PROPOSED RULES

FEDERAL RESERVE SYSTEM

12 CFR Part 226

Regulation Z; Docket No. TIL-1
FR Doc. 92-29552
Filed 12-8-92

Truth in Lending; Proposed Update to Official Staff Commentary

Wednesday, December 9, 1992

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed official staff interpretation.

SUMMARY: The Board is publishing for comment proposed revisions to the official staff commentary to Regulation Z (Truth in Lending). The commentary applies and interprets the requirements of Regulation Z. The revisions being proposed are limited, and attempt to address regulatory provisions needing clarification or issues for which there may be a general need for more guidance. The revisions address the interplay between the Truth in Lending rules on demand features and other Federal rules dealing with credit extended to executive officers of depository institutions. They provide greater flexibility in complying with the disclosure requirements under Regulation Z in these transactions. The disclosure rules for security interests (particularly those in rescindable transactions) also would be clarified. The commentary would offer creditors alternative methods of disclosing security interests in rescindable transactions.

DATES: Comments must be received on or before January 29, 1993.

ADDRESSES: Comments should refer to Docket No. TIL-1 and be mailed to Mr. William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, Washington, DC 20551. They may also be delivered to the guard station in the Eccles Building courtyard on 20th Street, NW. (between Constitution Avenue and C Street, NW.) between 8:45 a.m. and 5:15 p.m. on weekdays. Except as provided in the Board's rules regarding the availability of information (12 CFR 261.8), all comments received will be available for inspection and copying by any member of the public in the Freedom of Information Office, room B-1122 of the Eccles Building, between 9 a.m. and 5 p.m. on weekdays.

FOR FURTHER INFORMATION CONTACT:Michael Bylsma, Leonard Chanin, Kyung Cho, Kurt Schumacher, or Mary Jane Seebach, Attorneys, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, DC 29551, at (202) 452-3667. For the hearing impaired only, contact Dorothea Thompson, Telecommunications Device for the Deaf (TDD), at (202) 452-3544.

SUPPLEMENTARY INFORMATION: (1) General. The Truth in Lending Act (15 U.S.C. 1601 et seq.) governs consumer credit transactions and is implemented by the Board's Regulation Z (12 CFR part 226). Effective October 13, 1981, an official staff commentary (TIL-1, Supp. I to 12 CFR part 226) was

published to interpret the regulation. The commentary is designed to provide guidance to creditors in applying the regulation to specific transactions and is updated periodically to address significant questions that arise. It is expected that the proposed update will be adopted in final form in March 1993 with compliance optional until October 1, 1993, the uniform effective date for mandatory compliance.

(2) Form of comments. The Board requests that, when possible, comments be prepared using a standard typeface with a type size of 10 or 12 characters per inch. This will enable the Board to convert the text into machine-readable form through electronic scanning, and will facilitate automated retrieval of comments for review. Comments may also be submitted on 3 1/2 inch or 5 1/4 inch computer diskettes in any IBM-compatible DOS-based format with a paper copy of the comment included.

(3) Proposed revisions. The following is a description of the proposed revisions to the commentary:

Subpart A--General

Section 226.2 Definitions and Rules of Construction

2(a) Definitions

2(a)(25) Security interest. The Board has received numerous questions recently about the disclosure of security interests--particularly in rescission notices--and about the appropriate use of the model rescission form for a refinancing with an original creditor. Comment 2(a)(25)-6 would be revised to clarify that disclosures about collateral securing a transaction need not specify how the security interest is taken, for example, by "acquiring" a new security interest or by "retaining" an existing security interest. The proposed revision would expand on an interpretation added in the 1989 commentary update (54 FR 9417, March 7, 1989). It would be added to that comment on the definition of "security interest" because of its applicability to the security interest disclosures under multiple sections of the regulation (§§ 226.6, 226.15, 226.18 and 226.23). Sample language would be provided to illustrate how a rescission notice could disclose the fact that a transaction is secured by the consumer's home without any additional detail about the security interest.

The proposed comment further states that the model form for rescission of refinancings with an original creditor (model form H-9) which discloses the retention of a security interest in a consumer's principal dwelling, also adequately discloses the fact of a security interest where a new security interest is acquired (and the preexisting security interest is replaced by the new one). As stated in the Supplementary Information to the 1989 commentary update, comment 2(a)(25)-6 was intended to clarify "that the disclosure that an interest is retained, as in form H-9, is adequate in a refinancing where a new mortgage if filed and a new advance is made." The revision now being proposed would specifically incorporate that position into the commentary.

The proposed commentary revisions should make clear that the requirements about disclosure of a security interest in a rescission notice may be satisfied with either a generic statement of the fact that the consumer's home is security for the transaction or with a more detailed disclosure about that security interest. It would further make clear, as an

alternative to modifying rescission notices to include more generic disclosures, that the form H-9 may be used--without modification--in any case in which an original creditor refinances a transaction (whether or not the refinancing involves keeping in place an existing security interest for any period of time or involves taking a new security interest).

Subpart B--Open-End Credit

Section 226.5b Requirements for Home-Equity Plans

5b(d) Content of Disclosures

5b(d)(4) Possible actions by creditor--Paragraph 5b(d)(4)(iii). Comment 5b(d)(4)(iii)-1 would be revised to reflect the amendment to § 226.5b(f)(2) adopted by the Board in August 1992. (57 FR 34676, August 6, 1992.) The Board amended the regulation to provide that a depository institution may terminate and demand payment of the balance on any home equity line of credit extended to its executive officers to the extent Federal law requires that the credit shall be due and payable on demand. (See § 226.5b(f)(2)(iv).) For example, Regulation O contains this requirement for state member banks of the Federal Reserve System. (See 12 CFR 215.5.)
In the Supplementary Information accompanying the amendment, the Board stated that the regulation requires that this provision be part of the home-equity agreement, although this feature is not required to be disclosed with the preapplication disclosures. The proposed commentary would restate this position.
5b(f) Limitations on home equity plans--Paragraph 5b(f)(2). Comment 5b(f)(2)-1 would be revised to clarify that a creditor may terminate a plan as provided in § 226.5b(f)(2)(iv).

Section 226.6 Initial Disclosure Statement

6(e) Home Equity Plan Information

Comment 6(e)-1 would be revised to add a cross reference to comment 5b(d)(4)(iii)-1. This reflects the position taken in the Supplementary Information of the August 6, 1992 Federal Register notice that the termination feature in § 226.5b(f)(2)(iv) also need not be specifically disclosed under § 226.6(e).

Subpart C--Closed-End Credit

Section 226.18 Content of Disclosures

18(i) Demand Feature

Comment 18(i)-2 would be revised to address how the rule in the Board's Regulation O (and other comparable Federal financial regulatory agency rules) relates to the disclosure rules for demand features in closed-end credit transactions. It parallels the treatment of such features in open-end credit. The proposed comment provides that if an institution retains the ability to demand payment of a loan in its closed-end credit agreement with its executive officers to the extent required by Federal law, the institution need not provide demand disclosures. Of course, if an institution has a demand feature in its closed-end agreement with its executive officers that is broader than that required by Federal law, such a feature would have to be disclosed under § 226.18(i).

Section 226.19 Certain Residential

Mortgage and Variable-Rate Transactions

19(b) Certain Variable-Rate Transactions

Paragraph (19)(b)(2)(xi). Demand features must be disclosed in variable rate mortgages covered by § 226.19(b). Since disclosure of a demand feature for variable-rate mortgages is determined by reference to § 226.18(i), a cross-reference would be added to comment 19(b)(2)(xi)-1 dealing with demand features.

List of Subjects in 12 CFR Part 226

Advertising, Federal Reserve System, Reporting and recordkeeping requirements, Truth in lending.
Certain conventions have been used to highlight the proposed revisions. New language is shown inside bold-faced arrows, while language that would be deleted is set off with brackets. The Board is publishing only those sections of the commentary that would be affected by the changes.

Text of Proposed Revisions

For the reasons set forth in the preamble and pursuant to authority granted in section 105 of the Truth in Lending Act (15 U.S.C. 1604 as amended), the Board proposes to amend the official staff commentary to Regulation Z (12 CFR part 226, Supplement I) as follows:

PART 226--(AMENDED)

1. The authority citation for part 226 continues to read as follows:

Authority: Truth in Lending Act, 15 U.S.C. 1604 and 1637(c)(5); sec. 1204(c), Competitive Equality Banking Act, 12 U.S.C. 3806.

SUPPLEMENT I TO PART 226--(AMENDED)

2. In Supplement I to part 226, under the heading "2(a) Definitions", comment 2(a)(25)-6 would be amended by adding three new sentences at the end to read as follows:
2(a)(25) Security interest.

6. Specificity of disclosure. In disclosing the fact that the transaction is secured by the collateral, the creditor also need not disclose how the security interest arose. Thus, a rescission notice need not specifically state that a new security interest is "acquired" or an existing security interest is "retained" in a transaction. The retention or acquisition of a security interest in the consumer's principal dwelling instead may be disclosed in a rescission notice with a general statement such as the following: "Your home is the security for the new transaction." A statement such as this may be used, for example, instead of the second sentence in model form H-9 and could apply both to a refinancing in which a new security interest is taken by the original creditor and one in which an existing security interest is maintained. (Of course, because model form H-9 adequately discloses the fact that the home is security for the transaction, it may be used without modification in both a refinancing in which a new security interest is taken by the original creditor and one in which an existing security interest is retained by that creditor.)

SUPPLEMENT I TO PART 226--

(AMENDED)

3. In Supplement I to part 226, under the heading "5b(d) Content of Disclosures", comment 5b(d)(4)(iii)-1 would be amended by revising the fourth sentence and adding a sentence after the fourth sentence to read as follows:
Paragraph 5b(d)(4)(iii).
1. Disclosure of conditions. As an alternative to disclosing the conditions in this manner, the creditor may simply describe the conditions using the language in §§ 226.5b(f)(2) (i)-(iii), 226.5b(f)(3)(i) (regarding freezing the line when the maximum annual percentage rate is reached), and 226.5b(f)(3)(vi) or language that is substantially similar. The condition contained in § 226.5b(f)(2)(iv) need not be stated.

SUPPLEMENT I TO PART 226--(AMENDED)

4. In Supplement I to part 226, under the heading "5b(f) Limitations on Home Equity Plans", comment 5b(f)(2)-1 would be amended by revising the second sentence to read as follows:
Paragraph 5b(f)(2).
1. Limitations on termination and acceleration. However, creditors may take these actions in the (three) four circumstances specified in § 226.5b(f)(2).

SUPPLEMENT I TO PART 226--(AMENDED)

5. In Supplement I to part 226, under the heading "6(e) Home Equity Plan Information", comment 6(e)-1 would be amended by adding a parenthetical at the end to read as follows:

1. Additional disclosures required. Creditors also must disclose a list of the conditions that permit the creditor to terminate the plan, freeze or reduce the credit limit, and implement specified modifications to the original terms. (See comment 5b(d)(4)(iii)-1.)

SUPPLEMENT I TO PART 226--(AMENDED)

6. In Supplement I to part 226, under the heading "18(i) Demand feature", comment 18(i)-2 would be amended by adding a new sentence at the end to read as follows:
2. Covered demand features. A creditor may, but need not, treat its contractual right to demand payment of a loan made to its executive officers as a demand feature, when such a provision is required by Federal law.

SUPPLEMENT I TO PART 226--(AMENDED)

7. In Supplement I to part 226, under the heading "19(b) Certain variable-rate transactions", comment 19(b)(2)(xi)-1 would be amended by revising the first sentence to read as follows:
Paragraph 19(b)(2)(xi).
1. Demand feature. If a variable-rate loan subject to § 226.19(b) requirements contains a demand feature as discussed in § 226.18(i), this fact must be disclosed.

Board of Governors of the Federal Reserve System, December 1, 1992.

William W. Wiles,

Secretary of the Board.