



FEDERAL RESERVE BANK
OF DALLAS

ROBERT D. McTEER, JR.
PRESIDENT
AND CHIEF EXECUTIVE OFFICER

November 15, 1996

DALLAS, TEXAS
75265-5906

Notice 96-110

TO: The Chief Executive Officer of
each financial institution in the
Eleventh Federal Reserve District

SUBJECT

**Slip-sheet Amendments to
Regulations A, D, and Z; Revised Pamphlets
for Regulations E, S, Securities Credit Transactions
(G, T, U, and X), and to the Official Staff
Commentary on Regulation E**

DETAILS

The Board of Governors of the Federal Reserve System has published slip-sheet amendments to Regulation A, effective February 5, 1996; Regulation D, effective December 19, 1995; and Regulation Z, effective April 1, 1996.

In addition, the Board has published revised pamphlets for Regulation E, effective May 1, 1996; the Official Staff Commentary on Regulation E, effective May 2, 1996; Regulations G, T, U, and X, with various effective dates; and Regulation S, effective July 12, 1996.

For additional copies, bankers and others are encouraged to use one of the following toll-free numbers in contacting the Federal Reserve Bank of Dallas: Dallas Office (800) 333-4460; El Paso Branch *Intrastate* (800) 592-1631, *Interstate* (800) 351-1012; Houston Branch *Intrastate* (800) 392-4162, *Interstate* (800) 221-0363; San Antonio Branch *Intrastate* (800) 292-5810.

ENCLOSURES

The amendment slip sheets, the revised pamphlets, and an updated index to regulations are enclosed. Please insert them in your Regulations binders.

MORE INFORMATION

For more information regarding Regulation A, please contact the Discount and Credit Department at (214) 922-5333. For more information regarding Regulation D, please contact the Reserve and Risk Management Division at (214) 922-5646.

For more information regarding Regulation E, the Official Staff Commentary on Regulation E, Regulations G, T, U, and X, or Regulation Z, please contact Eugene Coy at (214) 922-6201. For more information regarding Regulation S, please contact James Dean at (214) 922-6237.

For additional copies of this Bank's notice, the slip sheets, or the index to regulations, please contact the Public Affairs Department at (214) 922-5254.

Sincerely yours,

Robert D. McTeer, Jr.

Amendments to Regulation A Extensions of Credit by Federal Reserve Banks February 1996*

1. *Effective February 5, 1996, section 201.51 has been amended to read as follows:*
2. *Effective November 18, 1994, section 201.52 has been amended to read as follows:*

SECTION 201.51—Adjustment Credit for Depository Institutions

The rates for adjustment credit provided to depository institutions under section 201.3(a) are:

<i>Federal Reserve Bank</i>	<i>Rate</i>	<i>Effective</i>
Boston	5.00	February 1, 1996
New York	5.00	January 31, 1996
Philadelphia	5.00	January 31, 1996
Cleveland	5.00	January 31, 1996
Richmond	5.00	February 1, 1996
Atlanta	5.00	January 31, 1996
Chicago	5.00	February 1, 1996
St. Louis	5.00	February 5, 1996
Minneapolis	5.00	January 31, 1996
Kansas City	5.00	February 1, 1996
Dallas	5.00	January 31, 1996
San Francisco	5.00	January 31, 1996

* A complete Regulation A, as amended effective February 5, 1996, consists of—

- the regulation pamphlet dated May 1994 (see inside front cover) and
- this slip sheet.

SECTION 201.52—Extended Credit for Depository Institutions

(a) *Seasonal credit.* The rate for seasonal credit extended to depository institutions under section 201.3(b) is a flexible rate that takes into account rates on market sources of funds, but in no case will the rate charged be less than the rate for adjustment credit as set out in section 201.51.

(b) *Extended credit.* For extended credit to depository institutions under section 201.3(c), for credit outstanding for more than 30 days, a flexible rate will be charged that takes into account rates on market sources of funds, but in no case will the rate charged be less than the rate for adjustment credit, as set out in section 201.51, plus one-half percentage point. At the discretion of the Federal Reserve Bank, the 30-day time period may be shortened.

Amendments to Regulation D Reserve Requirements of Depository Institutions January 1996*

1. *Effective December 19, 1995, the table in section 204.9(a)(1) is amended to read as follows:*

<i>Category</i>	<i>Reserve requirement*</i>
NET TRANSACTION ACCOUNTS	
\$0 to \$52.0 million	3% of amount
Over \$52.0 million	\$1,560,000 plus 10% of amount over \$52.0 million
NONPERSONAL TIME DEPOSITS	
	0%
EUROCURRENCY LIABILITIES	
	0%

* Before deducting the adjustment to be made by paragraph (a)(2) of this section.

2. *Effective December 19, 1995, section 204.9(a)(2) is amended by changing \$4.2 million to \$4.3 million.*

* A complete Regulation D, as amended effective December 19, 1995, consists of—

- the regulation pamphlet dated April 1993 (see inside cover) and
- this slip sheet.

Amendments to the Official Staff Commentary on Regulation Z Truth in Lending June 1996*

1. *Effective April 1, 1996, comment 4(d)-5 is amended to read as follows:*

5. *Required credit life insurance.* Credit life, accident, health, or loss-of-income insurance must be voluntary in order for the premium or charges to be excluded from the finance charge. Whether the insurance is in fact required or optional is a factual question. If the insurance is required, the premiums must be included in the finance charge, whether the insurance is purchased from the creditor or from a third party. If the consumer is required to elect one of several options—such as to purchase credit life insurance, or to assign an existing life insurance policy, or to pledge security such as a certificate of deposit—and the consumer purchases the credit life insurance policy, the premium must be included in the finance charge. (If the consumer assigns a preexisting policy or pledges security instead, no premium is included in the finance charge. The security interest would be disclosed under section 226.6(c) or section 226.18(m). See the commentary to section 226.4(b)(7) and (8).)

2. *Effective April 1, 1996, a sentence is added at the end of comment 6(b)-1, item v., to read as follows:*

* * * For example, if the primary benefit of membership in an organization is the opportunity to apply for a credit card, and the other benefits offered (such as a newsletter or a member information hotline) are merely incidental to the credit feature,

the membership fee would be disclosed as an "other charge."

3. *Effective April 1, 1996, the last sentence of comment 12(c)(2)-1 is amended and comment 12(c)(2)-2 is added to read as follows:*

* * * * *

- Nothing in this provision prohibits the card issuer from undertaking its normal collection activities for the delinquent and undisputed portion of the account.

2. *Settlement of dispute.* A card issuer may not consider a dispute settled and report an amount disputed as delinquent or begin collection of the disputed amount until it has completed a reasonable investigation of the cardholder's claim. A reasonable investigation requires an independent assessment of the cardholder's claim based on information obtained from both the cardholder and the merchant, if possible. In conducting an investigation, the card issuer may request the cardholder's reasonable cooperation. The card issuer may not automatically consider a dispute settled if the cardholder fails or refuses to comply with a particular request. However, if the card issuer otherwise has no means of obtaining information necessary to resolve the dispute, the lack of information resulting from the cardholder's failure or refusal to comply with a particular request may lead the card issuer reasonably to terminate the investigation.

4. *Effective April 1, 1996, comment 14(c)-10 is added to read as follows:*

10. *Transactions at end of billing cycle.* The annual percentage rate reflects trans-

* A complete commentary pamphlet, as amended effective April 1, 1996, consists of—

- the commentary pamphlet dated July 1995 (see inside front cover) and
- this slip sheet.

actions and charges imposed during the billing cycle. However, it may be impracticable to post a transaction that occurs at the end of a billing cycle until the following cycle, such as a cash advance that occurs on the last day of a billing cycle and is posted to the account in the following cycle. A card issuer that uses the date of the transaction to figure finance charges shall calculate the annual percentage rate as follows for the billing cycle in which the transaction and charges are posted:

- i. The denominator shall be calculated as if the transaction occurred on the first day of the billing cycle; and
- ii. The numerator shall include the amount of the transaction charge plus all finance charges derived from the application of the periodic rate to the amount of the transaction (including all charges from a prior cycle).

5. *Effective April 1, 1996, the first and last paragraphs of comment 17(c)(1)-10 are amended to read as follows:*

10. *Discounted and premium variable-rate transactions.* In some variable-rate transactions, creditors may set an initial interest rate that is not determined by the index or formula used to make later interest-rate adjustments. Typically, this initial rate charged to consumers is lower than the rate would be if it were calculated using the index or formula. However, in some cases the initial rate may be higher. In a discounted transaction, for example, a creditor may calculate interest rates according to a formula using the six-month Treasury bill rate plus a 2 percent margin. If the Treasury bill rate at consummation is 10 percent, the creditor may forgo the 2 percent spread and charge only 10 percent for a limited time, instead of setting an initial rate of 12 percent.

When creditors use an initial interest rate that is not calculated using the index or formula for later rate adjustments, the disclosures should reflect a composite annual percentage rate based

on the initial rate for as long as it is charged and, for the remainder of the term, the rate that would have been applied using the index or formula at the time of consummation. The rate at consummation need not be used if a contract provides for a delay in the implementation of changes in an index value. For example, if the contract specifies that rate changes are based on the index value in effect 45 days before the change date, creditors may use the index value in effect during the 45 days before consummation in calculating a composite annual percentage rate.

* * * * *

A loan in which the initial interest rate is set according to the index or formula used for later adjustments but is not set at the value of the index or formula at consummation. For example, if a creditor commits to an initial rate based on the formula on a date prior to consummation, but the index has moved during the period between that time and consummation, a creditor should base its disclosures on the initial rate.

6. *Effective April 1, 1996, comment 17(c)(1)-18 is added to read as follows:*

18. *Pawn Transactions.* When, in connection with an extension of credit, a consumer pledges or sells an item to a pawnbroker creditor in return for a sum of money and retains the right to redeem the item for a greater sum (the redemption price) within a specified period of time, disclosures are required. In addition to other disclosure requirements that may be applicable under section 226.18, for purposes of pawn transactions:

- i. The amount financed is the initial sum paid to the consumer. The pawnbroker creditor need not provide a separate itemization of the amount financed if that entire amount is paid directly to the consumer and the dis-

closed description of the amount financed is "the amount of cash given directly to you" or a similar phrase.

- ii. The finance charge is the difference between the initial sum paid to the consumer and the redemption price plus any other finance charges paid in connection with the transaction. (See section 226.4.)
- iii. The term of the transaction, for calculating the annual percentage rate, is the period of time agreed to by the pawnbroker creditor and the consumer. The term of the transaction does not include a grace period (including any statutory grace period) after the agreed redemption date.

7. *Effective April 1, 1996, comment 18(c)(1)(iii)-2 is added to read as follows:*

2. *Charges added to amounts paid to others.* A sum is sometimes added to the amount of a fee charged to a consumer for a service provided by a third party (such as for an extended warranty or a service contract) that is payable in the same amount in comparable cash and credit transactions. In the credit transaction, the amount is retained by the creditor. Given the flexibility permitted in meeting the requirements of the amount financed itemization (see the commentary to section 226.18(c)), the creditor in such cases may reflect that the creditor has retained a portion of the amount paid to others. For example, the creditor could add to the category "amount paid to others" language such as "(we may be retaining a portion of this amount)."

8. *Effective April 1, 1996, comment 20(a)-3 is amended to read as follows:*

3. *Variable rate.*

i. If a variable-rate feature was properly disclosed under the regulation, a rate change in accord with those disclosures is not a refinancing. For example, no new

disclosures are required when the variable-rate feature is invoked on a renewable balloon-payment mortgage that was previously disclosed as a variable-rate transaction.

ii. Even if it is not accomplished by the cancellation of the old obligation and substitution of a new one, a new transaction subject to new disclosures results if the creditor either:

- A. Increases the rate based on a variable-rate feature that was not previously disclosed; or
- B. Adds a variable-rate feature to the obligation. A creditor does not add a variable-rate feature by changing the index of a variable-rate transaction to a comparable index, whether the change replaces the existing index or substitutes an index for one that no longer exists.

iii. If either of the events in paragraph 20(a)(iii) ii.A. or ii.B. occurs in a transaction secured by a principal dwelling with a term longer than one year, the disclosures required under section 226.19(b) also must be given at that time.

9. *Effective April 1, 1996, comments on subpart E are added to read as follows:*

**SUBPART E—SPECIAL RULES
FOR CERTAIN HOME
MORTGAGE TRANSACTIONS**

SECTION 226.31—General Rules

31(c) Timing of Disclosure

31(c)(1) Disclosures for Certain Closed-End Home Mortgages

1. *Furnishing disclosures.* Disclosures are considered furnished when received by the consumer.

2. *Pre-consummation waiting period.* A creditor must furnish section 226.32 disclosures at least three business days prior to consummation. Under section 226.32, "business day" has the same meaning as

the rescission rule in comment 2(a)(6)-2—all calendar days except Sundays and the federal legal holidays listed in 5 USC 6103(a). However, while the disclosure rule under sections 226.15 and 226.23 extends to midnight of the third business day, the rule under section 226.32 does not. For example, under section 226.32, if disclosures were provided on a Friday, consummation could occur any time on Tuesday, the third business day following receipt of the disclosures. If the timing of the rescission rule were to be used, consummation could not occur until after midnight on Tuesday.

31(c)(1)(i) Change in Terms

1. *Redisclosure required.* Creditors must provide new disclosures when a change in terms makes disclosures previously provided under section 226.32(c) inaccurate, including disclosures based on and labeled as an estimate. A change in terms may result from a formal written agreement or otherwise.

31(c)(1)(ii) Telephone Disclosures

1. *Telephone disclosures.* Disclosures by telephone must be furnished at least three business days prior to consummation, calculated in accord with the timing rules under section 226.31(c)(1).

31(c)(1)(iii) Consumer's Waiver of Waiting Period before Consummation

1. *Modification or waiver.* A consumer may modify or waive the right to the three-day waiting period only after receiving the disclosures required by section 226.32 and only if the circumstances meet the criteria for establishing a bona fide personal financial emergency under section 226.23(e). Whether these criteria are met is determined by the facts surrounding individual situations. The imminent sale of the consumer's home at foreclosure during the three-day period is one example of a bona fide personal financial emergency. Each consumer entitled to the three-day waiting period must sign the

handwritten statement for the waiver to be effective.

31(c)(2) Disclosures for Reverse Mortgages

1. *Business days.* For purposes of providing reverse-mortgage disclosures, "business day" has the same meaning as in comment 31(c)(1)-2—all calendar days except Sundays and the federal legal holidays listed in 5 USC 6103(a). This means if disclosures are provided on a Friday, consummation could occur any time on Tuesday, the third business day following receipt of the disclosures.

2. *Open-end plans.* Disclosures for open-end reverse mortgages must be provided three business days before the first transaction under the plan (see section 226.5(b)(1)).

31(d) Basis of Disclosures and Use of Estimates

1. *Redisclosure.* Section 226.31(d) allows the use of estimates when information necessary for an accurate disclosure is unknown to the creditor, provided that the disclosure is clearly identified as an estimate. For purposes of subpart E, the rule in section 226.31(c)(1)(i) requiring new disclosures when the creditor changes terms also applies to disclosures labeled as estimates.

SECTION 226.32—Requirements for Certain Closed-End Home Mortgages

32(a) Coverage

Paragraph 32(a)(1)(i)

1. *Application date.* An application is deemed received when it reaches the creditor in any of the ways applications are normally transmitted. (See section 226.19(a).) For example, if a borrower applies for a 10-year loan on September 30 and the creditor counteroffers with a 7-year loan on October 10, the application is deemed received in September and the

creditor must measure the annual percentage rate against the appropriate Treasury security yield as of August 15. An application transmitted through an intermediary agent or broker is received when it reaches the creditor, rather than when it reaches the agent or broker. (See comment 19(b)-3 to determine whether a transaction involves an intermediary agent or broker.)

2. *When fifteenth not a business day.* If the 15th day of the month immediately preceding the application date is not a business day, the creditor must use the yield as of the business day immediately preceding the 15th.

3. *Calculating annual percentage rates for variable-rate loans and discount loans.* Creditors must use the rules set out in the commentary to section 226.17(c)(1) in calculating the annual percentage rate for variable-rate loans (assume the rate in effect at the time of disclosure remains unchanged) and for discount, premium, and stepped-rate transactions (which must reflect composite annual percentage rates).

4. *Treasury securities.* To determine the yield on a Treasury security for the annual percentage rate test, creditors may use the Board's "Selected Interest Rates" (statistical release H-15) or the actual auction results. Treasury auctions are held at regular intervals for the different types of securities. These figures are published by major financial and metropolitan newspapers and are also available from Federal Reserve Banks. Creditors must use the yield on the security that has the nearest maturity at issuance to the loan's maturity. For example, if a creditor must compare the annual percentage rate to Treasury securities with either 7-year or 10-year maturities, the annual percentage rate for an 8-year loan is compared with securities that have a 7-year maturity; the annual percentage rate for a 9-year loan is compared with securities that have a 10-year maturity. If the loan maturity is exactly halfway between, the annual percentage rate is compared with the Treasury security that has the lower yield. For example, if the loan has a maturity of 20

years and comparable securities have maturities of 10 years with a yield of 6.501 percent and 30 years with a yield of 6.906 percent, the annual percentage rate is compared with 10 percentage points over the yield of 6.501 percent, the lower of the two yields.

Paragraph 32(a)(1)(ii)

1. *Total loan amount.* For purposes of the "points and fees" test, the total loan amount is calculated by taking the amount financed, as determined according to section 226.18(b), and deducting any cost listed in section 226.32(b)(1)(iii) that is both included as points and fees under section 226.32(b)(1) and financed by the creditor. Some examples follow, each using a \$10,000 amount borrowed, a \$300 appraisal fee, and \$400 in points:

- i. If the consumer finances a \$300 fee for a creditor-conducted appraisal and pays \$400 in points at closing, the amount financed under section 226.18(b) is \$9,900 (\$10,000 plus the \$300 appraisal fee that is paid to and financed by the creditor, less \$400 in prepaid finance charges). The \$300 appraisal fee paid to the creditor is added to other points and fees under section 226.32(b)(1)(iii). It is deducted from the amount financed (\$9,900) to derive a total loan amount of \$9,600.
- ii. If the consumer pays the \$300 fee for the creditor-conducted appraisal in cash at closing, the \$300 is included in the points and fees calculation because it is paid to the creditor. However, because the \$300 is not financed by the creditor, the fee is not part of the amount financed under section 226.18(b) (\$10,000, in this case). The total loan amount is \$9,600 (\$10,000, less \$400 in prepaid finance charges).
- iii. If the consumer finances a \$300 fee for an appraisal conducted by someone other than the creditor or an affiliate, the \$300 fee is not included with other points and fees under section 226.32(b)(1)(iii). The amount financed

under section 226.18(b) is \$9,900 (\$10,000 plus the \$300 fee for an independently conducted appraisal that is financed by the creditor, less the \$400 paid in cash and deducted as prepaid finance charges).

2. *Annual adjustment of \$400 amount.* A mortgage loan is covered by section 226.32 if the total points and fees payable by the consumer at or before loan consummation exceed the greater of \$400 or 8 percent of the total loan amount. The \$400 figure is adjusted annually by the Board; the adjusted figure becomes effective on January 1 of the following year. The adjusted figure for 1996 is \$412, reflecting a 3.00 percent increase in the CPI-U from June 1994 to June 1995, rounded to the nearest whole dollar. The Board will publish adjustments after the June figures become available each year. The adjustment for the upcoming year will be included in any proposed commentary published in the fall, and incorporated into the commentary the following spring.

32(b) Definitions

Paragraph 32(b)(1)(i)

1. *General.* Items defined as finance charges under section 226.4(a) and 226.4(b) are included under this paragraph as a component of the total "points and fees." Items excluded from the finance charge under other provisions of section 226.4 are not included under paragraph 32(b)(1)(i), although a fee may be included in "points and fees" under paragraphs 32(b)(1)(ii) and 32(b)(1)(iii).

Paragraph 32(b)(1)(ii)

1. *Mortgage broker fees.* In determining "points and fees" for purposes of this section, compensation paid by a consumer to a mortgage broker (directly or through the creditor for delivery to the broker) is included in the calculation whether or not the amount is disclosed as a finance charge. Mortgage broker fees that are not

paid by the consumer are not included. Mortgage broker fees already included in the calculation as finance charges under section 226.32(b)(1)(i) need not be counted again under section 226.32(b)(1)(ii).

2. *Example.* Section 226.32(b)(1)(iii) defines "points and fees" to include all items listed in section 226.4(c)(7), other than amounts held for the future payment of taxes. An item listed in section 226.4(c)(7) may be excluded from the "points and fees" calculation, however, if the charge is reasonable, the creditor receives no direct or indirect compensation from the charge, and the charge is not paid to an affiliate of the creditor. For example, a reasonable fee paid by the consumer to an independent, third-party appraiser may be excluded from the "points and fees" calculation (assuming no compensation is paid to the creditor). A fee paid by the consumer for an appraisal performed by the creditor must be included in the calculation, even though the fee may be excluded from the finance charge if it is bona fide and reasonable in amount.

32(c) Disclosures

1. *Format.* The disclosures must be clear and conspicuous but need not be in any particular type size or typeface, nor presented in any particular manner. The disclosures need not be a part of the note or mortgage document.

32(c)(3) Regular Payment

1. *General.* The regular payment is the amount due from the borrower at regular intervals, such as monthly, bimonthly, quarterly, or annually. There must be at least two payments, and the payments must be in an amount and at such intervals that they fully amortize the amount owed. In disclosing the regular payment, creditors may rely on the rules set forth in section 226.18(g); however, the amounts for voluntary items not agreed to by the consumer such as credit life insurance

may not be included in the regular payment.

i. If the loan has more than one payment level, the regular payment for each level must be disclosed. For example:

- A. In a 30-year graduated payment mortgage where there will be payments of \$300 for the first 120 months, \$400 for the next 120 months, and \$500 for the last 120 months, each payment amount must be disclosed, along with the length of time that the payment will be in effect.
- B. If interest and principal are paid at different times, the regular amount for each must be disclosed.
- C. In discounted or premium variable-rate transactions where the creditor sets the initial interest rate and later rate adjustments are determined by an index or formula, the creditor must disclose both the initial payment based on the discount or premium and the payment that will be in effect thereafter. Additional explanatory material which does not detract from the required disclosures may accompany the disclosed amounts. For example, if a monthly payment is \$250 for the first six months and then increases based on an index and margin, the creditor could use language such as the following: "Your regular monthly payment will be \$250 for six months. After six months your regular monthly payment will be based on an index and margin, which currently would make your payment \$350. Your actual payment at that time may be higher or lower."

32(c)(4) Variable Rate

1. *Calculating "worst-case" payment example.* Creditors may rely on instructions in section 226.19(b)(2)(x) for calculating the maximum possible increases in rates in the shortest possible timeframe, based on the face amount of the note (not the hypothetical loan amount of \$10,000 required by section 226.19(b)(2)(x)). The

creditor must provide a maximum payment for each payment level, where a payment schedule provides for more than one payment level and more than one maximum payment amount is possible.

32(d) Limitations

32(d)(1)(i) Balloon Payment

1. *Regular periodic payments.* The repayment schedule for a section 226.32 mortgage loan with a term of less than five years must fully amortize the outstanding principal balance through "regular periodic payments." A payment is a "regular periodic payment" if it is not more than twice the amount of other payments.

32(d)(2) Negative Amortization

1. *Negative amortization.* The prohibition against negative amortization in a mortgage covered by section 226.32 does not preclude reasonable increases in the principal balance that result from events permitted by the legal obligation unrelated to the payment schedule. For example, when a consumer fails to obtain property insurance and the creditor purchases insurance, the creditor may add a reasonable premium to the consumer's principal balance, to the extent permitted by the legal obligation.

32(d)(4) Increased Interest Rate

1. *Variable-rate transactions.* The limitation on interest-rate increases does not apply to rate increases resulting from changes in accordance with the legal obligation in a variable-rate transaction, even if the increase occurs after default by the consumer.

32(d)(5) Rebates

1. *Calculation of refunds.* The limitation applies only to refunds of precomputed (such as add-on) interest and not to any other charges that are considered finance charges under section 226.4 (for example, points and fees paid at closing). The calculation of the refund of interest includes

odd-days interest, whether paid at or after consummation.

32(d)(6) Prepayment Penalties

1. *State law.* For purposes of computing a refund of unearned interest, if using the actuarial method defined by applicable state law results in a refund that is greater than the refund calculated by using the method described in section 933(d) of the Housing and Community Development Act of 1992, creditors should use the state law definition in determining if a refund is a prepayment penalty.

32(d)(7) Prepayment-Penalty Exception

Paragraph 32(d)(7)(iii)

1. *Calculating debt-to-income ratio.* "Debt" does not include amounts paid by the borrower in cash at closing or amounts from the loan proceeds that directly repay an existing debt. Creditors may consider combined debt-to-income ratios for transactions involving joint applicants.

2. *Verification.* Verification of employment satisfies the requirement for payment records for employment income.

32(e) Prohibited Acts and Practices

32(e)(1) Repayment Ability

1. *Determining repayment ability.* The information provided to the creditor in connection with section 226.32(d)(7) may be used to show that the creditor considered the consumer's income and obligations before extending the credit. Any expected income can be considered by the creditor, except equity income that the consumer would obtain through the foreclosure of a mortgage covered by section 226.32. For example, a creditor may use information about income other than regular salary or wages such as gifts, expected retirement payments, or income from housecleaning or childcare. The creditor also may use unverified income, as long as the creditor has a reasonable basis for believing that

the income exists and will support the loan.

32(e)(2) Home-Improvement Contracts

Paragraph 32(e)(2)(i)

1. *Joint payees.* If a creditor pays a contractor with an instrument jointly payable to the contractor and the consumer, the instrument must name as payee each consumer who is primarily obligated on the note.

32(e)(3) Notice to Assignee

1. *Subsequent sellers or assignors.* Any person, whether or not the original creditor, that sells or assigns a mortgage subject to this section must furnish the notice of potential liability to the purchaser or assignee.

2. *Format.* While the notice of potential liability need not be in any particular format, the notice must be prominent. Placing it on the face of the note, such as with a stamp, is one means of satisfying the prominence requirement.

SECTION 226.33—Requirements for Reverse Mortgages

33(a) Definition

1. *Nonrecourse transaction.* A nonrecourse reverse-mortgage transaction limits the homeowner's liability to the proceeds of the sale of the home (or any lesser amount specified in the credit obligation). If a transaction structured as a closed-end reverse-mortgage transaction allows recourse against the consumer, and the annual percentage rate or the points and fees exceed those specified under section 226.32(a)(1), the transaction is subject to all the requirements of section 226.32, including the limitations concerning balloon payments and negative amortization.

Paragraph 33(a)(2)

1. *Default.* Default is not defined by the statute or regulation, but rather by the legal obligation between the parties and state or other law.

2. *Definite term or maturity date.* To meet the definition of a reverse-mortgage transaction, a creditor cannot require any principal, interest, or shared appreciation or equity to be due and payable (other than in the case of default) until after the consumer's death, transfer of the dwelling, or the consumer ceases to occupy the dwelling as a principal dwelling. Some state laws require legal obligations secured by a mortgage to specify a definite maturity date or term of repayment in the instrument. Stating a definite maturity date or term of repayment in an obligation does not violate the definition of a reverse-mortgage transaction if the maturity date or term of repayment used would in no case operate to cause maturity prior to the occurrence of any of the events recognized in the regulation. For example, a provision that allows a reverse-mortgage loan to become due and payable only after the consumer's death, transfer, or cessation of occupancy, or after a specified term, but which automatically extends the term for consecutive periods as long as none of the events specified in this section had yet occurred.

33(c) Projected Total Cost of Credit

33(c)(1) *Costs to Consumer*

1. *Costs and charges to consumer—relation to finance charge.* All costs and charges to the consumer that are incurred in a reverse-mortgage transaction are included in the projected total cost of credit, and thus in the total-annual-loan-cost rates, whether or not the cost or charge is a finance charge under section 226.4.

2. *Annuity costs.* As part of the credit transaction, some creditors require or permit a consumer to purchase an annuity that immediately—or at some future time—supplements or replaces the creditor's payments. The amount paid by the consumer for the annuity is a cost to the consumer under this section, regardless of whether the annuity is purchased through the creditor or a third party, or whether the purchase is mandatory or voluntary.

3. *Disposition costs excluded.* Disposition costs incurred in connection with the sale or transfer of the property subject to the reverse mortgage are not included in the costs to the consumer under this paragraph. (However, see the definition of Val₁ in appendix K to the regulation to determine the effect certain disposition costs may have on the total-annual-loan-cost rates.)

33(c)(2) *Payments to Consumer*

1. *Payments upon a specified event.* The projected total cost of credit should not reflect contingent payments in which a credit to the outstanding loan balance or a payment to the consumer's estate is made upon the occurrence of an event (for example, a "death benefit" payable if the consumer's death occurs within a certain period of time). Thus, the table of total-annual-loan-cost rates required under section 226.33(b)(2) would not reflect such payments. At its option, however, a creditor may put an asterisk, footnote, or similar type of notation in the table next to the applicable total-annual-loan-cost rate, and state in the body of the note, apart from the table, the assumption upon which the total-annual-loan-cost is made and any different rate that would apply if the contingent benefit were paid.

33(c)(3) *Additional Creditor Compensation*

1. *Shared appreciation or equity.* Any shared appreciation or equity that the creditor is entitled to receive pursuant to the legal obligation must be included in the total cost of a reverse-mortgage loan. For example, if a creditor agrees to a reduced interest rate on the transaction in exchange for a portion of the appreciation or equity that may be realized when the dwelling is sold, that portion is included in the projected total cost of credit.

33(c)(4) *Limitations on Consumer Liability*

1. *In general.* Creditors must include any limitation on the consumer's liability

(such as a nonrecourse limit or an equity-conservation agreement) in the projected total cost of credit. These limits and agreements protect a portion of the equity in the dwelling for the consumer or the consumer's estate. For example, the following are limitations on the consumer's liability that must be included in the projected total cost of credit:

- i. A limit on the consumer's liability to a certain percentage of the projected value of the home.
- ii. A limit on the consumer's liability to the net proceeds from the sale of the property subject to the reverse mortgage.

2. *Uniform assumption for "net proceeds" recourse limitations.* If the legal obligation between the parties does not specify a percentage for the "net proceeds" liability of the consumer, for purposes of the disclosures required by section 226.33, a creditor must assume that the costs associated with selling the property will equal 7 percent of the projected sale price (see the definition of the Val_n symbol under appendix K(b)(6)).

10. *Effective April 1, 1996, comments on appendixes K and L are added to read as follows:*

APPENDIX K—Total-Annual-Loan-Cost Rate Computations for Reverse-Mortgage Transactions

1. *General.* The calculation of total-annual-loan-cost rates under appendix K is based on the principles set forth and the estimation or "iteration" procedure used to compute annual percentage rates under appendix J. Rather than restate this iteration process in full, the regulation cross-references the procedures found in appendix J. In other aspects the appendix reflects the special nature of reverse-mortgage transactions. Special definitions and instructions are included where appropriate.

(b) Instructions and Equations for the Total-Annual-Loan-Cost Rate

(b)(5) *Number of Unit Periods between Two Given Dates*

1. *Assumption as to when transaction begins.* The computation of the total-annual-loan-cost rate is based on the assumption that the reverse-mortgage transaction begins on the first day of the month in which consummation is estimated to occur. Therefore, fractional unit periods (used under appendix J for calculating annual percentage rates) are not used.

(b)(9) *Assumption for Discretionary Cash Advances*

1. *Amount of credit.* Creditors should compute the total-annual-loan-cost rates for transactions involving discretionary cash advances by assuming that 50 percent of the initial amount of the credit available under the transaction is advanced at closing or, in an open-end transaction, when the consumer becomes obligated under the plan. (For the purposes of this assumption, the initial amount of the credit is the principal loan amount less any costs to the consumer under section 226.33(c)(1).)

(b)(10) *Assumption for Variable-Rate Reverse-Mortgage Transactions*

1. *Initial discount or premium rate.* Where a variable-rate reverse-mortgage transaction includes an initial discount or premium rate, the credit should apply the same rules for calculating the total-annual-loan-cost rate as are applied when calculating the annual percentage rate for a loan with an initial discount or premium rate (see the commentary to section 226.17(c)).

(d) Reverse Mortgage Model Form and Sample Form

(d)(2) *Sample Form*

1. *General.* The "clear and conspicuous"

standard for reverse-mortgage disclosures does not require disclosures to be printed in any particular type size. Disclosures may be made on more than one page, and use both the front and the reverse sides, as long as the pages constitute an integrated document and the table disclosing the total-annual-loan-cost rates is on a single page.

**APPENDIX L—Assumed Loan
Periods for Computations of Total-
Annual-Loan-Cost Rates**

1. *General.* The life expectancy figures

used in appendix L are those found in the U.S. Decennial Life Tables for women, as rounded to the nearest whole year and as published by the U.S. Department of Health and Human Services. The figures contained in appendix L must be used by creditors for all consumers (men and women). Appendix L will be revised periodically by the Board to incorporate revisions to the figures made in the decennial tables.



Report on Indebtedness of Executive Officers and Principal Shareholders and their Related Interests to Correspondent Banks (Form FFIEC 004)

A. For the Calendar Year Ending December 31, 19____
 To be submitted to your bank's board of directors by January 31.

B. _____
 Name of Executive Officer _____ or Principal Shareholder _____ Submitting Report (Please check one)

C. _____
 If the Report is Submitted for Indebtedness of a Related Interest, Name and Address of Related Interest for Which the Report is Submitted

D. _____
 Name of Bank to which Report is Submitted

City _____ State _____

To be submitted by executive officers and principal shareholders of insured banks in satisfaction of the reporting requirements of the Federal Reserve Board's Regulation O (12 CFR Part 215) and as incorporated by the Office of Thrift Supervision (12 CFR Part 563.43), and Part 349 of the Federal Deposit Insurance Corporation's Rules and Regulations (12 CFR Part 349) with respect to indebtedness to correspondent banks and savings associations.

Report the Maximum Amount of Indebtedness Outstanding at Any Time During the Reporting Year, Even if Fully Repaid. Please Read Carefully the Instructions on the Reverse Side of this Report.

E. Name and Address of Correspondent Bank	F. Original Amount	G. Range of Interest Rates (%)	H. Repayment Terms	I. Maturity Date	J. Description of Collateral (If unsecured indicate "none")	K. Balance (10 days prior to this report) (in thousands of dollars)	L. Maximum Amount of Indebtedness Outstanding in Previous Calendar Year (Indicate method used.) (in thousands of dollars)	M. Other Terms (if unusual)

N. I hereby certify that the information given above is complete, correct, and true to the best of my knowledge.

Disclosure of Estimated Burden

The burden associated with this information collection is estimated to vary from 1 to 2 hours per response, depending on individual circumstances. Burden estimates include the time for reviewing instructions, gathering and maintaining data in the required form, and completing the information collection, but exclude the time for compiling and maintaining business records in the normal course of a respondent's activities. A Federal agency may not conduct or sponsor, and an organization (or a person) is not required to respond to a collection of information, unless it displays a currently valid OMB control number. Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be directed to the Office of Information and Regulatory Affairs, Office of Management and Budget, Washington, D.C. 20503, and to one of the following:

Signature of official responsible for report

Secretary
 Board of Governors of the Federal Reserve System
 Washington, D.C. 20551

Legislative and Regulatory Analysis Division
 Office of the Comptroller of the Currency
 Washington, D.C. 20219

Assistant Executive Secretary
 Federal Deposit Insurance Corporation
 Washington, D.C. 20429

Supervision Policy
 Office of Thrift Supervision
 Washington, D.C. 20552

Date Signed

Instructions

Why Report

The Financial Institutions Regulatory and Interest Rate Control Act of 1978, as amended by the Garn-St. Germain Depository Institutions Act of 1982, prohibits preferential lending by a bank to certain insiders of another bank when there is a correspondent account relationship between the banks. Regulation O, 12 CFR Part 215, which implements these statutes, specifies the reporting requirements necessary to ensure compliance.

Terms used in this report are defined in Regulation O and 12 CFR Part 349. The Office of Thrift Supervision has incorporated Regulation O by reference at 12 CFR 563.43 and applies Regulation O, with the exception of 12 CFR 215.13, to savings associations in the same manner and to the same extent as if the association were a bank or member bank. As used in this report, the term bank should be read to include savings associations.

Noncompliance with the reporting requirements of Regulation O could result in civil money penalties for the bank and the reporting executive officer or principal shareholder.

Who Must Report

Executive officers and principal shareholders must report extensions of credit outstanding during the calendar year from correspondent banks of their insured bank. Executive officers and principal shareholders must also report extensions of credit from correspondent banks to their related interests.

How to Report

The reports may be filed on Form 004, Report on Indebtedness to Correspondent Banks, or any form containing identical information. The information must be submitted to the board of directors with a copy maintained at the bank.

When to Report

Reports must be submitted annually by January 31 for the calendar year ending December 31 of the previous year.

What to Report

Executive officers and principal shareholders must report all indebtedness to correspondent banks, including indebtedness of their related interests. Loans that were outstanding at any time during the reporting calendar year must be reported, even if they have been paid off.

Completing the Form

A. Report Date. Enter the calendar year for which you are reporting.

B. Name of Executive Officer or Principal Shareholder. Enter your name. (A person who is not an executive officer or principal shareholder at the time the report is required to be filed is not required to file.)

An *"executive officer"* is defined in section 215.2(e) of Regulation O and generally means an individual who participates or has authority to participate (other than in the capacity of a director) in major policymaking functions of the company or bank, whether or not the officer has an official title, the title designates the officer as an assistant, or the officer is serving without salary or compensation. Certain categories of bank officers (e.g., vice president) are presumed in Regulation O to be executive officers unless the officer is excluded by resolution of the board of directors of the bank or by the bylaws of the bank or company from participation in major policymaking functions of the bank or company, and the officer does not actually participate therein.

A *"principal shareholder of a member bank"* as defined in section 215.11(a)(1) means any person (other than an insured bank, or a foreign bank as defined in 12 USC 3101(7)) that, directly or indirectly, owns, controls, or has power to vote more than 10 percent of any class of voting securities of the member bank. The term includes a person that controls a principal shareholder (e.g., a person that controls a bank holding company). Shares of a bank (including a foreign bank), bank holding company, or other company owned or controlled by a member of an individual's immediate family are presumed to be owned or controlled by the individual for the purposes of determining principal shareholder status.

"Immediate family" as defined in section 215.2(g) means the spouse of an individual, the individual's minor children, and any of the individual's children (including adult children) residing in the individual's home. For reporting purposes, only one individual in the immediate family must file a report if that individual's report includes the required information on indebtedness of his/her immediate family.

C. Related Interests. If you are reporting indebtedness of a related interest, enter the name and address of the related interest. You must complete a separate report for each related interest.

A *"related interest"* as defined in section 215.11(a)(2) means (1) any company controlled by a natural person, or (2) any political or campaign committee controlled by a natural person or the funds or services of which will benefit a natural person.

"Control" of a company is defined generally in section 215.2(c) of Regulation O as ownership or control of 25 percent or more of a company's outstanding voting shares. Control is presumed, however, in certain cases where less than 25 percent ownership exists.

The term *"indebtedness"* includes any extension of credit (as defined in section 215.3 of Regulation O), but does not include: (1) commercial paper, bonds and debentures issued in the ordinary course of business; and (2) consumer credit in an aggregate amount of \$5,000 or less from each

correspondent bank, provided the credit is incurred under terms that are not more favorable than those offered the general public.

D. Reporting Bank. Enter the name of the bank in which you are an executive officer or principal shareholder.

E. Correspondent Bank. Enter the correspondent bank's name and address. You may report indebtedness from more than one correspondent bank on the same form. You also may include the loan number or any other relevant identifying information in this column.

A "correspondent bank" generally means a bank that maintains one or more correspondent accounts for the officer's or principal shareholder's bank that in the aggregate exceed an average daily balance during the reporting calendar year of \$100,000 or 0.5 percent of the officer's or principal shareholder's bank's total deposits (as reported in the bank's first Consolidated Report of Condition or Thrift Financial Report during the calendar year), whichever is smaller. *All insured banks are required by law to make available to their executive officers and principal shareholders a list of their correspondent banks.*

F. Original Amount. Enter the original amount of the loan. If the indebtedness is a line of credit, report the maximum authorized amount.

G. Range of Interest Rates. Enter the range of interest rates charged throughout the reporting year.

H. Repayment Terms. Describe the repayment terms.

I. Maturity Date. Enter the maturity date.

J. Description of Collateral. If the loan is secured, describe the collateral and its value.

K. Balance. Enter the amount of indebtedness outstanding to the correspondent bank as of ten business days before the date of the report. If this balance is not available, or cannot be readily ascertained by the filing date, estimate the amount and provide the actual amount to the board of directors within thirty days.

L. Maximum Amount of Indebtedness. The maximum amount of indebtedness is either (1) the highest outstanding indebtedness during the calendar year for which the report is made, or (2) the highest end of the month indebtedness outstanding during the calendar year for which the report is made. You must consistently use the same method for all indebtedness to the same correspondent bank. You also must indicate whether the maximum amount was determined as of the end of the month or on a daily basis.

M. Other Terms. Describe any unusual terms or other conditions of the loan.

N. Signature. Sign and date the report.