FEDERAL RESERVE BANK OF NEW YORK

[Circular No. 6969
July 5, 1972]

REGULATION Z

Proposed Amendments; Interpretations

To All State Member Banks, and Others Concerned, in the Second Federal Reserve District:

Following is the text of a statement issued June 26 by the Board of Governors of the Federal Reserve System:

> The Board of Governors of the Federal Reserve System today announced that it proposes to amend its Regulation Z (Truth in Lending) in two respects, dealing with disclosures on open-end credit billing statements, such as those issued in connection with bank credit cards and revolving charge accounts.
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> The amendments would:
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> —Require disclosure of a prospective nominal annual percentage rate on billing statements although no finance charges are imposed for the billing period represented by the statement.
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> —Require disclosure of minimum finance charges on billing statements.
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> Interested persons are invited to submit written views or information to the Secretary of the Board, at Washington, D. C. 20551, or to any Federal Reserve Bank for transmittal to the Board, not later than July 31, 1972.

At the same time, the Board of Governors also published two interpretations of its Regulation Z, concerning the determination of the balance that may be used as the basis for a finance charge on open-end credit accounts and the allocation of payments in such accounts.

Printed below are the texts of the proposed amendments and of the interpretations. Comments on the proposed amendments should be submitted by July 31 and may be sent to our Regulations and Bank Analysis Department.

ALFRED HAYES,
President.

[Reg. Z]

TRUTH IN LENDING

Proposed Amendments on Open End Credit

1. Pursuant to the authority contained in the Truth in Lending Act (15 U.S.C. 1601 et seq.) the Board of Governors proposes to amend Part 226 (Regulation Z), in the manner and for the reasons set forth below:

§ 226.5(a)(3) would be amended to read as follows:

§ 226.5—DETERMINATION OF ANNUAL PERCENTAGE RATE

(a) General Rule—open end credit accounts * * *

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(3) Where the finance charge imposed during the billing cycle is or includes

(i) any minimum, fixed, or other charge not due to the application of a periodic rate, other than a charge with respect to any specific transaction during the billing cycle, by dividing the total finance charge for the billing cycle by the amount of the balance(s) to which applicable and multiplying the quotient (expressed as a percentage) by the number of billing cycles in a year; or

(ii) any charge with respect to any specific transaction during the billing cycle (even if the total finance charge also includes any other minimum, fixed, or other charge not due to the application of a periodic rate), by dividing the total finance charge imposed during the billing cycle by the total of all balances and other amounts on which any finance charge was imposed during the billing cycle without duplication and multiplying the quotient (expressed as the percentage) by the number of billing cycles in a year;[5a] except that the annual percentage rate shall not be less than the largest rate determined by multiplying each periodic rate imposed during the billing cycle by the number of periods in a year.

(iii) any minimum, fixed, or other charge not due to the application of a periodic rate and the total finance charge imposed during the billing cycle does not exceed 50¢ for a monthly or longer billing cycle, or the pro rata part of 50¢ for a billing cycle shorter than monthly, by multiplying each applicable periodic rate by the number of periods in a year, notwithstanding the provisions of subdivisions (i) and (ii) of this subparagraph.

[5a] In determining the denominator of the fraction under § 226.5(a)(3)(ii) no amount will be used more than once when adding the sum of the balances to which periodic rates apply to the sum of the amounts financed to which specific transaction charges apply. In every case the full amount of transactions to which specific transaction charges apply shall be included in the denominator. Other balances or parts of balances shall be included according to the manner of determining the balance to which a periodic rate is applied, as illustrated in the following examples of accounts on monthly billing cycles:

1. Previous balance—none

A specific transaction of $100 occurs on first day of the billing cycle. The average daily balance is $100. A specific transaction charge of 3% is applicable to the specific transactions. The periodic rate is 1½% applicable to the average daily balance. The numerator is the amount of the finance charge, which is $4.50. The denominator is the amount of the transaction (which is $100), plus the amount by which the balance to which the periodic rate applies exceeds the amount of specific transactions (such excess in this case is 0), totaling $100.

The annual percentage rate is the quotient (which is 4.5%) multiplied by 12 (the number of months in a year), *i.e.* 54%.

2. Previous balance—$100

A specific transaction of $100 occurs at midpoint of the billing cycle. The average daily balance is $150. A specific transaction charge of 3% is applicable to the specific transaction. The periodic rate is 1½% applicable to the average daily balance. The numerator is the amount of finance charge which is $5.25. The denominator is the amount of the transaction (which is $100), plus the amount by which the balance to which the periodic rate applies exceeds the amounts of specific transactions (such excess in this case is $50), totaling $150.

As explained in example 1, the annual percentage rate is 3.5% x 12 = 42%.

3. If, in example 2, the periodic rate applies only to the previous balance, the numerator is $4.50 and the denominator is $200 (the amount of the transaction, $100, plus the balance to which only the periodic rate is applicable, the $100 previous balance). As explained in example 1, the annual percentage rate is 2.25% x 12 = 27%.

4. If, in example 2, the periodic rate applies only to an adjusted balance (previous balance less payments and credits) and the customer made a payment of $50 at midpoint of billing cycle, the numerator is $3.75 and the denominator is $150 (the amount of the transaction, $100, plus the balance to which only the periodic rate is applicable, the $50 adjusted balance). As explained in example 1, the annual percentage rate is 2.5% x 12 = 30%.

5. Previous balance—$100

A specific transaction (check) of $100 occurs at the midpoint of the billing cycle. The average daily balance is $150. The specific transaction charge is 25 cents per check. The periodic rate is 1½% applied to the average daily balance. The numerator is the amount of the finance charge, which is $2.50, and includes the 25 cents check charge and the $2.25 resulting from the application of the periodic rate. The denominator is the full amount of the specific transaction (which is $100) plus the amount by which the average daily balance exceeds the amount of the specific transaction (which in this case is $50), totaling $150. As explained in example 1, the annual percentage rate would be 1⅔% x 12 = 20%.

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§ § 226.7(b)(5), 226.7(b)(6), and 226.7(c) would be amended to read as follows:

§ 226.7—OPEN END CREDIT ACCOUNTS—SPECIFIC DISCLOSURES

(b) Periodic statements required. * * *

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(5) Each periodic rate, using the term "periodic rate" (or "rates"), that may be used to compute the finance charge (whether or not applied during the billing cycle), the range of balances to which it is applicable, and the corresponding annual percentage rate determined by multiplying the periodic rate by the number of periods in a year. The words "corresponding annual percentage rate," "corresponding nominal annual percentage rate," "nominal annual percentage rate" or "annual percentage rate" (or "rates") may be used to describe the corresponding annual percentage rate. The requirements of § 226.6(a) of this Part with respect to disclosing the term "annual percentage rate" more conspicuously than other required terminology shall not be applicable to the disclosure made under this subparagraph, although such term (or words incorporating such term) may, at the creditor's option, be shown as conspicuously as the terminology required under subparagraph 6 of this paragraph. Where a minimum charge may be applicable to the account, the amount of such minimum charge shall be disclosed.[9a]

(6) When a finance charge is imposed during the billing cycle, the annual percentage rate or rates determined under § 226.5(a) using the term "annual percentage rate" (or "rates").

* * *

(c) Location of disclosures. The disclosures required by paragraph (b) of this section shall be made on the face of the periodic statement, except that, at the creditor's option:

(1) Itemization of the amounts and dates of each extension of credit (or the dates such extensions of credit were debited to the account) required to be disclosed under paragraph (b)(2) and of the "credits" disclosed under (3) of this section, and itemization of the amount of any finance charge required to be disclosed under paragraph (b)(4) of this section, may be made on the reverse side of the periodic statement or on a separate accompanying statement(s), provided that the totals of such respective amounts are disclosed on the face of the periodic statement; and

(2) The disclosures required under paragraph (b)(5) and (b)(8) of this section, except the balance on which the finance charge was computed, may be made on the

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[9a] A creditor imposing minimum charges is not required to adjust the disclosure of the range of balances to which each periodic rate would apply in order to reflect the range of the balances below which the minimum charge applies. If a creditor does not impose a finance charge when the outstanding balance is less than a certain amount, the creditor is not required to disclose that fact or the balance below which no such charge will be imposed.

reverse side of the periodic statement or on the face of a single supplemental statement which shall accompany the periodic statement.

(3) If the creditor exercises any of the options provided under this paragraph, the face of the periodic statement shall contain one of the following notices, as applicable: "NOTICE: See reverse side for important information" or "NOTICE: See accompanying statement(s) for important information" or "NOTICE: See reverse side and accompanying statement(s) for important information," and the disclosures shall not be separated so as to confuse or mislead the customer or obscure or detract attention from the information required to be disclosed.

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2. These proposals, in part, are a republication of certain proposals issued for public comment on August 6, 1971. They have been modified on the basis of comments received on them and further study.

3. The amendment to § 226.5(a)(3) relocates the formula for computing annual percentage rates in the case of finance charges imposed with respect to specific transactions during the billing cycle—for example, one time fees on cash advances—to the section dealing with annual percentage rate computation. The formula was previously contained in § 226.7(b)(6) and Board interpretation § 226.704. This amendment would also clarify the fact that the Regulation does not require computation of the annual percentage rate by the quotient method when the total finance charge, including charges with respect to specific transactions, does not exceed 50¢.

4. A requirement has been added to § 226.7(b)(5) that the corresponding annual percentage rate for each periodic rate applicable to the account be shown on each periodic statement, whether or not a finance charge is imposed during the billing cycle. Many creditors have previously made this disclosure, which was permissible, although not required, under Regulation Z. A variety of specified wording may be used to describe these rates under the new proposal. The permitted use of optional wording is to allow creditors maximum freedom to choose wording to distinguish between rates which were actually applied during the billing cycle (required to be disclosed under § 226.7(b)(6)) and the prospective nominal rates required to be disclosed by this subparagraph, where those rates differ. The optional wording will also minimize the need for reprinting periodic statements where nominal rate disclosures have previously been made by the creditor. Whatever wording is chosen may, though need not be, used to satisfy the terminology requirements for the initial disclosures under § 226.7(a)(4) and advertising under § 226.10(c)(4). Although the "more conspicuous" requirement of § 226.6(a) for the term "annual percentage rate" will not be applicable to disclosures under § 226.7(b)(5), it will continue to apply to the term "annual percentage rate" in opening disclosures under § 226.7(a) and in advertising under § 226.10(c), even if the creditor chooses to make disclosures under § 226.7(a)(4) and § 226.10(c)(4) using optional wording which simply incorporates this term—e.g., "corresponding ANNUAL PERCENTAGE RATE." No additional disclosures will be required by the new provisions for many open end creditors such as those who compute finance charges simply by the application of one or more periodic rates and who are already supplying this information.

The new provision also would require disclosure of minimum charges which may be imposed on accounts with balances below a certain amount. This new disclosure requirement does not compel creditors to disclose the range of balances to which the minimum charge may be applicable; creditors may continue to disclose ranges of balances to which periodic rates apply under § 226.7(b)(5) without specifically designating the portion of any such range to which the minimum charge, instead of the periodic rate, is applicable. For example, disclosure could be made that "a periodic rate of 1½% per month which is an ANNUAL PERCENTAGE RATE of 18% will be applied to balances from $0 to $500, with a minimum charge of 50¢."

5. The amendment to § 226.7(b)(6) consists of the addition of the opening phrase "when a finance charge is imposed during the billing cycle." In addition, the words "and, where there is more than one rate, the amount of the balance to which each rate is applicable" have been deleted since the applicable requirement is already contained in § 226.7(b)(5) which requires disclosure of the range of balances to which each rate is applicable. The amendment is primarily designed to clarify the fact that the annual percentage rate disclosures under this paragraph (as determined by § 226.5(a)) are only required when finance charges are imposed during the billing cycle. Material relating to computation of the annual percentage rate where transaction charges are imposed during the billing cycle has been removed from the provision and incorporated into the new § 226.5(a)(3)(ii).

6. The amendment of § 226.7(c), which deals with the location of required disclosures on periodic statements, would simplify placement of the disclosures in a way which is expected to be more meaningful and useful to the customer and minimize confusion. The amendment incorporates Board interpretation § 226.702.

If the proposed amendments are adopted, the Board will issue the amendments in final form with an appropriate prospective date so as to permit such changes in printed forms and procedures as may be necessary for compliance in an orderly manner.

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

To aid in the consideration of these matters by the Board, interested persons are invited to submit relevant data, views, or arguments. Any such material should be submitted in writing to the Secretary, the Board of Governors of the Federal Reserve System, Washington, D. C. 20551, or to any Federal Reserve Bank for transmittal to the Board, to be received at the Board not later than July 31, 1972. Such material will be made available for inspection and copying upon request, except as provided in § 261.6(a) of the Board's Rules Regarding Availability of Information.

By order of the Board of Governors, June 21, 1972.

PART 226—TRUTH IN LENDING

Miscellaneous Interpretations

Interpretation § 226.703 is amended to read as follows:

§ 226.703 Finance charge based on average daily balance in open end credit accounts

Section 226.7(b)(8) requires that periodic statements for open end accounts shall disclose, among other things, "the balance on which the finance charge was computed, and a statement of how that balance was determined." In some instances, creditors compute a finance charge on the average daily balance by application of a monthly periodic rate. In such case, this information is adequately disclosed if the statement gives the amount of the average daily balance on which the finance charge was computed, and also states how the balance is determined. In other instances, the finance charge is computed on the balance each day by application of a daily periodic rate and such charges are accumulated and debited to the account in a single amount for the billing cycle. The question arises whether the periodic statement must show for each day of the billing cycle a balance on which a finance charge was computed.

If a daily periodic rate is used, the balance to which it is applicable shall be stated as follows:

(1) A balance for each day in the billing cycle; or

(2) A balance for each day in the billing cycle on which the balance in the account changes; or

(3) The sum of the daily balances during the billing cycle; or

(4) The average daily balance during the billing cycle in which case the creditor shall state on the face of the periodic statement, its reverse side, or on an enclosed supplement wording to the effect that the average daily balance is or can be multiplied by the number of days in the billing cycle and the periodic rate applied to the product to determine the amount of the finance charge.

(Interprets and applies 15 U.S.C. 1637.)

§ 226.706 Open end credit—allocation of payments

Section 226.7(a)(2) provides that before the first transaction is made on any open end credit account, the creditor must disclose "the method of determining the balance upon which a finance charge may be imposed." Section 226.7(b)(8) requires the creditor to disclose on the periodic statement "the balance on which the finance charge was computed, and a statement of how that balance was determined." The question is raised whether these provisions require a creditor to provide a description of the manner in which payments or other credits are applied to various portions of the balance or balances on which finance charges are computed.

In disclosing the method of determining the balance(s) upon which finance charges are computed, it is not necessary to show the method of allocating payments or other credits. For example, explanation of the manner in which payments or credits may be applied to late charges, overdue balances, finance charges, insurance premiums or other portions of balances is not required. Similarly, explanation of the method of allocating such payments between cash advance and purchase portions of the account is not required. Such explanations in many cases involve lengthy and complex descriptions which may unduly complicate disclosures.

Explanation of the allocation method may be made by creditors where it can be done in conformity with § 226.6(c) which authorizes additional information or explanations as long as they are not stated, utilized, or placed so as to mislead or confuse the customer or contradict, obscure, or detract attention from the required disclosures.

(Interprets and applies 15 U.S.C. 1637.)