FEDERAL RESERVE press release

For immediate release November 27, 1990

The Federal Reserve Board today issued for public comment proposed revisions to its staff commentary for Regulation Z, Truth in Lending. The proposed interpretations address such issues as renewals of home equity lines of credit, credit card substitution, and renewable balloon payment mortgages. Comment is requested by January 28, 1991.

The Board's notice is attached.

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Attachment

FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Reg. Z; TIL-1]

TRUTH IN LENDING

Proposed Update to Official Staff Commentary

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 and is a substitute for individual staff interpretations. The proposed revisions address several issues, including renewals of home equity lines, credit card substitution, and renewable balloon payment mortgages.

DATES: Comments must be received on or before January 28, 1991.

ADDRESSES: Comments should refer to Docket No. TIL-1 and be sent to Mr. William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, Washington, DC 20551. They may be delivered to Room B-2222 of the Eccles Building between 8:45 a.m. and 5:15 p.m. weekdays or delivered to the guard station in the Eccles Building Courtyard on 20th Street, N.W. (between Constitution Avenue and C Street, N.W.) any time. All comments received at the above address 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 9:00 a.m. and 5:00 p.m. weekdays.

FOR FURTHER INFORMATION CONTACT: The following attorneys in the Division of Consumer and Community Affairs, at (202) 452-3667 or (202) 452-2412: Jane Ahrens, Sharon Bowman, Leonard Chanin, Adrienne Hurt, Thomas Noto, Kurt Schumacher, Mary Jane Seebach, John Wood. For the hearing impaired only, Telecommunications Device for the Deaf (TDD), Earnestine Hill or Dorothea Thompson, at (202) 452-3544, Board of Governors of the Federal Reserve System, Washington, DC 20551.

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 1991 with optional compliance until the uniform effective date of October 1, 1991, for mandatory compliance.

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

SUBPART A -- GENERAL

SECTION 226.4 -- Finance Charge

4(a) Definition

Comment 4(a)-2 would be revised to explain that a tax imposed on a creditor by a state is a finance charge if the creditor separately imposes the charge on the consumer in connection with a credit transaction (instead of absorbing the charge as a cost of doing business), even if the creditor is authorized by the state to pass the charge on to the consumer.

SUBPART B -- OPEN-END CREDIT

SECTION 226.5a -- Credit and Charge Card Applications and Solicitations

5a(b) Required Disclosures

5a(b)(2) Fees for Issuance or Availability

Comments 5a(b)(2)-1 and 5a(b)(2)-2 would be revised to clarify that disclosures presented in the tabular format should not include certain membership fees and fees for enhancements.

5a(c) Direct-Mail Applications and Solicitations

Comment 5a(c)-1 would be revised to correct an error. Under section 226.5a(b)(1)(ii), for direct-mail applications and solicitations, an accurate variable annual percentage rate is one in effect within 60 days before mailing.

Comment 5a(c)-2 currently indicates that a single application form can be used both in direct mailings and in public locations as "take-ones," provided the card issuer meets certain conditions. One of the conditions is that the form not

include the disclosures referred to in section 226.5a(e)(1)(ii) and (iii) (the printing date, the statement that the credit terms are accurate as of that date and subject to change thereafter, the statement that the consumer should contact the issuer for updated information, and a toll-free telephone number or a mailing address). The comment would be revised to give card issuers more flexibility, in that the disclosures identified above could either be omitted or included, provided the issuer adheres to certain requirements relating to the accuracy of the credit terms in each case.

5a(e) Applications and Solicitations Made Available to General Public

5a(e)(1) Disclosure of Required Credit Information

Comment 5a(e)(1)-2 would be revised by making a technical correction. Currently the comment states that the disclosures specified in section 226.5a(e)(1)(i), (ii), and (iii) may appear either in or outside the table containing the credit term disclosures. Since the disclosures referred to in section 226.5a(e)(1)(i) are themselves the credit term disclosures, the comment would be revised to refer only to section 226.5a(e)(1)(ii) and (iii).

SECTION 226.5b -- Requirements for Home Equity Plans

Existing comments 5b-2 through 5b-5 would be redesignated as comments 5b-3 through 5b-6, respectively. New comment 5b-2 would be added to provide guidance on when changes to a home equity plan are governed by the change in terms rules in section

226.9(c), and when changes constitute a new plan requiring completely new disclosures.

5b(d) Content of Disclosures

5b(d)(4) Possible Actions by Creditor

Paragraph 5b(d)(4)(iii)

A technical change would be made to comment 5b(d)(4)(iii)-1 to provide guidance concerning the ability of creditors to retain the right to freeze a line of credit if the maximum annual percentage rate is reached. This provision is added in light of the recent amendment to section 226.5b(f)(3)(i) (55 FR 38310, September 18, 1990; correction notice at 55 FR 39538, September 27, 1990). That amendment permits a creditor to provide in its initial agreement that further advances will be prohibited or the credit limit reduced when the maximum annual percentage rate is reached.

5b(d)(5) Payment Terms

Paragraph 5b(d)(5)(iii)

Comment 5b(d)(5)(iii)-4 would be revised to clarify the treatment of reverse mortgages with shared appreciation features. The comment would correct a cross reference. A reverse mortgage with an appreciation feature is not a variable rate plan if the underlying interest rate is fixed. As discussed in the commentary to section 226.6(a)(2), a plan is variable rate only if the rate may change. Under open-end credit, the rate is not affected by a shared appreciation feature.

5b(d)(8) Fees Imposed by Third Parties to Open a Plan

Comment 5b(d)(8)-2 would be revised to clarify that while a creditor must always state the total of third party fees, the total sum need not include costs for property insurance if the creditor discloses that such insurance is required. The comment also would clarify that an itemization of third party fees provided in response to a consumer's request must contain the disclosure about property insurance. (The creditor either may disclose the amount of the premium or state that property insurance is required.)

5b(f) Limitations on Home Equity Plans

Paragraphs 5b(f)(3)(i) and (vi)

Comments 5b(f)(3)(i)-1 and 5b(f)(3)(vi)-1 would be revised in light of the recent amendments to section 226.5b(f)(3)(i) and 226.5b(f)(3)(vi). These amendments permit a creditor to provide in its initial agreement that further advances will be prohibited or the credit limit reduced when the maximum annual percentage rate is reached.

SECTION 226.6 -- Initial Disclosure Statement

6(e) Home Equity Plan Information

Comment 6(e)-4 would be revised to clarify that when disclosures are the same for the draw and repayment phase, creditors need not explicitly state that the information applies to both phases, as long as this fact is clear.

SECTION 226.9 -- Subsequent Disclosure Requirements

9(c) Change in Terms

Paragraph 9(c)(1) Written Notice Required

Section 226.9(c)(1) requires creditors to provide a notice whenever any term required to be disclosed under section 226.6 is changed. Section 226.6(e)(7) requires creditors to give certain variable-rate and payment examples for home equity plans, unless the disclosures provided with the application were in a form the consumer could keep and included representative payment examples covering the payment option chosen by the consumer.

Comment 9(c)(1)-6 would be revised to clarify that if the index is changed, the maximum annual percentage rate is increased, or a variable rate feature is added to a fixed rate plan, the creditor must give the maximum rate information required by section 226.5b(d)(12)(x) and historical example required by section 226.5b(d)(12)(xi), unless these disclosures are unchanged from those given earlier. A parenthetical referencing section 226.30 is included to alert creditors to the fact that comment 30-11 permits a creditor to increase the maximum rate on a home equity plan only for the period after the original maturity. The comment also would clarify that if the minimum payment requirement is changed, the creditor must give the payment disclosures required by section 226.5b(d)(5)(iii) (and, in variable rate plans, the disclosures required by section 226.5b(d)(12)(x) and (d)(12)(xi)) unless the disclosures given earlier contained representative examples covering the new

minimum payment requirement. As provided under section 226.5b(f)(3)(iv) (discussing beneficial changes), a creditor may offer the consumer the option of making lower payments without giving a change in terms notice.

SECTION 226.12 -- Special Credit Card Provisions

12(a) Issuance of Credit Cards

Comment 12(a)(2)-2 currently indicates that a card issuer may replace one card with an unsolicited substitute card in a number of instances, including where credit features are added or changed. The comment would be revised to explain that certain replacements are not considered permissible substitutions for purposes of section 226.12(a). The proposed revision provides that certain additions or changes may so alter an underlying credit card account relationship that the unsolicited replacement of the card on the original account by a new card cannot be deemed to be a substitution, and is impermissible. Such a situation would occur, for example, if a second credit account is established that will be accessed by the same card and for which the creditor must give initial disclosures to the cardholder.

SECTION 226.16 -- Advertising

16(d) Additional Requirements for Home Equity Plans

Comment 16(d)-4 would be revised to clarify that creditors may state, for example, "no closing costs" in cases where property insurance may be required as long as the creditor includes a disclosure that such insurance may be required. Such treatment would address the concern that, in many cases,

insurance already is being carried on the property, and would parallel the treatment of such insurance in other parts of the regulation.

SUBPART C -- CLOSED-END CREDIT

SECTION 226.17 -- General Disclosure Requirements

17(a) Form of Disclosures

Paragraph 17(a)(1)

There have been occasional requests (particularly by creditors using multi-purpose disclosure forms) to allow disclosure of the assumability of non-residential mortgage transactions. Comment 17(a)(1)-5 would be revised to indicate that a creditor may disclose in the segregated disclosures ("federal box") whether or not a secured credit transaction is assumable (even if the transaction is not a residential mortgage transaction).

17(c) Basis of Disclosures and Use of Estimates

Paragraph 17(c)(1)

Comment 17(c)(1)-11 would be revised to provide additional guidance on when a renewable loan with a balloon payment (formerly referred to as a "renegotiable-rate" mortgage instrument) should be disclosed as a long-term variable-rate loan as opposed to a short-term balloon loan. The comment would provide that such loans should be disclosed as variable-rate transactions when the creditor is either unconditionally obligated to renew the loan or is obligated to renew subject only to conditions within the consumer's control. The proposed

comment provides examples of conditions within the consumer's control and those outside the consumer's control. As an example of applying the analysis, the Federal National Mortgage Association (FNMA) seven-year extendable balloon product (which provides that the creditor need not renew if the rate would be more than 5% higher than the initial loan rate) would be disclosed as a balloon payment loan and not as a variable-rate transaction.

SECTION 226.19 -- Certain Residential Mortgage Transactions

19(b) Certain Variable-Rate Transactions

Comment 19(b)-3 provides factors to determine whether or not a transaction involves an "intermediary agent or broker," which affects the timing rules for certain disclosures. The factors look to whether there is a relationship between the creditor and the broker in which the creditor has knowledge of and exercises control over the broker's actions. The third factor describing the amount of work completed by the broker would be revised to recognize that a large amount of work performed by a broker may not necessarily evidence this sort of relationship. For example, for purposes of this factor, a broker's submission of a completed loan package to a creditor may not indicate a close relationship between the two if such a practice is customary in a particular area.

Comment 19(b)-5 would be revised to parallel the proposed revisions to comment 17(c)(1)-11 describing renewable balloon-payment mortgage instruments.

SECTION 226.20 -- Subsequent Disclosure Requirements

20(a) Refinancings

Comment 20(a)-3 would be revised to reflect the name change for describing a renewable balloon-payment mortgage (formerly referred to as a "renegotiable-rate" mortgage) in proposed comments 17(c)(1)-11 and 19(b)-5.

20(c) Variable-Rate Adjustments

An issue concerning the accuracy of adjustments made to variable-rate loans has arisen in recent months. Concern has been raised that some creditors may not be adjusting such loans consistent with the terms of the underlying legal obligation, resulting in inaccurate interest rate and payment adjustments. Just as rate and payment adjustments must reflect the terms of the legal obligation, the subsequent disclosures under Regulation Z, required for certain variable-rate transactions, must reflect the terms of the legal obligation. Section 226.20(c) requires disclosures to be provided to consumers in cases where the interest rate is adjusted in variable-rate transactions subject to section 226.19(b), including disclosures about the new interest rate and payment. Comment 20(c)-3 would be added to reiterate that the general requirement of section 226.17(c)(1), that disclosures reflect the terms of the legal obligation between the parties, applies to the disclosures for variable rate transactions required under section 226.20(c). Thus, for example, disclosures about the new interest rate and payment must

be based on the index type and index value specified in the legal obligation.

SUBPART D - MISCELLANEOUS

SECTION 226.28 -- Effect on State Laws

28(a) Inconsistent Disclosure Requirements

Comment 28(a)-15 would be added to reflect the Board's recent determination of the effect of the Truth in Lending Act and Regulation Z on certain provisions of the law of Wisconsin dealing with disclosures for home equity plans and the right of a creditor to accelerate the outstanding balance when a nonapplicant spouse terminates a plan. The notice of this determination was published at 55 FR 31815 (August 6, 1990).

SECTION 226.30 -- Limitation on Rates

Comment 30-1 would be revised to reflect the name change for describing a renewable balloon-payment mortgage (formerly referred to as a "renegotiable-rate" mortgage) in proposed comment 17(c)(1)-11.

List of Subjects in 12 CFR Part 226

Advertising, Banks, Banking, Consumer protection, Credit, Federal Reserve System, Finance, Penalties, Rate limitations, 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.

(3) Text of proposed revisions. 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 Supp. I) as follows:

1. The authority citation for Part 226 continues to read:

AUTHORITY: Truth in Lending Act, 15 U.S.C. 1604 and sec. 2, Pub. L. 100-583, 102 Stat. 2960; sec. 1204(c), Competitive Equality Banking Act, 12 U.S.C. 3806.

SUBPART A -- GENERAL

Section 226.4 -- Finance Charge

2. Comment 4(a)-2 would be amended by adding a second bullet after the first bullet to read as follows:

4(a) Definition.

* * * * *

2. *Costs of doing business*. * * *

►• A tax imposed by a state on a creditor is a finance charge if the creditor separately imposes the charge on the consumer, even if the state permits the creditor to pass the tax on to the consumer.◄

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SUBPART B -- OPEN-END CREDIT

Section 226.5a -- Credit and Charge Card Applications and Solicitations

3. Comments to 5a(b)(2) would be amended by revising the third sentence in comment 5a(b)(2)-1, and by revising comment 5a(b)(2)-2 to read as follows:

5a(b) Required Disclosures

* * * * *

5a(b)(2) Fees for Issuance or Availability

1. *Membership fees*. * * * Such a fee ▸should◂ [need] not be disclosed ▸in the table◂ if membership results merely in eligibility to apply for an account.

2. *Enhancements*. Fees for optional services in addition to basic membership privileges in a credit or charge card account (for example, travel insurance or card-registration services) ▸should◂ [need] not be disclosed ▸in the table◂ [under this paragraph] if the basic account may be opened without paying such fees.

* * * * *

4. Comments to 5a(c) would be amended by revising the second sentence in comment 5a(c)-1, and by revising the third sentence and adding a new sentence after the third sentence in comment 5a(c)-2 to read as follows:

5a(c) Direct-Mail Applications and Solicitations

1. *Accuracy*. * * * (An accurate variable annual percentage rate is one in effect within [30] ▸60◂ days before mailing.)

2. *Mailed publications*. * * * In addition, a card issuer may use a single application form as a "take-one" (in racks in public locations, for example) and for direct mailings, if the card issuer complies with the requirements of section 226.5a(c) even when the form is used as a "take-one" -- that is, by [providing current information and] presenting the required ▸section 226.5a(b)◂ disclosures in a tabular format [and

eliminates the information required under section 226.5a(e)(1)(ii) and (iii)]. ►When used in a direct mailing, the credit term disclosures must be accurate as of the mailing date whether or not the section 226.5a(e)(1)(ii) and (iii) disclosures are included; when used in a take-one, the disclosures must be accurate for as long as the take-one forms remain available to the public if the section 226.5a(e)(1)(ii) and (iii) disclosures are omitted. (If those disclosures are included in the take-one, the credit term disclosures need only be accurate as of the printing date.)◄

* * * * *

5. Comment 5a(e)(1)-2 would be revised to read as follows:

5a(e) Applications and Solicitations Made Available to General Public

* * * * *

5a(e)(1) Disclosure of Required Credit Information

* * * * *

2. *Form of disclosures*. The disclosures specified in section 226.5a(e)(1)[(i),](ii)[,] and (iii) may appear either in or outside the table containing the required credit disclosures.

* * * * *

6. Comments 5b-2 through 5b-5 would be redesignated as comments 5b-3 through 5b-6, respectively, and new comment 5b-2 would be added to read as follows:

Section 226.5b -- Requirements for Home Equity Plans

* * * * *

►2. *Changes to home equity plans entered into on or after November 7, 1989*. Section 226.9(c) applies if, by written agreement under section 226.5b(f)(3)(iii), a creditor changes the terms of a home equity plan before its scheduled expiration, for example, by renewing a plan on different terms. A new plan results, however, if the plan is renewed (with or without changes to the terms) after the scheduled expiration. The new plan is subject to all open-end credit rules, including sections 226.5b, 226.6, and 226.15.◄

* * * * *

7. Comment 5b(d)(4)(iii)-1 would be amended by revising the fourth sentence to read as follows:

5b(d) Content of Disclosures

* * * * *

5b(d)(4) Possible Actions by Creditor

* * * * *

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 section 226.5b(f)(2) ►, 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.

* * *

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8. Comment 5b(d)(5)(iii)-4 would be amended by revising the second sentence in the fourth bullet to read as follows:

5b(d)(5) Payment Terms

* * * * *

Paragraph 5b(d)(5)(iii)

* * * * *

4. *Reverse mortgages*. * * *

• * * * The appreciation feature must be disclosed in accordance with ►this◄ section [226.5b(d)(12)].

* * * * *

9. Comment 5b(d)(8)-2 would be amended by revising the first sentence, and by adding a new sentence after the fourth sentence to read as follows:

5b(d)(8) Fees Imposed by Third Parties to Open a Plan

* * * * *

2. *Itemization of third-party fees*. In all cases creditors must state the total of third-party fees as a single dollar amount or a range ►except that the total need not include costs for property insurance if the creditor discloses that such insurance is required◄. * * * ►Any itemization provided upon the consumer's request must include the disclosure about property insurance (either the amount of the premium or the fact that property insurance is required).◄

* * * * *

10. Comment 5b(f)(3)(i)-1 would be amended by revising the first sentence, and by adding a new sentence after the first sentence to read as follows:

5b(f) Limitations on Home-Equity Plans

* * * * *

Paragraph 5b(f)(3)(i)

1. *Changes provided for in the agreement*. A creditor may provide in the initial agreement [for] ►that further advances will be prohibited or the credit line reduced during any period in which the maximum annual percentage rate is reached. A creditor also may provide for other◄ specific changes to take place upon the occurrence of specific events. * * *

* * * * *

11. Comment 5b(f)(3)(vi)-1 would be amended by revising the first sentence and by adding a new sentence after the first sentence to read as follows:

Paragraph 5b(f)(3)(vi)

1. *Suspension of credit privileges or reduction of credit limit*. A creditor may prohibit additional extensions of credit or reduce the credit limit in the circumstances specified in ►this section of◄ the regulation. ►In addition, as discussed under section 226.5b(f)(3)(i), a creditor may contractually reserve the right to take such action when the maximum annual percentage rate is reached.◄ * * *

* * * * *

Section 226.6 -- Initial Disclosure Statement

12. Comment 6(e)-4 would be amended by revising the third sentence to read as follows:

6(e) Home Equity Plan Information

* * * * *

4. *Disclosures for the repayment period.* * * * To the extent the corresponding annual percentage rate, the information in footnote 12, and any other required disclosures are the same for the draw and repayment phase, the creditor need not repeat such information, as long as [the disclosure clearly states] ▸it is clear◂ that the information applies to both phases.

* * * * *

Section 226.9 -- Subsequent Disclosure Requirements

13. Comment 9(c)(1)-6 would be amended by revising the heading, by revising the first sentence, and by adding three new sentences after the first sentence to read as follows:

9(c) Change in Terms:

* * * * *

9(c)(1) Written notice required.

* * * * *

6. [*Home-equity plans.*] ▸*Changes to home-equity plans.*◂ [If a creditor renews the draw period for a home equity plan] ▸Section 226.9(c) applies when, by written agreement under section 226.5b(f)(3)(iii), a creditor changes the terms of a home equity plan before its scheduled expiration, for example, by renewing a plan◂ on terms different from those of the original plan [, the

requirements of section 226.9(c) apply to such a change]. ►In disclosing the change:

- If the index is changed, the maximum annual percentage rate is increased (to the limited extent permitted by section 226.30), or a variable-rate feature is added to a fixed-rate plan, the creditor must include the disclosures required by section 226.5b(d)(12)(x) and (d)(12)(xi), unless these disclosures are unchanged from those given earlier.
- If the minimum payment requirement is changed, the creditor must include the disclosures required by section 226.5b(d)(5)(iii) (and, in variable-rate plans, the disclosures required by section 226.5b(d)(12)(x) and (d)(12)(xi)) unless the disclosures given earlier contained representative examples covering the new minimum payment requirement. (See the commentary to section 226.5b(d)(5)(iii), (d)(12)(x), and (d)(12)(xi) for a discussion of representative examples.)◄ * * *

* * * * *

Section 226.12 -- Special Credit Card Provisions

14. Comment 12(a)(2)-2 would be amended by adding two sentences at the end of the third bullet to read as follows:

12(a) Issuance of credit cards.

* * * * *

Paragraph 12(a)(2)

* * * * *

2. *Substitution - examples*. "Substitution" encompasses the replacement of one card with another because the underlying account relationship has changed in some way -- such as when the card issuer has: * * *

- Changed the credit or other features available on the account. For example, the original card could be used to make purchases and obtain cash advances at teller windows. The substitute card might be usable, in addition, for obtaining cash advances through automated teller machines. (If the substitute card constitutes an access device, as defined in Regulation E, then the Regulation E issuance rules would have to be followed.) ►If, however, in changing the credit or other features available on the account, a new open-end credit card account is opened (which would require initial disclosures to be given), the unsolicited replacement of one card with another is not a permissible substitution. For example, if a retail card issuer replaces its credit card with a co-branded bank card and the creditors maintain two separate accounts, the replacement card cannot be provided to consumers without solicitation since the addition of the bank card account would require initial disclosures under section 226.6.◄

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Section 226.16 -- Advertising

15. Comment 16(d)-4 would be amended by adding two new sentences after the second sentence to read as follows:

16(d) Additional Requirements for Home Equity Plans

* * * * *

4. *Misleading terms prohibited*. * * * ►In the case of property insurance, however, a creditor may state, for example, "no closing costs" even if property insurance may be required, as long as the creditor also provides a statement that such insurance may be required. (See the commentary to this section regarding fees to open a plan.)◄

* * * * *

SUBPART C -- CLOSED-END CREDIT

16. Comment 17(a)(1)-5 would be amended by adding a bullet after the thirteenth bullet to read as follows:

Section 226.17 -- General Disclosure Requirements

17(a) Form of disclosures

Paragraph 17(a)(1).

* * * * *

5. *Directly related*. * * *

►• A statement whether or not a subsequent purchaser of the property securing an obligation may be permitted to assume the remaining obligation on its original terms.◄

* * * * *

17. Comment 17(c)(1)-11 would be amended by revising the first bullet to read as follows:

17(c) Basis of disclosures and use of estimates

Paragraph 17(c)(1).

* * * * *

11. *Other variable-rate transactions*. Examples of variable-rate transactions include:

- [Renegotiable-rate mortgage instruments that involve a series of short-term loans secured by a long-term obligation,] ►Renewable balloon-payment instruments◄ where the [lender is] ►creditor is unconditionally◄ obligated to renew the short-term loan[s] at the consumer's option ►(or is obligated to renew subject to conditions within the consumer's control) and at◄ [. At] the time of renewal, the [lender] ►creditor◄ has the option of increasing the interest rate. Disclosures must be [given for the longer term of the obligation] ►based on the payment amortization (unless the specified term of the obligation with renewals is shorter)◄, with all disclosures calculated on the basis of the rate in effect at the time of consummation of the transaction. ►Examples of conditions within a consumer's control include requirements that a consumer be current in payments or continue to reside in the mortgaged property. In contrast, setting a limit on the rate at which the creditor would be obligated to renew or reserving the right to change the credit standards at the time of renewal are examples of conditions outside a consumer's control. Thus, for example, language in the obligation allowing the creditor to obtain a credit report at the time of renewal to verify the continuation of the consumer's credit standing would not affect disclosure of the transaction as a long term variable-rate obligation. If the obligation permits

the creditor to apply a new credit standard at the time of renewal, however, the transaction must be disclosed as a short-term balloon-payment loan.◄

* * * * *

Section 226.19 -- Certain Residential Mortgage and Variable-Rate Transactions

18. Comment 19(b)-3 would be amended by revising the third bullet and the paragraph following that bullet to read as follows:

19(b) Certain Variable-Rate Transactions.

* * * * *

3. *Intermediary agent or broker*. * * *

- The amount of work (such as document preparation) the creditor expects to be done by the broker on an application based on the creditor's prior dealings with the broker and on the creditor's requirements for accepting applications ►, taking into consideration the customary practice of brokers in a particular area◄. The more [preparation] ►work◄ that the creditor expects the broker to do on an application, ►in excess of what is usually expected of a broker in that area,◄ the less likely it is that the broker would be considered an "intermediary agent or broker" of the creditor.

An example of an "intermediary agent or broker" is a broker who, customarily within a brief time after receiving an application, inquires about the credit terms of several creditors with whom the broker does business and submits the application to one of them. The broker is responsible for only a small percentage of

the applications received by that creditor. During the time the broker has the application, it might request a credit report and an appraisal ►(or even prepare an entire loan package if customary in a particular area)◄.

* * * * *

19. Comment 19(b)-5 would be amended by revising the first bullet to read as follows:

5. *Examples of variable-rate transactions*. * * *

- [Renegotiable-rate mortgage instruments that involve a series of short-term loans secured by a long-term obligation,] ►Renewable balloon-payment instruments◄ where the [lender] ►creditor◄ is ►unconditionally◄ obligated to renew the short-term loan[s] at the consumer's option ►(or is obligated to renew subject to conditions within the consumer's control) and at◄ [. At] the time of renewal, the [lender] ►creditor◄ has the option of increasing the interest rate. ►(See the commentary to section 226.17(c)(1) on examples of variable-rate transactions for discussion of conditions within a consumer's control in connection with renewable balloon-payment loans.)◄

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20. In section 226.19, under "References," in the paragraph designated "1981 changes," the phrase "ection 226.20 -- Subsequent Disclosure Requirements" at the end of the paragraph would be deleted, and a new heading "Section 226.20 -- Subsequent

Disclosure Requirements" would be added, directly below that paragraph.

Section 226.20 -- Subsequent Disclosure Requirements

21. Comment 20(a)-3 would be amended by revising the second sentence to read as follows:

20(a) Refinancings

* * * * *

3. *Variable rate*. * * * For example, a [renegotiable rate] ►renewable balloon-payment◄ mortgage that was disclosed as a variable-rate transaction is not subject to new disclosure requirements when the variable-rate feature is invoked.

* * * * *

22. Comment 20(c)-3 would be added to read as follows:

* * * * *

20(c) Variable-Rate Adjustments

►3. *Legal obligation*. The disclosures required under this section must reflect the terms of the parties' legal obligation, as required under section 226.17(c)(1).◄

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SUBPART D -- MISCELLANEOUS

Section 226.28 -- Effect on State Laws

23. Comment 28(a)-15 would be added to read as follows:

28(a) Inconsistent disclosure requirements

* * * * *

►15. *Preemption determination -- Wisconsin*. Effective October 1, 1991, the Board has determined that the following provisions in the state law of Wisconsin are preempted by the federal law:

- Section 422.308(1) -- the disclosure of the annual percentage rate in cases where the amount of the annual percentage rate disclosed to consumers under the state law differs from the amount that would be disclosed under federal law, since in those cases the state law requires the use of the same term as the federal law to represent a different amount than the federal law.
- Section 766.565(5) -- the provision permitting a creditor to include in an open-end home equity agreement authorization to declare the account balance due and payable upon receiving notice of termination from a non-obligor spouse, since such provision is inconsistent with the purpose of the federal law.◄

* * * * *

Section 226.30 -- Limitation on Rates

24. Comment 30-1 would be amended by revising the second sentence in the fourth bullet to read as follows:

1. *Scope of coverage*. * * *

• * * * (Contrast with the [renegotiable-rate] ►renewable balloon-payment◄ instrument described in comment 17(c)(1)-11.)

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Board of Governors of the Federal Reserve System, November 21, 1990.

(signed) Jennifer J. Johnson

Jennifer J. Johnson
Associate Secretary of the Board