FEDERAL RESERVE BANK
OF DALLAS

WILLIAM H. WALLACE
FIRST VICE PRESIDENT
AND CHIEF OPERATING OFFICER

DALLAS, TEXAS 75222

February 7, 1989

Circular 89-6

TO: The Chief Executive Officer of all
member banks and others concerned in
the Eleventh Federal Reserve District

SUBJECT

Request for public comment on a proposal to amend Regulation Z (Truth in Lending) to implement the Home Equity Loan Consumer Protection Act

DETAILS

The Board of Governors of the Federal Reserve System has requested public comment on a proposal to amend its Regulation Z, Truth in Lending, to implement the Home Equity Loan Consumer Protection Act. The proposed amendment requires creditors to provide consumers with disclosures when they receive an application for an open-end home equity line of credit. It also would limit a creditor's ability to terminate the loan and accelerate any outstanding balance, or to change the terms of a loan after it has been opened.

Comments should be addressed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551. All correspondence should refer to Docket No. R-0655 and must be received by March 21, 1989.

ATTACHMENTS

The Board's press release and the material as published in the Federal Register are attached.

MORE INFORMATION

For further information, please contact Jane Anne Schmoker at (214) 651-6228.

Sincerely yours,

William H. Wallace

For additional copies of any circular please contact the Public Affairs Department at (214) 651-6289. Banks and others are encouraged to use the following incoming WATS numbers in contacting this Bank (800) 442-7140 (intrastate) and (800) 527-9200 (interstate).

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FEDERAL RESERVE press release

For immediate release January 12, 1989

The Federal Reserve Board today issued for public comment a proposal to amend its Regulation Z, Truth in Lending, to implement the Home Equity Loan Consumer Protection Act.

Comment is requested by March 21.

The proposed amendment requires creditors to provide consumers with disclosures when they receive an application for an open-end home equity line of credit. More specifically, creditors will be required to supply consumers with information regarding the payment options, any fees imposed by the creditor, and other terms of the agreement. If the home equity line of credit has a variable-rate feature, the creditor must provide information about the index upon which the rate is based including a 15-year history of changes in the index values.

In addition to these disclosure requirements, the proposed amendment would limit a creditor's ability to terminate the loan and accelerate any outstanding balance, or to change the terms of a loan after it has been opened. The limitations also prohibit the type of index that can be used for home equity lines of credit with variable rates.

The Board's proposed amendment also imposes duties on third parties who provide applications to consumers and modifies the rules relating to advertisements for home equity loans.

The Board's notice is attached.

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FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Reg. Z: Docket No. R-0655]

Truth in Lending; Home Equity Disclosure and Substantive Rules

AGENCY: Board of Governor of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: The Board is publishing for comment a proposal to amend Regulation Z (Truth in Lending). The proposal implements provisions of the Home Equity Loan Consumer Protection Act of 1988, which requires creditors to provide consumers with more information for open-end credit plans secured by the consumer's dwelling, and imposes substantive limitations on these plans. Creditors would have to provide information at the time an application is provided to the consumer, including information about the payment terms,

fees imposed under the plan, and, for variable-rate plans, information about the index and a fifteen-year history of changes in the index values. Creditors would be required to provide consumers with a brochure prepared by the Board (or one substantially similar) describing home equity plans. The proposal also imposes duties on third parties who provide applications to consumers and modifies the rules relating to advertisements for home equity plans.

In addition to these disclosure requirements, the proposal would amend Regulation Z to implement new substantive limitations imposed by the statute. The regulation would limit a creditor's right to terminate a plan and accelerate any outstanding balance, or to change the terms of a plan after it has been opened, as well as limit the type of index that can be used for variable-rate plans.

DATES: Comments must be received on or before March 21, 1989.

ADDRESSES: Comments should refer to Docket No. R–0655 and be mailed 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 to the guard station in the Eccles Building Courtyard on 20th Street NW. (between Constitution Avenue and C Street NW.) any time. Comments will be available for inspection 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: Sharon Bowman, Leonard Chanin or Thomas Noto, Staff Attorneys, or Mike Bylsma, Senior Attorney, Division of Consumer and Community Affairs, at (202) 452–3667 or 452–2412; for the hearing impaired only, contact Earnestine Hill or Dorothea Thompson, Telecommunications Device for the Deaf, at (202) 452–3544, Board of Governors of the Federal Reserve System, Washington, DC 20551.

SUPPLEMENTARY INFORMATION:

(1) Background

In December 1987 the Board proposed amendments to Regulation Z to change the existing disclosure requirements for home equity lines of credit secured by the consumer's principal dwelling (52 FR 48702). The proposal would have (1) required disclosures to be given at the time an application form is provided to the consumer (or before the consumer pays a nonrefundable fee, if that occurs earlier); (2) required that the disclosures be segregated from other information; and (3) increased the number of required disclosures. Subsequently, the Home Equity Loan Consumer Protection Act was enacted on November 23, 1988 (Pub. L. No. 100–709). The law superseded the Board's proposal. While both the Board's 1987 proposal and the statute address many of the same disclosure and advertising issues, the statute also places substantive limitations on how home equity plans operate.

The statute, which requires the Board to issue regulations, provides that the statutory provisions and rules adopted by the Board shall apply to open-end credit plans entered into five months after the promulgation of final regulations. The Board is proposing amendments for comment, and expects to adopt final regulations in May 1989. Compliance with the law would be mandatory around October 1989.

Under Truth in Lending and Regulation Z, creditors offering open-end credit are currently required to provide consumers with a limited amount of information prior to the first transaction under the plan. The disclosures must reflect the features of the specific plan. Creditors must disclose the information clearly and conspicuously, but are permitted to integrate the disclosures into the contractual agreement.

The statute and proposed amendments to the regulation leave in place the existing disclosure requirements. They would add, however, two requirements to this framework. First, as is the case for closed-end adjustable-rate mortgages that are secured by the consumer's principal dwelling and have a term over one year (see § 226.19(b) of Regulation Z), creditors generally would be required to provide detailed disclosures about their home equity plans when an application is provided to the consumer. Second, creditors would be required to provide the information again, along with the current disclosures, prior to the first transaction under the plan.

The Board is publishing proposed sample disclosure forms to assist creditors in preparing their plan disclosures. The Board expects to publish along with the final regulation tables of values for commonly used indices for home equity plans.

(2) Proposed Amendments to Regulation Z

The Home Equity Loan Consumer Protection Act is quite detailed and, for the most part, the proposed amendments mirror the statutory requirements. The proposed amendments to Regulation Z would incorporate the disclosure provisions into a new § 226.5b of the regulation and into existing § 226.6. (A new § 226.5a has been proposed recently by the Board to implement the Fair Credit and Charge Card Disclosure Act. See 53 FR 51785, December 23, 1988.) Modifications would be made to the advertising rules contained in § 226.16, and technical amendments would be made to §§ 226.1 and 226.5.

(i) Coverage

The proposed amendments to Regulation Z would apply to all open-end credit plans secured by the consumer's dwelling, as set forth in § 226.5b. Thus, the rules apply not only to plans secured by the consumer's principal dwelling, but also to those secured by second or vacation homes.

(ii) Format of Disclosures

Unlike existing Truth in Lending requirements for closed-end and other types of open-end credit, the proposed amendments would not require that the disclosures provided at the time of application be in a form the consumer can keep. (See footnote 8 accompanying § 226.5(a).) Thus, under the proposal, although the disclosures would have to be in writing, creditors would be permitted to place the first set of disclosures on the application form the consumer returns to the creditor to apply for the plan.

Section 226.5b(a) of the proposal would require most of the disclosures to be grouped together and "segregated" from unrelated information provided to the consumer in connection with the application. The brochure and the variable rate information could be provided either separately from or with the other disclosures. Under the proposal, greater flexibility would be permitted in complying with the segregation standard than currently exists for closed-end credit. Disclosures for home equity plans tend to be less concise and more narrative in form than those for closed-end credit. Therefore, the Board proposes to apply a more liberal standard that would permit information that explains or expands on the required disclosures to be included. Information on other aspects of the plan that is not related to the required disclosures, such as underwriting criteria, however, would not be permitted to be interspersed with the disclosures. Such information, of course, could be provided as long as it is separated from the required disclosures.

The segregation standard would not apply to the second set of disclosures provided by the creditor prior to the first transaction under the plan. The additional disclosures would be given

with the information currently required under Regulation Z, which is not required to be segregated from other information. These disclosures could be combined and could be integrated into the contract. Like the disclosures currently required, the additional disclosures would have to be in a form the consumer can keep.

In the first set of disclosures, § 226.5 (a)(2) of the proposal provides that certain items would be further highlighted by requiring them to precede the other disclosures. Consumers would be notified that (1) they should keep a copy of the disclosures; (2) they have a right to obtain a refund of fees if any terms change and they decide not to enter into the contract as a result; (3) they risk the loss of the dwelling in the event of default; and (4) a creditor may terminate a plan or suspend future advances under certain circumstances.

Creditors would state all aspects of their plans in the first set of disclosures. For example, if a creditor offers several payment options, all options would have to be set forth. Furthermore, if any aspects of a plan are linked together—for example, if the consumer can obtain only certain payment options in conjunction with plans of certain lengths—the creditor must clearly disclose the relation among those plan features. As an alternative to the combined disclosure method, the Board proposes to permit creditors to create separate disclosure documents where features may vary. Creditors pursuing this latter alternative would have to include a statement in the early disclosures that the consumer should "ask about" the creditor's other home equity programs. Creditors would have to provide disclosures in response to any such request.

(iii) Timing of Disclosures

Section 226.5b(b) would require the disclosures and a brochure to be given to consumers at the time an application is provided. In the case of applications contained in magazines or taken by telephone or through third parties, footnote 10a would allow the creditor to mail or deliver the disclosures and brochure to the consumer within three business days of receipt of the application.

In addition to providing these disclosures early in the application process, the statute and § 226.6(e) would require creditors to provide all of the disclosures again along with the disclosures currently required for open-end credit, to the extent they are not duplicative. Creditors also would disclose a list of the conditions that permit the creditor to terminate the plan, freeze or reduce the credit limit, and implement modifications to the original terms. (This requirement could be met by providing a separate list or by identifying the provisions in the contract which contain such conditions.) The disclosures would be provided prior to the first transaction under the plan, in accordance with the existing rule in § 226.5(b). (See the discussion below concerning the specific requirements for this second set of disclosures.)

(iv) Duties of Third Parties

In addition to requiring creditors to provide disclosures to consumers at an earlier time, § 226.5b(c) of the proposed amendments also would impose a duty on third parties who provide applications to consumers. The statute requires that a third party, such as a loan broker, that provides a consumer with an application also must give a brochure and disclosures. The statute recognizes, however, that in some circumstances third parties may not be able to provide disclosures since specific information about the plan terms may be unavailable.

The Board believes that requiring both a third party and a creditor to provide the consumer with identical information about the same plan may result in unnecessary duplication. Under § 226.5b(c) of the proposal, therefore, a third party would be required to provide disclosures only if that party has the disclosures for a creditor's particular home equity plan in its possession. Third parties would not have an affirmative duty to obtain such disclosures about a creditor's programs, or to create a set of disclosures based on what the third party knows about a creditor's program. If, however, a creditor supplies disclosures to a third party along with its application form, the third party would have to give the consumer the disclosures. In all cases, consumers will be provided disclosures by the creditor within three days after the creditor receives the application. While consumer shopping might be enhanced if third parties provided the disclosures at the earlier time, consumers will still be able to shop for credit since neither a creditor nor any other party is permitted to collect a nonrefundable fee until three days after disclosures have been received by the consumer.

Although the duty of third parties to provide the disclosures may arise infrequently, the proposal would require third parties to give the home equity brochure at the time an application is given to the consumer. Because providing the brochure is not linked to the availability of information from a creditor about its specific plan, the Board believes third parties would have access to the brochure, and, thus, be able to provide it with the application. (See the discussion below concerning the responsibility of the creditor if the third party has already given the consumer a brochure.)

(v) Content of Disclosures

Section 226.5b(d) of the proposal lists the information that would be given to consumers when they apply for home equity plans. As is the case with existing Truth in Lending disclosure rules, the information would be provided only to the extent applicable; thus, for example, if negative amortization cannot occur in a program, no mention of it need be made. Because the disclosures need not be in a form the consumer can keep, the consumer would be advised to retain a copy of the disclosures. Creditors would include a statement of any time by which an application must be submitted to obtain specific terms disclosed. If creditors choose not to "guarantee" all or some of the terms, they would provide a statement of the terms that may change prior to opening the plan. Creditors also would have to notify the consumer of the right to refund of all fees paid in connection with the application if any disclosed terms (other than a variable rate) change prior to opening the plan, and as a result the consumer chooses not to enter into the plan. Creditors would have to disclose the fact that a security interest is being taken in the consumer's dwelling and that the consumer may lose the home in the event of default.

(A) Possible Actions by Creditor

Under § 226.5b(d)(4) of the proposal, a statement must be provided that, under certain circumstances, a creditor may terminate the plan and accelerate any outstanding balance, prohibit additional advances or reduce the credit limit or, as set forth in the initial agreement, implement modifications to the original terms. In light of § 226.5b(f)(3)(i) of the proposal, which would permit such modifications if they are explicitly provided for in the contract, the Board is proposing to add this last condition to the disclosure. A creditor would be required to state if fees may be imposed if the account is terminated. Consumers would be notified that they can receive, upon request, a list of the conditions that permit the creditor to terminate the plan, prohibit additional advances or reduce the credit limit, and implement modifications during the term of the plan. Upon receiving a request from a consumer, creditors would be required

to provide this information in writing in a form the consumer can keep. (See § 226.5b(g) of the proposal.)

Although the statute calls only for a disclosure of the right to receive upon request the list of conditions, the Board proposes in § 226.5b(d)(4)(iii) to permit creditors to provide the actual list with the early disclosures in lieu of that statement. The Board believes this flexibility may help consumers compare home equity lines, and may assist creditors by reducing the circumstances in which consumers will request that this information be provided. Creditors would be permitted to provide this list with the segregated disclosures or apart from those disclosures. Section 226.6(e) would provide that the list of these conditions also would have to be given with the disclosures currently required for open-end credit. (This requirement could be met by identifying the provisions in the contract which contain such conditions.)

(B) Payment Terms

Under § 226.5b(d)(5) of the proposal, creditors would be required to describe the payment terms of the plan, including the length of the draw period and any repayment period. (The combined length of the draw period and any repayment period would not have to be stated.) If the terms are indefinite, creditors would state that fact. All payment options under the plan would be stated, including any different payment terms that may exist during the draw period or during any repayment period, as well as any differences that may apply within either period. If the plan permits the consumer to convert any of the loan balance to a fixed term loan, this information would be provided in the disclosures. How the minimum periodic payment is determined, the frequency of payments, and whether making only the minimum payments would not repay any or all of the principal balance during the draw and repayment periods would be set forth. The proposed regulation also calls for a disclosure if a balloon payment is required under the plan—to give consumers an accurate picture of their payment obligations. An explanation of the balance computation method would not have to be provided.

Creditors would disclose an example, based on an assumed $10,000 outstanding balance and a recent annual percentage rate (APR), showing the minimum periodic payment and any balloon payment, and the time it would take to pay off the balance if the consumer made only those payments. Footnote 10c of the proposal would provide that, for fixed rate plans, a recent APR is one that has been in effect under the plan within the twelve months prior to the date the disclosures are provided to the consumer. For variable rate plans, a recent APR would be the most recent rate provided in the historical table, or a more recent rate.

(C) Annual Percentage Rate

Section 226.5b(d)(6) of the proposal provides that, for fixed-rate plans, a recent APR would have to be provided. Consumers would be told that the APR does not include costs other than interest.

(D) Fees Imposed By the Creditor and By Third Parties

Under § 226.5b(d)(7) of the proposal, creditors would have to provide a description and the amount of charges required to open and use the account and a statement of when the consumer must pay the charges. These charges could be stated as an estimated dollar amount for each fee, or as a percentage of a hypothetical amount of credit. These fees include application fees, points, annual fees, and transaction fees. Under § 226.5b(d)(8) of the proposal, an estimate of fees imposed by third parties stated as a single dollar amount or a range (and a statement that the consumer may request more specific information about such fees from the creditor) also would be provided.

(E) Other Provisions

Under § 226.5b(d)(9), a statement if the plan has a negative amortization—which will reduce the consumer's equity in the dwelling—most be provided. Section 226.5b(d)(10) would require creditors to state any limitations on the number of extensions or amount of credit that can be obtained during any time period and any minimum draw or minimum outstanding balance requirement stated as dollar amount or as a percentage. Section 226.5(d)(11) would require that consumers be told to consult a tax advisor regarding the deductibility of interest and charges under the plan.

(vi) Variable-Rate Disclosures

Section 226.5b(d)(12) of the proposal would require creditors to provide information about the variable-rate feature contained in a plan. Many of these disclosures closely parallel the disclosures currently required for closed-end variable-rate transactions secured by a consumer's principal dwelling. The Board is proposing to add a few additional variable-rate disclosures to those required by the statute. These minor additions would help make the home equity rules and the rules for closed-end ARMs more uniform, and thus make compliance easier for creditors. Furthermore, these additional disclosures would provide consumers with more complete information about the variable-rate feature of home equity lines.

(A) Index and APR

Creditors would be required to state that the APR may change and that the payment or term may change due to the fact that the APR is variable. The frequency of changes in the APR would be provided. Creditors would have to identify the index used to determine rate adjustments and a source of information about the index. Creditors would have to describe how the corresponding APR will be determined (for example, by stating that a margin is added to the index value). If the initial rate is discounted, a disclosure of that fact as well as the disclosure forms could be preprinted and rate information may not be accurate, consumers would be told to "ask about" the current index value, margin, and APR. Rules relating to changes in the index value and resulting changes in the APR would be set forth. This provision would require an explanation, for example, of a preferred-rate provision, where the rate will increase upon the occurrence of some event, such as an employee leaving the creditor's employ. Similarly, an explanation would have to be given if the plan permits the consumer to convert from a variable rate plan to a fixed rate.

(B) Rate and Payment Limitations

Any annual rate caps must be stated and, if there are no such limits, that fact must be stated. The maximum rate that may be imposed under each payment option under the plan also would be provided. This rate could be stated as a specific rate (for example, 18%), or as a percentage above an initial rate (for example, 5% above the initial rate). In either circumstance creditors could use a range in expressing the maximum rate in the early disclosures. In addition, creditors would have to show, if the maximum rate were in effect, the minimum periodic payment based on a $10,000 outstanding balance. (If a range is used, the highest rate in the range should be used for this disclosure.) Finally, any payment limitations would be provided.

(C) Historical Table

A 15-year historical table, based on an assumed $10,000 extension of credit and showing how the APRs and payments would have been affected by the index value changes under the plan, would be

provided. If the values for an index have not been available for 15 years, creditors would need only go back as far as the values have been available in giving the history and may start the example at the year for which values are first available. The history would reflect the method of choosing values for each plan. For instance, if an average of index values is used, averages would be used in the history, but if a single index value is used, a single index value would be shown. The creditor would assume one date within a year (or one period, if an average is used) on which to base the history of index values for each loan plan. The creditor could choose to use index values as of any date or period as long as the index value as of this date or period is used for each year in the index history. Only one index value per year need be shown, even if the plan provides for adjustments to the APR or payment more than once a year. In such cases, the creditor would assume that the index rate remained constant for the full year for the purpose of calculating the annual percentage rate and payment. Updating will be necessary only once each year to reflect the most recent year's index value. To assist creditors in constructing histories of certain common indices, the Board expects to include tables of index values when the final rule is published. In its final regulation, the Board expects to publish rate information for the prime rate published in the Wall Street Journal, the average prime rate published in the Federal Reserve Bulletin, and United States Treasury securities adjusted to constant maturities of 90 days and 6 months. The Board requests that commenters provide the names of any other indices for which it would be useful to have rate histories.

The payment figures in the example must reflect all significant loan program terms. For example, features such as rate and payment caps, a discounted APR, negative amortization, and interest carryover would be taken into account by creditors in calculating the payment figures. One payment per year would be shown in the table, even though payments may vary during a year. (The calculations, however, should be based on the actual payment computation formula.) Balloon payments need not be reflected in the table.

Because disclosures will be given early, creditors would need to assume a value for the margin in order to do the calculations for the example. Creditors would select a margin that they used during the preceding six months and disclose on the form that the margin is one that they have used recently. The margin selected may be used until a creditor updates the disclosure form to reflect the most recent 15 years of index values. Similarly, if the home equity plan has a discounted initial rate, creditors also will be permitted to assume an amount by which the initial rate will be discounted—which is representative of the amount of a discount used by the creditor during the preceding six months—and disclose on the form that the initial rate has been discounted.

In setting forth payment information, both the draw and any repayment period would be illustrated in the table. In providing this information, creditors would assume that the $10,000 balance is reduced according to the terms of the plan. To minimize compliance costs, the Board proposes to permit the use of a representative term within a range of a five-year period in setting forth the draw and repayment information in the table. For example, if a creditor offers plans with a five-year draw period, and repayment periods ranging from six to fifteen years, the creditor would use the actual length of the draw period. In figuring the repayment period for the table, the creditor could use any term from six to ten years (for example, eight years), and any term from eleven to fifteen years (for example, thirteen years). If different payment options are available during either period, payments under each option would have to be shown.

(D) Other Information

Consumers would be informed that rate information will be provided with the periodic statement.

Sample home equity disclosure forms that show how the proposed requirements might be met are provided in proposed Appendix G.

(vii) Later Disclosures

As discussed earlier, § 226.6(e) would require creditors to provide the disclosures set forth in § 226.5b(d) a second time along with the disclosures would be provided prior to the first transaction under the plan, in accordance with the existing rule in § 226.5(b), and could be integrated into the contract.

(A) Duplicative Information

Information that duplicates the current disclosures need not be provided. For example, because § 226.6(a)(4) and (b) require the disclosure of any finance and "other" charges, respectively, creditors would not have to disclose fees imposed by the creditor (see proposed § 226.(d)(7)) or fees imposed by third parties (see proposed § 226.5b(d)(8)).

(B) Inapplicable Information

Creditors need not provide information that is inapplicable. For example, because § 226.5(a)(1) requires that the disclosures be in a form the consumer may keep, creditors would not make the statement in proposed § 226.5b(d)(1) that consumers should make a copy of the disclosures. Similarly, because proposed § 226.6(e)(2) would require creditors to disclose the conditions under which the creditor may, for example, terminate the plan and require payment of the outstanding balance in full in a single payment upon termination, creditors need not disclose that the consumer may receive, upon request, this information, as required by proposed § 226.5b(d)(4).

(C) Current Information

Creditors would be required to provide current information about aspects of the plan that may vary among consumers. For example, if the creditor offers a variety of payment options and the consumer chooses one option (and the others are unavailable), the specific payment terms selected would have to be disclosed. Similarly, if the first set of disclosures stated the maximum APR that could be imposed (for variable-rate plans) as a range, the later disclosures would have to reflect the specific rate cap.

(D) Historical Information

Creditors could provide the same historical information about the program that was given in the first set of disclosures. For example, the historical table provided in the earlier disclosures would not have to be modified for the later disclosures to reflect more recent margins or discounts, since the table is intended to show historical rate fluctuations and their effects on payments (and need only be updated once a year).

(viii) Consumer Brochure

Section 226.5b(e) would require creditors and third parties providing applications to furnish consumers with a brochure prepared by the Board describing home equity plans, or a brochure that provides substantially similar information. As required by the statute, the brochure will describe home equity plans, including the potential advantages and disadvantages. The brochure also will provide guidance on how to compare home equity plans with closed-end credit. The Board envisions that any substitutes must be, at a

minimum, comparable in substance and comprehensiveness, recognizing that some lenders' brochures may contain more detailed descriptions of their particular home equity programs than contained in the Board's brochure. The Board is currently preparing a brochure and will have it available when the regulation is issued in final form.

The proposal would mirror the statute in requiring third parties to provide consumers with the brochure if an application is given to the consumer. The Board believes, however, that requiring a second brochure to be given by the creditor in such circumstances is unnecessary. Therefore, the Board believes that the creditor's duty to provide the brochure would be met if the third party provides the brochure to the consumer. This will avoid duplication. The creditor would have a duty, however, to ensure that the third party has provided the brochure if the creditor chooses not to give the consumer the brochure.

(ix) Right of Rescission—Material Disclosures

The Board is soliciting comment on whether it should amend footnote 36, accompanying § 226.15(a)(3) of the regulation, to provide that the payment information required under proposed § 226.5b(d)(5) (i) and (ii) that is given at the time an account is opened be treated as "material disclosures" for purposes of the right of rescission (§ 226.15). Section 226.15(a)(3) states that the consumer may exercise the right of rescission until midnight of the third business day following the opening of the plan, delivery of the notice of the right to rescind, or delivery of all "material disclosures," whichever occurs last. Footnote 36 of the regulation currently defines material disclosures to include the method of determining the finance charge and the balance upon which a finance charge will be imposed, the annual percentage rate, and the amount or method of determining the amount of any membership or participation fee that may be imposed as part of the plan. Including such payment information in the definition of "material disclosures" would be consistent with the material disclosure definition in the closed-end credit rescission provisions.

(x) Advertising Requirements

Under the open-end advertising rules in § 226.16, any reference to an item required to be disclosed under § 226.6 requires the disclosure of cost information such as the APR, any membership or participation fee, and any minimum, fixed, transaction, or activity charge. Under current rules, a creditor may refer to a payment term in an advertisement for open-end credit without having to make additional disclosures about other material terms. Furthermore, only items stated affirmatively require further information. Under § 226.16(d)(1) of the proposed regulation, any reference to a payment term in a home equity advertisement would "trigger" further disclosures, including loan fees, estimates of other fees that may be imposed, and, for variable-rate plans, the maximum rate that may be imposed under the plan. Proposed § 226.16(d)(3) provides that, if such an advertisement states a payment amount, it would have to state, if applicable, that the plan contains a balloon payment. Furthermore, if any of the "triggers" is stated affirmatively *or* negatively, further disclosures must be given. For example, if a creditor states "no annual fee" in an advertisement, additional information must be provided.

In addition, § 226.16(d)(2) of the proposal provides that if an advertisement states a "discounted" APR it must state in equal prominence the APR derived by use of the fully-indexed value. Creditors would be prohibited by § 226.16(d)(5) from referring to home equity plans as "free money" or using similarly misleading terms. Finally, if an advertisement states that any interest under the plan may be tax deductible, the advertisement must not be misleading about such deductibility. (See § 226.16(d)(4).) For example, an advertisement referring to deductibility might include a statement that the consumer should consult a tax advisor regarding the deductibility of interest.

(xi) Substantive Limitations

The act imposes three substantive limitations on the way home equity plans can be structured. In some provisions the statute speaks in terms of creditor actions. In other provisions the statute speaks in terms of what may be contained in the credit contract. Under § 226.5b(f) of the Board's proposal, the substantive limitations would apply to both actions creditors may take and the provisions that may be contained in contracts. These limitations also would apply to assignees and holders.

(A) Index For Variable-Rate Plans

Under § 226.5b(f)(1) of the proposal, a creditor may change the APR after the plan is opened only if the change is based on an index outside the creditor's control and the index value is available to the public. This provision would prohibit a creditor from using its own prime rate or simply retaining the right to change rates at its discretion. A creditor would be permitted to use the Wall Street Journal prime rate, for example, or any other index not within the creditor's control.

(B) Termination

Under the statute and proposed § 226.5b(f)(2), creditors are prohibited from terminating an account and accelerating payment of the outstanding balance prior to the scheduled expiration of the plan. The act, however, provides three exceptions to the rule. First, a creditor may terminate the plan if there has been fraud or material misrepresentation by the consumer in connection with the plan. Second, a creditor may terminate the plan if the consumer has failed to meet the repayment terms of the agreement. This provision would permit termination only if the consumer fails to actually make payments. A creditor could not terminate a plan if, for example, the consumer, in error, sends a payment to the wrong location, such as a branch rather than the main office of the creditor. Finally, a creditor is permitted to terminate the plan if the consumer acts or fails to act in a way that adversely affects the creditor's security interest. This provision would permit termination, for example, if the consumer transferred title to the property without the permission of the creditor or if the consumer failed to maintain required insurance on the dwelling.

If any of these three events occurs, a creditor may also be able to take action short of terminating an account and accelarating payment of the outstanding balance. These three events would likely constitute circumstances that would permit a creditor to prohibit additional extensions of creditor or reduce the credit limit. (See the later discussion of the ability of a creditor to change the terms due to default and other events.)

Creditors would not be permitted to specify in their contracts other events that would permit terminating an account and accelerating payment of the outstanding balance. Thus, for example, a contract could not provide that the account will be terminated and the balance accelerated if a judgment is filed against the consumer.

(C) Change of Terms

Section 226.5b(f)(3), which implements the third substantive limitation, provides that a creditor may not unilaterally change the terms under the plan after the account has been opened. There are, however, several exceptions to this rule.

(1) Events provided for in the contract. The legislative history makes clear that a creditor was not meant to be prohibited from implementing specific changes set forth in the contract that are contemplated on the occurrence of a specific event; this exception has been incorporated in proposed § 226.5b(f)(3)(i). Both the triggering event and the resulting modification must be stated with specificity. For example, in an employee loan program, the contract could provide that a specified higher rate will apply if the borrower's employment ends. Similarly, a creditor would be permitted to suspend additional extensions of credit if the maximum APR is reached, as long as this is expressly provided for in the agreement. A creditor using this provision could only suspend advances for the period the APR would exceed the rate cap, and would have to permit further advances if the applicable rate drops to or below the cap, if that occurs during the draw period set forth in the initial agreement. The Board solicits comment on whether other examples should be provided such as permitting contracts to provide for a replacement index in the event the original index in a variable-rate plan becomes unavailable.

While the Board proposes to permit creditors to specify in the initial agreement specific changes that are contemplated on the occurrence of specific events, there are two limitations on the provisions that could be set forth in the contract. First, under the regulation, creditors would not be permitted to include a general provision in the agreement permitting them to change any or all of the terms of the plan. For example, creditors could not include "boilerplate" language in the agreement stating that they reserve the right to change the payment obligations under the plan. Second, creditors would not be permitted to include in the initial agreement any events which the regulation expressly addresses. For example, the statute and § 226.5b(f)(3)(iii) of the regulation provide that a creditor may prohibit additional extensions of credit or reduce the credit limit during any period in which the value of the dwelling that secures the plan declines significantly below the property's appraised value. Because the statute expressly provides for this situation, and specifically sets forth what action the creditor may take if it arises, the contract may not authorize the creditor to take more sweeping action. For example, a creditor could not permanently refuse to make further advances if the value of the property declines significantly below the property's appraised value, since the statute provides that further advances can be prohibited only during the period in which the value of the property remains significantly below the appraised value. Similarly, a contract may not authorize the creditor to take any additional action beyond prohibiting further advances or reducing the credit limit when the creditor reasonably believes that the consumer will be unable to fulfill the repayment obligations due to a material change in the consumer's financial circumstances—since this condition also is set forth in the statute. The Board believes permitting creditors to expand on the exceptions set forth in the statute would be inconsistent with the intent of the legislation.

(2) Changes made by mutual written agreement. The statute and the proposed amendments to the regulation prohibit *unilateral* changes. The Board proposes to permit creditors to change the terms after a plan is opened provided the consumer expressly agrees in writing to the change. Thus, for example, under footnote 10d to § 226.5b(f)(3), a consumer and a creditor could agree to extend the period during which advances can be obtained, or could agree to change the repayment terms from, for example, interest-only payments to payments that reduce the principal balance. Under the proposal, creditors would not be permitted to assume consent because the consumer uses an account (even if that implies acceptance under state law). The Board believes this will carry out the Congressional intent to limit changes after a plan is opened, yet accommodate the need for adjustments agreed to by both parties to the contract.

(3) Insignificant changes. The statute and § 226.5b(f)(3) of the proposal provide another exception to the general prohibition against changing terms, for changes to "insignificant terms." This is intended to address operational problems, such as changing the address of the creditor for purposes of sending payments. This exception would not permit a creditor to unilaterally change a term such as a fee charged for late payments.

(4) Substitution of index. Section 226.5b(f)(3)(ii) of the proposal also provides that the creditor may change the index and margin used under the plan if the original index becomes unavailable, as long as historical fluctuations in the two indices were substantially similar, and as long as the new index and margin would have resulted in a rate similar to the rate that was in effect at the time the original index became unavailable.

(5) Beneficial changes. Creditors also would be permitted under proposed § 226.5b(f)(3)(iv) to make any changes that "unequivocally benefit" the consumer as long as the change is beneficial for the entire term of the agreement. A creditor would not be able to change the payment obligations of the plan in reliance on this exception. For example, reducing the amount of the minimum payment may not be unequivocally beneficial since it may result in less principal being repaid over the term of the plan and may result in a higher total amount of finance charges. While this exception is narrow, as noted above, a consumer and creditor would be permitted to change the terms of the plan by mutual written agreement.

(6) Changes due to default and other events. Section 226.5b(f)(3)(iii) of the proposal incorporates the statutory provisions that provide that a creditor may prohibit additional extensions of credit or reduce the credit limit in four circumstances. First, a creditor may take such action if the value of the dwelling that secures the plan declines significantly below the property's appraised value for purposes of the plan. Second, a creditor may prohibit additional extensions of credit or reduce the credit line if the creditor reasonably believes the consumer will be unable to fulfill the repayment obligations under the plan due to a material change in the consumer's financial circumstances. Two conditions must be met for a creditor to use this exception. First, there must be a "material change" in the consumer's financial circumstances. For example, a significant decrease in the consumer's income would meet this part of the requirement. Second, as a result of this change, the creditor must have a reasonable belief, based on some evidence (such as failure to pay other debts), that the consumer will be unable to fulfill the payment obligations of the plan.

The third exception permits a creditor to prohibit additional extensions of credit or reduce the credit line if the consumer is in default of any material obligations under the agreement. (Sections 226.5b(d)(4) and 226.6(e)(2) require that the creditor provide or make available a list of the conditions that would permit prohibiting additional extensions of credit or reducing the credit line.) The final exception permits a creditor to prohibit additional advances or reduce the credit line because action by a governmental body either (a) precludes the creditor from imposing the agreed-upon APR (for

example, enactment of a lower state rate ceiling after the plan has been entered into), or (b) adversely affects the priority of the creditor's security interest to the extent that the value of the security is less than 120 percent of the amount of the credit line (for example, through imposition of a tax lien).

Under the proposed regulation, creditors are permitted to prohibit additional extensions of credit or reduce the credit limit only as long as any of these four circumstances exist. Thus, for example, if the creditor limits the ability of the consumer to obtain further advances due to a significant decline in the value of the dwelling, and during the length of the draw period the value of the property subsequently increases, the creditor would have to reinstate credit drawing privileges. Similarly, a creditor may reduce the credit limit only during the period any of the circumstances exists.

(D) Refund of Fees

Section 226.5b(g) of the proposal imposes a duty on a creditor to refund all fees paid by the consumer in connection with an application if any term disclosed (other than a variable rate) changes between the time disclosures are provided to the consumer and the plan is opened, and if, as a result of the change, the consumer decides to not enter into the plan. This rule applies to any fees paid in connection with the plan, such as credit report fees and appraisal fees, whether paid directly to the creditor or to third parties. This right is distinct from the existing right of rescission under § 226.15, which begins only when a plan secured by the consumer's principal dwelling is actually opened.

(E) Imposition of Fees

Finally, under § 226.5b(h) of the proposal, neither the creditor nor any other party may impose a nonrefundable fee in conjunction with an application until three business days after the disclosures and brochure have been provided to the consumer. If disclosures are mailed to the consumer, footnote 10e of the regulation provides that a fee cannot be collected until six business days after the mailing. If a refundable fee is collected prior to the consumer receiving the disclosures, the fee would have to be refunded to the consumer if the consumer decides not to enter into the agreement.

(xii) Effective Date

The statute provides that the act and regulations shall apply to: (1) Any agreement to open a plan which is entered into five months after the regulations become final; and (2) any application to open a plan which is distributed by or received by a creditor five months after regulations become final. Under this requirement, creditors would have to provide the first set of disclosures to consumers if an application is received after the effective date of the regulations, even if the application was provided to the consumer prior to the effective date of the rule. The Board plans to provide a rule in the supplemental information to the final amendments allowing creditors to provide the first set of disclosures to consumers within three days of receipt of the application in such cases.

(xiii) Disclosure Samples and Model Clauses

In connection with the other revisions, the Board is proposing to revise Appendix G of the regulation to incorporate disclosure samples (G–17A and G–17B), and model clauses (G–18) to assist creditors in preparing disclosures.

(A) Disclosure Samples

Form G–17A illustrates a variable-rate plan with 10-year draw period followed by a 5-year repayment period. The payments are based on a percentage of the outstanding balance so that, independent of rate changes, payments will vary each month during the plan. Consequently, payments are stated as a range in the minimum payment example. In the historical table, which illustrates both the draw and the repayment periods, only one payment per year is reflected and the fact that payments would have varied during each year is stated. All calculations, however, are conducted using the actual payment computation formula. The Board specifically solicits comment on whether this treatment is appropriate for such payment arrangements.

Form G–17B illustrates a variable-rate plan with interest-only payments during the draw period followed by a repayment period, the length of which depends on the size of the outstanding balance. The consumer is permitted to select between two payment arrangements—monthly or quarterly payments—during the draw period. Accordingly, the payment disclosures and examples illustrate such payment option. In addition, by including two payment columns, the form illustrates how one historical table can be used to disclose multiple payment options.

(B) Model Clauses

Appendix G–18 contains a number of model clauses that may be used in preparing disclosures. Information that must be inserted is indicated by italicized language within parentheses. Alternative language is set forth in brackets and separated by a slash. Disclosures that may not be applicable to a given plan are set forth in brackets.

(3) Economic Impact Statement

The Board's Division of Research and Statistics has prepared an economic impact statement on the proposed revisions to Regulation Z. A copy of the analysis may be obtained from Publications Services, Board of Governors of the Federal Reserve System, Washington, DC, 20551, at (202) 452–3245.

List of Subjects in 12 CFR Part 226

Advertising, Banks, banking, Consumer protection, Credit, Federal Reserve System, Finance, Penalties, Rate limitations, Truth in Lending.

(4) Text of Proposed Revisions

Certain conventions have been used to highlight the proposed revisions. New language is shown inside arrows. 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 Regulation Z (12 CFR Part 226).

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

Authority: Sec. 105, Truth in Lending Act, as amended by sec. 605, Pub. L. No. 96–221, 94 Stat 170 (15 U.S.C. 1604 et seq.); section 1204(c), Competitive Banking Equality Act, Pub. L. No. 100–86, 101 Stat. 552.

2. Regulation Z (12 CFR Part 226) is proposed to be amended by adding a sentence to the end of paragraph (b) of § 226.1 (the first sentence is republished), by adding paragraph (3), § 226.1(c), by revising the second sentence of paragraph (2) to § 226.1(d) (the first sentence is republished), by revising footnote 8, by adding paragraph (4) to § 226.5(a) (a) introductory text is republished) by adding paragraph (4) to § 226.5(b), by adding § 226.5b, by adding paragraph (e) to § 226.6, and by adding paragraph (d) to § 226.16.

Subpart A—General

§ 226.1 Authority, purpose, coverage, organization, enforcement and liability.

(b) *Purpose.* The purpose of this regulation is to promote the informed use of consumer credit by requiring disclosures about its terms and cost. * * * ►In addition, the regulation requires a maximum interest rate to be stated in variable-rate contracts secured by the consumer's dwelling, and imposes limitations on home equity

plans that are subject to the requirements of § 226.5b.◄

(c) *Coverage.* * * *

►(3) In addition, certain requirements of § 226.5b apply to persons who are not creditors but who provide applications for home equity plans to consumers.◄

(d) *Organization.* * * *

(2) Subpart B contains the rules for open-end credit. It requires that initial disclosures and periodic statements be provided►, as well as additional disclosures for home equity plans subject to the requirements of § 226.5b◄. * * *

* * * * *

Subpart B—Open-End Credit

§ 226.5—General disclosure requirements.

(a) *Form of disclosures.* (1) The creditor shall make the disclosures required by this subpart clearly and conspicuously in writing,[7] in a form that the consumer may keep.[8]

* * * * *

►(4) For rules governing the form of disclosures for home equity plans, see § 226.5b(a).◄

(b) *Time of disclosures.* * * *

►(4) *Home equity plans.* Disclosures for home equity plans shall be made in accordance with § 226.5b(b).◄

►§ 226.5b Requirements for home equity plans.

The requirements of this section apply to open-end credit plans secured by the consumer's dwelling.

(a) *Form of disclosures*—(1) *General.* The disclosures required by § 226.5b(d) shall be made clearly and conspicuously and shall be grouped together and segregated from all other unrelated information. The disclosures may be provided on the application form or on a separate form. The variable-rate information required in paragraph (d)(12) of this section, as well as the disclosure provided for under paragraph (d)(4)(iii) of this section, may be provided separately from the other required disclosures.

(2) *Precedence of certain disclosures.* The disclosures required by paragraphs (d)(1) through (4)(ii) of this section shall precede the other required disclosures.

(b) *Time of disclosures.* The disclosures and brochure required by paragraphs (d) and (e) of this section shall be provided at the time an application is provided to the consumer.[10a] (See § 226.6(a) for additional disclosures to be provided later.)

(c) *Duties of third parties.* Persons other than the creditor who provide applications to consumers for home equity plans must provide the brochure required under paragraph (e) of this section at the time an application is provided. If such persons have the disclosures for a creditor's home equity plan, they also shall provide the disclosures at such time.

(d) *Content of disclosures.* The creditor shall provide the following disclosures, as applicable:

(1) *Retention of information.* A statement that the consumer should make or otherwise retain a copy of the disclosures.

(2) *Conditions for disclosed terms.* (i) A statement of the time by which the consumer must submit an application to obtain specific terms disclosed and an identification of any disclosed term that is subject to change prior to opening the plan.

(ii) A statement that, if a disclosed term changes (other than a change due to a variable-rate feature) prior to opening the plan and the consumer therefore elects not to open the plan, the consumer may receive a refund of all fees paid in connection with the application.

(3) *Security interest and risk to home.* A statement that the creditor will acquire a security interest in the consumer's dwelling and that loss of the dwelling may occur in the event of default.

(4) *Possible actions by creditor.* (i) A statement that the creditor, under certain conditions, may terminate the plan and require payment of the outstanding balance in full in a single payment upon termination, and that fees may be imposed upon termination; that the creditor may prohibit additional extensions of credit or reduce the credit limit under certain conditions; and that the creditor, as specified in the initial agreement, may modify certain terms of the plan.

(ii) A statement that the consumer may receive, upon request, information about the conditions under which such actions may occur.

(iii) In lieu of the disclosure required under paragraph (d)(4)(ii) of this section, a statement of such conditions.

(5) *Payment terms.* The payment terms of the plan, including:

(i) The length of the plan.

(ii) An explanation of how the minimum periodic payment will be determined and the timing of the payments. If paying only the minimum periodic payments will not repay any of the principal or will repay less than the outstanding balance, a statement of this fact, as well as a statement of any balloon payment that will result.[10b]

(iii) An example, based on a $10,000 outstanding balance and a recent annual percentage rate,[10c] showing the minimum periodic payment, any balloon payment, and the time it would take to repay the $10,000 outstanding balance if the consumer made only those payments and obtained no additional extensions of credit.

If different payment terms may apply to the period during which the consumer may obtain additional extensions of credit and the period during which the consumer must repay the outstanding balance without obtaining additional extensions of credit, or if different payment terms may apply within either period, the disclosures shall reflect the different payment terms.

(6) *Annual percentage rate.* For fixed rate plans, a recent annual percentage rate [10c] imposed under the plan and a statement that the rate does not include costs other than interest.

(7) *Fees imposed by creditor.* An itemization of any fees imposed by the creditor to open, use, or maintain the plan, stated as a dollar amount or percentage, and when such fees are payable.

(8) *Fees imposed by third parties.* An estimate, stated as a single dollar amount or range, of any fees that may be imposed by persons other than the creditor, as well as a statement that the consumer may request from the creditor a good faith itemization of such fees.

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[7] The disclosure required by § 226.9(d) when a Finance charge is imposed at the time of a transaction need not be written.

[8] The ►home equity disclosures required under § 226.5b(d), the◄ alternative summary billing rights statement provided for in § 226.9(a)(2), and the disclosures made under § 226.10(b) about payment requirements need not be in a form that the consumer can keep.

[10a] The disclosures and the brochure may be delivered or placed in the mail not later than three business days following receipt of a consumer's application in the case of applications contained in magazines or other publications, or when the application reaches the creditor by telephone or through an intermediary agent or broker.

[10b] A balloon payment results if paying the minimum periodic payments will not fully amortize the outstanding balance by a specified date, and the consumer will be required to repay the entire outstanding balance at such time.

[10c] For purposes of this section, an annual percentage rate is the annual percentage rate as determined under § 226.14(b). For fixed rate plans, a recent annual percentage rate is a rate that has been in effect under the plan within the twelve months preceding the date the disclosures are provided to the consumer. For variable rate plans, a recent annual percentage rate is the most recent rate provided in the historical table or a rate that has been in effect under the plan since the date of the most recent rate in the table.

(9) *Negative amortization.* A statement that negative amortization may occur and that negative amortization increases the principal balance and reduces the consumer's equity in the dwelling.

(10) *Transaction requirements.* Any limitations on the number of extensions of credit and the amount of credit that may be obtained during any time period, as well as any minimum outstanding balance and minimum draw requirements, stated as dollar amounts or percentages.

(11) *Tax implications.* A statement that the consumer should consult a tax advisor regarding the deductibility of interest and charges under the plan.

(12) *Disclosures for variable-rate plans.* In a variable-rate plan, the following disclosures:

(i) The fact that the annual percentage rate, payment, or term may change due to the variable-rate feature.

(ii) A statement that the annual percentage rate does not include costs other than interest.

(iii) The index used in making rate adjustments and a source of information about the index.

(iv) An explanation of how the annual percentage rate will be determined, including an explanation of how the index is adjusted, such as by the addition of a margin.

(v) A statement that the consumer should ask about the current index value, margin, and annual percentage rate.

(vi) A statement that the initial annual percentage rate is not based on the index and margin used to make later rate adjustments, and the period of time such initial rate will be in effect.

(vii) The frequency of changes in the annual percentage rate.

(viii) Any rules relating to changes in the index value and resulting changes in the annual percentage rate and payment amount, including, for example, an explanation of payment limitations and interest rate carryover.

(ix) A statement of the maximum amount that the annual percentage rate may change in any one-year period (or a statement that no such limitation exists), as well as a statement of the maximum annual percentage rate that may be imposed under each payment option.

(x) The minimum periodic payment required when the maximum annual percentage rate for each payment option is in effect for a $10,000 outstanding balance, and a statement of the earliest date the maximum rate may be imposed.

(xi) An historical table, based on a $10,000 extension of credit, illustrating how annual percentage rates and payments would have been affected by index value changes implemented according to the terms of the plan. The historical table shall be based on the most recent 15 years of index values (selected for the same time period each year) and shall reflect all significant plan terms, such as rate discounts, rate and payment limitations, rate carryover, and negative amortization, that would have been affected by the index movement during the period.

(xii) A statement that rate information will be provided on or with each periodic statement.

(e) *Brochure.* The home equity brochure published by the Board or any brochure that provides substantially similar information shall be provided.

(f) *Limitations on home equity plans.* No creditor may, by contract or otherwise:

(1) Change the annual percentage rate unless:

(i) Such change is based on an index that is not under the creditor's control; and

(ii) Such index is available to the general public.

(2) Terminate a plan and demand repayment of the entire outstanding balance in advance of the original term unless:

(i) There has been fraud or material misrepresentation by the consumer in connection with the plan;

(ii) The consumer has failed to meet the repayment terms of the agreement for any outstanding balance; or

(iii) Any action or inaction by the consumer has adversely affected the creditor's security for the plan.

(3) Change any term [10d] (other than an insignificant term), except that a creditor may:

(i) Provide in the initial agreement that specified changes will occur if a specific event takes place (for example, that the annual percentage rate will increase a certain amount if the consumer leaves the creditor's employment or that further extensions of credit will not be made if the maximum annual percentage rate is reached).

(ii) Change the index and margin used under the plan if the original index is no longer available, the new index has an historical movement substantially similar to that of the original index, and the new index and margin would have resulted in an interest rate substantially similar to the rate in effect at the time the original index became unavailable.

(iii) Prohibit additional extensions of credit or reduce the credit limit applicable to an agreement during any period in which:

(A) The value of the dwelling that secures the plan declines significantly below the property's appraised value for purposes of the plan;

(B) The creditor reasonably believes that the consumer will be unable to fulfill the repayment obligations under the plan because of a material change in the consumer's financial circumstances;

(C) The consumer is in default of any material obligation under the agreement;

(D) The creditor is precluded by government action from imposing the annual percentage rate provided for in the agreement; or

(E) The priority of the creditor's security interest is adversely affected by government action to the extent that the value of the security interest is less than 120 percent of the credit line.

(iv) Make any change that will unequivocally benefit the consumer throughout the remainder of the plan.

(g) *Disclosure required upon request.* A creditor shall provide, at the consumer's request, a statement of the conditions under which the creditor may take the actions described in paragraph (d)(4)(i) of this section.

(h) *Refund to consumer.* A creditor shall refund all fees paid by the consumer to anyone in connection with an application if any term required to be disclosed under paragraph (d) of this section changes (other than a change due to a variable-rate feature) before the plan is opened and, as a result, the consumer elects not to open the plan.

(i) *Imposition of nonrefundable fees.* Neither a creditor nor any other person may impose a nonrefundable fee in connection with an application until three business days after the consumer receives the disclosures and brochure required under this section.[10e]

§ 226.6 Initial disclosure statement.

* * * * *

►(e) *Home equity plan information.* (1) The disclosures required under § 226.5b(d), to the extent they are not duplicative.

(2) A statement of the conditions under which the creditor may take the actions described in § 226.5b(d)(4)(i).◄

* * * * *

§ 226.26 Advertising.

* * * * *

►(d) *Additional requirements for home equity plans.*—(1) *Advertisement*

[10d] The creditor may implement changes during the plan if a specific written agreement is made with the consumer at that time.

[10e] If the disclosures and brochure are mailed to the consumer, the consumer is considered to have received them three business days after they have been mailed.◄

of terms that require additional disclosures. If any of the terms required to be disclosed under § 226.6(a) or (b) or the payment terms of the plan are set forth, affirmatively or negatively, in an advertisement for a home equity plan subject to the requirements of § 226.5b, the advertisement shall also clearly and conspicuously set forth the following:

(i) Any loan fee that is a percentage of the credit limit under the plan and an estimate of any other fees imposed for opening the plan, stated as a single dollar amount or a reasonable range.

(ii) Any periodic rate used to compute the finance charge, expressed as an annual percentage rate as determined under § 226.14(b).

(iii) The maximum annual percentage rate that may be imposed in a variable-rate plan.

(2) *Discounted and premium rates.* If an advertisement states an initial annual percentage rate that is not based on the index and margin used to make later rate adjustments in a variable-rate plan, the advertisement also shall state the period of time such rate will be in effect, and, with equal prominence to the initial rate, a reasonably current annual percentage rate that would have been in effect using the index and margin.

(3) *Balloon payment.* If an advertisement contains a statement about any minimum periodic payment, the advertisement also shall state, if applicable, that a balloon payment[10b] will result.

(4) *Tax implications.* An advertisement that states that any interest expense incurred under the home equity plan is or may be tax deductible may not be misleading in this regard.

(5) *Misleading terms.* An advertisement may not refer to a home equity plan as "free money" or contain a similarly misleading term.◄

* * * * *

3. Appendix G is amended by adding G–17A, G–17B, and G–18.

Appendix G—Open-End Model Forms And Clauses

* * * * *

►G–17A Home Equity Sample.
G–17B Home Equity Sample.
G–18 Home Equity Model Clauses.◄

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►*G—17A Home Equity Sample*

IMPORTANT TERMS OF OUR HOME EQUITY LINE OF CREDIT

This disclosure contains important information about our Home Equity Line of Credit. You should read it carefully and keep a copy for your records.

Availability of Terms: To obtain the terms described below, you must submit your application before April 1, 1989.

If any of these terms changes (other than the annual percentage rate) and you decide, as a result, to not enter into an agreement with us, you are entitled to a refund of any fees that you paid in connection with your application.

Security Interest: We will take a mortage in your home. You could lose your home if you don't meet the obligations in your agreement with us.

Possible Actions: Under certain circumstances, we can (1) terminate your account and require you to pay us the entire outstanding balance in one payment and also charge you certain fees, (2) refuse to make additional extensions of credit, and (3) reduce your credit limit.

Upon request, we will provide you with more specific information about when we can take these actions.

Minimum Payment Requirements: You can obtain credit advances for 10 years (the "draw period"). During the draw period, payments will be due monthly. Your minimum monthly payment will equal the greater of 1/360th of the outstanding balance plus the finance charges that have accrued on the outstanding balance, or $100.

After the draw period ends, you will no longer be able to obtain credit advances and must pay the outstanding balance on your account over 5 years (the "repayment period"). During the repayment period, payments will be due monthly. Your minimum monthly payment will equal all payments past due, plus 1/60th of the balance that was outstanding at the end of the draw period plus the finance charges that have accrued on the remaining balance.

Minimum Payment Example: If you made only the minimum monthly payment and took no other credit advances, it would take 15 years to pay off a credit advance of $10,000 at an ANNUAL PERCENTAGE RATE of 12.00%. During that period, you would make 120 monthly payments varying between $127.78 and $100.00 followed by 60 monthly payments varying between $187.06 and $118.08.

Fees and Charges: In order to open and maintain an account, you must pay certain fees and charges. The following fees must be paid to us:

Application fee: $150 (due at application)
Points: 1% of credit limit (due when account opened)
Annual maintenance fee: $75 (due each year)

You also must pay certain fees to third parties such as appraisers, credit reporting firms, and government agencies. These fees generally total between $500 and $900. Upon request, we will provide you with an itemization of the fees you will have to pay to third parties.

Minimum Draw and Balance Requirements: The minimum credit advance that you can receive is $500. You must maintain an account balance of at least $100.

Tax Deductibility: You should consult a tax advisor regarding the deductibility of interest and charges under the plan.

Variable-Rate Feature: The plan has a variable-rate feature, and the annual percentage rate and the minimum monthly payment can change as a result. The annual percentage rate does not include costs other than interest.

The annual percentage rate is based on the value of an index. The index is the monthly average prime rate charged by banks and is published in the *Federal Reserve Bulletin.* To determine the annual percentage rate that will apply to your account, we add a margin to the value of the index.

Ask us for the current index value, margin and annual percentage rate. After you open an account, rate information will be provided on periodic statements that we send you.

Rate Changes: The annual percentage rate can change monthly. There is no limit on the amount by which the rate can change during any one-year period. The maximum ANNUAL PERCENTAGE RATE that can apply during the plan is 18%.

Maximum Rate and Payment Examples: If you had an outstanding balance of $10,000 at the beginning of the draw period, the minimum monthly payment at the maximum ANNUAL PERCENTAGE RATE of 18% would be $177.78. This annual percentage rate could be reached during the first month of the draw period.

If you had an outstanding balance of $10,000 at the beginning of the repayment period, the minimum monthly payment at the maximum ANNUAL PERCENTAGE RATE of 18% would be $316.67. This annual percentage rate could be reached during the first month of the repayment period.

Variable-Rate Example: The following table shows how the annual percentage rate and the minimum monthly payments for a single $10,000 credit advance would have changed based on changes in the index over the last 15 years. The index values are from September of each year. While only one payment amount per year is shown, payments would have varied slightly during each year.

The table assumes that no additional credit advances were taken and that only the minimum payment was made each month. It does not necessarily indicate how the index or your payments would change in the future.

Year	Percentage—			Minimum monthly payment
	Index	Margin	Annual rate	
1974	12.00	2	14.00	$144.44
1975	7.88	2	9.88	$106.50
1976	7.00	2	9.00	$100.00

Year	Percentatge—			Minimum monthly payment
	Index	Margin	Annual rate	
1977	7.13	2	9.13	$100.00
1978	9.41	2	11.41	$105.47
1979	12.90	2	14.90	$126.16
1980	12.23	2	14.23	$117.53
1981	20.08	2	[1] 18.00	$138.07
1982	13.50	2	15.50	$117.89
1983	11.00	2	13.00	$100.00
1984	12.97	2	14.97	$203.81
1985	9.50	2	11.50	$170.18
1986	7.50	2	9.50	$149.78
1987	8.70	2	10.70	$141.50
1988	10.00	2	12.00	$130.55

[1] This rate reflects the 18 percent maximum rate limitation.

C-17B Home Equity Sample

IMPORTANT TERMS OF OUR HOME EQUITY LINE OF CREDIT

This disclosure contains important information about our Home Equity Line of Credit. You should read it carefully and keep a copy for your records.

Availability of Terms: All of the terms described below are subject to change.

If any of these terms changes (other than the annual percentage rate) and you decide, as a result, to not enter into an agreement with us, you are entitled to a refund of any fees that you paid in connection with your application.

Security Interest: We will take a mortgage in your home. You could lose your home if you don't meet the obligations in your agreement with us.

Possible Actions: Under certain circumstances, we can (1) terminate your account and require you to pay us the entire outstanding balance in one payment and also charge you certain fees, (2) refuse to make additional extensions of creidt, (3) reduce your credit limit, and (4) make specific changes that are set forth in your agreement with us.

Upon request, we will provide you with more specific information about when we can take these actions.

Minimum Payment Requirements: You can obtain credit advances for 15 years (the "draw period"). When you open your account, you can choose to make either monthly or quarterly payments during the draw period. If you choose the monthly payment option, your monthly payment will equal the finance charges that accrued during the preceding month. If you choose the quarterly payment option, your quarterly payment will equal the finance charges that accrued during the preceding quarter. Under either option, if the accrued finance charges are less than $50, the minimum payment will equal $50 or the account balance, whichever is less. Balances of less than $50 must be paid in full.

Under either the monthly or quarterly payment option, the minimum payment during the draw period will not reduce the principal that is outstanding on your account.

After the draw period ends, you will no longer be able to obtain credit advances and must repay the outstanding balance on your account (the "repayment period"). The length of the repayment period will depend on the balance outstanding on your account at the beginning of it. During the repayment period, payments will be due monthly and will equal 3% of the then outstanding balance (including finance charges) on your account or $100, whichever is greater.

Minimum Payment Examples: If you made only the minimum payment and took no other credit advances, it would take 22 years and 11 months to pay off a credit advance of $10,000 at an ANNUAL PERCENTAGE RATE of 12.00%. Under the monthly payment option, you would make 180 monthly payments of $100.00 followed by 94 monthly payments varying between $303.00 and $100.00 and a final payment of $30.27. Under the quarterly payment option, you would make 60 quarterly payments of $303.01 followed by 94 monthly payments varying between $303.00 and $100.00 and a final payment of $30.27.

Fees and Charges: In order to open and maintain an account, you must pay certain fees and charges. The following fees must be paid to us:

Application fee: $100 (due at application)
Points: 1% of credit limit (due when account opened)
Annual maintenance fee: $75 (due each year)

You also must pay certain fees to third parties such as appraisers, credit reporting firms, and government agencies. These fees generally total between $500 and $900. Upon request, we will provide you with an itemization of the fees you will have to pay to third parties.

Minimum Draw Requirement: The minimum credit advance that you can receive is $200.

Tax Deductibility: You should consult a tax advisor regarding the deductibility of interest and charges under the plan.

Variable-Rate Feature: The plan has a variable-rate features, and the annual percentage rate and the minimum monthly payment can change as a result. The annual percentage rate does not include costs other than interest.

The annual percentage rate is based on the value of an index. The index is the monthly average prime rate charged by banks and is published in the *Federal Reserve Bulletin*. To determine the annual percentage rate that will apply to your account, we add a margin to the value of the index.

Ask us for the current index value, margin and annual percentage rate. After you open an account, rate information will be provided on periodic statements that we send you.

Rate Changes: The annual percentage rate can change monthly. There is no limit on the amount by which the rate can change during any one-year period. The maximum ANNUAL PERCENTAGE RATE that can apply during the plan is 18%.

Maximum Rate and Payment Examples: Under the monthly payment option, if you had an outstanding balance of $10,000 at the beginning of the draw period, the minimum monthly payment at the maximum ANNUAL PERCENTAGE RATE of 18% would be $150.00. Under the quarterly payment option, the minimum quarterly payment would be $456.78. This annual percentage rate could be reached during the first month of the draw period.

If you had an outstanding balance of $10,000 at the beginning of the repayment period, the minimum monthly payment at the maximum ANNUAL PERCENTAGE RATE of 18% would be $304.50. This annual percentage rate could be reached during the first month of the repayment period.

Variable-Rate Example: The following table shows how the annual percentage rate and payments for a single $10,000 credit advance would have changed based on changes in the index over the last 15 years. The index values are from September of each year.

The table assumes that no additional credit advances were taken and that only the minimum payment was made. It does not necessarily indicate how the index or your payments would change in the future.

Year	Percentage—			Minimum payment—	
	Index	Margin	Annual rate	Monthly	Quarterly
1974	12.00	2	14.00	$116.67	$354.10
1975	7.88	2	9.88	$82.33	$249.04
1976	7.00	2	9.00	$75.00	$226.69
1977	7.13	2	9.13	$76.08	$229.99
1978	9.41	2	11.41	$95.08	$287.97
1979	12.90	2	14.90	$124.17	$377.14
1980	12.23	2	14.23	$118.58	$359.99
1981	20.08	2	[1] 18.00	$150.00	$456.78
1982	13.50	2	15.50	$129.17	$392.53
1983	11.00	2	13.00	$108.33	$328.53
1984	12.97	2	14.97	$124.75	$378.94
1985	9.50	2	11.50	$95.83	$290.26
1986	7.50	2	9.50	$79.17	$239.39
1987	8.70	2	10.70	$89.17	$269.89
1988	10.00	2	12.00	$100.00	$303.01

[1] This rate reflects the 18-percent maximum rate limitation.

G–18 Home Equity Model Clauses

Retention of Information: This disclosure contains important information about our Home Equity Line of Credit. You should read it carefully and keep a copy for your records.

Availability of Terms: To obtain the terms described below, you must submit your application before (*date*). However the (*description of terms*) are subject to change.

If any of these terms changes [(other than the annual percentage rate)] and you therefore decide to not enter into an agreement with us, you need not do so. You will then be entitled to a refund of any fees that you paid in connection with your application.

Security Interest: We will take a [security interest in/mortgage on] your home. You could lose your home if you don't meet the obligations in your agreement with us.

Possible Actions: Under certain circumstances, we can (1) terminate your account and require you to pay us the entire outstanding balance in one payment [, and also charge you certain fees], (2) refuse to make additional extensions of credit, (3) reduce your credit limit [, and (4) make specific changes that are set forth in your agreement with us].

[Upon request, we will provide you with more specific information about when we can take these actions./We can take these actions under the following circumstances: (*when actions may be taken*).]

Minimum Payment Requirements: The length of the [draw period/repayment period] is (*length*). Payments will be due (*frequency*). Your minimum payment will equal (*how payment determined*).

The minimum payment will not repay the balance that is outstanding on your account by (*time*). You will then be required to pay the entire balance in a single payment.

Minimum Payment Example: If you made only the minimum monthly payment and took no other credit advances, it would take (*length of time*) to pay off a credit advance of $10,000 at an ANNUAL PERCENTAGE RATE of (*recent rate*). During that period, you would make (*number*) (*frequency*) payments of $___.

Fees and Charges: To open and maintain an account, you must pay certain fees and charges. The following fees must be paid to us:

(*Description of fee*) [$___/___% of _____]
(*When payable*)
(*Description of fee*) [$___/___% of _____]
(*When payable*)

You also must pay certain fees to third parties such as appraisers, credit reporting firms, and government agencies. These fees generally total [$___/___% of _____]. Upon request, we will provide you with an itemization of the fees you will have to pay to third parties.

Minimum Draw and Balance Requirements: The minimum credit advance that you can receive is $___. You must maintain an account balance of at least $___.

Negative Amortization: Under some circumstances, negative amortization may occur. Negative amortization will increase the amount that you owe us and reduce your equity in your home.

Tax Deductibility: You should consult a tax advisor regarding the deductibility of interest and charges for the plan.

Variable-Rate Feature: The plan has a variable-rate feature and the annual percentage rate and the [minimum payment/term of the plan] can change as a result. The annual percentage rate does not include costs other than interest.

The annual percentage rate is based on the value of an index. The index is the (*identification of index*) and is published in (*source of information*). To determine the annual percentage rate that will apply to your account, we add a margin to the value of the index.

Ask us for the current index value, margin and annual percentage rate. After you open an account, rate information will be provided on periodic statements that we send you.

[The initial annual percentage rate is not based on the index and margin used for later rate adjustments. The initial rate will be in effect for (*period*).]

Rate Changes: The annual percentage rate can change (*frequency*). [The rate cannot increase by more than ___ percentage points in any one year period./There is no limit on the amount by which the rate can change in any one year period.] [The maximum ANNUAL PERCENTAGE RATE that can apply during the plan is ___%./The ANNUAL PERCENTAGE RATE cannot increase by more than ___ percentage points above the initial rate during the plan.]

Maximum Rate and Payment Examples: If you had an outstanding balance of $10,000, the minimum payment at the maximum ANNUAL PERCENTAGE RATE of ___% would be $___. This annual percentage rate could be reached (*when maximum rate could be reached*).

Variable-Rate Example: The following table shows how the annual percentage rate and the minimum payments for a single $10,000 credit advance would have changed based on changes in the index over the last 15 years. The index values are from (*when values are measured*).

The table assumes that no additional credit advances were taken and that only the minimum payment was made. It does not necessarily indicate how the index or your payments would change in the future.

Year	Percentage—			Minimum payment
	Index	Margin	Annual rate	
1974				
1975				
1976				
1977				
1978				
1979				

Year	Percentage—			Minimum payment
	Index	Margin	Annual rate	
1980				
1981				
1982				
1983				
1984				
1985				
1986				
1987				
1988				

By order of the Board of Governors of the Federal Reserve System, January 11, 1989.

William W. Wiles,

Secretary of the Board.

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