# FEDERAL RESERVE BANK OF NEW YORK

[Circular No. 8095
April 21, 1977]

## INTERPRETATIONS OF REGULATIONS C AND Z

### —Disclosures Under the Home Mortgage Disclosure Act

### —Dealer Participation in Consumer Credit Contracts

### Withdrawal of Proposed Amendment to Regulation Z

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

The Board of Governors of the Federal Reserve System has issued two interpretations of its Regulation C—Home Mortgage Disclosure—and an interpretation of its Regulation Z—Truth in Lending—to clarify certain aspects of these regulations. The Board of Governors has also withdrawn a proposed amendment to Regulation Z.

Following is the text of a statement issued by the Board on March 31, 1977:

The Board of Governors of the Federal Reserve System today adopted three interpretations intended to clarify certain aspects of its consumer credit protection regulations.

The Board adopted an interpretation of its Truth in Lending Regulation Z stating that the amount of a dealer's participation in the finance charge on the credit purchase of an automobile or other durable goods need not be disclosed as a separate part of the finance charge.

At the same time, the Board withdrew a proposal that would have required disclosure of the fact but not the amount of a dealer's participation.

The Board took these actions because it did not feel that disclosure of a dealer participation in a finance charge would significantly benefit consumers in shopping for credit.

At the same time, the Board adopted two technical interpretations of its Home Mortgage Disclosure Regulation C. The Home Mortgage Disclosure Act and Regulation C require depository institutions with offices in metropolitan areas to disclose publicly the geographic area where they are making their residential mortgage loans.

The first interpretation permits a depository institution subject to the Act that is majority-owned by another depository to disclose its mortgage loan data separately from that of the parent.

The second interpretation of Regulation C clarifies what disclosures must be made by depositories that were exempt from the provisions of the Act, but lose their exemption. A depository is exempt if (a) it does not have an office in a Standard Metropolitan Statistical area (SMSA), (b) does not have assets on the last day of its fiscal year of $10 million or more or (c) is a State chartered institution subject to a State disclosure law that the Board has determined imposes disclosure requirements substantially similar to those of the Home Mortgage Disclosure Act.

The Board's interpretation makes it clear that previously exempt institutions which become subject to the Act (by extension of an SMSA to cover one or more of its offices or by growth of its assets) may report on their mortgage lending during their last full fiscal year by Postal ZIP code areas and thereafter by Census Bureau census tracts. This is the same treatment accorded depositories in the first year after Regulation C became effective (June 28, 1976).

Enclosed are copies of the interpretations, which have been reprinted from the *Federal Register* of April 12, 1977. Questions thereon may be directed to our Consumer Affairs Division (Tel. No. 212-791-5919).

Additional copies of the enclosures will be furnished upon request.

PAUL A. VOLCKER,
*President.*

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Board of Governors of the Federal Reserve System

# HOME MORTGAGE DISCLOSURE

## INTERPRETATION OF REGULATION C

[Reg. C; Docket No. R-0092]

### PART 203—HOME MORTGAGE DISCLOSURE

#### Interpretations

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Interpretations.

SUMMARY: In response to requests from Federal agencies and institutions affected by the Home Mortgage Disclosure Act, the Board has issued two interpretations of Regulation C, which implements the act. The first interpretation permits a parent depository institution, such as a bank, savings and loan association, or credit union, to treat any bank or savings and loan association in which it owns a majority interest as a separate, unaffiliated institution for disclosure purposes. Public disclosure will be enhanced if that potion is chosen. The second interpretation clarifies the disclosure requirements applicable to a depository institution that ceases to be exempt under the act.

EFFECTIVE DATE: April 1, 1977.

FOR FURTHER INFORMATION CONTACT:

Anne J. Geary, Acting Chief, Equal Credit Opportunity Section, Division of Consumer Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 20551. (202-452-3946).

SUPPLEMENTARY INFORMATION: The Board has issued the following two interpretations of Regulation C pursuant to its authority under section 305(a) of the Home Mortgage Disclosure Act of 1975 (12 U.S.C. 2801-2809).

203.001: TREATMENT OF MAJORITY-OWNED, DEPOSITORY SUBSIDIARIES OF DEPOSITORY INSTITUTIONS

The Board has been asked whether a majority-owned, depository subsidiary of a depository institution should be treated in the same way as a non-depository subsidiary. The first sentence of § 203.2(c) defines a depository institution as "any commercial bank, savings bank, savings and loan association, building and loan association, homestead association (including cooperative banks), or credit union, which makes federally related mortgage loans." The second sentence deals with subsidiaries: "Any majority-owned subsidiary of a depository institution shall be deemed to be part of its parent depository institution for the purposes of this part." The purpose of the subsidiary provision is to provide a more complete picture of a parent's lending patterns by including information regarding the lending activities of any non-depository, majority-owned subsidiary.

A few depository institutions, however, have majority-owned subsidiaries that are themselves depository institutions. This raises the issue of how a depository institution as defined in the first part of § 203.2(c), which is also a majority-owned subsidiary of a depository institution, should be treated for Regulation C disclosure purposes. If, absent the second part of § 203.2(c), the depository subsidiary otherwise would make separate disclosures under Regulation C, then combining the subsidiary's loan data with the parent's into a single statement would reduce public disclosure, contrary to the intent of § 203.2(c) and the purpose of the Home Mortgage Disclosure Act.

Therefore, to further the intent of the act and the regulation, a parent depository institution may draw a distinction for disclosure purposes between depository and non-depository, majority-owned subsidiaries. A majority-owned, non-depository subsidiary of a depository institution should be treated as an integral part of its parent, with no distinction made between them for reporting purposes, in accordance with the second sentence of § 203.2(c). On the other hand, at the parent's option, a majority-owned, depository subsidiary of a depository institution may be treated as a distinct, unaffiliated entity since it is a depository institution as defined in the first sentence of § 203.2(c).

203.002: DISCLOSURE AFTER LOSS OF EXEMPTION

The Board has been requested to clarify the Regulation C disclosure requirements that apply to a depository institution that ceases to be exempt from the Home Mortgage Disclosure Act.

Section 203.3(a) of Regulation C describes the three classes of depository institutions that are exempt from the regulation's disclosure requirements. They are: (1) Institutions that have assets of $10,000,000 or less as of the last day of their fiscal year; (2) institutions that do not have an office in a standard metropolitan statistical area; and (3) State-chartered institutions that are subject to a State disclosure law that the Board has determined imposes substantially similar requirements to those mandated by the Home Mortgage Disclosure Act.

Section 203.3(b) sets forth the initial disclosure requirements applicable to an exempt institution that subsequently loses its exemption. It states:

> A depository institution that was exempt on or after the effective date of this Part on the basis of paragraph (a) of this section and that subsequently becomes no longer exempt shall compile the data described in § 203.4 of this Part for each fiscal year beginning with its last full fiscal year ending prior to the date it was no longer exempt, and that last full fiscal year shall be deemed to be a "full fiscal year ending prior to July 1, 1976" for the purposes of § 203.4 of this Part.

The first point on which clarification has been sought is the meaning of the language "last full fiscal year ending prior to the date it was no longer exempt * * *." For any depository institution that loses its exemption under § 203.3(a)(2) because of the re-definition of a standard metropolitan statistical area or loses its exemption under § 203.3(a)(3) because applicable State disclosure law is found not to be substantially similar to the Federal act, "its last full fiscal year ending prior to the date it was no longer exempt" is its fiscal year immediately preceding the fiscal year during which the exemption was lost. For example, a depository institution having a calendar fiscal year that ceases to be exempt during 1977 would have to disclose relevant 1976 data.

For any depository institution that loses its exemption under § 203.3(a)(1) because its assets exceeded $10,000,000 on the final day of its last fiscal year, the period to be covered by its initial disclosure statement is that last fiscal year. For example, a calendar fiscal year institution that has assets of more than $10,000,000 on December 31, 1977 would have to disclose relevant 1977 loan information.

The Board also has been asked to explain the significance of the phrase " 'full fiscal year ending prior to July 1, 1976 * * *.' " The purpose in § 203.3(b) of equating an institution's "last full fiscal year ending prior to the date it was no longer exempt" with a " 'full fiscal year ending prior to July 1, 1976' " is to make available to an institution that loses its exemption the same disclosure options that were available to institutions when Regulation C became effective. Thus, for the purposes of § 203.4, a depository institution that ceases to be exempt may compile the necessary mortgage and home improvement loan data by United States Postal Service ZIP codes, in lieu of Census Bureau census tracts, for its last full fiscal year and any portion of its current fiscal year ending prior to the loss of exemption. In addition, such an institution may exercise the options and rely on the presumption contained in paragraphs (a)(4)(ii) and (c) of § 203.4





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as if it had lost its exemption and become subject to the regulation on July 1, 1976.

The following examples illustrate the points made in this interpretation. Assume that a depository institution having a calendar fiscal year ceases to be exempt under § 203.3(a) (2) on April 1, 1977, because of the enlargement of a standard metropolitan statistical area to include a county in which the institution has an office. Pursuant to § 203.5(a) (1) (iii), that institution would be required to prepare and make available publicly a disclosure statement by June 29, 1977, ninety days after its loss of exemption.

Under § 203.3(b), the disclosure statement would have to cover the institution's "last full fiscal year ending prior to the date it was no longer exempt," which, as indicated previously, would be 1976. Pursuant to § 203.4(a) (2) (i), read in view of § 203.3(b), the institution could compile the necessary loan information for 1976 by ZIP code if it chose.

Also, under § 203.4(a) (2) (ii), it could elect to issue a separate disclosure statement, compiled on a ZIP-code basis, for the first three months of its current fiscal year—January, February, March 1977, if it also made that statement available on June 29, 1977. If it chose that option, then it would report on its relevant lending activities for the remainder of 1977 by census tract on March 31, 1978. The alternative to this latter option would be for the institution to report on all of its relevant lending activities during 1977 by census tract on March 31, 1978. Finally, the institution may exercise the reporting options and rely on the residence presumption set forth in §§ 203.4(a) (4) (ii) and 203.4(c) for its 1976 disclosure statement and the January through March 1977 statement if that option is chosen.

The second example assumes that a depository institution having a calendar fiscal year ceases to be exempt under § 203.3(a) (1) because its assets exceed $10,000,000 as of December 31, 1977. Pursuant to the applicable provisions of the regulation as outlined in the preceding example, the institution would have to prepare a disclosure statement by March 31, 1978, covering its relevant lending activities during 1977 on a ZIP-code basis. Since the loss of exemption would not have occurred during the course of its fiscal year, no partial fiscal year report would be possible. The options and presumption contained in §§ 203.4(a) (4) (ii) and 203.4(c) respectively could be used, however, in preparing the 1977 disclosure statement.

By order of the Board of Governors, March 28, 1977.

THEODORE E. ALLISON,
*Secretary of the Board.*

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## Board of Governors of the Federal Reserve System

# TRUTH IN LENDING

# INTERPRETATION OF REGULATION Z

[Reg. Z; Docket No. R–0053]

### PART 226—TRUTH IN LENDING

#### Interpretation on Disclosure of Amount of Dealer Participation

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board hereby adopts an interpretation of Regulation Z stating that a dealer participation need not be identified or disclosed in Truth in Lending disclosures as a separate component of the finance charge. Simultaneous with the adoption of the interpretation, the Board withdraws a proposed amendment to regulation Z which would have required separate disclosure of the existence, but not the amount, of a dealer participation. The Board takes this action based on its conclusions (1) that a dealer participation is not a "finder's fee or similar charge" within the meaning of Regulation Z and so need not be separately disclosed under the present regulation, and (2) that amending the regulation to require separate disclosure of the existence of a dealer participation would not significantly aid consumers in shopping for credit but would result in more complex Truth in Lending disclosure statements and possible confusion or misunderstanding.

EFFECTIVE DATE: March 28, 1977.

FOR FURTHER INFORMATION CONTACT:

D. Edwin Schmelzer, Chief, Fair Credit Practices Section, Division of Consumer Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, 202–452–2412.

SUPPLEMENTARY INFORMATION: On August 23, 1976, the Board of Governors published for comment a proposed Interpretation § 226.821 of Regulation Z relating to the separate disclosure of a dealer participation in a consumer credit transaction (41 FR 35536). A dealer participation is typically a portion of the interest component of a finance charge which is allocated to a seller of consumer goods either by a creditor which provides direct consumer financing arranged through the seller or by an assignee which purchases a retail instalment contract from the seller. The Board was asked to determine whether a dealer participation constitutes a "finder's fee or similar charge" within the meaning of § 226.4(a)(3) of the regulation and so must be itemized and disclosed as a separate component of the finance charge pursuant to § 226.8(c)(8)(i). The proposed interpretation stated, in essence, that inasmuch as a dealer participation is simply a part of the single component of the finance charge computed by the application of a percentage rate or rates to the amount financed, it is not considered a finder's fee or similar charge and need not be separately identified or disclosed.

The Board received more than 250 comments on the proposed interpretation, the vast majority favoring the interpretation. However, comments from Federal agencies and consumer representatives indicated to the Board that consumer benefits might be derived from disclosure of the existence of a dealer participation. Therefore, on January 6, 1977, the Board published for comment (42 FR 1268) a proposed amendment to Regulation Z which, if adopted, would have become § 226.8(c)(9) and which would have required that in credit sales the disclosure statement furnished to the consumer contain, where applicable, a disclosure of the existence but not the amount of a dealer participation. For convenient reference, the proposed amendment is republished below:

Section 226.8—*Credit other than open end—specific disclosures.*

* * * * *

(c) *Credit sales.* * * *

(9) A statement that the seller or other party to the transaction arranging credit may receive from another creditor in the transaction a portion of the finance charge imposed on that transaction.

The Board indicated in publishing the proposed amendment that it would take final action on the proposed Interpretation § 226.821 in connection with its final determination on the proposed amendment.

The Board received approximately 400 comments on the proposed amendment to Regulation Z. The comments came from financial institutions, automobile dealers and other merchants, trade associations, a Federal agency, State consumer agencies, consumer groups, a university consumer affairs office, private and legal services attorneys, and private individuals. The comments can readily be broken down into three broad categories: (1) more than 81 percent of the commenters expressed opposition to the amendment requiring disclosure of dealer participations, (2) over 12 percent favored the amendment, and (3) more than 6 percent expressed the belief that the amendment was not stringent enough or did not require enough disclosure and, therefore, should not be adopted. Additionally, a significant number of commenters, almost half of those in category 2 and almost all of those in category 3, felt that the amount as well as the fact of a dealer participation should be disclosed.

As a result of the comments received, both in response to the proposed Interpretation § 226.821 and the proposed amendment § 226.8(c)(9), the Board has reached certain conclusions which are set forth below.

Dealer participation is largely a phenomenon of the financing of automobile purchases, wherein the automobile dealer secures financing for a purchaser from a lending institution in connection with the sale of a car and receives some portion of the finance charge imposed by the lending institution. In an alternative mode of proceeding, the dealer may finance the purchase of a car for it customer and thereafter assign the credit agreement to a financial institution and receive a portion of the finance charge imposed from that financial institution. Typically, in connection with the extension of credit to the customer, the dealer interviews the customer and takes a credit application, prepares the loan documents, and reviews the terms of the loan and relevant disclosures with the customer. The customer is generally able to complete all aspects of financing his or her purchase without leaving the dealer's place of business. Often the arrangement between the dealer and the lending institution provides for "recourse" by the lender against the dealer for any loss suffered by the lender if the consumer defaults on the loan. Because of these resourse arrangements, consumers with only marginal credit may be able to obtain financing for major purchases. The dealer's participation in the finance charge may serve as compensation for the work done in arranging the financing and for the risk of loss which is shared with the lending institution. Therefore, the Board believes that, in many instances, the portion of the finance charge which represents the dealer's participation is not an amount which the consumer could save by obtaining a direct loan from a lending institution.

Further, although rates available on direct loans are often somewhat lower than in dealer-arranged loans, the Board believes that consumers are generally aware of this fact. The Board feels that disclosure of the total finance charge, the annual percentage rate and the periodic payment, all required by the Truth in Lending Act and Regulation Z, together with the widespread advertisement of credit terms, have afforded and continue to afford consumers the most important information with which to comparison shop for credit. The Board does not believe that the proposed



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§ 226.8(c)(9) would significantly enhance the consumer's ability to shop for credit. Conversely, the addition of another disclosure requirement to Regulation Z would result in more complex disclosure statements and could lead to confusion or misunderstanding by consumers. The adoption of an additional disclosure requirement of doubtful value to consumers is also contrary to the perceived need for simplification of Regulation Z.

For the reasons set forth above, the Board has determined to withdraw the proposed § 226.8(c)(9) and not to require the disclosure of the existence of a dealer participation. Furthermore, in the Board's view, Interpretation § 226.821 represents a proper application of the requirements of Regulation Z to the issue of dealer participation. A dealer participation of the type described in the interpretation differs from the finder's fee or similar charge which must be disclosed pursuant to § 226.4(a)(3) and need not be separately itemized when it consists of a part of a finance charge attributable to the application of a percentage rate or rates to the amount financed. The Board also notes that its position is in accord with a recent appellate court decision on this issue, *Meyers v. Clearview Dodge Sales, Inc.*, 539 F.2d 511 (5th Cir. 1976).

The text of Interpretation § 226.821, effective immediately, is as follows:

**§ 226.821 Disclosure of dealer participation.**

(a) Section 226.8(c)(8)(i) requires the itemization of each component of a finance charge consisting of more than one type of charge. Section 226.4(a)(3) lists among the types of charges to be included in the finance charge a "finder's fee or similar charge." In certain credit transactions, such as the sale of automobiles and other consumer goods, where the finance charge is determined by application of a percentage rate or rates to the amount financed, a portion of that charge may be allocated to the dealer by the financial institution as a dealer participation. The question arises whether such allocations must be itemized as a separate component of the total finance charge in the nature of a finder's fee.

(b) The requirement for itemization of a finance charge which includes a finder's fee or other elements in addition to an interest component is intended to assure that the total finance charge disclosed to the customer properly reflects all components which must be included in that amount. Any component of the finance charge which is computed by the application of a percentage rate or rates to the amount financed constitutes a single charge of the type described in § 226.4(a)(1). As such, it must be included in the finance charge calculation and disclosure. A portion of such single component of the finance charge which is distributed to a dealer is not considered a "finder's fee or similar charge" and need not be separately identified or disclosed. The concept of a "finder's fee," as that term is used in § 226.4(a)(3), is intended to cover certain charges in the nature of brokerage fees which are imposed in addition to that portion of the finance charge attributable to the application of a percentage rate or rates to the amount financed. Any such separate fee must, of course, be separately itemized.

(Interprets and applies 12 CFR 226.8.)

By order of the Board of Governors, March 28, 1977.

THEODORE E. ALLISON,
*Secretary of the Board.*

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