



American Revolution Bicentennial

## FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 76-153  
November 8, 1976

### REGULATION Z--TRUTH-IN-LENDING

#### Notice of Proposed Rulemaking on the Disclosure of Variable Interest Rate Loans

**TO ALL BANKS, OTHER CREDITORS,  
AND OTHERS CONCERNED IN THE  
ELEVENTH FEDERAL RESERVE DISTRICT:**

On October 21, 1976, the Board of Governors of the Federal Reserve System proposed to amend Regulation Z--Truth-in-Lending--to require disclosure to the customer, in advance of signing a loan agreement, of any variable rate clause in the contract and a number of related matters.

Previously, on December 18, 1974 (see Circular No. 74-335, dated December 31, 1974), the Board proposed to require disclosure that: (1) the annual percentage rate might vary; (2) the conditions under which the rate might be changed; and (3) if applicable, the range within which the rate could vary.

After considering suggestions for additional disclosures in comment received, and in light of the growing use of variable rate loans, particularly in mortgages, the Board decided to propose the following additional disclosure requirements:

-- The manner in which the change in the annual percentage rate might be implemented (for example, by shortening or lengthening the maturity of the loan, by changing the amount of periodic payments, or by a change in the amount due on the loan at maturity, if the loan is not entirely repaid by the periodic payments).

-- A statement of the effect on the amount of the periodic payment that would result from a change, immediately after consummation of the loan, assuming both a decrease and an increase of one-quarter of one percent in the annual percentage rate (or a greater change if the contract permits) when there is no change in the maturity of the loan.

-- A statement of how such a variation of a quarter of one percent in the annual percentage rate (or a greater change if permitted by the contract) would affect the maturity of the loan, when no change is made in the periodic payment.

The last two requirements would apply to a typical home mortgage loan contract containing a variable interest rate provision. They would not apply to some other transactions, such as single payment loans and loans payable upon demand.

Printed on the following pages is the text of the Board's notice as submitted for publication in the FEDERAL REGISTER.

Comments on the proposed amendments should be submitted in writing to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, to be received not later than November 29, 1976. All material submitted should include the docket number R-0003.

Sincerely yours,

T. W. Plant

First Vice President

FEDERAL RESERVE SYSTEM

[12 CFR PART 226]

[Reg. Z]

[Docket No. R-0003]

Notice of Proposed Rulemaking on the  
Disclosure of Variable Interest Rate Loans

The Board of Governors of the Federal Reserve System is publishing for comment a proposed amendment to Regulation Z to require creditors to disclose to customers, in advance of their becoming obligated on a credit contract, a variable interest rate clause if the contract, note, or other instrument evidencing the obligation so provides. On December 27, 1974, the Board published for comment in the Federal Register (39 F.R. 44779) a proposed amendment to Regulation Z, § 226.8(b)(8), which would have required disclosure of the fact that the annual percentage rate is subject to change, the conditions under which the rate may be changed and, if applicable, the maximum and minimum rates stipulated in the credit contract.

The comments received by the Board on its earlier proposal generally supported mandatory disclosure of variable rate clauses, but several commenters suggested that the proposed regulation did not require disclosure of sufficient information to enable customers to compare variable rate loans with fixed rate loans or to alert customers to the impact of a change in rates. Therefore, the proposed amendment has been expanded to require

disclosure of certain additional information that may be necessary for a meaningful evaluation of the economic consequences to the customer of a variable rate loan.

This new proposed amendment to § 226.8(b) establishes disclosure requirements for certain other than open end credit plans in which the annual percentage rate is prospectively subject to change. The Truth in Lending disclosures given to the customer prior to the consummation of the original extension of credit would include:

- (1) the conditions under which any change in rate may occur;
- (2) the manner in which the change in rate may be effected, e.g., change of maturity, change in periodic payments, or change in the amount due at maturity;
- (3) a statement of the change in the amount of the periodic payment caused by an immediate decrease and increase of one quarter of one percentage point in the annual percentage rate (or a greater change if that is permitted in the contract), assuming no change in maturity; and
- (4) a statement of the change in maturity caused by an immediate decrease and increase of one quarter of one percentage point in the annual percentage rate (or a greater change if that is permitted in the contract) assuming no change in the amount of the periodic payment.

The third and fourth disclosures would be applicable primarily to a typical real estate mortgage transaction but would not apply to some other credit transactions, such as single payment loans and demand loans. An example of how these disclosures could be made, assuming a 20-year, level monthly payment real estate mortgage for \$40,000 at an initial annual percentage rate of 9%, in which the mortgage note permitted a maximum incremental change of one percentage point in the annual percentage rate, and in which the change could be effected either by changing the amount of the monthly payment or by changing the maturity, is shown below:

A. Based on the principal outstanding at the time this contract is consummated, if the annual percentage rate were decreased one percentage point, to 8%, under the terms of this contract, the monthly payment to principal and interest would be decreased by \$25.32. If the annual percentage rate were increased one percentage point, to 10%, under the terms of this contract, the monthly payment to principal and interest would be increased by \$26.11. Under either condition the maturity of the debt and the number of payments would remain unchanged.

B. Based on the principal outstanding at the time this contract is consummated, if the annual percentage rate were decreased one percentage point, to 8%, under the terms of this contract, the number of monthly payments would be decreased by 36. If the annual percentage rate were increased one percentage point, to 10%, under the terms of this contract, the number of

monthly payments would be increased by 75. Under either condition the amount of the monthly payment to principal and interest would remain unchanged.

This example is presented for illustrative purposes only and does not indicate that any particular format or substantive credit terms are required by the Board.

Pursuant to the authority granted in 15 U.S.C. § 1604(1970), the Board proposes to amend Regulation Z, 12 C.F.R. Part 226, as follows:

1. Section 226.8(b) would be amended by the addition of subparagraph (8) as follows:

§ 226.8--Credit other than open end--Specific Disclosures

\* \* \* \* \*

(b) \* \* \*

(8) If the annual percentage rate as disclosed under § 226.8(b)(2) is prospectively subject to change, the following additional disclosures shall be made:

(i) The fact that the annual percentage rate is subject to change and the conditions under which such rate may change, including:

(A) identification of the index, if any, with respect to which such change in annual percentage rate is tied; and (B) any limitation on such change;

(ii) the manner (such as a change in payment amounts, number of scheduled periodic payments, or change in the amount due at maturity) in which any change in the annual percentage rate may be effected;

(iii) if the obligation is repayable in substantially equal instalments at substantially equal intervals (including those obligations providing for "balloon" payments) and the change could be effected by a change in the periodic payment amount, a statement of the estimated decrease and increase in the amount of the payment caused by a hypothetical immediate decrease and increase of the maximum amount of incremental change in the annual percentage rate allowed by the contract, or if there is no such limitation, a change of one quarter of one percentage point, based upon the number of scheduled periodic payments and original amount financed disclosed at consummation;

(iv) if the obligation is repayable in substantially equal instalments at substantially equal intervals (including those obligations providing for "balloon" payments) and the change could be effected by a change in the number of periodic payments, a statement of the estimated decrease and increase in the number of periodic payments caused by a hypothetical immediate decrease and increase of the maximum amount of incremental change in the annual percentage rate allowed by the contract, or if there is no such limitation, a change of one quarter of one percentage point, based upon the periodic payment amount and the original amount financed disclosed at consummation.

Any change in the annual percentage rate within the conditions or limitations disclosed in accordance with this paragraph is a subsequent occurrence under § 226.6(g) and is not a refinancing under § 226.8(j).

2. Should the Board adopt the proposed amendment after considering the comments received, § 226.810 would be rescinded, and an effective date would be set far enough in advance to allow for the orderly change of forms where necessary.

3. To aid in the consideration of these matters by the Board, interested persons are invited to submit relevant data, views, comments, or arguments. Any such material should be submitted in writing to the Secretary, The Board of Governors of the Federal Reserve System, Washington, D. C. 20551, to be received at the Board not later than November 29, 1976. All material submitted should include the docket number R-0003.

4. This notice is published pursuant to § 553(b) of Title 5 United States Code and § 262.2(a) of the Rules of Procedure of the Board of Governors of the Federal Reserve System (12 CFR 262.2(a)).

By order of the Board of Governors, October 20, 1976.

(signed) Theodore E. Allison

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Theodore E. Allison  
Secretary of the Board

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