FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 80-83
April 24, 1980

AMENDMENTS TO CREDIT RESTRAINT PROGRAM AND ADDITIONAL QUESTIONS AND ANSWERS

TO ALL BANKS
AND OTHERS CONCERNED IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:

The Federal Reserve Board announced two technical amendments to its Consumer Credit Restraint Program. They deal with changes in the terms of certain consumer credit accounts and with the relationship of the program to maximum finance charge rates permitted by State and Federal laws and Department of Energy rules.

The amendments are extensions of revisions in the consumer credit restraint regulations announced April 2 establishing uniform national rules for creditors to follow if they impose or increase finance or other charges or make certain other changes in the terms of consumer credit accounts.

The revisions, which are effective April 14, clarify that the requirements for changes in the terms of consumer credit accounts apply not only to open end accounts (where the consumer may pay the balance due in installments), but also to open accounts (such as 30-day accounts where the consumer may incur new debt from time to time but is expected to pay the full amount due upon being billed); and also clarify that the provisions for changes in the terms of consumer credit accounts do not affect the maximum finance charge permitted under State laws, or the maximum rates permitted under the Depository Institutions Deregulation and Monetary Control Act of 1980, but that Federal finance charge limitations for other covered creditors, such as regulations governing oil company credit programs, are superseded to the extent they are inconsistent with the Board's rules. The Federal Register document is enclosed.

The staff of the Federal Reserve Board has supplied additional sets of answers to questions concerning the Board's anti-inflation program initiated on March 14. These questions and answers may be added to those previously supplied, under the headings previously used and continuing previous numbering of questions. This set consists of questions and answers under two new subject headings: Short Term Financial Intermediaries and Changes in Terms of Consumer Credit Accounts.

Sincerely yours,

Robert H. Boykin

First Vice President

Enclosures

Title 12-Banks and Banking

CHAPTER II-FEDERAL RESERVE SYSTEM

SUBCHAPTER A-BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Subpart A; Docket No. R-0284]

PART 229-CREDIT RESTRAINT

Consumer Credit

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final Rule.

SUMMARY: On April 2, 1980, the Board amended its consumer credit restraint regulation (45 Federal Register 24444, April 10, 1980) to permit covered creditors to change certain terms relating to certain credit accounts if two conditions were met. First, the creditor would have to mail or deliver a written notice of the proposed change to each affected accountholder at least 30 days before the effective date of the change. Second, the creditor would have to allow the accountholder to repay the balance outstanding on the effective date according to the existing terms unless the consumer made a credit purchase or obtained a credit advance on or after that date; in which case, the new terms would apply to the outstanding balance plus new credit.

The Board is now making two technical amendments to its April 2 amendment. The first makes clear that the change in terms requirements apply not only to open-end credit accounts where the consumer may pay the balance due in installments subject to a finance charge, but also to open accounts (such as so-called 30-day accounts referred to at 45 FR 17928) where the consumer may make credit purchases or obtain credit advances from time to time, yet is expected to pay in full upon being billed. The intent of the April 2 amendment was to cover both types of account.

The second technical amendment clarifies that the change in terms provision does not affect the maximum finance charge rate permitted by state law or, for depository institutions, the maximum rate allowed by Title V of the Depository Institutions Deregulation and Monetary Control Act of 1980 (Public Law 96-221). It makes clear, however, that federal finance charge limitations for other covered creditors, such as the Department of Energy's regulations governing oil company credit programs, are superseded by § 229.6(a) of the credit restraint regulation to the extent that that provision authorizes an action otherwise prohibited by federal law. That was the intent of the April 2 amendment as indicated in the Federal Register supplementary information (45 FR 24444).

EFFECTIVE DATE: April 14, 1980.

FOR FURTHER INFORMATION CONTACT: Nathaniel E. Butler, Associate Director, or David A. Myers, Attorney, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 20551 (202-452-3000).

SUPPLEMENTARY INFORMATION: Since the two amendments that are being made to the consumer credit restraint regulation are merely interpretative in nature and do not change the substance of the regulation, the Board finds that publication of the changes for public comment or a delay in their effectiveness is neither necessary nor required under 5 U.S.C. § 553(b). Therefore, pursuant to its authority under the Credit Control Act (12 U.S.C. §§ 1901-1909), as implemented by Executive Order 12201, the Board hereby amends 12 CFR Part 229, Subpart A, §§ 229.6(a) and (b)(1), effective April 14, 1980, as follows:

* * *

(a) Notwithstanding the terms of any credit agreement or the provision of any other law, a covered creditor, with respect to its open-end or other open credit accounts, may (1) impose or increase any finance or other charge, (2) change the method of computing the balance upon which charges are imposed, or (3) increase the required minimum periodic payment, if the following two conditions are met.

* * *

(b)(1) This section does not authorize a covered creditor to impose a rate of interest or finance charge in excess of the maximum permitted by state law, nor does it authorize a depository institution (as defined in section 19(b) of the Federal Reserve Act as amended by the Monetary Control Act of 1980) to impose a rate of interest or finance charge in excess of the maximum permitted by federal law.

* * *

Board of Governors of the Federal Reserve System, April 14, 1980.

(signed) Theodore E. Allison
Theodore E. Allison
Secretary of the Board

[SEAL]

CONSUMER CREDIT

Covered Credit -- Page 8

24. Does the Federal Reserve contemplate preempting state usury laws in its administration of the credit restraint program?

Answer: No. The Federal Reserve Board has not preempted state usury ceilings.

(NOTE: This question appears to have become confused with Board action on April 2 which established a uniform national policy with respect to notice creditors must give consumers if changes in consumer credit accounts are made, and under what circumstances those changes could apply to outstanding balances in such accounts.)

25. Do the provisions covering changes in the terms of consumer credit accounts announced April 16 affect Federal finance charge limitations for covered creditors?

Answer: They do not affect maximum rates permitted to creditors provided for under the Depository Institutions Deregulation and Monetary Control Act of 1980. Federal finance charge limitations for other covered creditors, such as oil company credit programs, are superseded.

26. A closed-end loan is extended on an unsecured basis. Some time after the loan is closed, the creditor takes a security interest in the property purchased with the proceeds. Does the addition of the security interest affect the classification of the loan as covered credit?

Answer: No. The loan was originally covered and remains so, despite the later addition of a security interest.

27. Is a loan for the payment of personal income taxes to be included in covered credit?

Answer: Yes. Unless one of the exceptions, such as a loan secured by a savings deposit, applies, the loan is covered credit.

28. A creditor extends loans which are partially guaranteed by the federal or state government. Should the full amount of the loan be considered exempt from covered credit, or only that portion subject to the guarantee?

Answer: So long as any portion of the loan is guaranteed, the entire loan comes within the exemption and should be excluded from covered credit.

CONSUMER CREDIT

Covered Credit -- Page 9

29. Is the financing of insurance premiums by an insurance company considered covered credit?

Answer: Yes. Unless the credit is secured by the insurance policy to which the premiums apply, it is covered credit.

30. Where a holding company includes savings and loan subsidiaries subject to the jurisdiction of the Federal Home Loan Bank Board, which agency should receive the holding company's reports and any special deposits?

Answer: If the report is filed by the holding company on behalf of all of the subsidiaries, the reports and any deposit should be handled by the Federal Reserve Bank for that holding company. If the holding company designates one of its subsidiaries to file the reports, the agency with jurisdiction over that subsidiary should receive the reports and any special deposit. For example, if the holding company designates a savings and loan association subject to the Federal Home Loan Bank Board, that agency should receive the reports. If, on the other hand, the holding company selects a subsidiary subject to the Federal Reserve Board, the appropriate Federal Reserve Bank should receive the reports.

The Base -- Page 7

20. Must a holding company or other parent corporation elect a single base reporting method for all of its subsidiaries or may each subsidiary choose between the March 14 base and the adjusted base, in compiling aggregate figures for the credit reports?

Answer: The holding company or parent corporation must elect a single method which will be binding on all of its subsidiaries.

21. Prior to March 14, 1980, a covered creditor enters into a binding contract for a sale without recourse of covered credit to occur after March 14. The selling creditor will no longer extend the type of covered credit that is being sold. May the base of the purchasing creditor be adjusted?

Answer: Assuming that the contract is in all other respect enforceable and the parties agree to the transfer of the base, the selling creditor may reduce its base by the amount of covered credit sold and the purchasing creditor may increase its base by the same amount. In that event, the adjustment of the bases should be promptly reported to the Federal Reserve Bank or other appropriate agency at the time the sale is completed.

CONSUMER CREDIT

Changes in Terms of Consumer Credit Accounts -- Page 1

1. Under the amendments to the consumer credit restraint program announced April 2 establishing a uniform national policy with respect to notice creditors must give consumers if changes in consumer credit accounts are made, and how outstanding b balances may be handled, may a covered creditor impose a charge (e.g., a transacton charge or an annual fee), adopt a different method for computing the balance on which a finance charge is imposed, or elimate a "free-ride" period if any of those actions is otherwise prohibited by state or federal law?

Answer: No. The change in terms amendment is not intended to allow a creditor to impose a charge in excess of the maximum permitted by law, or to change the method of computing the balance on which a finance charge is imposed (including elimination of a "free-ride" period), if a particular method or a "free-ride" period is either required or prohibited by law.

2. When does a consumer "incur additional debt" so as to trigger acceptance of the new terms?

Answer: For purchases, it is the date of the purchase transaction. For check and share draft accounts with a line of credit, it is the date that the credit extension is debited to the consumer's account. For all cash advances on a credit line, it is the date that the advance is debited to the consumer's account.

3. If a creditor changes the terms of an account, may it continue to use its existing stock of initial and periodic disclosure statements required by (Truth in Lending) Regulation Z, despite the fact that those statements reflect the old account terms?

Answer: Yes. A creditor may use its present stock of disclosure forms so long as they are amended as necessary by correction notices or other information sent along with the inaccurate forms.

4. If a customer incurs additional debt several months after the effective date of change in the terms of the account may a creditor apply the new account terms to a balance that was outstanding on the effective date, even though the customer has paid off a portion or all of that balance?

Answer: No. A creditor may apply the new terms only to the balance outstanding on the date that the customer makes the charge, or to the balance outstanding during the billing cycle within which the customer makes the charge.

5. If a consumer has authorized his or her account to be automatically and periodically debited to pay premiums for credit life, disability, or similar insurance, does such automatic debiting after the effective date of a change trigger acceptance of the new terms?

Answer: If the insurance coverage was voluntarily purchased, and can be voluntarily terminated, and if the creditor in its notice to customers indicates that such preauthorized charge will be considered an agreement by the customer to the change,

CONSUMER CREDIT

Changes in Terms of Consumer Credit Accounts -- Page 2

then such automatic debiting will trigger acceptance. If the insurance coverage was required in connection with an extension of credit, then automatic debiting of such premiums to an open-end account cannot be considered "incurring additional debt".

6. A covered creditor has the operational capacity -- and is permitted by state law -- to impose two different sets of terms on old and new credit balances. May the creditor utilize the provisions of the April 2 announcement for changes in consumer credit accounts, but permit its customers to pay off outstanding balances on the old terms, even where those customers incur additional debt after the effective date of the change in terms?

Answer: Yes. A creditor that wishes to do so may continue to impose the old account terms on existing balances, imposing the new terms only on additions to those balances. The notice of the change in terms should be modified to reflect this fact.

18. If a corporation reporting on form FR 2062e does not have timely, or any, records for some components of the corporation's indebtedness to non-U.S. entities--in particular, debt initially placed in the United States through third parties, and open-book credit--and is unable even to make a "good faith" estimate of such components, how should these items be reported?

Answer: It is not necessary for reporting corporations to determine the amount of debt issued directly to U.S. lenders or raised through U.S. dealers or other U.S. third parties that is now held by non-U.S. entities. No part of the outstanding amounts of such debt should be reported in item A2 of form FR 2062e. However, a shift toward placing debt abroad through U.S. third parties for other than normal business reasons would, of course, not be consistent with the spirit of the Special Credit Restraint Program.

Reporting corporations are expected to include open-book credit (trade notes and accounts payable) in reporting their indebtedness to non-U.S. entities, if this is feasible. If data on net payables to non-U.S. subsidiaries and affiliates and/or gross payables to other non-U.S. entities are available, but not on a timely basis, the corporation should consult with its Reserve Bank as to whether to include this component with a lag or to make some other adjustment. If there is no practical way for the corporation to develop data on open-book credit owed to non-U.S. entities, this component may be omitted from item A2 but the Reserve Bank should be informed of the omission. In any event, open-book credit--and all other components as well--should be reported on a consistent basis from month to month.

19. May data be reported as of some day other than the one called for on the reporting forms--that is, other than the last Wednesday of the month for commercial banks, branches and agencies of foreign banks and bank holding companies, and the last business day of the month for all other reporting entities?

Answer: It is not necessary to develop data as of the stipulated day if records for all or part of the reporting entity are generally available only as of some other day during the month. However, data should be reported on a consistent basis from month to month, and the date (or dates, in the case of mixed reporting) to which they refer should be noted on the reporting form.

20. At least part of the data for a bank's foreign offices that are required to complete the bank's (or holding company's) Special Credit Restraint Program report normally do not become available to the U.S. parent in time to permit filing the report with the Reserve Bank by the stipulated deadline. Is an extended deadline available? May some or all data be reported with a one-month lag? For example for the April report, may the "current month" in fact be March either for some items in their entirety, or for the foreign-office component of all items?

Answer: Reporting problems of this kind should be discussed with the Reserve Bank, since they will be considered on a case-by-case basis. In general, extension of the reporting deadline by a few days is preferable to lagged reporting, especially for data relating to loans. In cases where lack of timely data for

foreign offices relates only to the liquidity and capital measures, reporting with a one-month lag of items affected by the foreign data will be considered. Any such adjustments in reporting must be approved by the Reserve Bank in advance.

21. Are industrial revenue bonds to be included in total loans and leases subject to the 6 to 9 percent growth limitation?

Answer: No. Industrial revenue bonds are defined as investments, not loans. However, Reserve Banks should be alert to the possibility of a bank's arranging an industrial revenue bond financing as a substitute for the commercial and industrial loan the bank would have made in the absence of the Special Credit Restraint Program. Any bank that appears to be acquiring an unusually large amount of industrial revenue bonds should be asked for an explanation.

22. Are factoring receivables included in total loans subject to the 6 to 9 percent limitation?

Answer: Since the instructions to the Call Report appear to define such accounts as loans, they should be defined as loans for purposes of the Special Credit Restraint Program.

MANAGED LIABILITIES -- Page 2*

2. When should interest accrued but unpaid on time deposits be considered subject to the marginal reserve/special deposit program?

Answer: Interest amounts accruing on any managed liabilities are subject to the marginal reserve/special deposit program only when those amounts are credited to the accounts. Thus, any interest amount not included in customer account balances is not a managed liability.

3. How should the managed liabilities base be calculated in the case of a merger of another bank into a member bank?

Answer: The base for the merged bank should be calculated by combining the actual amount of managed liabilities outstanding for each bank during the base periods. If such data are not available, the surviving bank may use the base of either bank entering the merger, or $100 million, whichever is larger. With respect to any reduction in foreign loans in future periods, however, if either bank had such loans, the surviving bank must submit reports combining the foreign loans outstanding during September 13-26, 1979, for both banks entering the merger.

4. Are Eurodollar placements or term federal funds sold to foreign offices of other banks to be included in foreign loans?

Answer: Yes. Reductions in such assets permit banks to extend credit to domestic borrowers without increasing managed liabilities subject to the marginal reserve/special deposit requirement.

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*The last previous entry under this heading was in the set of Q&As dated March 26 and had no page number or question number.

SHORT TERM FINANCIAL INTERMEDIARIES

Unit Investment Trusts -- Page 1

1. Section 229.12(b)(4) of revised Subpart B provides that a unit investment trust established after March 14, 1980, shall have a base equal to its covered credit if, among other things, the units are held entirely by persons who held units in an expiring trust of the same sponsor with a base equal to the amount of its covered credit. How can a sponsor be certain, for purposes of disclosure to investors, that all persons purchasing units in a new trust held units in an eligible expiring trust?

Answer: The sponsor of any unit investment trust may treat the holders of record on the books of the trustee as the unit holders for purposes of satisfying the existing unit holder requirement. The Board expects that broker-dealers and other holders of record will make reasonable efforts to offer units of new trusts to beneficial holders of expiring trusts.

2. If a unit investment trust has a base equal to the amount of its covered credit and the proportion of its units held by trustees and other fiduciaries changes through secondary market transactions, does its amount of covered credit change?

Answer: No. If it has a base equal to its covered credit at the time it is established its unitholders at expiration will be eligible to purchase units in a new trust with a base equal to the covered credit of the new trust even if the proportion has changed. There is no requirement that the covered credit of the new trust be identical to that of the expiring trust.

3. On what date is the amount of a unit investment trust's covered credit determined?

Answer: The value of a unit investment trust's assets should be determined on the date of deposit though the special deposit will not be made until the settlement date. The proportion of trustees or other fiduciaries holding units should be determined as of the reporting date, two days prior to settlement.

Bank Trust Activities -- Page 1

1. Are collective investment funds covered creditors?

Answer: All collective investment funds primarily[1/] investing in short term assets, including short term investment funds, are covered creditors. However, if a covered creditor does not hold any covered credit, for instance because all its liabilities are to exempt fiduciary accounts, it need not file reports.

2. Are master notes and similar arrangements covered creditors?

Answer: Yes. Any collective investment vehicle of a bank including master notes and open end repurchase agreements are covered creditors. The extensions of credit under a master note are equal to the amount funded at any one time, not the limit of the note.

1/ For definition of "primarily" see second paragraph of the answer to Question No. 1, on the first page of this set of questions and answers.

SHORT TERM FINANCIAL INTERMEDIARIES

General -- Page 1

1. What does "primarily" mean?

Answer: For a managed creditor, "primarily" means 50 percent. However, if a fund's investment objective is to invest in equities or in long or medium term debt securities, it will not become a covered creditor unless it meets the 50 percent test on an average basis for a period of 13 reporting weeks after March 14, 1980. Thus, if for any 13 week period the average of its daily percentage of assets with maturities of 13 months or less is 50 percent or greater, the investment company or collective investment fund becomes a managed creditor. Once an investment company or collective investment fund becomes a managed creditor, it remains a managed creditor and must file weekly reports unless it receives the Board's permission to withdraw from managed creditor status.

For a unit investment trust "primarily" means 100 percent, and is determined as of its settlement date. A trust whose investments have initial maturities of 14 months may be 100 percent invested in assets with maturities less than 13 months for most of its duration. Therefore in order to avoid the special deposit requirement a unit investment trust must be fully invested in longer term assets on its settlement date.

2. What is included in extensions of credit?

Answer: In general, all assets except coin and currency, physical assets such as furniture, equity securities, and the creditor's special deposit with the Federal Reserve Bank are extensions of credit. Extensions of credit include checking accounts, receivables, and prepaid expenses.

3. Are registered investment companies in Puerto Rico, the Virgin Islands, and other U.S. Territories covered creditors?

Answer. Yes.