FEDERAL RESERVE BANK
OF NEW YORK

REGULATION X

REAL ESTATE CREDIT

**Interpretations of Regulation X
Issued by the Board of Governors
of the Federal Reserve System
through December 31, 1951**

Circular No. 3804
January 2, 1952
(Supersedes Circular No. 3677)

FEDERAL RESERVE BANK
OF NEW YORK

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To all Persons Engaged in the Business of Extending Real Estate Credit in the Second Federal Reserve District:

This circular contains the interpretations of Regulation X which have been issued through December 31, 1951 by the Board of Governors of the Federal Reserve System. It includes those contained in our Circular No. 3677, dated March 15, 1951, which this circular supersedes. Also included are questions relating to the regulation submitted to the Board of Governors by the American Bankers Association, and the Board's answers. The circular has been printed in a form similar to that of the regulation so that you may keep both together.

Additional copies of this circular will be furnished upon request.

ALLAN SPROUL,
President.

NOTE

To reflect a revision of the regulation made after the issuance of an interpretation or answer, the language of the interpretation or answer has been changed without altering the principle as originally stated. New matter so added appears in *italics*. Interpretations incorporated in subsequent revisions of the regulation have been omitted. The interpretations and questions and answers are arranged in the same order as the sections of the regulation to which they relate *(see page 27 for table of contents)*.

The section number of the regulation to which each interpretation principally pertains has been added after the catch line indicative of its subject matter; the section number of the regulation has also been added after the catch line preceding each question and its answer. Each interpretation that has been published is followed by an editorial note containing cross references to the Federal Register (F.R.), the Federal Reserve Bulletin, and circular, if any, of this Bank.

The interpretations and answers should be used only as aids in studying the application of the regulation. Since certain facts involved in the interpretations and answers have been assumed, there can be no assurance that the facts in new situations will be identical with those assumed. Therefore, caution should be exercised against reaching a conclusion in a given case solely on the basis of similarity to the facts in any one of the interpretations or answers.

REGULATION X

REAL ESTATE CREDIT

Interpretations

Real Estate Brokers—Sec. 1

An inquiry has been received by the Board of Governors regarding the status under Regulation X of real estate brokers: When are they Registrants and, in cases where they are, does this affect sales of real property by non-Registrants, when the broker acts as the vendor's sales agent?

The second paragraph of section 1 of the regulation provides that the regulation applies to any person who is engaged in the business of extending certain real estate credit, "including any person who acts as agent in arranging for such credit." The quoted phrase means that the regulation applies to persons who are engaged in the business of arranging for such credit as agents for lenders, not as agents for borrowers.

In a typical sale of real estate, where the real estate broker acts as sales agent for the vendor, the broker may also arrange the financing for the sale. In such cases, if the broker receives a fee from a lender for his services in arranging the financing, whether the lender is the vendor or a third party, the broker ordinarily would be considered an agent for the lender. However, if the broker does not receive such a fee, but merely contacts or otherwise negotiates with the lender on behalf of the vendor or vendee, he ordinarily would not be considered an agent for the lender.

It is the opinion of the Board that a real estate broker would be a Registrant under Regulation X if, in his own right or as agent for a lender or as a fiduciary, he either (1) extends or has extended such real estate credit more than three different times during the current calendar year or during the preceding calendar year, or (2) extends or has extended such real estate credit in an amount or amounts aggregating more than $50,000 during the current calendar year or during the preceding calendar year. For this purpose, a transaction in which a real estate broker acts as agent of the lender in arranging the financing as described above is to be considered an extension of credit by him.

The mere fact, however, that a real estate broker acting as sales agent in a sale of real property may be a Registrant does not affect a sale by a non-Registrant, unless the real estate broker extends or arranges as agent for an extension of real estate construction credit in connection with the sale.

Under section 4(a)(6) of Regulation X, a sale in which the vendee assumes, or takes the property subject to, a mortgage is not permissible if the amount of outstanding credit (extended after October 12, 1950, or January 12, 1951, *or February 15, 1951,* as the case may be) exceeds the maximum loan value. However, this restriction is applicable only to a

Registrant who is acting as principal and, therefore, does not apply to a real estate broker who is acting as agent in connection either with the sale or the financing which may be involved. Of course, if additional real estate construction credit over and above the maximum loan value of the property were extended in connection with the sale, the other provisions of section 4 would apply to a real estate broker who acted as agent in arranging for the extension of such additional credit in the manner described above.

[16 F.R. 1593; FEDERAL RESERVE BULLETIN, Feb. 1951, p. 162.]

Church Unit Extending Credits—Sec. 1

A church organized on a nationwide basis has a central organization which, in turn, has boards and agencies. The church also has regional organizations which, in turn, have a number of congregations and missions. Each such unit of the church is a corporate entity. Credit sometimes is extended by such units in connection with new construction being purchased or constructed by other units of the church. The question has been raised whether the credit is subject to the provisions of Regulation X.

The credit is not subject to the regulation if the new construction is a church because section 2(r)(3) of the regulation excludes churches from the definition of "nonresidential structure." However, credit extended to finance the purchase or construction of new construction covered by the regulation is subject to the regulation when the unit of the church extending the credit is a Registrant, that is, if the unit has made sufficient extensions of credit to be deemed to be engaged in the business of extending real estate credit. So long as such units are corporate entities, the funds borrowed must be considered as funds of the units lending them rather than funds of the over-all church organization.

It may be noted, however, that the regulation does not affect in any way the purchase or construction of new construction by a unit of the church in possession of the necessary funds, or its participation on an equity basis in the construction or purchase of new construction by another unit of the church.

[16 F.R. 4981; FEDERAL RESERVE BULLETIN, June 1951, p. 647.]

Commodity Credit Corporation Loans—Sec. 2(e)

An inquiry has been received concerning the application of Regulation X to loans which are made by banks and other lending agencies pursuant to commodity loan programs of the Commodity Credit Corporation and which the Commodity Credit Corporation is committed to purchase. It is the Board's view that such loans should be regarded for this purpose as loans guaranteed by a wholly owned Government corporation and that, therefore, they do not constitute real estate construction credit as defined in section 2(e) of Regulation X and are not subject to Regulation X.

[16 F.R. 495; FEDERAL RESERVE BULLETIN, Jan. 1951, p. 33.]

Participating Share in Cooperative Development—Sec. 2(e)

An inquiry has been received asking whether borrowing by a prospective tenant in a cooperative development is subject to Regulation X if the loan is for the purpose of purchasing a participating share in the cooperative development which will entitle the owner thereof to acquire or use a family unit in the cooperative development.

Cooperative developments ordinarily are built and operated by a nonprofit corporation organized for that specific purpose. Credit secured by a blanket mortgage covering the development is extended to the corporation. The corporation's equity or capital investment is raised by the sale of shares of capital stock to the individual cooperators. Ownership of a share carries with it the right to acquire a long term lease upon a family unit in the cooperative development.

It is the opinion of the Board that borrowing is subject to Regulation X when it is for the purpose of purchasing a share in a cooperative development. The total amounts borrowed by the corporation and the individual shareholders may not exceed the maximum loan value of the cooperative development.

[16 F.R. 2969; FEDERAL RESERVE BULLETIN, April 1951, p. 390; FRBNY Circular No. 3695, April 27, 1951.]

Painting, Reroofing, and Repairs as "Major Improvement"—Sec. 2(g)

It is the Board's view that painting, reroofing, and repairs constitute a "major improvement", within the meaning of section 2(g) of Regulation X, if their cost exceeds *amount prescribed in section 2(g). (See Regulation W of the Board of Governors of the Federal Reserve System regulating instalment credits not exceeding $2,500 with respect to residential repairs, alterations, or improvements and items of household equipment.)*

[15 F.R. 7383; FEDERAL RESERVE BULLETIN, Nov. 1950, p. 1474.]

Allowance for Labor—Sec. 2(i)

Inquiries have been received under section 2(i)(2)(B) of Regulation X where the facts are these: A prospective borrower owns a vacant lot on which he, with the help of his family and friends, will perform the necessary labor to build a residence. He applies to a Registrant for credit to be secured by a mortgage upon the residential property, the proceeds of the loan to be used to pay for materials used in the new construction. The question is: How does a Registrant determine the "value" of the residential property?

If the entire cost of the property has been incurred by the prospective borrower not more than 12 months prior to the extension of credit or is to be incurred by him after such extension of credit, the "value" is the bona fide cost of the property to the borrower, including a bona fide estimate of the cost of completing the new construction. It is the view of

the Board that a reasonable bona fide estimate of the value of the labor to be performed by the prospective borrower, his family, and friends may be included in the "bona fide estimate of the cost of completing new construction."

If the lot has been purchased or any other part of the cost of the property has been incurred by the prospective borrower more than 12 months prior to the extension of credit, or if any part of such property has been acquired by gift, exchange, or inheritance, the "value" shall be the appraised value as determined in good faith by the Registrant.

[15 F.R. 7383; FEDERAL RESERVE BULLETIN, Nov. 1950, p. 1475.]

Allowance for Builder's Profit and Costs of Sale—Sec. 2(i)

Section 2(i) provides that, in certain circumstances, the "value" of residential property shall be "the bona fide cost of the property to the borrower, including a bona fide estimate of the cost of completing new construction on such property when the extension of credit is for the purpose of financing such new construction." Questions have been raised concerning the inclusion of builder's profit and sales cost in determining "value" in cases where, in lieu of obtaining short-term construction credit which would be refinanced upon the sales of the houses, a builder constructing houses for sale seeks long-term mortgage loans for the purpose of financing the construction of the houses and with the expectation that the houses will be sold subject to such indebtedness.

It is the Board's view that in such cases a reasonable builder's profit and a reasonable estimate of the cost of selling the houses may be included as a part of the cost to the borrower (builder) for the purposes of determining "value" under the above-mentioned provision of Regulation X. However, in connection with the sale of the houses, consideration must be given to the provisions of section 4(a)(6) of Regulation X relating to the sale of property by a Registrant subject to indebtedness which exceeds, or as a result of such sale would exceed, the applicable maximum loan value of such property.

[15 F.R. 8713; FEDERAL RESERVE BULLETIN, Dec. 1950, p. 1622.]

Appraised Value of Improved Real Property—Sec. 2(i)

Several inquiries have been received by the Board regarding the determination under Regulation X of "appraised value as determined in good faith" where there is to be construction on improved real property. The inquiries have related particularly to cases where there is an existing structure on the property such as a residence, servants' quarters, garage, or garage-apartment, but similar inquiries should be answered in accordance with the principles of this interpretation. In such cases, should the Regis-

trant, in making his appraisal in good faith, appraise only the land or should he appraise the land and improvements?

In cases where the existing structure and the proposed construction are to be so located on the property that the possibility of separation in the case of resale would be remote and unlikely, it is the opinion of the Board that the Registrant may appraise the land and improvements. However, any outstanding credit secured by the improved real property necessarily would have to be taken into consideration in determining the amount of credit the Registrant could extend.

For example, if a prospective borrower desires to build a new residence at a cost of $20,000, on improved real property having a "value" of $10,000, the Registrant's appraised value may be $30,000, and the maximum loan value $15,000. However, if there were outstanding credit secured by the improved real property in an amount of, say, $5,000, the Registrant could not extend additional credit in an amount exceeding $10,000.

In cases where the existing structure and the proposed construction are to be so located that separation in the case of resale would not only be possible, but would be likely, it is the opinion of the Board that the Registrant should appraise only the land area on which the new construction is to be located.

For example, if the prospective borrower owns a tract of land consisting of several adjoining lots, some of which are improved with existing structures, and the borrower proposes to build a new structure on one of the vacant lots, the Registrant should appraise only the vacant lot.

[16 F.R. 2552; FEDERAL RESERVE BULLETIN, March 1951, p. 272.]

Appraised Value of Lot and Residence—Sec. 2(i)

Where a residence is to be constructed on a lot acquired more than twelve months ago, the "value" of the residential property, in accordance with the provisions of section 2(i)(2)(B)(ii) of Regulation X, is the appraised value of both the lot and residence.

[16 F.R. 5320; FEDERAL RESERVE BULLETIN, June 1951, p. 647.]

Determination of Value of Residential Property—Sec. 2(i)

Inquiries have been received concerning the application of section 2(i)(2)(B) of Regulation X to a case where, through unforeseen delays, credit is extended more than one year after the acquisition of property.

A typical example might be as follows: On June 5, 1950, an individual purchased a lot. On December 5, 1950, a Registrant committed himself to provide permanent financing to the extent of the maximum loan value computed on the basis of bona fide estimated cost. Because of unforeseen delays, however, construction will not be completed until July 1951. The question raised is whether the Registrant must now base the maximum loan value

on his appraisal rather than the estimated cost, or whether the commitment to extend credit may be considered an extension of credit.

The Board has ruled in other cases in the past that a commitment to extend credit cannot be considered an extension of credit. Therefore, it will be necessary in such cases for the Registrant to base his loan on an appraisal rather than on estimated cost.

[16 F.R. 5950; FEDERAL RESERVE BULLETIN, July 1951, p. 813.]

House Trailers—Sec. 2(k)

The question has been raised whether Regulation X applies to extensions of credit in connection with sales of house trailers. It is the view of the Board that such extensions of credit are subject to the regulation where the trailers *have kitchen facilities or space designed for kitchen facilities, and* are to be used for dwelling purposes, and the wheel assemblies are to be detached and the trailer placed on a foundation constructed on real property.

[15 F.R. 7798; FEDERAL RESERVE BULLETIN, Dec. 1950, p. 1621.]

Warehouses and Office Buildings Used in Processing Goods—Sec. 2(r)

The Board has received several inquiries as to whether warehouses and office buildings used in connection with a manufacturing business are subject to Regulation X. As indicated in footnote 11 on page 6 of the regulation, office buildings and warehouses, as well as other buildings, are ordinarily subject to the regulation. They are not subject to the regulation, however, if they fall within one of the exclusions from the definition of "nonresidential structure", namely, structures exclusively used or designed for use by a public utility or by any Government or political subdivision, or structures more than 80 per cent of the floor space of which is used or designed for use (i) in processing materials, goods, or articles into finished or partly finished manufactured products, (ii) in mining or otherwise extracting raw materials, or (iii) on farm property in the production, shelter, or storage incidental thereto, of crops, livestock or other agricultural commodities. It is the opinion of the Board that space in such structures as office buildings and warehouses is used or designed for use in processing materials, goods, or articles into finished or partly finished manufactured products where such office building or warehouse is essential to and an integral part of the operations involved in the processing of such materials, goods, or articles. Unless the office building or warehouse, however, is essential to the processing operation and an integral part thereof, it is subject to the regulation.

[16 F.R. 2551; FEDERAL RESERVE BULLETIN, March 1951, p. 272.]

Newspaper Printing Plant—Sec. 2(r)

It is the opinion of the Board that a newspaper is a "manufactured product" within the meaning of section 2(r)(5)(i) of Regulation X. Accordingly, the definition of "nonresidential structure" in section 2(r) does not include a structure more than 80 per cent of the floor space of which is used or designed for use in the printing of newspapers and, therefore, credit for the financing of such construction is not subject to Regulation X.

[16 F.R. 4340; FEDERAL RESERVE BULLETIN, May 1951, p. 509.]

Dining Cars as Nonresidential Structures—Sec. 2(r)

The question has been raised whether Regulation X applies to extensions of credit in connection with sales of what are commonly known as "dining cars" to be used as restaurants.

It is the view of the Board that when a "dining car" is placed on a foundation constructed on real property, and the utility connections necessary for its operation as a restaurant are installed, it becomes a "nonresidential structure" within the meaning of section 2(r) of Regulation X; accordingly, in such cases, an extension of credit in connection with the sale of the dining car is subject to Regulation X.

[16 F.R. 7460; FEDERAL RESERVE BULLETIN, August 1951, p. 959.]

Medical Centers and Clinics as Hospitals—Sec. 2(r)

Individual groups of medical doctors who are associated in organizations variously known as "medical centers" and "medical clinics" have from time to time contended to different Federal Reserve Banks that structures used by them are "hospitals" within the meaning of section 2(r) of Regulation X. Such medical groups are organized to provide medical services and often have extensive facilities, including radiological departments, laboratories, dispensaries, physical therapy and BMR (basal metabolism rate tests) and EKG (electrocardiogram facilities, as well as facilities for minor surgery. These medical centers and clinics sometimes provide "out-patient" diagnostic and treatment services which often are accessory to services contributed by hospitals, and which may be provided only through the employment of most extensive physical facilities.

Heretofore, in order for an institution to be considered as a "hospital" under section 2(r) of Regulation X, it has been our view that it must include as a minimum requirement "in-patient" facilities coupled with extensive medical services normally provided by hospitals. It seems apparent, however, that the medical services made available by some medical centers and clinics are an equally essential and indispensable part of the public health facilities of some communities, and for that reason we believe that medical centers, clinics, and individual doctors' offices which offer reasonably complete medical services for diagnosis and treatment should be considered

"hospitals" within the meaning of Regulation X, even though they do not have "in-patient" facilities.

[16 F.R. 12225; FEDERAL RESERVE BULLETIN, December 1951, p. 1529.]

Radio and Television Broadcasting Companies Not Public Utilities—Sec. 2(s)

In answer to inquiries received it is the opinion of the Board that radio and television broadcasting companies are not public utilities within the meaning of section 2(s) of Regulation X. Accordingly, structures exclusively used or designed for use by such companies are nonresidential structures within the meaning of section 2(r) of the regulation.

[16 F.R. 2552; FEDERAL RESERVE BULLETIN, March 1951, p. 273.]

Interstate Trucking Companies as Public Utilities—Sec. 2(s)

Inquiries have been received by the Board asking whether companies engaged in an interstate trucking business are public utilities within the meaning of section 2(s) of Regulation X.

The Interstate Commerce Commission has authority to regulate three types of interstate motor carriers. They are "common carrier by motor vehicle", "contract carrier by motor vehicle" and "private carrier of property by motor vehicle." The degree of regulation and supervision exercised by the Commission differs with respect to the three types of carriers. Common carriers are required to obtain certificates of convenience and necessity outlining the extent of their proposed service, the routes over which they propose to operate, and other requirements deemed necessary by the Commission. Contract carriers must obtain a permit outlining the territory over which they propose to operate, the type of business, and any other conditions or limitations deemed necessary by the Commission in the public interest. Private carriers require neither certificates nor permits to operate.

Not only does the degree of regulation and supervision differ with respect to the three classes of carriers, but also the extent of their operations "for the convenience, service or accommodation of the public." Common carriers undertake for hire to transport from place to place the goods of anyone who chooses to employ them. Contract carriers transport for a limited number of shippers under special contracts designed to meet their particular needs. Private carriers need not transport for compensation, but may be the owner, lessee, or bailee of the goods transported.

For the above reasons, it is the opinion of the Board that, in the absence of other pertinent facts, only those companies engaged in an interstate trucking business as a "common carrier by motor vehicle" are public utilities within the meaning of section 2(s) of Regulation X.

[16 F.R. 2552; FEDERAL RESERVE BULLETIN, March 1951, p. 273.]

Privately-Owned Public Warehouse Not a Public Utility—Sec. 2(s)

A privately-owned public warehouse used for the storage of grain and other foodstuffs is not a "public utility" within the meaning of section 2(s) of Regulation X, and hence is not excluded from the definition of "non-residential structure" by section 2(r)(4)(i) of the regulation, even though the operations of the warehouse are supervised by a Federal or State agency. It is the Board's opinion that a warehouse is not similar to a transportation company, electric light or power company, or other similar companies specifically mentioned in section 2(s).

[16 F.R. 4980; FEDERAL RESERVE BULLETIN, June 1951, p. 647.]

Instruments Evidencing Exempt Credit—Sec. 4(a)(5)

The prohibitions of section 4(a)(5) of Regulation X with respect to a Registrant purchasing, discounting, or lending on credit instruments evidencing real estate construction credit apply only to credit instruments evidencing credit which is subject to and not exempt from Regulation X. Under section 6(b) of the regulation, credit extended pursuant to firm commitments made prior to the effective date of the regulation is exempt. Accordingly, there is no prohibition with respect to purchasing, discounting, or lending on credit instruments evidencing such credit.

[15 F.R. 7179; FEDERAL RESERVE BULLETIN, Nov. 1950, p. 1473.]

Sale of New Residence Subject to Pre-effective Date Indebtedness—Sec. 4(a)(6)

Inquiries have been received regarding the application of Regulation X to a sale of *1-2 family unit residence* on which there is new construction, where the vendee assumes, or takes the property subject to, indebtedness secured by a mortgage on the property and such indebtedness exceeds the maximum loan value of the property but evidences credit extended prior to October 12, 1950, the effective date of the regulation *with respect to 1-2 family unit residence.*

Regulation X does not prohibit such a sale or require that the indebtedness be reduced to the maximum loan value of the property. Under the definition contained in section 2(d) of Regulation X, such a sale constitutes an extension of credit by the vendor of the property; but, even though the vendor may be a Registrant, the sale is not prohibited by Regulation X because the provisions of section 4(a)(6) of the regulation, which deal specifically with such transactions, prohibit a sale only if the amount of outstanding credit (including any credit exempt from, or not subject to the prohibitions of, this regulation) which was extended after the effective date of the regulation with respect to the property exceeds, or as a result of such sale or transfer would exceed, the applicable maximum loan value of such property, or if any outstanding real estate construction credit

(subject to and not exempt from this regulation) with respect to such property does not conform with the provisions of this regulation and the Supplement thereto. However, any additional extension of credit by a Registrant (including the vendor if he is a Registrant) in connection with such a sale would be prohibited by section 4(a)(1) of Regulation X.

For example, in a sale of a *1-2 family unit residence* on which there is new construction where the bona fide sale price is $12,000, and the vendee pays $2,000 for the equity of redemption and assumes, or takes such property subject to, a $10,000 mortgage which evidences credit extended prior to October 12, it is not necessary that the $10,000 mortgage be rewritten to conform with Regulation X. However, no part of the $2,000 paid by the vendee for the equity of redemption may be borrowed from a Registrant because the amount of credit outstanding with respect to the property already exceeds the maximum loan value of the property.

[15 F.R. 7383; FEDERAL RESERVE BULLETIN, Nov. 1950, p. 1474.]

Necessity for Statement of Borrower for Nonregulated Credit—Sec. 4(c)

A Registrant makes an unsecured loan to a mortgage company, the proceeds of which are to be used by the mortgage company to make real estate loans, including some subject to Regulation X. Must the Registrant obtain any Statement of the Borrower?

As described, the loan by the Registrant to the mortgage company is not an extension of real estate construction credit or a loan on credit instruments evidencing real estate construction credit. The Registrant is required only to be satisfied, and maintain records which reasonably demonstrate on their face, that the loan to the mortgage company is not real estate construction credit. This requirement may be met by the execution by the mortgage company of a Statement of the Borrower of the kind described in the *last sentence* of section 4(c) of Regulation X and the acceptance of the statement by the Registrant in good faith. *Section 4(c) as amended prescribes other methods of meeting the requirement and relieving Registrant in certain circumstances from duty to ascertain nature of the credit.*

[15 F.R. 7179; FEDERAL RESERVE BULLETIN, Nov. 1950, p. 1473.]

Statement of Borrower Where Credit Secured by Mortgage Collateral—Sec. 4(d)

A Registrant makes a loan to a mortgage company on a note secured by a pledge of collateral consisting of real estate mortgages, including some subject to Regulation X. May the Registrant rely upon a statement by the mortgage company that all of the pledged mortgages which are subject to Regulation X conform with the requirements of the regulation? Must the Registrant procure a copy of the Statement of the Borrower which the mortgagor signed, pursuant to section 4(d) of Regulation X, with respect to each pledged mortgage which is subject to Regulation X?

Section 4(a)(5) of Regulation X provides that no Registrant shall lend on any credit instrument evidencing real estate construction credit which is subject to and not exempt from the regulation, unless the terms of such credit conformed with the provisions of the Supplement to the regulation when such credit was originally extended, or conform at the time of such loan. In the case described, the Registrant may not rely upon the statement by the mortgage company to establish that the pledged mortgages which are subject to Regulation X conform with the requirements of the regulation. The Registrant, however, may rely upon a signed statement accepted in good faith in which the mortgage company states which of the pledged mortgages do, and which do not, evidence real estate construction credit subject to Regulation X; and in determining whether a mortgage which is subject to Regulation X conforms with the regulation, the Registrant may rely upon the facts stated in a copy of the Statement of the Borrower signed by the mortgagor and which the Registrant accepts in good faith.

[15 F.R. 7179; FEDERAL RESERVE BULLETIN, Nov. 1950, p. 1473.]

Short-Term Residential Construction Credits—Sec. 5(b)

In answer to questions that have been raised concerning the exemption in the first sentence of section 5(b) of Regulation X for short-term construction credits having a maturity of not more than 18 months, it is the opinion of the Board (1) that a demand note complies with the 18 months' maturity limitation if it is understood by the parties that payment will be demanded within a reasonable time and in any event within 18 months from the date the credit is extended; and (2) that a note having a maturity of less than 18 months may be renewed pending completion of construction if the date of maturity of the renewal is not more than 18 months after the date the credit originally was extended.

[15 F.R. 7799; FEDERAL RESERVE BULLETIN, Dec. 1950, p. 1621.]

Section 5(b) of Regulation X exempts from the prohibitions of Regulation X certain construction loans having a maturity of not more than 18 months. The Board, in the preceding interpretation, stated that a note evidencing such a construction loan which has a maturity of less than 18 months may be renewed pending completion of construction if the date of maturity of the renewal is not more than 18 months after the date the credit originally was extended.

It is the opinion of the Board, however, that such a note having a maturity of less than 18 months may not be renewed after the construction has been completed, even if the date of maturity of the renewal is not more than 18 months after the date the credit originally was extended.

[16 F.R. 5320; FEDERAL RESERVE BULLETIN, June 1951, p. 647.]

Casualty Exemption for Tenants—Sec. 5(e)

In answer to an inquiry concerning section 5(e) of Regulation X, it is the opinion of the Board that the applicability of the exemption extends to tenants as well as owners of structures destroyed or substantially damaged by flood, fire, or other similar casualties.

[16 F.R. 8048; FEDERAL RESERVE BULLETIN, August 1951, p. 960.]

Exemptions for Contemplated Construction—Sec. 5(g)

It is the view of the Board that exemptions under section 5(g) of Regulation X should not be granted unless there is a clear showing of substantial hardship. The mere fact that a builder or other person may have made substantial commitments or undertakings before August 3, 1950 is not sufficient basis for the granting of an exemption unless he is also able to show that he will suffer substantial hardship if he has to comply with Regulation X in obtaining credit rather than obtaining it on the basis previously contemplated by him and the Registrant. The builder or other person must also be able to show that he had contacts or negotiations with a Registrant prior to August 3, 1950, with a view to possible subsequent agreement for extension of credit to such builder or other person. Section 5(g) relates only to the credit to finance new construction which is extended to the builder or other person who made substantial commitments or undertakings before August 3, 1950 and the provision does not apply to credit involved in a subsequent sale of the property by such builder or other person.

[15 F.R. 8075; FEDERAL RESERVE BULLETIN, Dec. 1950, p. 1622; FRBNY Circular No. 3611, Nov. 9, 1950.]

Unavoidable Delay in Credit Extension—Sec. 5(k)

Section 5(k) of Regulation X provides that the regulation does not apply to real estate construction credit extended prior to 32 days after certain new construction is completed. Credit extended after the 32-day period is exempt, however, in cases where the extension of credit is necessarily delayed by title difficulties, pending litigation with respect to the property, or comparable circumstances.

[16 F.R. 8048; FEDERAL RESERVE BULLETIN, August 1951, p. 959.]

Firm Commitment Prior to Effective Date—Sec. 6(b)

(Herein "effective date" means October 12, 1950 where 1-2 family unit residence; January 12, 1951 where 3-4 family or multi-unit residence; February 15, 1951 where nonresidential property.)

Section 6(b) of Regulation X provides that the *prohibitions of subsections (a) and (b) of section 4* of the regulation shall not apply to or affect any credit extended pursuant to any firm commitment to extend credit made prior to the effective date of the regulation. Inquiries have been received concerning the application of this section to agreements entered

into by a Registrant and a builder prior to the effective date of the regulation under which the Registrant agreed to lend a stated amount on stated terms to any purchaser of particular residences built or to be built by the builder if the purchaser has a credit standing satisfactory to the Registrant and if the residence has been constructed according to prescribed plans and specifications.

Section 6(b) defines a firm commitment as either (1) a written agreement under which the Registrant is required without option or discretion on his part to extend credit upon demand by the borrower or upon compliance by the borrower with one or more conditions referred to in such agreement; or (2) any other agreement to extend credit which has been entered into in good faith by the parties and in reliance upon which the prospective borrower has taken specific action prior to the effective date of the regulation, if the Registrant prior to January 1, 1951 *(where 1-2 family unit residence) or prior to March 15, 1951 (where 3-4 family or multi-unit residence)* shall have sent to the Federal Reserve Bank of the district in which he does business a letter or other statement reciting the facts with respect to such agreement and the specific action taken by the prospective borrower prior to the effective date of the regulation.

If an agreement of the kind described above is in writing, it constitutes a firm commitment within the meaning of clause (1) of the definition of that term and the fact that the borrower (purchaser) must have a credit standing satisfactory to the Registrant is merely one of the conditions with which the borrower must comply.

If such an agreement is not in writing *(on nonresidential property there is an exemption only if the firm commitment is in writing and made prior to February 15, 1951),* it constitutes a firm commitment within the meaning of clause (2) of the definition if the builder has taken specific action in reliance upon the agreement prior to the effective date of the regulation and the Registrant furnishes the required information to the appropriate Federal Reserve Bank *prior to prescribed date.* For this purpose, the term "prospective borrower" in clause (2) of the definition is deemed to include the builder to whom the commitment was made.

[15 F.R. 7180; FEDERAL RESERVE BULLETIN, Nov. 1950, p. 1474.]

Modification of Pre-effective Date Firm Commitment—Sec. 6(b)

(Herein "effective date" means October 12, 1950 where 1-2 family unit residence; January 12, 1951 where 3-4 family or multi-unit residence; February 15, 1951 where nonresidential property.)

Section 6(b) of Regulation X provides that the *prohibitions of subsections (a) and (b) of section 4* of the regulation shall not apply to or affect any credit extended pursuant to any firm commitment to extend credit made prior to the effective date of the regulation. Questions have been raised concerning the application of this provision where firm commitments made prior to the effective date of the regulation are modified subsequent to that

date by (1) substituting a new borrower for the one named in the commitment, (2) increasing the amount which the Registrant is committed to lend in order to cover increases in construction costs, or (3) extending the time within which the Registrant is committed to make the loan. It is the Board's opinion that credit extended pursuant to such a modification of a prior commitment is not exempt from Regulation X except in the case of reasonable extensions of time in accordance with customary practices where the closing of loans is delayed by title difficulties, unforeseen delays in the completion of construction, or comparable circumstances.

[15 F.R. 8076; FEDERAL RESERVE BULLETIN, Dec. 1950, p. 1622.]

Extension of Credit for Mixed Purposes—Sec. 6(h)

Inquiries have been received regarding the application of Regulation X to extensions of credit for mixed purposes. For example, a prospective borrower applies to a Registrant for a loan to be secured by a mortgage on residential property on which there is no new construction. A part of the loan is for the purpose of financing a major addition to the residence which will cost $8,000, and $2,000 of the loan will be used (A) to retire an existing mortgage on the property, or (B) to retire outstanding indebtedness not secured by a mortgage on the property, or (C) for some other purpose which would not make the loan subject to Regulation X. The question is: How much credit can the Registrant extend and on what terms?

It is the view of the Board that in such cases Regulation X requires that the amount and terms of the loan shall be such as would result if the loan were divided into two or more parts on the basis of the purposes of the loan and each part were treated as if it stood alone; and the amount and terms of the loan would comply with Regulation X if they satisfied the requirements of the regulation applicable to that part which is subject to Regulation X.

By way of illustration, in each of the examples set forth above, the maximum amount of credit permitted by Regulation X would be $8,800, that is, $6,800 (the maximum loan value of the $8,000 major addition) plus $2,000. The maturity and amortization of that part ($6,800) which is subject to Regulation X would have to conform with the provisions of the Supplement; or, in other words, the payments on the loan would have to be such as to repay $6,800 of the loan within the time and at the rate required by the Supplement.

The same principles apply in the case of a loan secured by a mortgage on farm property where part of the loan is for the purpose of financing the construction of a residence on such property and the remainder of the loan is for purposes which would not make the loan subject to Regulation X.

[15 F.R. 7384; FEDERAL RESERVE BULLETIN, Nov. 1950, p. 1475.]

Maximum Maturity—Sec. 6(i)

The maturity provision in the Supplement to Regulation X provides for a maximum maturity of 20 years (or 25 years, in some cases) "from the date such credit is extended." In trade practice, provision often is made for the payment of the first instalment of an amortized loan on the first day of the second calendar month after the month in which the credit is extended. In order to permit this practice, the Board, in a *ruling which appeared on page 1621 of the Federal Reserve Bulletin for December 1950,* stated: "* * * in calculating the maximum maturity of credit subject to the regulation, a Registrant may, at his option, use any date not more than 32 days subsequent to the date such credit is extended."

Regulation X, as amended, provides in section 6(*i*) that "In calculating the maximum maturity of credit subject to this regulation, a Registrant may use, at his option, as 'the date such credit is extended', any date not more than 32 days subsequent to the actual date such credit is extended."

Section 6(i) of the regulation does not mean that the first instalment of an amortized loan must be paid within 32 days after the date the credit is extended. *It does* mean, in effect, that the maximum maturity of credit subject to Regulation X may be 20 years and 32 days (or, in some cases, 25 years and 32 days) from the actual date such credit is extended.

For example, if a 20-year loan payable monthly were closed on January 1, 1951, and the first payment is made on March 1, 1951, the last payment would be made on February 1, 1971. Here the Registrant would be using February 1, 1951, which is 31 days subsequent to the actual date such credit is extended, as "the date such credit is extended", and the loan would mature 20 years from such date. The loan, in effect, would have a maturity of 20 years and 31 days from January 1, 1951, the actual date such credit was extended.

The principle of section 6(*i*) of the regulation is not limited to monthly payment loans. The amortization provision in the Supplement to Regulation X permits repayment through substantially equal monthly, quarterly, semiannual, or annual payments. As a further illustration, in the case of a 20-year loan payable annually in 20 instalments, where the loan is closed on February 1, 1951, the first payment could be made on March 1, 1952, because the last payment would be made and the loan would mature on March 1, 1971. Here the Registrant would be using March 1, 1951, which is 28 days subsequent to the actual date such credit is extended, as "the date such credit is extended", and the loan would mature 20 years from such date.

[16 F.R. 1593, Federal Reserve Bulletin, Feb. 1951, p. 161.]

Actual Date Credit is Extended—Sec. 6(i)

Inquiries have been received by the Board concerning the meaning of the phrase "actual date such credit is extended" as used in section 6(i) of Regulation X.

Many types of credit extensions are subject to Regulation X and it is administratively impossible to prescribe a specific rule which would be fairly applicable to all types of financing arrangements affected by the regulation. However, for the purposes of Regulation X the general rule to be followed in most extensions of credit affected by the regulation is that the "actual date such credit is extended" is that date which is (1) the date on which the lender first disburses funds to, or makes funds available to the account of, the borrower, or (2) the date of execution of the note or other credit instrument evidencing the credit extended, whichever shall last occur.

[16 F.R. 2551; FEDERAL RESERVE BULLETIN, March 1951, p. 272.]

Compliance with Amortization Provisions—Supplement

Clause (2) of the amortization provision in Schedule I and the amortization provision in Schedule III of the Supplement to Regulation X provide for amortization payments which "will fully liquidate the original principal amount of such credit not later than the date of the maturity of the credit . . ."

In cases where the maturity of credit subject to the regulation is less than the maximum permitted by the regulation, it is the opinion of the Board that the amortization provisions referred to above will be complied with if amortization payments are made until the maturity of the credit which, had they been continued until the maximum permissible maturity, would have fully liquidated the original principal amount of such credit by the date of such maximum permissible maturity.

For example, if the maximum maturity is 20 years, and the credit has a maturity of 10 years, the amortization provisions would be complied with if amortization payments are made during the 10 years which, had they been continued for 20 years, would have fully liquidated the original principal amount of such credit within 20 years.

[16 F.R. 2551; FEDERAL RESERVE BULLETIN, March 1951, p. 272.]

REGULATION X
REAL ESTATE CREDIT

Questions and Answers

Real Estate Construction Credit—Sec. 2(e)

Q. To what extent, if any, is existing construction subject to the controls of Regulation X, or is it limited solely to new construction?

A. Regulation X applies only to new construction, that is, any structure, or any major addition or major improvement to a structure, begun after August 3, 1950.

* * *

Q. A two-family house has been converted and is being occupied by three families (3 baths, 3 kitchens, etc.). This change was made in violation of city code. Will the sale of the property under GI or FHA loan come under Regulation X?

A. It would not be subject to Regulation X if sale is entirely financed by a GI or FHA loan.

* * *

Q. A builder has commitments given during July of 1950, for the construction of ten new homes to be financed by conventional loans. The applications were not processed and the buildings were not started prior to August 3, 1950. The houses are built and financed by six-month conventional loans and then offered for sale with FHA or GI financing. Are such sales subject to Regulation X?

A. If purchases of such houses, although "new construction", are financed entirely through FHA or GI financing, such financing is not subject to Regulation X, as issued by the Board of Governors.

* * *

Q. A man owns a *one-family* house ten years of age. Subsequent to August 3, 1950, he expends $3,000 of his own money on remodeling and improvement, which is thus a "major alteration or improvement." Subsequently, he desires to sell the house. Is the financing in connection with this sale regulated in whole or in part?

A. Under section 2(e) of Regulation X, real estate construction credit includes any credit extended on "new construction on real property or real property on which there is new construction, if such new construction is a residence or a major addition or major improvement to a residence." Consequently, financing in connection with the sale of an

old house to which a major addition is made after August 3, 1950, would be subject in its entirety to Regulation X.

* * *

New Construction—Sec. 2(f)

Q. Define what exactly constitutes the start of new construction for purposes of the new regulations. Would a placement of a portion of the needed materials on a proposed building site be sufficient?

A. Under the regulation, construction is considered as having been begun when any essential materials which are to be an integral part of the structure have been affixed to or incorporated on the site in a permanent form. The placement of a portion of the needed materials, such as the stacking of lumber, on the proposed site would not be sufficient. For example, pouring of footings would be considered as evidence of commencement of construction.

* * *

Q. A borrower excavated the ground for the cellars of ten homes prior to August 3, 1950. No actual construction work, other than the excavation, was started prior to that date. Would these ten contemplated homes be considered construction begun prior to August 3, 1950?

A. Pursuant to the provisions of section 2(f) of the regulation, mere excavation would not constitute the beginning of new construction.

* * *

Q. Construction of a home was started in April of 1950. It is a self-built home and while work has been done continuously, completion has lagged. The building is now 70% completed, and the owner applies for a $5,000 loan to cover the cost of the completion. Is this considered a major improvement, and subject to Regulation X, or is it exempt by way of construction having been started prior to August 3, 1950?

A. Since work has been done continuously, although construction has lagged, this structure is exempt from Regulation X because the construction was begun prior to August 3, 1950.

* * *

Maximum Loan Value—Sec. 2(i)

Q. Please amplify the term "maximum loan value" where the entire cost of the property to the borrower has been incurred by him not more than 12 months prior to the extension of credit (section 2, subsection i).

A. The provision of the regulation in question refers to the method of computing the total value of the property and the maximum loan value

is computed on the basis of this total value as prescribed in the Supplement to the regulation. If the entire cost of the property is incurred not more than 12 months prior to the extension of credit the "value" is the bona fide cost of the property to the borrower, including a bona fide estimate of the cost of completing the new construction. Also, where a builder constructing houses for sale seeks long-term mortgage loans for the purpose of financing construction with the expectation that the houses will be sold subject to such indebtedness, a reasonable builder's profit and reasonable estimate of the cost of selling the houses may be included as a part of the cost to the borrower (builder) for purposes of determining "value." In the rare case in which the prospective borrower is to perform the labor on the new house, a bona fide estimate of the value of the labor may be included in the "bona fide estimate of the cost of completing new construction."

* * *

Real Estate Construction Credit to Build New Residence—Sec. 4(a) (1)

Q. A customer has asked for a $10,000 loan upon stock collateral. He intends to lend this money to his son, who will build a new home to cost $10,000. Informal discussions suggest that this loan is not regulated, as the father can properly sign a statement that the proceeds of the loan that he is getting from us on the stock is not for "new construction." What is your opinion?

A. While the father could, of course, sign such a statement, nevertheless, the loan by the bank to the father is in fact an indirect extension of credit to the son and if it is for the purpose of circumventing the regulation, the son would be the real borrower and the extension of credit would violate the regulation.

* * *

Q. An individual contemplates building a *one-family* residence on a lot which cost him $1,500 and under a contract in the amount of $16,000, so that his ultimate investment or transaction price will be $17,500. As a national bank and under Section 24, the maximum loan we could extend would be $10,500 or 60% of the cost, whereas under Regulation X, the loan could be $11,300.

To obtain the necessary funds to build, the applicant proposes to borrow the sum of $3,900 on life insurance policies, which under the regulation is an exempt transaction. The applicant is presently the owner of a property, clear of encumbrance, valued at $12,000. Under Section 24 we could make a 50% loan, or $6,000, where the loan had a maturity of less than five years. He proposes to further borrow the sum of $6,100

on a construction mortgage having a six months' maturity, which under Section 24 we would be permitted to make provided the advances under the construction mortgage do not at any time exceed 60% of the value of work done.

This question assumes that for appraisal purposes, valuation as indicated above will be supported. As we see the picture, this particular case involves four loan transactions. The question is, are each of them considered separate transactions and, therefore, will Regulation X prevail, and on which of the transactions, and what type of statement should be obtained from the borrower?

A. In lending on real estate a national bank must conform with the requirements of Regulation X or Section 24 of the Federal Reserve Act whichever is the stricter.

The "value" of the residential property would be $17,500 and the maximum loan value would be $11,300. Assuming that all four loans are to be made at the same time or that the Registrant knows or has reason to know that all four loans are contemplated by the borrower, the total amount of credit that may be extended, exclusive of the amount which is fully secured by the cash surrender value of the life insurance policy, cannot exceed $11,300, or in this particular case, where the sum of $3,900 is to be borrowed on a life insurance policy, the total amount of credit that can be extended is $15,200.

In a case of this kind the statement required to be obtained from the borrower should conform to section 4(d) of the regulation.

• • •

Q. A man builds a house that comes under Regulation X, but borrows on a mortgage on an existing house he presently owns free of encumbrance. It is pretty clear that if he then wants to borrow on the new construction, the amount he can borrow on it is reduced by the amount of the loan on the existing structure. I wonder if this situation does not change with respect to the amount of money to be borrowed on the new house if either the new or the old house is sold.

A. If the old house is sold and the seller continues to be liable on the existing mortgage with respect to that house, the sale has no effect upon the amount of credit which may be outstanding with respect to the new construction; the mortgage on the old house would still be included. If the new house is sold, the outstanding mortgage on the old house would not be relevant to the amount of credit which could be extended to the purchaser of the new house. The purchaser would be entitled to borrow up to the maximum loan value of the new house although, of course, the amount of the mortgage on the new house would have to be con-

sidered in determining the maximum amount which he might borrow if the purchaser assumes the mortgage or takes the property subject to it. The subsequent sale of the old house is not subject to Regulation X even though the mortgage placed on the old house was security for the credit extended to build a new house.

* * *

Real Estate Construction Credit to Finance Major Addition or Major Improvement—Sec. 4(a) (2)

Q. A borrower applies for a $3,600 first mortgage *on a single-family residence.* Out of the proceeds, there are "prior obligations" comprising either:

(a) a first mortgage

(b) an FHA Title I loan

(c) consumer credit obligations or a combination thereof aggregating in total $1,900 to be paid. Balance of the proceeds to be applied to the payment of repairs, improvements or alterations to the property.

Is the application for a mortgage of $3,600 eligible for processing under Regulation X or would Regulation W control because of the fact that the $1,900 prior obligation would be excluded and consideration given only to the repairs and improvements of which 90% could be loaned under Regulation X, resulting in a credit for the repairs and improvements of less than $2,500?

A. If a pre-existing credit with respect to an old house is consolidated with a $1,900 loan for consumer credit obligations and the total credit exceeds $2,500, the loan is outside the provisions of Regulation W unless automobile credit is involved. If the credit to be applied to the payments for repairs, improvements or alterations, exceeds $2,500, it must conform with the provisions of Regulation X.

Assuming that the balance devoted to the payment of repairs, improvements, or alterations does not exceed $2,500 and the consolidated loan exceeds $2,500, Regulation W would not apply; and Regulation X would not apply because that portion for improvements is less than the minimum amount subject to the regulation. *(See sec. 5(a).)*

* * *

Ascertaining Nature of Credit—Sec. 4(c)

Q. Is it necessary (or advisable) to get a Statement of Borrower on all extensions of credit, particularly loans under $2,500, loans with maturities of less than 18 months, or loans to corporations who have maintained an open line of credit with the bank for some time?

A. In the case of any extension of credit by a Registrant, it is required by section 4(c) of the regulation that the Registrant shall be satisfied, and shall maintain records which reasonably demonstrate on their face, whether such credit is or is not real estate construction credit; and a statement by the borrower is one of the means by which this requirement may be met. *Under certain circumstances specified in section 4(c), the requirements of that section do not apply and the Registrant is relieved from the duty to ascertain the nature of the credit. For example, where the Registrant does not have actual knowledge that the credit is real estate construction credit, the requirements of section 4(c) do not apply to any extension of credit in the ordinary course of business for a commercial, agricultural, or business purpose where the Registrant, because of a previous course of dealings or correspondence between himself and the borrower has no reason to believe that the credit is or will be real estate construction credit.* If the credit is in fact real estate construction credit, whether or not exempt from the regulation, the Registrant must obtain a Statement of the Borrower in accordance with *section 4(d)*. A form of Borrower's Statement for this purpose is available at the Federal Reserve Bank, and it will be observed that in the case of an exempt credit only the first two questions need be answered.

* * *

Statement of the Borrower—Sec. 4(d)

Q. Would a short-form Statement of Borrower, rubber stamped on credit application forms, meet the requirements of the regulation? If so, would you suggest an abbreviated statement, practical for such use?

A. A form of statement rubber stamped upon the credit instrument or upon any other papers in connection with the credit and signed by the Registrant stating that he is satisfied that the credit in question is not real estate construction credit would be sufficient. However, if the credit advanced is "real estate construction credit", it might be difficult to consolidate the facts necessary to be stated to fit a short form suitable for a rubber stamp application.

* * *

Q. May the lender rely on a written statement of the builder that construction was started prior to August 3, 1950, or does he have a responsibility to make some kind of an investigation?

A. The Registrant may accept in good faith the signed statement of a builder or borrower as to the date on which construction was begun.

* * *

Q. The Federal Reserve Board issued an interpretation *(see page 10 of this circular)* having to do with statements required from a mortgage company when a loan is made to that mortgage company secured by a pledge of other mortgages. I understand that this interpretation requires a statement from the mortgagor of each pledged mortgage which is subject to the regulation, setting forth the required information, but that the lender may rely upon a signed statement from the mortgage company as to which of the pledged mortgages do and which do not involve "real estate construction credit." In an instance of this kind, is it necessary to take another statement from the mortgage company in which they certify that the proceeds of the loan made to the mortgage company will not be used for "new construction"?

A. With respect to the bank's loan to the mortgage company the bank must comply with the requirements of section 4(c) of the regulation, that is, the Registrant must be satisfied, and maintain records which reasonably demonstrate on their face, whether the credit is or is not real estate construction credit and may accept a Statement of the Borrower for this purpose. In addition, as required by section 4(a)(5) of the regulation the mortgages securing the loan by the bank must conform to the requirements of the regulation and the bank should take steps, as indicated in the interpretation of the Board referred to in the question, to satisfy itself that such mortgages do in fact conform.

* * *

Minimum Amount—Sec. 5(a)

Q. A man owns a one-family house valued at $16,000 on which there is a conventional loan—original amount $11,500—present balance $10,000. He wishes to have a new roof put on which will cost $1,500.

If the mortgage is an open-end instrument, can the lender advance $1,500, less 10% cash down payment (Regulation W) so that the present balance would become $11,350, or does he have to make a special 36-month loan for $1,350?

If it is not an open-end mortgage and the lender and owner wish to recast the older mortgage, can they arrange a new loan of $11,350 ($10,000 plus $1,500, less 10%) payable over a 15-year period (original maturity)?

If the above is not permitted, what action would you suggest where the house requires a new roof and the owner cannot meet his regular monthly payment on the original mortgage and the additional payment on a 36-month modernization loan?

A. In neither case would the credit be controlled by Regulation X because it would be a mixed-purpose loan *(see sec. 6(h))* and the portion subject to the regulation would not exceed $2,500. Regardless of the type of

security, the advance for the new roof properly may be made without restriction if consolidated with the outstanding indebtedness of $10,000 on the old house since Regulation W, except in the case of an automobile credit, does not apply to credit in a principal amount of over $2,500. On the other hand, if the advance for the new roof is handled as a separate obligation, then under Regulation W the 90 per cent maximum loan value requirement would apply and the maximum maturity could not exceed 36 months.

* * *

Q. A man makes home improvements and repairs costing $2,000. He applies to the bank for a mortgage of $2,000 to be repaid over a 20-year period. He has no existing mortgage.

(a) Is this transaction within Regulation W?

(b) Assume that he has a presently existing mortgage of $2,500 and applies for a $4,500 loan to refinance as well as to pay for repairs. Is this within Regulation X? W?

(c) Assume in (b) the existing mortgage is $3,500, making the combined mortgage $5,500.

A. (a) The transaction would violate Regulation W since the improvement and repairs are in connection with an existing structure as specified in Part 1, Group D of the Supplement to Regulation W.

(b) Unless it is made to finance purchase of an automobile, the consolidated loan, if represented by a single obligation, would not be subject to Regulation W because the desired loan plus the outstanding credit with respect to the old property exceeds $2,500. Regulation X would not apply because the portion for improvements would not exceed $2,500.

(c) Same as (b) without the qualification as to automobile credit.

* * *

Q. A borrower applies for a mortgage loan of $1,200 against a *one-family residence* on which there is an existing mortgage loan of $6,200 with which it is proposed the additional loan be consolidated, creating a single lien of $7,400. The proceeds of the additional loan will be used for the construction of a garage.

Is the loan eligible for processing under the provisions of Regulation X?

A. Assuming that the existing mortgage relates to realty on which there is an old house, only that portion of the loan which may be subject to Regulation X need be considered. If the garage is to be attached to the residence, the portion of the credit for the garage would not constitute credit for a major addition or improvement since it is less than

$2,500; if the garage is to be detached the portion for the garage would not be subject to the regulation.

* * *

Short-Term Residential Construction Credits—Sec. 5(b)

Q. If work has not been completed under an 18-month construction loan, can the loan be extended?

A. If the loan has an 18-month maturity, it may not be extended unless, as provided in section 6(e) of the regulation, the loan is in default and is the subject of a bona fide collection effort by the Registrant. If the loan has a maturity of less than 18 months, it may be renewed if the date of the maturity of the renewal is not more than 18 months after the date the credit was originally extended.

* * *

Q. A man builds a house that comes under Regulation X, borrows the full amount permitted in a first mortgage, and then wishes to borrow a $1,000 instalment loan and pay it off within one year. Does the instalment loan come under the exemptions as defined by "short-term *residential* construction credits"? This additional credit is "for the purpose of financing the construction of a residence."
A man is building a new home at a cost of $20,000, and the real estate loan which we have granted upon the property has been computed in accordance with Regulation X. He asked for a temporary commercial loan on stock collateral above the amount allowed by the regulation, which loan would be due in one year and would be repaid from a bonus he will receive from his employer. Is this supplementary loan on the stock collateral regulated, as it falls within the 18-month maturity exemption on temporary loans for "new construction."

A. The situation in both cases is much the same. Assuming that construction of the house has not been completed, the short-term loan, if for the purpose of financing the construction of the residence, would be exempt; but the long-term mortgage loan would have violated the regulation if at that time the Registrant knew or had reason to know that the short-term loan was contemplated by the borrower. *(See sec. 4(b).)*

* * *

Contracts to Sell—Sec. 5(f)

Q. The exemption provided in Regulation X for contracts is not too clear. Does this exemption contemplate only agreements which are actually in purpose a deposit or option? Are contracts for sale, wherein a buyer agrees to make periodic payments for the purchase of property, and later receives deed to it, subject to the regulation?

A. The only purpose of the exemption contained in section 5(f) is to provide that the execution of a simple contract to sell real estate, with merely a deposit of earnest money, would not violate the regulation if the contract is of the kind described in section 5(f). However, the exemption has no application to an extension of credit in connection with the subsequent settlement and transfer of title pursuant to a sales contract.

* * *

Extension of Credit for Mixed Purposes—Sec. 6(h)

Q. A man owns a home valued at $10,000. He has an existing mortgage of $3,000. He desires to make a major addition to his residence costing $5,000 and combine the original mortgage with the money needed for the repairs. What is the largest amount of loan which he can secure under Regulation X?

A. In such cases, assuming the house itself is not new construction, Regulation X requires that the amount and terms of the loan shall be such as would result if the loan were divided into two or more parts on the basis of the purposes of the loan and each part were treated as if it stood alone; and the amount and terms of the loan would comply with Regulation X if they satisfied the requirements of the regulation applicable to that part which is subject to Regulation X. The largest amount of loan that could be secured under the facts given in this problem would be $7,500, $4,500 of which must conform to the amortization and maturity provisions prescribed by the Supplement to this regulation.

* * *

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Questions and Answers