FEDERAL RESERVE BANK
OF NEW YORK

Circular No. 6389
August 19, 1969

Interpretations of Regulation Z

*To All State Member Banks, and Others Concerned,
in the Second Federal Reserve District:*

Printed below is an excerpt from the Federal Register of August 16, containing the text of three interpretations by the Board of Governors of the Federal Reserve System of provisions in its Truth in Lending Regulation Z.

Additional copies of this circular will be furnished upon request.

Alfred Hayes,
President.

Title 12—BANKS AND BANKING

Chapter II—Federal Reserve System

SUBCHAPTER A—BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Reg. Z]

PART 226—TRUTH IN LENDING

Miscellaneous Interpretations

§ 226.404 Premiums for vendor's single interest insurance required by creditor.

(a) Under § 226.4(a)(6), charges or premiums for insurance, written in connection with a credit transaction, against loss of or damage to property may be excluded from the finance charge if the creditor makes the disclosures required under that subparagraph. Under § 226.4(a)(7), a premium or other charge for any other guarantee or insurance protecting the creditor against the customer's default or other credit loss is included in the finance charge. The question arises as to whether Vendor's Single Interest (V.S.I.) coverage, when required by the creditor to be written in connection with a transaction, is insurance of the type described in § 226.4(a)(6) or in § 226.4(a)(7).

(b) V.S.I. coverage is written only in connection with a credit transaction and indemnifies the creditor against, among other perils, conversion, embezzlement, and secretion of the collateral by the customer; and amounts payable on account of loss are payable only to the creditor; and the amount of any indemnity payable under the policy is directly related to the amount of the credit loss, in that such indemnity can never exceed the amount of the unpaid principal balance of the debt. The insurer has no liability under a V.S.I. policy unless, at the time the policy was written, no payment was more than a specified number of days past due, and a claim under the policy is not valid unless the customer has defaulted in payment. Additionally, many V.S.I. policies indemnify the creditor against expense incurred in transporting the collateral to the creditor from the place of repossession.

(c) V.S.I. coverage is, therefore, insurance which protects the creditor against the customer's default or other credit loss, and when required by the creditor to be written in connection with any transaction, the premium therefore is included in the finance charge under § 226.4(a)(7).

(Interprets and applies 15 U.S.C. 1605)

§ 226.405 Property insurance written in connection with a transaction—obtained from or through the creditor.

(a) Footnote 4 to § 226.4(a)(6) specifies that a policy of insurance against loss or damage to property or liability arising out of its use is not considered to be "written in connection with" a transaction when it "* * * was not purchased by the customer for the purpose of being used in connection with that extension of credit." Therefore, whenever such a policy is purchased by the customer for the purpose of being used in connection with a specific extension of credit, it is insurance "written in connection with" that transaction.

(b) If such property insurance which is written in connection with a transaction is required by the creditor and is obtainable from or through him, the cost thereof for the term of the initial policy or policies must be disclosed to the customer, irrespective of whether the customer purchases or expects to purchase such insurance from the creditor, in order for the premium to be excluded from the finance charge.

(Interprets and applies 15 U.S.C. 1605)

§ 226.811 Renewals of notes by mail.

(a) Under paragraph (j) of § 226.8, renewals of notes with new maturity dates constitute refinancings and are consequently new transactions. A common practice is for creditors to permit renewal of such notes by mail. In many of such instances the creditor does not know whether the customer will reduce his original obligation by a payment on principal or, if reduced, the amount of that reduction. The question arises as to what disclosures should be made by mail to the customer in these circumstances.

(b) If the creditor knows the amount of the principal payment, all disclosures should be made on the basis of the resulting new amount financed. If, however, the creditor does not know whether the customer will reduce his original obligation, or if so, by how much, he should disclose on the assumption that there will be no reduction. In such circumstances he may make one or more additional disclosures based on one or more examples of graduated principal reduction. For example, if a single payment note was for $1,000 at 8 percent for 3 months, in addition to the other required disclosures, the creditor should disclose an amount financed of $1,000 with a finance charge of $20, and may, in addition, disclose that with a principal payment of $300 the amount financed would be $700 with a finance charge of $14, and with a principal payment of $500 the amount financed would be $500 with a finance charge of $10.

(Interprets and applies 15 U.S.C. 1639)

Dated at Washington, D.C., the 1st day of August 1969.

By order of the Board of Governors.

[SEAL] KENNETH A. KENYON,
Deputy Secretary.

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