

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 8032]
January 11, 1977

PROPOSED AMENDMENTS TO REGULATION Z

- Discounts for Cash Payment and Surcharges for Credit-Card Payment
—Disclosure of Dealer Participation in Consumer Credit Contracts

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

The Board of Governors of the Federal Reserve System has proposed amendments to its Regulation Z, "Truth in Lending," that would—

- (a) Implement changes and clarifications in the Truth in Lending Act relating to discounts for cash payment and surcharges for the use of credit cards; and
- (b) Require disclosure of the fact that a seller arranging consumer credit may receive part of the finance charge imposed by the creditor.

Comments on the proposals should be made by February 4 and may be sent to our Bank Regulations Department.

The Board of Governors also made a technical correction in the definitions section of the regulation, to clarify the meaning of "open end credit" as used in the section on discounts for payments in cash.

Printed below are the texts of the Board's press statements and Orders relating to the proposals and technical correction. Additional copies of this circular will be furnished upon request.

PAUL A. VOLCKER,
President.

Discounts for Cash Payment

Following is the text of a statement issued December 28, 1976 by the Board of Governors:

The Board of Governors of the Federal Reserve System today issued for public comment a proposed amendment to its Truth in Lending regulation to clarify provisions that permit discounts for cash customers.

Comment should be received by February 4.

The proposal would carry out provisions of Public Law 94-222 that permits discounts for cash purchases, as opposed to surcharges for credit card use. The proposal also specifies that cash discounts are not to be considered charges for credit under the usury or credit card disclosure laws of any State.

At the same time, the Board announced adoption of a technical amendment correcting an error in the Fair Credit Billing section of the Regulation.

The following excerpts from the *Federal Register* of January 4, 1977 contain the texts of the proposal and of the technical correction:

FEDERAL RESERVE SYSTEM

[12 CFR Part 226]

[Reg. Z; Docket No. R-0072]

TRUTH IN LENDING

Discounts for Payment in Cash

Pursuant to the authority contained in the Truth in Lending Act (15 USC 1604), the Board of Governors proposes to amend Part 226 (Regulation Z) to implement changes and clarifications made by Public Law 94-222 which was signed into law on February 27, 1976. One of the purposes of the law was to clarify the fact that section 167 of the Truth in Lending Act (15 USC 1666f) was intended by Congress to exempt discounts of up to five per cent for payment in cash instead of by credit card from disclosure as finance charges but was not intended to provide a similar exemption from disclosure for surcharges of up to five per cent on the use of credit cards. Public Law 94-222 not only provided that surcharges do not qualify for the section 167 exemption from disclosure but also prohibited the imposition of surcharges on the use of credit cards for three years. The clarifying statutory amendments also provided that any discount qualifying under section 167 shall not be considered a charge for credit under State usury, disclosure, and other credit laws.

The proposed amendments to Regulation Z to implement the discount-surcharge provisions of Public Law 94-222 add three new definitions to § 226.2, amend paragraphs (1) (iii) and (4) of § 226.4(i) and add a new paragraph (5) to § 226.4(i). The definitions added are those of "discount," "surcharge," and "regular price." When read in conjunction with these definitions, § 226.4(i) provides that only discounts and not surcharges qualify for the exemption contained in section 167.

The definition of "discount" read together with that of "regular price" is intended to clarify that the price differential resulting from a pricing system in which the merchant tags or posts both a credit card price and a cash price is a discount and qualifies for nondisclosure under section 167. Under these definitions, the following examples of pricing situations would involve "discounts" that would not have to be disclosed if offered in accordance with the requirements of § 226.4(i):

1. Merchant posts or tags goods with a single price which is charged for credit purchases and offers up to a 5 percent discount off this price to cash purchasers.
2. Merchant posts or tags goods with both a credit price and a cash price which is up to 5 percent lower than the credit price.
3. Merchant does not tag or post prices, but offers cash purchasers a price which is up to 5 percent lower than that offered to credit purchasers.

Any pricing system in which the only price tagged or posted is a cash price

which is not available to someone purchasing with a credit card would involve a "surcharge" and would, therefore, be illegal until February 27, 1979.

The proposed amendment to paragraph (1) (iii) of § 226.4(i) would prevent consumers from being misled by a low advertised price when there is an additional charge for credit card purchases. Advertisements promoting goods or services for which a discount for cash is offered would not have to state any price, but if the lower cash price were disclosed, the credit price would also have to be disclosed.

The proposed revision of paragraph (4) of § 226.4(i) makes it clear that it is against the law for merchants to impose surcharges on the use of credit cards until February 27, 1979, even if the amount of the surcharge is disclosed as a finance charge.

The proposed paragraph (5) of § 226.4(i) implements the provision of Public Law 94-222 which states that a discount for payment in cash instead of by credit card which qualifies for the exemption under section 167 shall not be considered a charge for credit for purposes of State laws on usury, credit cost disclosure, and permissible credit charges. This provision was necessary because the fact that such discounts are not considered finance charges for purposes of Truth in Lending has no effect on their treatment under State law. This provision assures that the offering of a discount for cash in accordance with § 226.4(i) will not inadvertently place the merchant or the card issuer in violation of State law.

This notice is published pursuant to section 553(b) of Title 5, United States Code, and § 262.2(a) of the Rules of Procedure of the Board of Governors of the Federal Reserve System (12 CFR 262.2(a)).

Interested persons are invited to submit relevant data, views, or arguments concerning this proposal. Any such material should be submitted in writing to the Secretary, the Board of Governors of the Federal Reserve System, Washington, D.C. 20551, or to any Federal Reserve Bank for transmittal to the Board, to be received at the Board not later than February 4, 1977. Such material will be made available for inspection and copying upon request, except as provided in 12 CFR 261.6(a) of the Board's rules regarding availability of information. Pursuant to the authority granted in 15 U.S.C. 1604, the Board proposes to amend Regulation Z 12 CFR Part 226 as follows:

1. To implement section 3(a) of Public Law 94-222, § 226.2 is amended by adding new paragraphs (tt), (uu) and (vv) as set forth below:

§ 226.2 Definitions and rules of construction.

* * * * *

(tt) The term "regular price" means the tag or posted price charged for

property or a service if a single price is tagged or posted. If two prices for the property or service are tagged or posted, one price which is charged for cash purchases and one which is charged for credit card purchases, or if no price for the property or service is tagged or posted, the "regular price" is the price charged for credit card purchases of the property or service.

(uu) The term "discount," as used in § 226.4(i), means a reduction made from the "regular price," as defined in § 226.2(tt).

(vv) The term "surcharge," as used in § 226.4(i), means an additional charge added to the "regular price," as defined in § 226.2(tt), to arrive at the selling price of property or services for credit card purchases.

§ 226.4 [Amended]

2. To implement sections 3(a) and 3(c) of Pub. L. 94-222, § 226.4(i) is amended as follows:

(a) paragraph (1) (iii) is amended by adding at the end thereof a new sentence as follows:

* * * If a price other than the regular price, as defined in § 226.2(tt), is disclosed in an advertisement, telephone contact, or other correspondence promoting goods or services for which a discount for cash is offered, the regular price shall also be disclosed.

(b) paragraph (4) is revised as follows:

(4) No creditor in any sales transaction may impose a surcharge on a cardholder who elects to use a credit card in lieu of payment by cash, check, or similar means. This paragraph shall cease to be effective on February 27, 1979.

(c) new paragraph (5) is added as follows:

(5) Notwithstanding any other provisions of this Part, any discount for cash which, pursuant to paragraph (1), is not a finance charge for purposes of this Part shall not be considered a finance charge or other charge for credit under the laws of any State relating to:

(i) usury; or

(ii) disclosure of information in connection with credit extensions; or

(iii) the types, amounts, or rates of charges, or the element or elements of charges permissible in connection with the extension or use of credit.

PART 226—TRUTH IN LENDING

Fair Credit Billing; Open End Credit; Discounts for Cash; Correction

In FR Doc. 75-24962 appearing at page 43200 in the FEDERAL REGISTER of September 19, 1975, paragraph (x) of § 226.2 appearing on page 43202 is corrected in the fifteenth line by adding "226.4(i);" after the section symbols (§§) and immediately prior to "226.7(a) (6)".

Pursuant to 5 U.S.C. 533, the Board finds that prior notice of this rulemaking

is unnecessary and that public participation is impractical since, in its view, the change is in the nature of a technical correction clearly mandated by the Truth in Lending Act. § 226.4(i) was inadvertently not included in the enumeration of sections in § 226.2(x) for which "open end credit" shall mean "consumer credit extended on an account by use of a credit card * * *" when the final Fair Credit Billing amendments to Regulation Z were published on September 19. It is essential that § 226.4(i) be included in this enumeration in order for the Regulation

to fully implement section 167 of the Truth in Lending Act which provides that discounts of up to five per cent for payment in cash in lieu of by credit card do not constitute finance charges.

By order of the Board of Governors,
December 27, 1976.

THEODORE E. ALLISON,
Secretary of the Board.

[FR Doc.77-186 Filed 1-3-77;8:45 am]

(Note: In the Regulation Z pamphlet, it is the eighth line of the second column on page 4 that should be corrected as indicated above.)

Disclosure of Dealer Participation

Following is the text of a statement issued December 30, 1976 by the Board of Governors:

The Board of Governors of the Federal Reserve System today issued for comment a proposal to amend its Truth in Lending regulation to require disclosure of a dealer participation in a consumer credit contract.

Comment should be received by the Board by February 4.

Last August the Board proposed an interpretation of the Regulation stating that the amount of a dealer participation need not be separately itemized in Truth in Lending disclosures presented to a customer. The dealer participation, if any, is already a part of the finance charge and annual percentage rate.

In a participation, the seller of a product such as an automobile shares a portion of the finance charge with the creditor who finances the purchase.

Comments received on the interpretation indicated to the Board that some consumer benefit might be derived from disclosure of the existence of a dealer participation. The proposed amendment does not require a separate itemization of the amount of a dealer participation. It would require that the disclosure statement given a customer notify the customer that the seller of the product may receive a portion of the finance charge involved in the transaction.

Final action on the proposed interpretation will be taken when the Board considers final action on the proposed amendment.

Printed below is the text of the Board's proposal:

[Reg. Z; Docket No. R-0053]

TRUTH IN LENDING

Proposed Amendment on Disclosure of Dealer Participation

The Board of Governors of the Federal Reserve System has published for comment a proposed interpretation of Regulation Z relating to the separate disclosure of the portion of the finance charge which is allocated to sellers of consumer goods by a second creditor of a consumer credit transaction. Comments on that proposal have led the Board to believe that separate itemization of the portion of the finance charge payable to the dealer is probably not a necessary disclosure for consumers. However, disclosure of the fact that the seller will receive a portion of the finance charge may be meaningful to consumers wishing to shop for credit or bargain for a better price and possibly should be made a requirement under Regulation Z. To solicit comments on this issue, the Board hereby publishes a proposed amendment to Regulation Z to require disclosure of the fact that a seller may share in the finance charge imposed on consumer credit transactions.

On August 23, 1976, proposed Interpretation §226.821 was published for comment in the *Federal Register* (41 FR 35536). The interpretation relates to the requirements of §226.8(c)(8)(i) of Regulation Z with respect to identification of allocations by creditors to sellers of a portion of the finance charge on credit used to finance the purchase of consumer goods. The amount of seller participation typically represents a portion of the interest component of a finance charge which is paid by a creditor to the seller for arranging or referring a direct loan from the second creditor. For convenient reference, the proposed interpretation is republished below:

§226.821—Disclosure of dealer participation.

(a) Section 226.8(c)(8)(i) requires the itemization of each component of a finance charge consisting of

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

(b) The requirement for itemization of a finance charge which includes a finder's fee or other elements in addition to an interest component is intended to assure that the total finance charge disclosed to the customer properly reflects all components which must be included in that amount. Any component of the finance charge which is computed by the application of a percentage rate or rates to the amount financed constitutes a single charge of the type described in §226.4(a)(1). As such, it must be included in the finance charge calculation and disclosure. A portion of such single component of the finance charge which is distributed to a dealer is not considered a "finder's fee or similar charge" and need not be separately identified or disclosed. The concept of a "finder's fee," as that term is used in §226.4(a)(3), is intended to cover certain charges in the nature of brokerage fees which are imposed in addition to that portion of the finance charge attributable to the application of a percentage rate or rates to the amount financed. Any such separate fee must, of course, be separately itemized. (Interprets and applies 12 C.F.R. Part 226.8.)

The Board has received more than 250 comments on this proposal. Comments from several Federal agencies and consumer representatives have indicated to the Board that certain consumer benefits might be derived from disclosure of the existence of a seller participation. These comments contend that consumer awareness of this element might encourage further comparison of credit terms and greater competition among credit sources. Because these comments suggest that the primary goals of the Truth in Lending Act might be better served by disclosure of this factor, the Board has determined that an amendment to Regulation Z, requiring

such disclosure in the future, should be considered.

The amendment which the Board now proposes does not require separate itemization of the amount of a dealer participation. The Board believes that such an additional requirement would be unduly burdensome and would not significantly enhance consumers' awareness of the credit terms. Instead, the amendment would require that the disclosure statement simply notify the consumer that the seller or some other party to the transaction may receive a portion of the finance charge from the transaction. In the Board's view, disclosure of the fact of a seller participation could alert consumers to the possible benefits of further comparison shopping without unduly complicating the mathematical disclosures now required, and may be of assistance to consumers in evaluating the price offered by the seller.

For the reasons stated above, the Board proposes to amend Regulation Z to require disclosure of the fact that a seller arranging consumer credit may receive a portion of the finance charge imposed on the transaction from a creditor of that transaction. The Board invites written comments on the proposal, to be received not later than February 4, 1977. Comments should be addressed to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, and should include a reference to Docket No. R-0053.

The Board will take final action on the proposed Interpretation §226.821 in connection with its final determination on this proposed amendment.

Pursuant to the authority granted in 15 U.S.C. §1604 (1970), the Board proposes to amend Regulation Z, 12 C.F.R. Part 226 by adding a new §226.8(c)(9) to read as follows:

SECTION 226.8—CREDIT OTHER THAN OPEN END—SPECIFIC DISCLOSURES

* * *

(c) Credit sales.***

* * *

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