FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 9627
January 26, 1984]

ELECTRONIC FUND TRANSFERS

TRUTH IN LENDING

Proposed Amendments to Regulations E and Z and the Official Staff Commentaries

To All Depository Institutions, and Others Concerned,
in the Second Federal Reserve District:

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

The Federal Reserve Board has issued for public comment proposals affecting the use of credit cards under its Regulation Z (Truth in Lending) and of debit cards under its Regulation E (Electronic Fund Transfers).

The Board requested comment by February 24, 1984.

The Board proposed to amend Regulation Z to clarify that *all* credit cards are covered by rules in the regulation concerning the issuing of credit cards and the limits of cardholder liability for unauthorized charges.

The proposal would affect credit cards issued for use in extensions of credit by registered brokers and dealers; certain extensions of credit of more than $25,000; and for extensions of credit extended for public utility services. Such extensions of credit are generally exempt from the provisions of Regulation Z. The proposed amendment would not affect the application of these exemptions to other provisions of Regulation Z.

The proposal would make it clear that these exemptions do not extend to the credit card provisions of Regulation Z (1) prohibiting the unsolicited issuance of credit cards and (2) limiting consumer liability for the unauthorized use of credit cards to a maximum of $50.

Questions have arisen about the applicability of these two credit card rules, due to changes in the structure of the telephone industry and the issuance of millions of telephone credit cards in recent years, as well as the fact that many paper telephone cards will soon be replaced by plastic cards that function much like retail credit cards.

Under Regulation E the Board is publishing for comment proposals (1) to expand consumer protection by covering debit card transactions that are processed electronically but do not go through an electronic terminal at the point of sale (such as the case in which a debit card is used to imprint a sales slip), and (2) to allow more flexibility in the disclosure of charges for electronic fund transfers on periodic statements.

A debit card is one allowing consumers to charge a purchase of goods or services directly to their checking or other transaction accounts (as distinguished from the use of a credit card, which results in the promise by a customer to pay for a purchase at some future time).

Debit cards may be used at point-of-sale electronic terminals, which send the information to the consumer's financial institution by electronic means. Such transactions are subject to the rules of Regulation E concerning disclosure of charges, losses resulting from unauthorized use of debit cards and resolution of errors. However, questions have arisen whether

(OVER)

these rules apply if an electronic terminal is not involved, and the charge information is not immediately sent electronically, but is converted to electronic form in two steps: (1) the sales slip on which the debit card has been imprinted is sent to the merchant's financial institution and (2) the charge information is there converted to electronic form for debiting the consumer's account.

The proposed amendment would clarify that the fund transfers resulting from such two-step processing — which is the most common way point-of-sale debit card transactions are handled — are subject to the same rules as one-step transactions (where the charge is sent electronically from the place where the sale is made).

The other proposed amendment makes a technical change that would permit financial institutions that issue debit cards to itemize EFT charges on a periodic statement of account on a transaction-by-transaction basis, rather than to show a total. Institutions could use either method.

The Board's notices in these matters may be obtained from the Federal Reserve Banks. The notices include a proposed update to the official staff commentary on Regulation E, and a proposed revision of Regulation Z dealing with the applicability of the regulation to certain extensions of securities credit made by registered brokers and dealers.

Enclosed — for depository institutions in the Second Federal Reserve District — is the text of the Board's proposals, which have been reprinted from the *Federal Register* of January 18, 1984; it will be provided to others upon request directed to the Circulars Division of this Bank (Tel. No. 212-791-5216).

Comments on these proposals should be submitted by February 24, 1984, and may be sent to our Regulations Division.

ANTHONY M. SOLOMON,
President.

federal register

Wednesday
January 18, 1984

Part III

Federal Reserve System

12 CFR Part 205

Electronic Fund Transfers; Proposed Rule and Proposed Update to Official Staff Commentary

12 CFR Part 226

Truth in Lending; Credit Cards; Issuance and Liability; Proposed Rule

12 CFR Part 226

Truth in Lending; Official Staff Commentary Revision; Proposed Rule

[Enc. Cir. No. 9627]

FEDERAL RESERVE SYSTEM

12 CFR Part 205

[Reg. E; Docket No. R-0502]

Electronic Fund Transfers; Proposed Rule and Proposed Update to Official Staff Commentary

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule and proposed update to official staff commentary.

SUMMARY: The Board is publishing for comment proposed amendments to Regulation E. The proposals would amend the regulation (1) to cover, within the definition of electronic fund transfer, transfers resulting from debit card transactions that are processed electronically but do not involve an electronic terminal at point of sale, and extend the time periods for error resolution with respect to these transfers; and (2) to provide more flexibility for the disclosure of charges for electronic fund transfers on periodic statements. The notice also contains a number of proposed changes to the official staff commentary.

DATE: Comments must be received on or before February 24, 1984.

ADDRESS: Comments may be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, or delivered to the C Street entrance, 20th and C Streets NW., Washington, D.C., between 8:45 a.m. and 5:15 p.m. weekdays. Comments may be inspected in Room B-1122 between 8:45 a.m. and 5:15 p.m. weekdays. All material submitted should refer to Docket No. R-0502.

FOR FURTHER INFORMATION CONTACT: Regarding the regulation and commentary, contact: Gerald P. Hurst (Staff Attorney), Jesse B. Filkins (Senior Attorney), or John C. Wood (Senior Attorney), Division of Cosumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, (202) 452-3667 or (202) 452-2412. Regarding the economic impact analysis, contact: Frederick J. Schroeder, staff economist, Division of Research and Statistics, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, (202) 452-2584.

SUPPLEMENTARY INFORMATION:

1. General

The Electronic Fund Transfer Act (15 U.S.C. 1693 *et seq.*) governs any transfer of funds that is electronically initiated and that debits or credits a consumer's account. This statute is implemented by the Board's Regulation E (12 CFR Part 205). The Board is proposing an amendment to the regulation to cover transfers resulting from debit card transactions at the point of sale that do not involve electronic terminals but that are processed electronically. The Board believes that coverage of these transfers is necessary in order to effectuate the primary purpose of the Electronic Fund Transfer (EFT) Act—the providing of individual consumer rights with respect to electronic fund transfers. The Board is also publishing a proposed amendment to provide more flexibility in the disclosure of electronic fund transfer charges on periodic statements, by allowing disclosure of these charges as a total amount or on a transaction-by-transaction basis.

The comment period ends on February 24. Comments must be received on or before that date to ensure consideration. The Board believes that prompt resolution of these matters is essential and in the public interest to provide necessary clarification regarding the scope of the EFT Act's coverage.

2. Transfers Resulting From Point-of-Sale Transactions

The Electronic Fund Transfer Act defines an electronic fund transfer (EFT) as:

> Any transfer of funds, other than a transaction originated by check, draft, or similar paper instrument, which is initiated through an electronic terminal, telephonic instrument, or computer or magnetic tape so as to order, instruct, or authorize a financial institution to debit or credit an account.

The act and regulation include specific examples of transfers that are EFTs, such as automated teller machine transactions and direct deposits, but the coverage is not narrowly defined nor is it limited to the examples given.

There has been some uncertainty about whether the act and regulation cover transfers resulting from transactions that involve the use of a debit card for the purchase of goods or services, but do not involve an electronic terminal. Because the debit card is used to create a sales slip, either by the use of an imprinter or by having the account or card number entered into the cash register, these transactions are often referred to as paper-based point-of-sale (POS) transactions. The vast majority of the debit cards used in this way are issued by financial institutions participating in the Visa and MasterCard systems.

The debit card functions in a fashion that is virtually identical to a credit card; this is true not only of procedures at the point of sale, but also of procedures during processing. With a credit card, however, the consumer is billed for transactions, while in a debit card transaction a transfer is made from the consumer's asset account.

All transactions resulting from use of debit cards involve sales slips, even transactions at a merchant with terminals or cash registers that electronically capture the transaction information. The presence of the sales slip has caused many institutions to regard the transfers resulting from these transactions as paper-based rather than electronic, and has created uncertainty within the industry as to whether the transfers are EFTs covered by the act and Regulation E. Some institutions treat the transfers as covered while other institutions' disclosures indicate that only transfers resulting from transactions made by use of the card at electronic terminals are covered.

The fact that many financial institutions view the transfers resulting from these POS transactions as not covered by Regulation E leaves the rights and responsibilities of a considerable number of consumers subject only to their contracts with the individual financial institutions. The absence of coverage by the act could be particularly troublesome for consumers who are under the impression that they have protections that do not exist under agreements with their financial institutions. Two factors may lead consumers to believe they are protected by federal law, either the Truth in Lending Act or the Electronic Fund Transfer Act: (1) The similarities between the debit card and credit card, both in appearance and function; and (2) the lack of consumer understanding of possible legal distinctions when the same debit card is used in a POS transaction that involves electronic data capture at the point of sale, and in one that does not.

While the Board is not aware of consumer problems resulting from the uncertainty about coverage, there have been numerous inquiries from financial institutions and concern has been expressed by consumer representatives and other agencies about the applicability of the act and Regulation E to these POS transactions.

In addition, as a policy matter it is important to consider congressional purpose. In passing the EFT Act, Congress intended to define the rights and liabilities of consumers, financial institutions, and intermediaries in the developing systems involving EFTs—primarily by establishing individual consumer rights, such as limited liability

for unauthorized use and the right to prompt resolution of errors. The Board believes that, in order to effectuate this congressional purpose, Regulation E should be amended to cover transfers resulting from these POS transactions.

The Board believes it is important that the coverage issue be resolved at this time because the number of debit cards being used in POS transactions is increasing. According to industry information, at the end of 1978 approximately 400,000 accounts with 590,000 cardholders were accessible by debit cards.[1] By the end of 1982, there were more than 3 million accounts with almost 4½ million cardholders. By the end of 1983, the number of debit cardholders was expected to exceed 6 million. There has also been an increase in the number and dollar volume of transactions made with these cards. Figures from industry sources indicate that approximately 50 million transactions with a value of approximately $2.4 billion were made at the point of sale in the past year. It is estimated that more than 90 percent of these transactions at the point of sale did not involve electronic data capture at the time of the transaction.

Electronic Initiation

An EFT is generally defined in terms of a transfer that is initiated electronically. In the case of POS transactions, the majority result in truncation of the sales slip at the merchant's financial institution. The instructions to debit the consumer's asset account are converted into an electronic form, usually magnetic tape, at that point. Once truncation occurs, the processing involves electronics and culminates in the electronic debiting of funds from the consumer's account at the account-holding institution.

When a consumer uses an automated teller machine (ATM) owned or operated by the account-holding financial institution, fund transfers are made directly from the consumer's account. In POS transactions, several steps are often involved before a fund transfer is made from a consumer's account. In such cases, one could focus on any one of these steps to determine how or when the transfer of funds from the consumer's account is "initiated." For example, one could focus on the point at which the card is run through the imprinter, the point when the data on the sales slip is converted to an electronic form and transmitted to the account-holding institution, or the point at which the account-holding institution actually receives the order or instruction to debit the consumer's asset account. The Board believes that specifying the first step in the POS transaction as determinative of the initiation issue would result in a narrow reading of the Act's coverage, and would significantly undermine the purposes of the Act.

Congress clearly intended to include within coverage of the act fund transfers resulting from the use of new instruments referred to as debit cards when it described the covered transfers generally as being initiated electronically. The transfers resulting from POS transactions are as much the result of the use of a debit card as are transfers with debits cards at ATM's or at electronic terminals at points of sale. The Board believes that whether these fund transfers are covered does not depend on whether there is an electronic terminal at the point of sale, but on whether there is electronic ordering, instructing, or authorizing involved in the debiting or crediting of a consumer asset account. Most of the fund transfers resulting from POS transactions involve electronic ordering, instructing, or authorizing, and thus are EFTs for purposes of coverage.

In some instances, the merchant's financial institution may be the same as the consumer's account-holding institution. It can be argued that in these POS transactions the funds transfer from the consumer's account does not involve electronic initiation, and thus should not be covered by the act. Excluding them from coverage, however, would result in continued uncertainty as to the protections available to consumers in this narrow class of transactions. Moreover, it does not seem equitable or rational to determine consumer rights based upon whether an account relationship exists with a particular institution. Consequently, the Board is seeking comment on whether it should cover *all* fund transfers resulting from point-of-sale debit card transactions.

"Similar Paper Instrument" Exclusion

The EFT definition in the act excludes transactions "originated by check, draft, or similar paper instrument." The Board believes that this exclusion is not applicable to the fund transfers that result from POS transactions because the transactions arguably are originated with the card (or the card in combination with the sales slip), not by the sales slip alone. More importantly, although the transaction involves a paper sales slip, that sales slip is not a paper instrument that is "similar" to a check or a draft.

The exclusion from the act's coverage for transactions originated by "check, draft, or similar paper instrument" was directed at excluding check truncation systems, in light of the potentially broad coverage of the EFT definition. The word "similar" has special significance related to negotiability. Checks and drafts are negotiable instruments under the Uniform Commercial Code (UCC) and are subject to its provisions; the sales slip used in POS transactions are not negotiable instruments, because they are not conditional and are not payable to order or bearer.

The sales slip clearly play a part in effectuating transactions in the debit card payment system and, in that sense, they function in much the same way that checks do in a check truncation payment system. However, there is a significant difference—again related to negotiability. The check payment system is governed by Article 3 and 4 of the UCC. The rules for sales slip transactions, on the other hand, are in many respects unclear. Because sales slips are not negotiable instruments, Article 3 does not apply. Article 4 applies to both negotiable and non-negotiable instruments, but even these rules may not apply with respect to sales slips, because financial institutions may insert provisions in their agreements with consumers that alter the UCC rules.

In the absence of uniform rules that establish the rights and responsibilities for all parties to these transactions, the Board believes that a sales slip cannot and should not be viewed as a "similar paper instrument" just because it functions in the payments world somewhat like a check.

Board's Authority for Defining Coverage

The Board is given broad rulewriting authority under the EFT Act—authority that was viewed by the Congress as essential to the act's effectiveness. The scope of the act's coverage is an area where it appears that Congress particularly wanted the Board to have flexibility and to exercise its rulewriting authority. For example, the act expressly provides that if EFT services are made available to consumers by a person other than a financial institution holding a consumer's account, "the Board shall by regulation assure that the disclosures, protections, responsibilities, and remedies" created by the EFT Act

[1] The reference to debit cards and the numbers given for accounts, cardholders, and transactions refers only to the debit cards that have been issued for use for POS transactions. There are millions of debit cards that have been issued by financial institutions for use in automated teller machines. These ATM cards and the transfers resulting from their use are clearly covered by Regulations E.

are made applicable to such persons and services.

The EFT Act gives the Board broad authority to prescribe regulations that will carry out the purposes of the act, and to deal with questions regarding coverage. (In exercising this authority, the Board has in some cases refined the act's coverage—for example, by excluding intrainstitutional electronic fund transfers and by defining coverage of telephone-initiated EFTs as being limited to transfers made under a written agreement.) The Senate reports accompanying Senate bills S. 3156 and S. 3499 (S. Rep. No. 915, 95th Cong., 1st Sess. 9, and S. Rep. No. 1273, 95th Cong., 1st Sess. 25 and 26) state that:

> The definition of "electronic fund transfer" is intended to give the Federal Reserve Board flexibility in determining whether new or developing electronic services should be covered by the act and, if so, to what extent. . . . Whether [a] service should be covered by the act requires a determination of whether such transfers will be initiated electronically, whether current laws provide adequate consumer safeguards, and whether coverage is necessary to achieve the act's basic objectives. This delegation of authority to the Board is an important aspect of this legislation as it would enable the Board to examine new services on a case-by-case basis and would contribute substantially to the act's overall effectiveness.

The first—whether the fund transfers are initiated electronically—has been discussed above. In summary, it is the Board's view that while the *purchase transaction* may not result in simultaneous data capture for electronic transmittal to the account-holding institution, the *transaction information* necessary to make the fund transfer is convered to electronics and is transmitted electronically to the account-holding institution. Thus the transfer is deemed to have been initiated electronically.

The other two issues mentioned in the Senate reports—whether other laws provide adequate consumer protections and whether coverage is necessary to achieve the act's objectives—are both questions that relate to the policy considerations underlying the act.

As noted above, approximately nine out of every ten POS transactions using debit cards are made at non-electronic terminals. There appears to be little or no consumer protection offered by state laws or other federal laws in regard to these POS transactions. If these POS transactions are not covered by Regulation E, important safeguards will be lacking. For example, a consumer could be subject to unlimited liability for the unauthorized use of a lost or stolen debit card, and the rights and responsibilities of the parties in the resolution of errors would be undefined. In light of the lack of safeguards, coverage by Regulation E is necessary to achieve the basic objectives of the EFT Act—that is, to establish the rights and responsibilities of the parties to the transfers and, as the primary objective, to provide for individual consumer rights.

In summary, the Board believes that:

- The definition of an EFT encompasses all transfers of funds that are initiated electronically. When the instructions contained on a sales slip are converted to and transmitted in an electronic form, the financial institution holding the consumer asset account unquestionably is ordered, authorized, or instructed to debit the consumer's account by electronic means. As a result, the transfer of funds resulting from these POS debit card transactions are initiated electronically and the resulting transfers are EFTs.
- Neither the POS transactions nor the fund transfers are excluded from the definition of an electronic fund transfer. Even though there is an exclusion for "transaction[s] originated by check, draft, or similar paper instrument," the Board believes this exclusion is limited to negotiable instruments and for that reason does not apply to POS debit card transactions.
- The broad authority given to the Board to carry out the purposes of the act supports coverage so as to ensure that the purpose of the act is effectuated—that is, that the rights and responsibilities of all the parties to the transfers are established.

The Board therefore proposes amending Regulation E to cover transfers resulting from these POS transactions.

The Board requests specific comment on whether the regulation should be amended to cover *all* transfers resulting from point-of-sale debit card transactions, including those transfers resulting from transactions where the merchant's financial institution is the same as the account-holding institution. This would avoid the possibility of continued uncertainty as to the consumer protections for those transactions.

Extension of Periods for Error Resolution

Many financial institutions are already complying with the regulation for certain transactions because (1) the debit cards are capable of being used at merchant terminals or cash registers that capture data electronically; and (2) many of the debit cards that have been issued for POS transactions are also capable of being used for transactions at ATMs. However, some institutions will probably have to make changes in their programs, including the giving of new or corrected disclosures, in order to comply with Regulation E coverage.

The Board has considered the extent of the compliance burden that might result from coverage of these POS transactions by Regulation E. Some of the regulatory requirements would not apply to those transfers, and hence represent no compliance problem. For example, unless they capture data electronically, the sales registers at point of sale are not *electronic terminals* for purposes of the regulation, even though the transfers are characterized as *electronic fund transfers*. Thus the requirement that terminal receipts be given would not apply. Similarly, in the absence of an electronic terminal, the periodic statement need not include a terminal location—a disclosure that would otherwise be required and that, if applicable, might represent a significant problem.

One regulatory provision that appears to require an adjustment is error resolution, specifically with regard to the time limits for resolution of an error. Regulation E permits the financial institution to take up to 45 calendar days to resolve an error, but requires in such cases that the financial institution provisionally recredit the consumer's account by the tenth business day. When an error is alleged, it is often necessary to obtain documentation of the transaction in order to verify the date, amount, etc. of the transaction. Obtaining documentation, usually in the form of a copy of the sales slip, often takes longer than 10 business days. The time limits are of particular concern to securities firms that offer access to consumers' asset management accounts by means of debit cards. These firms encounter delays in obtaining copies of sales slips because they usually are not dealing directly with the financial institutions that truncated the sales slips, but are working through the financial institution that issued the debit cards on the firm's behalf.

Note.—The act and regulation contain an exemption for certain securities-related transfers, but that exemption is limited to transfers the *primary purpose* of which is the purchase or sale of securities. Transfers resulting from a consumer's use of a debit card to purchase goods or services are not excluded from coverage even though securities may be redeemed as a result of the transaction.

To facilitate compliance, the Board proposes to amend the regulation to allow 20 business days for the resolution of error allegations related to these POS transfers prior to requiring that the financial institution provisionally recredit the consumer's account, and to allow the financial institution up to 90 days for ultimate resolution of these

errors. These extended time periods are the same as those that the Board approved for resolution of errors involving EFTs that are initiated in a foreign country. The Board believes that this modification would minimize the potential compliance burden to financial institutions without resulting in a significant reduction in consumer protection.

In order to further minimize the effect of covering these transfers, the Board also proposes that the requirements of the regulation applicable to these transfers have a delayed effective date of six months from the date of final action by the Board—except for the limitations on unsolicited issuance and consumer liability for unauthorized transfers, which would take effect upon adoption of the amendment. This would provide financial institutions with lead time for changes that may be necessary to comply with requirements such as error resolution procedures and the furnishing of new corrected disclosures.

The board requests comment as to the effects of these proposed amendments (including cost information), whether the proposed extension of the time periods for error resolution is necessary in order to facilitate industry compliance, and whether extending those time periods would have an adverse impact on consumers.

3. Disclosure of EFT Charges

Regulation E currently requires that the periodic statement disclose, as a total sum, all charges assessed against the account during the statement period for electronic fund transfers or for the right to make such transfers, or for account maintenance. Some financial institutions would like to itemize EFT charges on a transaction-by-transaction basis, rather than disclose a total charge. The Board believes that disclosure of EFT charges on a transaction-by-transaction basis is likely to be at least as informative to the consumer as the disclosure of a total figure. The Board therefore proposes an amendment to the regulation that would permit disclosure of charges on an itemized basis. Disclosure of a total amount would continue to be permitted as an alternative, at the institution's option.

4. Economic Impact Analysis

While representing only a small share of all transactions by consumers at point of sale, paper-based debit transactions have grown substantially in number since enactment of the Electronic Fund Transfer Act. The proposed extension of Regulation E coverage to these transactions would provide benefit through the definition of rights and responsibilities of parties involved in these transactions. The costs of implementing and complying with the proposed amendments are not expected to be great for three reasons:

While all financial institutions will have to familiarize themselves with the proposed rules changes, relatively few institutions currently issue debit cards and will have to comply. Regulation E applies only to financial institutions, defined to include (1) depository institutions and any other person who, directly or indirectly, holds an EFT-accessibly account belonging to a consumer; and (2) any person who issues an EFT access device and agrees with a consumer to provide EFT services. The proposed amendments will primarily affect only the relatively few financial institutions not already covered by Regulation E and offering point-of-sale debit cards that can be used in transactions that may not involve electronic terminals. The impact of the proposed amendments is expected to be small because of the relatively narrow class of affected institutions and because most issuers of POS debit cards provide other EFT services to consumers. For these reasons, these institutions will already have established the compliance procedures required by the proposed amendments.

The large credit and debit card associations are expected to help streamline compliance for most affected institutions. It is anticipated that most of the issuers affected will belong to the major credit card associations. While a significant and growing number of transactions will be covered, the issuers and their associations have well-established systems and methods in place for resolving errors, providing documentation, and otherwise controlling credit card transactions. The amendments as proposed are unlikely to impose a significant additional burden on these systems.

Additional information about the number and type of entities, particularly small entities, likely to experience a significant cost or operational impact from the proposed amendments would be useful.

The terminal receipt requirements would not apply and an extension of error resolution procedure time limits would minimize the impact of the proposed amendments. An important feature of the proposed amendments is the absence of any terminal receipt requirements. Because the terminals involved in paper-based debit card transactions are not electronic terminals for purposes of the act and regulation, no documentation at POS is required by the regulation. In any case, the consumer would normally receive some form of documentation. Furthermore, because there is no required terminal receipt, there is no obligation to conform the information in periodic statements with the information on POS receipts. Periodic statements must identify third parties to whom funds were transferred by EFT, but this information would appear in any case as the merchant identification for each transaction.

The proposed amendments also extend the time periods allowed for error resolution. The modification would allow 20 business days for error resolution before the provisional recrediting provisions of Regulation E take effect, with a maximum of 90 days for error resolution. The existing regulation allows 10 business days and 45 days, respectively, for error resolution, except that 20 business days and 90 days, respectively are allowed for error resolution with respect to EFTs initiated in foreign countries. In preliminary discussions, industry representatives have indicated that the proposed time limits appear adequate for resolving most errors. These provisions eliminate some of the potentially most costly requirements of the regulation, without significantly reducing the consumer protections intended by the act.

In summary, the compliance requirements of the proposals are not expected be very burdensome. Nonetheless, most financial institutions are likely to incur some cost associated with familiarizing themselves with and interpreting these amendments to determine whether the specific provisions apply. Those institutions to which the amendments apply will have to incur the costs of revising operating manuals and procedures. The assistance that the large credit and debit card organizations provide to their members is expected to streamline compliance for most institutions and minimize the burden of compliance requirements.

Information on problems that might arise for institutions in attempting to comply with the proposed amendments would be useful. Also, information on the impact of the compliance requirements for small entities is particularly solicited.

Section 904(a)(2) of the EFT Act requires the Board to prepare an analysis of the economic impact of any regulations under the act. In addition, section 603 of the Regulatory Flexibility Act (5 U.S.C. 603) requires that proposed regulations be accompanied by an initial regulatory flexibility analysis. The

foregoing analysis satisfies both of these requirements.

5. Update to staff commentary

The Board is also publishing for comment an update to the official staff commentary, interpreting Regulation E (EFT–2, Supp. II to 12 CFR Part 205). This represents the second periodic update; the first was published on April 6, 1983 (48 FR 14880).

The questions that have been added are self-explanatory, and respond to inquiries received by the staff. Question 2–21.5 and the proposed revision to question 2–24 are contingent on the Board's adoption in final form of the proposed regulatory amendment covering point-of-sale transactions, discussed above. Question 3–3.5 codifies a longstanding position, first presented in a Federal Register notice of May 3, 1979 (44 FR 25850). Question 6–6.5 regarding consumer negligence addresses a question that has arisen from time to time and reflects the Board's longstanding position, which is based on the statutory provisions and legislative history of the act.

Questions 5–1.5 and 7–5.5 address the addition of new accounts. The positions taken in questions 7–15.5 and 9–31.5 parallel interpretations under the Regulation Z commentary (Supp. I to CFR Part 226), and address questions that have arisen in the context of developing interchange systems, as do questions 7–6.5 and 9–40.5. Revised question 9–31 would implement the Board's proposed change to § 205.9(b)(3), discussed above. Two questions deal with preauthorized debits. Question 10–18.5 is new. Question 10–19 contains a proposed modification to the current interpretation, in response to requests for further guidance from representatives of automated clearing houses. Finally, question 12–1 revises the position currently stated in the commentary, which may be misleading regarding the preemptive effect of federal law.

List of Subjects in 12 CFR Part 205

Banks, banking, Consumer protection, Electronic fund transfers, Federal Reserve System, Penalties.

Regulatory Text

PART 205—[AMENDED]

Certain conventions have been used to highlight the proposed revisions. New language is shown inside bold-faced arrows, while language that would be deleted is set off with brackets. Pursuant to the authority granted in section 904 of the Electronic Fund Transfer Act, 15 U.S.C. 1693b, the Board proposes to amend Regulation E, 12 CFR Part 205, by revising §§ 205.2(g), 205.9(b)(3), and 205.11(c)(4), as follows:

§ 205.2 Definitions and rules of construction.

* * * * *

(g) "Electronic fund transfer" means any transfer of funds, other than a transaction originated by check, draft, or similar paper instrument, that is initiated through an electronic terminal, telephone, or computer or magnetic tape for the purpose of ordering, instructing, or authorizing a financial institution to debit or credit an account. The term includes, but is not limited to, point-of-sale transfers, automated teller machine transfers, direct deposits or withdrawals of funds, and transfers initiated by telephone. ►It includes transfers resulting from point-of-sale transactions that do not involve an electronic terminal but do involve the conversion of transaction information into an electronic form for transmission to the account-holding institution.◄ The term does not include payments made by check, draft, or similar paper instrument at an electronic terminal.

* * * * *

§ 205.9 Documentation of transfers.

* * * * *

(b) *Periodic statements.* * * *

(3) The [total] amount of any fees or charges, other than a finance charge under 12 CFR 226.7(f), assessed against the account during the statement period for electronic fund transfers or the right to make such transfers, or for account maintenance.

* * * * *

§ 205.11 Procedures for resolving errors.

* * * * *

(c) *Investigation of errors.* * * *

(4) If a notice of an error involves an electronic fund transfer that was not initiated in a state as defined in § 205.2(k), ►or involves an electronic fund transfer resulting from a point-of-sale transaction that did not involve an electronic terminal,◄ the applicable time periods for action in paragraphs (c), (e), and (f) of this section shall be 20 business days in place of 10 business days, and 90 calendar days in place of 45 calendar days.

* * * * *

7. Text of Proposed Commentary Revision

Conventions used above to highlight the proposed regulatory changes (bold-faced arrows and brackets) have also been used to highlight the proposed changes to the commentary. The proposed revision to the Official Staff Commentary on Regulation E (EFT–2, Supp. II to 12 CFR Part 205) reads as follows:

Supplement II—Official Staff Interpretations

Section 205.2—Definitions and rules of construction.

* * * * *

►Q2–21.5: *Fund transfer—POS transaction.* A consumer uses a debit card at point of sale (POS) to purchase goods or services. The card is used to generate a sales slip that is later truncated. The payment data is converted to electronic form for transmittal to the account-holding institution, where the consumer's asset account is debited for the amount of the transaction. Is this transfer subject to the regulation?

A: Yes. the definition of "electronic fund transfer" covers transfers of this type even when no electronic terminal is involved since the account-holding institution is ordered, instructed, or authorized to debit the consumer's account by electronic means. However, because no electronic terminal is involved, a terminal receipt is not required and the periodic statement need not disclose teminal location. (§§ 205.2(g), and 205.9(a) and (b)(1)(iv))◄

* * * * *

Q2–24: *Point-of-sale terminals.* Does the regulation cover POS [transfers] ►transactions◄ in which the consumer presents an access device, ►such as a debit card,◄ and does the terminal receipt requirement apply?

A: The regulation applies to transfers [initiated at point-of-sale terminals] ►resulting from point-of-sale debit card transactions whether or not an electronic terminal is involved, if the payment data is transmitted in electronic form; but terminal receipts are required only if there is an electronic terminal. Point-of-sale terminals are electronic terminals for purposes of the regulation◄ if they capture data electronically, for debiting or crediting to the consumer's asset account, using the consumer's access device—for example, when the consumer's personal identification number is required, in part, to activate the terminal. [Terminal receipts would be required in such cases.] ►(See question 2–21.5.)◄ (§ 205.2(h))

* * * * *

Section 205.3—Exemptions.

* * * * *

►Q3–3.5: *Securities exemption—asset management accounts.* Some consumer financial services include both an electronic fund transfer service and the purchase and sale of securities. An example is a program involving a debit card issued by a bank or other card issuer, which the consumer uses to purchase goods or services, and a money market mutual fund held with a broker. Debits are processed by the card issuer and transmitted via electronic means to the broker for payment from the money market mutual fund. Are such transfers exempt from the regulation under the securities exemption?

A: No. The regulation exempts only transfers whose "primary purpose" is the purchase or sale of securities—for example, a telephone order to a stockbroker to buy or sell securities. In the case of POS transactions, the purchase or sale of securities is not the primary purpose of the transfers. Rather, the primary purpose of the use of the card and the resulting transfer is, for example, to purchase goods or services or to obtain cash, and redemption of securities is incidental thereto. (§ 205.3(c))◄

* * * * *

Section 205.5—Issuance of Access Devices.

* * * * *

►Q5–1.5: *Issuance—addition of new accounts.* A consumer has been issued an access device for accessing an asset account. The account-holding institution wants to make an additionl account accessible to the consumer by means of the same access device. May the institution do so without a request by the consumer?

A: No. Making an additional account accessible through an existing access device is equivalent to issuing an access device for that account. Such issuance is subject to the unsolicited issuance provisions. (Additional disclosures may be required in some circumstances. See question 7–5.5.) (§ 205.5 (a)(1))◄

* * * * *

Section 205.6—Liability of Consumer for Unauthorized Transfers.

* * * * *

Q6–6.5: *Consumer negligence.* A consumer writes the PIN on a piece of paper and keeps it with the ATM card, or writes it on the card itself—actions that may constitute negligence under state law. Do such actions affect the liability for unauthorized transfers that may be imposed on the consumer?

A: No. Negligence on the consumer's part is not a factor in determining liability under the act and Regulation E. The extent of the consumer's liability is determined by the promptness in reporting loss or theft of an access device or unauthorized transfers appearing on a periodic statement. (§ 205.6(b))

* * * * *

Section 205.7—Initial Disclosure of Terms and Conditions.

Q7–5.5: *Addition of new accounts.* A consumer arranges for electronic fund transfers to and from an account, and receives disclosures. Later, the consumer arranges for transfers involving an additional account at the same financial institution. Does the addition of the new account require further disclosures?

A: The addition of a new account would require the institution to furnish any of the required disclosures that differ from those previously given. (See questions 5–1.5 and 7–6.) (§ 205.7(a))

* * * * *

Q7–6.5: *Addition of service—in interchange system.* A financial institution operates electronic terminals through which consumers can access their accounts, and gives the required disclosures regarding the service. Later, the institution joins an interchange or shared system of terminals, giving consumers access to terminals operated by other institutions in the system. Are new disclosures required?

A: The institution must provide any of the required disclosures that differ from those previously given. (§ 205.7(a))

* * * * *

Q7–15.5: *Charges—in interchange system.* In a shared or interchange system, a charge sometimes is imposed either by the system or by the terminal operator, for the use of terminals operated by an entity other than the account-holding institution. Must such charges be disclosed in initial disclosures?

A: A charge assessed by the interchange system must be disclosed. Charges assessed by terminal-operating institutions, on the other hand, are not within the purview of the account-holding institution's relationship with its customer and therefore need not be disclosed. (See question 4–1.) (§§ 205.7)a)(5) and 205.4(a))

Section 205.9—Documentation of Transfers.

* * * * *

Q9–31: *Periodic statements—charges.* What charges must be disclosed on the periodic statement?

A: Financial institutions should disclose either (1) the total charges assessed against the account during the statement period for electronic fund transfers or the right to make transfers; or (2) the total charges assessed during the period for account maintenance (including both EFT and non-EFT and both fixed feed and per-item charges); or (3) charges for electronic fund transfers, shown on a transfer-by-transfer basis, and the charge (if any) for the right to make transfers. (§ 205.9(b)(3))

Q9–31.5: *Periodic statements—charges in interchange system.* In a shared or interchange system a charge is imposed, either by the system or by the terminal operator, for the use of terminals operated by an entity other than the account-holding financial institution. Must such charges be disclosed on the periodic statement?

A: Yes; an exception applies, however, if the charge was imposed by a terminal-operating institution and was included in the amount of the transfer. (§ 205.9(a)(1), (b)(1)(i), and (b)(3))

* * * * *

Q9–40.5: *Receipts/periodic statements—interchange system; terminal location.* In a shared or interchange system, a consumer uses terminals operated by entities other than the account-holding institution. The terminal operators have terminals at more than one location, and the terminal receipts include a street address, city, and state in addition to the name of the terminal operator. In contrast, the periodic statement provided by the account-holding institution identifies the terminal location for these transfers by listing the name of the terminal operator and the city and state. Does this identification comply with the regulation?

A: Yes. For transfers initiated at non-proprietary terminals, the account-holding institution may describe the location by naming the entity at whose place of business the terminal is located (or which owns or operates the terminal), plus the city and state. It need not repeat on the periodic statement the street address given on the terminal numbers shown on the receipt by the terminal operator. (§ 205.9(a)(5) and (b)(1)(iv))

* * * * *

Section 205.10—Preauthorized Transfers.

* * * * *

10–18.5: *Preauthorized debits—authorization.* A consumer telephones the financial institution or designated payee to arrange for preauthorized electronic fund transfers from the consumers's account, and subsequently receives a form for authorizing the fund transfers. The consumer signs and returns one copy of the form, and retains a copy. Does this procedure comply with the regulation?

A: Yes; the confirmation form serves as the required written authorization. The regulation does not mandate a prescribed format. (§ 205.10(b))

Q10–19: *Preauthorized debits—stop-payment order.* On October 10, a consumer orally orders the financial institution to stop payment on a $30 utility bill that is scheduled to be paid on October 15. The payment is stopped. The consumer properly confirms the order in writing on October 17. On October 30 the utility company resubmits the $30 debit. Must the financial institution stop payment on the resubmitted item? How might the financial institution comply with the consumer's stop-payment request?

A: Yes. The institution may accomplish this, for example, by suspending all subsequent payments to the designated payee until the consumer notifies the institution that payments should resume. The act and regulation establish the consumer's right to stop payment of preauthorized electronic fund transfers. The institution may comply with the regulation and respond to the consumer's request by determining, when the consumer orally requests the financial institution to stop payment on an item, whether (1) the consumer wishes to revoke the payment authorization to the designated payee for all future payments, in which case the institution may suspend all subsequent payments to the designated payee until the consumer notifies the institution that payments should resume; or (2) the consumer wishes only the particular payment to be stopped, in which case the payment must be stopped even if it is resubmitted. (§ 205.10(c))

* * * * *

Section 205.12—Relation to State Law.

Q12–1: *Preemption of state EFT laws—specific determinations.* The regulation prescribes standards for determining whether state laws that govern electronic fund transfers are preempted by the act and the regulation. If, under these standard, state law is inconsistent with the federal law, is the state law it automatically preempted by operation of law, absent a Board determination of preemption?

A: No. A specific determination of preemption will be made by the Board. Interested parties seeking a determination should follow the procedures set forth in the regulation. If the state law is inconsistent

with the federal law and is not more protective than the federal, the state law is preempted even if the Board has not issued a determination on the question. (§ 205.12(a) and (b))

* * * * *

By order of the Board of Governors of the Federal Reserve System, January 12, 1984.

William W. Wiles,

Secretary of the Board.

[FR Doc. 84-1299 Filed 1-17-84; 8:45 am]

BILLING CODE 6210-01-M

---

12 CFR Part 226

[Reg. Z; Doc. No. R-0501]

Truth in Lending; Credit Cards; Issuance and Liability

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: The Board is publishing for comment a proposed amendment to revised Regulation Z (Truth in Lending). The proposal would clarify that credit cards issued for use with transactions that are exempt from all other provisions of the regulation are subject to the Regulation Z provisions governing the issuance of credit cards and the liability for unauthorized use. Questions concerning the applicability of these two credit card provisions have come from both the public and private sectors. The proposed amendment would resolve any remaining uncertainty that the issuance and liability protections apply to all credit cards regardless of use or cardholder status.

DATE: Comments must be received on or before February 24, 1984.

ADDRESS: Comments should be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, or delivered to the C Street entrance 20th and C Streets, N.W., Washington, D.C. between 8:45 a.m and 5:15 p.m. To aid in their consideration, comments should include a reference to Doc. No. R-0501. Comments may be inspected in Room B-1122 between 8:45 a.m. and 5:15 p.m.

FOR FURTHER INFORMATION CONTACT: Regarding the regulation: Ruth R. Amberg, Senior Attorney, or Lynn C. Goldfaden or Richard Garabedian, Staff Attorneys, in the Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 2051, at (202) 452-3667 or (202) 452-3867. Regarding the economic impact analysis: Robert Kurtz, Economist, Division of Research and Statistics, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, at (202) 452-2915.

SUPPLEMENTARY INFORMATION: (1) *General.* Section 226.3 of Regulation Z would be amended to make clear that the restriction on unsolicited issuance of credit cards in § 226.12(a) and the provision in § 226.12(b) limiting a cardholder's liability for unauthorized use of a credit card to a maximum of $50 (both based on the 1970 credit card amendments to the Truth in Lending Act) apply to credit cards issued for use in transactions that are exempt from other sections of the regulation. Questions concerning the applicablity of these two credit card provisions have come from both the public and private sectors. The proposed amendment would resolve any remaining uncertainty that the issuance and liability protections apply to all credit cards, regardless of use or cardholder status. The proposed amendment would not affect the application of the exemptions to the other provisions of the regulation, such as the cost disclosure, rescission, and advertising requirements.

The comment period ends on February 24. Comments must be received on or before that date to ensure consideration. The Board believes a prompt resolution of these matters is essential and in the public interest in order to provide clarification on the scope of the credit card protections.

(2) *Scope.* The Regulation Z exemptions most likely to be affected are those for (1) credit extended by registered broker-dealers for the purchase of securities or commodities, (2) extensions of credit for more than $25,000 (if unsecured by real estate or by the consumer's dwelling), and (3) credit extended by a regulated public utility for utility services, including credit extended by telephone companies. Business credit transactions also are generally exempt from the regulation; however, the regulation presently makes clear that the credit card provisions on unsolicited issuance and liability for unauthorized use apply to cards issued for obtaining business-purpose credit. Although the types of exempt transactions most commonly made with credit cards are business transactions, telephone calls, and securities purchases, the proposed amendment would make clear that *all* credit cards are covered by the provisions on issuance and liability for unauthorized use, so that the amendment also would affect credit cards issued for use with other types of transactions that are exempt under Regulation Z. (The regulation also exempts certain student loans and home fuel budget plans.)

The vast majority of the credit cards that will be affected by this amendment are telephone calling cards. Other than those used in consumer asset management accounts, there appear to be comparatively few cards issued for use with fixed credit lines over $25,000 that are not secured by real estate or a dwelling. Moreover, if the Board adopts the proposed amendment to cover all debit card transactions involving electronics under Regulations E (published elsewhere in this **Federal Register** issue), that regulation will govern the issuance and liability for unauthorized use of the majority of cards in consumer asset management accounts. (See the rule in § 226.12(i) of Regulation Z that designates which regulation applies when a transaction involves both an asset account and a credit extension.) Furthermore, many of the cards in consumer asset management accounts in which credit may be extended without first accessing an asset account are already covered by Regulation Z because they can be used to obtain non-exempt credit. For these reasons, this discussion will focus on telephone credit cards.

(3) *Telephone credit cards.* Questions regarding the applicability of the credit card amendments to telephone cards have become important primarily because of the millions of telephone credit cards that have been issued in recent years; the fact that many paper telephone cards are being replaced by plastic cards which resemble and function much like retail credit cards; and the structural changes in the telecommunications industry that even further expand the number of companies likely to issue cards. Although the Board understands that the current policies of the major telephone card issuers comply with the spirit of the credit card provisions, the proposed amendment would assure that these protections continue in the future.

The Board is concerned that, unless the credit card provisions apply to these cards, consumers who use credit cards in connection with credit programs involving exempt transactions will not have any federal protections restricting unsolicited issuance of such cards and limiting their liability for the unauthorized use of the card. Although there is no evidence of a pattern of abuse at this time, this lack of legal protection may have a serious impact in the future in light of the scope of these programs and the indications of their continued growth.

Approximately 47 million telephone cards have been issued, with most of them having been issued by a few of the 1,600 telephone companies. The use of cards is being encouraged as the companies seek to eliminate the substantial fraud losses and other costs associated with operator-assisted calls billed to third parties, as well as to provide consumers with easier access to telephone services. Presently, the major card issuers only issue cards upon request, and follow a policy of not imposing liability on a consumer for unauthorized charges made on a card. However, unless the credit card protections in Truth in Lending apply to these cards, it is unknown what policies will be set by these companies in the future. It is possible that the companies will reverse their past policies and seek to impose some liability on the cardholder whose card is used for unauthorized calls. The Board is not aware of any other laws specifically providing protections regarding unauthorized telephone card charges, and welcomes additional information on the subject.

Unsolicited issuance of cards presents the risk that a card may be stolen before it reaches the consumer. Since the consumer would not be expecting the card, the first sign of the theft could be a bill for unauthorized charges. Because the card contains all of the information necessary for immediate use, nothing insulates the consumer form unauthorized charges being made with the card. Although the Board has expressed concern in the past that restrictions on unsolicited issuance of typical retail credit cards might inhibit competition, it believes that the potential risk of unsolicited issuance of these cards outweighs any benefits of enhanced competition, as the cards may be used easily by anyone who has possession of them. Unlike the typical credit card, there is no face-to-face contact when the card is used, and no unique identifier of the cardholder, such as a secret personal identification number, or a signature to compare.

The Board also believes that since credit cards used by businesses and for business purposes are subject to the protections, it seems reasonable to conclude that credit cards used by consumers for personal credit transactions should be subject to the same protections. Consumers who use telephone cards, for example, are in no better position to protect themselves form the risks arising from unsolicited issuance and unauthorized use fo these cards than with other credit cards. Further, the policy underlying the public utilities exemption—that is, that other regulatory bodies would provide the needed protections on rates—does not appear to exists when the question concerns credit card issuance and liability for unauthorized use.

(4) *Particular issues for comment.* Although the vast majority of the existing telephone credit cards are issued by a relatively few large entities, there are many small companies in the industry that are or may become involved in card issuance. Therefore, the Board solicits comment on the potential impact of the amendment on small companies in the telecommunications or other potentially affected industries that currently have credit card programs, or that might develop them in the future.

The Board also solicits comment on other regulatory, operational, or cost factors that might be relevant to the proposal.

If the amendment is adopted, the Board will consider appropriate action to minmize initial compliance costs associated with the amendment. For example, the Board recognizes that some outstanding cards or agreements may contain language that is inconsistent with the liability limitation rules. (Some cards may reflect, for instance, that the cardholder is responsible for all charges made with the card.) Therefore, the Board solicits comment on whether it should stipulate that card issuers need not replace existing cards or agreements merely to change misleading language; rather, as new cards are issued or new agreements printed according to the normal replacement schedule, the inconsistent language would have to be modified to accurately reflect the limits. The limited liability protection would, of course, be effective notwithstanding the conflicting language. Such an accommodat in would avoid costly expenditures for mass issuance of replacement cards or agreements, and yet effectuate the goals of the amendment because consumers would have the benefits of the liability protection.

Furthermore, the Board is aware that American Telephone & Telgraph (AT&T)—as part of its plan to automate telephone use—is in the process of issuing, without request, a substitute card to all consumers who have either an existing Bell System card or a card issued by an independent company that can be used for service over AT&T facilities. While this distribution will probably be substantially complete before the effective date of the proposed amendment, the issuance of cards after that date may raise questions of unsolicited issuance because AT&T cannot void the existing credit cards when it issues the new cards. However, because of the unique circumstances involved, and the time, cost, and effort already devoted by AT&T to the project of automating card use the Board solicits comment on waiving the unsolicited issuance prohibition if there are any cards that have not yet been issued as part of this one-time substitution by the effective date of this amendment.

(5) *Economic Impact Analysis.* The Board's Division of Research and Statistics has prepared an economic impact analysis. A copy of the analysis may be obtained from Publications Services, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, at (202) 452–3245.

List of Subjects in 12 CFR Part 226

Advertising, Bank, banking, Consumer protection, Credit, Federal Reserve System, Finance, Penalties, Truth in lending.

(6) *Text of proposed revision.* Pursuant to the authority granted in section 105 of the Truth in Lending Act (15 U.S.C. 1604 as amended), the Board proposes to amend Regulation Z, 12 CFR Part 226, by removing footnote 4 to § 226.3(a) and adding a new footnote 4 to § 226.3 to read as follows:

[4] The provisions governing the issuance of credit cards and the liability for their unauthorized use in § 226.12 (a) and (b) apply to all credit cards, even if the credit cards are issued for use in connection with extensions of credit that otherwise are exempt under this section.

§ 226.3 Exempt transactions.

This regulation does not apply to the following:[4] * * *

* * * * *

By order of the Board of Governors of the Federal Reserve System, January 12 1984.

William W. Wiles,

Secretary of the Board.

[FR Doc. 84–1298 Filed 1–17–84; 8:45 am]

BILLING CODE 6210–01–M

---

12 CFR Part 226

[Reg. Z; TIL–1]

Truth in Lending; Official Staff Commentary Revision

AGENCY: Board of Governors of the Federal System.

ACTION: Proposed official staff interpretation.

SUMMARY: The Board is publishing for comment a proposed change to the official staff commentary to Regulation Z (Truth in Lending). The commentary

applies and interprets the requirements of Regulation Z with regard to consumer credit transactions and is a substitute for individual staff interpretations of the regulation. The proposal addresses the scope of the securities transaction exemption contained in § 226.3(d) of Regulation Z and is intended to clarify its application.

DATE: Comments must be received on or before February 24, 1984.

ADDRESS: Comments should be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, or delivered to the C Street entrance, 20th and C Streets, N.W., Washington, D.C. between 8:45 a.m. and 5:15 p.m. Comments should include a reference to TIL–1. Comments may be inspected in Room B–1122 between 8:45 a.m. and 5:15 p.m.

FOR FURTHER INFORMATION CONTACT: Ruth R. Amberg, Senior Attorney, or Richard Garabedian, Staff Attorney, in the Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, at (202) 452–3667.

SUPPLEMENTARY INFORMATION: (1) *General.* Effective October 13, 1981, an official staff commentary was published to intepret Regulation Z (12 CFR Part 226). The commentary is designed to provide guidance to creditors in applying the regulation to specific transactions and is updated periodically to address significant questions that arise. The present proposal is not a general update, but rather a specific proposal addressing the relationship of the securities transaction exemption to consumer asset management accounts. The proposal is being published at this time, rather than with the most recent proposed update (48 FR 54642, December 6, 1983), because the Board's staff is also now publishing for comment a proposed update to Regulation E (Electronic Fund Transfers), some portions of which address the impact of that regulation on consumer asset management accounts. As both Regulations E and Z may be applicable to these accounts, the preparation of comments will be significantly aided if financial service providers can consider the impact of both regulations at the same time. It is expected that if this proposal is adopted it will be issued in final form in March 1984 with optional compliance until the uniform effective date of October 1 for mandatory compliance with commentary revisions.

Certain conventions have been used to highlight the proposed revisions. New language is shown inside bold-faced arrows, while language that would be deleted is set off with brackets.

(2) *Proposed revision.* Following is a brief description of the proposed revision to the commentary:

Subpart A—General

§ 226.3 Exempt transactions.

3(d) *Securities or commodities accounts.*

This section would be revised to clarify the scope of the exemption for securities or commodities transactions. The need for clarification has arisen largely in the context of consumer financial services that combine transaction and investment features ("consumer asset management accounts") and are offered by brokerage and investment firms.

Consumer asset management accounts permit the consumer to place assets (for example, cash and securities) in one account for the purpose of engaging in consumer transactions, investing excess cash balances in high-yield funds (for example, a money market mutual fund), and buying and selling securities. Typically, if the cash balances and liquidated money market shares are insufficient to pay for the consumer purchase, credit is extended by the broker and such credit is collateralized by securities in the account.

Regulation Z (12 CFR 226.3(d)) provides an exemption for "transactions in securities or commodities accounts in which credit is extended by a broker-dealer registered with the Securities and Exchange Commission or the Commodity Futures Trading Commission". The exemption is based on § 104(2) of the Truth in lending Act. The legislative history of the exemption indicates that it was placed in the act to exempt credit extended by a registered broker-dealer for purchasing or carrying securities. The exemption was premised on the Securities and Exchange Commission's adopting regulations requiring credit disclosures substantially similar to those required by the act. In response, the SEC adopted regulations (17 CFR 240.10b–16) requiring detailed disclosure of credit terms in connection with any securities transaction.

The proposed commentary amendment would make clear that credit that is extended by a broker-dealer through a consumer asset management account and is not for a securities transaction—but is for the payment of other goods and services—remains subject to Regulation Z. (Of course, credit extended by broker-dealers for non-securities transactions outside the context of such an account is also subject to the regulation.) Protections comparable to those in Regulation Z (including, for example, error resolution procedures) do not appear to exist for this category of transactions; comment is solicited on this point. The proposal also reflects the relationship between Regulations E and Z in consumer asset management accounts if electronic fund transfers are involved.

List of Subjects in 12 CFR Part 226

Advertising, Banks, banking, Consumer protection, Credit, Federal Reserve System, Finance, Penalties, Truth in lending.

(3) *Text of Revision.* New language is shown inside bold-faced arrows, while language that would be deleted is set off with brackets. The proposed revision to the commentary (Supplement I to Part 226) reads as follows:

Supplement I—Official Staff Commentary—TIL–1

Subpart A—General

* * * * *

Section 226.3—Exempt Transactions

* * * * *

3(d) *Securities or Commodities Accounts.*

1. *Coverage.* This exemption does not apply to [a transaction with a broker registered solely with the state or to a separate credit extension in which the proceeds are used to purchase securities.] ►the following:

- A transaction with a broker registered solely with the state.
- A separate credit extension in which the proceeds are used to purchase securities.
- A transaction that does not involve the purchase or carrying of securities, even if it is processed through a plan that may also be used to purchase or carry securities offered by a registered broker-dealer. For example, under certain types of consumer asset management accounts, a consumer may purchase any number of goods and services that do not involve securities. Payment for such items may be made, in some cases, by credit extend on the maximum loan value of the securities in the plan. Although Regulation Z applies to these non-securities transactions, note that if electronic fund transfers are involved in these plans, Regulation E supersedes provisions of Regulation Z regarding card issuance and liability for unauthorized use, as well as the procedures for resolving errors (except for § 226.13(d) and (g). ◄

* * * * *

(15 U.S.C. 1604)

Board of Governors of the Federal Reserve System, January 12, 1984.

William W. Wiles,

Secretary of the Board.

[FR Doc. 84–1297 Filed 1–17–84; 8:45 am]

BILLING CODE 6210–01–M