

# FEDERAL RESERVE SYSTEM

## 12 CFR Part 226

### [Regulation Z; Docket No. R-1118]

#### Truth in Lending

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

**ACTION:** Proposed rule; official staff commentary.

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**SUMMARY:** The Board is publishing for comment proposed revisions to the official staff commentary to Regulation Z, which implements the Truth in Lending Act. The commentary applies and interprets the requirements of Regulation Z. The proposed update would clarify how creditors that place Truth in Lending Act disclosures on the same document with the credit contract may satisfy the requirement for providing the disclosures in a form the consumer may keep before consummation. In addition, the proposed revisions provide guidance on disclosing costs for certain credit insurance policies and on the definition of “business day” for purposes of the right to rescind certain home-secured loans.

**DATES:** Comments must be received on or before February 1, 2002.

**ADDRESSES:** Comments should refer to Docket No. R-1118 and should be mailed to Ms. Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551, or mailed electronically to [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov). Comments addressed to Ms. Johnson may also be delivered, between 8:45 a.m. and 5:15 p.m., to the Board's mail facility in the West Courtyard, located on 21st Street between Constitution Avenue and C Street, N.W. Members of the public may inspect comments in Room MP-500 of the Martin Building between 9:00 a.m. and 5:00 p.m. on weekdays pursuant to § 261.12, except as provided in § 261.14, of the Board's Rules Regarding Availability of Information, 12 CFR 261.12 and 261.14.

**FOR FURTHER INFORMATION CONTACT:** David A. Stein, Senior Attorney, or Dan S. Sokolov, Attorney; Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, at (202) 452-3667 or 452-2412; for users of Telecommunications Device for the Deaf (“TDD”) only, contact (202) 263-4869.

## **SUPPLEMENTARY INFORMATION:**

### **I. Background**

The purpose of the Truth in Lending Act (TILA; 15 U.S.C. 1601 *et seq.*) is to promote the informed use of consumer credit by providing for disclosures about its terms and cost. The act requires creditors to disclose the cost of credit as a dollar amount (the finance charge) and as an annual percentage rate. Uniformity in creditors' disclosures is intended to assist consumers in comparison shopping for credit. TILA requires additional disclosures for loans secured by consumers' homes and permits consumers to rescind certain transactions that involve their principal dwelling. In addition, the act regulates certain practices of creditors.

TILA is implemented by the Board's Regulation Z (12 CFR part 226). The Board's official staff commentary (12 CFR part 226 (Supp. I)) interprets the regulation, and provides guidance to creditors in applying the regulation to specific transactions. Good faith compliance with the commentary affords protection from liability under section 130(f) of TILA. The commentary is a substitute for individual staff interpretations; it is updated periodically to address significant questions that arise. The Board expects to adopt final revisions to the commentary in March 2002; to the extent the revisions impose new requirements on creditors, compliance would be optional until October 1, 2002, the effective date for mandatory compliance.

### **II. Proposed Revisions**

#### **Subpart A ? General**

#### **Section 226.2 ? Definitions and Rules of Construction**

##### **2(a) Definitions**

##### **2(a)(6) Business Day**

Generally, when consumers have a right to rescind a home-secured loan, they may exercise the right until midnight of the third business day following consummation or the delivery of certain disclosures, whichever occurs last. Comment 2(a)(6)-2 provides that for purposes of rescission, "business day" means all calendar days except Sundays and the federal legal holidays listed in 5 U.S.C. 6103(a). Four legal holidays are identified in that statute by a specific date. Independence Day, July 4, is one example. The comment would be revised to clarify that only the date specified in the statute is considered a legal holiday for purposes of rescission. The proposed comment identifies the four legal holidays in 5 U.S.C. 6103(a) that are defined by a specific date, and provides an example to aid in compliance. The comment also would be amended to include a cross-reference to comment 31(c)(1)-1, which states that creditors may rely on the definition of "business day" used for the rescission rule for purposes of complying with the timing requirements in furnishing disclosures for high-cost loans covered by § 226.32.

## **Section 226.4 ? Finance Charge**

### **4(d) Insurance and Debt Cancellation Coverage**

Under § 226.4(d), amounts paid for credit insurance or debt cancellation coverage may be excluded from the finance charge if the creditor discloses the fee or premium for the initial term of coverage, among other conditions. Comment 4(d)-11 provides that the initial term is based on the period for which the insurer or creditor is initially obligated to provide coverage. Comment 4(d)-12 provides that creditors have the option of providing disclosures on the basis of one year of coverage, where the fee or premium for the coverage is assessed periodically and the consumer is under no obligation to continue the coverage after making the initial payment. Comment 4(d)-12 would be revised to clarify that this option applies even if the consumer can cancel the coverage prior to making the initial payment.

## **Subpart C ? Closed-End Credit**

## **Section 226.17 ? General Disclosure Requirements**

### **17(b) Time of Disclosures**

Creditors must give the required disclosures to the consumer in writing, in a form that the consumer may keep, before consummation of the transaction. See § 226.17(a)(1) and (b). Comment 17(b)-3 would be added to clarify how creditors satisfy this timing requirement when TILA disclosures are placed on the same document with the credit contract, as permitted under comment 17(a)(1)-3.

Questions have been raised about whether creditors must provide consumers with a separate copy of the document to keep before providing a second copy that the consumer may execute to become obligated on the credit contract. The proposed comment would clarify that creditors are not required to provide two separate copies to the consumer. A creditor satisfies the timing requirements by giving the consumer one copy of the unexecuted credit contract containing the disclosures to read and sign. The proposed comment would also clarify that it is not sufficient, however, if the document containing the TILA disclosures is merely shown to the consumer (and not given to the consumer) before the consumer signs and becomes obligated.

## **III. Form of Comment Letters**

Comment letters should refer to Docket No. R-1118, and, when possible, should use a standard typeface with a font size of 10 or 12. This will enable the Board to convert text submitted in paper form to machine-readable form through electronic scanning, and will facilitate automated retrieval of comments for review. Also, if accompanied by an original document in paper form, comments may be submitted on 3 1/2 inch computer diskettes in any IBM-compatible DOS- or Windows-based format. Comments may also be mailed electronically to [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov).

**IV. Solicitation of Comments Regarding the Use of “Plain Language”**

Section 722 of the Gramm-Leach-Bliley Act of 1999 requires the Board to use “plain language” in all proposed and final rules published after January 1, 2000. The Board invites comments on whether the proposed commentary is clearly stated and effectively organized, and how the Board might make the commentary easier to understand.

**List of Subjects in 12 CFR Part 226**

Consumer protection, Disclosures, Federal Reserve System, Truth in lending.

**Text of Proposed Revisions**

Certain conventions have been used to highlight the proposed revisions to the text of the staff commentary. New language is shown inside bold-faced arrows while language that would be deleted is set off with bold-faced brackets. Comments are numbered to comply with Federal Register publication rules.

For the reasons set forth in the preamble, the Board proposes to amend 12 CFR part 226 as follows:

**PART 226 -- TRUTH IN LENDING (REGULATION Z)**

- 1. The authority citation for part 226 would continue to read as follows:

**Authority:** 12 U.S.C. 3806; 15 U.S.C. 1604 and 1637(c)(5).

- 2. In Supplement I to Part 226, the following amendments would be made:
  - a. Under Section 226.2? Definitions and Rules of Construction, under 2(a)(6) Business Day, paragraph 2. would be revised.
  - b. Under Section 226.4? Finance Charge, under 4(d) Insurance and Debt Cancellation Coverage, paragraph 12. would be revised.
  - c. Under Section 226.17? General Disclosure Requirements, under 17(b) Time of Disclosures, a new paragraph 3. would be added.

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**SUPPLEMENT I TO PART 226—OFFICIAL STAFF INTERPRETATIONS**

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**SUBPART A? GENERAL**

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Section 226.2? Definition and Rules of Construction

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2(a)(6) Business day.

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2. Rescission rule. A more precise rule for what is a business day (all calendar days except Sundays and the federal legal holidays listed in 5 U.S.C. 6103(a)) applies when the right of rescission ? or mortgages subject to § 226.32 are involved. See also comment 31(c)(1)-1. Four federal legal holidays are identified in 5 U.S.C. 6103(a) by a specific date: New Year's Day, January 1; Independence Day, July 4; Veteran's Day, November 11; and Christmas Day, December 25. When one of these holidays falls on a Saturday, July 4 for example, federal offices and other entities may observe the holiday on the preceding Friday, July 3. The observed holiday, July 3, is a business day for purposes of rescission or the delivery of disclosures for certain high-cost mortgages covered by § 226.32? [is involved].

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Section 226.4? Finance Charge

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4(d) Insurance and debt cancellation coverage.

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12. Initial term; alternative. i. General. A creditor has the option of providing cost disclosures on the basis of ? an assumed initial term of? one year of insurance or debt-cancellation coverage instead of a longer initial term (provided the premium or fee is clearly labeled as being for one year) if:

A. The initial term is indefinite or not clear, or

B. The consumer has agreed to pay a premium or fee that is assessed periodically but the consumer is under no obligation to continue the coverage after ? consummation? [making the initial payment].

ii. Open-end plans. For open-end plans, a creditor also has the option of providing unit-cost disclosure on the basis of a period that is less than one year if the consumer has agreed to pay a premium or fee that is assessed periodically, for example monthly, but the consumer is under no obligation to continue the coverage.

iii. Examples. To illustrate:

A. A credit life insurance policy providing coverage for a 30-year mortgage loan has an initial term of 30 years even though premiums are paid monthly and the consumer is not required

to continue the coverage after ? consummation? [making the initial payment]. The creditor has the option of making disclosures on the basis of coverage for ? an assumed initial term of one year.

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SUBPART C? CLOSED-END CREDIT

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Section 226.17? General Disclosure Requirements

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17(b) Time of disclosures.

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? 3. Disclosures provided on credit contracts. Creditors must give the required disclosures to the consumer in writing, in a form that the consumer may keep, before consummation of the transaction. See § 226.17(a)(1) and (b). Sometimes the disclosures are placed on the same document with the credit contract, as permitted under comment 17(a)(1)-3. In such cases, the timing requirement is satisfied if the creditor gives a copy of the document containing the unexecuted credit contract and the disclosures to the consumer to read and sign, and the consumer is free to take possession of and review the document in its entirety before signing. It is not sufficient, however, if the document containing the disclosures is merely shown to the consumer before the consumer signs and becomes obligated; the creditor must give the document to the consumer. If after receiving the document, the consumer signs it and becomes obligated, the consumer may return it to the creditor to execute or process, provided the consumer is also given a copy at that time to keep.?

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By order of the Board of Governors of the Federal Reserve System, acting through the Director of the Division of Consumer and Community Affairs under delegated authority, December 7, 2001.

(signed) Jennifer J. Johnson\_\_\_\_\_

Jennifer J. Johnson  
Secretary of the Board