

FEDERAL RESERVE BANK
OF NEW YORK

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CREDIT RESTRAINT PROGRAM
Questions and Answers

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

Printed on the following pages is a series of questions and answers regarding (1) Regulation CC (Part 229) of the Board of Governors of the Federal Reserve System (special deposits—consumer credit, money market mutual funds, and nonmember commercial banks), (2) the Special Credit Restraint Program, (3) Marginal Reserves on Managed Liabilities (Regulation D), and (4) Application of Regulation Q to Bank Holding Companies. These questions and answers represent the views of the legal staffs of the Federal Reserve Bank of New York and the Board of Governors of the Federal Reserve System.

Additional questions regarding this material or other matters relating to the Credit Restraint Program may be directed to the following:

Special Credit Restraint Program

Banking Institutions—

- Questions relating to the administration of the Program—Donald E. Schmid, Manager, Bank Analysis Department (Tel. No. 212-791-6611).
- Questions relating to the completion of forms—Nathan Bednarsh, Chief, Bank Analysis Division (Tel. No. 212-791-6710).

Finance companies and selected large corporations—

- Questions relating to the administration of the Program—Eugene P. Emond, Manager, Credit and Discount Department (Tel. No. 212-791-6146).
- Questions relating to the completion of forms—Credit Analysis Division (Tel. Nos. 212-791-6148, 6153 and 6154).
- Legal questions—Raleigh M. Tozer, Senior Attorney, Legal Department (Tel. No. 212-791-5009).

Consumer Credit Restraint Program

- Legal questions—Donald L. Bittker, Assistant Counsel, Legal Department (Tel. No. 212-791-5036).
- All other questions—Tel. Nos. 212-344-1358, 1359, 2258, 2259, 2876, 3858, 3864, 3865, 4117, 4118 and 4119.

Money Market Mutual Funds Program

- Legal questions—Walker F. Todd, Assistant Counsel, Legal Department (Tel. No. 212-791-5041).
- All other questions—Tel. Nos. 212-344-3923 and 3924.

Marginal Reserves/Special Deposits on Managed Liabilities

- Legal questions—Bradley K. Sabel, Assistant Counsel, Legal Department (Tel. No. 212-791-5033).
- All other questions—Thomas J. Campbell, Accounting Officer (Tel. No. 212-791-5262); also Bank Relations Department (Tel. Nos. 212-791-6600 through 6606, 6071 and 6072).

Interest Rate Ceilings on Certain Bank Holding Company Obligations

- Questions relating to the Regulation Q amendment—Bank Relations Department (Tel. No. 212-791-6600 through 6606, 6071 and 6072) or Bank Regulations Division (Tel. No. 212-791-5914).
- Legal questions—Bradley K. Sabel, Assistant Counsel, Legal Department (Tel. No. 212-791-5033).

Surcharge on the Discount Rate

- All questions—Eugene P. Emond, Manager, Credit and Discount Department (Tel. No. 212-791-6146).

Additional copies of this circular will be furnished upon request to the Circulars Division of this Bank.

THOMAS M. TIMLEN,
First Vice President.

Subpart A of Regulation CC -- Special deposits on consumer credit

A-1. Q: Regulation Z, various state laws, and possibly other Federal regulations require a creditor to give a consumer advance notice (the Board's Division of Consumer Affairs has estimated this may range from 15 to 105 days' notice) of adverse changes in the terms of a consumer credit agreement. Many creditors believe that in order to minimize the amount of the special deposit required by the Board's credit restraint regulation they will have to modify the terms of existing credit accounts. Will the Board amend Regulation Z and preempt Federal and State law in order to accelerate the effective dates of modified account terms?

A: The matter will be presented to the Board in the near future for its consideration.

A-2. Q: A supplier of home heating fuels extends credit to its customers purchasing such fuels. Does this constitute covered credit?

A: No. Such credit falls within the exclusion for credit extended by providers of utility services.

A-3. Q: A farmer purchases a large denomination time deposit from a financial institution. During the course of the next year, the farmer borrows funds from the financial institution secured by the time deposit. The purchase of the borrowings is to provide funds for agriculture production, including living expenses of the farmer's family during the production period. Do such borrowings constitute covered credit?

A: Such borrowings would be considered to be for agriculture and business purposes and would not be covered credit.

A-4. Q: A borrower refinances his automobile loan with the original lender. The original loan was not covered credit. Does the refinancing constitute covered credit?

A: Refinancings of exempt credit with the original creditor does not constitute covered credit. However, if additional funds beyond the outstanding balance are provided to the borrower, that additional amount would constitute covered credit. If refinancing is obtained through a creditor other than the original creditor, the entire amount of the refinancing would constitute covered credit.

A-5. Q: To which Federal Reserve Bank should a creditor report if it has offices in more than one Federal Reserve District?

A: The creditor should select one of its offices as its reporting office and should report to the Federal Reserve Bank in the district in which that reporting office is located. At its discretion, a Federal Reserve Bank may instruct the creditor to file reports at a branch office of the Reserve Bank.

A-6. Q: Many creditors believe that in order to minimize the amount of the special deposit they will have to modify the terms of existing credit accounts. Across the board modifications of account terms may have a disparate effect on certain protected classes of borrowers. Will the Board amend or interpret Regulation B to protect a creditor that makes such modifications against allegations of Regulation B violations?

A: This matter is currently under consideration.

A-7. Q: May a creditor reduce the amount of its covered credit outstanding by any bad debt reserves it maintains for that credit?

A: No.

A-8. Q: Covered credit transferred on non-recourse basis is treated as covered credit of the transferee. Many transferors "hold back" a portion of the purchase price as a reserve against losses resulting from possible breach of warranty upon transfer. May the transferee reduce the amount of its covered credit outstanding by the amount of that "hold back"?

A: No.

A-9. Q: Is a retail installment sale in which the seller retains the goods until the final payment is made covered credit?

A: No, because it is secured credit in which the proceeds of the credit are used to purchase the collateral.

A-10. Q: Covered credit transferred on a non-recourse basis is treated as covered credit of the transferee. May the transferee adjust its base in such a case?

A: No, except in the case of certain mergers or consolidations which are explained in Question A-11.

A-11. Q: May a creditor that acquires 100 percent of another creditor's assets through a merger or consolidation adjust its base?

A: Yes, such a creditor may adjust its base as follows: (a) the acquiring creditor may increase its base as of the date of acquisition by adding the actual amount of covered credit the acquiring creditor had on the base date to the actual amount of covered credit the seller had on the base date (for example, a creditor with \$3 million of covered credit outstanding on the base date which acquires a creditor with \$1.5 million of outstanding on the base date will have its base adjusted \$4.5 million); or, (b) if such data are not available, the acquiring creditor may continue to use its pre-acquisition base, or in lieu of that, may select as its new base the selling creditor's base. If the selling creditor is a subsidiary, its former parent must make adjustments in its base if the base of the subsidiary is either assumed by, or added to the base of, the acquiring organization.

A-12. Q: May a creditor adjust its base when it acquires, other than through merger or consolidation, either 100 percent of a certain kind of covered credit (e.g., the credit card operations of a financial institution) or less than 100 percent of all the covered credit of another creditor?

A: No. However, if such sale is with recourse, the covered credit remains that of the selling creditor.

A-13. Q: Many creditors have made second mortgage ("home equity") loans (a) for home improvement, (b) for both home improvement and other purposes, and (c) for purposes unrelated to home improvement. How should a creditor which does not currently categorize by purpose its second mortgage loans calculate the amount of the those loans which are covered in computing its base?

A: If the creditor wishes to include any second mortgage credit in its base, the creditor should take a representative sample of second mortgage loans outstanding on the base date. It should apply the proportion of loans in the sample that fall in categories (b) and

(c) above to the total in its base. Thereafter, the creditor is required to maintain records which adequately document the purposes of the loan, and that portion of multipurpose loans that constitutes covered credit should be reflected in its monthly reports.

A-14. Q: In trying to determine its base of covered credit, a creditor only has records of its outstanding credit categorized by secured and unsecured lending. Does that creditor have to go through all of its individual records on its secured loans to determine which of those loans were extended to purchase the collateral?

A: No. If such a creditor wishes to include any secured credit in its base, the creditor should take a representative sample of its secured credit outstanding on the base date. It should apply the proportion of loans in the sample which were not extended to purchase the collateral to the total amount of secured loans, and should include the resulting amount in its base. Thereafter, the creditor is required to maintain records which adequately document whether the collateral was purchased with the loan proceeds. If the collateral was not purchased with the loan proceeds, such credit should be reflected in its monthly reports.

A-15. Q: If a creditor extends credit that is secured by collateral purchased from the loan proceeds but whose value is less than the total amount of the loan (for example, an automobile loan for \$5,000 where the price of the automobile is \$4,000), how should the loan be treated?

A: If a creditor wishes to include in its base any portion of such credit, the creditor should take a representative sample of its secured loans outstanding on the base date. It should apply the proportion of loans in the sample which are partially secured by the collateral purchased to the total amount of loans and should include the resulting amount in its base. Thereafter, the creditor is required to maintain records which adequately document the purposes of the loan, and that portion of secured loans that constitutes covered credit should be reflected in its monthly reports.

A-16. Q: Will the Board of Governors revise the program to permit, instead of a special deposit, a reduction in consumer lending?

- A: No. When a creditor's covered credit is reduced, the amount of the special deposit is reduced.
- A-17. Q: Are commitments to make consumer loans "covered credit"?
- A: No. Loans only include credit outstanding.
- A-18. Q: Is the purchase of a government security by a bank from a consumer a "covered credit"? Section 202(h) of the Credit Control Act defines "extension of credit" as including the supplying of funds through the acquisition of securities.
- A: No.
- A-19. Q: If a retailer opens a new store, will it receive a higher base?
- A: No. Covered credit extended by the new store must be added with the retailer's other covered credit.
- A-20. Q: Prior to the base date, a covered creditor has sold a portion of its consumer loan portfolio on a without recourse basis. Is the amount of that credit "covered credit" of the seller?
- A: No. Covered credit sold on a non-recourse basis on or before March 14 should not be included in the seller's base but is included in the covered credit of the buyer.
- A-21. Q: A law firm does personal legal work for clients and issues bills periodically. Is covered credit extended while the work is being done? Is covered credit extended from the period that the bill is issued until it is paid by the client?
- A: Covered credit is extended when the bill is issued, so long as the creditor bills on a regular basis.
- A-22. Q: A foreign company has two United States subsidiaries which are covered creditors. May the two subsidiaries file separate reports and maintain separate special deposits?
- A: No. As provided in Section 229.2(g) of Subpart A of the regulation the foreign company and its two subsidiaries constitute one covered creditor.

A-23. Q: Is a holding company and all its subsidiaries a single covered creditor for the purpose of filing reports and maintaining special deposits?

A: A holding company and its majority-owned subsidiaries should file one report and maintain one deposit account.

A-24. Q: When is credit-card credit extended for purposes of deciding on the outstanding amount?

A: Credit-card credit is to be considered extended and outstanding when it is charged to the account of the customer to whom the credit card is issued.

A-25. Q: The Board's press release states that "credit extended for utilities, health or educational services" is not covered. This clearly exempts all credit extended for such services, regardless of who extends the credit. On the other hand, the regulation states that "covered credit does not include . . . credit extended by . . . providers of utility, health, or educational services," limiting the exemption to credit extended by providers of such services. Which is correct?

A: The regulation is correct. The exemption is limited to credit extended by providers of utility, health, or education services. Note, however, that credit extended under State or Federal Government guaranteed loan programs, such as student loans, is also exempt.

Subpart C of Regulation CC and Regulation D -- Marginal reserves/
special deposits on managed liabilities

C-1. Q: For purposes of determining the amount of reduction in an institution's managed liabilities base, are the assets of a bank's foreign branches representing loans to non-United States residents and balances due from foreign offices of other institutions taken into account in such computation?

A: No. A member bank's base will be reduced only by the greater of 7 percent of its managed liabilities base (as determined for the base period September 13-26, 1979) or the reduction in its domestic office loans to non-United States residents and gross balances due from foreign offices of other institutions or the time deposits of which are exempt from the rate limitations of Regulation Q pursuant to Section 217.3(g). In the future, after March 19, a bank's base will be further reduced by decreases in such domestic office loans and balances.

Special Credit Restraint Program

S-1. Q: Does the Special Credit Restraint Program apply to sales of Federal funds?

A: No.

S-2. Q: Are loans to non-United States residents covered by guidelines under the Special Credit Restraint Program?

A: Loans by domestic or foreign offices to non-United States residents are not covered. However, excessive growth in such loans may have an undesirable effect on the liquidity and capital assets of the bank. Banks making such loans should ensure, to the extent possible, that the proceeds are used outside the United States.

Regulation Q -- Interest rate ceilings on certain bank holding company obligations

Q-1. Q: Are the interest rate ceilings applicable to those bank holding company obligations that were issued prior to March 14, 1980, the effective date of the amendment?

A: No.