

**FEDERAL RESERVE BANK  
OF NEW YORK**

[Circular No. 8098]  
April 26, 1977]

**AMENDMENTS TO REGULATION Z**

—Spanish Language Truth in Lending Disclosures

—Advance Disclosure of Variable Interest Rate Clauses

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

The Board of Governors of the Federal Reserve System has adopted amendments to its Regulation Z (Truth in Lending):

(a) To permit the use of the Spanish language within the Commonwealth of Puerto Rico in disclosures called for by the Truth in Lending Act and Regulation Z, although English language disclosures must be provided if the customer so requests; and

(b) To require a creditor to make certain advance disclosures regarding any variable interest rate clause in a credit contract that may result in an increase in the cost of the credit to the customer.

The amendment regarding Spanish language Truth in Lending disclosures became effective April 11, 1977; the amendment regarding advance disclosure of variable interest rate clauses is effective October 10, 1977.

**Spanish Language Disclosures**

In submitting the amendment regarding Spanish language disclosures for publication in the *Federal Register*, the Board of Governors issued the following explanatory notice:

**AGENCY:** Board of Governors of the Federal Reserve System.

**ACTION:** Final Rule.

**SUMMARY:** The Board hereby adopts an amendment to § 226.6(a) of Regulation Z permitting the use of Spanish rather than English language Truth in Lending disclosures in the Commonwealth of Puerto Rico. English language disclosures must be provided to customers if they so request. The Board's action is based upon the fact that Spanish is the traditional and predominant language used in Puerto Rico. This amendment will permit creditors to provide more meaningful disclosures to customers in a more efficient and effective manner.

**EFFECTIVE DATE:** Immediately.

**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 December 6, 1976, the Board issued a proposed amendment to § 226.6(a) of Regulation Z which would permit the use of Spanish rather than English language Truth in Lending disclosures in Puerto Rico. The proposed amendment required that English language disclosures be provided upon the customer's request, either in substitution for the Spanish disclosures or as additional information in accordance with § 226.6(c).

The purpose of this proposal was to conform the Truth in Lending Act's disclosure requirements to language use in Puerto Rico where the pervasive and dominant language is Spanish. The proposal recognized the unique status of the Spanish language in Puerto Rico as reflected in the Board's examination of case and statutory law and statistical data derived from census materials. This proposal was published for comment on December 17, 1976, (41 FR 55198). Twenty-five comments were received. The comments supported the idea of providing Spanish language Truth in Lending disclosures.

Based upon the Board's independent analysis and upon the comments received, the Board has concluded that Spanish rather than English language disclosures may be furnished to customers in Puerto Rico.

(OVER)



## Variable Interest Rate Disclosures

Printed below are the text of the Board of Governors' press statement, issued April 12, 1977, relating to the amendment regarding variable interest rate disclosures, and an excerpt from the *Federal Register* of April 20, 1977, containing an explanatory notice by the Board concerning that amendment:

The Board of Governors of the Federal Reserve System today amended its Regulation Z (Truth in Lending) to require advance disclosure of any variable rate clause in a credit contract that may result in an increase in the cost of the credit to the customer.

The new rule will become effective October 10, 1977.

The amendment adopted was substantially similar to a proposal issued by the Board for public comment last October.

The main requirements of the new rule include disclosure of:

—The fact that the annual percentage rate on the transaction is subject to increase. (The October proposal would have applied to all situations in which the annual percentage rate was subject either to an increase or decrease.)

—The conditions under which the rate may increase, including identification of any index to which the rate is tied, and any limitation on the increase.

—The manner in which an increase may be affected, including an increase in payment amounts, a change in the number of scheduled payments, or an increase in the amount due at maturity.

—Numerical examples—in the case of home mortgage transactions only—based on a hypothetical immediate increase of one quarter of a percentage point in the annual percentage rate, effected through a change in the number of scheduled payments, or an increase in the amount of those payments.

The requirement for numerical examples for residential mortgages applies to transactions in which a security interest is taken in real property used or expected to be used as the customer's dwelling and need not be made in transactions primarily for agricultural purposes.

[Reg. Z; Docket No. R-0003]

### PART 226—TRUTH IN LENDING

#### Amendment to Regulation Z Concerning Variable Interest Rates

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: This rule requires creditors to make certain additional disclosures when variable interest rate clauses are used in credit transactions. It requires disclosure of the fact that the annual percentage rate is subject to increase, the conditions under which an increase may occur, the manner in which an increase would be effected, and in some cases, information on the effect a rate increase would have on the payment amounts and/or maturity of the obligation. This rule was adopted in view of the increased use of variable-rate clauses in credit contracts and the consumers' need for more information about them. It is intended to promote consumer understanding of the operation and effect of variable rate clauses.

EFFECTIVE DATE: October 10, 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: The Board of Governors of the Federal Reserve System has amended Regulation Z to require a creditor to disclose to

customers, in advance of their becoming obligated on a credit contract, a variable interest rate clause if the contract, note, or other instrument evidencing the obligation so provides. The information that must be provided in all obligations in which the annual percentage rate is subject to increase includes the fact that the rate may increase, the conditions under which it may do so, any limitations on the increase, and the manner in which a rate increase may be effected, e.g., through an increase in the payment amount, number of payments or amount due at maturity. In addition, in certain types of transactions, examples must be provided showing the effect on the payment amount and/or the length of maturity that would be caused by a hypothetical immediate increase in the annual percentage rate of one quarter of one percentage point. The transactions for which these hypothetical examples must be given are those in which a security interest is taken in real property used or to be used as the customer's dwelling, if the obligations are repayable in substantially equal installments at substantially equal intervals. The hypothetical examples need not be provided for transactions primarily for agricultural purposes, transactions in which the substantially equal installments do not include repayments of principal, or certain optional insurance transactions.

If the rate should increase in accordance with the conditions and limitations so disclosed, such increase would not constitute a refinancing of the obligation and would not require new disclosures to be made at the time of the rate change.

When this amendment becomes effective, Board Interpretation § 226.810 concerning variable rate disclosures will be rescinded, inasmuch as the amendment makes the interpretation unnecessary.

On October 29, 1976, the Board published for comment in the *FEDERAL REGISTER* (41 FR 47497) a proposed amendment regarding variable interest rate disclosures. Two hundred and fifteen written comments on the proposal were received and analyzed. In light of the suggestions and comments made, the Board has revised the amendment as follows.

(1) The scope of the provision has been narrowed to apply only to those situations in which the annual percentage rate is prospectively subject to increase, rather than all those in which the rate is subject to change. This revision is in keeping with the Board's previous position that a reduction in the annual percentage rate does not constitute a refinancing and does not require new disclosures. If a creditor wishes to show the effect of rate decreases, of course, this would be permissible as additional information under § 226.6(c) of the regulation. The complexity of the required disclosures would be substantially reduced by this change. Furthermore, since the amounts disclosed for decreases are within a few cents of the amounts shown for increases, little additional information would be provided to the consumer. This change also avoids application of the provision to certain transactions which were not intended to be covered, e.g., a series of sales in which the annual percentage rate on a purchase may be reduced when a subsequent purchase extends the term of repayment for the first purchase to coincide with that of the second. It also avoids misapprehension by



creditors whose contracts provide only for rate increases that they would be required to show the effects of rate decreases.

It should be noted that the amendment by its terms applies to increases in the annual percentage rate rather than increases in the contract interest rate. Since interest is a component of the finance charge, increases in the interest rate would cause the annual percentage rate to increase.

(2) The scope of the provision has also been clarified by means of a footnote stating that it is not triggered by contracts permitting a higher rate of interest upon default, acceleration, late payment, assumption or transfer of property.

(3) The requirement of showing hypothetical examples of the effect of rate changes has been limited to transactions in which a security interest is taken in real property used or expected to be used as the customer's dwelling. This change is designed to provide information on the effect of rate changes in those transactions in which such information will most clearly be of the greatest importance. Typically, transactions involving a customer's dwelling are for large amounts and lengthy maturities. The requirement of giving the hypothetical examples has been deleted for three types of transactions: transactions primarily for agricultural purposes, transactions in which the substantially equal instalments do not include repayments of principal, and optional insurance agreements made pursuant to Board Interpretation § 226.814.

Agricultural transactions would be excepted because of the additional burden these requirements would place on agricultural lenders who use variable rate loans quite extensively. (It should be noted that many agricultural transactions are already exempted from disclosing an annual percentage rate pursuant to § 226.8(p), a special section for certain agricultural purpose transactions, and therefore would not be affected at all by the variable rate proposal.)

The second class of transactions that would be expected from the requirement of disclosing hypothetical examples is transactions in which the substantially equal instalments do not include repayments of principal. This technical change would avoid covering demand loans in which the periodic equal instalments consist of only interest, with the entire principal sum due on demand. These transactions were never intended by the Board to be covered, but they arguably would have been included under the language of the earlier version.

The third class of excepted transactions is insurance agreements entered subsequent to consummation with premiums added to the balance of the obligation. The Board believes this exclusion to be proper for two reasons: (1) These agreements are closely tied to the underlying obligation and the variable rate disclosures will already have been made for that obligation; and (2) the hypothetical changes in payment amount and maturity would be de minimus in this type of transaction.

It should be noted that in these three types of transactions, the hypothetical examples of § 226.8(b)(8) (iii) and (iv) need not be given, but there must still be disclosures of the fact that the rate is subject to increase, the conditions under which it may change, and the manner in which the change may be effected (§ 226.8(b)(8) (i) and (ii)).

(4) The October 1976 proposal would have required that the hypothetical examples of § 226.8(b)(8) (iii) and (iv) show the effect of the maximum amount of incremental change allowed by contract or, if there is no such limitation, a change of one quarter of one percentage point. The proposed amendment has been revised to require use of one quarter of one percentage point in all cases. Although use of the maximum allowed by contract might be of some value to the consumer in demonstrating the most extreme incremental change possible, it would have the undesirable effect of making a contract which sets limits appear less favorable than one in which the increases are unlimited. The Board believes it is preferable to have all creditors use the same measure and that one quarter of one percentage point is a realistic and manageable amount to use.

(5) In a minor change, § 226.8(b)(8) (ii) was revised to make it clearer that if rate changes can be effected in more than one manner (e.g., by increasing the payment and lengthening the maturity), this fact will be disclosed.

Enclosed is a copy of the amendments to Regulation Z. Questions thereon may be directed to our Consumer Affairs Division (Tel. No. 212-791-5919).

Additional copies of the enclosure will be furnished upon request.

PAUL A. VOLCKER,  
President.



**Board of Governors of the Federal Reserve System**  
**TRUTH IN LENDING**  
**AMENDMENTS TO REGULATION Z**

1. Effective April 11, 1977, paragraph (a) of § 226.6 is amended to read as follows:

**SECTION 226.6—GENERAL  
DISCLOSURE REQUIREMENTS**

**(a) Disclosures; general rule.\*\***

All disclosures required to be given by this Part shall be made in the English language except in the Commonwealth of Puerto Rico where disclosures may be made in the Spanish language with English language disclosures provided upon the customer's request, either in substitution for the Spanish disclosures or as additional information in accordance with § 226.6(c).

2. Effective October 10, 1977, a new subparagraph (8) is added to paragraph (b) of § 226.8 as follows:

**SECTION 226.8—CREDIT OTHER THAN  
OPEN END—SPECIFIC DISCLOSURES**

\* \* \*

**(b) Disclosures in sale and nonsale credit.**

\* \* \*

(8) If the annual percentage rate as disclosed under § 226.8(b)(2) is prospectively subject to increase <sup>10a</sup>, the following additional disclosures shall be made:

(i) the fact that the annual percentage rate is subject to increase and the conditions under which such rate may increase, including: (A) identification of the index, if any, with respect to which such increase in annual percentage rate is tied; and (B) any limitation on such increase;

(ii) the manner(s) (such as an increase in payment amounts, number of scheduled periodic payments, or in the amount due at maturity) in which any increase in the annual percentage rate may be effected;

(iii) if the obligation is repayable in substantially equal instalments at substantially equal intervals (including those obligations providing for "balloon" payments) and the increase could

be effected by an increase in the periodic payment amount, a statement of the estimated increase in the amount of the payment caused by a hypothetical immediate increase of one quarter of one percentage point, based upon the number of scheduled periodic payments and original amount financed disclosed at consummation;

(iv) if the obligation is repayable in substantially equal instalments at substantially equal intervals (including those obligations providing for "balloon" payments) and the increase could be effected by an increase in the number of periodic payments, a statement of the estimated increase in the number of periodic payments caused by a hypothetical immediate increase of one quarter of one percentage point, based upon the periodic payment amount and the original amount financed disclosed at consummation.

Any increase in the annual percentage rate within the conditions or limitations disclosed in accordance with this paragraph is a subsequent occurrence under § 226.6(g) and is not a refinancing under § 226.8(j).

The disclosures required under § 226.8(b)(8)(iii) and (iv) need be made only in transactions in which a security interest is taken in real property used or expected to be used as the customer's dwelling, and they need not be made in transactions primarily for agricultural purposes, transactions in which the obligation is repayable in substantially equal instalments which do not include repayments of principal, or transactions in which disclosures are made pursuant to § 226.814.

<sup>10a</sup> For this purpose, the phrase "prospectively subject to increase" does not apply to increases in the annual percentage rate upon such occurrences as default, acceleration, late payment, assumption or transfer of property.

3. Interpretation § 226.810, previously issued by the Board, is rescinded effective October 10, 1977, inasmuch as the amendment to § 226.8(b) of the Regulation makes this interpretation unnecessary.

For this Regulation to be complete, retain:

1) Regulation Z pamphlet, amended to March 23, 1977.

2) This slip sheet.

(The new Regulation Z pamphlet is currently in process of distribution)

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