. The position that both the initial disclosures and the periodic statements may be more than one page, as long as the pages constitute an integrated document, will be incorporated in the commentary.

Section 226.5(b) deals with the timing of discloures. Paragraph (b)(1) sets forth the timing requirement for the initial disclosure statement and is substantively unchanged from the December proposal and the current regulation.

Section 226.5(b)(2) sets forth the timing requirement for periodic statements. The provision identifying when a periodic statement need not be sent differs from the December proposal in two respects. First, the revised regulation reinstates the current regulatory standard that a statement need not be sent for an account for which deliquency collection proceedings have been instituted. Second, in response to commenters who were concerned that sending statements under certain circumstances would violate federal law (for example, after a consumer has filed for bankruptcy), the revised regulation provides that a statement need not be furnished if doing so would violate federal law.

Section 226.5(b)(2)(ii) requires the creditor to mail or deliver a periodic statement at least 14 days before the end of any free-ride period disclosed under § 226.7(j). This provision, along with footnote 10 which sets forth exceptions to the time limitation, remains unchanged from the December proposal and the current § 226.7(c)(2).

Section 226.5(c), regarding the basis of disclosures and the use of estimates, contains only a minor editorial revision from the December proposal. The revised regulation requires that disclosures be based on the "legal obligation" between the parties, whereas the December proposal used the phrase "legally enforceable obligation"; no substantive change was intended. This rule differs from the current regulatory interpretation that disclosures should reflect the terms the parties agreed upon, even if the terms differed from the legal obligation. Under the revised regulation, for example, when an employer offers a preferential employee rate, the disclosure should be based on the rate that is legally enforceable. Thus, the disclosure would not necessarily reflect the special discounted rate. The creditor is not prohibited, however, from also disclosing any other terms agreed upon by the parties, such as the preferential rate concession made for an employee.

As to the use of estimates, § 226.5(c) of the revised regulation provides that, when information essential for an accurate disclosure is unknown to the creditor, disclosures shall be made based on the best information reasonably available to the creditor, and the creditor must state that the disclosure is an estimate. This provision is more liberal than the current § 226.6(f), which allows the use of estimates only if disclosures were given at the latest possible time. The intent of this change is to encourage early disclosure.

Section 226.5(d) addresses disclosure requirements for both multiple creditor and multiple consumer situations. It requires that, in a multiple creditor situation, the consumer be given a complete set of disclosures, rather than partial disclosures from one or more of the creditors. A creditor may, of course, also furnish the consumer with additional copies of the required disclosures. Unlike the December proposal, the revised regulation further provides that creditors shall agree among themselves as to which creditor will make the complete set of disclosures.

In the case of multiple consumers, the revised regulation (like the current § 226.6(e) and the December proposal) would require disclosures to only one primarily liable consumer. The revised regulation explicitly states, however, that when the right of recission under § 226.15 is applicable, the initial disclosure statement (§ 226.6) and the notice of right to rescind (§ 226.15(b)) must be given to each person having the right to rescind.

Section 226.5(e) of the revised regulation governs the effect of subsequent events, and is unchanged from the December proposal. The provision is basically the same as the current § 226.6(g). The revised regulation provides that, although an inaccuracy resulting from an event subsequent to delivery of the disclosures is not a violation of the regulation, certain changes may require disclosures under § 226.9(c) (Change in terms).

§ 226.6 Initial disclosure statement.

Section 226.6 corresponds to the same section in the December proposal and to § 226.7(a) of the current regulation. It implements § 127(a) of the act, which lists the disclosures required upon opening an open-end credit account.

Form and timing requirements in the introductory paragraph of the current regulation are in § 226.5 of the revised regulation (General disclosure requirements). The requirement to use terminology consistent with that to be used on the periodic statement remains in the introductory paragraph to the revised § 226.6. As does § 226.7(a)(1) through (a)(4) of the current regulation, revised § 226.6(a) deals with the finance charge disclosure. While the structure and language of § 226.6(a) differs from that of the current regulation's § 226.7(a)(1)-(a)(4), few substantive differences exist. Language in § 226.6(a)(1) implements new statutory language requiring that a creditor indicate whether or not a time period exists within which any credit extended may be repaid without incurring a finance charge. The last sentence of § 226.6(a)(1) of the December proposal has been deleted as redundant.

Section 226.6(a)(2) corresponds to § 226.7(a)(4) of the current regulation and requires that, where one or more periodic rates may be used to compute the finance charge, each such rate must be disclosed together with the range of balances to which it is applicable and the corresponding annual percentage rate. The language in both the current regulation and the December proposal ***20858** referring to the method of determining the corresponding annual percentage rate has been deleted since the method is set out in revised § 226.14.

Language from the December proposal has been retained to indicate that, where different periodic rates apply to different types of transactions, those periodic rates and the annual percentage rates that correspond to them must be disclosed (see discussion in § 226.7(d)).

The material in footnote 6a of the current regulation has been divided into two footnotes (footnotes 11 and 13) in the revised regulation; this is an editorial change, with no change in substance intended.

Section 226.6(a)(3) of the revised regulation corresponds to § 226.7(a)(2) of the current regulation; it deals with disclosure of the method used to determine the balance on which the finance charge may be computed. The revised regulation makes clear that the method of computing the balance must be explained, and not merely identified by a shorthand phrase such as "previous balance method." Model clauses that describe various balance computation methods are contained in the appendix.

Footnote 12 specifies the disclosures required for variable rate programs. It replaces current Board Interpretation § 226.707. It requires that the creditor disclose on the initial disclosure statement the circumstances under which a rate may increase, the limits on the increase, and the effect that such an increase may have (for example, an increase in the periodic rate will occur when the prime rate increases and will be one percent over prime but will never exceed a periodic rate of 24%; however, should the periodic rate reach 20%, the creditor will require additional collateral.)

By disclosing on the initial disclosure statement the rules about when the periodic rate will increase, the creditor is relieved from providing a change in terms notice under § 226.9(c) in this regard.

The Board intends to incorporate Board Interpretation § 226.706 in the commentary; it provides that a creditor need not describe the manner in which payments and other credits are allocated. Interpretation § 226.706 intends to relieve the creditor of the responsibility to disclose, for example: (1) that payments are applied first to finance charges, then to purchases, and then to cash advances, or (2) that payments may be applied to late charges, overdue balances, and finance charges before being applied to the principal balance.

Sections 226.7(a)(5) and 226.11 of the current regulation deal with the Comparative Index of Credit Cost. Those sections are not reflected in the revised regulation. Their deletion results from a statutory amendment.

Section 226.6(b) corresponds to § 226.7(a)(6) of the current regulation and deals with the disclosure of charges, other than finance charges, that may be imposed as part of the open-end credit plan. The revised regulation implements statutory language changes and reflects editorial changes from the December proposal.

As the Board stated in the December proposal, membership or participation fees in open-end credit plans are considered other charges, as are late payment charges, fees for providing documentary evidence requested under proposed § 226.13, and over-the-credit-limit charges. In contrast, fees charged for documentary evidence of transactions for income tax purposes, for example, would not be considered other charges.

As pointed out in the December proposal and unlike current staff position, voluntary credit life insurance is not considered another charge. The Board continues to believe that disclosing the cost of voluntary credit life insurance on the initial disclosure statement as another charge is unnecessary since cost disclosure is already required by § 226.4. Required credit life or disability would, of course, be disclosed as a finance charge on the initial disclosure statement.

Section 226.6(c), which requires disclosure of the fact that a creditor has or will acquire a security interest under the plan, corresponds to § 226.7(a)(7) of the current regulation. The section is identical to the December proposal. It implements, however, a major statutory amendment to § 127(a). The current regulation requires disclosure of the conditions under which the creditor may retain or acquire a security interest, and a description or identification of the type of the interest. The revised statute and regulation simplify this disclosure by merely requiring the creditor to disclose the fact that the creditor has or will acquire a security interest either in the property purchased as part of the plan or in other property identified by item or type.

In the December proposal, the Board stated that creditors requiring security only when the balance in an account exceeded a pre-designated amount need only disclose to the consumer on the initial disclosure statement information about the security interest available to the creditor at the time that the disclosures were being made. The proposal provided that, at a later date, when the security interest was actually taken, the creditor would disclose to the consumer a description of the property in which the security interest was taken with more specificity.

Commenters objected to the latter requirement, pointing out that the security interest disclosures for closed-end credit did not require the specificity required in open-end disclosures. The Board agrees that it is not necessary for a creditor to provide the additional disclosures when the security interest is actually taken if the scope of the security interest taken is the same as, or is more specific than, that disclosed to the consumer on the initial disclosure statement. However, the Board continues to believe that if the security interest actually taken in the property is of greater scope than that disclosed on the initial disclosure statement, a change-in-terms notice is required.

For example, if the initial disclosures provided for a security interest in "household goods" and a security interest was later taken in certain household goods, no change-in-terms notice would be necessary. If, on the other hand, the initial security interest was disclosed as covering certain household goods and, at the time the pre-designated balance was exceeded, the actual security interest was taken in all household goods, it would be necessary for the creditor to provide a change-in-terms notice. The Board would point out that in the latter instance, if the creditor executes a new security agreement (a copy of which is given to the consumer), that security agreement will suffice as a change-in-terms notice.

As in the December proposal, and in the absence of a corresponding statutory provision, the minimum periodic payment requirement in § 226.7(a)(8) of the current regulation is not included in the revised regulation. The Board is of the opinion that a creditor would routinely provide such information to the consumer, and is unaware of any potential abuse requiring regulation. However, a provision requiring notice to the consumer regarding an increase in the minimum periodic payment has been incorporated in § 226.9(c).

Proposed § 226.6(d) corresponds to § 226.7(a)(9) of the current regulation; it deals with the billing rights statement requirement and is unchanged from the December proposal. Unlike the current regulation, a model billing error rights statement is included in the appendix rather than in the body of the regulation. The revised regulation includes a provision that the notice provided by the ***20859** creditor be substantially similar to the model statement. Unlike under the current regulation, the phrase "substantially similar" is intended to provide the creditor with greater flexibility in personalizing the notice and complying with "plain English" state laws. (See the appendix for a discussion of the "substantially similar" standard.)

Commenters requested that the regulation provide that the model billing error rights notice be deemed to comply with "plain English" state laws. The Board believes that it would be inappropriate to make such a determination.

§ 226.7 Periodic statements.

Section 226.7 corresponds to the same section in the December proposal and to § 226.7(b) of the current regulation; it requires that creditors provide consumers with periodic statements at the end of each billing cycle and identifies the information that must be disclosed on them. The general periodic disclosure requirements relating to timing, format, and applicability that appear in current § 226.7(b) appear in § 226.5 of the revised regulation. The definition of "billing cycle" in revised § 226.2 establishes the requirement that the interval between billing cycles be no longer than a quarter of a year.

The revised regulation does not contain the requirements in § 226.7(c) of the current regulation regarding the location of disclosures on the periodic statement. The Board believes that adequate consumer protection is afforded by the requirement in § 226.5 that Truth in Lending disclosures be made clearly and conspicuously.

Required terminology, with the exception of the terms "finance charge" and "annual percentage rate," has also been deleted from this section. A number of commenters favored elimination of required terminology because of the potential for nonsubstantive technical violation of the regulation.

Section 226.7(a) corresponds to § 226.7(b)(1)(i) of the current regulation. It requires disclosure of the outstanding account balance at the beginning of the billing cycle. The requirement that a credit balance be identified as such has been deleted from the regulation as unnecessary; where a credit balance exists, the requirement that it be disclosed clearly and conspicuously will insure its proper identification. As has always been the case, creditors may use a symbol or abbreviation to identify a credit balance as long as it is explained on or with the periodic statement.

The last sentence of the paragraph that appeared in the December proposal has been deleted from the regulation. It incorporated the present staff position that permits disclosure of a separate previous balance for each type of transaction. It will, instead, be incorporated in the commentary. The Board will also incorporate in the commentary the staff position that creditors disclosing a separate previous balance for each type of transaction on an account need not disclose a total previous balance.

Section 226.7(b) corresponds to § 226.7(b)(1)(ii) of the current regulation; it is the same as the current regulation except for minor editorial changes. It requires that each credit transaction be identified on the periodic statement in accordance with the specific identification requirements of § 226.8.

Section 226.7(c) requires disclosure of any credit to the account during the billing cycle. This disclosure must include the amount of the credit and its date of crediting. It corresponds to § 226.7(b)(1)(iii) of the current regulation. As in the December proposal, the revised regulation no longer requires specific identification of the type of credit. Creditors may also use symbols or abbreviations as long as they are explained on or with the periodic statement. The Board would point out, however, that, where a creditor uses the periodic statement to notify the consumer of a billing error correction, a specific identification of the credit must be provided.

Section 226.7(d) corresponds to § 226.7(b)(1)(v) of the current regulation and deals with disclosure of any periodic rate that may be used to compute the finance charge and the annual percentage rate that corresponds to it. The Board believes that the language of the paragraph can be read to require that the periodic rate(s) used to compute the finance charge must be disclosed whether or not applied during the billing cycle, and therefore has deleted the parenthetical phrase that appears in the current regulation. The Board would point out that, where an open-end plan offers a variety of features, the creditor must disclose the peridoic rate(s) and corresponding annual percentage rate(s) for only those types of transactions that the consumer has the privilege of utilizing without further application. For example, where the consumer requests and receive a line of credit that may be routinely accessed by a credit card or check overdraft, the periodic rate(s) and corresponding annual percentage rate(s) must be disclosed for those features on each periodic statement whether or not the consumer uses either feature during the billing cycle. If the same plan also offers individual advances for unsecured credit or credit secured by large-ticket items, the periodic rates and corresponding annual percentage rates for those features need not be disclosed if the consumer does not have the present ability to access the credit line routinely without special application.

Footnote 15 of the revised regulation deals with the disclosure that must appear on the periodic statement when a variable rate program is involved. The footnote requires that the creditor reflect on the periodic statement, where a variable rate program is involved, that the periodic rate may vary.

The alternative terminology that appears in the current regulation for the disclosure of the corresponding annual percentage rate has been deleted from the regulation. For the purposes of this paragraph, creditors may continue to modify the term "annual percentage rate" by using the terms corresponding, nominal, or corresponding nominal. Where one disclosure is given for both revised § 226.7 (d) and (g), however, only the term "annual percentage rate" may be used.

Language from the December proposal has been retained to indicate that, where different periodic rates apply to different types of transactions, those periodic rates and the annual percentage rates that correspond to them must be disclosed, together with the types of transactions to which they apply. Where different rates are involved, a periodic statement that does not reflect what the different rates apply to (that is, ranges of balances and/or types of transactions) would render the periodic rate disclosure meaningless.

The language referring to the method of determining the corresponding annual percentage rate has also been deleted from the current § 226.7(b)(1)(v) since the method is set out in revised § 226.14.

Section 226.7(e) of the December proposal is not reflected in the revised regulation. That paragraph required disclosure of the amount or method of computing the amount of any type of finance charge other than the periodic rate that may be imposed during the billing cycle. Several commenters stated that, in the absence of a corresponding statutory provision, the requirement unnecessarily duplicated information contained in the initial disclosures; that it might confuse consumers when the charge was not, in fact, imposed during the billing cycle; and that it would detract attention from other important disclosures. Because consumers are ***20860** informed of the existence of these charges on the initial disclosure statement, and of their imposition on the periodic statement, the Board believes that adequate consumer protection is afforded without this additional disclosure requirement.

Section 226.7(e) of the revised regulation corresponds to § 226.7(f) of the December proposal and § 226.7(b)(1)(viii) of the current regulation; it requires disclosure of the amount of the balance to which a periodic rate is applied and an explanation of how the balance was determined.

The revised paragraph returns to language similar to the current regulation, deleting language in the December proposal that required disclosure of the amount of each balance to which a different periodic rate is applied. The rule stated in the December proposal proved too broad in that it inadvertently required the separate breakout of balances where the disclosures of separate balances would in fact be unnecessary. For example, where the consumer has a balance of $1,000 on purchase transactions, and amounts up to $500 are subject to a periodic rate of 1 1/2 % per month and amounts over $500 are subject to a 1% periodic rate per month, there would be no need to disclose those balances separately. The Board believes, however, that there are certain circumstances in which more than one balance must be disclosed in order for the balance disclosure to be meaningful. For example, where a periodic rate of 1 1/2 % per month is applied to purchases and 1% per month to cash advances, the Board believes that both balances subject to the periodic rates must be disclosed. The Board intends to incorporate specific examples in the commentary, along with the present staff position that permits disclosure of separate balances for different types of transactions, at the creditor's option.

The revised paragraph retains the position set forth in the December proposal that only those balances to which a periodic rate was applied need be disclosed. The Board believes that to require the specific and separate identification of each balance involved in computing individual transaction charges or activity charges would significantly complicate the periodic statement.

Section 226.7(e) of the revised regulation continues to require disclosure of the balance computation method. Four model disclosures are contained in Appendix G.

Board Interpretation § 226.703, which deals with the disclosure of the balance when one or more daily periodic rates are imposed, will be incorporated in the commentary.

Section 226.7(f) corresponds to § 226.7(g) of the December proposal and § 226.7(b)(1)(iv) of the current regulation; it requires disclosure of the amount of any finance charge debited or added to the account during the billing cycle. The last sentence of the paragraph incorporates current Board Interpretation § 226.701, which provides that, where there is more than one periodic rate, the finance charge attributable to each rate need not be separately itemized and identified.

The Board is aware that some creditors do not debit or add finance charges to an account during a billing cycle, but instead allocate from each payment the amount of the finance charge that has accrued since the last payment. The Board intends to incorporate in the commentary the present staff position that those creditors need not disclose finance charges that may have accrued between the date of the last payment and the closing date. The Board also intends to expand the applicability of this position to the disclosures required by revised §§ 226.7(a) (Previous balance) and 226.7(i) (New balance).

Section 226.7(g) of the revised regulation corresponds to § 226.7(h) of the December proposal and § 226.7(b)(1)(vi) of the current regulation. It requires disclosure of the annual percentage rate (calculated in accordance with revised § 226.14) whenever a finance charge is imposed during the billing cycle. Language in the December proposal provided that, where an annual percentage rate could not be determined because there was no outstanding balance in the account, no annual percentage rate need be disclosed. That sentence has been deleted as unnecessary; no substantive change is intended, however. The Board believes that the reference in § 226.14 to the circumstances under which an annual percentage rate cannot be determined is sufficient to relieve creditors of the duty to disclose it under this paragraph.

Section 226.7(h) has no corresponding section in the current regulation; rather, it implements a present staff position that charges other than finance charges imposed during the billing cycle must be reflected on the periodic statement. The revised regulation does not require a separate disclosure of the total of other charges.

As in the December proposal, the requirements of current § 226.7(b)(1)(ix) have been divided into two paragraphs for clarity. Section 226.7(i) corresponds to § 226.7(j) of the December proposal and requires disclosure of the closing date of the billing cycle and the outstanding account balance on that date. The language of the current regulation requiring appropriate identification of a credit balance has been dropped for the same reasons given for deletion of similar language regarding the balance at the beginning of the billing cycle. The last sentence of the paragraph that appeared in the December proposal has been dropped; it indicated that a creditor could disclose an outstanding balance for each type of transaction on an account. The Board will incorporate that position in the commentary. As is currently the case, a creditor may, at its option, disclose an outstanding balance for each type of transaction in lieu of a total outstanding balance.

The second part of current § 226.7(b)(1)(ix) is found in § 226.7(j) of the revised regulation and corresponds to § 226.7(k) of the December proposal. It deals with the disclosure of any free-ride period permitted on the account; it is substantially the same as the current regulation.

Section 226.7(k) corresponds to § 226.7(b)(1)(x) of the current regulation and § 226.7(1) of the December proposal. It requires disclosure of the address to be used for notice of a billing error. In light of the fact that required terminology has been eliminated, with the exceptions noted above, the "Send inquiries to:" language requirement has been deleted. The Board believes that the general requirement in § 226.5 that Truth-in-Lending disclosures be made "clearly and conspicuously" will insure adequate consumer protection.

Several commenters asked the Board if a telephone number could be disclosed with the billing error address without giving a precautionary instruction that telephoning will not preserve the consumer's billing error rights. While the Board recognizes that nothing in the act prohibits giving the telephone number as additional information, the Board believes that, depending on the overall format of the disclosure statement, disclosure of a telephone number without a precautionary instruction could be misleading.

§ 226.8 Identification of transactions.

This section of the revised regulation corresponds to § 226.8 of the December proposal and to § 226.7(k) of the current regulation; it deals with the requirement that the creditor identify on the periodic statement credit transactions made in an open-end plan. This section ***20861** implements § 127(b)(2) of the act. While the revised regulation reflects a few editorial changes, it is substantively unchanged from the December proposal.

Comparing the revised regulation with the current regulation reveals little substantive change. The revised regulation reflects, however, a significant reorganization which should facilitate its use. Moreover, much of the explanatory detail contained in the current regulation has been deleted for more appropriate inclusion in the commentary.

Footnote 16 (which deals with a creditor's failure to disclose required identifying information and which applies to all creditors) and footnote 18 (which details a special provision for small creditors) implement provisions in the amended act regarding the liability implications for failure to provide required identifying information in certain circumstances. Footnote 16 also replaces § 226.7(k) (4) and (5) of the current regulation, which contain specific provisions allowing the creditor to substitute or omit unavailable information in certain instances. Under the revised regulation the creditor need no longer show that information is actually unavailable--only that the creditor has maintained reasonable procedures to procure it. Section 226.7(k)(6)(i) of the current regulation, which allows a creditor to rely on information supplied by a non-related seller, has also been deleted as unnecessary due to the protection afforded by footnote 16.

Some commenters asked for guidance on how to correct the account for purposes of footnotes 16, 17, and 18 to this section. There is no separate rule for correction under § 226.8; § 226.13(e) applies. For example, under § 226.13(e) when the consumer is correct (and the consumer is considered to be correct under these footnotes), the creditor may not impose any finance or other charges on the transaction in question.

As is the case in the current regulation, the rules for identifying transactions on periodic statements vary depending upon three factors: (1) whether the transaction involves a purchase or a cash advance; (2) whether a copy of the credit document reflecting the transaction accompanies the statement; and (3) if purchases are involved, whether the creditor and seller are the same or related persons.

Several commenters asked the Board to clarify whether a creditor should identify a transaction as sale or nonsale credit when a consumer uses a debit card with an overdraft feature to purchase goods and, in doing so, activates the overdraft. The Board believes that the credit portion of such transactions could be viewed as a cash advance, and may therefore be disclosed as nonsale credit at the creditor's option even though a purchase is involved.

The current regulation states that a facsimile draft (for example, a draft in which the required information is typed in, as opposed to a duplicate copy) is not considered an "actual copy of the document evidencing the transaction" for purposes of this section. This position about the use of facsimile drafts has been deleted from the revised regulation, but will be incorporated in the commentary.

Section 226.8(a)(2) of the revised regulation, which sets forth the requirements for descriptive billing of purchases when the creditor and seller are the same or related persons, corresponds to § 226.7(k)(2)(i) of the current regulation. Footnote 9(b) of the current regulation provides guidance as to whether a creditor and seller are the same or related persons for purposes of this section. This material has been deleted from § 226.8(a)(2) of the revision, but will be incorporated in the commentary. The commentary will also reflect that creditors may use either the "related" or "non-related" rules in describing transactions with third party sellers resulting from promotional material mailed by the creditor. The commentary will further provide that a seller and creditor are not related merely because they have a corporate connection, if that connection is not obvious from the names used by the seller and the creditor.

Footnote 9(c) of the current regulation provides guidance on disclosing the transaction date for a transaction not billed in full on any single statement but for which precomputed installments are billed periodically. This material will appear in the commentary rather than in the revised regulation. The Board takes the position that the creditor may disclose on the first periodic statement reflecting the transaction either the full amount of the transaction together with the date the transaction actually took place; or the amount of the first installment and the date of the transaction or the date the first installment was debited to the account. In either event, subsequent periodic statements should reflect each installment due, together with any other identifying information required by this section. On subsequent statements, the debiting date may be used as the date of the transaction.

Section 226.8(a)(2) of the revised regulation requires a brief identification of property or services purchased, as does the current regulation. While the revised regulation does not contain the material in current footnote 9(d) about the use of department names or symbols instead of designations such as "merchandise" and "miscellaneous," this material will be included in the commentary. The commentary will also incorporate current staff position that designations such as "promotional items" are insufficient property identifications.

As noted above, footnote 18 of the revised regulation reflects the statutory amendment to § 127(b)(2) allowing two-party creditors with fewer than 15,000 open-end credit accounts to delete the brief identification and provide, in certain instances, only the amount and date of each credit extension and the seller's name and location. In response to comments, the Board wishes to make clear that, in determining whether a creditor may take advantage of this provision, the creditor counts only its own accounts, and not those merely serviced by the same data processor or other shared service provider.

Section 226.8(a)(3) deals with descriptive billing when the creditor and seller are not the same or related persons. The current regulation specifically permits the creditor to use understandable and generally accepted abbreviations of the seller's address. This material has been deleted from the revised regulation, but will appear in the commentary. Footnote 19 of the revision, which corresponds to current § 226.7(k)(5)(ii), allows the creditor to omit the address or provide some suitable designation to assist the consumer in identifying the transaction when the transaction took place at a non-fixed location or in the consumer's home, or was a mail or telephone order. No substantive change is intended, although editorial changes have been made. The revised regulation deletes some explanatory material that will, however, be incorporated in the commentary.

The current regulation also specifically permits the seller's name to be disclosed on the periodic statement either as it appeared on the credit document or as a more complete spelling of a name that was alphabetically abbreviated on the credit document. The revised regulation deletes this material, but will incorporate it in the commentary. In addition, the Board believes that a creditor may use an acceptable abbreviation of the seller's name on the periodic statement even if the name appears in a more complete spelling on the sales receipt.

***20862** Section 226.8(b) of the revised regulation sets forth the requirements for the identification of nonsale credit transactions. Paragraphs (b) (1) and (2) of the December proposal have been combined for editorial reasons; no substantive change is intended. The section differs from the December proposal and the current regulation by deleting the examples of appropriate identifications of nonsale transactions. These examples--cash advance, loan, and overdraft loan--will be included in the commentary rather than in the regulation. A footnote has been added to permit the creditor the same alternative means of identification on the periodic statement as is available for sale credit transactions. The footnote permits the use of a number or symbol that also appears on the credit document furnished to the consumer at the time of the transaction if that number reasonably identifies the transaction with the creditor. If the creditor uses the number or symbol, however, and the consumer submits a notice of a billing error regarding the transaction, the creditor must comply with the billing error resolution procedures.

Revised § 226.8(b) contains one other change from the current regulation. The revision permits the use of the debiting date in all nonsale credit transactions. In the current regulation, this alternative is available only to creditors with overdraft checking plans (and to a limited extent for other nonsale credit plans), unless an actual copy of the credit document containing the amount and date is provided to the consumer.

§ 226.9 Subsequent disclosure requirements.

Section 226.9 corresponds to the same section of the December proposal and to several provisions in § 226.7 of the current regulation. Section 226.9(a) implements the statutory requirement that the creditor provide the billing rights statement annually. That paragraph also provides the creditor with an alternative means of complying with the annual requirement. The remaining paragraphs provide creditors with guidance on satisfying the act where they add new features or devices to an existing open-end credit plan; where they make a significant term change; and where they impose a finance charge at the time of the credit extension.

(a) Furnishing statement of billing rights. Section 226.9(a) of the revised regulation corresponds to § 226.7(d) of the current regulation. This section implements a provision in the amended act that the long-form billing rights statement be provided annually rather than semi-annually as the original act and regulation mandated. The statute and the December proposal provide that the notice be furnished during one billing cycle per calendar year to all consumers entitled to a periodic statement for that cycle. Comment raised the question of whether the notice requirement could also be satisfied by providing the billing rights statement to each consumer at some time during the year, such as when a renewal card is sent or an annual membership fee is imposed. Under such a procedure, all consumers would receive the billing rights statement annually (not merely those consumers entitled to a periodic statment for a particular cycle), while allowing the creditor to utilize more than one billing cycle in which to complete sending the notices. The Board believes that this practice is entirely compatible with Congressional intent; therefore, the revised regulation permits this alternative.

Section 226.9(a)(2) of the revised regulation, which gives the creditor the option of sending a summary of the consumer's billing rights with each periodic statement, instead of the longer annual statement, is substantively unchanged from the December proposal. In the Federal Register material accompanying the December proposal, the Board indicated its intent to reverse a staff position that has permitted the summary statement to be on a portion of the periodic statement that the consumer would return to the creditor (for example, on the back of a payment stub). Since many commenters believed that this restriction might preclude them from using the summary statement alternative because of space limitations, the Board is incorporating the staff position in the revised regulation (see § 226.5).

(b) Supplemental credit devices and additional features. Section 226.9(b) of the revised regulation deals with disclosures for supplemental credit devices and additional features. With respect to disclosures for supplemental credit devices, it corresponds to § 226.7(j) of the current regulation.

The December proposal required new finance charge disclosures under § 226.6(a) whenever credit devices or features were added that were subject to finance charge terms different from those previously disclosed. Under both the current regulation and the December proposal, even if the credit devices or features were offered on the same terms, the finance charge disclosures were required if the devices or features were added more than 30 days after the initial disclosures were given. While the revised regulation does not require that the finance charge disclosures be provided when a consumer is merely given another means of accessing the account on the same terms as were previously disclosed, the Board believes that, if the new means of access is provided more than 30 days after the consumer receives disclosures, the consumer should be told that the device is a credit device, and referred to the initial disclosure statement previously furnished. No required language or particular phrasing is contemplated for this disclosure. Rather, the requirement is intended merely to draw the consumer's attention to the fact that the device is not a replacement for cash. For example, in mailing checks that directly access the credit line, the creditor might use a disclosure such as "Use this as you would your XYZ card to obtain a cash advance from our bank. See your contract for further details." The creditor may, of course, make the finance charge disclosures required by § 226.6(a) as an alternative means of satisfying the requirement.

Several commenters noted that the original issuance of a credit card may take more than 30 days to be delivered after initial disclosures are given because of printing or other processing delays. To accommodate this concern, § 226.9(b)(1) excepts the original issuance of credit cards from the disclosure requirement even when the cards are delivered more than 30 days after the initial disclosures.

Section 226.9(b) differs from § 226.7(j) of the current regulation in several respects. The current regulation requires a complete set of finance charge disclosures to be made with supplemental credit devices delivered more than 30 days after delivery of the initial disclosures, even if the terms were the same. Section 226.7(j) also requires that the disclosures accompany the device, and that they be on a single written statement without any promotional material. The revised § 226.9(b) is more flexible in that (1) disclosures need be made to the consumer before the consumer uses the feature or device for the first time; (2) the restriction on accompanying material has been removed; and, (3) as with other open-end credit disclosures, the creditor basically has the flexibility to make the disclosures in any manner that is clear, conspicuous, and in a written form that the consumer may keep.

Section 226.9(b)(3) of the December proposal, regarding the timing of the disclosure requirements, has been ***20863** deleted for editorial reasons. This information is now included in paragraphs (b)(1) and (b)(2); no substantive change is intended.

(c) Change in terms. Section 226.9(c), which corresponds to § 226.7(f) of the current regulation, outlines the requirements for notifying consumers in the event a creditor makes a change in the terms of a consumer's account. The revised regulation is unchanged from the December proposal, but differs significantly from the current regulation.

The current regulation requires that notice of an increase in a periodic rate or any minimum, fixed, service, transaction, or similar charge be sent to all consumers at least 15 days prior to the beginning date of the billing cycle in which the increase is imposed. Section 226.9(c) of the revised regulation reflects a change in the timing of the delivery of the notice from 15 days prior to the billing cycle in which the change will be effective to 15 days prior to the effective date of the change. This modification would permit mid-cycle changes when there is clearly no retroactive impact, such as the imposition of a transaction fee. A change in the balance computation method, in contrast, would need to be disclosed prior to the billing cycle in which the change was to be implemented.

Board interpretation § 226.705 of the current regulation provides that certain changes in balance computation methods would not require a term change notice because the new method could result in lowered finance charges. Since such a determination often depends upon a particular consumer's use of the account, the applicability of such an interpretation is considered questionable. Consequently, the revised regulation would consider any change in the balance computation method to require a change in terms notice.

The revised regulation also substantially reduces the types of term changes for which notice need be given. The revised regulation continues to require advance notice to all consumers whenever the change involves an increase in the periodic rate, or any minimum, fixed, service, transaction, activity, membership, or similar charges. The revised regulation also continues the current regulatory requirement (but differs from the December proposal) in providing that creditors give advance notice of an increase in any minimum payment required on the account. No notice need be given, however, when the change involves late payment, documentation, or over-the-limit charges; or when the change results from the consumer's default or delinquency (unless the periodic rate or any other finance charge is increased); or when the change results from an agreement involving a court proceeding. The revised regulation also provides that no advance notice is necessary--although a notice is still required--when the change has been agreed to by the consumer (for example, a consensual collateral substitution) or when the change is an increase in a periodic rate or other finance charge as a result of the consumer's default or delinquency.

The Board wishes to emphasize that this section is meant to apply to changes made by the creditor (with or without the consumer's agreement) rather than those arising merely by operation of law. For example, if the creditor has taken and disclosed a security interest in the consumer's vehicle, and, upon the consumer's sale of the vehicle, the creditor's interest automatically extends to the proceeds, no change in terms notice is required under this section.

(d) Finance charge imposed at the time of transaction. Section 226.9(d), which corresponds to § 226.7(e) of the current regulation, deals with disclosure requirements when a finance charge is imposed by a creditor other than the card issuer at the time of honoring a consumer's credit card. The Board believes that adequate consumer protection is afforded by the creditor's disclosing the amount of the finance charge, either orally or in writing, at the time the card is honored. Consequently, unlike the December proposal and the current regulation, the revised regulation no longer requires written disclosure of the amount financed and annual percentage rate, figured in accordance with the closed-end credit provisions.

§ 226.10 Prompt crediting of payments.

Section 226.10, which corresponds to § 226.7(g) of the current regulation, sets forth the rules for a creditor to follow in crediting payments to a consumer's account. It implements § 164 of the act. This section of the revised regulation has been substantially rewritten in order to reduce complexity by establishing precise, easy-to-apply rules. The revised regulation also deletes the explanatory detail contained in the current regulation; much of this material will be incorporated in the commentary. The format of this section is the same as that contained in the December proposal; however, a major change has been made from the proposed timing requirement.

(a) General rule. Section 226.10(a) of the revised regulation, which requires that a payment be credited as of the date of receipt except when a delay does not result in the imposition of a finance or other charge, corresponds to the introductory paragraph of § 226.7(g) and to § 226.7(g)(4) of the current regulation. Although the language of the revised § 226.10(a) differs from that of the current regulation, no substantive change is intended in the application of the general crediting rule. The "date of receipt" for purposes of this section is the date that payment is made at any location where the creditor conducts business, or at a location specified under paragraph (b), as long as the payment is received before the creditor's close of business or a reasonable cut-off time specified in accordance with paragraph (b). This paragraph differs from the December proposal in incorporating proposed footnote 16 into the body of the regulation and adding language to make clear that a creditor, specifying requirements pursuant to paragraph (b), need not credit non-conforming payments as of the date of receipt.

(b) Specific requirement for payments. Section 226.10(b) of the revised regulation, which corresponds to § 226.7(g) (2) and (3) of the current regulation, permits a creditor to specify requirements (such as form, manner, and location) for the consumer to follow in making payments. The current regulation provides that, if a creditor specifies a location requirement, but nonetheless accepts payment at another location, the creditor is not under an obligation to credit the payment on the date of receipt but must still credit it promptly, with an outside limit of five calendar days.

The revised regulation differs from the current regulation in three respects. First, a creditor may avail itself of the extra time when it accepts a payment that does not conform to the specified requirements in some other manner, not just when it is sent to the wrong location. Second, the separate promptness standard has been deleted to avoid uncertainty in applying the rule; under the revised regulation, a creditor simply has five calendar days in which to credit a non-conforming payment. Third, the word "reasonable" that preceded requirements in the current regulation and the December proposal has been deleted. This deletion is not intended to result in a substantive change. The requirements specified by the creditor must continue to be those with which the majority of consumers can comply in order not to frustrate the statutory requirement in § 164 of the act that the "regulations shall prevent a finance charge being imposed on any obligor if the creditor has received the obligor's payment in readily identifiable form in the amount, manner, location, and time indicated by the creditor. . . ."

***20864** Section 226.10(b) of the revised regulation also differs in another way from the December proposal. The December proposal required merely that nonconforming payments be credited "promptly." A number of commenters requested the reinstatement of a specific time limit to avoid unnecessary proof problems regarding whether a creditor acted promptly in a particular situation.

Section 226.10(b) of the revised regulation continues the current regulatory provision that any payment requirements be stated on or with the periodic statement. As is the case under the current regulation, these requirements need not be located on a part of the statement that the consumer may retain. In the revised regulation this provision is stated in § 226.5(a), which sets forth all of the form requirements for disclosures made under Subpart B.

The revised regulation also differs from § 226.7(g)(2) of the current regulation in deleting, as inappropriate regulatory material, the detail about time, manner, and location for receipt of payments when no such requirements are specified by the creditor. This guidance will be incorporated in the commentary.

(c) Adjustment of account. Section 226.10(c) is substantially the same as § 226.7(g)(1) of the current regulation. This paragraph provides for the adjustment of an account when a creditor fails to post a consumer's payment as required by this section in time to avoid the imposition of finance, late payment, or other charges that would not have been assessed had the creditor complied with paragraph (a) or (b), as applicable.

The revised regulation differs from the December proposal by adding language to clarify that paragraph (c) applies to creditors proceeding under both paragraphs (a) and (b) of this section.

§ 226.11 Treatment of credit balances.

Section 226.11 of the revised regulation, which establishes requirements for the treatment of credit balances, corresponds to § 226.7(h) of the current regulation. This section implements the amended § 165 of the act, and differs significantly from the current regulation.

The current regulation provides that a creditor's duties arise under this section when a consumer transmits a payment(s) that exceeds the disclosed new balance by more than $1. The revised regulation, in accordance with the amended statute, provides that a creditor's duties arise when the creditor receives any credit to the consumer's account that exceeds the balance by more than $1. Thus, when the balance is created by a return or a rebate, the provisions of § 226.11 apply.

When a credit balance is created, the current regulation provides the creditor with two basic options: to credit the consumer's account with the amount of the balance due and refund the remainder promptly (but within five business days) or to credit the account with the total payment and, if the consumer so requests, refund the credit balance promptly (but within five business days). Section 226.11(a) of the revised regulation retains these options with two substantive changes. First, the revised regulation requires the creditor to act within seven business days, thus replacing the promptness standard with a precise rule and expanding the outside time limit by two business days to accommodate any time necessary for investigations of non-payment type credits. Second, the revised regulation makes clear that what the creditor need refund is any remaining credit balance in the account at the time refund must be made. This differs from the current regulation and the December proposal by permitting the creditor to take account of a consumer's intervening debits in determining the amount of the required refund. This change is intended to accommodate operational concerns raised by commenters in response to the December proposal.

Section 226.11(b) of the revised regulation implements the new requirement in the amended act that the creditor make a good faith effort to refund credit balances that remain in an account for more than six months. This section differs from the December proposal in that it allows a creditor to refund a credit balance to a consumer by crediting the amount to a deposit account maintained with the creditor.

The Board notes that § 226.7(h)(3) of the current regulation has been deleted from the revised regulation as inappropriate regulatory material. That paragraph provides that a creditor may refund a credit balance even in the absence of a consumer's request. The Board notes that nothing in the regulation restricts a creditor from refunding the excess prior to the time that it is required to do so under this section.

§ 226.12 Special credit card provisions.

As in the December proposal, § 226.12 contains special rules applicable to credit cards and credit card accounts. It corresponds to § 226.13 of the current regulation.

(a) Issuance of credit cards. This provision contains the rules governing the distribution and renewal of credit cards. It differs from the December proposal in that footnotes 17 and 18 of that proposal have been deleted, and paragraph (a)(1) and footnote 19 of the proposal have been revised. In paragraph (a)(1), the words "for the card" have been substituted for "by a cardholder." In footnote 19 of the proposal (footnote 21 of the revised regulation), the phrase "or an authorized user" has been deleted in two places.

The effect of these changes is to return the text of paragraph (a) to a form very close to that in the current regulation (except for the addition of the footnote defining "accepted credit card," and the deletion of some material which now will be contained in the commentary). However, no change in substance from the December proposal is intended. As was stated in footnote 18 of the December proposal, paragraph (a) permits credit cards to be sent to the person making the request, as well as to any other person for whom a card is requested. No liability for unauthorized use may be imposed on a person who has not requested a card, but nothing in this provision prevents the imposition on that person of liability on the account generally. Whether or not such liability may be imposed is a matter of state law. Finally, the issuer may send more than one credit card to a person if so requested, and may imprint any name(s) requested on any card(s).

As was stated in footnote 17 in the December proposal, paragraph (a) does not prohibit the issuance of an unsolicited device that may become a credit card provided that (1) the device has some substantive purpose other than obtaining credit, (2) it is not capable of being used as a credit card when issued, and (3) credit capability will be added only upon the recipient's request. All of this material has been deleted from the December proposal but will be covered in the commentary.

(b) Liability of cardholder for unauthorized use. Paragraph (b) sets forth limitations on the amount of liability that may be imposed on a cardholder for unauthorized use of a credit card or a credit card account, and specifies the conditions for imposing liability. Footnote 20 of the December proposal, which referred to the burden-of-proof rules in § 133(b) of the act, has been deleted as inappropriate regulatory material.

Paragraph (b)(1) limits liability for unauthorized use to $50 or the amount of unauthorized transactions before notification to the issuer, whichever is less; this is unchanged from the December proposal.

Paragraph (b)(2) lists the conditions for imposing liability. As proposed in ***20865** December, paragraph (b)(2)(iii) required that, in order to impose liability for unauthorized use, the issuer must have disclosed to the cardholder a telephone number and address to be used for notifying the issuer of loss or theft of a credit card or possible unauthorized use. The disclosure would have had to appear on or with the periodic statement immediately preceding the unauthorized use. Proposed paragraph (b)(2)(iii) was intended to implement § 133(a)(1)(D) of the act as amended by the Simplification Act.

The Board believes that § 133(a)(1)(D) does not require the disclosure to appear on or with a periodic statement (rather, the references to a periodic statement serve as examples) and does not require disclosure of any specific means of notification. Therefore, proposed paragraph (b)(2)(iii) has been deleted, and § 133(a)(1)(D) is now implemented by paragraph (b)(2)(ii). (Paragraph (b)(2)(ii) also continues to implement § 133(a)(1)(C) of the act, as did paragraph (b)(2)(ii) of the December proposal.) It requires that, in order to impose liability, an issuer must have provided adequate notice of the cardholder's maximum liability and of a means by which the card issuer may be notified of loss or theft. Paragraph (b)(2)(ii) no longer requires, as it did in the December proposal, that this disclosure appear on the credit card or within two years preceding the unauthorized use; it also does not require, as did the December proposal, that the disclosure contain an address to be used for notification. Thus, the disclosure can be given at any time preceding the unauthorized use (for example, on or with the initial disclosures), and may state any means by which the card issuer may be notified (for example, a telephone number, an address, or both). Of course, the disclosure must also contain the other items specified, such as the dollar limitation on liability.

The remainder of paragraph (b)(2) is unchanged from the December proposal, except for the redesignation of proposed paragraph (b)(2)(iv) as paragraph (b)(2)(iii).

Paragraph (b)(3) specifies what constitutes notification to a card issuer of loss or theft of a card or of possible unauthorized use. It differs from the December proposal in that the phrase "required in the ordinary course of business" is substituted for the word "necessary," and the word "the" has been added before the phrase "pertinent information." The substituted language is the same as that in the current regulation and in the act.

Paragraphs (b) (4) and (5) relate to the effect of state law or an agreement regarding liability, and to business use of credit cards, respectively. They are unchanged from the December proposal and substantively unchanged from the current regulation.

The principal differences between the current regulation and the revised regulation regarding liability for unauthorized use can be summarized as follows. First, one of the conditions of imposing liability in the current regulation, the provision to the cardholder of a postage-paid, preaddressed card or envelope for notification of loss or theft, has been deleted (corresponding to an amendment to the act.) Second, another condition of liability, the provision of a disclosure of maximum liability and of means of notification, has been substantially revised, as described above, to simplify it and add flexibility. A third condition of liability, the provision of means of identification, has been relaxed in that now the issuer may provide a means to identify either the cardholder or the authorized user (rather than only the latter). Finally, the standard for notification to a card issuer of loss, theft, or possible unauthorized use differs from that in the current regulation in that anyone may provide the notification, rather than only the cardholder as under the current regulation. In addition to these substantive changes, some portions of the liability provisions have been considerably shortened and rephrased for simplicity, and certain obsolete material has been deleted.

(c) Right of cardholder to assert claims or defenses against card issuer. Paragraph (c) deals with the cardholder's right to assert against the card issuer any claim or defense concerning property or services purchased with a credit card, if the merchant has been unwilling to resolve the dispute.

Paragraphs (c) (1), (2), and (3) of the December proposal set forth the basic right to assert claims or defenses, certain geographic and dollar amount limitations on that right, exceptions to those limitations, and a formula for determining the maximum amount of claims or defenses assertable. In substance, these provisions are unchanged. However, for greater clarity, they have been renumbered paragraphs (c) (1) and (3), and certain material has been placed in footnotes.

Paragraph (c)(4) of the December proposal listed certain types of transactions that were excluded from the right to assert claims or defenses. This paragraph has been deleted, but its contents have been revised and now appear as a footnote to the heading of paragraph (c). The footnote exempts from the requirements of the paragraph check guarantee cards and debit cards when used in connection with overdraft credit plans, and check guarantee cards when used in connection with cash advance checks (special checks that draw on a credit account rather than an asset account).

The December proposal exempted check guarantee cards only when there was no agreement between the card issuer and the merchant relating to honoring the card or the associated checks, and the proposal did not exempt debit cards. The Board decided to broaden the exemption in the way described above because of serious operational problems cited by commenters as arising from applying the claims and defenses provisions to check guarantee and debit card transactions.

The debit card exemption applies whether the card accesses an asset account via point-of-sale terminals, automated teller machines, or in any other way, and whether the card qualifies as an "access device" under Regulation E or is only a paper-based debit card. On the other hand, when a single card serves both as an ordinary credit card and as a check guarantee or debit card, it will be subject to the provisions of § 226.12(c) when used as an ordinary credit card, but exempt when used as a check guarantee or debit card.

Another change in the exemption provision is that the exemption for use of a credit card to obtain a cash advance unrelated to any specific credit sale item has been deleted. The Board believes the exemption is unnecessary, in that such a transaction would not involve "property or services purchased with the credit card," and therefore such a transaction would not be included under the general rule of paragraph (c)(1).

Paragraph (c)(5) of the December proposal, prohibiting adverse credit reports where a claim or defense is asserted, has been renumbered paragraph (c)(2) and has been revised. First, a clause that appeared in the December proposal has been deleted; it conditioned the issuer's obligation not to make an adverse report on the issuer's knowing (or having reason to know) that the claim or defense had been asserted. This language does not appear in the current regulation. Section 130(c) of the act provides that a creditor may not be held liable for any violation if the creditor shows by a preponderance of the evidence that the violation was not ***20866** intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid any such error. Thus, essentially the same protection that would have been provided by the deleted language is provided by the act.

Another change is revised paragraph (c)(2) is the deletion of a sentence requiring correction of adverse credit reports in cases where the issuer has already made an adverse report, and then learns that a claim or defense has been asserted. This language also does not appear in the current regulation; the change parallels a corresponding deletion of language concerning correction of adverse credit reports in § 226.13. A number of commenters stated that the requirement to correct adverse reports would cause serious operational problems, since there is no time limit on the right to assert claims or defenses.

As a result of these changes, the provisions concerning the right to assert claims or defenses substantially parallel their counterparts in the current regulation. The provisions on excluded transactions differ, however. The language in the current regulation excluding certain cash advances has been deleted; as noted above, the Board believes that these transactions would not be covered by the general rule of paragraph (c)(1) in any event. Also, as discussed above, new exclusions have been added by footnote 24 to this paragraph. The revised regulation also differs from the current in that certain portions of this provision have been considerably simplified and shortened; no change in substance is intended.

(d) Offsets by card issuer prohibited. This portion of § 226.12 prohibits card issuers from offsetting a cardholder's credit card indebtedness against the cardholder's deposit account held with the card issuer. Paragraph (d)(1) sets forth the basic prohibition, and is unchanged from the December proposal.

Paragraph (d)(2) lists a number of actions of a card issuer that do not constitute violations of the prohibition on offsets. One type of permissible action is obtaining or enforcing a consensual security interest in funds of the cardholder on deposit with the issuer. The December version of this provision required that such a security interest be limited to an agreed-upon amount; as finally revised, the provision does not contain such a limitation.

The Board believes that § 169 of the act was not intended to apply to the granting of security interests in cardholders' deposit accounts. In addition, requiring that security interests obtained by depository institutions be limited to a specified amount, while security interests obtained by other types of creditors need not be so limited, would place depository institutions in a worse position than other creditors. Finally, circumvention of the offset prohibition should be prevented because (1) only consensual security interests are permitted, and thus the cardholder must affirmatively agree to grant the security interest; (2) the security interest can be enforced only through procedures by which other creditors could enforce their security interests in the same funds; and (3) any security interest granted to secure credit card indebtedness will be disclosed in the card issuer's initial disclosures to the cardholder. These requirements should eliminate the possibility of unfair surprise to the consumer, and of unfair advantage for depository institutions over other creditors that Congress sought to avoid in enacting § 169.

In the December proposal, the Board solicited comment on whether Regulation Z should contain provisions restricting the placing of holds on cardholders' deposit accounts. No such provision has been added to the regulation. However, the Board believes that placing a hold on funds in a cardholder's deposit account in connection with indebtedness arising under a credit card plan would, because the effect is the same as that of an offset, contravene the rule prohibiting offsets.

Paragraph (d)(3) states that the offset prohibition does not prohibit plans for automatic periodic debits against the cardholder's deposit account to repay the cardholder's credit card debt. These plans must be authorized in writing by the cardholder. This provision is substantively unchanged from the December proposal. Comment on the December proposal raised the question of whether it would be permissible for the issuer to debit the cardholder's deposit account to repay credit card indebtedness, not on an automatic periodic basis, but simply upon the specific request of the cardholder. For example, the cardholder might check a box on the credit card bill stub, requesting the issuer to debit the cardholder's account to pay the bill. The Board views this procedure as permissible, because the resulting debit would not constitute an offset.

Paragraph (d) as finally revised does not differ in substance from the current regulation, except that (1) various existing staff interpretations have been incorporated into the text of the regulation; (2) in addition to adding the staff position on consensual security interests to the text, that position has been changed in that such a security interest need no longer be limited to an agreed-upon amount; and (3) certain obsolete provisions (relating to automatic debit plans) have been deleted.

(e) Prompt notification of returns and crediting of refunds. Paragraph (e) sets certain requirements applicable to merchants and card issuers where the merchant agrees to accept a return of property, or forgive a debt for services, and accordingly to put through a credit to the consumer's credit card account. Paragraph (e)(1) requires any such merchant (other than a merchant that is also the card issuer) to transmit a credit statement to the card issuer within seven business days after accepting the return or forgiving the debt. It is unchanged from the version appearing in the December proposal. Comment on the December proposal indicated concern that merchants may be unable to meet the time limit in certain circumstances (for example, when refund requests are initiated at foreign locations). The Board notes that the seven business days begin to run when the merchant actually agrees to accept the return or forgive the debt, not at the time the refund request is initiated.

Paragraph (e)(2) requires a card issuer receiving such a credit statement to credit the consumer's account with a refund within three business days after receiving the statement. It is identical to its counterpart in the December proposal. Paragraph (e)(3) prohibits merchants from discriminating in their refund policy against credit card customers as opposed to cash customers. It is also unchanged from the December proposal.

Paragraph (e) as revised is substantively the same as the corresponding provision in the current regulation, except for the deletion of a promptness standard, which in the current regulation applies in addition to the seven-business-day and three-business-day standards.

(f) Discounts; tie-in arrangements. Paragraph (f)(1) provides that card issuers may not prohibit merchants from offering discounts for payment in cash instead of by credit card. This paragraph is unchanged from the December proposal. It differs from the current regulation in that it is phrased in terms of offering a discount to "a consumer," rather than to "all customers," in order to make clear that prohibiting discounts for particular customers would be as impermissible as prohibiting discounts for all customers of a merchant.

***20867** Paragraph (f)(2) provides that card issuers may not require merchants to maintain accounts, or obtain any other service not essential to the operation of a credit card plan, as a condition of participating in the plan. This paragraph is also unchanged from the December proposal. It differs from the current regulation in that an existing staff position has been incorporated in the regulatory text, to the effect that maintenance of an account for clearing purposes may be required if it is determined to be essential to the credit card plan and if no service charges or minimum balance requirements are imposed. Commenters urged that issuers be permitted to mandate the use of clearing accounts with services charges or minimum balance requirements; however, the Board believes that without the restrictions on these features of clearing accounts, the statutory provisions would be rendered meaningless.

(g) Relation to Electronic Fund Transfer Act and Regulation E. Paragraph (g) of the December proposal would have prohibited merchants from imposing surcharges for using a credit card rather than cash or a check. It corresponds to § 226.4(i)(4) of the current regulation. The provision has been deleted because the statutory prohibition on surcharges expired on February 27, 1981.

Paragraph (g) of the revised regulation corresponds to paragraph (h) of the December proposal. (The provision has no counterpart in the current regulation.) The paragraph provides guidance for cards or transactions that involve both credit and EFT aspects (for example, a debit card that accesses a checking account with overdraft credit privileges). It is intended to aid in determining whether Regulation Z or Regulation E rules apply regarding issuance and liability for unauthorized use. As to other § 226.12 matters, it makes clear that Regulation Z rules apply even though a transaction has EFT aspects.

The paragraph differs from the December proposal in that it primarily refers the reader to Regulation E, where the relevant rules are spelled out in detail, rather than repeating these detailed rules in full here. No change in substance is intended.

§ 226.13 Billing Error Resolution.

Section 226.13 addresses error resolution procedures and corresponds to §§ 226.2(j), 226.2(cc), and 226.14 of the current regulation, and to § 226.13 of the December proposal.

This section, like the December proposal, reflects a complete restructuring of the current regulatory provisions. The new structure should simplify the task of understanding and complying with the extremely complex statutory provisions in §§ 161 and 162 of the act. For example, under the revised regulation, the creditor's responsibilities are arranged in chronological sequence.

In addition, significant substantive changes have been made from the current regulation to facilitate creditor compliance with this section. For example, certain location requirements have been deleted, and the rules pending resolution have been streamlined.

A footnote to this section prohibits a creditor from accelerating a consumer's debt or restricting or closing the account because the consumer has exercised billing error rights, and alerts creditors to the statutory forfeiture penalty for failure to comply with any of the requirements of § 226.13. This footnote reflects protections afforded by § 701 of the Equal Credit Opportunity Act, § 161(d) of the Truth in Lending Act and § 226.14(b) of the current regulation. Although the footnote does not refer to the liability provisions of § 130 of the act, that section, of course, applies to violations of § 226.13 as it does to those of other sections.

(a) Definition of billing error. Section 226.13(a), which sets forth the definition of a billing error, corresponds to § 226.2(j) of the current regulation. The language of the billing error definition has been simplified in the revised regulation, and § 226.2(j)(1) of the current regulation has been divided into two paragraphs, § 226.13(a) (1) and (2), for clarity. No substantive change is intended in the definition of billing error, however, with the exception of the error defined in § 226.13(a)(7). That paragraph, which implements amended § 161(b) of the act, provides that the creditor's failure to transmit a periodic statement to the consumer's current address is a billing error, unless the creditor received notice of the address change fewer than 20 days before the end of the billing cycle requiring the periodic statement. In contrast to the current regulation, the revision specifies that notice of an address change must be in writing, and it expands the creditor's lead time from 10 to 20 days. The revised regulation differs from the December proposal by permitting the creditor to count the 20 days from the time it receives the notice, rather than from when the consumer mailed it.

(b) Billing error notice. Section 226.13(b) of the revised regulation corresponds to the current § 226.2(cc) ("Proper written notification of a billing error"). Most of the changes that have been made in paragraph (b) are editorial. For instance, the phrase "billing error notice" is used instead of "proper written notification of a billing error." The two footnotes to this provision reflect material in the body of the current regulation. The first footnote, which corresponds to § 226.14(a) of the current regulation and implements language in § 161(a) of the act, relieves the creditor from continuing error resolution responsibilities when the consumer concludes that no error occurred. While editorial changes have been made in the footnote, no substantive change is intended. Footnote 29, which corresponds to textual material in § 226.2(cc) of the current regulation and to § 161(a) of the act, permits creditors to require that the billing error notice not be made on the payment stub.

The regulatory text of this paragraph and the accompanying footnotes are identical to the corresponding provisions in the December proposal and implement parts of § 161(a) of the act. The timing requirements were misstated in the December Federal Register explanatory material. The 60-day period during which a consumer may assert a billing error notice begins when the creditor transmits the periodic statement, not when the consumer receives it.

(c) Time for resolution; general procedures. Section 226.13(c) corresponds to § 226.14(a) (1) and (2) of the current regulation and is substantively unchanged, although minor editorial revisions have been made. This provision implements parts of § 161(a) of the act. Section 226.13(c)(3) of the December proposal has been deleted from the revised regulation but will be contained in the commentary. That provison stated that a creditor could make a final correction of an alleged billing error without investigation, provided the creditor complied with all other applicable requirements of the section.

(d) Rules pending resolution. Section 226.13(d) consolidates all the rights and duties of the consumer and the creditor pending final resolution of the dispute. It corresponds to provisions in § 226.14 (a) through (e) of the current regulation and portions of §§ 161 and 162 of the act. This section has been reorganized from the December proposal.

Section 226.13(d)(1), which deals with a consumer's right to withhold disputed amounts, corresponds to parts of § 226.14 (a), (b), and (c) of the current regulation. A number of commenters asked for clarification of the meaning of "disputed amount" when the allegation concerns some part of the description ***20868** other than a dollar amount, such as the date or the seller's name. In such instances, the disputed amount would be the amount of the transaction or charge that corresponds to the disputed date or seller's name.

Section 226.13(d)(1) of the revised regulation and the related footnote also make clear what actions a creditor may take regarding the disputed amount pending resolution. This part of the provision implements § 161(a)(3) of the act by prohibiting a creditor from taking action to collect the disputed amount. The current regulatory provision, which also appeared in the December proposal with some modifications, immunizes a creditor from liability for inadvertently taking collection action within two days after receiving a billing error notice. In accord with the simplification principles, this latter provision has been deleted from the revised regulation. The Board believes that § 130(c) of the act adequately addresses inadvertent violations of the regulation that result from a bona fide error, despite the maintenance of procedures reasonably adapted to avoid any such error, and that a separate provision is therefore unnecessary.

Footnote 30 of the revised regulation corresponds to § 226.14 (b)(4) and (d) of the current regulation and § 226.13(d)(2) of the December proposal without substantive change. The footnote provides that a creditor is not prohibited from sending a periodic statement that reflects a disputed amount and related finance or other charges, provided that the creditor indicates on or with the periodic statement that payment of the disputed amount is not required pending resolution. In order to provide creditors with increased flexibility in designing disclosure forms, this paragraph deletes the requirement in the current regulation that the disclosure appear "on the face" of the periodic statement. In addition, to further reduce processing costs, the revised regulation differs from the current regulation and the December proposal by making clear that a creditor may preprint on all of its periodic statements that payment of any disputed amount is not required pending resolution. The footnote also provides that a creditor is not prohibited from deducting any disputed amount and related finance or other charges from the maximum amount of credit available to the consumer.

The revised regulation deletes as inappropriate regulatory material the provision in the December proposal prohibiting the imposition of additional finance or other charges on the undisputed portion of the amount solely because the consumer withholds payment of the disputed amount. The Board believes that this material should be included in the commentary.

The second sentence of § 226.13(d)(1) of the revised regulation, which corresponds to § 226.13(d)(5) of the December proposal, completely revises the requirements in current § 226.14(c) but contains only editorial changes from the December proposal. This provision sets forth the consumer's right to withhold payment, when payment is made automatically under a credit card plan. In such a plan, a cardholder authorizes a card issuer to deduct periodically an agreed-upon amount from the cardholder's account in order to pay the cardholder's indebtedness. Under the current regulation, the card issuer must prevent or restore an automatic debit of a disputed amount if it receives a billing error notice within 16 days after transmitting the first periodic statement that reflects the error. The new provision requires the card issuer to prevent an automatic debit of a disputed amount and related finance or other charges only if it receives a billing error notice up to three business days before the scheduled payment date. The card issuer does not have to restore a disputed amount if the billing error notice arrives after the three-business-day cut-off. If, however, any part of the disputed amount is still outstanding and unresolved at the time of the next automatic debit, the card issuer must prevent the automatic debit.

Section 226.13(d)(2) (Adverse credit reports prohibited), which corresponds to § 226.14(e)(1) of the current regulation, implements § 162(a) of the act by prohibiting a creditor from issuing an adverse credit report because the consumer fails to pay the disputed amount. The current regulatory provision, which was continued in modified form in the December proposal, immunizes a creditor from liability for inadvertently issuing an adverse credit report within two days after receiving a billing error notice. In addition, the current regulation and the December proposal delineated the creditor's reponsibilities if it received a billing error notice after having issued an adverse credit report regarding the disputed amount. The revised regulation returns to the statutory prohibitions, and deletes the separate provisions dealing with the grace period and corrective action. As noted in the discussion of § 226.13(d)(1), the Board believes that these provisions are unnecessary in light of § 130(c) of the act which addresses inadvertent violations. Section 226.13(d)(2) also differs from the December proposal, and reinstates the current regulatory language, by extending the prohibitions of this paragraph to any agent of the creditor.

The revised regulation also deletes the guidance in footnote 19 of the current regulation and § 226.13(d)(4) of the December proposal that the prohibition on adverse credit reports does not prohibit a creditor from reporting the amount or account as being in dispute. The Board intends to incorporate this position in the commentary.

(e) Procedures after creditor determines that a billing error occurred as asserted. Section 226.13(e), which corresponds to portions of § 226.14(a)(2)(i) and (b)(2) in the current regulation, outlines the creditor's responsibilities when it determines that a billing error has occurred. This provision substitutes the phrase, "a billing error occurred," for the term "erroneous billing" used in § 226.14(a)(2) and (b)(2) of the current regulation. The second part of paragraph (e)(2) of the December proposal, which permitted a creditor to notify a consumer of the correction on a periodic statement that is mailed within the time for resolution, has been deleted as inappropriate regulatory material. This position, which corresponds to footnote 18 of the current regulation, will be incorporated in the commentary. The current regulation and the December proposal contain a separate requirement that a billing error correction be identified as such on a periodic statement. The revised regulation also deletes this provision as unnecessary, in light of the general requirement that a creditor make clear disclosures, and thus the amount would need to be specifically identified when the creditor uses the periodic statement to satisfy its notice of corrections requirement. The Board intends to incorporate this guidance in the commentary.

(f) Procedures after creditor determines different billing error or no billing error occurred. Section 226.13(f), which corresponds to portions of § 226.14(a)(2) (ii) and (iii) in the current regulation, outlines the creditor's responsibilities when it determines, after making a reasonable investigation, that a billing error different from the error alleged by the consumer has occurred or that no billing error occurred. Footnote 31, which corresponds to material contained in § 226.14(a)(2) of the current regulation, sets forth the standard for reasonable investigation; it differs from the December proposal by reinstating the current regulatory language that a creditor may not deny a consumer's ***20869** allegation that property was not delivered unless the creditor determines that the property was actually "mailed or sent" as agreed.

The provision in § 226.13(f)(1) of the December proposal permitting the creditor to send its explanation either separately or with a periodic statement has been deleted from the revised regulation. The Board intends to incorporate this guidance in the commentary.

(g) Creditor's rights and duties after resolution. Section 226.13(g) corresponds to provisions in § 226.14(b)(3), (e)(1), and (e)(2) of the current regulation. This provision consolidates all of the creditor's responsibilities after determining whether a billing error occurred under paragraphs (e) and (f).

Section 226.13(g)(1), which corresponds to § 226.14(b)(3)(i) of the current regulation, requires a creditor to notify the consumer promptly if the consumer still owes all or part of a disputed amount, and to specify when payment is due. The current regulation expressly relieves the creditor from mailing a separate notification of the amount owed, if it was provided in the creditor's explanation that no billing error occurred. Although the Board continues to take the position that the requirements of paragraphs (f)(1) and (g)(1) may be met in a single notice, this interpretation will be incorporated in the commentary rather than in the revised regulation.

Section 226.13(g)(1) of the revised regulation also deletes as inappropriate regulatory material the explanation in the December proposal that the amount the consumer still owes may include minimum periodic payments that accrued during the error resolution process. The Board also believes that the amount may include related finance and other charges that accrued pending resolution. The Board intends to incorporate these positions in the commentary.

Section 226.13(g)(2) of the revised regulation, which corresponds to § 226.14(b)(3)(ii) of the current regulation, requires a creditor to allow a consumer the same free-ride period disclosed under §§ 226.6(a)(1) and 226.7(j), if any, to pay any part of the disputed amount still owed. The current regulation requires the creditor to give the consumer the greater of the customary free-ride period in which to pay, or at least ten days, if any lesser free-ride is normally given. The reference to a minimum period is deleted in the revised regulation as unnecessary, as the creditor is required to mail or deliver the periodic statement at least 14 days prior to the closing date of the free-ride period. Moreover, the revised regulation refers to the disclosed free-ride period rather than a customary free-ride period, in keeping with the principle that precise rules should apply whenever possible. Provisions in § 226.13(g)(2) of the December proposal that were similar to the current regulation have been changed for the reasons discussed above.

The revised regulation has no separate counterpart to § 226.14(b)(3)(iii) of the current regulation, which provides that a creditor need not give a free-ride period after error resolution if one normally is not given. The Board believes that the substance of this provision is appropriate commentary material.

Section 226.13(g)(3) corresponds to § 226.14(e)(1) of the current regulation, with one clarifying change. The current regulation permits the creditor to report an account as delinquent if an disputed amount remains unpaid after any customary free-ride period or ten days, whichever is longer. The revised regulation uses any free-ride period disclosed as the relevant time period, rather than any "customary" free-ride period. As discussed in connection with § 226.13(g)(2), this change is intended to furnish a more precise, easy-to-apply standard. The paragraph is unchanged from the December proposal; however, commenters asked for further clarification of the time period during which a consumer may make a payment before a creditor may issue an adverse credit report. If the creditor normally provides a free-ride period, both here and under § 226.13(g)(2), the creditor may use its usual triggering event to toll the time for payment. If no free-ride is normally given by the creditor to measure the payment period, however, the

Board believes that the consumer has ten days to pay from receipt of the notice of the amount owed before the creditor may issue an adverse credit report.

Section 226.13(g)(4), which corresponds to § 226.14(e)(2) of the current regulation, imposes certain credit reporting responsibilities on a creditor that receives further written notice from a consumer disputing the amount after resolution. This provision eliminates the current requirement that the creditor report the subsequent resolution of a previously reported delinquency "in writing." It adopts the flexible approach in § 162(c) of the act permitting other reasonable forms of notice.

(h) Reassertions of billing error. Section 226.13(h), which relieves the creditor from further error resolution responsibility if a consumer reasserts substantially the same billing error, corresponds to language in § 161(a) of the act and to the last paragraph in § 226.14(a)(2)(iii) of the current regulation with one minor change. The revised regulation clarifies that a creditor still has post-resolution credit reporting responsibilities if the consumer sends a further written notice that the amount is still in dispute, as provided in paragraph (g)(4). This provision is unchanged from the December proposal.

(i) Relation to Electronic Fund Transfer Act and regulations. Section 226.13(i) of the revised regulation has no counterpart in the current regulation. It is designed to facilitate compliance when financial institutions extend credit incident to electronic fund transfers that are subject to the Board's Regulation E. The section provides that a creditor must comply with the error resolution procedures in Regulation E, and with Regulation Z § 226.13(d) (Rules pending resolution) and (g) (Creditor's rights and duties after resolution). This provision is unchanged from the December proposal.

The Board notes that § 226.14(j) of the current regulation and § 226.13(i) of the December proposal, regarding the creditor's forfeiture penalty for failure to follow the error resolution procedures properly, have no counterpart in the revised regulation. In deleting this provision, the Board adopts a longstanding staff interpretation that the forefeiture penalty, as a self-executing liability provision, does not lend itself to regulatory interpretation. As previously stated, footnote 27 is designed, in part, to alert creditors to this penalty provision.

§ 226.14 Determination of annual percentage rate.

Revised § 226.14 corresponds to § 226.5(a) of the current regulation. Section 226.14(a) defines the annual percentage rate and establishes the disclosure tolerance for open-end credit. The tolerance is the same as that under the current regulation, that is, 1/8 of one percentage point above or below the annual percentage rate determined in accordance with the section. A footnote to this paragraph incorporates the material that appeared in § 226.14(e) of the December proposal and affords creditors special protection for errors that result from the good faith use of faulty calculation tools. While the Board believes that this protection will no longer be appropriate or necessary in light of the expanded defense for such errors under § 130 of the act, the provision has been included in response to commenters that expressed concern ***20870** about the applicability of this defense before April 1, 1982, the effective date of the amended act.

The rule for determining the annual percentage rate for initial disclosures required under § 226.6(a)(2) and for advertising purposes under § 226.16(b)(2) is the same; consequently, these two instances are addressed together in revised § 226.14(b).

Section 226.14(c) states the rules applicable to the determination of the annual percentage rate for purposes of the periodic statement. The introductory language of the paragraph states that the annual percentage rate for purposes of § 226.7(d) is computed by multiplying each periodic rate by the number of periods in a year. The remainder of the section states the requirements for determination of an annual percentage rate where a finance charge is in fact imposed during the billing cycle and disclosure of the annual percentage rate is required under § 226.7(g).

Section 226.14(c)(1) corresponds to § 226.5(a)(1) of the current regulation and provides that where the finance charge is solely the product of the application of one or more periodic rates to the balance of the account, the creditor may determine the annual percentage rate by one of two methods. The creditor may either multiply the periodic rate(s) by the number of periods in a year or it may use the "quotient method." With the exception of some minor editorial changes, this section is the same as in the current regulation.

Section 226.5(a)(2) of the current regulation deals with the annual percentage rate calculation when a creditor imposes periodic finance charges in amounts based on specified ranges or brackets of balances. The paragraph was deleted from the December proposal and the Board again solicited comment as to whether any creditor relied on this paragraph to calculate an annual percentage rate. In light of the fact that the Board received no indication that any creditors rely on the paragraph, in response to either the May or December proposals, the provision has been deleted from the revised regulation.

Current regulation § 226.5(a)(3)(i)-(iii) has been restructured for clarity and now appears at § 226.14(c)(2)-(4). Section 226.14(c)(2) contains the material in current § 226.5(a)(3)(i) and, as was the case in the December proposal, the revised regulation recognizes that an annual percentage rate cannot be determined where a finance charge is imposed during a billing cycle with no outstanding balance. (See footnote 32.) Paragraphs (c) (3) and (4) contain the material in current § 226.5(a)(3) (ii) and (iii), respectively, and, with the exception of minor editorial revisions, remain the same.

A footnote has been added to § 226.14(c) (2) and (3) of the revised regulation. It deals with calculation of the annual percentage rate where a loan fee, points, or any similar charge is imposed upon the opening of an account. The regulation now provides that the amount of any such finance charge should not be added to the total finance charge in calculating the annual percentage rate.

In the December draft, the Board stated that it believed that such fees would be collected at the time of application and that they would not enter into the annual percentage rate calculation on the periodic statement. The finance charges, in that instance, would be disclosed only on the initial disclosure statement under revised § 226.6(a)(4). It appears, however, that there are instances in which such finance charges are imposed at the time the account is opened and are either billed on the subsequent periodic statement or withheld from the proceeds of the first advance on the account.

In either event, since the charges do not relate to a specific transaction or activity on the account, but relate solely to the opening of the account, such charges should not be included in the calculation of the annual percentage rate. The Board believes that their inclusion would result in significant distortions of the annual percentage rate and delivery of a meaningless, possibly misleading, disclosure to consumers. Moreover, § 107(a)(2) of the act does not appear to require the inclusion of such charges in the annual percentage rate calculation for open-end plans. That section requires that the "finance charge for the period to which it relates" be divided by the "amount upon which the finance charge for that period is based." These types of finance charges are neither related to the billing period nor are they based upon a specific amount for the period.

Section 226.14(d), like the December proposal, incorporates the first two paragraphs of Board Interpretation § 226.506. It addresses the situation in which a creditor uses the quotient method to determine the annual percentage rate and applies a daily periodic rate or rates to determine some or all of the finance charge on the account. Under the current regulation and under revised paragraphs (c)(1)(ii) and (c)(2), the creditor must multiply the quotient of the finance charge divided by the balance(s) to which it is applicable by the number of "billing cycles" in a year. Where a daily periodic rate is used, the formula does not apply. This paragraph provides creditors with an alternate method to determine the annual percentage rate under those circumstances. The remainder of current Board Interpretation § 226.506 is in a footnote to Appendix F.

§ 226.15 Right of rescission.

Section 226.15 of the revised regulation corresponds to the same section of the December proposal and to § 226.9 of the current regulation. It applies to a consumer's rescission rights on an open-end credit plan that is secured by the consumer's principal dwelling. Footnote 31 of the December proposal, which set forth exempted transactions, has been deleted and replaced with a new paragraph, § 226.15(f).

(a) Consumer's right to rescind. Under the amended statute, a consumer's rescission right arises with each transaction (defined by § 125(a) of the act also to include opening an account and increasing a credit limit) that is secured by the consumer's principal residence. Section 125(e) of the amended act provides, however, that for a three-year trial period a creditor need not provide the right to rescind at the time of each individual credit extension made under a secured open-end credit plan, if the extensions are made in accordance with a previously established credit limit for the plan. (After March 31, 1985, however, the consumer will have the right to rescind each subsequent extension made under an open-end credit plan secured by the consumer's principal dwelling.) Consequently, § 226.15(a)(1) has been revised to implement more precisely the statutory scheme.

Section 226.15(a)(1) of the revised regulation implements another statutory change in that it provides the right to rescind a transaction secured by the consumer's principal dwelling, even where that dwelling is characterized as personal property rather than real property.

The revised regulation narrows the scope of the rescission right from the current regulation by no longer applying the right to property "expected to be used as the consumer's principal dwelling." The right is limited, instead, to property used as the consumer's principal dwelling at the time the security interest is retained.

A number of commenters contended that the language in the December proposal could be read to provide the ***20871** right to rescind to a non-resident co-owner of the property. To clarify this matter, the definition of "consumer" in the revised regulation provides that, for rescission purposes, a consumer is any natural person who is both an owner and resident of a dwelling which is or will be subject to a security interest as part of the credit transaction.

Section 226.15(a)(2) of the revised regulation is substantively unchanged from § 226.9(a) of the current regulation and § 226.15(a)(2) of the December proposal.

Section 226.15(a)(3) provides that the consumer must be given three business days in which to rescind the transaction. The Board recognizes the need for a special business day definition for rescission purposes (see discussion in § 226.2). Consequently, the revised regulation, unlike the December proposal, provides that for purposes of rescission, the term means Monday through Saturday, excluding certain specified federal holidays. This business day definition corresponds to that in footnote 14 of the current regulation.

Regardless of when the required rescission notice and material disclosures are delivered, § 226.15(a)(3) provides for termination of the rescission right three years from the occurrence giving rise to the right of rescission, upon transfer of all of the consumer's interest in the property, or upon sale of the property, whichever occurs first. This provision differs from both the December proposal and the current regulation in specifically including sale of the property as an event that terminates the consumer's rescission right. A sale of the property would include a transaction in which a consumer sells the dwelling and takes back legal title through a purchase money note and mortgage. Transfer of all of the consumer's interest includes such transfers as bequests and gifts. Neither a sale of the property nor transfer of all of the consumer's interest need be voluntary. Accordingly, a foreclosure sale would terminate an unexpired right to rescind.

The footnote to § 226.15(a)(3) lists the material disclosures for purposes of this section. All of the listed material disclosures must be given whenever the right of rescission arises. The disclosures must contain sufficient information to meet the content requirements for those disclosures set forth in § 226.6. For a variable rate program, this would include the required information on the circumstances under which the rate may increase, limitations on the increase, and the effect of an increase. The Board contemplates that giving the initial disclosure statement would satisfy the requirement of providing the material disclosures.

Section 226.15(a)(4), which corresponds to § 226.9(f)(1) of the current regulation, provides that a rescission by only one consumer entitled to rescind is effective as to all consumers involved in the transaction.

(b) Notice of right to rescind. Section 226.15(b), which sets forth the timing, form, and content requirements for the rescission notice, is unchanged from the December proposal. The revised provision differs from § 226.9(b) of the current regulation is not requiring the use of specified language on the notice or that the notice be in a particular type size. To allow further flexibility, and Board takes the position that the notice may be either separate from the material disclosures or combined with them, even when the creditor uses an initial disclosure statement to furnish the material disclosures. This position, which differs from the rule that governs closed-end transactions, is based in part on the fact that the more liberal format requirements for open-end credit allow a creditor to combine disclosures on a multi-page document in a manner that would still be clear and conspicuous to the consumer. The notices in the appendix are models for creditors to use in complying with the requirements of this paragraph.

(c) Delay of creditor's performance. Section 226.15(c) of the revised regulation is unchanged from the December proposal and essentially restates § 226.9(c) of the current regulation. In light of the operational problems involved in notifying all merchants who might grant credit extensions once a consumer's account is established, a special provision (included in both the December proposal and the revised regulation) relieves the creditor from civil liability for having violated this section when a third party, with no knowledge that the credit limit has been raised or that an additional security interest has been added, provides materials or services to the consumer within the rescission period. This situation might occur, for example, when a consumer makes a credit card purchase below the merchant's floor limit, so that the card issuer is not contacted for authorization and has no opportunity to instruct the merchant to delay the transaction. The protection afforded by this provision is available to the creditor as long as it does not in fact take a security interest in the consumer's dwelling to secure debts on such materials or services.

Since agricultural credit is no longer subject to Truth in Lending, § 226.15(c) also differs from the current regulation in its deletion of the agricultural credit exemption.

(d) Effects of rescission. This section, which implements amended § 125(b) of the act, sets forth the effects of rescission and outlines the obligations of both the creditor and the consumer once the consumer has rescinded the transaction. The section basically restates the current regulation (with the necessary statutory amendments), but is substantially reorganized from the December proposal. The December proposal addressed in separate sections the differing effects of rescission when an individual credit extension is rescinded, in contrast to when a consumer rescinds upon the occurrence of some other transaction (for example, an increase in the credit limit). When a consumer rescinds within the initial three-day rescission period after one of the latter occurrences, the creditor is required to delay providing the consumer with goods and services, and therefore the property exchange procedures applicable to the rescission of individual credit extensions are not relevant. However, when a consumer exercises a right of rescission that did not expire within the original period (for example, because material disclosures were never given) the property exchange provisions might well be applicable because of intervening credit extensions. By restructuring the paragraph, the Board intends no substantive change from the December proposal in the effects of rescission when no credit extension is involved. In addition to cancelling the applicable portion of the security interest, the credit limit increase, or the plan, the creditor would be obliged to return any amounts related to the event that gives rise to the rescission right. For example, if a consumer rescinds the plan when it is opened, the creditor would be obliged to return any membership or application fee paid; a consumer who rescinds an increase in the credit limit would be refunded any fee imposed for a new credit report.

When a consumer rescinds a credit extension, the consumer is not liable for any amount, including any finance charge, related to the credit extension. The Board emphasizes that the term "any amount" does not refer to cash advances or to property given by the creditor to the consumer. The term does include such amounts as application and commitment fees and sums that may have been expended by the creditor to purchase services from other parties, such as title fees and required appraisal or survey fees. Moreover, because § 125(b) of the act requires the creditor ***20872** to return money or property given as earnest money, downpayment, or otherwise, the creditor must also return any money or property given by the consumer to third parties in connection with the credit transaction. The Board emphasizes, however, that creditors are not responsible for returning money given by the consumer to third parties unrelated to the credit transaction.

Section 226.15(d) (2) and (3) sets forth the procedures for the cancellation of the security interest and the exchange of property between the consumer and the creditor. Section 226.15(d)(2) of the revised regulation also reflects the statutory amendment expanding from 10 to 20 days the time period within which the creditor must return a consumer's money or property and take the necessary action to terminate the security interest. Further, to reflect the staff's longstanding interpretation of this provision, the term calendar days is used to describe the time period.

Section 226.15(d)(3) provides that the consumer may retain possession of any money or property received from the creditor until the creditor has performed under paragraph (d)(2). Once the creditor has met its obligations, the consumer must tender the money or property to the creditor. (For example, a consumer would tender to a card issuer the amount of purchases made with a bank credit card, or the actual appliances to the merchant in a two-party situation.) If the tender of property would be impracticable, the consumer may offer to pay its reasonable value. Property may be tendered at the location of the property or at the consumer's residence, but money must be tendered at the creditor's place of business. The latter rule has been specifically incorporated into the regulation.

This paragraph also provides that if a creditor does not take possession of the money or property within 20 calendar days after the consumer's tender, the consumer may keep it without further obligation. The 20-day limit in this paragraph also reflects a statutory change. The period does not begin until the consumer tenders the property.

Section 226.15(d)(4) reflects amended § 125(b) of the act. It provides that a court may modify the procedures outlined in paragraphs (d)(2) and (d)(3).

(e) Consumer's waiver of right to rescind. This provision is unchanged from the December proposal but it differs significantly from the provisions of § 226.9(e) of the current regulation about the nature of the emergency giving rise to a consumer's waiver of the rescission right. Under the revised regulation, the consumer need only determine that the extension of credit is needed to meet a bona fide personal financial emergency. This standard essentially mirrors that in § 125(d) of the act. While the requirements are eased, this provision continues to prohibit the use of preprinted forms for purposes of waiver, in order to prevent any abuse of the waiver rule.

The Board emphasizes that waiver or modification of the rescission right should not become a pro forma matter, but should occur only in rare circumstances. Although several commenters urged that a waiver automatically insulate a creditor from liability for failing to provide the rescission right, the Board believes that such protection is unwarranted. Accordingly, before accepting a waiver, creditors must assure themselves that the reasons given for the waiver are both substantial and credible and that the waiver is in all respects bona fide. This requirement, combined with the prohibition on the use of preprinted forms, will prevent abusive practices, while at the same time permitting consumers to waive the rescission right in appropriate circumstances. The Board also notes that under § 226.28 of the revised regulation creditors are required to retain evidence of compliance for a period of two years. This includes rescission waivers. This paragraph also retains the rule in § 226.9(f)(2) of the current regulation, which requires that the waiver be signed by all consumers entitled to rescind.

(f) Exempt transactions. This paragraph of the revised regulation sets forth the types of transactions that are exempt from the right of rescission in an open-end credit plan. The paragraph corresponds to footnote 31 of the December proposal and § 226.9(g) of the current regulation.

In implementing amended § 125(e)(1) of the act, § 226.15(f)(1) differs from the December proposal in that it exempts residential mortgage transactions from the right of rescission. In the accompanying material to the December proposal, the Board suggested that residential mortgage transactions would never be made on bona fide open-end credit plans, and therefore the exemption was not necessary. Several commenters noted, however, that an advance on a bona fide open-end credit plan could be made for a downpayment for the purchase of a dwelling with other advances contemplated on the open-end plan. In such a case, the advance for the purchase of the dwelling would be exempt from the rescission right. Accordingly, the exemption for residential mortgage transactions has been included in the revised regulation.

In addition, § 226.15(f)(2) reinstates the statutory and current regulatory provision that the right to rescind does not apply to plans in which a state agency is a creditor. This differs from the December proposal by deleting the proposed exemption for plans in which a federal agency is a creditor.

§ 226.16 Advertising.

This section deals with the advertising of open-end credit plans; it corresponds to the provisions of § 226.10 of the current regulation and § 226.16 of the December proposal.

Section 226.16(a), like § 226.10(a) of the current regulation, sets forth the general requirement that creditors may advertise only those terms that they actually arrange or offer. In response to requests from commenters the words "or will arrange or offer" have been added to clarify that creditors may advertise the terms of upcoming programs without being in violation of this section.

Section 226.16(b) corresponds to the same section in the December proposal and to § 226.10(c) of the current regulation. It sets forth those terms, so-called "trigger" terms, which, when appearing in an advertisement, require the disclosure of additional credit terms also set forth in this section. This section also details which disclosures must be made an advertisement contains a trigger term.

As a result of statutory changes to § 143 of the act, the "triggering" terms have been reduced to the initial disclosures as set forth in § 226.6, and the additional disclosures required by the use of those terms have been modified to include only finance charges and membership charges.

Section 226.16(c), generally, corresponds to and is substantially the same as § 226.10(b) of the current regulation, setting forth the requirements for advertising in catalogs and multiple-page advertisements.

Paragraphs 226.16(c)(2), however, has no counterpart in the current regulation. The provision, which is unchanged from the December proposal, incorporates into the revised regulation the essence of current Board Interpretation § 226.1002. That interpretation provides that a catalog or multiple-page advertisement complies with the regulation if the table or schedule of terms included in the advertisement incorporates all appropriate disclosures for a representative scale of amounts up to a level of the more commonly sold higher-priced property or services offered.

***20873** Subpart C--Closed-End Credit

Subpart C incorporates all provisions in Regulation Z that relates to closed-end credit. It includes not only the general rules for content, timing and form of closed-end disclosures, but all advertising, rescission and annual percentage rate provisions of the regulation as they apply to such transactions.

§226.17 General disclosure requirements.

Section 226.17 contains the general requirements relating to the time, form and content of closed-end credit disclosures. The section is based on §§ 121, 122, 124 and 128 of the act and §§ 226.6 and 226.8 of the current regulation.

(a) Form of disclosures. This paragraph prescribes the manner in which Truth in Lending disclosures must be presented. The rules, based on §§ 122 and 128(b) of the act, are designed to highlight for consumers the essential credit terms.

Disclosures must be segregated from other matters. They may be presented in a separate document or incorporated in documents containing other terms related to the transaction. If the disclosures are included in documents containing other terms (such as the contract), they must be separated from the other items. This may be done, for example, by placing the disclosures in a boxed section of the form or by separating them from the contract provisions with bold print dividing lines. This approach differs from the current regulation which permitted disclosures to be interspersed with other material on the contract documents. The phrase "either on the credit contract or on a separate document" has been deleted from paragraph (a)(1) as unnecessary. In addition, the disclosures need no longer appear "beginning on the front of the document." The Board believes that this requirement is unnecessary. However, the location of the required disclosures remains subject to the regulation's general clear and conspicuous standard.

Paragraph (a)(1) and accompanying footnotes contain special rules and exceptions to the general requirement of segregation of required disclosures.

The last sentence of the paragraph requires that the itemization of the amount financed under § 226.18(c) always appear separate from the segregated disclosures. Footnote 38 permits four disclosures required by § 226.18 to appear apart from the segregated disclosures. These disclosures are the creditor's identity under § 226.18(a), variable rate information under § 226.18(f)(4), credit life or property insurance premiums under § 226.18(n), and certain charges related to a security interest which are excludable from the finance charge under § 226.18(o). Any of these disclosures may appear with the segregated disclosures, together or separately on other documents, or combined with the itemization of the amount financed under § 226.18(c)(1).

Footnote 37 to paragraph (a)(1) specifically permits the inclusion of five items of information even though they are not "directly related" to the segregated disclosures: an acknowledgment of receipt, the consumer's name, account number, and address, and the date of the transaction. These last two items are additions to those in the December proposal.

The term "directly related," as used in this paragraph, is construed very narrowly in order to implement the congressional intent in requiring the segregation of Truth in Lending disclosures. No additional information may appear with the federal disclosures, except as specifically permitted.

Paragraph (a)(2) states that the words "finance charge" and "annual percentage rate" must be presented more conspicuously than the other required disclosures. This paragraph is based on § 122(a) of the act and § 226.6(a) of the current regulation. It is substantially similar to its counterpart in the December proposal, with minor editorial revisions.

Section 226.6(a) of the current regulation requires that numerical amounts be expressed as numerals and that those numerals meet a minimum type size standard. Those requirements have been eliminated as unnecessary.

(b) Time of disclosures. This paragraph, which implements § 128(b) of the act, states the timing rules for closed-end credit disclosures. It continues to reflect the original regulatory requirement, found in § 226.8(a), that disclosures be provided before consummation of the transaction. However, as noted in the discussion of § 226.2 above, the definition of consummation has been modified. Consummation is defined as the time at which the consumer becomes contractually obligated on a credit transaction, as determined by applicable law. This is contrary to staff interpretations of the current regulation which held that consummation could occur upon the payment of a nonrefundable fee, even in the absence of a legally binding obligation.

(c) Basis of disclosures and use of estimates. This paragraph is designed to provide guidance to creditors in making disclosures, particularly when the necessary information may not be known with any certainty at the time the disclosures are made. This paragraph reflects a number of editorial changes as well as substantive revisions.

Paragraph (c)(1) requires that disclosures reflect the terms of the legal obligation between the parties. This approach differs from interpretations of the current regulation, which looked to the actual agreement between the parties as the basis for disclosures even if that agreement was contrary to the legal obligation.

One editorial change has been made to this paragraph. The phrase "legal obligation" replaces the phrase "legally enforceable obligation" in the December proposal. This change was made to avoid any implication that a creditor may be subject to a Truth in Lending violation if a court reviewed the credit transaction and determined that an already agreed-upon contract term was unenforceable on the basis of equity or other grounds.

Paragraph (c)(2) provides that disclosures may be estimated if the exact information is unknown at the time the disclosures are made. This provision is based on § 121(c) of the act and § 226.6(f) of the current regulation. Under the revised regulation, as in the present rule, a creditor has no liability for an inaccurate disclosure if the necessary information is not reasonably available by the time of consummation. However, even if a disclosure is validly marked as an estimate before consummation, the creditor may still be required to redisclose if more accurate information is available by the time of consummation, as set forth in § 226.17(f). The estimates must be made in good faith, on the basis of the best information reasonably available, and designated as estimates in the segregated disclosures. No further explanation of the basis for the disclosures may be included with those disclosures, although an explanation may appear as additional information apart from the segregated disclosures.

Paragraph (c)(3) permits certain factors to be disregarded by creditors in making calculations and disclosures for Truth in Lending purposes. The four factors designated are very similar to §§ 226.6(j) and 226.8(s) of the present regulation, with one revision. Paragraph (c)(3)(ii) permits creditors to disregard the fact that payment schedules may change as a result of the creditor's "business day," rather than "Saturday, Sunday or holiday."

Paragraph (c)(4) permits creditors to ignore certain payment schedule variations in making calculations and ***20874** disclosures and incorporates in one provision two separate but similar "minor irregularities" rules. Both the December proposal and the current regulation contain one special rule regarding schedule irregularities for annual percentage rate calculations (§ 226.22(e) and § 226.5(b)(5), respectively) and another rule for irregularities for all other calculations (§ 226.17(c)(4) and § 226.8(r), respectively). The annual percentage rate rule has permitted creditors to disregard the effects of a first period variation and any payment irregularity caused by that period variation. The non-annual percentage rate rule has also permitted creditors to disregard first period variations, but has limited the resulting payment irregularities that could be ignored to only the final payment.

To eliminate the unnecessary complexity of two separate but similar rules, new § 226.17(c)(4) combines in one provision both of the special "minor irregularities" rules, adopting the slightly broader scope found in the annual percentage rate rule. Under the revised regulation, creditors may treat as regular certain odd first periods and any odd payments flowing from that odd first period, in calculating and disclosing all required terms. In the current regulation and the December proposal, a footnote to this provision addresses the manner in which the term of the transaction, the first period and the regular period may be measured. This material has been deleted from the regulation, and the issue will be addressed in the commentary. The Board anticipates the text of the footnote will be incorporated in the commentary without substantive change.

Paragraph (c)(5) continues the policy in § 226.4(g) of the current regulation of requiring that disclosures for demand obligations be calculated on the basis of a specified maturity. Like the December proposal, this paragraph provides for an assumed maturity of one year, rather than the one-half year specified in the current regulation. Under § 226.18(i), the demand feature must be disclosed, as well as the assumed one-year maturity, where applicable.

Disclosures for demand obligations should be based on the alternate maturity date, rather than an assumed maturity of one year, only in those cases in which the alternate maturity date is stated in the legal obligation between the parties. This is contrary to interpretations of the current regulation, which require that the disclosures be based on any informal side agreement between the parties that might differ from the legal obligation. Under the revised regulation, when the parties have only informally agreed to a repayment schedule, the obligation is viewed purely as a demand obligation with the disclosures based on an assumed maturity date of one year. However, when the repayment agreement constitutes a legal obligation between the parties (as determined by state law) the disclosures must be based on that agreement.

Several types of mortgages include features which, in the Board's view, make them demand obligations. Some obligations may contain a demand feature which may be exercised at any point during the term, while others may convert to demand obligations after a fixed term. The latter type has been addressed in Board Interpretation § 226.816 of the current Regulation Z. Another example of a mortgage with a demand feature is one containing the call option required by the Federal National Mortgage Association (FNMA). In states prohibiting due-on-sale clauses, FNMA requires mortgages purchased by it to include a call option rider that may be exercised after seven years. These mortgages are generally written as long-term obligations, but contain a demand feature which may only be exercised within a thirty-day period at seven years. The disclosures for these mortgages should be based upon the legally enforceable alternate maturity date, unless there is none; in that case, disclosures should be based on an assumed one-year term. For instance, if a mortgage containing the seven-year FNMA call option were written as a thirty-year obligation, the disclosures would be based on the thirty-year term since that is the alternate maturity date.

The Board does not consider typical balloon payment mortgages, where payments are based on a long-term amortization schedule, but with final payment due after a shorter term, to be demand obligations. In these transactions, no demand feature is actually provided for in the contract. For example, a mortgage with a payment schedule based on 30 years and a term of five years would not be treated as a mortgage with a demand feature, in the absence of any contractural demand provision.

Paragraph (c)(6)(i), based on § 226.8(i) of the current regulation, provides rules relating to the treatment of multiple advances under a written agreement to extend credit up to a certain amount. It permits the creditor either to treat all of the advances as a single transaction or to disclose each advance as a separate transaction. Under the current regulation, all advances must be disclosed as a single transaction. Except for minor editorial revisions, this paragraph is substantially similar to § 226.17(c)(6)(ii) of the December proposal.

Paragraph (c)(6)(ii), previously designated as paragraph (c)(6)(iii) in the December proposal, provides a similarly flexible rule for the disclosure of construction loans that may be permanently financed. These transactions have two distinct phases, similar to two separate transactions. The construction period usually involves several disbursements of funds at times and in amounts that are unknown at the beginning of that period, and the consumer generally pays only accrued interest until construction is completed. Unless the obligation is paid at that time, the loan then converts to permanent financing in which the loan amount is amortized just as in a standard mortgage transaction. This special rule permits the creditor to give either one combined disclosure for both the construction financing and the permanent financing, or a separate set of disclosures for the two phases. It is available whether the consumer was initially obligated to accept construction financing only or both construction and permanent financing. If the consumer is obligated on both phases and the creditor chooses to give two sets of disclosures, both sets must be given to the consumer initially, because both transactions would be consummated at that time.

Paragraphs (c)(6)(i) and (ii) are not mutually exclusive. For example, in a transaction that finances the construction of a dwelling which may be permanently financed by the same creditor, the construction phase may consist of a series of advances under an agreement to extend credit up to a certain amount. In such cases, the creditor may disclose the construction phase as one or more than one transaction and also disclose the permanent financing as a separate transaction.

The substance of Board Interpretation § 226.813 has been incorporated as Appendix D to the revised regulation. Its use is limited to multiple advance loans for the construction of a dwelling.

Paragraph (c)(6)(i) in the December proposal, which concerned splitting and consolidating transactions, has been deleted in the revised regulation. In most instances, the determination of whether a single transaction is involved is not difficult but the Board recognizes that guidance may be needed in unusual ***20875** circumstances. For example, it may be unclear on what basis a creditor should disclose the same-day purchase of a television and a stereo, or a loan that includes the incidental sale of insurance. Creditors must retain considerable flexibility in structuring their transactions in order to meet the needs of their customers, as well as their own operational requirements. Similarly, the regulation should allow flexibility to creditors in tailoring disclosures to those transactions. Thus, in the first example the creditor could disclose the sales as either one or two credit sale transactions. In the second example, the creditor may disclose the loan and the sale of insurance as one transaction (either loan or credit sale) or disclose on the basis of two transactions, one a loan and the other a credit sale.

Comment was solicited in the December proposal on the disclosure of "wrap-around" mortgages. This type of transaction involves a creditor's "wrapping" the outstanding balance on an existing loan and advancing additional funds to a borrower. The borrower makes a single payment to the new creditor, who makes the payments on the pre-existing loan to the original creditor. The Board believes that "wrap-around" loans should be treated as new transactions, but with the disclosures calculated as they would be for a refinancing. This approach is based on Official Staff Interpretation FC-0146, which treats "wrap-around" loans as the equivalent of refinancings. To illustrate, the amount financed would equal the principal balance remaining on the original obligation plus the amount of the new advances.

(d) Multiple creditors; multiple consumers. This paragraph provides special rules for transactions involving more than one creditor or consumer. It is based on § 121(a) and (b) of the act, as well as § 226.6(d) and (e) of the current regulation.

The first sentence has been revised from its counterpart in the December proposal to allow multiple creditors to decide among themselves which one is to provide the required disclosures. The Board has left this decision to the creditors because a uniform rule designating which creditor must provide disclosures could not readily accommodate a variety of situations and might have imposed a greater burden than necessary on creditors. In any case, however, the consumer must receive a complete integrated set of disclosures, rather than partial disclosures from each creditor.

In view of the revised definition of "creditor," transactions involving multiple creditors are not likely to occur. When there are multiple creditors, however, all disclosures for the transaction must be given, even if the disclosing creditor would not otherwise have been obligated to make a particular disclosure. For example, when an automobile dealer and a bank are both creditors financing the sale of a car, the total sale price under § 226.18(j) must be disclosed, even though the creditors have agreed that the non-seller bank will make the disclosures.

(e) Effect of subsequent events. This paragraph, which is similar to § 226.6(g) of the current regulation, protects creditors against liability for inaccurate disclosures when a later event occurs to make those disclosures inaccurate. However, creditors may still be responsible for providing more accurate information to consumers, as outlined in §§ 226.17(f), 226.19 and 226.20.

(f) Early disclosures. This paragraph, which has no counterpart in the current regulation, provides special redisclosure rules when creditors make early disclosures to consumers. Under the current regulation, if a creditor discloses before the point of consummation and a subsequent event makes the disclosures inaccurate in any way, all new disclosures must be provided. In the Board's view, this may discourage creditors from providing information at an earlier time, when that information could be most useful to consumers in comparing credit sources.

To address this problem, the December proposal would have relieved creditors of any redisclosure responsibility when early disclosures were given. Because this approach does not assure that consumers receive updated information regarding significant changes in credit costs, the new regulation requires redisclosure under certain circumstances when the creditor makes disclosures before the date of consummation. Applying the standard set forth for certain mortgage transactions in § 128(b) of the act and § 226.19 of the revised regulation, paragraph (f) requires creditors that choose to disclose before the date of consummation to redisclose before consummation when the annual percentage rate has changed from the disclosed rate by more than 1/8 of 1 percentage point in regular transactions or more than 1/4 of 1 percentage point in irregular transactions, as defined in the general annual percentage rate rules in § 226.22(a). At their option, creditors may either furnish a complete set of new disclosures or disclose only the changed terms.

(g) Mail or telephone orders--delay in disclosures. This paragraph provides special timing rules for mail or telephone transactions. It implements § 128(c) of the act, and is based on § 226.8(g) and Board Interpretation § 226.802 of the current regulation, with the additon of the total sale price as a required disclosure.

This paragraph permits a creditor to delay making the disclosures until the due date of the first payment if certain conditions are met. If the conditions are not met, the general timing rules apply, and disclosures must be made before consummation. Paragraph (f)(2) of the December proposal, which reflected this general rule, has been deleted as unnecessary.

The list of required information has been expanded from the December proposal to require the same information on variable rates as required by § 226.18(f)(1)-(3). The Board believes that information regarding variable rates is essential to informed credit decisions, particularly in light of the increasing prevalence of this term and its impact on other credit information. The paragraph also reflects several minor editorial revisions from its counterpart in the December proposal.

(h) Series of sales--delay in disclosures. This paragraph provides special timing rules for credit sales that are made in a series under an agreement permitting subsequent sales to be added to an outstanding balance. It implements § 128(d) of the act, and is based on § 226.8(h) and Board Interpretations §§ 226.804 and 226.805 of the current regulation. Several editorial changes have been made in the paragraph, but it remains substantially similar to its counterpart in the December proposal.

(i) Interim student credit extensions. This paragraph restates, with one substantive revision, the special rule for interim student credit extensions found in footnote 37 to § 226.18 of the December proposal and in Board Interpretation § 226.809 of the current regulation. It permits creditors in certain student credit extensions to omit disclosure of the finance charge, payment schedule, total of payments and total sale price.

The substantive change relates to the types of student credit extensions that may utilize this special rule. Although the credit extension must still be of an interim nature and for educational purposes, it need no longer be guaranteed by any state, federal or private agency. In the Board's view, the abbreviated disclosures are necessitated by the interim nature of the extensions, and the fact that they are guaranteed is not relevant to the coverage of the rule.

"Interim credit extension" is intended to cover transactions without a set ***20876** repayment schedule. This phrase is used in place of "student loan" since some transactions of this type are actually credit sales, as, for example, where a university is the creditor.

§ 226.18 Content of disclosures.

Section 226.18 sets forth the disclosures required in closed-end credit transactions and corresponds generally to current § 226.8(b), (c), and (d).

The disclosures required by this section need be made only as applicable. Multiple-purpose standard forms, designed for use with a variety of transactions, may be used so long as the required disclosures are clear and conspicuous. Where the amounts of several numerical disclosures are the same, the "as applicable" language would also permit creditors to combine the terms, so long as it is done in a clear and conspicuous manner. For example, if in a particular transaction the amount financed equals the total of payments, the creditor may disclose "amount financed/total of payments," together with descriptive language, followed by a single amount. However, if the terms are separated on the disclosure statement and separate space is provided for each amount, both disclosures must be completed, even though the same amount is entered in each space.

Footnote 37 in the December proposal provided special abbreviated disclosures for certain student credit extensions. In revised form that footnote has been incorporated in § 226.17 as new paragraph (i).

Five of the disclosures required by this section must be further explained to the consumer in a manner similar to the descriptive phrases shown in the regulation. While the regulation does not require each term and its descriptive phrase to be placed together in any particular manner, creditors may not separate them in such a way as to obscure their relationship to each other.

(a) Creditor. This paragraph corresponds to § 226.8(a) of the current regulation and requires that the creditor making the disclsoures be identified. At the creditor's option, the creditor's address or telephone number may be included, although the name of the creditor is sufficient. As discussed in § 226.17(a), this disclosure is one of four in § 226.18 that may appear apart from the segregated disclosures.

(b) Amount financed. Paragraph (b) requires disclosure of the "amount financed," using that term, and a descriptive explanation. In variable rate transactions, the information in the descriptor may be revised to reflect the variable rate feature.

A number of comments on the December proposal expressed concern regarding the calculation of the amount financed, as set forth in paragraph (b). Their concern focused on the fact that, as then drafted, paragraphs (b)(1) and (b)(3) read together appeared to call for two deductions of the same finance charge that resulted in an erroneously low amount financed. Under § 226.18(b), all finance charges must be deducted from the amount of credit in calculation of the amount financed. If the principal loan amount reflects finance charges which meet the definition of a prepaid finance charge in § 226.2, those charges would be included in the paragraph (b)(1) amount and deducted under paragraph (b)(3). However, if the principal loan amount includes finance charges which do not meet the definition of a prepaid finance charge (such as add-on or discount interest added to the face amount of the obligation), the amount referred to in paragraph (b)(1) must exclude those finance charges.

Because an accurate paragraph (b)(1) amount is essential to calculating an accurate amount financed and because the presence of an add-on or discount finance charge in a loan frequently complicates this process, the following examples illustrate the application of paragraph (b) to these types of transactions. Each example assumes a loan request of $1000 for one year, subject to a 6% precomputed interest rate, with a $10 loan fee collected at consummation.

In the first example, the creditor assesses add-on interest of $60 which is added to the $1000 in loan proceeds for an obligation with a face amount of

$1060. In this example, the principal for purposes of paragraph (b)(1) is $1000; no amounts are added under paragraph (b)(2), and the $10 loan fee (a prepaid finance charge) is deducted under paragraph (b)(3). The amount financed is $990.

The second and third examples both assume the application of a discount finance charge, on the same terms as set forth above. The difference between these latter two examples--and a source of confusion regarding discount transactions under Regulation Z--lies in the amount of loan proceeds provided to the consumer. In one instance, the creditor distributes $940 to the consumer, who is liable for an obligation with a face amount of $1000. In this example, the principal under paragraph (b)(1) is $940, which results in an amount financed of $930, after deduction of the $10 prepaid finance charge under paragraph (b)(3). In the other instance, the creditor collects the discount finance charge by increasing the face amount of the obligation to $1060, with the consumer receiving $1000. The principal under paragraph (b)(1) is thus $1000 and the amount financed $990, after deducting the $10 prepaid finance charge under paragraph (b)(3).

In paragraph (b)(1), "principal loan amount" essentially corresponds to the term "amount of credit" found in present § 226.8(d)(1). In the second portion of this paragraph, relating to credit sales, the phrase "cash price (subtracting any downpayment)" corresponds to the "unpaid balance of cash price" in present § 226.8(c)(3). "Downpayment" includes any pick-up payment that meets the § 226.2 definition of downpayment. As explained in that section, a creditor has the option of treating a deferred downpayment as part of the downpayment if that deferred payment meets the criteria set forth in the definition. Deferred downpayments that are not treated as part of the downpayment (either because they do not meet the definition or the creditor simply chooses not to treat them as a downpayment) are included in the amount financed. Deferred downpayments that do meet the § 226.2 definition and are treated as such are not part of the amount financed under § 226.18(b)(1).

Paragraph (b)(2) refers primarily to those charges which would be characterized as "other charges" under § 226.8(c) and (d) of the current regulation. These would normally include any fees that are not part of the finance charge, to the extent that the customer decides to finance them rather than paying them separately at consummation of the transaction. This paragraph would not encompass any amount already accounted for under paragraph (b)(1). For purposes of calculation, the creditor may, at its option, include any such amounts (other than finance charges) as part of the basic credit amount in paragraph (b)(1), rather than adding them separately under paragraph (b)(2). These two paragraphs require only that such amounts not be either counted twice or ignored in calculating the amount financed.

Paragraph (b)(3) requires the deduction of any prepaid finance charges from the amount financed. As discussed in § 226.2, prepaid finance charges are defined to include amounts withheld from the proceeds and amounts paid separately by the consumer.

(c) Itemization of amount financed. This paragraph requires a written itemization of the amount financed at ***20877** the customer's request. Creditors may provide a written itemization of the amount financed as a matter of course, without awaiting a request from the customer. If the creditor chooses not to provide an itemization as a matter of course, the disclosures must include a statement of the customer's right to receive that itemization.

The order of the items listed in this paragraph has been changed and now parallels the model form that is contained in Appendix H. The itemization must be separated from the remainder of the required disclosures and must be provided at the same time as the other disclosures.

This paragraph establishes only a minimum standard for the itemization of the amount financed. At the creditor's option, more information may be included in the itemization, such as additional categories or a mathematical progression that depicts the arithmetic relationship of the items.

In the December proposal, the Board requested comment on whether transactions subject to the Real Estate Settlement Procedures Act (RESPA) should be exempt from paragraph (c). RESPA requires creditors to provide good faith estimates of closing costs similar to the amount financed itemization. The legislative history indicates that creditors subject to RESPA could comply with that Truth in Lending requirement by using the estimates of closing costs. The comments also support a complete exemption. Therefore, footnote 39 to paragraph (c) exempts RESPA transactions entirely from the requirements of that paragraph.

Paragraph (c)(1)(i) normally reflects the amount of the check given to the consumer in the transaction. Paragraph (c)(1)(ii) would typically include a credit sale balance with the creditor or the payment of the loan balance on a prior loan.

Paragraph (c)(1)(iii) calls for disclosure of amounts such as the following: amounts paid to other creditors of the customer in bill consolidation loans; amounts paid to insurance companies for credit life or property insurance; amounts paid to credit bureaus, appraisers or public officials. Amounts paid to other persons generally must be identified by name except as noted in footnote 40, which permits a generic identification for certain types of charges.

(d) Finance charge. This paragraph, which requires disclosure of the total finance charge, is substantially revised from both the current regulation and the December proposal.

A new footnote to the paragraph provides a tolerance for disclosure of the finance charge. The disclosed finance charge will be considered accurate if it is not more than $5 above or below the exact finance charge in a transaction involving an amount financed of $1000 or less, or not more than $10 above or below the exact finance charge where the amount financed exceeds $1000. In the December proposal, the Board solicited comment on a general finance charge tolerance equivalent to 1/8 of 1 percent of the annual percentage rate. While the current regulation includes several cause-related tolerances, such as the so-called "minor irregularities" provisions, Regulation Z has never provided a per se margin of error unrelated to particular causes. The Board believes that a slight tolerance for de minimis errors is appropriate, particularly in light of the specific congressional authorization for non-annual percentage rate tolerances, but not one so large as to significantly understate the true cost of credit for consumers. The footnote to this paragraph therefore provides for a small per se tolerance for minor discrepancies. This tolerance is in addition to the existing tolerances for minor irregularities and other specific causes, which have been incorporated into the revised regulation.

Paragraph (d) also reflects two other revisions from the current regulation that incorporate statutory changes. First, the regulation no longer calls for itemization of the components of the finance charge. Second, real estate transactions are no longer exempt from disclosure of the total finance charge.

(e) Annual percentage rate. Paragraph (e) corresponds to § 226.8(b)(2) of the original regulation. It requires disclosure of the annual percentage and a descriptive phrase briefly defining that term. As in paragraph (d), the creditor may modify the descriptive phrase for variable rate transactions. The de minimis exception to this disclosure found in current § 226.8(b)(2) has been retained in accordance with the statute, and is set forth in a footnote to this paragraph.

(f) Variable rate. In a substantially revised form, paragraph (f) corresponds to § 226.8(b)(8) of the current regulation and requires additional disclosures for transactions in which the annual percentage rate may increase. It reflects two substantive changes from its counterpart in the December proposal and the current regulation.

First, a new footnote to this section exempts from the requirements of § 226.18(f) transactions in which the creditor has complied with variable rate regulations of other federal agencies. This exemption eliminates redundant disclosure of a variable rate provision which is already described for consumers under other regulations.

Second, paragraph (f)(4) has been changed to reflect the extension of the hypothetical increase to all variable rate transactions, rather than only real estate transactions with variable rate features. Variable rate transactions are becoming increasingly common for credit extensions outside of the real estate loan context and non-residential mortgage transactions may also involve large amounts of money. Even in small transactions, the hypothetical example is needed because it better provides the customer with an understanding of the impact a potential increase has in terms of dollars and cents.

No specific numerical basis for the hypothetical disclosure is required. The Board believes this requirement should be flexible in order to enable creditors to tailor the example to their own credit programs and their lending environment. At the creditor's option, the disclosed hypothetical may be either general or transaction-specific. The creditor may provide a standard example that represents the general type of credit offered by the creditor or an example that directly reflects the terms and conditions of the particular transaction.

Several editorial changes have also been made in paragraph (f) which are not intended to affect the substance of the paragraph. Material in paragraphs (f)(1) and (f)(3) of the December proposal, relating to identification of an index and reference to payment schedule changes, will be incorporated into the commentary.

For all transactions subject to the requirements of this pargraph, the disclosures must be given for the full term of the transaction, with all disclosures calculated on the basis of the rate in effect at the time of consummation of the transaction.

The limitations referred to in paragraph (f)(2) do not include any legal limits in the nature of usury or rate ceilings under state or federal statutes or regulations. In addition, paragraph (f) does not apply to increases resulting from delinquency (including late payment), default, assumption, acceleration or transfer of the collateral.

In the December proposal, the Board solicited comment on the proper treatment under Regulation Z of several unusual mortgage financing arrangements. After futher analysis and consideration of comments received, the Board has determined that at least two such mortgages--renegotiable rate ***20878** mortgages and shared appreciation mortgages--should be viewed as variable rate transactions.

Renegotiable rate mortgage instruments as described in Offical Staff Interpretation FC-0172 involve a series of short-term loans secured by a long-term mortgage, where the lender is obligated to renew the short-term loans at the customer's option. At the time of renewal, the interest rate may increase. Disclosures must be given for the term of the mortgage (e.g. 30 years) with all disclosures calculated on the basis of the rate in effect at the time of consummation of the transaction.

"Shared equity" or shared appreciation" mortgages bear a fixed rate of interest and contingent interest based on the consumer's equity in the mortgaged property. The contingent interest is payable in a lump sum at a specified time. All disclosures should be based on the fixed interest rate, while the shared appreciation feature, including the conditions for its imposition, the time at which it would be collected, and the limitation on the creditor's share, must be described under § 226.18(f).

Graduated payment mortgages are not considered variable rate transactions and are not subject to the disclosure requirements of this paragraph.

(g) Payment schedule. Under paragraph (g), which corresponds to current § 226.8(b)(3), creditors must disclose the payment schedule. This paragraph contains two material changes from its counterpart in the December proposal.

A footnote to the December proposal permitted creditors to make an abbreviated disclosure of payment schedules involving payment amounts not varying more than five percent in a series. This special rule, which has no counterpart in the current regulation, was intended to accommodate the same types of disclosure problems addressed in current Interpretation § 226.808 and similar special rules. After consideration of the comments received and further analysis, the Board has determined that the proposed five percent rule should not be adopted. The comments indicated that this provision did not resolve the problems it was intended to address and may have needlessly complicated the disclosures.

As an alternative, paragraph (g) incorporates a special rule similar to Interpretation § 226.808. Paragraph (g)(2) permits creditors to make an abbreviated payment schedule disclosure where the application of a rate to a declining balance creates irregular payments. Transactions of the type specifically described in the Board Interpretation, as well as mortgage transactions such as those discussed in Official Staff Interpretations FC-0003, FC-0025, FC-0030, and FC-0104, may take advantage of this provision. In the abbreviated payment schedule, the creditor must disclose the dollar amount of both the highest and lowest payments and a reference to the variations in payments.

Creditors may combine the disclosures permitted by paragraph (g)(2) with the general payment schedule requirements, in transactions such as graduated payment mortgages where only a portion of the payment schedule may fit the conditions set forth in the paragraph. For example, in a graduated payment mortgage where payments rise sharply for five years and then decline gradually over the next 25 years as the mortgage insurance premium decreases, the first five years would be disclosed pursuant to the general rule in paragrph (g) of the regulation and the next 25 years could be disclosed according to the footnote.

As in present Interpretation § 226.808, the special rule provided in paragrpah (g)(2) applies only to the payment schedule disclosure. Whether or not the payment schedule is disclosed pursuant to the paragraph, the actual amounts of payments must be taken into account in calculating and disclosing the finance charge and the annual percentage rate.

A portion of Board Interpretation § 226.815 has been added as paragraph (g)(1). In demand obligations with no alternate maturity date, the creditor has the option of disclosing only the due dates or periods of scheduled interest payments in the first year. The other required disclosures under paragraph (g) need not be given for those transactions.

For purposes of this paragraph, payments may include amounts beyond the amount financed and finance charge. These would include certain insurance premiums of the type described in Official Staff Interpretation FC-0157, where the premiums are not part of either the amount financed or the finance charge, as well as real estate escrow amounts such as taxes added to the payments in mortgage transactions. The Board believes that the inclusion of these items in the payment schedule may provide a more accurate picture of the amount the creditor actually collects from the consumer and may assist consumers in better understanding the terms of transactions.

As discussed in § 226.2, deferred downpayments or "pick-up payments" that meet the conditions set forth in the definition of downpayment may be treated as part of the downpayment. Even if treated as a downpayment, that amount may nevertheless be disclosed as part of the payment schedule, at the creditor's option.

(h) Total of payments. Paragraph (h) corresponds to § 226.8(b)(3) of the current regulation and requires disclosure of the total of payments, using that term. The paragraph also requires that the disclosure contain a descriptive explanation similar to that contained in the regulation. The descriptive explanation may be modified for variable rate transactions with a brief phrase such as "based on the current annual percentage rate which may change."

The total of payments is the sum of the payments disclosed under § 226.18(g). For example, if the creditor disclosed a deferred portion of the downpayment as part of the payment schedule, that payment must be reflected in the total disclosed under this paragraph.

The footnote to this paragraph permits creditors to omit disclosure of the total of payments in single-payment transactions. This exception does not apply to a transaction calling for a single payment of principal combined with periodic payments of interest.

(i) Demand feature. This paragraph requires special disclosures for demand obligations. It is based on Interpretation § 226.815 of the current regulation, but in a substantially revised form. The demand disclosure requirement applies to transactions that are payable on demand from the outset of the transaction, as well as to transactions that are not payable on demand at the time of consummation but convert to a demand status after a stated period. The latter type of transaction would include mortgages with demand features as addressed in Board Interpretation § 226.816 and Federal National Mortgage Association call option mortgages. As discussed in § 226.17(c)(5), those transactions would be considered demand obligations subject to paragraph (i).

The demand feature triggering the disclosures required by this paragraph is intended to include only those demand features provided for by the parties as part of the agreement. For example, this provision would not apply to transactions which convert to a demand status as a result of the customer's default. In addition, loans without an ascertainable maturity date are not considered demand loans unless the agreement actually provides for a demand feature.

Demand obligations with an alternate stated maturity are subject to the same disclosure requirements as other ***20879** transactions, including disclosure of the payment schedule. Thus, if those demand loans call for periodic interest payments, the number, amounts and timing of the payments must be shown under paragraph (g). In addition, the term of the payment schedule must reflect that alternate maturity date and not the assumed one-year term, which applies only to obligations without a stated maturity.

As explained in paragraph (g), demand obligations with no alternate maturity date may take advantage of a special rule similar to current Board Interpretation § 226.815 in disclosing the payment schedule. Under paragraph (g)(1), creditors need only disclose the due dates or periods of payments of any scheduled interest payments for one year.

(j) Total sale price. This paragraph, which requires disclosure of the total sale price in a credit sale transaction, is unchanged from the December proposal. It corresponds to the "deferred payment price" in § 226.8(c)(8)(ii) of the current regulation and is the sum of the cash price, other charges of the type described in paragraph (b)(2), and the finance charge. A new definition of downpayment has been added to the regulation in § 226.2. That definition addresses the treatment of deferred downpayments and the continued availability of Board Interpretation § 226.504.

(k) Prepayment. This paragraph requires that the consumer be told whether or not a penalty will be imposed or a rebate given in the event of prepayment of the obligation in full. This section has been substantially revised from § 226.8(b) of the current regulation.

The revised regulation, in accordance with § 128(a)(11) of the amended statute, eliminates the requirement that an explanation be given of how rebates or penalties would be computed. The only disclosure required is whether or not a penalty and/or rebate will occur if the obligation is prepaid in full.

Paragraph (k)(1) applies to simple interest obligations. Paragraph (k)(2) covers transactions with precomputed finance charges. These two paragraphs, like current § 226.8(b)(6) and (7), are intended to distinguish two separate types of transactions according to the nature of the finance charges imposed. The regulation recognizes, however, that a single transaction may include both types of finance charges, requiring disclosure under both paragraph (k)(1) and paragraph (k)(2).

Both paragraphs require a disclosure of "whether or not" a rebate will be given or a penalty imposed, reflecting the statutory language. This language requires a negative disclosure in transactions where prepayment will not result in a refund or penalty; silence in such cases will not comply with paragraph (k).

The disclosure requirements apply to any prepayment, whether voluntary or involuntary, as in the case of prepayments resulting from acceleration. If a penalty or refund is possible for any type of prepayment, even though not for all, a positive disclosure is required. Any difference in rebate or penalty policy, depending on whether prepayment is voluntary or not, may not be disclosed with the segregated disclosures.

Reflecting the approach taken in the December proposal, paragraph (k)(1) defines simple interest obligations very narrowly to include only those transactions in which the interest calculation takes account of each reduction in principal. This definition would exclude charges, including certain types of mortgage insurance premiums, that may be calculated on the basis of a declining principal balance but do not take every principal reduction into account.

The word "penalty" as used in paragraph (k)(1) encompasses only those charges which are assessed strictly because of the prepayment in full of the obligation, as an addition to all other amounts. Charges assessed or contemplated at the outset of the transaction, such as points in a mortgage loan, would not be considered a penalty for purposes of this paragraph. However, the Board considers a minimum finance charge in a simple interest transaction as a penalty for purposes of paragraph (k)(1).

Paragraph (k)(2) encompases any finance charge that does not meet the requirements of paragraph (k)(1). This provision includes typical precomputed finance charges such as add-on or discount finance charges, as well as simple interest transactions that do not fit the strict requirements of paragraph (k)(1). Paragraph (k)(2) has been redrafted to more closely reflect the statutory language of § 128(a)(11), with no substantive change intended. Although the word "rebate" is used in the regulation, creditors retain some flexibility in terminology, as illustrated by the use of the word "refund" in the model form in Appendix H.

(1) Late payment. Paragraph (1) implements amended § 128(a)(10) of the act. This provision requires disclosure only of charges imposed on account of late payments before maturity, that is, charges added to individual delinquent installments by a creditor who otherwise considers the transaction ongoing on its original terms. This is a change in emphasis from the current regulation, which requires disclosure of default charges as well as charges imposed solely for individual late payments.

This provision does not apply to a variety of terms which, in the Board's view, do not constitute late payment charges. Several of these terms have been addressed in official staff interpretations and will be reflected in the commentary to the regulation. For example, as stated in Official Staff Interpretation FC-0054, a right of acceleration is not a late payment charge. Fees imposed for actual collection costs, such as attorneys fees assessed prior to maturity, are also not late payment charges for purposes of paragraph (1). As indicated in Official Staff Interpretation FC-0083, the continued accrual of a finance charge in a simple interest obligation need not be disclosed as a late charge, unless a higher rate of interest is imposed once a payment is overdue.

The use of a statutorily required limit as the basis for disclosure under this paragraph is permissible. For example, stating that the charge in the event of a late payment is 5% of the late amount, not to exceed $5.00, is sufficient.

(m) Security interest. Paragraph (m) requires disclosure of a security interest. This provision is unchanged from the December proposal but has been significantly reduced by statute from § 226.8(b)(5), its counterpart in the current regulation. The paragraph no longer requires disclosure of the type of security interest taken. In addition, the creditor need not further describe the property to which the security interest attaches if the property purchased with the credit serves as collateral for the obligation. Any transaction in which the credit is being used to purchase the collateral is considered a purchase money transaction and the more abbreviated property identification disclosure required for these types of transactions may be used, even when the obligation does not meet the definition of a credit sale. Unlike the current regulation, disclosure of after-acquired property clauses is not required.

In non-purchase money transactions, the property subject to the security interest must be identified by "item or type." This disclosure would be satisfied by a general disclosure of the category of property subject to the security interest, such as "household goods." At the creditor's option, however, a more precise identification of the goods may be provided.

***20880** The question of what constitutes a security interest that must be disclosed under this paragraph is addressed in the definition of a security interest in § 226.2 of the new regulation. As noted in that discussion, the definition is much narrower than that used in the current regulation. It excludes many incidental property interests, such as an interest in insurance proceeds, unearned insurance premium rebates, accessions and improvements.

Several commenters expressed concern over the disclosure implications of "spreader" or "dragnet" clauses. A spreader clause is one which states that the collateral for a particular loan will also secure all future extensions of credit from the creditor. The fact that collateral for other loans is being used to secure the present obligation constitutes a security interest and must be disclosed. However, the Board has determined that a specific identification of that collateral would unnecessarily complicate the disclosures and that a reminder of the interest arising from the prior indebtedness would be most helpful to consumers. The disclosure can be accomplished by language such as "collateral securing other loans with us may also secure this loan." At the creditor's option, a more specific description of the property involved may be given.

(n) Insurance. This paragraph requires disclosure of the information outlined in § 226.4(d), if creditors wish to exclude credit life and property insurance premiums from the finance charge. The provision is unchanged from the December proposal.

The disclosures to which this paragraph refers are contained in § 226.4(a)(5) and (6) of the current regulation. However, § 226.8 of the current regulation contains no specific counterpart to paragraph (n).

As noted in the discussion of § 226.17(a)(1), this disclosure is one of four § 226.18 terms that may appear apart from the other disclosures. If this disclosure is made separate from the other transactional disclosures, it may appear with any other information, including the amount financed explanation, any information prescribed by state law or other supplementary material. However, if the creditor includes this disclosure with the segregated disclosures, no additional information may accompany it.

(o) Certain security interest charges. This paragraph requires disclosure of certain charges associated with a security interest, if the creditor wishes to exclude those charges from the finance charge. It is based on § 226.4(b) of the current regulation. This provision has been amended from the December proposal by the addition of a specific description of the charges that are excludable under § 226.4(e) of the revised regulation. This will reduce the necessity for the creditor to refer to § 226.4(e) in order to determine the scope of paragraph (o). This disclosure may appear, at the creditor's option, apart from the other § 226.18 disclosures.

(p) Contract reference. This paragraph, requiring a reference to the contract documents for certain additional information, remains unchanged from the December proposal.

The current regulation contains no counterpart to this provision, which was added by § 128(a)(12) of the amended act. Since some disclosures have been eliminated and others abbreviated by statute, this provision requires a cross-reference to the contract documents for certain information not contained in the disclosure statement. This includes information about nonpayment, default, the right to accelerate the maturity of an obligation, and prepayment rebates and penalties.

In addition to the items required to be referenced in the disclosure, the new regulation provides for two optional contract references. In the Board's view, the inclusion of a contract reference for security interest and assumption information may be useful to consumers.

The specific language of paragraph (p) is not mandatory. A creditor may alter the statement with a reference to the specific contract document, such as "promissory note" or "retail installment contract."

In the December proposal, the Board solicited comment on whether creditors should be permitted to separate portions of the statement and place each component with the particular disclosure to which it relates. Although most comments did not oppose this possibility, the Board believes, after further analysis, that the entire text of the contract reference should appear in one location. Placing a contract reference near each pertinent substantive disclosure would lengthen and complicate the disclosures.

(q) Assumption policy. This paragraph provides that in residential mortgage transactions, the consumer must be told whether or not a subsequent purchaser or assignee may be permitted to assume the obligation on its original terms.

It implements amended § 128(a)(13) of the act, a new required disclosure with no counterpart in the current regulation.

A number of commenters expressed concern that the disclosure required by this paragraph would commit them to permitting assumptions, when in fact the ultimate decision would depend on circumstances unknown at the time of disclosure. To alleviate this concern, creditors may include a brief phrase such as "subject to conditions" or "under certain circumstances" in complying with paragraph (q).

(r) Required deposit. This paragraph requires a statement that the annual percentage rate does not reflect the effect of a required deposit, which is defined as a deposit that the creditor requires the consumer to maintain as a condition of a specific credit extension. This requirement has no counterpart in the December proposal and is based, in substantially revised form, on the concept of required deposit balances in § 226.8(e)(2) of the current regulation.

Under the current regulation, a required deposit balance must be disclosed to the consumer and taken into account in calculation of the annual percentage rate. While the Board believes that the existence of the required deposit is of importance to consumers and should be disclosed, the calculations necessary to reflect the deposit in the annual percentage rate are extremely complex and impose a substantial burden on creditors. Therefore, the revised regulation requires creditors to inform consumers of the presence of a required deposit and its potential effect on the cost of credit, but eliminates the requirement that the deposit be included in calculation of the annual percentage rate.

The footnote to this paragraph sets forth three types of deposits that need not be considered required deposits subject to the requirement. Use of the phrase "need not" permits creditors to include the disclosure required by paragraph (r) even in cases where there is doubt as to whether the deposit constitutes a "required deposit" within the meaning of the paragraph.

The first exception is based, in expanded form, on the escrow account exception in current § 226.8(e)(2)(i). Unlike the current regulation, the exception is not limited to real estate transactions, nor is it restricted to escrows for taxes and insurance. For example, the escrow account may be for maintenance fees (such as condominium fees) or for repairs, as in the case of completion escrows.

The second exception is for deposits that earn at least 5 per cent per year. The Board believes that where the consumer receives more than nominal interest on the deposit, that amount need not be viewed as a required deposit. This exception applies whether ***20881** the deposit is held by the creditor itself or by a third party.

The third exception is for Morris Plan transactions. This is a deposit balance that will be wholly applied toward satisfaction of the consumer's obligation in the transaction. This provision is similar to what appears in § 226.8(e)(2)(ii) of the current regulation.

The exceptions in § 226.8(e)(2) (iii) and (iv) of the current regulation for pre-existing deposits offered as security and "forced savings" plans have been deleted. However, if such deposits earn at least 5 per cent, they need not be considered required deposits.

In an effort to assist creditors in determining whether this disclosure is required and to ease the burden of compliance, the Board believes a list of transactions that do not fit the general definition is important. The following situations need not be treated as required deposits:

requirement that a borrower be a customer or a member, even if there is a fee or a minimum balance involved

deposits that are immediately available to the customer

required property insurance escrow on a mobile home transaction

refund of interest when the obligation is paid in full

escrow of condominium fees

funds deposited with the creditor to be disbursed (for example, for construction) before the loan proceeds are advanced

escrow of loan proceeds to be released when the repairs are completed

This list is not intended to be all-inclusive but rather to give guidance in determining whether a deposit is a required deposit for purposes of this paragraph.

Proposed Official Staff Interpretation FC-0171, published for comment on March 31, 1980 (45 FR 02771), addressed the application of the required deposit balance provisions in the current regulation to so-called "loop-hole" accounts. In those transactions, a portion of the funds necessary for the purchase of a certificate of deposit is advanced to the consumer by the issuing bank. The interpretation states that the portion of the deposit contributed by the consumer is not a required deposit balance under § 226.8(e)(2). Paragraph (r) specifically exempts these deposits from the required deposit provision, since the portion of the funds contributed by the consumer is subject to an interest rate of more than 5 per cent. Because the revised regulation clearly resolves the primary issue addressed in that letter, proposed Official Staff Interpretation FC-0171 is being withdrawn as unnecessary.

§ 226.19 Certain residential mortgage transactions.

This section, which implements § 128(b)(2) of the act, has no corresponding provision in current Regulation Z. The rule requires early disclosure of credit terms in residential mortgage transactions that are subject to the Real Estate Settlement Procedures Act (RESPA). Disclosures must be given the earlier of (1) three business days after the creditor's receipt of a written application, or (2) consummation. "Business day" is defined in § 226.2 of the regulation. This three-day requirement coincides with the time period contained in RESPA for providing good faith estimates of settlement costs.

Paragraph (a) is unchanged from § 226.19 of the December proposal. The Board solicited comment on the proper definition of "written application" and, in particular, whether the definition should correspond to that in RESPA. The majority of commenters agreed with the Board that "application" should parallel RESPA in light of the congressional intent that RESPA and

Truth in Lending disclosures be coordinated. Thus, "written application" is defined as in RESPA and is subject to any interpretations of that term by the Department of Housing and Urban Development. Although a few commenters raised serious problems regarding the use of RESPA terminology in this regard, the Board believes that the clear meaning of the act, in the light of congressional intent, mandates a parallel approach. The commentary will more fully explain the relationship between the use of "application" in RESPA and its use in this section.

The December proposal also solicited comment on whether an application that is rejected or withdrawn within three days requires early disclosures under this section. The commenters overwhelmingly agreed that such disclosures would be unnecessary, and the Board reaffirms its earlier position that this type of application requires no early disclosure.

As in the December proposal, the tolerance contained in paragraph (b), which governs whether new disclosures must be made at consummation or settlement, reflects the tolerance contained in § 226.22(a). The general tolerance is 1/8 of 1 percentage point above or below the annual percentage rate originally disclosed, but irregular transactions, as defined in § 226.22, will be measured against a 1/4 of 1 percentage point tolerance.

The redisclosure requirements set forth in paragraph (b) are unchanged from the December proposal, except for editorial revisions that do not affect the substance of the paragraph. Only the changed terms, rather than a complete set of new disclosures, need be disclosed in the event that the annual percentage rate falls outside of the tolerance. Many commenters asserted that this provision would considerably alleviate the burden of redisclosure. Other commenters, however, claimed that furnishing a complete set of new disclosures would be easier than providing only the changed terms. Recognizing that due to operating procedures, redisclosure of all the credit terms may be less burdensome for certain creditors, the Board wishes to clarify that creditors have the option of giving either a complete set of new disclosures or only the changed terms.

Paragraph (b) has been altered from the December proposal to permit settlement, as an alternative to consummation, as an optional time for redisclosure. This option to redisclosing at consummation is provided in the act, and the majority of commenters regarded the option as worthwhile. Because Congress intended this provision to reduce duplication of disclosure when possible, "settlement," as used in this section, follows the RESPA definition. "Consummation" is defined in § 226.2 of Regulation Z.

Section G(4) in Appendix G of the December proposal, which contained the model form for combining the good faith estimates of settlement costs under RESPA and the itemization of the amount financed under Truth in Lending, has been deleted. Since the legislative history indicates that furnishing the good faith estimates under RESPA would satisfy the itemization requirement under Truth in Lending, the Board believes that the model form for combining these disclosures is unnecessary. Instead, disclosure of the itemization of the amount financed will be satisfied by the good faith estimates under RESPA, as noted above in the discussion of § 226.18(c).

In the December proposal, comment was solicited on whether special types of mortgage transactions, which have become increasingly common, warrant specific treatment in the regulation. Those mentioned were "wrap-around" mortgages, "shared equity" or "shared appreciation" mortgages, and mortgages with a demand feature. "Wrap-around" mortgages and mortgages with a demand feature have been addressed in the Federal Register material on § 226.17(c), which relates to the basis of disclosures. The Federal Register notice accompanying § 226.18(f) deals with the ***20882** disclosure of "shared appreciation" mortgages as variable rate transactions. All of these mortgages will also be discussed in greater detail in the commentary.

Comment was also solicited in the December proposal on another alternative mortgage issue. The Board expressed concern about the overlapping coverage of these mortgages by different regulations. That issue is now addressed in § 226.18(f) and discussed in the Federal Register material accompanying that provision. In some instances, compliance with disclosure requirements contained in other regulations will constitute compliance with the variable rate provisions of Regulation Z.

§ 226.20 Subsequent disclosure requirements.

(a) Refinancings. This paragraph requires new Truth in Lending disclosures when an existing obligation is satisfied and replaced by a new obligation. This definition substantially changes the concept of refinancing reflected in § 226.8(j) of the current regulation, which generally treats any change in terms as a new transaction requiring new disclosures. Paragraph (a) is similar to its counterpart in the December proposal, with the addition of five exceptions to the new definition.

The revised definition of refinancing most closely resembles the events intended to be covered by refinancing disclosures. The Board's primary concern in originally creating the concept of refinancing, which is not required by statute, was to address the practice of "flipping," in which an obligation involving precomputed finance charges is prepaid and replaced with a new obligation. This practice may permit lenders to obtain a higher yield, by application of favorable rebate methods to calculate unearned finance charges on the original obligation. New disclosures at this time may provide consumers with useful information regarding the cost of refinancing under these circumstances. The new standard also provides a simpler and more precise rule for determining when a new transaction occurs, in contrast to the current definition in § 226.8(j). Particularly since the new definition is more in accord with the definition of refinancing used in the credit industry, creditors should be able to readily determine whether new disclosures are required when an event occurs after consummation of the original transaction.

The new definition is revised from the December proposal to exempt from refinancing five events which the Board believes should not require new disclosures. Depending on the way in which these occurrences are structured, they may not in all cases constitute refinancings under the new definition, even without a specific exception in the regulation. The exceptions in § 226.20(a) simply insure that these events will not under any circumstances require new disclosures. Most of the exceptions, such as renewals of single-payment obligations and reductions in annual percentage rates, have been exempt from disclosure under the current regulation. In other cases, the Board believes that an exception is appropriate because the event is not one for which the consumer is likely to make a new credit decision, as for example, an agreement resulting from a judicial proceeding.

Paragraph (a)(1) exempts from disclosure a renewal of a single-payment obligation on terms essentially similar to the terms of the original obligation, so long as Truth in Lending disclosures were given on the earlier obligation. In an abbreviated form, it incorporates existing Board Interpretation § 226.811.

Paragraph (a)(2) requires no further disclosures when the new obligation involves a reduction in the annual percentage rate, with no change in terms beyond the payment schedule revisions necessary to reflect the reduction. It is substantially similar to current Board Interpretation § 226.817.

Paragraph (a)(3) exempts from refinancing disclosures agreements that arise from a judicial proceeding. This would include formal workout agreements and reaffirmations of debts discharged in bankruptcy, so long as the agreements involve a court proceeding.

Paragraph (a)(4) excludes informal workout agreements or similar arrangements between a creditor and consumer resulting from the consumer's default or delinquency, including changes relating to restructuring of the payment schedule or the additional collateralization of the transaction. However, this paragraph would not exempt such agreements from redisclosure if the change in terms includes an increase in the annual percentage rate or the advance of additional credit beyond amounts already accrued plus insurance premiums.

Paragraph (a)(5), which is based on current Board Interpretation § 226.814, exempts from redisclosure the renewal of optional insurance added to an existing credit transaction. Under this paragraph, the creditor need not make new disclosures relating to the insurance financing at the time of renewal of the insurance coverage. The increase in the existing obligation itself would not constitute a refinancing requiring new disclosures since that obligation is not extinguished. As under the present regulation, however, the initial purchase of the insurance must be accompanied by the appropriate Truth in Lending disclosures.

(b) Assumptions. This paragraph defines an assumption to include only those transactions in which a creditor expressly agrees in writing to accept a subsequent consumer as a primary obligor on an existing residential mortgage transaction. If the assumption meets the definition set forth in the first sentence of paragraph (b), the creditor must provide new disclosures to the assuming consumer.

Paragraph (b), which has no statutory counterpart, is based on § 226.8(k) and Board Interpretation § 226.807 of the current regulation. It differs from the current regulation in that it is limited to residential mortgage transactions, and from the December proposal in that it incorporates a portion of Board Interpretation § 226.807. This special rule permits creditors in transactions involving add-on or discount finance charges to make abbreviated disclosures of certain credit terms. In simple interest transactions, a complete set of new disclosures, based on the remaining obligation, must be provided before the assumption occurs. This is in accord with the current regulation.

The scope of the revised provision, other than its limitation to residential mortgage transactions, is very similar to the current regulatory provision. In order to incur disclosure responsibilities, the creditor must specifically agree to accept a subsequent party as a primary obligor in the transaction. Mere approval of creditworthiness or receipt of notification of a change in records does not constitute an assumption, although the retention of the original consumer as an obligor does not by itself preclude the transaction from being an assumption.

The acceptance by the creditor of a subsequent obligor may be accompanied by a change in terms in the obligation. The imposition of new terms does not by itself exclude a transaction from the assumption definition, so long as the criteria set forth including the continuation of an "existing residential mortgage transaction," are met. Any such changes in credit terms must be reflected in the disclosures given to the assuming consumer.

***20883** *§ 226.21 Treatment of credit balances.*

Section 226.21, which establishes the requirements for the treatment of credit balances, has no counterpart in the closed-end credit provisions of the current regulation. It implements § 165 of the act, the scope of which was broadened to apply to any type of credit account, not merely open-end accounts.

The act provides that a credit balance in excess of one dollar created by transmittal of funds in excess of the total balance due on the account, rebates of unearned finance charges or insurance premiums, or amounts otherwise owed to or held for the benefit of an obligor must be either credited to the consumer's account or refunded upon the consumer's request. The corresponding provision in the regulation mirrors the act, except that, in accordance with the open-end credit provision, it has been revised to clarify that a creditor may require the consumer's request to be in writing.

With respect to closed-end credit, the Board believes that these requirements will be applicable to such situations as the full payment of a loan by transmittal of funds in excess of the total balance due on the account, and the early payoff of a loan entitling the debtor to a rebate of insurance premiums and finance charges. The statutory language regarding "total balance due" refers to repayment of the total outstanding balance. Thus, this provision applies only where payments and credits exceed the total balance owed and not where the customer has simply paid an amount in excess of the installment payment due for a certain period.

The act requires a creditor to make a good faith effort to refund to the consumer by cash, check or money order any part of the credit balance remaining in the account for more than six months. Paragraph (c) of the regulation has been revised since the December proposal to permit a creditor to refund by crediting a deposit account of the consumer held with the creditor in lieu of refunding by cash, check or money order. For example, where a consumer maintains both a checking (or savings) account and an installment loan account with the same creditor, and a credit is created in the installment account by transmittal of funds in excess of the total balance owed, a creditor may refund the excess by crediting it to the consumer's checking (or savings) account.

When any part of a credit balance remains in a consumer's account for more than six months, the act and the regulation require the creditor to make a good faith effort to refund it to the consumer. A creditor may, however, without a request from the consumer, make the refund before the expiration of six months. When the creditor does not know the consumer's current location, the Board contemplates that the minimum tracing requirement will include use of the consumer's last known address and telephone number. A creditor is not required to trace the consumer when the amount of the credit balance is less than one dollar. If the consumer cannot be traced, the disposition of the money remaining in the account after six months is a matter of state or other applicable law. If the consumer cannot be traced through the last known address or telephone number, that law--and not Regulation Z--determines whether the creditor may treat the balance as income or make other disposition of it.

Section 226.21 does not override contractual arrangements between the creditor and consumer regarding entitlement to rebates of unearned finance charges and insurance premiums. With respect to such rebates, this section applies only in those situations where the borrower has not contracted away his or her entitlement to rebates of unearned finance charges and/or insurance premiums in the event of prepayment.

This section is not intended to limit a creditor's right of set-off under state law nor to override a creditor's contractual arrangement with a debtor. For example, if the collateral securing an account is repossessed and sold as a result of a debtor's default, a creditor is permitted to use any surplus from the sale to offset a deficieny in any other account that was also secured by the collateral sold, so long as such offset is permitted by state law or contractually agreed to by the parties. Likewise, if a creditor accelerates a loan as a result of default and obtains a rebate of insurance premiums, the creditor may use the rebate to offset the outstanding, unpaid loan balance.

§ 226.22 Determination of annual percentage rate.

The general rule for determining the annual percentage rate remains similar to the December proposal but contains two significant revisions from § 226.5 of the current regulation. These revisions concern the tolerance for irregular transactions and the special protection for faulty calculation tools.

Section 107(c) of the act authorizes the Board to provide a tolerance greater than 1/8 of 1 percentage point in transactions involving irregular payments. The December proposal included a 1/4 of 1 percentage point tolerance for irregular transactions, defined as those involving multiple advances, irregular payments or irregular payment amounts. In view of the potential difficulty of calculating an annual percentage rate in complex transactions and congressional recognition of this fact, the Board continues to believe that the wider tolerance is appropriate. Therefore, § 226.22(a)(3) provides a tolerance of 1/4 of 1 percentage point for irregular transactions. However, the definition of an irregular transaction has been revised from the December proposal to exclude transactions whose only irregularity is an odd first or final payment or an odd first period. The Board believes that a greater tolerance for these transactions is unnecessary since these payment schedule variations do not unduly complicate annual percentage rate calculations.

The payment schedule irregularities provision, formerly the minor irregularities provision under § 226.5(b)(5) of the current regulation and § 226.22(e) of the December proposal, has been deleted from § 226.22 and incorporated in § 226.17(c)(4). No substantive change is intended by this revision. As discussed more fully in § 226.17, the same minor irregularities rule as before continues to apply to annual percentage rate calculations, but is now extended to all calculations under the regulation.

Annual percentage rates computed using this rule are not afforded the 1/4 of 1 percentage point tolerance for irregular transactions, unless the transaction includes an irregularity other than an odd first period or odd first or last payment.

Supplement I, which contains the explanations, equations and technical instructions for calculating the actuarial annual percentage rate, has been redesignated as Appendix J, and is set forth below. As indicated in the discussion of the appendices, several minor revisions have been made to this material.

Section 226.5(c) of the current regulation insulates creditors from liability for errors resulting from good faith use of faulty calculation tools. In light of the expanded defense for such erors in § 130, the civil liability section of the act, the Board belives that this regulatory provision will no longer be necessary under the revised act. Therefore, after April 1, 1982, this provision will be eliminated from the regulation. Until that time, the special rule is incorporated into footnote 45a, formerly § 226.22(f) in the December proposal.

***20884** *§ 226.23 Right of rescission.*

(a) Consumer's right to rescind. Paragraph (a) implements § 125(a) of the act and represents a substantial change from the general rule in § 226.9(a) of the current regulation. It provides the right to rescind a transaction secured by a consumer's principal dwelling.

The scope of this provision has been modified in two ways. Unlike the original regulation, the revised regulation applies not only to real property used as the consumer's principal dwelling, but to personal property as well. Moreover, unlike the current regulation, the revised regulation no longer applies to property "expected to be used" as the consumer's principal dwelling but is limited to property used as the consumer's principal dwelling at the time the security interest is retained.

As was the case in the original regulation, a security interest need not be retained at consummation to give rise to the right of rescission. For example, materialmen's or mechanic's liens arising by operation of law may not arise until performance has begun. The right of rescission is still applicable in such transactions, even when the security interest has not yet been created.

To give rise to the right of rescission, the security interest must be retained as part of the credit transaction. Therefore, a materialmen's lien obtained by a contractor who is not a party to the credit transaction, but merely receives the proceeds of the consumer's unsecured bank loan, does not create a rescindable transaction between either the bank and the customer or the contractor and the customer. In that case, the security interest is not a term of the credit transaction but merely obtained by an unrelated third party. Nevertheless, a security interest acquired by a contractor who is a creditor in the transaction gives rise to the right to rescind, because the security interest is retained in connection with the credit extension. The same result occurs when a materialmen's lien is retained by a subcontractor of a creditor-contractor, even when the latter has waived its rights under the law. In the Board's view, the subcontractor is acting as an agent of the creditor-contractor in such cases, and the security interest therefore forms part of the credit transaction. This position incorporates Board

Interpretation § 226.901.

Under paragraph (a)(1), a consumer has the right to rescind only if the transaction involves the consumer's principal dwelling and the consumer's ownership interest in that dwelling is or will be subject to a security interest. A number of commenters contended that the language in the December proposal could be interpreted to provide the right to rescind to a nonresident co-owner of a dwelling. To avoid such interpretations, the definition of "consumer" in § 226.2 has been expanded to clarify that, for purposes of rescission, a consumer is any natural person who is both an owner and a resident of a dwelling that is or will be subject to a security interest as part of the credit transaction. The definition therefore encompasses persons who are not parties to the credit agreement but who have signed the security agreement. As a signatory to the security agreement, that person is a party to the credit transaction and is obligated to the extent that his or her ownership interest is encumbered by the creditor's security interest. Accordingly, joint owners in this situation must be given the right of rescission, so long as the property represents the joint owners' principal dwelling.

The footnote to paragraph (a)(1) provides that the addition of a security interest to a preexisting obligation is rescindable. The right of rescission applies only to the added security interest, however, and not to the original obligation. In such situations only the paragraph (b) notice need be delivered, not new material disclosures.

Paragraph (a)(2), which corresponds to § 226.9(a) of the current regulation, describes how the right of rescission may be exercised. It further provides that the consumer's notification that the transaction has been rescinded is considered given to the creditor when mailed or filed for telegraphic transmission. However, the 20-day limit for performing the obligations in paragraph (d)(2) does not begin to run until the creditor receives the notice.

Paragraph (a)(3) requires that consumers be given three business days to rescind the transaction. This three-day period runs from the last of three events: consummation, delivery of the rescission notice required by paragraph (b) and delivery of the "material disclosures" as defined in the footnote to the paragraph. The definition of "business day" as applied to rescission differs from the December proposal. The definition in footnote 14 to § 226.9 of the current regulation has been retained and is incorporated in § 226.2 of the revised regulation.

The last portion of paragraph (a)(3) provides for termination of an unexpired right of rescission three years from consummation, upon transfer of all of the consumer's interest in the property, or upon sale of the property, whichever is first. This provision differs from both the original regulation and the December proposal in that a third event, sale of the property, has been added. A sale of the property would include a transaction in which the consumer sells the dwelling, and takes back legal title through a purchase money note and mortgage. Transfer of all the consumer's interest includes such transfers as bequests and gifts. Neither a sale of the property nor a transfer of all of the consumer's interest need be voluntary. Accordingly, a foreclosure sale would terminate an unexpired right to rescind.

Paragraph (a)(4) reflects the rule in § 226.9(f)(1) of the original regulation. It provides that rescission by any one consumer entitled to rescind is effective as to all consumers involved in the transaction.

(b) Notice of the right to rescind. Paragraph (b) is for the most part similar to § 226.9(b), its counterpart in the current regulation. Creditors are required to deliver two copies of the notice of the right to rescind to each consumer entitled to rescind, and that notice must be on a separate document that identifies the transaction. Identification of the transaction may be made by simply giving the date of the transaction. Unlike the current regulation, however, the revised regulation prescribes no specific text or format for the notice. Instead, to give creditors greater flexibility, only five required disclosures other than the identification of the transaction have been specified. The notices in Appendix H provide models for creditors to use in complying with these requirements. The creditor may provide a separate form that the consumer may use to exercise the right of rescission, or that form may be combined with the other rescission disclosures, as is done in the appendix.

(c) Delay of creditor's performance. Paragraph (c) is substantially similar to § 226.9(c) of the current regulation and has no statutory counterpart. It prohibits disbursement of money (other than into escrow), performance of services, and delivery of materials until the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded.

(d) Effects of rescission. Paragraph (d) is based on § 226.9(d) of the current regulation and reflects amended § 125(b) of the act. It describes the effects of rescission and outlines the obligations of both the creditor and consumer, once the consumer has rescinded. Paragraph (d)(1) provides that the security interest giving rise to the rescission right becomes void when the consumer exercises that right. Upon rescission, the ***20885** consumer is not liable for any amount, including any finance charge. The term "any amount" includes any money or property given by the consumer to the creditor or a third party in connection with the credit transaction. It includes charges such as application and commitment fees or fees for a title search or appraisal, whether paid to the creditor, paid directly to a third party or passed on from the creditor to the third party. The fact that these amounts may not represent profit to the creditor but rather were used by the creditor to purchase services is irrevelant in determining whether the consumer is liable for them. However, the Board emphasizes that the term "any amount" does not apply to any money or property given by the creditor to the consumer. Similarly, creditors need not return any money given by the consumer to third parties outside of the credit transaction.

Although the original regulation and the amended statute use the language "any finance or other charge," the term "any amount" merely incorporates the staff's longstanding interpretation of that language. Furthermore, although undefined in the revised regulation, the term "other charge" in the current regulation has become a term of art which does not include all the fees which must be returned by the creditor. Use of the same term to define different amounts would be confusing.

Paragraph (d)(2) also reflects the statutory amendment expanding from 10 to 20 days the time period within which the creditor must return a consumer's money or property and take the necessary action to terminate the security interest. Further, to reflect the staff's longstanding interpretation of this provision, the term "calendar days" is used to describe the time period.

Paragraph (d)(3) provides that the consumer may retain possession of any money or property received from the creditor until the creditor has performed under paragraph (d)(2). Once the creditor has met its obligations, the consumer must tender the money or property to the creditor. If the tender of property would be impracticable, the consumer may pay its reasonable value. Property may be tendered at the location of the property or at the consumer's residence, but money must be tendered at the creditor's place of business. This provision has been specifically incorporated into the text of the regulation.

Paragraph (d)(3) also provides that if a creditor does not take possession of the money or property within 20 calendar days after the consumer's tender, the consumer may keep it without further obligation. The 20-day limit in this paragraph also reflects the statutory change. The Board emphasizes that the 20-day period does not begin until the consumer tenders the property.

Paragraph (d)(4) reflects amended § 125(b) of the act and provides that the procedures outlined in paragraphs (d)(2) and (d)(3) may be modified by a court.

(e) Consumer's waiver of right to rescind. Paragraph (e) prescribes how and when a consumer may waive the right to rescind. It differs from its counterpart in the current regulation but mirrors the standard used in § 125(d) of the act. There no longer need be an emergency which endangers persons or property. The consumer need only determine that the extension of credit is necessary to meet a bona fide personal financial emergency.

Some commenters were concerned that the relaxed standard would result in abuse of the waiver provisions. The Board emphasizes that waiver or modification of the rescission right should not become a pro forma matter, but should occur only in rare circumstances. Although several commenters urged that a waiver automatically insulate a creditor from liability for failing to provide the rescission right, the Board believes that such protection is unwarranted. Accordingly, before accepting a waiver, creditors must assure themselves that the reasons given for the waiver are both substantial and credible and that the waiver is in all respects bona fide. This requirement, combined with the continued prohibition against the use of preprinted forms, will prevent abusive practices, while at the same time permit consumers to waive the rescission right in appropriate circumstances. The Board wishes to further emphasize that under § 226.25 of the revised regulation creditors are required to retain evidence of compliance for a period of two years. This includes rescission waivers.

Paragraph (e) also retains the rule in § 226.9(f)(2) of the current regulation, which requires that the waiver be signed by all consumers entitled to rescind.

(f) Exempt transactions. Paragraph (f) is based on amended § 125(e) of the act and is significantly revised from § 226.9(g) of the current regulation.

Paragraph (f)(1) exempts from the right of rescission a residential mortgage transaction, as that term is defined in § 226.2. This exception is based on current § 226.9(g)(1), relating to first lien purchase money transactions, but differs in two material respects. First, property need not be classified as real property under state law in order for the exception to apply. Second, the lien status of the mortgage is irrelevant for purposes of the exemption; the fact that the mortgage has junior lien status does not by itself preclude application of § 226.23(f)(1). As in the current regulation, however, the exception applies to loans to finance the construction as well as the acquisition of a principal dwelling.

A question arises under paragraph (f)(1) as to whether a loan to acquire an existing dwelling and to make improvements to that dwelling is exempt. In the Board's judgment, even though a portion of the proceeds is used for purposes other than acquisition or initial construction, the entire transaction may be viewed as a residential mortgage transaction and therefore exempt from the right of rescission. This assumes, however, that the loan for acquisition and improvement is in fact treated as one transaction. If the loan for the acquisition of the dwelling and the subsequent advances for the improvements are treated as more than one transaction, then only the transaction financing the acquisition of the dwelling is exempt.

Paragraph (f)(2) incorporates the current position taken in Board Interpretation § 226.903 concerning the right of rescission in refinancings. The exemption applies only to new advances from the same creditor and only if the new amount financed does not exceed the unpaid principal balance plus any finance charge; however, the right of rescission does apply to refinancings by a different creditor and to that part of a refinancing by the same creditor that is in excess of the existing debt.

Paragraph (f)(3) exempts those transactions in which state agencies are creditors. It corresponds to § 226.9(g)(5) of the current regulation and is based on § 125(e)(1)(C) of the revised statute.

Paragraph (f)(4) corresponds to § 226.17(c)(6) of the revised regulation. Just as new disclosures need not be made for subsequent advances when treated as one transaction, no new rescission rights arise so long as the appropriate notice and disclosures are given at the outset. However, if the advances are treated as separate transactions, the right to rescind applies to each advance.

A number of commenters requested that a counterpart to current Board Interpretation § 226.814 be added as an exemption from the right of rescission. Paragraph (f)(5) exempts from rescission the renewal of optional insurance premiums added to an existing transaction. Disclosures, as well as any applicable right of rescission, must continue to be provided for the original purchase of the insurance.

***20886** The rule in current § 226.9(g)(4) concerning agricultural loans has been omitted pursuant to the statute. Furthermore, since exemptions from the right of rescission no longer depend on the priority status of the lien, the exemption in current § 226.9(g)(3) concerning a subsequent subordination of a security interest also has been deleted.

§ 226.24 Advertising.

Section 226.24 contains rules for advertising closed-end consumer credit and corresponds to § 226.10 (a), (b) and (d) of the current regulation. It is substantially similar to its counterpart in the December proposal.

(a) Actually available terms. This paragraph is based on § 226.10(a)(1) of the current regulation, which provides that no advertisement shall state that a specific amount of credit or installment amount can be arranged unless the creditor usually and customarily arranges or will arrange such terms. This paragraph permits advertisements to state only those terms that the creditor is actually prepared to offer. It is not intended to inhibit the promotion of new credit programs, but to prohibit advertisement of terms which the creditor does not actually intend to offer. For example, a creditor may not advertise a very low annual percentage rate that will not in fact be available at any time, but may advertise a rate that will be offered for only a limited period.

(b) Advertisement of rate of finance charge. Paragraph (b) requires that advertised rates be stated in terms of an annual percentage rate. It corresponds to § 226.10(d)(1) of the current regulation.

Unlike the current regulation, this paragraph requires a reference to any variable rate feature. As in § 226.18(f), relating to disclosure of a variable rate, the rate increase disclosure requirement in this paragraph does not apply to any rate increase due to delinquency (including late payment), default, acceleration, assumption, or transfer of collateral.

(c) Advertisement of terms that require additional disclosures. This paragraph corresponds to § 226.10(d)(2) of the current regulation. Paragraph (c)(1) sets forth the credit terms which, if used in an advertisement, require disclosure of the credit terms listed in paragraph (c)(2).

This provision differs from paragraph (d)(2) of the current regulation in that the list of terms that require additional disclosures has been streamlined to correspond with the list of terms mandated by the statute. "No downpayment" and "no charge for credit" have been eliminated as terms that would require additional disclosures under the new regulation since the statute specifies only that a statement of the downpayment "if any" is a triggering term.

Similarly, the additional disclosures in paragraph (c)(2) that must be made if a specified term appears in an advertisement have been reduced to only those disclosures mandated by the statute.

Paragraph (c)(2)(ii) requires disclosure of the "terms of repayment," as provided in the statute, instead of "number, amounts and timing of repayment," as required under the current regulation. This change is designed to provide greater flexibility to creditors in making this disclosure. Repayment terms may be expressed in a variety of ways in addition to the exact repayment schedule. For example, a creditor may use a unit-cost approach in making the required disclosure, e.g., "48 monthly payments of $27.83 per $1,000 borrowed." As another example, in an advertisement for credit secured by a dwelling, when any series of payments varies because of a graduated payment feature or because of the inclusion of mortgage insurance premiums, a creditor may comply with paragraph (c)(2)(ii) of this section by stating the number and timing of payments, the amounts of the largest and smallest of those payments, and the fact that other payments will vary between those amounts. This example reflects Board Interpretation § 226.808 of the current regulation and § 226.18(g) of the revised regulation.

The footnote to this paragraph reflects Board Interpretation § 226.1001, which deals with the advertisement of credit terms when all credit sales or loans are not made on the same basis. The advertisement of credit terms may be made by giving one or more examples of typical extensions of credit and stating all of the terms applicable to each example. The examples must be labelled as such and must reflect representative credit terms that are made available by the creditor to present and prospective customers.

(d) Catalogs and multiple-page advertisements. Paragraph (d), which contains special advertising rules for catalogs, brochures and similar material, corresponds to § 226.10(b) of the current regulation. It incorporates the requirement in current Board Interpretation § 226.1002 that the tables or schedules of terms in catalogs include all amounts up to the level of the more commonly sold higher priced property or services. In the Board's view, the remaining portion of that interpretation, regarding the method of computing disclosures and the $1,000 limit on the examples, is unnecessary and its inclusion would be contrary to the concept of simplification.

Subpart D--Miscellaneous

§ 226.25 Record retention.

The general rule is set forth in paragraph (a) that creditors must retain evidence of compliance for two years from the date disclosures are required to be made or action is required to be taken. Neither the December proposal nor the corresponding provision in the current regulation, § 226.6(i), stated when the two-year period begins when certain action, instead of disclosures, is required. Language has been added in the revised regulation to cover these situations.

The language in the December proposal that creditors may retain "information sufficient to reconstruct the required disclosures" has been deleted from the revised regulation, but it will be included in the commentary. Although some commenters expressed concern about this language, the Board does not intent this provision to require more information to be retained than under § 226.6(i) of the current regulation. It permits a creditor to keep only the information it needs to reconstruct the disclosures given, rather than requiring retention of the actual disclosures given.

Although the explanatory material in the December proposal stated that advertising is not covered by the record retention provisions, the proposed regulation itself did not reflect this fact. Language has been included in the revision to make clear that advertising requirements under §§ 226.16 and 226.24 are not covered by the record retention rules. This continues the position in § 226.6(i)(1) of the current regulation.

Paragraph (b) of the December proposal provided examples of recordkeeping methods that could be used to retain evidence of compliance. This paragraph has been deleted from the revised regulation as inappropriate regulatory material. These examples will be incorporated in the commentary.

The revised regulation does not contain the special record retention rule in § 226.6(i)(2) of the current regulation for creditors subject to the five federal agencies participating in the Regulation Z Enforcement Guidelines. In its place, paragraph (a) provides that enforcement agencies may require creditors under their jurisdiction to retain records for a period longer than two years if necessary to carry out enforcement responsibilities under § 108 of the act.

***20887** *§ 226.26 Use of annual percentage rate in oral disclosures.*

This section corresponds to a new § 146 in the act, and is based on Board Interpretation § 226.101 to the current regulation. Additional provisions have been added to the December proposal to modify the requirements for transactions where the creditor cannot determine in advance the annual percentage rate. This type of modification is specifically permitted by § 146.

In the open-end credit area, the exception will allow creditors to furnish the corresponding annual percentage rate and other information about the plan, such as transaction fees and minimum charges. In closed-end credit inquiries, the creditor may state an annual percentage rate for a standard, sample transaction, as well as more specific additional information about the particular transaction asked about by the consumer. This special rule should be particularly helpful to creditors responding to inquiries about mortgage credit. They may respond in terms of the annual percentage rate in a standard example, while also providing, for instance, information on the consumer's specific case in terms of interest rate and points.

Section 226.10(f) of the current regulation has been dropped, since it implemented the original § 146, now repealed.

§ 226.27 Spanish language disclosures.

This section is unchanged from the December proposal, except for minor editorial changes to improve its readability. It continues the requirements of § 226.6(a) of the current regulation.

§ 226.28 Effect on state laws.

This section sets forth the standards for the preemption of state law. In order to be preempted, a state law must be inconsistent with the act and the implementing provisions of the regulation. A state law is preempted to the extent of the inconsistency.

Paragraph (a)(1) deals with state laws that cover the types of requirements contained in chapter 1 (General provisions), chapter 2 (Credit transactions), and chapter 3 (Credit advertising) of the act and the implementing provisions of the regulation. The general standard here is that a state law is inconsistent if it requires disclosures or actions that contradict the requirements of the federal law. A state law that requires creditors to use the same term as the federal law where the state-required term represents a different amount or has a different meaning than the federal law is inconsistent. For example, if a state law requires use of the term "finance charge," but defines the term to include certain fees that the federal law excludes, or to exclude fees the federal law includes, such a law is preempted. A state law is also inconsistent if it mandates the use of a term that is different from a federal term, but describes the same item as the federal term. For example, if a state law requires a label such as "nominal annual interest rate" for the federal "annual percentage rate," the state law would be preempted.

Although the language "contradicts" is not the same as that used in § 226.6(b)(1) of the current regulation or in § 226.31(a)(1) of the December proposal, the Board believes it properly implements congressional intent with regard to preemption. The language lends a greater degree of certainty to the preemption standard, and better illustrates the guidelines that the Board will use in making preemption determinations. The Board believes that an assessment of whether state law contradicts federal law will result in the preemption of state laws requiring disclosures that would interfere with the intent of the federal scheme of disclosures, while leaving in place those state laws that do not interfere with the federal scheme.

Paragraph (a)(1) also sets forth who may request a Board determination on inconsistency under chapters 1, 2, and 3. These include a creditor, a state, or any other interested party, although the Board may also make determinations on its own motion without a request. Furthermore, the provision specifies that after the Board has made a determination of inconsistency with respect to a specific state law, the state law requirement that the Board has identified as specifically preempted must not be followed by a creditor in making disclosures. This provision implements the prohibition contained in amended § 111(a) of the act. The Board intends to provide sufficient time to permit creditors to make whatever revisions of forms or procedures that may be necessary to conform to the individual determinations on contradictory state disclosures.

A creditor may apply the preemption standards to state law and choose not to give state-required disclosures that it concludes are inconsistent with the federal law in advance of specific Board determinations. However, the absolute prohibition against giving the state disclosures does not apply until the Board makes its determination. Therefore, a creditor may choose to give state disclosures until the Board determines that the state law is inconsistent. This option for giving state disclosures is intended to relieve any uncertainty that a creditor might have prior to Board determinations of inconsistency.

Paragraph (a)(2) sets forth the preemption rules for the fair credit billing laws. The rules are substantively unchanged from § 226.6(b)(2) of the current regulation, although some of the language and the organization have been changed to make it more understandable. Paragraph (a)(2)(iii) continues the position of the current regulation that allows only states to request a Board determination under the fair credit billing laws.

The fair credit billing provisions in the December proposal restated the statutory language that a state law furnishing greater protection to the consumer than federal law is not inconsistent. The revised provisions return to the standards in the current regulation because they seem clearer and more precise.

Paragraph (b) covering equivalent disclosure requirements implements amended § 111(a)(2) and is substantively unchanged from § 226.31(b) of the December proposal. If a state-required disclosure is determined by the Board to be substantially the same in meaning as a federal disclosure, the state disclosure may be made in place of the federal disclosure. This provision does not apply to requirements relating to the finance charge or annual percentage rate. A creditor, state, or other interested party may make a request to the Board for an equivalency determination.

Paragraph (c) refers to Appendix A, which contains the procedures to be used in requesting a Board determination on preemption.

§ 226.29 State exemptions.

This section corresponds to § 226.12 of the current regulation. The substance of this section was contained in Appendix A of the December proposal. The material on exemptions has been rearranged to parallel the material covering the effect on state laws. This section sets forth the standards for exemptions and Appendix B contains the procedures for applying for and granting of an exemption. The reference in the December proposal to a list of the exemptions granted has been eliminated since there are no exemptions yet under the revised regulation.

***20888** Paragraph (a) sets forth the standards for exemption determinations and paragraph (b) states the fact that exemptions will not extend to the civil liability provisions of the act. They are the same as those in § 226.12(a) of the current regulation and Appendix A of the December proposal. The "substantially similar" standard is interpreted as requiring state provisions to be generally the same as the federal provisions, including provisions for reimbursement to consumers equivalent to those called for in amended § 108 of the act.

As mentioned in the notice accompanying the December proposal, the five existing exemptions under the original statute and regulation will be automatically revoked on April 1, 1982, when the new statute and regulation replace the old. The exemptions will continue fully effective until that time. The five exempt states will have one year to amend their statutes and regulations, apply for new exemptions, and receive determinations from the Board.

Appendix A--Effect on State Laws

This appendix sets forth the procedures to be followed in requesting Board determinations of whether a state law is inconsistent with or is substantially the same as federal law. The procedures were adapted from § 226.31(c) of the December proposal and from Supplement V of the current regulation (§ 226.70). The detailed explanations of the procedures have been very much streamlined, but the appendix provides the basic rules for filing requests, public comment (either upon request or upon the Board's own motion), and notification of determinations.

A delayed effective date for preemption determinations provided in § 226.31(c)(4) of the December proposal has been deleted. The Board intends, however, to provide sufficient time for creditors to revise their forms and procedures to comply with determinations.

Appendix B--State Exemptions

Appendix B sets forth the procedures for granting exemptions to states. These procedures were contained in Supplements II (Credit transactions), IV (Credit card issuance and liability), V (Credit billing), and VI (Consumer leasing) to the current regulation. The appendix represents a combination and streamlining of the procedures set forth in Supplements II, IV, and V, in order to provide uniform procedures for exemptions from chapters 2 and 4 of the act. The supplement covering procedures for consumer leasing exemptions has been separately incorporated into the new Regulation M on consumer leasing. Appendix A of the December proposal has been replaced by revised § 226.29, which sets out the exemption standards, and by this appendix, which sets out the exemption procedures.

The revisions to the appendix are designed to establish precise, simple rules that will be easy to understand and use, and to clarify those items of information that the Board deems essential for consideration of exemption applications.

The detailed material on criteria for determinations included in the supplements to the current regulation is not found in revised Appendix B. This deletion has been made to simplify the regulation, but with no intent to change the substance of the provisions. For example, as under the current regulation, the classes of transactions eligible for exemptions will continue to be only broad classes, and will not include narrow categories of credit transactions. Much of the other detail in the current supplements has been deleted, since these provisions are implicit in the requirement that an applicant submit a comparison of state and federal provisions and a statement of reasons for its claim that an exemption should be granted.

An important point should be emphasized about restitution. The amended act contains a new § 108(e) requiring creditors to reimburse consumers in certain cases involving understated annual percentage rates and finance charges. The Board believes that a state must adopt restitution provisions that are at least equivalent to those called for by the act. In addition, to assist the Board in determining the adequacy of enforcement, the supporting documentation to the application should contain material on examination procedures, practices and policies relating to enforcement of the regulation, including examination manuals, and instructions to examiners and training materials issued to the examiners. The application should also contain a thorough discussion of how creditors will be required to reimburse consumers for certain violations involving understated annual percentage rates and finance charges.

A delayed effective date for exemptions provided in Appendix B of the December proposal has been deleted. The Board intends, however, to provide sufficient time for creditors to revise their forms and procedures to comply with the laws of states receiving an exemption.

Appendix C--Issuance of Staff Interpretations

This appendix is based on Appendix B of the December proposal. The substance of Section I of the December proposal, covering general information on official staff interpretations, is contained in the revised appendix, with one addition. Language has been added to explain that a commentary to the regulation will be used as the primary vehicle for issuing official staff interpretations of the regulation. In most situations, official staff interpretations will not be issued separately but, instead, will be incorporated in this commentary. The Board believes that because the commentary will be amended periodically and on a regular basis, it represents the most practical method of providing guidance to creditors on how to comply with the regulation.

Language from Section II of the December proposal discussing the procedures for issuance of interpretations has been deleted as unnecessary regulatory material. Such procedures would have very limited applicability, since periodic updates of the commentary will be the regular vehicle for issuing interpretations.

Appendix D--Multiple Advance Construction Loans

Appendix D remains substantially unchanged from the December proposal except for a revision of the rule in Part II. B. for computing the first payment period and the resulting change to the APR computations. The appendix incorporates the substance of current Board Interpretation § 226.813, which provides a special procedure that creditors may use at their option in calculating and disclosing the terms of multiple-advance transactions when the amounts and timing of advances may be unknown at consummation of the transaction. In a revised format, this appendix utilizes a similar mathematical basis as the interpretation, but has been redrafted for greater clarity. The format reflects the approach taken in § 226.17(c)(6) which permits creditors to provide separate or combined disclosures for the construction period and the permanent financing, if any.

The appendix is limited specifically to construction loans. Currently, all multiple-advance transactions may take advantage of Board Interpretation § 226.813. In view of the fact that its assumptions, formulas, and examples are based only on the typical construction loan, the Board believes that its use for other types of ***20889** transactions, where such assumptions may not be valid, is inappropriate. Therefore, the Board limits this appendix to those multiple-advance construction loans which are either payable in a single sum at the close of the construction period or converted to permanent financing by the same creditor at that time.

Appendix E--Rules for Card Issuers That Bill on a Transaction-by-Transaction Basis

Appendix E incorporates current Board Interpretation § 226.709 and deals with the application of some of the provisions of open-end credit to card issuers that bill consumers on a transaction-by-transaction basis. Except for minor editorial changes, the appendix is unchanged from the December proposal and the current Board Interpretation.

Appendix F--Annual Percentage Rate Computations for Certain Open-End Credit Plans

Appendix F corresponds to Appendix E of the December proposal and incorporates footnote 5(a) to § 226.5(a)(3)(ii) of the current regulation. It deals with the annual percentage rate computation for open-end credit plans in which both a periodic rate and a transaction charge are applied during the same billing cycle. In addition to the examples that appear in the current regulation, the appendix incorporates a sixth example in which the transaction amount exceeds the amount of the balance subject to the periodic rate. Except for editorial changes and the additional example, the appendix is the same as the previous proposals and the current regulation.

Appendices G and H (Open-End and Closed-End Model Forms and Clauses)

General

Appendices G and H contain model forms and clauses for open-end plans and closed-end credit transactions. They are being issued pursuant to amended § 105(b) of the act which requires the Board to publish model forms for common transactions. In response to many of the commenters, the Board is providing a greater variety of models than were in the December proposal. Samples are also included which illustrate ways creditors may revise the closed-end models for use in various kinds of transactions.

As provided in § 105(b) of the act, use of the model forms is not required, but creditors using them properly will be deemed to be in compliance with the regulation. Creditors may make certain types of changes to the forms without losing the protection provided in the statute. For example, creditors may rearrange the format by using a vertical, rather than a horizontal, format, or by relocating the required descriptors. For instance, the descriptors may be placed outside the boxes containing the corresponding disclosures or may be grouped together as a glossary of terms in a separate section of the segregated disclosures. As § 105(b) of the act provides, however, the rearrangement of the models may not be so extensive as to affect the substance, clarity, or meaningful sequence of the forms. Any revisions with that effect would deprive creditors of the protection from civil liability afforded by the act.

In addition to changing the format, creditors would still satisfy the substantially similar standard where they delete from the model forms disclosures that are inapplicable to a transaction or a plan. Examples of ways to delete inapplicable information include crossing out, whiting out, filling in "N/A" (not applicable), checking a box for applicable disclosures, or circling applicable disclosures. Moreover, the "substantially similar" standard would not necessarily prohibit creditors from altering the forms or clauses to incorporate state "plain English" requirements.

Appendix G

Appendix G contains model disclosure notices and clauses for open-end transactions and corresponds to Appendix F in the December proposal. Four areas are covered by these models: (1) balance computation methods, G-1; (2) liability for unauthorized use, G-2; (3) billing error rights, G-3 and G-4; and (4) right to rescind, G-5 through G-9.

Model G-1 corresponds to § F(1) of the December proposal and contains four model disclosures for different balance computation methods. These disclosures may be used either in the initial disclosures under § 226.6 or the periodic disclosures under § 226.7. Several changes have been made in the disclosures to make them easier to read and understand and to state more precisely the balance computation methods. As is clear from the models given, the Board does not believe that "short-hand" descriptions of the balance computation methods are sufficient for purposes of the act and regulation.

It is expected that creditors will include the phrase "a portion of" the finance charge where the total finance charge includes other amounts, such as transaction charges, that are not due to the application of a periodic rate. In addition, where unpaid finance charges are subtracted in the balance calculation, that fact must be stated so that the disclosure of the computation method is accurate.

Model G-1(a) corresponds to § F(1)(a) of the December proposal and deals with the adjusted balance method. With the exception of minor editorial changes, it is the same as the December proposal.

Model G-1(b) corresponds to § F(1)(b) of the December proposal and deals with the previous balance method. The model has been changed and now refers to the balance owed at the beginning of the billing cycle; it also states that payments and credits received during the billing cycle are not subtracted. The last sentence of the model, which appears in brackets, reflects the total dollar amount of payments and credits received during the billing cycle. This disclosure is required on the periodic statement by § 127(b)(7) of the act and § 226.7(e) of the revised regulation. None of the other models contain this language because all assume that payments and credits received during the billing cycle are subtracted. If this is not the case, however, the language relating to payments and credits would have to be changed, and the disclosure of the dollar amount would have to be added.

Models G-1(c) and (d) correspond to § F(1) (c) and (d) of the December proposal and describe the average daily balance method excluding current transactions and the average daily balance method including current transactions, respectively. The models have been rewritten in an effort to state the computation methods more clearly and simply.

Models G-2 corresponds to § F(4) of the December proposal. It is the model for the notice of liability for unauthorized use of a credit card that is required under § 226.12(b)(2). The model is unchanged from the December proposal.

Models G-3 and G-4 correspond to §§ F(2) and F(3) of the December proposal and set out models for the long form billing error rights statement and the alternative billing error rights statement, respectively. With the exception of some minor editorial changes, the model notices are the same as those in the December proposal. As always, the model notices may be modified by deleting inapplicable information. For instance, if the creditor does not have the ability to automatically debit a consumer's savings or checking account for payment, it may delete the paragraph relating to stopping such a debit as it relates to a disputed amount. Also, if the ***20890** limitations on the rights stated in the special rule for credit card purchases are not applicable to a creditor, the limitations may be deleted. If the limitations are inapplicable for other reasons that are stated in revised § 226.12(c)(3), the notice may be modified accordingly. These notices also contain optional language and phrases that creditors may use. For example, if the creditor requires that notice of a billing error be submitted on something other than the payment ticket or other material accompanying the periodic disclosures, the notice must contain a statement to that effect. Also, the creditor may choose either to insert its address in the notice or to refer to the address that appears elsewhere on the bill.

Models G-5, G-6, and G-7 correspond to §§ F(6), F(5), and F(7) of the December proposal and set out notices of the right to rescind at the opening of an account, at the time of each transaction, and upon an increase in the credit limit, respectively. Models G-8 and G-9 are new. They have been added in response to commenters' requests to address situations where the right to rescind arises because the security on an account has either been added or increased. All of the notices of the right to rescind have been reorganized, and their language has been simplified further. The last paragraph of each of the rescission model forms contains a date by which the consumer's notice of cancellation must be sent or delivered. That date is three business days after the date of the event triggering the rescission right given in (1). A parenthetical has been added to the paragraph to address the situation in which the consumer's right to rescind the transaction exists beyond three business days following the date of the transaction, for example, where the notice or material disclosures are delivered late or where the date given in (1) is an estimate. The language of the parenthetical is not optional; without it, the date given in the paragraph may be misleading.

Appendix H

Appendix H contains model disclosure forms and clauses for closed-end credit transactions, as well as several samples of completed forms. Some changes have been made to the forms contained in §§ G(1) and G(2) of the December proposal in order to improve their clarity and readability. In models H-1 and H-2, for example, dotted lines are not utilized to indicate disclosures that are not required in all transactions. Instead, it is left to creditors to delete any of the disclosure items in the models that are not applicable to a given transaction.

Another change is that checkboxes rather than brackets have been used for alternative disclosures. Several commenters suggested this revision which will enable creditors simply to check the appropriate alternative for the prepayment and security interest disclosures, and consumers to check the appropriate box for the itemization of the amount financed option. Of course, in some cases creditors must fill in a blank (for example, a brief description of other property subject to a security interest) in addition to checking the correct box. Creditors are not required to use the checkbox approach.

Certain disclosures have been relocated in order to provide a more logical presentation. The filing fee information now appears directly below the security interest information, and the late charge disclosure directly above the prepayment disclosure. This rearrangement groups together related items. Finally, the symbol for estimated disclosures has been clarified to apply to any type of estimate, not just dollar amount estimates, as in the December proposal.

All of the models in Appendix H are written in the second person, instead of the first person, as was the case in Appendix G of the December proposal. However, disclosures requiring consumers to elect an option (for example, regarding the itemization of the amount financed and the credit insurance option) remain in the first person. The change was made in response to several commenters' concern that the use of the second person in the federal disclosure statement would make the disclosures more understandable to consumers, especially when other documents are written in the second person. Creditors, however, are not required to design their disclosure forms in the second person.

A few of the items included in §§ G(1) and G(2) of the December proposal have been eliminated. In models H-1 and H-2, the name of the creditor and the acknowledgment of receipt have both been deleted since the regulation does not require them to appear with the federal disclosures. The assumption disclosure has also been deleted because it applies only to residential mortgage transactions. This disclosure has been included as a model clause in H-6 and may be inserted into the disclosure form when applicable, as may the model clauses in H-4, H-5, and H-7 for variable rate obligations, demand obligations, and required deposits, respectively.

The credit life insurance disclosures in models H-1 and H-2 have been amended somewhat from the December proposal to reflect the fact that credit disability insurance may be offered separately by some creditors.

A few changes have been made to § G(3) of the December proposal, which corresponds to model H-3. This model is now entitled the itemization of the amount financed, rather than an explanation, to parallel the statutory language. The blank space for the total dollar figure representing the amounts paid to others has been deleted since the total amount is not a required disclosure.

As with the other model forms, appropriate revisions may be made to the amount financed itemization. For example, the items may be rearranged if creditors wish to present them in a mathematical progression. Also, additional categories may be included. In credit sales, for example, the amount given directly to the consumer may be shown as the result of the cash price minus the downpayment. Another type of additional information which may be included is the identification of individual government officials who receive various fees. As the model shows, the regulation permits creditors simply to label this category as fees paid to public officials without individually identifying the officials, but creditors may wish to show more detail.

Section G(4) in the December proposal, which combined the itemization of the amount financed with the good faith estimates required under the Real Estate Settlement Procedures Act (RESPA), has been deleted. The Board has taken this action in light of the legislative history indicating that the furnishing of good faith estimates under RESPA would satisfy Truth in Lending's requirement for an itemization of the amount financed. This change is in line with the Congress' general intent to simplify disclosures by eliminating duplicative information.

The model clauses in for variable rate transactions, contained in § G(6) of the December proposal, have been expanded in model H-4 by the addition of clauses illustrating the required hypothetical example. Creditors may refer either to the incremental change in rate or payment amount, or may refer to the resulting rate or payment amount. The Board intends that creditors have flexibility in constructing an appropriate example.

The model clauses for demand obligations set out in model H-5 are unchanged from § G(7) of the December proposal.

***20891** Two new model clauses have been added. Model H-6 contains the assumption clause which is required for residential mortgage transactions. This clause was deleted from the basic model forms because it is required only in a limited number of transactions. The revised disclosure refers to the fact that assumptions may be "subject to conditions," since this is so commonly the case in mortgage transactions. Model H-7 sets out the clause that must be included in disclosure statements for transactions involving required deposits. Sample H-11 includes this clause.

Some editorial changes have been made to the model rescission notice, which was set out in § G(5) of the December proposal. The format of models H-8 and H-9 has been conformed to the open-end rescission models contained in revised Appendix G, with the models divided into two sections entitled "Your Right to Cancel" and "How to Cancel." The "date of the transaction," listed as the first event triggering the right of rescission, means the date of consummation of the transaction as defined in § 226.2 of the regulation.

An additional rescission notice, model H-9, has been provided for a refinancing to which the right of rescission attaches. The Board agreed with commenters who suggested that a form showing the effects of rescission in a refinancing would be useful.

Appendix H also contains samples which illustrate how creditors may adapt the models for use in various kinds of specific transactions. The samples demonstrate the kinds of adjustments, rearrangements, additions, and deletions that a creditor may make to the forms and still be deemed to be in compliance with the regulation (assuming, of course, that the amounts of the disclosures are accurate and that the general clear and conspicuous standard is observed). For example, the Truth in Lending statement may include the following types of additional information: the creditor's address (Sample H-11); the consumer's name (Samples H-10, H-11, H-13 through H-15), address (Samples H-11, H-13 through H-15), and account number (Samples H-11, H-13 through H-15); the date of the transaction (Samples H-12 and H-13); and an acknowledgment of receipt (Sample H-10).

The samples also demonstrate various methods creditors may use to delete disclosures that are inapplicable to certain transactions. Examples of items that creditors may delete in appropriate cases include the following: the itemization of the amount financed option (Samples H-12 through H-15); the credit life and disability insurance disclosure (Samples H-11 and H-12); the property insurance disclosure (Samples H-10 through H-12, and H-14); the "filing fees" and "non-filing insurance" disclosure (Samples H-11 and H-12); the prepayment penalty and rebate (Samples H-12 and H-14); and the captions for disclosure items such as property insurance and demand feature (Sample H-13).

Another type of revision that creditors may make to the model forms applies to the late charge disclosure. If a creditor has a set policy regarding late charges (either a dollar amount or a percentage of the payment), the inapplicable portion may be deleted, or "N/A" or "0" may be put in the appropriate blank (Samples H-10, H-13, and H-14). If a creditor charges the lesser of two types of late charges, the necessary revisions may be made to reflect this fact (Samples H-11 and H-12).

Sample H-10 illustrates an automobile credit sale. The cash price is $7,500 with a downpayment of $1,500. there is an 8% add-on interest rate. The term is 3 years, with 36 equal monthly payments. The credit life insurance premium and the filing fees are financed by the creditor. There is a $25 credit report fee paid by the consumer before consummation.

Sample H-11 illustrates an installment loan. The amount of the loan is $5,000. There is a 12% simple interest rate. The term is 2 years. The date of the transaction is expected to be April 15, 1981, with the first payment due June 1, 1981. The odd days' interest is collected with the first payment. The remaining 23 monthly payments are equal.

Sample H-12 illustrates a refinancing. The amount of the loan is $5,000. There is a 15% simple interest rate. The term is 3 years. The date of the transaction is April 1, 1981, with the first payment due on May 1, 1981. The first 35 monthly payments are equal, with a varying final payment due on April 1, 1984. The credit disability insurance premium is financed.

Samples H-13 through H-15 illustrate various mortgage transactions. It has been assumed that these mortgages are subject to the Real Estate Settlement Procedures Act (RESPA). As a result, no option regarding the itemization of the amount financed has been included in the samples, because providing the good faith estimates of settlement costs required by RESPA satisfies Truth in Lending's amount financed itemization requirement.

Sample H-13 illustrates a mortgage with a demand feature. The loan amount is $44,900, payable in 360 monthly installments at a simple interest rate of 14.75%. The interim interest ($294.34) is collected as a prepaid finance charge at the time of consummation of the loan (April 15, 1981). The property insurance premiums are not included in the payment schedule. The demand feature disclosure is applicable to the seven-year call option required by the Federal National Mortgage Association (FNMA) in states where due-on-sale clauses are prohibited.

Sample H-14 illustrates a variable rate mortgage. The loan amount is $44,900 payable in 360 monthly installments at an initial interest rate of 14.75%. All periods are regular. Two points have been imposed and included in the prepaid finance charge. The note provides that the interest rate may vary with the lender's prime rate, with the maximum permissible increase over the term of the mortgage being 5%. The interest rate may not vary more frequently than once a year, and may not increase by more than 1% annually. The rate fluctuations will be reflected in the monthly payment amount.

Sample H-15 illustrates a graduated payment mortgage. The loan amount is $44,900, payable in 360 monthly installments at a simple interest rate of 14.75%. Two points, as well as an initial mortgage guarantee insurance premium of $225.00, are included in the prepaid finance charge. The mortgage guarantee insurance premiums are calculated on the basis of 1/4 of 1% of the outstanding principal balance under an annual reduction plan. The abbreviated disclosure permitted under § 226.18(g)(2) is used for the payment amount in years 6 through 30.

Appendix I--Federal Enforcement Agencies

This appendix is unchanged from Appendix I in the December proposal.

Appendix J--Annual Percentage Rate Computations for Closed-End Credit Transactions

Appendix J contains the rules and equations for calculating the annual percentage rate in closed-end credit transactions. It incorporates Supplement I of the current regulation with the exception of the two minor revisions discussed below.

A minor technical revision has been made to paragraph (b)(2) to make clear that the "term of the transaction" never begins any earlier than the date of consummation.

Another revision to current Supplement I concerns the treatment of single advance/single payment transactions. Some commenters expressed concern about Supplement I's two alternative rules (§ 226.40(b)(5) (vi) ***20892** and (vii)) for determining the number of unit-periods per year to be used in calculating the annual percentage rate. In a transaction with a term equal to a whole number of months, paragraph (vi) must be used, while paragraph (vii) must be applied to all other transactions. These two rules may produce different annual percentage rates for two transactions that are identical save for the starting date. A consumer may be quoted different rates for the same transaction by different creditors merely because the starting dates differ. The Board believes that requiring these paragraphs to be mutually exclusive may impede consumers' ability to compare credit sources and may unnecessarily disrupt normal creditor practices.

Therefore, Appendix J revises the rule in paragraph (b)(5)(vi) to Supplement I by permitting creditors, in all cases where the transaction term equals a whole number of months, to use either the 12-month method or the 365-day method to compute the number of unit periods per year.

(3) Text of amendments. In consideration of the foregoing and pursuant to the authority granted in § 105 of the Truth in Lending Act as amended by Sec. 605, Pub. L. 96-221, 94 Stat. 170 (15 U.S.C. 1604), the Board amends Regulation Z (12 CFR Part 226) as follows:

1. Effective April 1, 1982, all sections of Regulation Z in effect on March 31, 1981, are removed; all material accompanying Regulation Z in effect on March 31, 1981 (including appendices, interpretations, official staff interpretations, and supplements), is also removed effective April 1, 1982.

2. Effective April 1, 1981, Regulation Z Part 226 is revised as follows:

PART 226--TRUTH IN LENDING

Subpart A--General

226.1 Authority, purpose, coverage, organization, enforcement and liability.

226.2 Definitions and rules of construction.

226.3 Exempt transactions.

226.4 Finance charge.

Subpart B--Open-End Credit

226.5 General disclosure requirements.

226.6 Initial disclosure statement.

226.7 Periodic statement.

226.8 Identification of transactions.

226.9 Subsequent disclosure requirements.

226.10 Prompt crediting of payments.

226.11 Treatment of credit balances.

226.12 Special credit card provisions.

226.13 Billing error resolution.

226.14 Determination of annual percentage rate.

226.15 Right of rescission.

226.16 Advertising.

Subpart C--Closed-End Credit

226.17 General disclosure requirements.

226.18 Content of disclosures.

226.19 Certain residential mortgage transactions.

226.20 Subsequent disclosure requirements.

226.21 Treatment of credit balances.

226.22 Determination of annual percentage rate.

226.23 Right of rescission.

226.24 Advertising.

Subpart D--Miscellaneous

226.25 Record retention.

226.26 Use of annual percentage rate in oral disclosures.

226.27 Spanish language disclosures.

226.28 Effect on state laws.

226.29 State exemptions.

Appendix A--Effect on state laws.

Appendix B--State exemptions.

Appendix C--Issuance of staff interpretations.

Appendix D--Multiple advance construction loans.

Appendix E--Rules for card issuers that bill on a transaction-by-transaction basis.

Appendix F--Annual percentage rate computations for certain open-end credit plans.

Appendix G--Open-end model forms and clauses.

Appendix H--Closed-end model forms and clauses.

Appendix I--Federal enforcement agencies.

Appendix J--Annual percentage rate computations for closed-end credit transactions.

Authority: Sec. 105 of the Truth in Lending Act as amended by section 605, Pub. L. 96-221, 94 Stat. 170 (15 U.S.C. 1604 et seq.).

Subpart A--General

12 CFR § 226.1

§ 226.1 Authority, purpose, coverage, organization, enforcement and liability.

(a) Authority. This regulation, known as Regulation Z, is issued by the Board of Governors of the Federal Reserve System to implement the federal Truth in Lending and Fair Credit Billing Acts, which are contained in Title I of the Consumer Credit Protection Act, as amended (15 U.S.C. 1601 et seq.).

(b) Purpose. The purpose of this regulation is to promote the informed use of consumer credit by requiring disclosures about its terms and cost. The regulation also gives consumers the right to cancel certain credit transactions that involve a lien on a consumer's principal dwelling, regulates certain credit card practices, and provides a means for fair and timely resolution of credit billing disputes. The regulation does not govern charges for consumer credit.

(c) Coverage. (1) In general, this regulation applies to each individual or business that offers or extends credit when four conditions are met: (i) the credit is offered or extended to consumers; (ii) the offering or extension of credit is done regularly; [FN1] (iii) the credit is subject to a finance charge or is payable by a written agreement in more than 4 installments; and (iv) the credit is primarily for personal, family, or household purposes.

FN1 The meaning of "regularly" is explained in the definition of "creditor" in § 226.2(a).

(c)(2) If a credit card is involved, however, certain provisions apply even if the credit is not subject to a finance charge, or is not payable by a written agreement in more than 4 installments, or if the credit card is to be used for business purposes.

(d) Organization. The regulation is divided into subparts and appendices as follows:

(d)(1) Subpart A contains general information. It sets forth: (i) the authority, purpose, coverage, and organization of the regulation; (ii) the definitions of basic terms; (iii) the transactions that are exempt from coverage; and (iv) the method of determining the finance charge.

(d)(2) Subpart B contains the rules for open-end credit. It requires that initial disclosures and periodic statements be provided. It also describes special rules that apply to credit card transactions, treatment of payments and credit balances, procedures for resolving credit billing errors, annual percentage rate calculations, rescission requirements, and advertising rules.

(d)(3) Subpart C relates to closed-end credit. It contains rules on disclosures, treatment of credit balances, annual percentage rate calculations, rescission requirements, and advertising.

(d)(4) Subpart D contains rules on oral disclosures, Spanish language disclosure in Puerto Rico, record retention, effect on state laws, and state exemptions.

(d)(5) There are several appendices containing information such as the procedures for determinations about state laws, state exemptions and issuance of staff interpretations, special rules for certain kinds of credit plans, a list of enforcement agencies, and the rules for computing annual percentage rates in closed-end credit transactions.

(e) Enforcement and liability. Section 108 of the act contains the administrative enforcement provisions. Sections 112, 113, 130, 131, and 134 contain provisions relating to liability for failure to comply with the requirements of the act and the regulation.

12 CFR § 226.2

***20893** § 226.2 Definitions and rules of construction.

(a) Definitions. For purposes of this regulation, the following definitions apply:

(a)(1) "Act" means the Truth in Lending Act (15 U.S.C. 1601 et seq.).

(a)(2) "Advertisement" means a commercial message in any medium that promotes, directly or indirectly, a credit transaction.

(a)(3) "Arranger of credit" means a person who regularly arranges for the extension of consumer credit [FN2] by another person if:

FN2 A person regularly arranges for the extension of consumer credit only if it arranged credit more than 25 times (or more than 5 times for transactions secured by a dwelling) in the preceding calendar year. If a person did not meet these numerical standards in the preceding calendar year, the numerical standards shall be applied to the current calendar year.

(a)(3)(i) A finance charge may be imposed for that credit, or the credit is payable by written agreement in more than 4 installments (not including a downpayment); and

(a)(3)(ii) The person extending the credit is not a creditor.

(a)(4) "Billing cycle" or "cycle" means the interval between the days or dates of regular periodic statements. These intervals shall be equal and no longer than a quarter of a year. An interval will be considered equal if the number of days in the cycle does not vary more than 4 days from the regular day or date of the periodic statement.

(a)(5) "Board" means the Board of Governors of the Federal Reserve System.

(a)(6) "Business day" means a day on which a creditor's offices are open to the public for carrying on substantially all of its business functions. However, for purposes of rescission under §§ 226.15 and 226.23, the term means all calendar days except Sundays and the legal public holidays specified in 5 U.S.C. 6103(a), such as New Year's Day, Washington's Birthday, Memorial Day, Independence Day, Labor Day, Columbus Day, Veterans Day, Thanksgiving Day, and Christmas Day.

(a)(7) "Card issuer" means a person that issues a credit card or that person's agent with respect to the card.

(a)(8) "Cardholder" means a natural person to whom a credit card is issued for consumer credit purposes, or a natural person who has agreed with the card issuer to pay consumer credit obligations arising from the issuance of a credit card to another natural person. For purposes of § 226.12(a) and (b), the term includes any person to whom a credit card is issued for any purpose, including business, commercial, or agricultural use, or a person who has agreed with the card issuer to pay obligations arising from the issuance of such a credit card to another person.

(a)(9) "Cash price" means the price at which a creditor, in the ordinary course of business, offers to sell for cash the property or service that is the subject of the transaction. At the creditor's option, the term may include the price of accessories, services related to the sale, service contracts and taxes and fees for license, title, and registration. The term does not include any finance charge.

(a)(10) "Closed-end credit" means consumer credit other than "open-end credit" as defined in this section.

(a)(11) "Consumer" means a cardholder or a natural person to whom consumer credit is offered or extended. However, for purposes of rescission under §§ 226.15 and 226.23, the term also includes a natural person in whose principal dwelling a security interest is or will be retained or acquired, if that person's ownership interest in the dwelling is or will be subject to the security interest.

(a)(12) "Consumer credit" means credit offered or extended to a consumer primarily for personal, family, or household purposes.

(a)(13) "Consummation" means the time that a consumer becomes contractually obligated on a credit transaction.

(a)(14) "Credit" means the right to defer payment of debt or to incur debt and defer its payment.

(a)(15) "Credit card" means any card, plate, coupon book, or other single credit device that may be used from time to time to obtain credit.

(a)(16) "Credit sale" means a sale in which the seller is a creditor. The term includes a bailment or lease (unless terminable without penalty at any time by the consumer) under which the consumer:

(a)(16)(i) Agrees to pay as compensation for use a sum substantially equivalent to, or in excess of, the total value of the property and services involved; and

(a)(16)(ii) Will become (or has the option to become), for no additional consideration or for nominal consideration, the owner of the property upon compliance with the agreement.

(a)(17) "Creditor" means:

(a)(17)(i) A person (A) who regularly extends consumer credit [FN3] that is subject to a finance charge or is payable by written agreement in more than 4 installments (not including a downpayment), and (B) to whom the obligation is initially payable, either on the face of the note or contract, or by agreement when there is no note or contract.

FN3 A person regularly extends consumer credit only if it extended credit more than 25 times (or more than 5 times for transactions secured by a dwelling) in the preceding calendar year. If a person did not meet these numerical standards in the preceding calendar year, the numerical standards shall be applied to the current calendar year.

(a)(17)(ii) An arranger of credit.

(a)(17)(iii) For purposes of §§ 226.4(c)(8) (discounts), 226.9(d) (finance charge imposed at time of transaction), and 226.12(e) (Prompt notification of returns and crediting of refunds), a person that honors a credit card.

(a)(17)(iv) For purposes of Subpart B, any card issuer that extends either open-end credit or credit that is not subject to a finance charge and is not payable by written agreement in more than 4 installments.

(a)(17)(v) For purposes of Subpart B (except for the finance charge disclosures contained in §§ 226.6(a) and 226.7 (d) through (g) and the right of rescission set forth in § 226.15) and Subpart C, any card issuer that extends closed-end credit that is subject to a finance charge or is payable by written agreement in more than 4 installments.

(a)(18) "Downpayment" means an amount, including the value of any property used as a trade-in, paid to a seller to reduce the cash price of goods or services purchased in a credit sale transaction. A deferred portion of a downpayment may be treated as part of the downpayment if it is payable not later than the due date of the second otherwise regularly scheduled payment and is not subject to a finance charge.

(a)(19) "Dwelling" means a residential structure that contains 1 to 4 units, whether or not that structure is attached to real property. The term includes an individual condominium unit, cooperative unit, mobile home, and trailer, if it is used as a residence.

(a)(20) "Open-end credit" means consumer credit extended by a creditor under a plan in which:

(a)(20)(i) The creditor reasonably contemplates repeated transactions;

(a)(20)(ii) The creditor may impose a finance charge from time to time on an outstanding unpaid balance; and

(a)(20)(iii) The amount of credit that may be extended to the consumer during the term of the plan (up to any limit set by the creditor) is generally made available to the extent that any outstanding balance is repaid.

(a)(21) "Periodic rate" means a rate of finance charge that is or may be imposed by a creditor on a balance for a day, week, month, or other subdivision of a year.

(a)(22) "Person" means a natural person or an organization, including a corporation, partnership, proprietorship, ***20894** association, cooperative, estate, trust, or government unit.

(a)(23) "Prepaid finance charge" means any finance charge paid separately in cash or by check before or at consummation of a transaction, or withheld from the proceeds of the credit at any time.

(a)(24) "Residential mortgage transaction" means a transaction in which a mortgage, deed of trust, purchase money security interest arising under an installment sales contract, or equivalent consensual security interest is created or retained in the consumer's principal dwelling to finance the acquisition or initial construction of that dwelling.

(a)(25) "Security interest" means an interest in property that secures performance of a consumer credit obligation and that is recognized by state or federal law. It does not include incidental interests such as interests in proceeds, accessions, additions, fixtures, insurance proceeds (whether or not the creditor is a loss payee or beneficiary), premium rebates, or interests in after-acquired property. For purposes of disclosure under §§ 226.6 and 226.18, the term does not include an interest that arises solely by operation of law. However, for purposes of the right of rescission under §§ 226.15 and 226.23, the term does include interests that arise solely by operation of law.

(a)(26) "State" means any state, the District of Columbia, the Commonwealth of Puerto Rico, and any territory or possession of the United States.

(b) Rules of construction. For purposes of this regulation, the following rules of construction apply:

(b)(1) Where appropriate, the singular form of a word includes the plural form and plural includes singular.

(b)(2) Where the words "obligation" and "transaction" are used in this regulation, they refer to a consumer credit obligation or transaction, depending upon the context. Where the word "credit" is used in this regulation, it means "consumer credit" unless the context clearly indicates otherwise.

(b)(3) Unless defined in this regulation, the words used have the meanings given to them by state law or contract.

(b)(4) Footnotes have the same legal effect as the text of the regulation.

12 CFR § 226.3

§ 226.3 Exempt transactions.

This regulation does not apply to the following:

(a) Business, commercial, agricultural, or organizational credit. [FN4] (1) An extension of credit primarily for a business, commercial or agricultural purpose.

FN4 Extensions of credit that are exempt under paragraph (a)(1) and (2) remain subject to § 226.12(a) and (b) governing the issuance of credit cards and the liability for their unauthorized use.

(a)(2) An extension of credit to other than a natural person, including credit to government agencies or instrumentalities.

(b) Credit over $25,000 not secured by real property or a dwelling. An extension of credit not secured by real property, or by personal property used or expected to be used as the principal dwelling of the consumer, in which the amount financed exceeds $25,000 or in which there is an express written commitment to extend credit in excess of $25,000.

(c) Public utility credit. An extension of credit that involves public utility services provided through pipe, wire, other connected facilities, or radio or similar transmission (including extensions of such facilities), if the charges for service, delayed payment, or any discounts for prompt payment are filed with or regulated by any government unit. The financing of durable goods or home improvements by a public utility is not exempt.

(d) Securities or commodities accounts. Transactions in securities or commodities accounts in which credit is extended by a broker-dealer registered with the Securities and Exchange Commission or the Commodity Futures Trading Commission.

(e) Home fuel budget plans. An installment agreement for the purchase of home fuels in which no finance charge is imposed.

12 CFR § 226.4

§ 226.4 Finance charge.

(a) Definition. The finance charge is the cost of consumer credit as a dollar amount. It includes any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit. It does not include any charge of a type payable in a comparable cash transaction.

(b) Example of finance charge. The finance charge includes the following types of charges, except for charges specifically excluded by paragraphs (c) through (e) of this section:

(b)(1) Interest, time price differential, and any amount payable under an add-on or discount system of additional charges.

(b)(2) Service, transaction, activity, and carrying charges, including any charge imposed on a checking or other transaction account to the extent that the charge exceeds the charge for a similar account without a credit feature.

(b)(3) Points, loan fees, assumption fees, finder's fees, and similar charges.

(b)(4) Appraisal, investigation, and credit report fees.

(b)(5) Premiums or other charges for any guarantee or insurance protecting the creditor against the consumer's default or other credit loss.

(b)(6) Charges imposed on a creditor by another person for purchasing or accepting a consumer's obligation, if the consumer is required to pay the charges in cash, as an addition to the obligation, or as a deduction from the proceeds of the obligation.

(b)(7) Premiums or other charges for credit life, accident, health, or loss-of-income insurance, written in connection with a credit transaction.

(b)(8) Premiums or other charges for insurance against loss of or damage to property, or against liability arising out of the ownership or use of property, written in connection with a credit transaction.

(b)(9) Discounts for the purpose of inducing payment by a means other than the use of credit.

(c) Charges excluded from the finance charge. The following charges are not finance charges:

(c)(1) Application fees charged to all applicants for credit, whether or not credit is actually extended.

(c)(2) Charges for actual unanticipated late payment, for exceeding a credit limit, or for delinquency, default, or a similar occurrence.

(c)(3) Charges imposed by a financial institution for paying items that overdraw an account, unless the payment of such items and the imposition of the charge were previously agreed upon in writing.

(c)(4) Fees charged for participation in a credit plan, whether assessed on an annual or other periodic basis.

(c)(5) Seller's points.

(c)(6) Interest forfeited as a result of an interest reduction required by law on a time deposit used as security for an extension of credit.

(c)(7) The following fees in a transaction secured by real property or in a residential mortgage transaction, if the fees are bona fide and reasonable in amount:

(c)(7)(i) Fees for title examination, abstract of title, title insurance, property survey, and similar purposes.

(c)(7)(ii) Fees for preparing deeds, mortgages, and reconveyance, settlement, and similar documents.

(c)(7)(iii) Notary, appraisal, and credit report fees.

(c)(7)(iv) Amounts required to be paid into escrow or trustee accounts if the ***20895** amounts would not otherwise be included in the finance charge.

(c)(8) Discounts offered to induce payment for a purchase by cash, check, or other means, as provided in § 167(b) of the act.

(d) Insurance. (1) Premiums for credit life, accident, health, or loss-of-income insurance may be excluded from the finance charge if the following conditions are met:

(d)(i) The insurance coverage is not required by the creditor, and this fact is disclosed.

(d)(ii) The premium for the initial term of insurance coverage is disclosed. If the term of insurance is less than the term of the transaction, the term of insurance also shall be disclosed. The premium may be disclosed on a unit-cost basis only in open-end credit transactions, closed-end credit transactions by mail or telephone under § 226.17(g), and certain closed-end credit transactions involving an insurance plan that limits the total amount of indebtedness subject to coverage.

(d)(iii) The consumer signs or initials an affirmative written request for the insurance after receiving the disclosures specified in this paragraph. Any consumer in the transaction may sign or initial the request.

(d)(iii)(2) Premiums for insurance against loss of or damage to property, or against liability arising out of the ownership or use of property, [FN5] may be excluded from the finance charge if the following conditions are met:

FN5 This includes single interest insurance if the insurer waives all right of subrogation against the consumer.

(d)(iii)(2)(i) The insurance coverage may be obtained from a person of the consumer's choice, [FN6] and this fact is disclosed.

FN6 A creditor may reserve the right to refuse to accept, for reasonable cause, an insurer offered by the consumer.

(d)(iii)(2)(ii) If the coverage is obtained from or through the creditor, the premium for the initial term of insurance coverage shall be disclosed. If the term of insurance is less than the term of the transaction, the term of insurance shall also be disclosed. The premium may be disclosed on a unit-cost basis only in open-end credit transactions, closed-end credit transactions by mail or telephone under § 226.17(g), and certain closed-end credit transactions involving an insurance plan that limits the total amount of indebtedness subject to coverage.

(e) Certain security interest charges. If itemized and disclosed, the following charges may be excluded from the finance charge:

(e)(1) Taxes and fees prescribed by law that actually are or will be paid to public officials for determining the existence of or for perfecting, releasing, or satisfying a security interest.

(e)(2) The premium for insurance in lieu of perfecting a security interest to the extent that the premium does not exceed the fees described in paragraph (e)(1) of this section that otherwise would be payable.

(f) Prohibited offsets. Interest, dividends, or other income received or to be received by the consumer on deposits or investments shall not be deducted in computing the finance charge.

Subpart B--Open-End Credit

12 CFR § 226.5

§ 226.5 General disclosure requirements.

(a) Form of disclosures. (1) The creditor shall make the disclosures required by this subpart clearly and conspicuously in writing, [FN7] in a form that the consumer may keep. [FN8]

FN7 The disclosure required by § 226.9(d) when a finance charge is imposed at the time of a transaction need not be written.

FN8 The alternative summary billing rights statement provided for in § 226.9(a)(2), and the disclosures made under § 226.10(b) about payment requirements need not be in a form that the consumer can keep.

(a)(2) The terms "finance charge" and "annual percentage rate," when required to be disclosed with a corresponding amount or percentage rate, shall be more conspicuous than any other required disclosure. [FN9]

FN9 The terms need not be more conspicuous when used under § 226.7(d) on periodic statements and under § 226.16 in advertisements.

(b) Time of disclosures. (1) Initial disclosures. The creditor shall furnish the initial disclosure statement required by § 226.6 before the first transaction is made under the plan.

(b)(2) Periodic statements. (i) The creditor shall mail or deliver a periodic statement as required by § 226.7 for each billing cycle at the end of which an account has a debit or credit balance of more than $1 or on which a finance charge has been imposed. A periodic statement need not be sent for an account if the creditor deems it uncollectible, or if delinquency collection proceedings have been instituted, or if furnishing the statement would violate federal law.

(ii) The creditor shall mail or deliver the periodic statement at least 14 days prior to any date or the end of any time period required to be disclosed under § 226.7(j) in order for the consumer to avoid an additional finance or other charge. [FN10] A creditor that fails to meet this requirement shall not collect any finance or other charge imposed as a result of such failure.

FN10 This timing requirement does not apply if the creditor is unable to meet the requirement because of an act of God, war, civil disorder, natural disaster, or strike.

(c) Basis of disclosures and use of estimates. Disclosures shall reflect the terms of the legal obligation between the parties. If any information necessary for accurate disclosure is unknown to the creditor, it shall make the disclosure based on the best information reasonably available and shall state clearly that the disclosure is an estimate.

(d) Multiple creditors; multiple consumers. If the credit plan involves more than one creditor, only one set of disclosures shall be given, and the creditors shall agree among themselves which creditor must comply with the requirements that this regulation imposes on any or all of them. If there is more than one consumer, the disclosures may be made to any consumer who is primarily liable on the account. If the right of rescission under § 226.15 is applicable, however, the disclosures required by §§ 226.6 and 226.15(b) shall be made to each consumer having the right to rescind.

(e) Effect of subsequent events. If a disclosure becomes inaccurate because of an event that occurs after the creditor mails or delivers the disclosures, the resulting inaccuracy is not a violation of this regulation, although new disclosures may be required under § 226.9(c).

12 CFR § 226.6

§ 226.6 Initial disclosure statement.

The creditor shall disclose to the consumer, in terminology consistent with that to be used on the periodic statement, each of the following items, to the extent applicable:

(a) Finance charge. The circumstances under which a finance charge will be imposed and an explanation of how it will be determined, as follows:

(a)(1) A statement of when finance charges begin to accrue, including an explanation of whether or not any time period exists within which any credit extended may be repaid without incurring a finance charge. If such a time period is provided, a creditor may, at its option and without disclosure, impose no finance charge when payment is received after the time period's expiration.

(a)(2) A disclosure of each periodic rate that may be used to compute the finance charge, the range of balances to which it is applicable, [FN11] and the corresponding ***20896** annual percentage rate. [FN12] When different periodic rates apply to different types of transactions, the types of transactions to which the periodic rates apply shall also be disclosed.

FN11 A creditor is not required to adjust the range of balances disclosure to reflect the balance below which only a minimum charge applies.

FN12 If a creditor is offering a variable rate plan, the creditor shall also disclose: (1) the circumstances under which the rate(s) may increase; (2) any limitations on the increase; and (3) the effect(s) of an increase.

(a)(3) An explanation of the method used to determine the balance on which the finance charge may be computed.

(a)(4) An explanation of how the amount of any finance charge will be determined, [FN13] including a description of how any finance charge other than the periodic rate will be determined.

FN13 If no finance charge is imposed when the outstanding balance is less than a certain amount, no disclosure is required of that fact or of the balance below which no finance charge will be imposed.

(b) Other charges. The amount of any charge other than a finance charge that may be imposed as part of the plan, or an explanation of how the charge will be determined.

(c) Security interests. The fact that the creditor has or will acquire a security interest in the property purchased under the plan, or in other property identified by item or type.

(d) Statement of billing rights. A statement that outlines the consumer's rights and the creditor's responsibilities under §§ 226.12(c) and 226.13 and that is substantially similar to the statement found in Appendix G.

12 CFR § 226.7

§ 226.7 Periodic statement.

The creditor shall furnish the consumer with a periodic statement that discloses the following items, to the extent applicable:

(a) Previous balance. The account balance outstanding at the beginning of the billing cycle.

(b) Identification of transactions. An identification of each credit transaction in accordance with § 226.8.

(c) Credits. Any credit to the account during the billing cycle, including the amount and the date of crediting. The date need not be provided if a delay in crediting does not result in any finance or other charge.

(d) Periodic rates. Each periodic rate that may be used to compute the finance charge, the range of balances to which it is applicable, [FN14] and the corresponding annual percentage rate. [FN15] If different periodic rates apply to different types of transactions, the types of transactions to which the periodic rates apply shall also be disclosed.

FN14 See footnotes 11 and 13.

FN15 If a variable rate plan is involved, the creditor shall disclose the fact that the periodic rate(s) may vary.

(e) Balance on which finance charge computed. The amount of the balance to which a periodic rate was applied and an explanation of how that balance was determined. When a balance is determined without first deducting all credits and payments made during the billing cycle, that fact and the amount of the credits and payments shall be disclosed.

(f) Amount of finance charge. The amount of any finance charge debited or added to the account during the billing cycle, using the term "finance charge." The components of the finance charge shall be individually itemized and identified to show the amount(s) due to the appliction of any periodic rates and the amount(s) of any other type of finance charge. If there is more than one periodic rate, the amount of the finance charge attributable to each rate need not be separately itemized and identified.

(g) Annual percentage rate. When a finance charge is imposed during the billing cycle, the annual percentage rate(s) determined under § 226.14, using the term "annual percentage rate."

(h) Other charges. The amounts, itemized and identified by type, of any charges other than finance charges debited to the account during the billing cycle.

(i) Closing date of billing cycle; new balance. The closing date of the billing cycle and the account balance outstanding on that date.

(j) Free-ride period. The date by which or the time period within which the new balance or any protion of the new balance must be paid to avoid additional finance charges. If such a time period is provided, a creditor may, at its option and without disclosure, impose no finance charge when payment is received after the time period's expiration.

(k) Address for notice of billing errors. The address to be used for notice of billing errors. Alternatively, the address may be provided on the billing rights statement permitted by § 226.9(a)(2).

12 CFR § 226.8

§ 226.8 Identification of transactions.

The creditor shall identify credit transactions on or with the first periodic statement that reflects the transaction by furnishing the following information, as applicable. [FN16]

FN16 Failure to disclose the information required by this section shall not be deemed a failure to comply with the regulation if: (1) the creditor maintains procedures reasonably adapted to obtain and provide the information; and (2) the creditor treats an inquiry for clarification or documentation as a notice of a billing error, including correcting the account in accordance with § 226.13(e). This applies to transactions that take place outside a state, as defined in § 226.2(a), whether or not the creditor maintains procedures reasonably adapted to obtain the required information.

(a) Sale credit. For each credit transaction involving the sale of property or services, the following rules shall apply:

(a)(1) Copy of credit document provided. When an actual copy of the receipt or other credit document is provided with the first periodic statement reflecting the transaction, the transaction is sufficiently identified if the amount of the transaction and either the date of the transaction or the date of debiting the transaction to the consumer's account are disclosed on the copy or on the periodic statement.

(a)(2) Copy of credit document not provided--creditor and seller same or related person(s). When the creditor and the seller are the same person or related persons, and an actual copy of the receipt or other credit document is not provided with the periodic statement, the creditor shall disclose the amount and date of the transaction, and a brief identification [FN17] of the property or services purchased. [FN18]

FN17 As an alternative to the brief identification, the creditor may disclose a number or symbol that also appears on the receipt or other credit document given to the consumer, if the number or symbol reasonably identifies that transaction with that creditor, and if the creditor treats an inquiry for clarification or documentation as a notice of a billing error, including correcting the account in accordance with § 226.13(e).

FN18 An identification of property or services may be replaced by the seller's name and location of the transaction when: (1) the creditor and the seller are the same person; (2) the creditor's open-end plan has fewer than 15,000 accounts; (3) the creditor provides the consumer with point-of-sale documentation for that transaction; and (4) the creditor treats an inquiry for clarification or documentation as a notice of a billing error, including correcting the account in accordance with § 226.13(e).

(a)(3) Copy of credit document not provided--creditor and seller not same or related person(s). When the creditor and seller are not the same person or related persons, and an actual copy of the receipt or other credit document is not provided with the periodic statement; the creditor shall disclose the amount and date of the transaction; the seller's name; and the city, and state or foreign country where the transaction took place. [FN19]

FN19 The creditor may omit the address or provide any suitable designation that helps the consumer to identify the transaction when the transaction (1) took place at a location that is not fixed; (2) took place in the consumer's home; or (3) was a mail or telephone order.

(b) Nonsale credit. A nonsale credit transaction is sufficiently identified if the first periodic statement reflecting the transaction discloses a brief identification of the transaction; [FN20] the ***20897** amount of the transaction; and at least one of the following dates: the date of the transaction, the date of debiting the transaction to the consumer's account, or, if the consumer signed the credit document, the date appearing on the document. If an actual copy of the receipt or other credit document is provided and that copy shows the amount and at least one of the specified dates, the brief identification may be omitted.

FN20 See footnote 17.

12 CFR § 226.9

§ 226.9 Subsequent disclosure requirements.

(a) Furnishing statement of billing rights. (1) Annual statement. The creditor shall mail or deliver the billing rights statement required by § 226.6(d) at least once per calendar year, at intervals of not less than 6 months nor more than 18 months, either to all consumers or to each consumer entitled to receive a periodic statement under § 226.5(b)(2) for any one billing cycle.

(a)(2) Alternative summary statement. As an alternative to paragraph (a)(1) of this section, the creditor may mail or deliver, on or with each periodic statement, a statement substantially similar to that in Appendix G.

(b) Disclosures for supplemental credit devices and additional features. (1) If a creditor, within 30 days after mailing or delivering the initial disclosures under § 226.6(a), adds a credit feature to the consumer's account or mails or delivers to the consumer a credit device for which the finance charge terms are the same as those previously disclosed, no additional disclosures are necessary. After 30 days, if the creditor adds a credit feature or furnishes a credit device (other than as a renewal, resupply, or the original issuance of a credit card) on the same finance charge terms, the creditor shall disclose, before the consumer uses the feature or device for the first time, that it is for use in obtaining credit under the terms previously disclosed.

(b)(2) Whenever a credit feature is added or a credit device is mailed or delivered, and the finance charge terms for the feature or device differ from disclosures previously given, the disclosures required by § 226.6(a) that are applicable to the added feature or device shall be given before the consumer uses the feature or device for the first time.

(c) Change in terms. (1) Written notice required. Whenever any term required to be disclosed under § 226.6 is changed or the required minimum periodic payment is increased, the creditor shall mail or deliver written notice of the change to each consumer who may be affected. The notice shall be mailed or delivered at least 15 days prior to the effective date of the change. The 15- day timing requirement does not apply if the change has been agreed to by the consumer, or if a periodic rate or other finance charge is increased because of the consumer's delinquency or default; the notice shall be given, however, before the effective date of the change.

(c)(2) Notice not required. No notice under this section is required when the change involves late payment charges, charges for documentary evidence, or over-the-limit charges; a reduction of any component of a finance or other charge; suspension of future credit privileges or termination of an account or plan; or when the change results from an agreement involving a court proceeding, or from the consumer's default or delinquency (other than an increase in the periodic rate or other finance charge).

(d) Finance charge imposed at time of transaction. (1) Any person, other than the card issuer, who imposes a finance charge at the time of honoring a consumer's credit card, shall disclose the amount of that finance charge prior to its imposition.

(d)(2) The card issuer, if other than the person honoring the consumer's credit card, shall have no responsibility for the disclosure required by paragraph (d)(1) of this section, and shall not consider any such charge for purposes of §§ 226.6 and 226.7.

12 CFR § 226.10

§ 226.10 Prompt crediting of payments.

(a) General rule. A creditor shall credit a payment to the consumer's account as of the date of receipt, except when a delay in crediting does not result in a finance or other charge or except as provided in paragraph (b) of this section.

(b) Specific requirements for payments. If a creditor specifies, on or with the periodic statement, requirements for the consumer to follow in making payments, but accepts a payment that does not conform to the requirements, the creditor shall credit the payment within 5 days of receipt.

(c) Adjustment of account. If a creditor fails to credit a payment, as required by paragraphs (a) and (b) of this section, in time to avoid the imposition of finance or other charges, the creditor shall adjust the consumer's account so that the charges imposed are credited to the consumer's account during the next billing cycle.

12 CFR § 226.11

§ 226.11 Treatment of credit balances.

When a credit balance in excess of $1 is created on a credit account (through transmittal of funds to a creditor in excess of the total balance due on an account, through rebates of unearned finance charges or insurance premiums, or through amounts otherwise owed to or held for the benefit of a consumer), the creditor shall:

(a) Credit the amount of the credit balance to the consumer's account;

(b) Refund any part of the remaining credit balance within 7 business days from receipt of a written request from the consumer; and

(c) Make a good faith effort to refund to the consumer by cash, check, or money order, or credit to a deposit account of the consumer, any part of the credit balance remaining in the account for more than 6 months. No further action is required if the consumer's current location is not known to the creditor and cannot be traced through the consumer's last known address or telephone number.

12 CFR § 226.12

§ 226.12 Special credit card provisions.

(a) Issuance of credit cards. Regardless of the purpose for which a credit card is to be used, including business, commercial, or agricultural use, no credit card shall be issued to any person except:

(a)(1) In response to an oral or written request or application for the card; or

(a)(2) As a renewal of, or substitute for, an accepted credit card. [FN21]

FN21 For purposes of this section, "accepted credit card" means any credit card that a cardholder has requested or applied for and received, or has signed, used, or authorized another person to use to obtain credit. Any credit card issued as a renewal or substitute in accordance with this paragraph becomes an accepted credit card when received by the cardholder.

(b) Liability of cardholder for unauthorized use. (1) Limitation on amount. The liability of a cardholder for unauthorized use [FN22] of a credit card shall not exceed the lesser of $50 or the amount of money, property, labor, or services obtained by the unauthorized use before notification to the card issuer under paragraph (b)(3) of this section.

FN22 "Unauthorized use" means the use of a credit card by a person, other than the cardholder, who does not have actual, implied, or apparent authority for such use, and from which the cardholder receives no benefit.

(b)(2) Conditions of liability. A cardholder shall be liable for unauthorized use of a credit card only if:

(b)(2)(i) The credit card is an accepted credit card;

(b)(2)(ii) The card issuer has provided adequate notice [FN23] of the cardholder's maximum potential liability and of means by which the card issuer may be notified of loss or theft of the card. The ***20898** notice shall state that the cardholder's liability shall not exceed $50 (or any lesser amount) and that the cardholder may give oral or written notification, and shall describe a means of notification (for example, a telephone number, an address, or both); and

FN23 "Adequate notice" means a printed notice to a cardholder that sets forth clearly the pertinent facts so that the cardholder may reasonably be expected to have noticed it and understood its meaning. The notice may be given by any means reasonably assuring receipt by the cardholder.

(b)(2)(iii) The card issuer has provided a means to identify the cardholder on the account or the authorized user of the card.

(b)(3) Notification to card issuer. Notification to a card issuer is given when steps have been taken as may be reasonably required in the ordinary course of business to provide the card issuer with the pertinent information about the loss, theft, or possible unauthorized use of a credit card, regardless of whether any particular officer, employee, or agent of the card issuer does, in fact, receive the information. Notification may be given, at the option of the person giving it, in person, by telephone, or in writing. Notification in writing is considered given at the time of receipt or, whether or not received, at the expiration of the time ordinarily required for transmission, whichever is earlier.

(b)(4) Effect of other applicable law or agreement. If state law or an agreement between a cardholder and the card issuer imposes lesser liability than that provided in this paragraph, the lesser liability shall govern.

(b)(5) Business use of credit cards. If 10 or more credit cards are issued by one card issuer for use by the employees of an organization, this section does not prohibit the card issuer and the organization from agreeing to liability for unauthorized use without regard to this section. However, liability for unauthorized use may be imposed on an employee of the organization, by either the card issuer or the organization, only in accordance with this section.

(c) Right of cardholder to assert claims or defenses against card issuer. [FN24] (1) General rule. When a person who honors a credit card fails to resolve satisfactorily a dispute as to property or services purchased with the credit card in a consumer credit transaction, the cardholder may assert against the card issuer all claims (other than tort claims) and defenses arising out of the transaction and relating to the failure to resolve the dispute. The cardholder may withhold payment up to the amount of credit outstanding for the property or services that gave rise to the dispute and any finance or other charges imposed on that amount. [FN25]

FN24 This paragraph does not apply to the use of a check guarantee card or a debit card in connection with an overdraft credit plan, or to a check guarantee card used in connection with cash advance checks.

FN25 The amount of the claim or defense that the cardholder may assert shall not exceed the amount of credit outstanding for the disputed transaction at the time the cardholder first notifies the card issuer or the person honoring the credit card of the existence of the claim or defense. To determine the amount of credit outstanding for purposes of this section, payments and other credits shall be applied to: (1) late charges in the order of entry to the account; then to (2) finance charges in the order of entry to the account; and then to (3) any other debits in the order of entry to the account. If more than one item is included in a single extension of credit, credits are to be distributed pro rata according to prices and applicable taxes.

(c)(2) Adverse credit reports prohibited. If, in accordance with paragraph (c)(1) of this section, the cardholder withholds payment of the amount of credit outstanding for the disputed transaction, the card issuer shall not report that amount as delinquent until the dispute is settled or judgment is rendered.

(c)(3) Limitations. The rights stated in paragraphs (c)(1) and (2) of this section apply only if:

(c)(3)(i) The cardholder has made a good faith attempt to resolve the dispute with the person honoring the credit card; and

(c)(3)(ii) The amount of credit extended to obtain the property or services that result in the assertion of the claim or defense by the cardholder exceeds $50, and the disputed transaction occurred in the same state as the cardholder's current designated address or, if not within the same state, within 100 miles from that address. [FN26]

FN26 The limitations stated in paragraph (c)(3)(ii) of this section shall not apply when the person honoring the credit card: (1) is the same person as the card issuer; (2) is controlled by the card issuer directly or indirectly; (3) is under the direct or indirect control of a third person that also directly or indirectly controls the card issuer; (4) controls the card issuer directly or indirectly; (5) is a franchised dealer in the card issuer's products or services; or (6) has obtained the order for the disputed transaction through a mail solicitation made or participated in by the card issuer.

(d) Offsets by card issuer prohibited. (1) A card issuer may not take any action, either before or after termination of credit card privileges, to offset a cardholder's indebtedness arising from a consumer credit transaction under the relevant credit card plan against funds of the cardholder held on deposit with the card issuer.

(d)(2) This paragraph does not alter or affect the right of a card issuer acting under state or federal law to do any of the following with regard to funds of a cardholder held on deposit with the card issuer if the same procedure is constitutionally available to creditors generally: obtain or enforce a consensual security interest in the funds; attach or otherwise levy upon the funds; or obtain or enforce a court order relating to the funds.

(d)(3) This paragraph does not prohibit a plan, if authorized in writing by the cardholder, under which the card issuer may periodically deduct all or part of the cardholder's credit card debt from a deposit account held with the card issuer (subject to the limitations in § 226.13(d)(1)).

(e) Prompt notification of returns and crediting of refunds. (1) When a creditor other than the card issuer accepts the return of property or forgives a debt for services that is to be reflected as a credit to the consumer's credit card account, that creditor shall, within 7 business days from accepting the return or forgiving the debt, transmit a credit statement to the card issuer through the card issuer's normal channels for credit statements.

(e)(2) The card issuer shall, within 3 business days from receipt of a credit statement, credit the consumer's account with the amount of the refund.

(e)(3) If a creditor other than a card issuer routinely gives cash refunds to consumers paying in cash, the creditor shall also give credit or cash refunds to consumers using credit cards, unless it discloses at the time the transaction is consummated that credit or cash refunds for returns are not given. This section does not require refunds for returns nor does it prohibit refunds in kind.

(f) Discounts; tie-in arrangements. No card issuer may, by contract or otherwise:

(f)(1) Prohibit any person who honors a credit card from offering a discount to a consumer to induce the consumer to pay by cash, check, or similar means rather than by use of a credit card or its underlying account for the purchase of property or services; or

(f)(2) Require any person who honors the card issuer's credit card to open or maintain any account or obtain any other service not essential to the operation of the credit card plan from the card issuer or any other person, as a condition of participation in a credit card plan. If maintenance of an account for clearing purposes is determined to be essential to the operation of the credit card plan, it may be required only if no service charges or minimum balance requirements are imposed.

(g) Relation to Electronic Fund Transfer Act and Regulation E. For guidance on whether Regulation Z or Regulation E applies in instances involving both credit and electronic fund transfer aspects, refer to Regulation E, 12 CFR 205.5(c) regarding issuance and 205.6(d) regarding liability for unauthorized use. On matters other than issuance and liability, this section ***20899** applies to the credit aspects of combined credit/electronic fund transfer transactions, as applicable.

12 CFR § 226.13

§ 226.13 Billing error resolution. [FN27]

FN27 A creditor shall not accelerate any part of the consumer's indebtedness or restrict or close a consumer's account solely because the consumer has exercised in good faith rights provided by this section. A creditor may be subject to the forfeiture penalty under § 161(e) of the act for failure to comply with any of the requirements of this section.

(a) Definition of billing error. For purposes of this section, the term "billing error" means:

(a)(1) A reflection on or with a periodic statement of an extension of credit that is not made to the consumer or to a person who has actual, implied, or apparent authority to use the consumer's credit card or open-end credit plan.

(a)(2) A reflection on or with a periodic statement of an extension of credit that is not identified in accordance with the requirements of §§ 226.7(b) and 226.8.

(a)(3) A reflection on or with a periodic statement of an extension of credit for property or services not accepted by the consumer or the consumer's designee, or not delivered to the consumer or the consumer's designee as agreed.

(a)(4) A reflection on a periodic statement of the creditor's failure to credit properly a payment or other credit issued to the consumer's account.

(a)(5) A reflection on a periodic statement of a computational or similar error of an accounting nature that is made by the creditor.

(a)(6) A reflection on a periodic statement of an extension of credit for which the consumer requests additional clarification, including documentary evidence.

(a)(7) The creditor's failure to mail or deliver a periodic statement to the consumer's last known address if that address was received by the creditor, in writing, at least 20 days before the end of the billing cycle for which the statement was required.

(b) Billing error notice. [FN28] A billing error notice is a written notice [FN29] from a consumer that:

FN28 The creditor need not comply with the requirements of paragraphs (c) through (g) of this section if the consumer concludes that no billing error occurred and voluntarily withdraws the billing error notice.

FN29 The creditor may require that the written notice not be made on the payment medium or other material accompanying the periodic statement if the creditor so stipulates in the billing rights statement required by §§ 226.6(d) and 226.9(a).

(b)(1) Is received by a creditor at the address disclosed under § 226.7(k) no later than 60 days after the creditor transmitted the first periodic statement that reflects the alleged billing error;

(b)(2) Enables the creditor to identify the consumer's name and account number; and

(b)(3) To the extent possible, indicates the consumer's belief and the reasons for the belief that a billing error exists, and the type, date, and amount of the error.

(c) Time for resolution; general procedures. (1) The creditor shall mail or deliver written acknowledgment to the consumer within 30 days of receiving a billing error notice, unless the creditor has complied with the appropriate resolution procedures of paragraphs (e) and (f) of this section, as applicable, within the 30-day period; and

(c)(2) The creditor shall comply with the appropriate resolution procedures of paragraphs (e) and (f) of this section, as applicable, within 2 complete billing cycles (but in no event later than 90 days) after receiving a billing error notice.

(d) Rules pending resolution. Until a billing error is resolved under paragraphs (e) or (f) of this section, the following rules apply:

(d)(1) Consumer's right to withhold disputed amount; collection action prohibited. The consumer need not pay (and the creditor may not try to collect) any portion of any required payment that the consumer believes is related to the disputed amount (including related finance or other charges). [FN30] If the cardholder maintains a deposit account with the card issuer and has agreed to pay the credit card indebtedness by periodic deductions from the cardholder's deposit account, the card issuer shall not deduct any part of the disputed amount or related finance or other charges if a billing error notice is received any time up to 3 business days before the scheduled payment date.

FN30 A creditor is not prohibited from taking action to collect any undisputed portion of the item or bill; from deducting any disputed amount and related finance or other charges from the consumer's credit limit on the account; or from reflecting a disputed amount and related finance or other charges on a periodic statement, provided that the creditor indicates on or with the periodic statement that payment of any disputed amount and related finance or other charges is not required pending the creditor's compliance with this section.

(d)(2) Adverse credit reports prohibited. The creditor or its agent shall not (directly or indirectly) make or threaten to make an adverse report to any person about the consumer's credit standing, or report that an amount or account is delinquent, because the consumer failed to pay the disputed amount or related finance or other charges.

(e) Procedures if billing error occurred as asserted. If a creditor determines that a billing error occurred as asserted, it shall within the time limits in paragraph (c)(2) of this section:

(e)(1) Correct the billing error and credit the consumer's account with any disputed amount and related finance or other charges, as applicable; and

(e)(2) Mail or deliver a correction notice to the consumer.

(f) Procedures if different billing error or no billing error occurred. If, after conducting a reasonable investigation, [FN31] a creditor determines that no billing error occurred or that a different billing error occurred from that asserted, the creditor shall within the time limits in paragraph (c)(2) of this section:

FN31 If a consumer submits a billing error notice alleging either the nondelivery of property or services under paragraph (a)(3) of this section or that information appearing on a periodic statement is incorrect because a person honoring the consumer's credit card has made an incorrect report to the card issuer, the creditor shall not deny the assertion unless it conducts a reasonable investigation and determines that the property or services were actually delivered, mailed, or sent as agreed or that the information was correct.

(f)(1) Mail or deliver to the consumer an explanation that sets forth the reasons for the creditor's belief that the billing error alleged by the consumer is incorrect in whole or in part;

(f)(2) Furnish copies of documentary evidence of the consumer's indebtedness, if the consumer so requests; and

(f)(3) If a different billing error occurred, correct the billing error and credit the consumer's account with any disputed amount and related finance or other charges, as applicable.

(g) Creditor's rights and duties after resolution. If a creditor, after complying with all of the requirements of this section, determines that a consumer owes all or part of the disputed amount and related finance or other charges, the creditor:

(g)(1) Shall promptly notify the consumer in writing of the time when payment is due and the portion of the disputed amount and related finance or other charges that the consumer still owes;

(g)(2) Shall allow any time period disclosed under §§ 226.6(a)(1) and 226.7(j), during which the consumer can pay the amount due under paragraph (g)(1) of this section without incurring additional finance or other charges;

(g)(3) May report an account or amount as delinquent because the amount due under paragraph (g)(1) of this section remains unpaid after the creditor has allowed any time period disclosed under §§ 226.6(a)(1) and 266.7(j) or 10 days (whichever is longer) during which the consumer can pay the amount; but

(g)(4) May not report that an amount or account is delinquent because the ***20900** amount due under paragraph (g)(1) of the section remains unpaid, if the creditor receives (within the time allowed for payment in paragraph (g)(3) of this section) further written notice from the consumer that any portion of the billing error is still in dispute, unless the creditor also:

(g)(4)(i) Promptly reports that the amount or account is in dispute;

(g)(4)(ii) Mails or delivers to the consumer (at the same time the report is made) a written notice of the name and address of each person to whom the creditor makes a report; and

(g)(4)(iii) Promptly reports any subsequent resolution of the reported delinquency to all persons to whom the creditor has made a report.

(h) Reassertion of billing error. A creditor that has fully complied with the requirements of this section has no further responsibilities under this section (other than as provided in paragraph (g)(4) of this section) if a consumer reasserts substantially the same billing error.

(i) Relation to Electronic Fund Transfer Act and Regulation E. If an extension of credit is incident to an electronic fund transfer, under an agreement between a consumer and a financial institution to extend credit when the consumer's account is overdrawn or to maintain a specified minimum balance in the consumer's account, the creditor shall comply with the requirements of Regulation E, 12 CFR 205.11 governing error resolution rather than those of paragraphs (a), (b), (c), (e), (f), and (h) of this section.

12 CFR § 226.14

§ 226.14 Determination of annual percentage rate.

(a) General rule. The annual percentage rate is a measure of the cost of credit, expressed as a yearly rate. An annual percentage rate shall be considered accurate if it is not more than [FN18] of 1 percentage point above or below the annual percentage rate determined in accordance with this section. [FN31a]

FN31a An error in disclosure of the annual percentage rate or finance charge shall not, in itself, be considered a violation of this regulation if: (1) the error resulted from a corresponding error in a calculation tool used in good faith by the creditor; and (2) upon discovery of the error, the creditor promptly discontinues use of that calculation tool for disclosure purposes, and notifies the Board in writing of the error in the calculation tool. This footnote shall cease to be effective on April 1, 1982.

(b) Annual percentage rate for initial disclosures and for advertising purposes. Where one or more periodic rates may be used to compute the finance charge, the annual percentage rate(s) to be disclosed for purposes of §§ 226.6(a)(2) and 226.16(b)(2) shall be computed by multiplying each periodic rate by the number of periods in a year.

(c) Annual percentage rate for periodic statements. The annual percentage rate(s) to be disclosed for purposes of § 226.7(d) shall be computed by multiplying each periodic rate by the number of periods in a year and, for purposes of § 226.7(g), shall be determined as follows:

(c)(1) If the finance charge is determined solely by applying one or more periodic rates, at the creditor's option, either:

(c)(1)(i) By multiplying each periodic rate by the number of periods in a year; or

(c)(1)(ii) By dividing the total finance charge for the billing cycle by the sum of the balances to which the periodic rates were applied and multiplying the quotient (expressed as a percentage) by the number of billing cycles in a year.

(c)(2) If the finance charge imposed during the billing cycle is or includes a minimum, fixed, or other charge not due to the application of a periodic rate, other than a charge with respect to any specific transaction during the billing cycle, by dividing the total finance charge for the billing cycle by the amount of the balance(s) to which it is applicable [FN32] and multiplying the quotient (expressed as a percentage) by the number of billing cycles in a year. [FN33] N

FN32 If there is no balance to which the finance charge is applicable, an annual percentage rate cannot be determined under this section.

FN33 Where the finance charge imposed during the billing cycle is or includes a loan fee, points, or similar charge that relates to the opening of the account, the amount of such charge shall not be included in the calculation of the annual percentage rate.

(c)(3) If the finance charge imposed during the billing cycle is or includes a charge relating to a specific transaction during the billing cycle (even if the total finance charge also includes any other minimum, fixed, or other charge not due to the application of a periodic rate), by dividing the total finance charge imposed during the billing cycle by the total of all balances and other amounts on which a finance charge was imposed during the billing cycle without duplication, and multiplying the quotient (expressed as a percentage) by the number of billing cycles in a year, [FN34] except that the annual percentage rate shall not be less than the largest rate determined by multiplying each periodic rate imposed during the billing cycle by the number of periods in a year. [FN35] N

FN34 See Appendix F regarding determination of the denominator of the fraction under this paragraph.

FN35 See footnote 33.

(c)(4) If the finance charge imposed during the billing cycle is or includes a minimum, fixed, or other charge not due to the application of a periodic rate and the total finance charge imposed during the billing cycle does not exceed 50 cents for a monthly or longer billing cycle, or the pro rata part of 50 cents for a billing cycle shorter than monthly, at the creditor's option, by multiplying each applicable periodic rate by the number of periods in a year, notwithstanding the provisions of paragraphs (c)(2) and (3) of this section.

(d) Calculations where daily periodic rate applied. If the provisions of paragraphs (c)(1)(ii) or (2) of this section apply and all or a portion of the finance charge is determined by the application of one or more daily periodic rates, the annual percentage rate may be determined either:

(d)(1) By dividing the total finance charge by the average of the daily balances and multiplying the quotient by the number of billing cycles in a year; or

(d)(2) By dividing the total finance charge by the sum of the daily balances and multiplying the quotient by 365.

12 CFR § 226.15

§ 226.15 Right of rescission.

(a) Consumer's right to rescind. (1)(i) Except as provided in paragraph (a)(1)(ii) of this section, in a credit plan in which a security interest is or will be retained or acquired in a consumer's principal dwelling, each consumer whose ownership interest is or will be subject to the security interest shall have the right to rescind: each credit extension made under the plan; the plan when the plan is opened; a security interest when added or increased to secure an existing plan; and the increase when a credit limit on the plan is increased.

(ii) As provided in § 125(e) of the act, the consumer does not have the right to rescind each credit extension made under the plan if such extension is made in accordance with a previously established credit limit for the plan.

(ii)(2) To exercise the right to rescind, the consumer shall notify the creditor of the rescission by mail, telegram, or other means of written communication. Notice is considered given when mailed, or when filed for telegraphic transmission, or, if sent by other means, when delivered to the creditor's designated place of business.

(ii)(3) The consumer may exercise the right to rescind until midnight of the third business day following the occurrence described in paragraph (a)(1) of this section that gave rise to the right of rescission, delivery of the notice required by paragraph (b) of this section, or delivery of all material ***20901** disclosures, [FN36] whichever occurs last.   If the required notice and material disclosures are not delivered, the right to rescind shall expire 3 years after the occurrence giving rise to the right of rescission, or upon transfer of all of the consumer's interest in the property, or upon sale of the property, whichever occurs first. In the case of certain administrative proceedings, the rescission period shall be extended in accordance with § 125(f) of the act.

FN36 The term "material disclosures" means the information that must be provided to satisfy the requirements in § 226.6 with regard to the method of determining the finance charge and the balance upon which a finance charge will be imposed, the annual percentage rate, and the amount or method of determining the amount of any membership or participation fee that may be imposed as part of the plan.

(ii)(4) When more than one consumer has the right to rescind, the exercise of the right by one consumer shall be effective as to all consumers.

(b) Notice of right to rescind. In any transaction or occurrence subject to rescission, a creditor shall deliver 2 copies of the notice of the right to rescind to each consumer entitled to rescind. The notice shall identify the transaction or occurrence and clearly and conspicuously disclose the following:

(b)(1) The retention or acquisition of a security interest in the consumer's principal dwelling.

(b)(2) The consumer's right to rescind, as described in paragraph (a)(1) of this section.

(b)(3) How to exercise the right to rescind, with a form for that purpose, designating the address of the creditor's place of business.

(b)(4) The effects of rescission, as described in paragraph (d) of this section.

(b)(5) The date the rescission period expires.

(c) Delay of creditor's performance. Unless a consumer waives the right to rescind under paragraph (e) of this section, no money shall be disbursed other than in escrow, no services shall be performed, and no materials delivered until after the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded. A creditor does not violate this section if a third party with no knowledge of the event activating the rescission right does not delay in providing materials or services, as long as the debt incurred for those materials or services is not secured by the property subject to rescission.

(d) Effects of rescission. (1) When a consumer rescinds a transaction, the security interest giving rise to the right of rescission becomes void, and the consumer shall not be liable for any amount, including any finance charge.

(d)(2) Within 20 calendar days after receipt of a notice of rescission, the creditor shall return any money or property that has been given to anyone in connection with the transaction and shall take any action necessary to reflect the termination of the security interest.

(d)(3) If the creditor has delivered any money or property, the consumer may retain possession until the creditor has met its obligation under paragraph (d)(2) of this section. When the creditor has complied with that paragraph, the consumer shall tender the money or property to the creditor or, where the latter would be impracticable or inequitable, tender its reasonable value. At the consumer's option, tender of property may be made at the location of the property or at the consumer's residence. Tender of money must be made at the creditor's designated place of business. If the creditor does not take possession of the money or property within 20 calendar days after the consumer's tender, the consumer may keep it without further obligation.

(d)(4) The procedures outlined in paragraphs (d)(2) and (3) of this section may be modified by court order.

(e) Consumer's waiver of right to rescind. The consumer may modify or waive the right to rescind if the consumer determines that the extension of credit is needed to meet a bona fide personal financial emergency. To modify or waive the right, the consumer shall give the creditor a dated written statement that describes the emergency, that specifically modifies or waives the right to rescind, and that bears the signatures of the consumers entitled to rescind. Printed forms for this purpose are prohibited.

(f) Exempt transactions. The right to rescind does not apply to the following:

(f)(1) A residential mortgage transaction.

(f)(2) A credit plan in which a state agency is a creditor.

12 CFR § 226.16

§ 226.16 Advertising.

(a) Actually available terms. If an advertisement for credit states specific credit terms, it shall state only those terms that actually are or will be arranged or offered by the creditor.

(b) Advertisement of terms that require additional disclosures. If any of the terms required to be disclosed under § 226.6 is set forth in an advertisement, the advertisement shall also clearly and conspicuously set forth the following:

(b)(1) Any minimum, fixed, transaction, activity or similar charge that could be imposed.

(b)(2) Any periodic rate that may be applied expressed as an annual percentage rate as determined under § 226.14(b). If the plan provides for a variable periodic rate, that fact shall be disclosed.

(b)(3) Any membership or participation fee that could be imposed.

(c) Catalogs and multiple-page advertisements. (1) If a catalog or other multiple-page advertisement gives information in a table or schedule in sufficient detail to permit determination of the disclosures required by paragraph (b) of this section, it shall be considered a single advertisement if:

(c)(i) The table or schedule is clearly and conspicuously set forth; and

(c)(ii) Any statement of terms set forth in § 226.6 appearing anywhere else in the catalog or advertisement clearly refers to that page on which the table or schedule begins.

(c)(ii)(2) A catalog or multiple-page advertisement complies with this paragraph if the table or schedule of terms includes all appropriate disclosures for a representative scale of amounts up to the level of the more commonly sold higher-priced property or services offered.

Subpart C--Closed-End Credit

12 CFR § 226.17

§ 226.17 General disclosure requirements.

(a) Form of disclosures. (1) The creditor shall make the disclosures required by this subpart clearly and conspicuously in writing, in a form that the consumer may keep. The disclosures shall be grouped together, shall be segregated from everything else, and shall not contain any information not directly related [FN37] to the disclosures required under § 226.18. [FN38] The itemization of the amount financed under § 226.18(c)(1) must be separate from the other disclosures under that section.

FN37 The disclosures may include an acknowledgment of receipt, the date of the transaction, and the consumer's name, address, and account number.

FN38 The following disclosures may be made together or separately from other required disclosures: the creditor's identity under § 226.18(a), the variable rate example under § 226.18(f)(4), insurance under § 226.18(n), and certain security interest charges under § 226.18(o).

(a)(2) The terms "finance charge" and "annual percentage rate," when required to be disclosed under § 226.18 (d) and (e) together with a corresponding amount or percentage rate, shall be more conspicuous than any other disclosure, except the creditor's identity under § 226.18(a).

(b) Time of disclosures. The creditor shall make disclosures before ***20902** consummation of the transaction. In certain residential mortgage transactions, special timing requirements are set forth in § 226.19. In certain transactions involving mail or telephone orders or a series of sales, the timing of the disclosures may be delayed in accordance with paragraphs (g) and (h) of this section.

(c) Basis of disclosures and use of estimates. (1) The disclosures shall reflect the terms of the legal obligation between the parties.

(c)(2) If any information necessary for an accurate disclosure is unknown to the creditor, it shall make the disclosure based on the best information reasonably available and shall state that the disclosure is an estimate.

(c)(3) The creditor may disregard the effects of the following in making calculations and disclosures.

(c)(3)(i) That payments must be collected in whole cents.

(c)(3)(ii) That dates of scheduled payments and advances may be changed because the scheduled date is not a business day.

(c)(3)(iii) That months have different numbers of days.

(c)(3)(iv) The occurrence of leap year.

(c)(4) In making calculations and disclosures, the creditor may disregard any irregularity in the first period that falls within the limits described below and any payment schedule irregularity that results from the irregular first period:

(c)(4)(i) For transactions in which the term is less than 1 year, a first period not more than 6 days shorter or 13 days longer than a regular period;

(c)(4)(ii) For transactions in which the term is at least 1 year and less than 10 years, a first period not more than 11 days shorter or 21 days longer than a regular period; and

(c)(4)(iii) For transactions in which the term is at least 10 years, a first period shorter than or not more than 32 days longer than a regular period.

(c)(5) If an obligation is payable on demand, the creditor shall make the disclosures based on an assumed maturity of 1 year. If an alternate maturity date is stated in the legal obligation between the parties, the disclosures shall be based on that date.

(c)(6)(i) A series of advances under an agreement to extend credit up to a certain amount may be considered as one transaction.

(c)(6)(ii) When a multiple-advance loan to finance the construction of a dwelling may be permanently financed by the same creditor, the construction phase and the permanent phase may be treated as either one transaction or more than one transaction.

(d) Multiple creditors; multiple consumers. If a transaction involves more than one creditor, only one set of disclosures shall be given and the creditors shall agree among themselves which creditor must comply with the requirements that this regulation imposes on any or all of them. If there is more than one consumer, the disclosures may be made to any consumer who is primarily liable on the obligation. If the transaction is rescindable under § 226.23, however, the disclosures shall be made to each consumer who has the right to rescind.

(e) Effect of subsequent events. If a disclosure becomes inaccurate because of an event that occurs after the creditor delivers the required disclosures, the inaccuracy is not a violation of this regulation, although new disclosures may be required under paragraph (f) of this section, § 226.19, or § 226.20.

(f) Early disclosures. If disclosures are given before the date of consummation of a transaction and a subsequent event makes them inaccurate, the creditor shall disclose the changed terms before consummation, if the annual percentage rate in the consummated transaction varies from the annual percentage rate disclosed under § 226.18(e) by more than 1/8 of 1 percentage point in a regular transaction, or more than 1/4 of 1 percentage point in an irregular transaction, as defined in § 226.22(a).

(g) Mail or telephone orders--delay in disclosures. If a creditor receives a purchase order or a request for an extension of credit by mail, telephone, or any other written or electronic communication without face-to-face or direct telephone solicitation, the creditor may delay the disclosures until the due date of the first payment, if the following information for representative amounts or ranges of credit is made available in written form to the consumer or to the public before the actual purchase order or request:

(g)(1) The cash price or the principal loan amount.

(g)(2) The total sale price.

(g)(3) The finance charge.

(g)(4) The annual percentage rate, and if the rate may increase after consummation, the following disclosures:

(g)(4)(i) The circumstances under which the rate may increase.

(g)(4)(ii) Any limitations on the increase.

(g)(4)(iii) The effect of an increase.

(g)(5) The terms of repayment.

(h) Series of sales--delay in disclosures. If a credit sale is one of a series made under an agreement providing that subsequent sales may be added to an outstanding balance, the creditor may delay the required disclosures until the due date of the first payment for the current sale, if the following two conditions are met:

(h)(1) The consumer has approved in writing the annual percentage rate or rates, the range of balances to which they apply, and the method of treating any unearned finance charge on an existing balance.

(h)(2) The creditor retains no security interest in any property after the creditor has received payments equal to the cash price and any finance charge attributable to the sale of that property. For purposes of this provision, in the case of items purchased on different dates, the first purchased is deemed the first item paid for; in the case of items purchased on the same date, the lowest priced is deemed the first item paid for.

(i) Interim student credit extensions. For each transaction involving an interim credit extension under a student credit program, the creditor need not make the following disclosures: the finance charge under § 226.18(d), the payment schedule under § 226.18(g), the total of payments under § 226.18(h), or the total sale price under § 226.18(j).

12 CFR § 226.18

§ 226.18 Content of disclosures.

For each transaction, the creditor shall disclose the following information as applicable:

(a) Creditor. The identity of the creditor making the disclosures.

(b) Amount financed. The "amount financed," using that term, and a brief description such as "the amount of credit provided to you or on your behalf." The amount financed is calculated by:

(b)(1) Determining the principal loan amount or the cash price (subtracting any downpayment);

(b)(2) Adding any other amounts that are financed by the creditor and are not part of the finance charge; and

(b)(3) Subtracting any prepaid finance charge.

(c) Itemization of amount financed. (1) A separate written itemization of the amount financed, including: [FN39]

FN39 Good faith estimates of settlement costs provided for transactions subject to the Real Estate Settlement Procedures Act (12 U.S.C. 2601 et seq.) may be substituted for the disclosures required by paragraph (c) of this section.

(c)(i) The amount of any proceeds distributed directly to the consumer.

(c)(ii) The amount credited to the consumer's account with the creditor.

(c)(iii) Any amounts paid to other persons by the creditor on the consumer's behalf. The creditor shall identify those persons. [FN40]

FN40 The following payees may be described using generic or other general terms and need not be further identified: public officials or government agencies, credit reporting agencies, appraisers, and insurance companies.

***20903** (c)(iv) The prepaid finance charge.

(c)(iv)(2) The creditor need not comply with paragraph (c)(1) of this section if the creditor provides a statement that the consumer has the right to receive a written itemization of the amount financed, together with a space for the consumer to indicate whether it is desired, and the consumer does not request it.

(d) Finance charge. The "finance charge," using that term, and a brief description such as "the dollar amount the credit will cost you." [FN41]

FN41 The finance charge shall be considered accurate if it is not more than $5 above or below the exact finance charge in a transaction involving an amount financed of $1,000 or less, or not more than $10 above or below the exact finance charge in a transaction involving an amount financed of more that $1,000.

(e) Annual percentage rate. The "annual percentage rate," using that term, and a brief description such as "the cost of your credit as a yearly rate." [FN42]

FN42 For any transaction involving a finance charge of $5 or less on an amount financed of $75 or less, or a finance charge of $7.50 or less on an amount financed of more than $75, the creditor need not disclose the annual percentage rate.

(f) Variable rate. If the annual percentage rate may increase after consummation, the following disclosures: [FN43]

FN43 Information provided in accordance with variable rate regulations of other federal agencies may be substituted for the disclosures required by paragraph (f) of this section.

(f)(1) The circumstances under which the rate may increase.

(f)(2) Any limitations on the increase.

(f)(3) The effect of an increase.

(f)(4) An example of the payment terms that would result from an increase.

(g) Payment schedule. The number, amounts, and timing of payments scheduled to repay the obligation.

(g)(1) In a demand obligation with no alternate maturity date, the creditor may comply with this paragraph by disclosing the due dates or payment periods of any scheduled interest payments for the first year.

(g)(2) In a transaction in which a series of payments varies because a finance charge is applied to the unpaid principal balance, the creditor may comply with this paragraph by disclosing the following information:

(g)(2)(i) The dollar amounts of the largest and smallest payments in the series.

(g)(2)(ii) A reference to the variations in the other payments in the series.

(h) Total of payments. The "total of payments," using that term, and a descriptive explanation such as "the amount you will have paid when you have made all scheduled payments." [FN44]

FN44 In any transaction involving a single payment, the creditor need not disclose the total of payments.

(i) Demand feature. If the obligation has a demand feature, that fact shall be disclosed. When the disclosures are based on an assumed maturity of 1 year as provided in § 226.17(c)(5), that fact shall also be disclosed.

(j) Total sale price. In a credit sale, the "total sale price," using that term, and a descriptive explanation (including the amount of any downpayment) such as "the total price of your purchase on credit, including your downpayment of $." The total sale price is the sum of the cash price, the items described in paragraph (b)(2), and the finance charge disclosed under paragraph (d) of this section.

(k) Prepayment. (1) When an obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance, a statement indicating whether or not a penalty may be imposed if the obligation is prepaid in full.

(k)(2) When an obligation includes a finance charge other than the finance charge described in paragraph (k)(1) of this section, a statement indicating whether or not the consumer is entitled to a rebate of any finance charge if the obligation is prepaid in full.

(l) Late payment. Any dollar or percentage charge that may be imposed before maturity due to a late payment, other than a deferral or extension charge.

(m) Security interest. The fact that the creditor has or will acquire a security interest in the property purchased as part of the transaction, or in other property identified by item or type.

(n) Insurance. The items required by § 226.4(d) in order to exclude certain insurance premiums from the finance charge.

(o) Certain security interest charges. The disclosures required by § 226.4(e) in order to exclude from the finance charge certain fees prescribed by law or certain premiums for insurance in lieu of perfecting a security interest.

(p) Contract reference. A statement that the consumer should refer to the appropriate contract document for information about nonpayment, default, the right to accelerate the maturity of the obligation, and prepayment rebates and penalties. At the creditor's option, the statement may also include a reference to the contract for further information about security interests and, in a residential mortgage transaction, about the creditor's policy regarding assumption of the obligation.

(q) Assumption policy. In a residential mortgage transaction, a statement whether or not a subsequent purchaser of the dwelling from the consumer may be permitted to assume the remaining obligation on its original terms.

(r) Required deposit. If the creditor requires the consumer to maintain a deposit as a condition of the specific transaction, a statement that the annual percentage rate does not reflect the effect of the required deposit. [FN45]

FN45 A required deposit need not include, for example: (1) an escrow account for items such as taxes, insurance or repairs; (2) a deposit that earns not less than 5 percent per year; or (3) payments under a Morris Plan.

12 CFR § 226.19

§ 226.19 Certain residential mortgage transactions.

(a) Time of disclosure. In a residential mortgage transaction subject to the Real Estate Settlement Procedures Act (12 U.S.C. 2601 et seq.) the creditor shall make good faith estimates of the disclosures required by § 226.18 before consummation, or shall deliver or place them in the mail not later than 3 business days after the creditor receives the consumer's written application, whichever is earlier.

(b) Redisclosure required. If the annual percentage rate in the consummated transaction varies from the annual percentage rate disclosed under § 226.18(e) by more than 1/8 of 1 percentage point in a regular transaction or more than 1/4 of 1 percentage point in an irregular transaction, as defined in § 226.22, the creditor shall disclose the changed terms no later than consummation or settlement.

12 CFR § 226.20

§ 226.20 Subsequent disclosure requirements.

(a) Refinancings. A refinancing occurs when an existing obligation that was subject to this subpart is satisfied and replaced by a new obligation undertaken by the same consumer. A refinancing is a new transaction requiring new disclosures to the consumer. The new finance charge shall include any unearned portion of the old finance charge that is not credited to the existing obligation. The following shall not be treated as a refinancing:

(a)(1) A renewal of a single payment obligation with no change in the original terms.

(a)(2) A reduction in the annual percentage rate with a corresponding change in the payment schedule.

(a)(3) An agreement involving a court proceeding.

***20904** (a)(4) A change in the payment schedule or a change in collateral requirements as a result of the consumer's default or delinquency, unless the rate is increased, or the new amount financed exceeds the unpaid balance plus earned finance charge and premiums for continuation of insurance of the types described in § 226.4(d).

(a)(5) The renewal of optional insurance purchased by the consumer and added to an existing transaction, if disclosures relating to the initial purchase were provided as required by this subpart.

(b) Assumptions. An assumption occurs when a creditor expressly agrees in writing with a subsequent consumer to accept that consumer as a primary obligor on an existing residential mortgage transaction. Before the assumption occurs, the creditor shall make new disclosures to the subsequent consumer, based on the remaining obligation. If the finance charge originally imposed on the existing obligation was an add-on or discount finance charge, the creditor need only disclose:

(b)(1) The unpaid balance of the obligation assumed.

(b)(2) The total charges imposed by the creditor in connection with the assumption.

(b)(3) The information required to be disclosed under § 226.18(k), (l), (m), and (n).

(b)(4) The annual percentage rate originally imposed on the obligation.

(b)(5) The payment schedule under § 226.18(g) and the total of payments under § 226.18(h) based on the remaining obligation.

12 CFR § 226.21

§ 226.21 Treatment of credit balances.

When a credit balance in excess of $1 is created in connection with a transaction (through transmittal of funds to a creditor in excess of the total balance due on an account, through rebates of unearned finance charges or insurance premiums, or through amounts otherwise owed to or held for the benefit of a consumer), the creditor shall:

(a) Credit the amount of the credit balance to the consumer's account;

(b) Refund any part of the remaining credit balance, upon the written request of the consumer; and

(c) Make a good faith effort to refund to the consumer by cash, check, or money order, or credit to a deposit account of the consumer, any part of the credit balance remaining in the account for more than 6 months, except that no further action is required if the consumer's current location is not known to the creditor and cannot be traced through the consumer's last known address or telephone number.

12 CFR § 226.22

§ 226.22 Determination of annual percentage rate.

(a) Accuracy of annual percentage rate. (1) The annual percentage rate is a measure of the cost of credit, expressed as a yearly rate, that relates the amount and timing of value received by the consumer to the amount and timing of payments made. The annual percentage rate shall be determined in accordance with either the actuarial method or the United States Rule method. Explanations, equations and instructions for determining the annual percentage rate in accordance with the actuarial method are set forth in Appendix J to this regulation. [FN45a]

FN45a An error in disclosure of the annual percentage rate or finance charge shall not, in itself, be considered a violation of this regulation if: (1) the error resulted from a corresponding error in a calculation tool used in good faith by the creditor; and (2) upon discovery of the error, the creditor promptly discontinues use of that calculation tool for disclosure purposes and notifies the Board in writing of the error in the calculation tool. This footnote shall cease to be effective on April 1, 1982.

(a)(2) As a general rule, the annual percentage rate shall be considered accurate if it is not more than 1/8 of 1 percentage point above or below the annual percentage rate determined in accordance with paragraph (a)(1) of this section.

(a)(3) In an irregular transaction, the annual percentage rate shall be considered accurate if it is not more than [FN14] of 1 percentage point above or below the annual percentage rate determined in accordance with paragraph (a)(1) of this section. [FN46] N

FN46 For purposes of paragraph (a)(3) of this section, an irregular transaction is one that includes one or more of the following features: multiple advances, irregular payment periods, or irregular payment amounts (other than an irregular first period or an irregular first or final payment).

(b) Computation tools. (1) The Regulation Z Annual Percentage Rate Tables produced by the Board may be used to determine the annual percentage rate, and any rate determined from those tables in accordance with the accompanying instructions complies with the requirements of this section. Volume I of the tables applies to single advance transactions involving up to 480 monthly payments or 104 weekly payments. It may be used for regular transactions and for transactions with any of the following irregularities: an irregular first period, an irregular first payment, and an irregular final payment.

Volume II of the tables applies to transactions involving multiple advances and any type of payment or period irregularity.

(b)(2) Creditors may use any other computation tool in determining the annual percentage rate if the rate so determined equals the rate determined in accordance with Appendix J, within the degree of accuracy set forth in paragraph (a) of this section.

(c) Single add-on rate transactions. If a single add-on rate is applied to all transactions with maturities up to 60 months and if all payments are equal in amount and period, a single annual percentage rate may be disclosed for all those transactions, so long as it is the highest annual percentage rate for any such transaction.

(d) Certain transactions involving ranges of balances. For purposes of disclosing the annual percentage rate referred to in § 226.17(g)(4) (Mail or telephone orders--delay in disclosures) and (h) (Series of sales--delay in disclosures), if the same finance charge is imposed on all balances within a specified range of balances, the annual percentage rate computed for the median balance may be disclosed for all the balances. However, if the annual percentage rate computed for the median balance understates the annual percentage rate computed for the lowest balance by more than 8 percent of the latter rate, the annual percentage rate shall be computed on whatever lower balance will produce an annual percentage rate that does not result in an understatement of more than 8 percent of the rate determined on the lowest balance.

12 CFR § 226.23

§ 226.23 Right of rescission.

(a) Consumer's right to rescind. (1) In a credit transaction in which a security interest is or will be retained or acquired in a consumer's principal dwelling, each consumer whose ownership interest is or will be subject to the security interest shall have the right to rescind the transaction, except for transactions described in paragraph (f) of this section. [FN47] N

FN47 For purposes of this section, the addition to an existing obligation of a security interest in a consumer's principal dwelling is a transaction. The right of rescission applies only to the addition of the security interest and not the existing obligation. The creditor shall deliver the notice required by paragraph (b) of this section but need not deliver new material disclosures. Delivery of the required notice shall begin the rescission period.

(a)(2) To exercise the right to rescind, the consumer shall notify the creditor of the rescission by mail, telegram or other means of written communication. Notice is considered given when mailed, when filed for telegraphic transmission or, if sent by other means, when delivered to the creditor's designated place of business.

***20905** (a)(3) The consumer may exercise the right to rescind until midnight of the third business day following consummation, delivery of the notice required by paragraph (b) of this section, or delivery of all material disclosures, [FN48] whichever occurs last. If the required notice or material disclosures are not delivered, the right to rescind shall expire 3 years after consummation, upon transfer of all of the consumer's interest in the property, or upon sale of the property, whichever occurs first. In the case of certain administrative proceedings, the rescission period shall be extended in accordance with § 125(f) of the act.

FN48 The term "material disclosures" means the required disclosures of the annual percentage rate, the finance charge, the amount financed, the total of payments, and the payment schedule.

(a)(4) When more than one consumer in a transaction has the right to rescind, the exercise of the right by one consumer shall be effective as to all consumers.

(b) Notice of right to rescind. In a transaction subject to rescission, a creditor shall deliver 2 copies of the notice of the right to rescind to each consumer entitled to rescind. The notice shall be on a separate document that identifies the transaction and shall clearly and conspicuously disclose the following:

(b)(1) The retention or acquisition of a security interest in the consumer's principal dwelling.

(b)(2) The consumer's right to rescind the transaction.

(b)(3) How to exercise the right to rescind, with a form for that purpose, designating the address of the creditor's place of business.

(b)(4) The effects of rescission, as described in paragraph (d) of this section.

(b)(5) The date the rescission period expires.

(c) Delay of creditor's performance. Unless a consumer waives the right of rescission under paragraph (e) of this section, no money shall be disbursed other than in escrow, no services shall be performed and no materials delivered until the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded.

(d) Effects of rescission. (1) When a consumer rescinds a transaction, the security interest giving rise to the right of rescission becomes void and the consumer shall not be liable for any amount, including any finance charge.

(d)(2) Within 20 calendar days after receipt of a notice of rescission, the creditor shall return any money or property that has been given to anyone in connection with the transaction and shall take any action necessary to reflect the termination of the security interest.

(d)(3) If the creditor has delivered any money or property, the consumer may retain possession until the creditor has met its obligation under paragraph (d)(2) of this section. When the creditor has complied with that paragraph, the consumer shall tender the money or property to the creditor or, where the latter would be impracticable or inequitable, tender its reasonable value. At the consumer's option, tender of property may be made at the location of the property or at the consumer's residence. Tender of money must be made at the creditor's designated place of business. If the creditor does not take possession of the money or property within 20 calendar days after the consumer's tender, the consumer may keep it without further obligation.

(d)(4) The procedures outlined in paragraphs (d) (2) and (3) of this section may be modified by court order.

(e) Consumer's waiver of right to rescind. The consumer may modify or waive the right to rescind if the consumer determines that the extension of credit is needed to meet a bona fide personal financial emergency. To modify or waive the right, the consumer shall give the creditor a dated written statement that describes the emergency, specifically modifies or waives the right to rescind, and bears the signature of all of the consumers entitled to rescind. Printed forms for this purpose are prohibited.

(f) Exempt transactions. The right to rescind does not apply to the following:

(f)(1) A residential mortgage transaction.

(f)(2) A refinancing or consolidation by the same creditor of an extension of credit already secured by the consumer's principal dwelling. If the new amount financed exceeds the unpaid principal balance plus any unearned unpaid finance charge on the existing debt, this exemption applies only to the existing debt and its security interest.

(f)(3) A transaction in which a state agency is a creditor.

(f)(4) An advance, other than an initial advance, in a series of advances or in a series of single-payment obligations that is treated as a single transaction under § 226.17(c)(6), if the notice required by paragraph (b) of this section and all material disclosures have been given to the consumer.

(f)(5) A renewal of optional insurance premiums that is not considered a refinancing under § 226.20(a)(5).

12 CFR § 226.24

§ 226.24 Advertising.

(a) Actually available terms. If an advertisement for credit states specific credit terms, it shall state only those terms that actually are or will be arranged or offered by the creditor.

(b) Advertisement of rate of finance charge. If an advertisement states a rate of finance charge, it shall state the rate as an "annual percentage rate," using that term. If the annual percentage rate may be increased after consummation, the advertisement shall state that fact. The advertisement shall not state any other rate, except that a simple annual rate or periodic rate that is applied to an unpaid balance may be stated in conjunction with, but not more conspicuously than, the annual percentage rate.

(c) Advertisement of terms that require additional disclosures. (1) If any of the following terms is set forth in an advertisement, the advertisement shall meet the requirements of paragraph (c)(2) of this section:

(c)(i) The amount or percentage of any downpayment.

(c)(ii) The number of payments or period of repayment.

(c)(iii) The amount of any payment.

(c)(iv) The amount of any finance charge.

(c)(iv)(2) An advertisement stating any of the terms in paragraph (c)(1) of this section shall state the following terms, [FN49] as applicable:

FN49 An example of one or more typical extensions of credit with a statement of all the terms applicable to each may be used.

(c)(iv)(2)(i) The amount or percentage of the downpayment.

(c)(iv)(2)(ii) The terms of repayment.

(c)(iv)(2)(iii) The "annual percentage rate," using that term, and, if the rate may be increased after consummation, that fact.

(d) Catalogs and multiple-page advertisements. (1) If a catalog or other multiple-page advertisement gives information in a table or schedule in sufficient detail to permit determination of the disclosures required by paragraph (c)(2) of this section, it shall be considered a single advertisement if:

(d)(i) The table or schedule is clearly set forth; and

(d)(ii) Any statement of the credit terms in paragraph (c)(1) of this section appearing anywhere else in the catalog or advertisement clearly refers to the page on which the table or schedule begins.

(d)(ii)(2) A catalog or multiple-page advertisement complies with paragraph (c)(2) of this section if the table or schedule of terms includes all appropriate disclosures for a representative scale of amounts up to ***20906** the level of the more commonly sold higher-priced property or services offered.

Subpart D--Miscellaneous

12 CFR § 226.25

§ 226.25 Record retention.

(a) General rule. A creditor shall retain evidence of compliance with this regulation (other than advertising requirements under §§ 226.16 and 226.24) for 2 years after the date disclosures are required to be made or action is required to be taken.   The administrative agencies responsible for enforcing the regulation may require creditors under their jurisdictions to retain records for a longer period if necessary to carry out their enforcement responsibilities under § 108 of the act.

(b) Inspection of records. A creditor shall permit the agency responsible for enforcing this regulation with respect to that creditor to inspect its relevant records for compliance.

12 CFR § 226.26

§ 226.26 Use of annual percentage rate in oral disclosures.

(a) Open-end credit. In an oral response to a consumer's inquiry about the cost of open-end credit, only the annual percentage rate or rates shall be stated, except that the periodic rate or rates also may be stated. If the annual percentage rate cannot be determined in advance because there are finance charges other than a periodic rate, the corresponding annual percentage rate shall be stated, and other cost information may be given.

(b) Closed-end credit. In an oral response to a consumer's inquiry about the cost of closed-end credit, only the annual percentage rate shall be stated, except that a simple annual rate or periodic rate also may be stated if it is applied to an unpaid balance. If the annual percentage rate cannot be determined in advance, the annual percentage rate for a sample transaction shall be stated, and other cost information for the consumer's specific transaction may be given.

12 CFR § 226.27

§ 226.27 Spanish language disclosures.

All disclosures required by this regulation shall be made in the English language, except in the Commonwealth of Puerto Rico, where creditors may, at their option, make disclosures in the Spanish language. If Spanish disclosures are made, English disclosures shall be provided on the consumer's request, either in substitution for or in addition to the Spanish disclosures. This requirement for providing English disclosures on request shall not apply to advertisements subject to §§ 226.16 and 226.24 of this regulation.

12 CFR § 226.28

§ 226.28 Effect on state laws.

(a) Inconsistent disclosure requirements. (1) State law requirements that are inconsistent with the requirements contained in chapter 1 (General provisions), chapter 2 (Credit transactions), or chapter 3 (Credit advertising) of the act and the implementing provisions of this regulation are preempted to the extent of the inconsistency. A state law is inconsistent if it requires a creditor to make disclosures or take actions that contradict the requirements of the federal law. A state law is contradictory if it requires the use of the same term to represent a different amount or a different meaning than the federal law, or if it requires the use of a term different from that required in the federal law to describe the same item. A creditor, state, or other interested party may request the Board to determine whether a state law requirement is inconsistent. After the Board determines that a state law is inconsistent, a creditor may not make disclosures using the inconsistent term or form.

(a)(2)(i) State law requirements are inconsistent with the requirements contained in §§ 161 (Correction of billing errors) or 162 (Regulation of credit reports) of the act and the implementing provisions of this regulation and are preempted if they provide rights, responsibilities, or procedures for consumers or creditors that are different from those required by the federal law. However, a state law that allows a consumer to inquire about an open-end credit account and imposes on the creditor an obligation to respond to such inquiry after the time allowed in the federal law for the consumer to submit written notice of a billing error shall not be preempted in any situation where the time period for making written notice under this regulation has expired. If a creditor gives written notice of a consumer's rights under such state law, the notice shall state that reliance on the longer time period available under state law may result in the loss of important rights that could be preserved by acting more promptly under federal law; it shall also explain that the state law provisions apply only after expiration of the time period for submitting a proper written notice of a billing error under the federal law. If the state disclosures are made on the same side of a page as the required federal disclosures, the state disclosures shall appear under a demarcation line below the federal disclosures, and the federal disclosures shall be identified by a heading indicating that they are made in compliance with federal law.

(a)(2)(ii) State law requirements are inconsistent with the requirements contained in chapter 4 (Credit billing) of the act (other than §§ 161 or 162) and the implementing provisions of this regulation and are preempted if the creditor cannot comply with state law without violating federal law.

(a)(2)(iii) A state may request the Board to determine whether its law is inconsistent with chapter 4 of the act and its implementing provisions.

(b) Equivalent disclosure requirements. If the Board determines that a disclosure required by state law (other than a requirement relating to the finance charge or annual percentage rate) is substantially the same in meaning as a disclosure required under the act or this regulation, creditors in that state may make the state disclosure in lieu of the federal disclosure. A creditor, state, or other interested party may request the Board to determine whether a state disclosure is substantially the same in meaning as a federal disclosure.

(c) Request for determination. The procedures under which a request for a determination may be made under this section are set forth in Appendix A.

12 CFR § 226.29

§ 226.29 State exemptions.

(a) General rule. Any state may apply to the Board to exempt a class of transactions within the state from the requirements of chapter 2 (Credit transactions) or chapter 4 (Credit billing) of the act and the corresponding provisions of this regulation. The Board shall grant an exemption if it determines that:

(a)(1) The state law is substantially similar to the federal law or, in the case of chapter 4, affords the consumer greater protection than the federal law; and

(a)(2) There is adequate provision for enforcement.

(b) Civil liability. (1) No exemptions granted under this section shall extend to the civil liability provisions of §§ 130 and 131 of the act.

(b)(2) If an exemption has been granted, the disclosures required by the applicable state law (except any additional requirements not imposed by federal law) shall constitute the disclosures required by this act.

(c) Applications. The procedures under which a state may apply for an exemption under this section are set forth in Appendix B to this part.

Appendix A--Effect on State Laws

Request for Determination

A request for a determination that a state law is inconsistent or that a state ***20907** law is substantially the same as the act and regulation shall be in writing and addressed to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551. The request shall be made pursuant to the procedures herein and the Board's Rules of Procedure (12 CFR Part 262).

Supporting Documents

A request for a determination shall include the following items:

(c)(1) The text of the state statute, regulation, or other document that is the subject of the request.

(c)(2) Any other statute, regulation, or judicial or administrative opinion that implements, interprets, or applies the relevant provision.

(c)(3) A comparison of the state law with the corresponding provision of the federal law, including a full discussion of the basis for the requesting party's belief that the state provision is either inconsistent or substantially the same.

(c)(4) Any other information that the requesting party believes may assist the Board in its determination.

Public Notice of Determination

Notice that the Board intends to make a determination (either on request or on its own motion) will be published in the Federal Register, with an opportunity for public comment, unless the Board finds that notice and opportunity for comment would be impracticable, unnecessary, or contrary to the public interest and publishes its reasons for such decision.

Subject to the Board's Rules Regarding Availability of Information (12 CFR Part 261), all requests made, including any documents and other material submitted in support of the requests, will be made available for public inspection and copying.

Notice After Determination

Notice of a final determination will be published in the Federal Register, and the Board will furnish a copy of such notice to the party who made the request and to the appropriate state official.

Reversal of Determination

The Board reserves the right to reverse a determination for any reason bearing on the coverage or effect of state or federal law.

Notice of reversal of a determination will be published in the Federal Register and a copy furnished to the appropriate state official.

Appendix B--State Exemptions

Application

Any state may apply to the Board for a determination that a class of transactions subject to state law is exempt from the requirements of the act and this regulation. An application shall be in writing and addressed to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, and shall be signed by the appropriate state official. The application shall be made pursuant to the procedures herein and the Board's Rules of Procedure (12 CFR Part 262).

Supporting Documents

An application shall be accompanied by:

(1) The text of the state statute or regulation that is the subject of the application, and any other statute, regulation, or judicial or administrative opinion that implements, interprets, or applies it.

(2) A comparison of the state law with the corresponding provisions of the federal law.

(3) The text of the state statute or regulation that provides for civil and criminal liability and administrative enforcement of the state law.

(4) A statement of the provisions for enforcement, including an identification of the state office that administers the relevant law, information on the funding and the number and qualifications of personnel engaged in enforcement, and a description of the enforcement procedures to be followed, including information on examination procedures, practices, and policies. If an exemption application extends to federally chartered institutions, the applicant must furnish evidence that arrangements have been made with the appropriate federal agencies to ensure adequate enforcement of state law in regard to such creditors.

(5) A statement of reasons to support the applicant's claim that an exemption should be granted.

Public Notice of Application

Notice of an application will be published, with an opportunity for public comment, in the Federal Register, unless the Board finds that notice and opportunity for comment would be impracticable, unnecessary, or contrary to the public interest and publishes its reasons for such decision.

Subject to the Board's Rules Regarding Availability of Information (12 CFR Part 261), all applications made, including any documents and other material submitted in support of the applications, will be made available for public inspection and copying. A copy of the application also will be made available at the Federal Reserve Bank of each district in which the applicant is situated.

Favorable Determination

If the Board determines on the basis of the information before it that an exemption should be granted, notice of the exemption will be published in the Federal Register, and a copy furnished to the applicant and to each federal official responsible for administrative enforcement.

The appropriate state official shall inform the Board within 30 days of any change in its relevant law or regulations. The official shall file with the Board such periodic reports as the Board may require.

The Board will inform the appropriate state official of any subsequent amendments to the federal law, regulation, interpretations, or enforcement policies that might require an amendment to state law, regulation, interpretations, or enforcement procedures.

Adverse Determination

If the Board makes an initial determination that an exemption should not be granted, the Board will afford the applicant a reasonable opportunity to demonstrate further that an exemption is proper. If the Board ultimately finds that an exemption should not be granted, notice of an adverse determination will be published in the Federal Register and a copy furnished to the applicant.

Revocation of Exemption

The Board reserves the right to revoke an exemption if at any time it determines that the standards required for an exemption are not met.

Before taking such action, the Board will notify the appropriate state official of its intent, and will afford the official such opportunity as it deems appropriate in the circumstances to demonstrate that revocation is improper. If the Board ultimately finds that revocation is proper, notice of the Board's intention to revoke such exemption will be published in the Federal Register with a reasonable period of time for interested persons to comment.

Notice of revocation of an exemption will be published in the Federal Register. A copy of such notice will be furnished to the appropriate state official and to the federal officials responsible for enforcement. Upon revocation of an exemption, creditors in that state shall then be subject to the requirements of the federal law.

***20908** Appendix C--Issuance of Staff Interpretations

Official Staff Interpretations

Officials in the Board's Division of Consumer and Community Affairs are authorized to issue official staff interpretations of this regulation. These interpretations provide the protection afforded under § 130(f) of the act. Except in unusual circumstances, such interpretations will not be issued separately but will be incorporated in an official commentary to the regulation which will be amended periodically.

Requests for Issuance of Official Staff Interpretations

A request for an official staff interpretation shall be in writing and addressed to the Director, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 20551. The request shall contain a complete statement of all relevant facts concerning the issue, including copies of all pertinent documents.

Scope of Interpretations

No staff interpretations will be issued approving creditors' forms, statements, or calculation tools or methods. This restriction does not apply to forms, statements, tools, or methods whose use is required or sanctioned by a government agency.

Appendix D--Multiple Advance Construction Loans

Section 226.17(c)(6) permits creditors to treat multiple advance loans to finance construction of a dwelling that may be permanently financed by the same creditor either as a single transaction or as more than one transaction. If the actual schedule of advances is not known, the following methods may be used to estimate the interest portion of the finance charge and the annual percentage rate and to make disclosures. If the creditor chooses to disclose the construction phase separately, whether interest is payable periodically or at the end of construction, Part I may be used. If the creditor chooses to disclose the construction and the permanent financing as one transaction, Part II may be used.

Part I--Construction period disclosed separately.

A. If interest is payable only on the amount actually advanced for the time it is outstanding:

1. Estimated interest--Assume that one-half of the commitment amount is outstanding at the contract interest rate for the entire construction period.

2. Estimated annual percentage rate--Assume a single payment loan that matures at the end of the construction period. The finance charge is the sum of the estimated interest and any prepaid finance charge. The amount financed for computation purposes is determined by subtracting any prepaid finance charge from one-half of the commitment amount.

3. Repayment schedule--The number and amounts of any interest payments may be omitted in disclosing the payment schedule under § 226.18(g). The fact that interest payments are required and the timing of such payments shall be disclosed.

4. Amount financed--The amount financed for disclosure purposes is the entire commitment amount less any prepaid finance charge.

B. If interest is payable on the entire commitment amount without regard to the dates or amounts of actual disbursement:

1. Estimated interest--Assume that the entire commitment amount is outstanding at the contract interest rate for the entire construction period.

2. Estimated annual percentage rate--Assume a single payment loan that matures at the end of the construction period. The finance charge is the sum of the estimated interest and any prepaid finance charge. The amount financed for computation purposes is determined by subtracting any prepaid finance charge from one-half of the commitment amount.

3. Repayment schedule--Interest payments shall be disclosed in making the

repayment schedule disclosure under § 226.18(g).

BILLING CODE 6210-01-M

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***20912** Appendix E--Rules For Card Issuers That Bill on a Transaction-By-Transaction Basis

The following provisions of Subpart B apply if credit cards are issued and (1) the card issuer and the seller are the same or related persons; (2) no finance charge is imposed; (3) consumers are billed in full for each use of the card on a transaction-by-transaction basis, by means of an invoice or other statement reflecting each use of the card; and (4) no cumulative account is maintained which reflects the transactions by each consumer during a period of time, such as a month:

Section 226.6(d), and, as applicable, § 226.6(b) and (c). The disclosure required by § 226.6(b) shall be limited to those charges that are or may be imposed as a result of the deferral of payment by use of the card, such as late payment or delinquency charges.

Section 226.7(b) and § 226.7(k). Creditors may comply by placing the required disclosures on the invoice or statement sent to the consumer for each transaction.

Section 226.9(a). Creditors may comply by mailing or delivering the statement required by § 226.6(d) (See Appendix G-3) to each consumer receiving a transaction invoice during a one-month period chosen by the card issuer or by sending either the statement prescribed by § 226.6(d) or an alternative billing error rights statement substantially similar to that in Appendix G-4, with each invoice sent to a consumer.

Section 226.9(c).

Section 226.10.

Section 226.11. This section applies when a card issuer receives a payment or other credit that exceeds by more than $1 the amount due, as shown on the transaction invoice. The requirement to credit amounts to an account may be complied with by other reasonable means, such as by a credit memorandum. Since no periodic statement is provided, a notice of the credit balance shall be sent to the consumer within a reasonable period of time following its occurrence unless a refund of the credit balance is mailed or delivered to the consumer within 5 business days of its receipt by the card issuer.

Section 226.12 including § 226.12(c) and (d), as applicable. Section 226.12(e) is inapplicable.

Section 226.13, as applicable. All references to "periodic statement" shall be read to indicate the invoice or other statement for the relevant transaction. All actions with regard to correcting and adjusting a consumer's account may be taken by issuing a refund or a new invoice, or by other appropriate means consistent with the purposes of the section.

Section 226.15, as applicable.

Appendix F--Annual Percentage Rate Computations for Certain Open-End Credit Plans

In determining the denominator of the fraction under § 226.14(c)(3), no amount will be used more than once when adding the sum of the balances [FN1] subject to periodic rates to the sum of the amounts subject to specific transaction charges. In every case, the full amount of transactions subject to specific transaction charges shall be included in the denominator. Other balances or parts of balances shall be included according to the manner of determining the balance subject to a periodic rate, as illustrated in the following examples of accounts on monthly billing cycles:

FN1 Where a portion of the finance charge is determined by application of one or more daily periodic rates, the phrase "sum of the balances" shall also mean the "average of daily balances."

1. Previous balance--none.

A specific transaction of $100 occurs on the first day of the billing cycle. The average daily balance is $100. A specific transaction charge of 3% is applicable to the specific transaction. The periodic rate is 1 1/2 % applicable to the average daily balance. The numerator is the amount of the finance charge, which is $4.50. The denominator is the amount of the transaction (which is $100), plus the amount by which the balance subject to the periodic rate exceeds the amount of the specific transactions (such excess in this case is 0), totaling $100.

The annual percentage rate is the quotient (which is 4 1/2 %) multiplied by 12 (the number of months in a year), i.e., 54%.

2. Previous balance--$100.

A specific transaction of $100 occurs at the midpoint of the billing cycle. The average daily balance is $150. A specific transaction charge of 3% is applicable to the specific transaction. The periodic rate is 1 1/2 % applicable to the average daily balance. The numerator is the amount of the finance charge which is $5.25. The denominator is the amount of the transaction (which is $100), plus the amount by which the balance subject to the periodic rate exceeds the amount of the specific transaction (such excess in this case is $50), totaling $150. As explained in example 1, the annual percentage rate is 3 1/2 % x 12 = 42%.

3. If, in example 2, the periodic rate applies only to the previous balance, the numerator is $4.50 and the denominator is $200 (the amount of the transaction, $100, plus the balance subject only to the periodic rate, the $100 previous balance). As explained in example 1, the annual percentage rate is 2 1/4 % x 12 = 27%.

4. If, in example 2, the periodic rate applies only to an adjusted balance (previous balance less payments and credits) and the consumer made a payment of $50 at the midpoint of the billing cycle, the numerator is $3.75 and the denominator is $150 (the amount of the transaction, $100, plus the balance subject to the periodic rate, the $50 adjusted balance). As explained in example 1, the annual percentage rate is 2 1/2 % x 12 = 30%.

5. Previous balance--$100.

A specific transaction (check) of $100 occurs at the midpoint of the billing cycle. The average daily balance is $150. The specific transaction charge is $.25 per check. The periodic rate is 1 1/2 % applied to the average daily balance. The numerator is the amount of the finance charge, which is $2.50 and includes the $.25 check charge and the $2.25 resulting from the application of the periodic rate. The denominator is the full amount of the specific transaction (which is $100) plus the amount by which the average daily balance exceeds the amount of the specific transaction (which in this case is $50), totaling $150. As explained in example 1, the annual percentage rate would be 1 2/3 % x 12 = 20%.

6. Previous balance--none.

A specific transaction of $100 occurs at the midpoint of the billing cycle. The average daily balance is $50. The specific transaction charge is 3% of the transaction amount or $3.00. The periodic rate is 1 1/2 % per month applied to the average daily balance. The numerator is the amount of the finance charge, which is $3.75, including the $3.00 transaction charge and $.75 resulting from application of the periodic rate. The denominator is the full amount of the specific transaction ($100) plus the amount by which the balance subject to the periodic rate exceeds the amount of the transaction ($0). Where the specific transaction amount exceeds the balance subject to the periodic rate, the resulting number is considered to be zero rather than a negative number ($50-$100=-$50). The denominator, in this case, is $100. As explained in example 1, the annual percentage rate is 3 3/4 % x 12 = 45%.

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***20934** Appendix I--Federal Enforcement Agencies

The following list indicates which federal agency enforces Regulation Z for particular classes of businesses. Any questions concerning compliance by a particular business should be directed to the appropriate enforcement agency.

National Banks

Office of Customer and Community Programs, Comptroller of the Currency, Washington, D.C. 20219.

State Member Banks

Federal Reserve Bank serving the district in which the State member bank is located.

Nonmember Insured Banks

Federal Deposit Insurance Corporation Regional director for the region in which the nonmember insured bank is located.

Savings Institutions Insured by the FSLIC and Members of the FHLB System (Except for Savings Banks Insured by FDIC)

The Federal Home Loan Bank Board Supervisory Agent in the district in which the institution is located.

Federal Credit Unions

Regional office of the National Credit Union Administration serving the area in which the federal credit union is located.

Creditors subject to Civil Aeronautics Board

Director, Bureau of Consumer Protection, Civil Aeronautics Board, 1825 Connecticut Avenue, N.W., Washington, D.C. 20428.

Creditors Subject to Packers and Stockyards Act

Nearest Packers and Stockyards Administration area supervisor.

Federal Land Banks, Federal Land Bank Associations, Federal Intermediate Credit Banks and Production Credit Associations

Farm Credit Administration, 490 L'Enfant Plaza, S.W., Washington, D.C. 20578.

Retail, Department Stores, Consumer Finance Companies, All Other Creditors, and All Nonbank Credit Card Issuers (Creditors operating on a local or regional basis should use the address of the FTC Regional Office in which they operate.)

Division of Credit Practices, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

Appendix J--Annual Percentage Rate Computations for Closed-End Credit Transactions

(a) Introduction. (1) Section 226.22(a) of Regulation Z provides that the annual percentage rate for other than open end credit transactions shall be determined in accordance with either the actuarial method or the United States Rule method. This appendix contains an explanation of the actuarial method as well as equations, instructions and examples of how this method applies to single advance and multiple advance transactions.

(2) Under the actuarial method, at the end of each unit-period (or fractional unit-period) the unpaid balance of the amount financed is increased by the finance charge earned during that period and is decreased by the total payment (if any) made at the end of that period. The determination of unit-periods and fractional unit-periods shall be consistent with the definitions and rules in paragraphs (b) (3), (4) and (5) of this section and the general equation in paragraph (b)(8) of this section.

(3) In contrast, under the United States Rule method, at the end of each payment period, the unpaid balance of the amount financed is increased by the finance charge earned during that payment period and is decreased by the payment made at the end of that payment period. If the payment is less than the finance charge earned, the adjustment of the unpaid balance of the amount financed is postponed until the end of the next payment period. If at that time the sum of the two payments is still less than the total earned finance

charge for the two payment periods, the adjustment of the unpaid balance of the amount financed is postponed still another payment period, and so forth.

(b) Instructions and equations for the actuarial method. (1) General rule. The annual percentage rate shall be the nominal annual percentage rate determined by multiplying the unit-period rate by the number of unit-periods in a year.

(2) Term of the transaction. The term of the transaction begins on the date of its consummation, except that if the finance charge or any portion of it is earned beginning on a later date, the term begins on the later date. The term ends on the date the last payment is due, except that if an advance is scheduled after that date, the term ends on the later date. For computation purposes, the length of the term shall be equal to the time interval between any point in time on the beginning date to the same point in time on the ending date.

(3) Definitions of time intervals. (i) A period is the interval of time between advances or between payments and includes the interval of time between the date the finance charge begins to be earned and the date of the first advance thereafter or the date of the first payment thereafter, as applicable.

(ii) A common period is any period that occurs more than once in a transaction.

(iii) A standard interval of time is a day, week, semimonth, month, or a multiple of a week or a month up to, but not exceeding, 1 year.

(iv) All months shall be considered equal. Full months shall be measured from any point in time on a given date of a given month to the same point in time on the same date of another month. If a series of payments (or advances) is scheduled for the last day of each month, months shall be measured from the last day of the given month to the last day of another month. If payments (or advances) are scheduled for the 29th or 30th of each month, the last day of February shall be used when applicable.

(4) Unit-period. (i) In all transactions other than a single advance, single payment transaction, the unit-period shall be that common period, not to exceed 1 year, that occurs most frequently in the transaction, except that

(A) If 2 or more common periods occur with equal frequency, the smaller of such common periods shall be the unit-period; or

(B) If there is no common period in the transaction, the unit-period shall be that period which is the average of all periods rounded to the nearest whole standard interval of time. If the average is equally near 2 standard intervals of time, the lower shall be the unit-period.

(ii) In a single advance, single payment transaction, the unit-period shall be the term of the transaction, but shall not exceed 1 year.

(5) Number of unit-periods between 2 given dates. (i) The number of days between 2 dates shall be the number of 24-hour intervals between any point in time on the first date to the same point in time on the second date.

(ii) If the unit-period is a month, the number of full unit-periods between

2 dates shall be the number of months measured back from the later date. The remaining fraction of a unit-period shall be the number of days measured forward from the earlier date to the beginning of the first full unit-period, divided by 30. If the unit-period is a month, there are 12 unit-periods per year.

(iii) If the unit-period is a semimonth or a multiple of a month not exceeding ***20935** 11 months, the number of days between 2 dates shall be 30 times the number of full months measured back from the later date, plus the number of remaining days. The number of full unit-periods and the remaining fraction of a unit-period shall be determined by dividing such number of days by 15 in the case of a semimonthly unit-period or by the appropriate multiple of 30 in the case of a multimonthly unit-period. If the unit-period is a semimonth, the number of unit-periods per year shall be 24. If the number of unit-periods is a multiple of a month, the number of unit-periods per year shall be 12 divided by the number of months per unit-period.

(iv) If the unit-period is a day, a week, or a multiple of a week, the number of full unit-periods and the remaining fractions of a unit-period shall be determined by dividing the number of days between the 2 given dates by the number of days per unit-period. If the unit-period is a day, the number of unit-periods per year shall be 365. If the unit-period is a week or a multiple of a week, the number of unit-periods per year shall be 52 divided by the number of weeks per unit-period.

(v) If the unit-period is a year, the number of full unit-periods between 2 dates shall be the number of full years (each equal to 12 months) measured back from the later date. The remaining fraction of a unit-period shall be

(A) The remaining number of months divided by 12 if the remaining interval is equal to a whole number of months, or

(B) The remaining number of days divided by 365 if the remaining interval is not equal to a whole number of months.

(vi) In a single advance, single payment transaction in which the term is less than a year and is equal to a whole number of months, the number of unit-periods in the term shall be 1, and the number of unit-periods per year shall be 12 divided by the number of months in the term or 365 divided by the number of days in the term.

(vii) In a single advance, single payment transaction in which the term is less than a year and is not equal to a whole number of months, the number of unit-periods in the term shall be 1, and the number of unit-periods per year shall be 365 divided by the number of days in the term.

(6) Percentage rate for a fraction of a unit-period. The percentage rate of finance charge for a fraction (less than 1) of a unit-period shall be equal to such fraction multiplied by the percentage rate of finance charge per unit-period.

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***20941** Regulatory Analysis of Revised Regulation Z

This regulatory analysis, required under current Board policy concerning rulemaking, has been prepared following passage of the Truth-in-Lending Simplification and Reform Act (Title VI of the Depository Institutions Deregulation and Monetary Control Act of 1980, Public Law 96-211) and preparation by the Division of Consumer and Community Affairs of a draft of revised Regulation Z to implement the new act and make other changes.

Summary

The draft of revised Regulation Z prepared by staff of the Division of Consumer and Community Affairs would make major changes in the currently existing regulation. These proposed changes arise from two sources: (1) revisions in the regulation necessitated by passage of the Truth-in-Lending Simplification and Reform Act; and (2) staff proposals to simplify the existing regulatory structure further within the limits of discretion granted to the Board by the Truth-in-Lending Act.

The Simplification and Reform Act has resulted in five major kinds of proposed revisions in the Federal regulatory structure: (1) required disclosures have been reduced in number; (2) creditor compliance has been made easier in a number of ways, especially by providing model forms guaranteeing compliance if used properly; (3) civil liability of creditors has been limited to certain important disclosures; (4) the main burden of compliance enforcement has been shifted away relatively from the kinds of private actions that have contributed to complex rules and court decisions in the past and toward relatively greater reliance on administrative enforcement; and (5) certain complex legal questions that have produced conflicting court decisions in the past have been clarified. Staff efforts to simplify the regulation further have resulted in additional significant kinds of changes designed to: (1) provide clearer definitions and standards of applicability; (2) make good faith compliance easier by providing for small disclosure tolerances; (3) minimize necessity of disclosures unrelated to credit decisionmaking; (4) allow creditors greater flexibility in preparing disclosures to fit the nature of individual transactions; and (5) eliminate other complexities and ambiguities.

On balance, each of the major proposed changes in the regulatory structure should produce net consumer benefits by substantially reducing regulatory burden without sacrificing important consumer protections. Important consumer disclosures would be retained in the revised regulation, but the complexity of compliance with the Federal act and frequency of changes should be reduced. This should reduce the regulatory burden by reducing legal costs, printing expenses, employee training costs, and programming and computing expenditures. These gains would only be achieved at the expense of start-up costs. It is not possible with currently available data to estimate accurately either the long-term savings or the short-term costs associated with changing to the new requirements, but the available lead time of one year should help minimize the latter. Furthermore, it appears that long run cost reductions should outweigh the start-up costs. In this regard, possibly the most important single contribution of the new regulation is the provision of model forms that guarantee compliance with the Federal law if used properly.

I. Background

Truth in Lending, enacted by Congress as Title I of the Consumer Credit Protection Act of 1968 (Public Law 90-321, May 29, 1968), is an important element of Federal consumer protection policy in the credit area. In essence, the various Federal consumer credit protections established by Congress since 1968, including Truth in Lending, might be characterized as combining two general regulatory approaches, although in different combinations. The first approach is disclosure--requiring that certain information be disclosed to comsumers in a prescribed manner. Information disclosure is an important ingredient in most Federal consumer credit protections; but it is so essential to some, including Truth in Lending, the Real Estate Settlement Procedures Act (1974), the Home Mortgage Disclosure Act (1975), the Consumer Leasing Act (1976), and the Electronic Funds Transfer Act (1978), that these acts might properly be classified as "information protections." In contrast, the second regulatory approach involves more than disclosure: it involves requiring institutions to do or not do certain things or act in certain ways in their relations with consumers in the marketplace. In these cases disclosures might also be required, but disclosures are subordinate in importance to other elements. As a result, these regulations might be classified better as "behavioral protections" or "market protections." Examples in the credit area include the Fair Credit Reporting Act (1970), the Fair Credit Billing Act (1974), the Equal Credit Opportunity Act (1974 and 1976), and the Fair Debt Collection Practices Act (1977). Each of these acts requires disclosures under certain circumstances, but their requirements governing the market conduct of institutions are more important.

On its face Truth in Lending (TIL) appears to be both a reasonable and simple idea, but in practice the problems have proven to be immense. The House, Senate, and Conference Committee Reports expressing the intentions of Congress reveal both the simplicity of the idea and the reason for its operational complexity. According to the Senate Report: [FN1]

FN1 United States Senate, Committee on Banking and Currency, Truth in Lending 1967, Report to Accompany S.5 (Washington: Government Printing Office, 1967), p. 1.

The basic purpose of the Truth-in-Lending bill is to provide a full disclosure of credit charges to the American consumer. The bill does not in any way regulate the credit industry nor does it prescribe ceilings on credit charges. Instead it requires that full disclosure of credit charges be made so that the consumer can decide for himself whether the charge is reasonable.

This passage makes it abundantly clear that Congress intended Truth in Lending to be a disclosure law and an information protection rather than a market protection. This notion is re-emphasized in many parts of the Committee Reports. However, this passage also reveals the genesis of many later problems with TIL exemplified by the concept of "full disclosure." Rather than concentrating on a few fundamental disclosures, Truth in Lending and Regulation Z have always required a much more extensive list. Apparently drafted under the assumption that more disclosure is necessarily better than less, TIL and Regulation Z have required disclosure of all information that conceivably might be useful to someone sometime. Together with the diversity of consumer credit transactions and the penalties for violating the law or regulation, this principle has contributed substantially to TIL's complexity.

Originally the Truth-in-Lending Act filled more than 13 printed pages in the

Conference Committee Report and included 30 separate sections. In addition, the original Regulation Z filled 30 pages in 98 separate sections plus a supplement booklet dealing with APR calculations. Moreover, Truth in Lending was amended in 1970, 1974, twice in 1976, and in 1978; Regulation Z was amended many times between July 1, 1969, and March, 1980. By early 1980 the Act filled 20 printed pages in 52 numbered sections, many with lengthy ***20942** subdivisions. The regulation measured 53 printed pages in 153 highly technical sections (many with subsections) plus the APR supplement.

However, probably most indicative of the difficulties surrounding TIL is the number of times that Regulation Z has been interpreted, both administratively and by the courts. By early 1980 more than 1500 interpretations had been published by the Federal Reserve Board and staff, with varying degrees of legal authority. In addition, by June 30, 1979, more than 13,000 TIL lawsuits had been filed in Federal courts, representing 2 per cent of the Federal civil caseload (but up to 50 per cent of the cases in some districts). [FN2] This almost continuous stream of amendments, interpretations, and court decisions, along with interacting changes in state laws affecting such things as rate ceilings and security interests, produced a situation where total compliance was very difficult, at best. As long as 9 years after the effective date of the Act (July 1, 1969), the Federal bank regulatory agencies reported that more than 80 per cent of banks were not wholly in compliance, although most violations were judged "nonsubstantive" or "technical." [FN3] By the late 1970's the legal situation became somewhat ironic in that much of the litigation over Truth in Lending concerned aspects of disclosures apart from credit cost disclosures, the critical elements of Truth in Lending according to Congress. Notable among disputed areas in the late 1970's were identity of the creditor, security interest issues, disclosure of loan proceeds, acceleration clause issues, and issues of rescission. [FN4]

FN2 Source: Administrative Office of the United States Courts.

FN3 Board of Governors of the Federal Reserve System, Annual Report to Congress on Truth in Lending for the year 1978 (January 3, 1979), pp. 10-11.

FN4 For a concise review of the issues and cases in these areas see David S. Willenzik, "Truth in Lending Litigation, Specific Problem Areas," Journal of Retail Banking, June 1979.

As a result of the difficult legal conditions surrounding Truth in Lending a movement to "simplify" the law gained support in the second half of the 1970's. "Simplification" is, of course, a concept that is relatively easy to support in principle, although strong differences may develop when the concept is defined more closely. Possibilities include: a more clearly worded statute, a less restrictive statute, fewer required disclosures, easier to read forms, less information-packed forms, reduced liability for creditors, additional defenses (for creditors or consumers), greater preemption of state laws, a shorter regulation, a clearer regulation, fewer interpretations, more but clearer interpretations, and so forth. Nevertheless, by mid-1977 the idea of "simplifying" Truth in Lending had gained a measure of bipartisan support in the United States Senate, even if not complete agreement on details. [FN5] Four bills were introduced in the 95th Congress in 1977, and after extensive hearings and markup sessions, a bill was reported out by the Senate Banking Committee and passed by the Senate on May 10, 1978. However, the House took no action in the 95th Congress and the bill was reintroduced in the 96th Congress in 1979. After another hearing the bill passed the Senate again in May, 1979, and eventually (with some amendments) the Truth in Lending Simplification and Reform Act was incorporated into the Depository Institutions Deregulation and Monetary Control Act of 1980 (Pub. L. 96-221), which was signed by the President on March 31. Shortly afterward, on May 5, 1980, the Federal Reserve Board issued for public comment a complete redraft of Regulation Z to implement the new Act.

FN5 See United States Senate, Committee on Banking, Housing and Urban Affairs, Simplify and Reform the Truth in Lending Act, Hearings on S. 1312, S. 1501, and S. 1653, July 11-13, 1977 (Washington: Government Printing Office, 1977).

II. Framework for Evaluation

Regulatory analysis of the draft of revised Regulation Z ultimately involves answering questions in two difficult areas. The first area involves comparing the new regulatory structure to the old: In particular, does the new structure improve upon and/or simplify the old, and what, if any, are the structural benefits of the new regulatory approach This question is examined in Section III. The second area concerns the new regulatory structure as an information protection: Specifically, is the new approach likely to affect consumers' information needs in the credit area or have other impacts on the goals of Truth in Lending This question forms the subject matter of Section IV.

III. Regulatory Structure

1. Changes Required by the Simplification and Reform Act. The Truth-in-Lending Simplification and Reform Act made extensive changes in the Truth-in-Lending Act. According to the Senate Committee on Banking, Housing, and Urban Affairs, which drafted the Reform Act, the Committee's efforts were focused on four general areas: "providing the consumer with simpler, more understandable information; making compliance easier for creditors; limiting creditor civil liability for statutory penalties to only significant violations; and strengthening administrative restitution enforcement of the act." [FN6] A fifth area concerned technical changes to eliminate legal problems that had arisen from inconsistent decisions among Federal district courts. Substantive changes were made in each of the five areas.

FN6 United States Senate, Committee on Banking, Housing, and Urban Affairs, Truth in Lending Simplification and Reform Act, Report to Accompany S. 108 (Washington: Government Printing Office, 1979), p. 3.

Table I lists major kinds of changes made in each of these areas by the Simplification and Reform Act and reflected in the draft of revised Regulation Z. As can be seen, the Simplification Act made such fundamental changes in each area that the 1980 amendments might be characterized better as producing a new Truth-in-Lending Act than merely as amending the old act. For example, among the important changes the number of disclosures has been reduced and the format changed, model forms have been required and other changes have been made to aid compliance, civil penalties have been limited to key disclosures, and enforcement provisions have been altered. Because changes in these and other areas of the act are so substantial, major changes are also required in Regulation Z.

Table I--Areas of Change in Draft Regulation Z Arising From the Truth-In-

Lending Simplification and Reform Act

1. Changes to Provide Consumers with Simpler, More Understandable Information:

A. Reduction in the absolute number of disclosures, especially by reducing itemizations on closed-end credit.

B. Providing that supplemental information may not be intermingled with Truth-In-Lending disclosures.

C. Providing for short descriptive phrases to accompany numerical disclosures.

D. Providing that residential first mortgage disclosures be given at some time as Real Estate Settlement Procedures Act (RESPA) disclosures.

2. Changes to Make Compliance Easier for Creditors:

A. Reduction in the absolute number of disclosures.

B. Requiring that the Federal Reserve promulgate model forms which would guarantee compliance if filled in properly.

C. Providing that all amendments or interpretations requiring forms changes ***20943** become effective on October 1 of each year, with at least six months notice.

D. Providing for true tolerances of 1/8 percent for annual percentage rate disclosures and for wider tolerances on complex transactions under regulations of the Board.

3. Changes Affecting Civil Liability Provisions:

A. Limiting creditors' liability for statutory penalties to only those disclosures regarded as being of central importance.

B. Extending the period during which a creditor can "cure" a violation and avoid civil penalties from 15 days to 60 days after discovery.

C. Providing that "discovery" of errors might be due to examination agency reports without cutting off the time period to cure.

D. Extending "bona fide error" defense to good faith calculation, computer, and printing errors as well as to clerical errors.

4. Changes to Strengthen Administrative Restitution Enforcement:

A. Requiring administrative agencies to order refunds when finance charges or APR's are understated and when errors are part of a clear pattern or practice, are the result of gross negligence, or are willful.

B. Providing for some administrative discretion in ordering restitution, except for willful violations.

5. Changes to Clarify Legal Issues:

A. Clarification concerning creditor responsible for disclosures on transactions involving more than one institution.

B. Clarification concerning adequate disclosure of security interests.

C. Clarification concerning disclosure of acceleration clauses.

D. Clarification concerning disclosure of right of rescission on certain transactions.

Beyond the specifics of the kinds of changes listed in Table I, the extent of the alterations in the act and regulation indicates some fundamental shifts in regulatory approach. One shift involves a movement away from the concept of full disclosure of everything as a Federal Truth-in-Lending matter. Rather, the new act and draft regulation concentrate on requiring fewer disclosures, especially those believed to be most important to most consumers. The idea behind this change is that beyond these critical disclosures, regulatory burden increases faster than the usefulness of the disclosures to consumers. A second shift involves significant attempts at relieving the most burdensome compliance problems for creditors, especially by providing model forms that will guarantee compliance if used properly. A third shift moves enforcement efforts away relatively from private court suits for civil penalties and focuses enforcement effort on administrative actions by government agencies. This change was designed to help slow the flow of court decisions that has required creditors constantly to be aware of potential changes in disclosure standards and which, on occasion, has produced differing disclosure standards among judicial districts.

2. Other Changes Proposed. Besides changes in Regulation Z mandated by the Simplification and Reform Act, the staff draft of revised Regulation Z reflects a large number of other proposed changes, which are listed in Table II. These changes are intended to provide additional simplifications in disclosure procedures so as to provide clearer standards, eliminate complexities, and provide a greater degree of flexibility in a regulation that had become quite inflexible. However, because each of the changes involves a tradeoff between full precise disclosures (which may be complex and difficult to make and understand) and simpler disclosures (that may be less complete or precise even if more understandable), some of the changes may be controversial. Nevertheless, the changes proposed appear consistent with the Congressional mandate for regulatory simplification.

Table II--Areas of Change in Draft Regulation Z Arising From Staff Attempts to Simplify the Regulatory Structure

1. Changes Designed to Provide Clearer Standards Concerning Applicability of Provisions of the Regulation:

A. Definition of creditor subject to regulation is make more precise by providing a standard stated in terms of number of annual credits (25, or 5 real estate credits) rather than a standard in terms of "ordinary course of business."

B. Coverage of credit where there is no finance charge is limited to written agreements, thereby excluding informal installment agreements often offered by physicians and other professionals and tradesmen.

C. Definition of "consummation" before which disclosures must be made is made more precise by defining it as the point in time when a contractual obligation is established rather than when a vaguer "economic incentive" to go forward is established.

D. Determination that disclosures be based on legally enforceable obligation rather than on any informal agreement that may be at variance with the enforceable agreement.

E. Exclusion of sellers' points from the finance charge on real estate transactions thereby obviating need to determine whether sale price of property was raised to include sellers' points.

2. Changes Designed to Make Good Faith Disclosures Easier Through Greater Availability of Small Tolerances:

A. Provision for tolerance on disclosure of finance charges equal to tolerance for disclosure of annual percentage rates (1/8 of 1 percent).

B. Provisions for wider tolerance of 1/4 of 1 percent on irregular transactions involving multiple advances or irregular payments.

C. Provision that slight changes in a transaction from good faith estimated disclosures do not necessitate full redisclosure.

D. Elimination of terminology requirements other than "annual percentage rate" and "finance charge" in open-end credit disclosures.

3. Changes Designed to Highlight Disclosures Relevant to Credit Decisionmaking:

A. Narrowing of definition of security interest that must be disclosed to exclude items such as proceeds of insurance that typically are unrelated to credit decisions but which have contributed to litigation and ambiguity.

B. Limiting the frequency of need for complete redisclosure when terms are changed.

C. Limiting necessity of disclosure on assumption of an obligation to the case of residential mortgages.

4. Changes Designed to Eliminate Complexities:

A. Exclusion from disclosure requirements of such transactions as utility "budget plans" and "layaway" plans that have some elements of a credit transaction but which, strictly speaking, are not credit.

B. Elimination of three-day waiting period on credit secured by residence if consumer certifies in writing (preprinted forms prohibited) that a bona fide personal financial emergency exists.

C. Elimination of need to consider compensating balances in annual percentage rate calculation.

D. Exclusion of debit cards attached to deposit accounts with check overdraft features from certain credit card requirements.

5. Changes Designed to Allow Creditor Flexibility in Preparing Disclosures to Fit the Nature of the Transaction in Question:

A. Allowing the creditor in a variable rate transaction to prepare the required ***20944** example in a way that fits the specific transaction.

B. Allowing the creditor in a transaction involving multiple credit advances to prepare disclosures that fit the specific transaction.

C. Allowing creditors flexibility either to include or exclude in disclosures any cash rebates offered by the creditor or a manufacturer.

D. Allowing creditors more flexibility in showing repayment schedules in credit advertising.

3. Evaluating the New Regulatory Structure. Ultimately, the regulatory structure associated with Truth in Lending, like the regulatory and administrative apparatus associated with other consumer-oriented legislation, should be evaluated in terms of its contributions to (or detractions from) (1) market efficiency and (2) consumer protection. However, in the case of TIL these criteria are especially closely related. Truth in Lending is largely an information protection, and the main purpose of information protections is to improve the functioning of markets. Unlike behavioral or market protections (like Equal Credit Opportunity) that involve direct governmental interventions to affect market behavior of participants (especially businesses), the impact of information protections is more indirect. Instead of directly altering behavior, information protection assist consumers by improving the quality or efficiency of markets.

Markets are, of course, mechanisms for exchanging goods, services, or resources for value; and the concept of efficiency refers, in a sense, to the smoothness of the exchange mechanism. The concept has two components. The first, operational efficiency, concerns the mechanics of the transfer process itself. In particular, operational efficiency refers to the ability of a market to facilitate the transfer of goods or resources without loss of real resources to the transfer mechanism. Viewed in this manner, Truth in Lending and Regulation Z certainly introduce a measure of operational inefficiency into consumer credit markets by raising creditors' costs that must be paid by consumers. However, this is only half of the question.

The second component of market efficiency is allocational efficiency. Allocational efficiency refers to the extent to which markets allocate resources to their best uses. It has both a supply side and a demand side. From the supply side the question for TIL is whether the regulatory structure interferes with market allocation of resources to areas of highest return for a given risk. In contrast, from the demand or consumer side (the focus of this analysis) the question is whether the TIL regulatory structure helps consumers obtain resources at least cost for a given level of credit risk. Stated in this manner the relationship between market efficiency and consumer protection is more apparent: The concept of efficiency means best value for expenditure; this is precisely the intent of an information protection.

Unfortunately, because of the number of different kinds of costs involved, the amount of operational inefficiency introduced by the TIL regulatory structure is very difficult to measure. As a result, little statistical information is available and no broad-based cost analyses have been prepared.

Nevertheless, despite these gaps in the record, it is still possible to indicate some cost-causing aspects of the regulatory apparatus and to make some comparisons of the old regulatory environment with the new. [FN7]

FN7 To a great extent the following discussion in this section concerns changes in Federal Truth in Lending only and is contingent upon validity of the assumption that implementation of the new Truth-in-Lending Act, including its new standards for preemption of state disclosure laws, will not have the effect of requiring creditors to make additional disclosures and incur additional liability under existing state statutes. Since this assumption is dependent upon certain Board actions, as well as upon possible actions by state legislatures and by state and Federal courts, the analysis and conclusions offered in this section may be subject to revisions, which could be substantial. This issue is discussed more fully in Appendix A.

A number of kinds of costs are incurred by creditors (and ultimately by consumers) as a result of Truth in Lending. In addition, each type of costs recurs (to a greater or lesser extent depending on the situation) whenever changes are made in the act or regulation. Before passage of the Simplification Act, frequent changes and interpretations of the regulation caused major compliance problems for creditors. Since one purpose of the new act is to reduce frequency of changes in the future, it should reduce costs in the long run. Nevertheless, to achieve these long-run advantages, substantial start-up costs will be incurred as the entire regulatory structure is changed. Delaying the effective date for one year and allowing transition to the new methods at any time during the year should reduce start-up costs relative to those of a more rapid implementation schedule.

A first group of costs associated with Truth in Lending is legal expenses. Legal expenses arise from a number of sources and problems. One source is the cost of designing disclosure forms that suit the credit programs of individual creditors but which also comply with Regulation Z. On some kinds of transactions (for example, large secured credit sales) required disclosures were quite complex prior to the Simplification Act, so legal preparation had to be quite detailed. Reduced disclosure requirements and issuance of model forms should help reduce costs in this area in the future. Likewise, the new regulatory structure should reduce the legal expenses of constant re-evaluation of disclosures, to the extent the act is successful in reducing frequency of changes and interpretations.

Another source of legal costs is litigation expenses. Truth in Lending has produced a substantial number of court cases, each of which requires legal attention. Unreported are the number of cases where some accommodation or settlement is reached without the formality of filing and litigating a suit. Expenses can be sizeable in either case, especially if plaintiffs' legal expenses are awarded as well. The simplified Truth-in-Lending Act and Regulation Z should reduce legal expenses of these kinds. Because compliance with the act has been made easier, legal expenses for both analysis and litigation should eventually be reduced, possibly after a spurt associated with implementing the new requirements.

A second TIL cost is the cost of forms and printing. After design, complying forms typically are printed by a commercial printer. As a result, any change in requirements necessitates not only new legal analysis, but new printing expenditures as well. Furthermore, often overlooked, a change in forms requires that all obsolete forms be retrieved or otherwise destroyed. For a large creditor with multiple branches and possibly hundreds or thousands of employees, this requirement can involve substantial effort. Again, the new regulatory structure should reduce costs in this area. Besides minimizing the need and likelihood of rapid changes in disclosure requirements, the new rules specify that forms changes will be required no more than once per year. In 1977 the Commission on Federal Paperwork estimated this provision alone would reduce costs by $600 million annually. [FN8]

FN8 Commission on Federal Paperwork, Consumer Credit Protection (Washington: Government Printing Office, 1977).

A third cost is the cost of employee training. If legal requirements change frequently and employees must be trained and retrained to use new forms correctly, substantial costs may result. ***20945** Partially in response to this problem, but also for other reasons of management control, some creditors have instituted automated computer-processed TIL disclosure forms in recent years. Rather than relying on employees to fill in changing disclosure forms correctly, some creditors have programmed their computers to supply disclosures through terminals in branches or stores. However, computers must be purchased or leased and programmed, so computer-related expenses constitute a fourth group of TIL costs. Actually, this category of costs should probably be expanded to encompass all kinds of calculating-disclosing aids including charts, tables, and calculators as well as computers. Since, to some extent, there is a tradeoff between sophistication of employees and extensiveness of calculation aids, training expenses and calculating-computing expenses might be added together in evaluating TIL. Nevertheless, regardless of how they are apportioned, costs associated with training and calculating should be reduced by the new regulatory structure, after an initial start-up phase.

Other TIL-related costs include the actual costs of disclosing required information and the costs of record retention. Actual costs of disclosing rates and other information are probably not very great on closed-end credit, given that terms must be negotiated or specified and contractual documents are prepared and signed anyway. Costs of disclosing on standard types of contracts consist of calculating the necessary information, placing it on the disclosure forms and handing the forms to consumers. Once the necessary legal judgments are made, forms prepared, employees trained and computers programmed (or charts and tables purchased) disclosures are not especially difficult or time consuming, as long as no changes are made in the procedures. On open-end credit finance charges must be disclosed on periodic statements (usually monthly); but, typically, the calculations would be made anyway since the disclosure statement also constitutes the periodic billing statement. The new act and regulation do not make substantive changes in the methods of actually making disclosures and so substantial cost savings are not expected from this source. Likewise, the new regulatory structure retains the earlier requirements on record retention (for compliance purposes), although retaining files can be costly. In 1977 the Commission on Federal Paperwork estimated that storage, filing, and clerical expense of maintaining files could amount to 16 cents per file. However, since creditors would be expected to keep files for a time anyway, not all of this expenditure can be attributed to TIL or other regulations. Nevertheless, Regulation Z requires that copies of disclosure statements be retained for 24 months which is beyond the closing date of many accounts. This requirement is not changed by the new regulation.

Reductions in all of these cost areas should ease burdens of complying with the Federal act for all creditors. However, some provisions of the new law may be especially important to smaller creditors. In particular, the provision of model forms should lessen legal costs associated with designing disclosure forms. In addition, less frequent changes in the regulation and less frequent interpretations should reduce burden for institutions with limited staff. While not specifically designed to benefit small creditors, the new Regulation Z is consistent with the purposes of the Regulatory Flexibility Act.

In sum, the new TIL regulatory structure should lead to lower compliance costs, thereby improving operational efficiency of credit markets. To the extent these gains can be achieved without sacrificing consumer protections, the new regulatory environment should produce a net gain for society as a whole through a more efficient market. However, before this conclusion is reached it is necessary, first, to examine TIL as an information protection. This topic forms the subject matter of Part IV.

IV. Truth in Lending as an Information Protection

1. Potential Evaluative Criteria. In evaluating the new Truth in Lending regulatory structure as an information protection, possibly the foremost concern is the need for an appropriate criterion or standard. The goal stated by Congress in Section 102 of the Act, avoidance of the "uninformed use of credit," is undoubtedly the Act's central purpose and a goal consistent with market efficiency, but measurement is subject to severe definitional and methodological difficulties. As a result, proxies are needed. Examination of the behavioral science literature as well as Congressional hearings and statements and the literature on Truth in Lending itself reveals that a large number of consumer-protection goals have been suggested as standards for TIL. Thirty-nine possible goals for Truth in Lending in nine separate categories are listed in Table III. There are probably also other goals that might be added to the list. However, the length of this table reveals the same difficulties in evaluating TIL as a consumer protection and the reason why simple tests are probably inadequate. Nevertheless, a few general principles might be stated.

Table III--Goals of Truth in Lending

I. General Philosophical or Educational Goals

1. Satisfy Consumers' Right to Know

2. Enhance Consumer Education

3. Enhance Consumers' General Understanding of the Credit Process

4. Promote Long-Term Rise in Consumer Sophistication

5. Promote the Informed Use of Credit

6. Promote Wiser Credit Use

II. Goals Associated with Improving Consumer Decisionmaking

7. Reduce Credit Search Costs

8. Simplify Information Processing

9. Improve Consumers' Ability to Make Conparisons [FN1] N

FN1 Referred to as the "Shopping Function" by the National Commission on Consumer Finance.

10. Enable Consumers to Match Products and Needs

11. Enable Consumers to Decide Between Using Credit and Using Liquid Assets [FN2] N

FN2 Referred to as the "Descriptive Function" by the National Commission on Consumer Finance.

12. Enable Consumers to Decide Between Using Credit and Delaying Consumption 2

13. Show Consumers Where Search Can Be Beneficial

III. Cognitive Goals: Awareness and Understanding

14. Improve Awareness of Credit Costs

15. Improve Awareness of Non-Cost Credit Terms

16. Improve Awareness of Differences Among Classes of Institutions

17. Improve Consumers Understanding of the Relationships Among Credit Cost Terms

IV. Behavioral Goals

18. Encourage Credit Shopping

V. Attitudinal Goals

19. Improve Consumer Satisfaction

20. Improve Consumer Confidence

VI. Credit Market Goals

21. Enhance Competition in Consumer Credit Markets

22. Drive Out High-Cost Producers

23. Encourage Industry to Reform

24. Improve Credit Market Products

25. Discourage Risk Shifting by Institutions

26. Discourage In Terrorem Boilerplate Clauses in Contracts

27. Provide Vehicle for Legal Reforms.

28. Protect Legitimate Businesses from Unethical Competition

***20946** VII. Institutional Control Goals

29. Promote Control of Institutions Through Compliance Requirements

30. Improve Consumers' Bargaining Position Relative to Institutions

31. Provide Defenses for Consumers

32. Provide Leverage for Hard-Pressed Debtors

VIII. Macroeconomic Goals

33. Enhance Economic Stabilization

IX. "Behavioral" or "Market Protection" Goals

34. Require Procedures for Credit Card Billing Error Resolution

35. Provide Protections for Consumer Leasing

36. Provide "Cooling Off" Period for Credit Secured By Residence

37. Provide "Cooling Off" Period for Credit Negotiated in Consumer's Home

38. Provide for Limited Liability on Lost or Stolen Credit Cards

39. Eliminate Unsolicited Credit Cards

First, TIL as a consumer protection cannot be evaluated fully by examining only a single behavioral measure like credit shopping. Behavioral goals are only one of nine categories in Table III, and encouraging shopping is only one of 39 goals listed. Consequently, evaluating TIL on shopping alone, or for that matter on any single criterion, is likely to produce an incomplete analysis of the impact of this information protection. As a corollary, if it is not appropriate to evaluate TIL on only one criterion, then it seems inappropriate to recommend wholesale changes in the protection based on a single criterion. At a minimum any proposed changes should be evaluated in terms of the likely effects on a variety of goals. Again, the shopping criterion provides a useful example; it simply may not be reasonable to make wholesale changes in the regulatory structure to encourage shopping unless either the changes simultaneously encourage other goals as well or the changes can be made at small cost. If costs are large or impacts on other goals are small, then there exists the possibility of achieving small gains in allocational efficiency at the expense of large losses of operational efficiency. This could produce a net loss for society as a whole.

Second, some goals do not suggest any measurable evaluative criteria and must be evaluated indirectly. Probably the general philosophical and educational goals in Category I of the table offer the best examples. The six goals listed there are almost universally recognized as important aspects of TIL, but they appear too general for direct analysis and invite only indirect conclusions. However, it might be noted that if two disclosure programs each appear to satisfy these general goals but one also appears to satisfy other goals as well, or to satisfy the general goals at lower cost, then this method is preferable, other things equal.

Third, while some goals do offer evaluative criteria, the criteria may differ among individuals making it difficult to draw general conclusions. Many of the goals in Category II of the table illustrate this phenomenon. For example, goal number 10, improved ability to match products and needs, might be examined by studying choices made in the marketplace. The problem is that consumers' needs differ and, consequently, so will the choices made even under conditions of perfect information. Likewise, consumers faced with deciding between using credit and paying cash (goal number 11) will not all reach the same conclusion. In a world of perfect information some people will choose cash and others credit, depending on their individual circumstances. As result, a simple criterion related to likelihood of taking one behavioral path or the other cannot be expected to produce useful analytical results.

Fourth, some goals may be more costly than others, especially if special attempts are made to achieve them without regard to costs. Encouragement of credit shopping (number 18) has already been mentioned as a possible example, but there are others as well. One is number 17, improving consumers' understanding of the relationships among credit cost terms. Much of the complexity, litigation, and costliness of the original TIL Act and Regulation Z arose, in a sense, out of attempts to satisfy this goal with extensive, detailed TIL disclosure statements. Possibly a better approach might have been to consider whether the details were necessary to achieve the other 38 goals or whether a simpler, less costly approach might thave been sufficient.

2. Evidence on the Effects of Truth in Lending. Unfortunately, there is relatively little direct evidence available about the impact of TIL on most of the goals listed in Table III. Furthermore, since evidence must typically be gathered by surveys at discrete points in time, the evidence is always subject to potential methodological problems, particularly that alternative explanations of the results are available. [FN9] Nevertheless, it is still possible to suggest some general conclusions concerning TIL as an information protection.

FN9 For discussion of methodological issues see Lynn W. Phillips and Bobby J. Calder, "Evaluating Consumer Protection Programs: Part I, Weak But Commonly Used Research Designs," Journal of Consumer Affairs, Winter 1979, and Lynn W. Phillips and Bobby J. Calder, "Evaluating Consumer Protection Laws II: Promising Methods," Journal of Consumer Affairs, Summer 1980.

While little can be said definitively about the impact of TIL on the general philosophical and educational goals listed in Group I of Table III, as a concept it seems likely that TIL disclosures have fostered the general goals of satisfying the consumer's right to know and enhancing general educational aims. Similarly, it seems that consumers' general understanding of the credit process has probably been enhanced by TIL, and the law has probably contributed to increasing consumers' general sophistication over the long term. TIL has probably also supplied the tools for informed use of credit and wiser use of credit by consumers. Although these latter goals might seem quite similar at first glance, they are actually quite different since the second involves a value judgment concerning what is wise. To use an analogy from public health, it seems likely that required disclosures of warnings by the surgeon general about smoking have contributed to informed use of tobacco, although possibly not to wiser use among those still smoking. In the tobacco case the value judgment is fairly obvious but in the credit case it may be less so. Nevertheless, it seems likely that TIL has contributed to both more informed and wiser credit use, if only because it has provided necessary tools in the form of standardized disclosures and terminology.

In terms of this first group of TIL goals, the new regulatory structure provided by the Simplification Act and revised Regulation Z should, on balance, prove beneficial. The new structure should be as effective as the old in enhancing these general TIL goals, but it seems likely it will be able to do so at lower operational cost. As a result, the net effect appears positive, since the beneficial aspects of general consumer protection have not been sacrificed, but they will be achieved at lower cost to supplier, after an initial costly phase-in.

The second group of goals involve individual consumers' decision processes. Studying the impact on these goals is especially difficult since decisionmaking criteria vary among consumers. However, as with the first group of goals, it seems likely that the new regulatory environment is an improvement on balance over the old because consumer protections in this area have not been sacrificed, even though costs may be lowered in the ***20947** future. Probably of primary importance is TIL's requirement that rates be calculated in identical fashion regardless of credit source or type, a requirement that is retained in the new structure. This should be important, for example, in satisfying goal number 10, enabling consumers to match products and needs. Likewise, decisions about using cash or delaying consumption rather than using credit should be facilitated with standardized credit cost calculations available. Although survey evidence indicates that relatively few credit users are influenced by disclosures in their decision to take on debt, [FN10] some unanswered questions may be as important. These include the extent to which cash buyers are dissuaded from using debt by its cost and the extent to which consumers' attention to and sensitivity to finance rates has changed over time. Regardless of answers to these questions, it seems that TIL has provided consumers with the necessary tools, for whatever purpose they want to use them.

FN10 See George S. Day and William K. Brandt, A Study of Consumer Credit Decisions: Implications for Present and Prospective Legislation (Washington, Technical Studies of the National Commission on Consumer Finance, Vol. I, Government Printing Office, 1973).

Most research on the effects of TIL has been concentrated on the third group of goals in Table I (the Cognitive Goals) and especially on awareness of credit costs (goal number 14). Research attention has probably been focused in this area for two reasons. The first is that these goals, especially awareness of credit costs, offers a convenient operational evaluative criterion for testing. As a result, it is possible to draw conclusions without some of the kinds of complications associated with evaluating other goals. The second reason is the reasonable contention that cognition logically precedes use of information for decision making, and so evidence of awareness is an important preliminary evaluation. The argument is that since cognition precedes use, there must be awareness before use of information can be expected. Although evidence of awareness does not, by itself, demonstrate that information will be used, lack of awareness probably indicates that information cannot be used. Consequently, evidence of lack of impact of TIL on awareness could be taken as an indication the law had little impact in other areas either.

Surveys of consumers have indicated increasing levels of awareness of percentage rates of charge on credit transactions since implementation of Truth in Lending in 1969. Using an operational definition of awareness established by staff of the National Commission on Consumer Finance, surveys have revealed a sharp increase in awareness in the first 15 months of Truth in Lending and continuing gains afterward. [FN11] By 1977 levels of rate awareness reached 54 percent for closed-end credit and 65 percent and 71 percent for retail revolving credit and bank credit-card credit, up from 14 percent, 35 percent, and 27 percent, respectively, in 1969. Although many factors undoubtedly affect credit knowledge, including gradually higher educational levels over time, it appears reasonable to conclude that TIL has focused attention on percentage rates and contributed to the sharp increases in awareness.

FN11 See Thomas A. Durkin and Gregory E. Elliehausen, The 1977 Survey of Consumer Credit (Washington: Board of Governors of the Federal Reserve System, 1978).

In contrast, despite changes in awareness of percentage rates since 1969, available consumer surveys indicate that credit shopping by consumers is not especially common. For example, a nationwide survey in 1977 found that only about one quarter of those with outstanding closed-end credit accounts had tried to obtain information about other creditors or credit terms before obtaining the credit. [FN12] Furthermore, a majority of those with outstanding closed-end credit indicated that familiarity with the creditor or prior good experience was the primary reason for obtaining credit from the particular creditor they chose. However, lack of shopping does not necessarily indicate unreasonable or irrational behavior. On the contrary, failure to shop may indicate an awareness of costs on the part of the consumer and may reflect the view that further shopping is unwarranted. Consumers may be wrong in their judgments, of course, but it does not seem that, by itself, failure to shop indicates a failure of TIL. Probably more important for TIL evaluation are the questions whether the regulatory structure increases cost awareness and whether it permits effective shopping, if desired. The first of these questions has already been answered affirmatively, and the second answer seems positive as well. By establishing a consistent unit price and standards of terminology, TIL permits consumers to shop for credit to whatever extent they feel is appropriate.

FN12 1 Ibid., chapter 5.

The fifth group of TIL goals concerns improving consumers' confidence in and satisfaction with the credit process. It seems likely that consumers, knowing that creditors must disclose certain costs and terms accurately under the watchful eye of regulatory authorities, might increase their confidence in the integrity of an otherwise complex transaction. This confidence could produce consumer benefits beyond any immediate specific uses consumers make of the disclosed information. However, since obtaining these benefits does not require any specific uses of the information disclosed, this group of goals argues for a simple disclosure scheme. Rather than a highly technical regulation with strict requirements, this group of goals could be addressed with simple methods. Thus, on balance, the new regulatory structure should provide net benefits in this area. Since benefits in the form of improvements in confidence and satisfaction with the credit process should not be reduced under the new regulatory structure, but costs should be reduced in the long run, net benefits should result.

Limited longitudinal survey evidence indicates that consumers' attitudes toward credit have improved since passage of the original Truth in Lending Act. Furthermore, attitudes have improved more rapidly during the years 1967-77 than 1959-67. [FN13] Clearly, however, changes in attitudes over time cannot be attributed solely to any piece of legislation. Income growth and employment stability over time for many members of the public may partly explain improved attitudes toward credit use. Inflation, which tends to reward early purchases of goods and to penalize accumulations of savings in the form of liquid assets, may also affect attitudes toward credit. Nevertheless, there remains the possibility that consumer protection regulations have contributed to overall increases in consumers' satisfaction with the credit process. Since any gains in this area might be achieved just as well by simple rules, though, this group of goals offers arguments for regulatory simplification.

FN13 1 Ibid., chapter 10.

The sixth group of goals is the credit market goals. Taken together, these goals refer to improvements in credit markets that might result from a generally more competitive environment. These include, all other things equal, such things as lower market prices, discouragement of unfavorable contract devices that might need to be disclosed, and protection of legitimate businesses from unethical competitors that might employ deceptive pricing in the absence of TIL. These, of course, were important originals goal of Truth in Lending and were extensively ***20948** discussed in Congressional hearings before passage of the Act.

As with the other groups of goals, evaluating the credit market goals is difficult because of competing explanations for any market changes and lack of specific data. Other things equal, a requirement that businesses provide pricing information calculated in a uniform manner should make markets more competitive. However, the magnitude of any effect depends on answers to a number of questions. One question concerns the importance consumers attach to the information disclosed. In the area of credit terms, available evidence suggests that consumers regard cost terms as most important. [FN14] As a result, requiring disclosure of cost-related terms would be consistent with improving market competitiveness. Obviously, this does not imply that disclosures need be complex or difficult to prepare. A second question concerns current competitive conditions in consumer credit markets. If markets are already fairly competitive, then the gains from implementing or changing Truth in Lending to improve competitiveness are likely to be small. Evidence on consumer credit competition before Truth in Lending is scarce, although markets were assumed to be less than perfectly competitive. [FN15] In contrast, limited more recent evidence suggests that consumer credit markets are fairly competitive. [FN16] Although the precise impact of Truth in Lending in promoting competition cannot be determined, this finding may indicate that further changes in TIL are unlikely to produce substantial additional benefits from a more competitive market. Any benefits already provided by TIL, though, are unlikely to be lost under the new regulatory structure.

FN14 Ibid., chapter 4.

FN15 See National Commission on Consumer Finance, Consumer Credit in the United States: The Report of the National Commission on Consumer Finance (Washington, Government Printing Office, 1972).

FN16 See Gregory E. Boczar, "The Evidence on Competition Between Commercial Banks and Finance Companies, Journal of Bank Research, Summer 1975 and Gregory E. Boczar, "Competition Between Banks and Finance Companies: A Cross Section Study of Personal Loan Debtors," Journal of Finance, March 1978.

The seventh group of goals in Table I, the Institutional Control Goals, is probably the group most directly affected by the new regulatory structure. As outlined previously, the Senate Banking Committee's stated purposes in drafting the Truth in Lending Simplification and Reform Act included making compliance easier for creditors and strengthening administrative restitution enforcement authority. The latter purpose encourages goal number 29, but the former may discourage the others, especially numbers 31 and 32. It appears that the goals of providing defenses for consumers and leverage for hard-pressed debtors were not part of the original plans of Congress in 1969. Instead, they arose from the complexity of the regulatory structure that made it difficult for creditors always to be in complete technical compliance. Creditors instituting collection actions were resisted occasionally by debtors alleging Truth in Lending violations. Such actions could result in settlements or judgments for the debtor that might reduce or eliminate the debt. Under the new regulatory structure such situations should develop less often. Apparently believing that private enforcement of Truth in Lending had contributed to its growing complexity, Congress de-emphasized private enforcement in the Simplification Act and increased the importance of administrative enforcement actions. This change should reduce the importance of TIL as a defense or a device to obtain leverage over creditors and re-emphasize the original goals of Truth in Lending as an information protection.

The eighth category of goals, the Macroeconomic Goals, was discussed extensively in Congressional hearings before passage of the original act, but has received little attention since. The argument made in the Congressional hearings was that disclosure of finance charges and annual percentage rates would discourage consumers from using credit during an economic boom and encourage credit use in a depression, other things equal. Taken together these effects would encourage economic stabilization by helping dampen business cycles.

The argument that availability of credit cost information over the course of the business cycle might improve economic stabilization is consistent with economic theory. The question is the magnitude of the effect which depends on the degree of fluctuation in consumer credit rates, consumers' knowledge of and sensitivity to credit cost fluctuations, and the importance of other factors such as income changes or changes in expectations. If fluctuations in rates are small, if sensitivity to costs is low, or if the impact of other factors is quantitatively larger, then disclosure of rates would not have much impact on stabilization. Answers to these difficult questions are not essential for reviewing the new Truth in Lending regulatory structure because TIL has many goals of which macroeconomic stabilization is only one and clearly not the most important. Nevertheless, it is possible that regulatory rigidity in the past has limited creditors' willingness to change credit terms along with economic conditions. The new regulation should help minimize this problem by making compliance easier.

The final group of goals, the "Behavioral" or "Market Protection" Goals, do not generally concern Truth in Lending as an information protection; consequently, little will be said about them here. Furthermore, the new regulatory structure makes few changes in the market protection functions of TIL, and so potential impacts are not as great as they are in other areas.

V. Conclusion

In sum, it appears that the new regulatory structure resulting from passage of the Truth in Lending Simplification and Reform Act should result in net public benefits. Review of an extensive list of goals of TIL reveals that none of the original goals of the act will be affected adversely. However, consumer protections provided by the act ultimately should be available at less operational cost under the new structure, following start-up adjustment. An improvement in operational efficiency with no loss of allocational efficiency should lead to an improvement in the quality of the market, the goal of any information protection.

Appendix A: Preemption of State Disclosure Laws Patterned After Federal Truth in Lending

As indicated in section I of this regulatory analysis, the Senate Committee on Banking, Housing, and Urban Affairs, which drafted the Truth-in-Lending Simplification and Reform Act, included among its motives "making compliance easier for creditors (and) limiting creditor civil liability for statutory penalties to only significant violations." [FN17] To meet these goals the Committee bill recommended a substantial number of significant changes to Truth-in-Lendiing, many of which were enacted into law. [FN18] However, because Congress rejected outright preemption of state laws in the area of consumer credit disclosures, state laws which were modeled after Federal Truth in Lending--and which, consequently, were operationally redundant with only occasional impact on creditors' operations--may no longer ***20949** be parallel nor redundant. In those cases--in the absence of preemption by the Board under its authority contained in paragraph 111 of the Act or action by state legislatures--implementation of the new Federal Act may not decrease the number of required disclosures and the degree of regulatory burden.

FN17 United States Senate Committee, Report to Accompany S. 108, op. cit., page 3.

FN18 See Table I in this regulatory analysis, pages 9-10.

Discussion

In the years following enactment of the original Federal Truth in Lending Act in 1968, comparable and often parallel disclosure laws were enacted in a number of states. In some cases these state laws mandated disclosures beyond those required by the Federal law, but in other cases requirements were similar or even identical. [FN19] In the latter examples existence of parallel state and Federal laws did not necessitate multiple disclosures or impose any regulatory burdens beyond those imposed by the State or Federal requirements taken alone. However, if changes are made in either the state or Federal law without corresponding changes in the other statute, this conclusion would no longer follow. For example, reduction in required disclosures and changes in civil liability provisions in the Federal law would not eliminate the necessity of continued compliance with the same requirements under a previously redundant state law. As a result, the change to new Federal requirements would have the effect of increasing the number of required disclosures and adding to the length of forms. Moreover, to the extent that statutory minimum penalties apply for even technical violations under state laws, requests for interpretations and costly litigation could continue, simply transferred from Federal to state agencies and courts.

FN19 Staff of the Division of Consumer and Community Affairs are attempting to determine which states fall into these categories.

Congress presented a potential solution to this problem when it gave the Board authority to determine which state laws were "inconsistent" with provisions of Truth in Lending. According to paragraph 111 of the Act (as revised), "the laws of any state relating to the disclosure of information in connection with credit transactions" would be preempted "to the extent of the inconsistency." There are three problems for the Board in using this clause to solve the problem of potential increased regulatory burden from state laws. First is the meaning of "inconsistent." Second, the Board apparently does not have the authority to decide whether any state disclosure laws are inconsistent with Federal TIL without a line-by-line review of the state laws in question and this would be very time consuming. Third, paragraph 111 also states that "If the Board determines that a state-required disclosure is inconsistent, creditors located in that state may not make disclosures using that inconsistent term or form * * *." Thus, if the Board determines that any disclosures are inconsistent with Federal law, the practical effect would be to make it very difficult to use a combined contract and Federal Truth-in-Lending disclosure.

By order of the Board of Governors, March 26, 1981.

James McAfee,

Assistant Secretary of the Board.

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