FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Docket No. R–1366]

Regulation Z; Truth in Lending

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Interim rule; request for public comment.

SUMMARY: The Board is publishing for comment an interim rule amending Regulation Z, which implements the Truth in Lending Act (TILA). The interim rule implements certain requirements of the Mortgage Disclosure Improvement Act of 2008, which amended TILA. The amendments and this interim rule require creditors extending consumer credit secured by real property or a dwelling to disclose certain summary information about interest rates and payment changes, in a tabular format, as well as a statement that consumers are not guaranteed to be able to refinance their transactions in the future. The interest rate and payment summary tables replace the payment schedule previously required as part of the TILA disclosure for mortgage transactions. Disclosures for non-mortgage, closed-end consumer credit will continue to include the current payment schedule.

DATES: This interim rule is effective October 25, 2010. Compliance with its requirements is optional, however, until January 30, 2011; its requirements are mandatory for transactions for which an application for credit is received by the creditor on or after that date. Comments on this interim rule must be received on or before November 23, 2010.

ADDRESSES: You may submit comments, identified by Docket No. R–1366, by any of the following methods:

- *Agency Web site: http://www.federalreserve.gov.* Follow the instructions for submitting comments at *http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm.*
- *Federal eRulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.
- *E-mail: regs.comments@federalreserve.gov.* Include the docket number in the subject line of the message.
- *Fax:* (202) 452–3819 or (202) 452–3102.
- *Mail:* Address to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551.

All public comments will be made available on the Board's Web site at *http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm* as submitted, unless modified for technical reasons. Accordingly, comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper in Room MP–500 of the Board's Martin Building (20th and C Streets, NW.,) between 9 a.m. and 5 p.m. on weekdays.

FOR FURTHER INFORMATION CONTACT: Paul Mondor, Senior Attorney, or Kathleen C. Ryan, Senior Counsel, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, DC 20551, at (202) 452–2412 or (202) 452–3667. For users of Telecommunications Device for the Deaf (TDD) only, contact (202) 263–4869.

SUPPLEMENTARY INFORMATION:

I. Background

A. TILA and Regulation Z

Congress enacted the Truth in Lending Act (TILA) based on findings that economic stability would be enhanced and competition among consumer credit providers would be strengthened by the informed use of credit resulting from consumers' awareness of the cost of credit. One of the purposes of TILA is to provide meaningful disclosure of credit terms to enable consumers to compare credit terms available in the marketplace more readily and avoid the uninformed use of credit.

TILA's disclosures differ depending on whether credit is an open-end (revolving) plan or a closed-end (installment) loan. TILA also contains procedural and substantive protections for consumers. TILA is implemented by the Board's Regulation Z. An Official Staff Commentary interprets the requirements of Regulation Z. By statute, creditors that follow in good faith Board or official staff interpretations are insulated from civil liability, criminal penalties, and administrative sanction.

B. MDIA Amendments to TILA and Regulation Z

On July 30, 2008, Congress enacted the Mortgage Disclosure Improvement Act of 2008 (the MDIA).[1] The MDIA requires transaction-specific TILA disclosures to be provided within three business days after an application is received and before the consumer has paid a fee, other than a fee for obtaining the consumer's credit history.[2] In addition, the MDIA requires creditors to mail or deliver early TILA disclosures at least seven business days before consummation and provide corrected disclosures if the disclosed APR changes in excess of a specified tolerance. The consumer must receive the corrected disclosures no later than three business days before consummation. The MDIA also expanded coverage of the early disclosure requirement to include loans secured by a dwelling even when it is not the consumer's principal dwelling. The Board implemented these MDIA requirements in final rules published May 19, 2009, and effective July 30, 2009. 74 FR 23289, May 19, 2009 (MDIA Final Rule).

The MDIA also requires disclosure of payment examples if the loan's interest rate or payments can change. Such disclosures are to be formatted in accordance with the results of consumer testing conducted by the Board. And the MDIA requires disclosure of a statement that there is no guarantee the consumer will be able to refinance the transaction in the future. Those provisions of the MDIA become effective on January 30, 2011, or any earlier compliance date established by the Board. This interim rule implements those MDIA provisions.

C. The Board's Review of Closed-End Credit Rules

The Board's current review of Regulation Z was initiated in December 2004 with an advance notice of proposed rulemaking. 69 FR 70925, Dec. 8, 2004. At that time, the Board announced its intent to conduct its review of Regulation Z in stages, focusing first on the rules for open-end (revolving) credit accounts that are not home-secured, chiefly general-purpose credit cards and retailer credit card plans. In December 2008, the Board approved final rules for open-end credit that is not home-secured. 74 FR 5244, Jan. 29, 2009. In May 2009, Congress enacted the Credit Card Accountability Responsibility and Disclosure Act of 2009 (Credit Card Act), which amended TILA's provisions for open-end credit. The Board approved final rules

[1] The MDIA is contained in Sections 2501 through 2503 of the Housing and Economic Recovery Act of 2008, Public Law 110–289, enacted on July 30, 2008. The MDIA was later amended by the Emergency Economic Stabilization Act of 2008, Public Law 110–343, enacted on October 3, 2008.

[2] To ease discussion, the description of the closed-end mortgage disclosure scheme includes MDIA's amendments to TILA and the disclosure timing requirements implemented by the Board in 2008 through a final rule that preceded MDIA's enactment. 73 FR 44522, July 30, 2008 (2008 HOEPA Final Rule). The MDIA codified some of the 2008 HOEPA Final Rule and expanded its coverage and its requirements. The MDIA also made these requirements effective July 30, 2009.

implementing the Credit Card Act in January and June 2010. 75 FR 7658, Feb. 22, 2010; 75 FR 37526, June 29, 2010.

Beginning in 2007, the Board proposed revisions to the rules for home-secured credit in several phases. In 2007, the Board proposed rules for closed-end higher-priced mortgage loans secured by the consumer's principal dwelling, leading to the HOEPA Final Rule. On May 7, 2009, the Board adopted the MDIA Final Rule for closed-end loans secured by a dwelling. On July 23, 2009, the Board issued a proposed rule to revise the rules for disclosures for closed-end credit secured by real property or a consumer's dwelling. 74 FR 43232, Aug. 26, 2009 (2009 Closed-End Proposal). The Board also issued a proposed rule to revise the rules for disclosures for open-end lines of credit secured by a dwelling. 74 FR 43428, Aug. 26, 2009. Concurrently with this interim rule, the Board is publishing another proposed rule that would add and revise rules for rescission, reverse mortgages, and modifications to existing closed-end mortgage loans (2010 Closed-End Proposal).

D. Consumer Testing

A principal goal for the Regulation Z review is to produce revised and improved mortgage disclosures that consumers will be more likely to understand and use in their decisions, while at the same time not creating undue burdens for creditors. In 2007, the Board retained a research and consulting firm (ICF Macro) that specializes in designing and testing documents to conduct consumer testing to help the Board's review of mortgage rules under Regulation Z. Working closely with the Board, ICF Macro conducted several tests in different cities throughout the United States. The testing consisted of four focus groups and eleven rounds of one-on-one cognitive interviews. The goals of these focus groups and interviews were to learn how consumers shop for mortgages and what information consumers read when they receive mortgage disclosures, and to assess their understanding of such disclosures.

The consumer testing groups contained participants with a range of ethnicities, ages, educational levels, and mortgage-shopping behaviors, including first-time mortgage shoppers, prime and subprime borrowers, and consumers who had obtained one or more closed-end mortgages. For each round of testing, ICF Macro developed a set of model disclosure forms to be tested. Interview participants were asked to review model forms and provide their reactions, and were then asked a series of questions designed to test their understanding of the content. Data were collected on which elements and features of each form were most successful in providing information clearly and effectively. The findings from each round of interviews were incorporated in revisions to the model forms for the following round of testing. Several of the model forms included in the 2009 Closed-End Proposal were developed through the testing. A report summarizing the results of the testing is available on the Board's public Web site: *http://www.federalreserve.gov/boarddocs/meetings/2009/20090723/Full%20Macro%20CE%20Report.pdf.*

II. Summary of the Interim Rule

MDIA requires creditors to disclose examples of rates and payments, including the maximum rate and payment, for loans with variable rates or payments. MDIA also requires creditors to disclose a statement that consumers should not assume they can refinance their loans. The 2009 Closed-End Proposal included provisions that would implement these MDIA requirements, including provisions interpreting the statute's requirement that creditors disclose "examples" of payment adjustments other than the maximum during the life of the loan and the "no-guarantee-to-refinance" statement. Those provisions, proposed §§ 226.38(c) and 226.38(f)(3), respectively, would require the TILA disclosure to contain certain interest rate and payment summary tables and the "no-guarantee-to-refinance" statement. *See* 74 FR 43232, 43334–35 and 43337, Aug. 26, 2009. The Board does not expect to finalize that proposal, however, before the January 30, 2011 statutory effective date of the MDIA requirement to disclose examples of payment adjustments. Accordingly, this interim rule implements the MDIA requirements now, so that mortgage creditors will have the guidance necessary to comply with them by January 30, 2011. This interim rule adopts the provisions of the 2009 Closed-End Proposal requiring disclosure of interest rate and payment summary tables as proposed, except as discussed below and with minor modifications for clarity.

Under this interim rule, creditors will be required to disclose in a tabular format the contract interest rate together with the corresponding monthly payment, including any escrows for taxes and property and/or mortgage insurance. Special disclosure requirements are imposed for adjustable-rate or step-rate loans to show the interest rate and payment at consummation, the maximum interest rate and payment at any time during the first five years after consummation, and the maximum interest rate and payment possible during the life of the loan. Additional special disclosures are required for loans with negatively-amortizing payment options, introductory interest rates, interest-only payments, and balloon payments. Finally, the interim rule requires the disclosure of a statement that there is no guarantee the consumer will be able to refinance the loan with a new transaction in the future.

III. Legal Authority

A. Rulemaking Authority

TILA Section 105(a) directs the Board to prescribe regulations to carry out the Act's purposes. 15 U.S.C. 1604(a). TILA also authorizes the Board to issue regulations that contain such classifications, differentiations, or other provisions, or that provide for such adjustments and exceptions for any class of transactions, that in the Board's judgment are necessary or proper to effectuate the purposes of TILA, facilitate compliance with the act, or prevent circumvention or evasion. MDIA also specifically provides that the disclosures shall be in accordance with the Board's implementing regulations, as discussed above.

B. Authority To Issue Interim Rule

The Administrative Procedures Act (APA), 5 U.S.C. 551 *et seq.,* generally requires public notice before promulgation of regulations. *See* 5 U.S.C. 553(b). The 2009 Closed-End Proposal provided the public with notice and an opportunity to comment on the Board's proposed disclosure changes, including the proposed interest rate and payment summary tables. The Board is now adopting only that aspect of the 2009 Closed-End Proposal. The Board therefore believes this action complies with the APA's public notice and opportunity to comment requirement. The Board is adopting the provisions concerning interest rates and payments as an interim rule, rather than as a final rule, because the Board intends to conduct additional testing of this and other disclosure requirements, including quantitative testing, and may revise these interim provisions further in light of further testing results. The interim rule will permit further public comment while also giving the provisions effect so that creditors will have the guidance they need and the time to implement it by January 30, 2011, as discussed above.

C. Authority for October 25, 2010 Effective Date

TILA Section 105(d) generally provides that a regulation requiring any disclosure that differs from the disclosures previously required shall have an effective date no earlier than "that October 1 which follows by at least six months the date of promulgation." 15 U.S.C. 1604(d). This interim rule substitutes the interest rate and payment summary tables for the existing payment schedule in the TILA disclosure requirements, effective October 25, 2010 and with compliance mandatory as of January 30, 2011. The new requirements will take effect, however, on January 30, 2011 pursuant to the MDIA, with or without this rulemaking. To the extent that the interim rule contains disclosure requirements that are already in effect on January 30, 2011 under the statute, TILA Section 105(d) does not apply. Moreover, the Board believes that the effective date mandated by the MDIA for the specific disclosures required under TILA Section 128(b)(2)(C) overrides the general provision in TILA Section 105(d).

IV. Overview of Comments Received on the Interest Rate and Payment Summary Tables

The Board received over 6,000 comments on the 2009 Closed-End Proposal. The great majority of those, however, were from mortgage brokers, loan officers, and other mortgage industry representatives that commented exclusively on the proposed regulation of loan originator compensation. Those commenters who commented on proposed § 226.38, which contained the new disclosure requirements, focused their comments more extensively on other provisions in the August 2009 Closed-End Proposal, not on §§ 226.38(c) and 226.38(f)(3). Consequently, the Board received little comment specifically on the proposed interest rate and payment summary tables, and no commenters addressed the proposed no guarantee to refinance statement.

Six consumer and community groups commented jointly on the proposal. Regarding the interest rate and payment summary proposal, they expressed strong support for including a statement of the maximum payment. These commenters indicated that the table was flawed, however, as applied to negative amortization products because the resulting table is too different to permit comparison between amortizing and negatively amortizing adjustable-rate mortgages. The consumer groups also stated that the payments in the table should reflect estimated taxes and insurance regardless of whether an escrow account is required because the need for monthly budgeting for those obligations should be emphasized. These groups also criticized the manner in which the maximum possible payment was calculated for the sample forms included in the proposal.

Mortgage creditors offered suggested revisions to the proposed interest rate and payment summary requirements, including a revision that would emphasize the fact that escrow amounts are estimated. Most creditors, though not all, agreed with the consumer advocates that estimated taxes and insurance should be included regardless of whether an escrow account is required. Some strongly questioned the need for some of the graphical details of the model forms, such as the large arrow pointing downward to highlight the additional amount borrowed by making only minimum payments on a negative amortization loan and the use of shading and highlighting. One bank indicated that the content of the table would be duplicative of the information presented in the good faith estimate of settlement costs and the HUD–1 settlement statement required under Regulation X, which implements the Real Estate Settlement Procedures Act (RESPA), but that the information is presented differently. This commenter also questioned the inclusion of taxes and insurance in any but the initial payment disclosed because of the fact that those amounts can change significantly over the life of the loan.

In general, as discussed below, the Board has considered the comments received and is adopting the interest rate and payment summary table and the no-guarantee-to-refinance statement as proposed, with minimal modification. As stated above, the Board intends to conduct additional testing and will consider the comments further as part of the testing process. The Board is reluctant at this time, however, to make significant changes to the format and content of the tables without the benefit of such testing. To afford guidance on how to comply with the MDIA requirements by the January 30, 2011 statutory effective date, the Board is adopting these requirements substantially as proposed. The Board also seeks additional comment on the summary tables under this interim rule.

V. Section-by-Section Analysis

Section 226.17 General Disclosure Requirements

17(a) Form of Disclosures

17(a)(1)

Comment 17(a)(1)–1 provides guidance on the general requirement that the TILA disclosures be clear and conspicuous. The comment currently states that no minimum type size is mandated for the disclosures. This interim rule amends the comment by adding a parenthetical exception to that general rule, to conform to the fact that new § 226.18(s), discussed below, requires a minimum 10-point type size.

Section 226.18 Content of Disclosures

18(g) Payment Schedule

The interim rule makes a conforming amendment to § 226.18(g). That section imposes the current payment schedule disclosure for closed-end consumer credit. As discussed below, § 226.18(s) replaces the payment schedule with the new interest rate and payment summary table for a transaction secured by real property or a dwelling, other than a transaction secured by a consumer's interest in a timeshare plan. Thus, § 226.18(g) is amended to exclude such transactions from its coverage.

18(s) Interest Rate and Payment Summary for Mortgage Transactions

This interim rule adopts a new § 226.18(s), which provides requirements for disclosure of the contract interest rate and the periodic payment for most transactions secured by real property or a dwelling. The information required by § 226.18(s)(2)–(4) must be in the form of a table, as provided in § 226.18(s)(1), substantially similar to Model Clause H–4(E), H–4(F), H–4(G), or H–4(H) in Appendix H. As noted above, some industry commenters on the 2009 Closed-End Proposal questioned the use of shading in the proposed model forms. The Board recognizes these commenters' concern that shading can undermine the forms' legibility when they are photocopied or faxed. By requiring that disclosures be "substantially similar" to the models, however, the Board does not intend that disclosures must include any shading that the models contain. Comment 18(s)–1 therefore clarifies that a disclosure that does not include the shading shown in a model clause but otherwise follows the model clause's headings and format is substantially similar to that model clause.

The rules for disclosing the interest rate and periodic payments for an amortizing loan are provided in

§§ 226.18(s)(2)(i) and 226.18(s)(3). Rules for disclosing the interest rate and periodic payments for a loan with negative amortization are in §§ 226.18(s)(2)(ii) and 226.18(s)(4). Special rules for disclosing balloon payments are found in § 226.18(s)(5). Additional explanations of introductory rates and negative amortization are required by §§ 226.18(s)(2)(iii) and 226.18(s)(6), respectively. Finally, § 226.18(s)(7) provides definitions for certain terms used in § 226.18(s).

Existing Requirements for Periodic Payments

TILA Section 128(a)(6) requires the creditor to disclose the number, amount, and due dates or period of payments scheduled to repay the total of payments, for closed-end credit. 15 U.S.C. 1638(a)(6). Currently, § 226.18(g) implements TILA Section 128(a)(6). Under § 226.18(g), creditors must show the number, amounts, and timing of payments scheduled to repay the obligation, except as provided in § 226.18(g)(2) for certain loans with varying payments.[3]

Comment 18(g)–1 provides that the payment schedule should include all components of the finance charge, not just interest. Thus, if mortgage insurance is required, the payment schedule must reflect the consumer's mortgage insurance payments until the date on which the creditor must automatically terminate coverage under applicable law. See comment 18(g)–5. Commentary to § 226.17(c) provides that, for an adjustable-rate loan, creditors should disclose the payments and other disclosures based only on the initial rate and should not assume that the rate will increase. The disclosures must reflect a discounted or premium initial interest rate, however, for as long as it is charged. The commentary permits, but does not require, creditors to include in the payments amounts that are not finance charges or part of the amount financed. Thus, creditors may, but need not, include insurance premiums excluded from the finance charge under § 226.4(d), and "real estate escrow amounts such as taxes added to the payment in mortgage transactions."

Effect of MDIA amendments. TILA Section 128(b)(2)(C), as added by the MDIA, requires additional disclosures for loans secured by a dwelling in which the interest rate or payments may vary. 15 U.S.C. 1638(b)(2)(C). Specifically, creditors must provide "examples of adjustments to the regular required payment on the extension of credit based on the change in the interest rates specified by the contract for such extension of credit. Among the examples required * * * is an example that reflects the maximum payment amount of the regular required payments on the extension of credit, based on the maximum interest rate allowed under the contract. * * *" 15 U.S.C. 1638(b)(2)(C).

TILA Section 128(b)(2)(C) provides that these examples must be in conspicuous type size and format and that the payment schedule be labeled "Payment Schedule: Payments Will Vary Based on Interest Rate Changes." TILA Section 128(b)(2)(C) requires the Board to conduct consumer testing to determine the appropriate format for providing the disclosures to consumers so that the disclosures can be easily understood, including the fact that the initial regular payments are for a specific time period that will end on a certain date, that payments will adjust afterwards potentially to a higher amount, and that there is no guarantee that the borrower will be able to refinance to a lower amount. 15 U.S.C. 1638(b)(2)(C). As discussed above, the Board conducted the required testing and, based on the results and other analysis, developed the mortgage disclosures contained in the 2009 Closed-End Proposal, including those aspects now being adopted in this interim rule.

The Interim Rule

The Board is adding new § 226.18(s) to implement TILA Section 128(a)(6) and Section 128(b)(2)(C) for most closed-end transactions secured by real property or a dwelling.[4] For all other closed-end credit transactions, § 226.18(g) continues to provide the rules for disclosing payments. Section 226.18(s) requires creditors to disclose the contract interest rate, regular periodic payment, and balloon payment if applicable. For adjustable-rate or step-rate amortizing loans, up to three interest rates and corresponding periodic payments are required, including the maximum possible interest rate and payment. If payments are scheduled to increase independent of an interest-rate adjustment, the increased payment must be disclosed. Payments for amortizing loans must separately itemize an estimate of the amount for taxes and insurance if the creditor will establish an escrow account. If a borrower may make one or more payments of interest only, all payment amounts disclosed must be itemized to show the amount that will be applied to interest and the amount that will be applied to principal. Special rate and payment disclosures are required for loans with negative amortization. Creditors must provide the information about interest rates and payments in the form of a table, and creditors are not permitted to include other, unrelated information in the table.

Scope of § 226.18(s). TILA Section 128(b)(2)(C) applies to all transactions secured by a dwelling, other than transactions secured by timeshare plans (discussed below). The Board proposed to expand the requirement in Section 128(b)(2)(C) to include loans secured by real property that do not include a dwelling and is now adopting that proposal. Thus, transactions secured by real property with no dwelling or other structure built thereon would be subject to the enhanced disclosures, assuming such transactions are consumer credit. Some creditors commented on the proposed expansion of the scope of the MDIA requirements, questioning its necessity. As discussed in the 2009 Closed-End Proposal, however, unimproved real property is likely to be a significant asset for most consumers, and consumers should receive the disclosures required in Section 128(b)(2)(C) before they become obligated on a loan secured by such an asset. The disclosures will alert consumers to the potential for interest rate and payment increases and help them to determine whether these risks are appropriate to their circumstances. The Board also believes that consistent disclosure requirements for all mortgage-secured, closed-end, consumer credit transactions, whether they include a dwelling or not, should ease compliance burdens for mortgage creditors.

The Board is adopting this adjustment to TILA Section 128(b)(2)(C) pursuant to its authority under TILA Section 105(a). 15 U.S.C. 1604(a). Section 105(a) authorizes the Board to make exceptions and adjustments to TILA for any class of transactions to effectuate the statute's purposes, which include facilitating consumers' ability to compare credit terms and helping consumers avoid the uninformed use of credit. 15 U.S.C. 1601(a), 1604(a). The class of transactions that would be affected is transactions secured by real property or a dwelling. As discussed, providing

[3] For a mortgage transaction with rates or fees that exceed certain thresholds, TILA Section 129 requires special disclosures regarding payments three business days before consummation of the transaction. *See* § 226.32(c)(3), (4). The Board is not revising those disclosures in this interim rule.

[4] TILA Section 128(b)(2)(C) also provides that the Board's testing should ensure that consumers can understand that there is no guarantee that they will be able to refinance. New § 226.18(t), discussed below, implements this aspect of Section 128(b)(2)(C).

examples of increased interest rates and payments will help consumers understand the risks involved in certain loans. The Board believes that this adjustment is proper to ensure that consumers receive meaningful disclosures that facilitate their informed use of credit.

Timeshare plans. TILA Section 128(b)(2)(G), as added by MDIA, excludes from the coverage of Section 128(b)(2)(C) an extension of credit secured by a timeshare plan. 15 U.S.C. 1638(b)(2)(G). Thus, the interim rule excludes these transactions from coverage of § 226.18(s).[5] This exclusion does not affect the determination of whether such transactions are subject to Regulation Z and § 226.18; if they are subject to that section, they must include the payment schedule under § 226.18(g).

Reverse mortgages. Section 226.18 currently applies to reverse mortgages. Reverse mortgages have unique features that make the disclosures in § 226.18, including the current payment schedule under § 226.18(g), difficult to apply and potentially confusing to consumers. The same is true of the new interest rate and payment summary tables required by this interim rule under § 226.18(s). Simultaneously with this interim rule, the Board is proposing improved comprehensive disclosure requirements tailored to closed- and open-end reverse mortgages. When those disclosures are adopted in final form, the Board anticipates that it also will exclude reverse mortgages from the coverage of the closed-end mortgage disclosure requirements. In the meantime, the Board is excluding reverse mortgages from the definition of "negative amortization mortgage" under § 226.18(s)(7) because the special interest rate and payment summary requirements for negative amortization mortgages, discussed below, would be especially unworkable for reverse mortgages and also especially likely to cause consumer confusion. Virtually all reverse mortgages being made in the market currently are, to the Board's knowledge, fixed-rate loans. Consequently, under the requirements discussed below, reverse mortgages would be disclosed under the relatively straightforward fixed-rate summary table requirements of §§ 226.18(s)(2)(i) and 226.18(s)(3).

[5] Credit secured by a timeshare plan is also excluded from MDIA's other requirements. Accordingly, the MDIA Final Rule excluded from the new timing, corrected disclosure, and related requirements a transaction "that is secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53D)." *See* § 226.19(a)(5).

Fixed-rate, fixed-payment loans. TILA Section 128(b)(2)(C) applies by its terms only to mortgages where the rate, payment, or both may change after consummation. Accordingly, the Board could apply the new interest rate and payment summary requirements to only such mortgages and leave fixed-rate, fixed-payment mortgages subject to § 226.18(g). The Board believes, however, that applying § 226.18(s) to all mortgages will simplify compliance for creditors and make comparing different loan products more straightforward for consumers. Accordingly, the interest rate and payment summary table is required for all transactions secured by real property or a dwelling, including fixed-rate, fixed-payment mortgages. The Board is adopting this requirement pursuant to its authority under TILA Section 105(a) to effectuate the purposes of TILA. 15 U.S.C. 1604(a).

Payment schedule label. The Board proposed in the 2009 Closed-End Proposal to revise the label for the interest rate and payment information from the text set out in the statute. The Board proposed to replace the statutory language, "Payment Schedule: Payments Will Vary Based on Interest Rate Changes," with "Interest Rate and Payment Summary" based on plain language principles, to make the disclosure more readily understandable. The Board is now adopting that proposal. The Board is making this adjustment pursuant to the same TILA Section 105(a) authority, and for the same class of transactions, as discussed above with respect to transactions subject to § 226.18(s).

Disclosure of the interest rate. Currently, TILA does not require disclosure of the contract interest rate for closed-end credit. In the consumer testing conducted for the Board, when consumers were asked what factors they considered when looking for a mortgage, the most common answers consumers provided were that they wanted to obtain the lowest interest rate possible and that they wanted the loan with the lowest possible monthly payment. Nevertheless, as they described their thought process, most consumers were primarily focused on the initial rate and payment, rather than how those terms might vary over time.

In addition, testing indicated that the current TILA payment schedule, which does not show the relationship between the interest rate and payments, is ineffective at communicating to consumers what could happen to their payments over time with an adjustable-rate mortgage. Most participants said they liked the current presentation of the payments because it was specific and detailed. When shown a payment schedule for an adjustable-rate mortgage with an introductory rate, however, many incorrectly assumed that payments shown were in fact their future payments, rather than payments based on the fully-indexed rate at consummation.

Under the Board's interim rule, the interest rate and payment are shown together in a table. The Board believes that highlighting the relationship between the interest rate and payment will enhance consumers' understanding of loan terms. If the interest rate is adjustable, the table indicates changes in the interest rate over time. In addition, payment changes that are not based on adjustments to the interest rate are indicated in the table. Highlighting potential changes to the interest rate and payment based on maximum interest rate increases, rather than showing a set payment schedule based on the assumption that the index used to calculate an adjustable interest rate will not change, will clarify to consumers not only *that* their interest rate and payments may change, but also *how* the interest rate and payment may change over time. Consumers will be better able to determine if an adjustable-rate loan will be affordable and appropriate for their individual circumstances.

Definitions for § 226.18(s). Section 226.18(s) uses several terms that are defined in § 226.18(s)(7). Under § 226.18(s)(7), the term "adjustable-rate mortgage" means a loan in which the annual percentage rate may increase after consummation. The term "step-rate mortgage" means a loan in which the interest rate will change after consummation, and the rates and periods in which they will apply are known. The term "fixed-rate mortgage" means a loan that is not adjustable-rate or step-rate. The term "interest-only" means that one or more periodic payments may be applied solely to interest and not to loan principal; an "interest-only loan" is a loan that permits interest-only payments. An "amortizing loan" is defined as a loan in which the regular periodic payments cannot cause the principal balance to increase; the term "negative amortization" means the regular periodic payments may cause the principal balance to increase; the term "negative amortization loan" means a loan with a negative amortization feature but explicitly excludes a reverse mortgage, as discussed above. Finally, the term "fully-indexed rate" means the interest rate calculated using the index value and margin.

18(s)(1)

Section 226.18(s)(1) requires the interest rate and payment information to be disclosed in the form of a table. This will ensure that payment examples required by the MDIA are in conspicuous format as required by TILA Section 128(b)(2)(C). The MDIA also requires conspicuous type size for the examples. Under § 226.18(s)(1), the table must be in a minimum 10-point font to ensure that it is clear and conspicuous.

The interim rule prescribes the number of interest rates and payments that may be shown in the table. The number of columns and rows for the table required by § 226.18(s) will vary depending on whether the loan is an amortizing loan and whether it has an adjustable rate. In all cases, § 226.18(s)(1) provides that the tables must have no more than five columns across, to avoid information overload for consumers. Creditors may not include information in the table that is not required under 226.18(s), to avoid information overload. Model clauses are provided in Appendix H.

18(s)(2) Interest Rates

18(s)(2)(i) Amortizing Loans

Section 226.18(s)(2)(i) requires disclosure of interest rates for amortizing loans. For a fixed-rate mortgage with no scheduled payment increases or balloon payments, the creditor discloses only one interest rate. Fixed-rate loans with payment increases require the creditor to disclose the interest rate along with each payment increase, even if the interest rate does not change. For adjustable-rate mortgages and step-rate mortgages, more than one interest rate must be shown, as discussed below.

Interest Rates for Fixed-Rate Mortgages

For fixed-rate mortgages, § 226.18(s)(2)(i)(A) requires creditors to disclose the interest rate applicable at consummation. If the transaction does not provide for any payment increases, only one interest rate is disclosed. Some fixed rate mortgages, however, have scheduled payment increases. In those cases the creditor must show the interest rate associated with such payments, even though the rate has not changed, as discussed under § 226.18(s)(2)(i)(C) below.

Interest Rates for Adjustable-Rate Mortgages and Step-Rate Mortgages

As discussed above, TILA Section 128(b)(2)(C) requires creditors to disclose examples of payment increases, including the maximum possible payment, for adjustable-rate mortgages and other mortgages where payments may vary. Under § 226.18(s)(2)(i), creditors must disclose more than one interest rate for adjustable-rate mortgages and step-rate mortgages because the payments can vary.

Interest rates at consummation. Under § 226.18(s)(2)(i)(B)(1), the creditor must provide the interest rate at consummation and the period of time until the first adjustment, labeled as "introductory rate and monthly payment." Additional explanation of discounted introductory rates is required by § 226.18(s)(2)(iii), discussed below.

Maximum during first five years. The Board proposed in the 2009 Closed-End Proposal to require disclosure of the maximum rate and payment at first adjustment, as one of the examples required by TILA Section 128(b)(2)(C). The proposal would have required the creditor to provide the maximum interest rate applicable at the first interest rate adjustment and the calendar month and year in which the first scheduled adjustment occurs.

The Board is modifying this aspect of the proposed rule. Instead of the maximum rate at the first scheduled adjustment, § 226.18(s)(2)(i)(B)(2) requires disclosure of the maximum possible rate at any time during the first five years after consummation, even if that is not the first adjustment, and the earliest date that rate may apply. The Board believes that requiring the example to reflect the first adjustment poses a risk that consumers would not be adequately warned of significant interest rate changes on a transaction where the first adjustment will be fairly modest under the transaction's terms. The limited first rate increase could be followed quickly by a much greater increase, which would not be disclosed under the rule as proposed. The Board solicits comment on whether five years is the appropriate period to address this concern. Consistent with the 2009 Closed-End Proposal, the creditor must take into account any limitations on interest rate increases when determining the interest-rate to be disclosed under § 226.18(s)(2)(i)(B)(2). If the interest rate may reach the maximum possible during the loan's term within the first five years, the creditor should disclose the rate as the maximum possible interest rate, discussed below.

Maximum possible interest rate. Section 226.18(s)(2)(i)(B)(3) requires creditors to disclose the maximum interest rate that could apply at any time, and the earliest date on which that rate could apply, as required by TILA Section 128(b)(2)(C). The Board is requiring this disclosure for step-rate mortgages as well, because the rate and payment may increase in such loans. As noted above, consumer advocates strongly supported this requirement in their comments. Consumer testing conducted for the Board also suggests that consumers find this information about the maximum rate and payment particularly important in evaluating a loan offer for an adjustable-rate mortgage. Participants indicated that this information is most useful to them in determining whether such a loan was affordable. If an amortizing adjustable-rate mortgage has intermediate limitations on interest rate increases, then the table required by proposed § 226.18(s) will have at least three columns; if the transaction has no intermediate limitations on interest rates, then the table will have two columns, one showing the rate at consummation and the other showing the maximum possible under the loan's terms.

Interest rate applicable at scheduled payment increase. Some mortgages provide for a payment increase that is not attributable to an interest rate adjustment or increase. For example, a loan may permit the borrower to make payments that cover only accrued interest for some specified period, such as the first five years following consummation; at the end of the interest-only period, the borrower must begin making larger payments to cover both interest accrued and principal. Section 226.18(s)(2)(i)(C) provides that, where such a payment increase will not coincide with an interest rate adjustment, the creditor must include a column that discloses the interest rate that would apply at the time the adjustment is scheduled to occur, and the date on which the increase would occur. Thus, for a fixed-rate mortgage, the creditor shows the same interest rate twice (and the corresponding payments as discussed below). The Board believes this will help the consumer understand that the increase in payment is due to the requirement to begin repaying loan principal and not to an interest-rate adjustment.

The same is true for adjustable-rate mortgages and step-rate mortgages. For example, some adjustable-rate mortgages permit the borrower to make interest-only payments for a specified period, such as the first five years following consummation. A scheduled payment increase may or may not coincide with a scheduled interest rate adjustment. Under § 226.18(s)(2)(i)(C), if a scheduled payment increase does not coincide with an interest rate adjustment (or rate increase for a step-rate mortgage), creditors must include a column that discloses the interest rate that will apply at the time of the increase, the date the increase is scheduled to occur, and an appropriate description such as "first increase" or "first adjustment," as appropriate. Comment 18(s)(2)(i)(C)–1 provides clarifying examples.

18(s)(2)(ii) Negative Amortization Loans

For negative amortization loans, for which any scheduled payment may cause the principal balance to increase, § 226.18(s)(2)(ii) requires disclosure of the interest rate applicable at consummation. Some ARM loans do not provide any limitations on interest rate increases ("interest rate caps"); the only cap is the maximum possible interest rate required by § 226.30(a). For these payment option loans, the creditor must disclose the interest rate in effect at consummation and assume that the interest rate reaches the maximum at the next adjustment—often the second month after consummation. The creditor must disclose that rate for the first and second scheduled payment increases, explained under the discussion of § 226.18(s)(4) below. And the creditor must disclose that rate a third time, in the last column, when the loan has recast, i.e., converted to fully amortizing payments over the remainder of the loan's term. This approach to interest rates for negative amortization loans is consistent with the MDIA, which requires disclosure of the payment at the maximum possible rate, and other examples of payment increases. Additional rules for disclosing the interest rate on a loan with negative amortization are found in § 226.18(s)(6), discussed below.

18(s)(2)(iii) Introductory Rate Disclosure for Amortizing Adjustable-Rate Mortgages

Many adjustable-rate mortgages have an introductory or "teaser" rate, set below the sum of the index and margin used for later adjustments. Section 226.18(s)(2)(iii) requires a special disclosure of any introductory rate. In consumer testing conducted for the Board, many participants did not understand the ramifications of an introductory interest rate. Participants understood that if market interest rates increased, the interest rate and payment on their loan would increase. In contrast, participants did not understand that, if they had an introductory rate, their interest rate and payment would increase when the introductory rate expired, even if market interest rates did not increase.

Several different disclosures designed to show the impact of an introductory rate were tested in tabular form, with mixed results. Therefore, the Board is requiring an explanation of the introductory rate below the table itself. Section 226.18(s)(2)(iii) requires disclosure of the introductory rate, how long it will last, and that the interest rate will increase at the first scheduled adjustment even if market rates do not increase. Creditors also must disclose the fully indexed rate that otherwise would apply at consummation. This disclosure must be placed in a box beneath the table, in a format substantially similar to Model Clause H–4(I).

Creditors commenting on the 2009 Closed-End Proposal expressed concern over the requirement to disclose the fully-indexed rate at consummation because the value of the index at consummation may be unknown when disclosures are required to be delivered within three business days after receipt of an application under § 226.19(a)(1). Comment 18(s)(2)(iii)(C)–1 would clarify that, for early disclosures, the fully-indexed rate disclosed under § 226.18(s)(2)(iii)(C) may be based on the index in effect at the time the disclosure is provided. "At consummation," as used in § 226.18(s)(2)(iii)(C), refers to disclosures delivered at consummation, or three business days before consummation pursuant to § 226.19(a)(2)(ii). The comment also adopts guidance for cases where the contract provides for a delay in the implementation of changes in an index value. In such cases, the disclosure may reflect an index value in effect anytime during the contractual delay period prior to the time of the disclosure. For example, if the contract specifies that rate changes are based on the index value in effect 45 days before the change date, creditors may use any index value in effect during the 45 days before consummation (or any earlier date of disclosure) in calculating the fully-indexed rate to be disclosed. This guidance is similar to existing comment 17(c)(1)–10.

18(s)(3) Payments for Amortizing Loans

18(s)(3)(i) Principal and Interest Payments

Section 226.18(s)(3)(i) requires disclosure of the principal and interest payment that corresponds to each interest rate disclosed under § 226.18(s)(2)(i). Under § 226.18(s)(3)(i), if all regular periodic payments include principal and interest, each disclosed payment amount must be listed in a single row in the table with a description such as "principal and interest." Separate rules apply to amortizing loans with interest-only payments under § 226.18(s)(3)(ii), discussed below.

Regular periodic payments. Under § 226.18(s)(3)(i)(A), for transactions where the regular periodic payment fully amortizes the loan, the payment amount including both principal and interest must be disclosed. Section 226.18(s)(3)(i)(B) requires disclosure of the payment amount at any scheduled payment increase that does not coincide with an interest rate adjustment, and the date on which the increase is scheduled to occur. For example, a fixed-rate loan might have terms under which part of the scheduled payment is applied to principal for an initial period, thus it is not an interest-only loan disclosed under § 226.18(s)(3)(ii). The amount of principal covered by such payments, however, may be insufficient to amortize the loan fully over its life. In such cases, a scheduled increase in the payment amount from such a partially amortizing payment to a fully amortizing payment would be required to be disclosed.

Escrows; mortgage insurance premiums. Section 226.18(s)(3)(i)(C) provides that, if an escrow account will be established, the creditor must disclose the estimated payment amount for taxes and insurance, including any mortgage insurance. For transactions secured by real property or a dwelling, creditors no longer have the flexibility provided in existing § 226.18(g) to exclude escrow amounts. Consumer testing conducted for the Board shows that many consumers compare loans based on the monthly payment amount. The Board believes that, for consumers to understand the monthly amount they actually will be required to pay for a particular loan, information about payments for taxes and insurance is necessary. Escrow information is included in the table to make it easier for consumers to identify whether there is an escrow account and how much of their payment applies to the escrow.

As noted above, both consumer advocates and some industry commenters argued that taxes and insurance estimates should be included even when no escrow account is established. The Board believes there may be valid reasons for such an approach. For purposes of this interim rule, however, the Board is adopting the requirement as proposed. The Board is concerned that disclosures of taxes and insurance in all cases may leave consumers confused as to whether an escrow account is included with the loan or not, in the absence of a clear and effective notice indicating which is the case. After additional testing can be conducted to determine whether such a notice is feasible and helpful to consumers, the Board will consider such an approach when it adopts the 2009 Closed-End Proposal as a final rule.

Comment 18(s)(3)(i)(C)–1 clarifies the types of taxes and insurance that are required to be included in the estimate. The comment also clarifies that the estimated escrow amounts disclosed under § 226.18(s)(3)(i)(C), other than mortgage insurance premiums, do not affect any other disclosures, including the finance charge and annual percentage rate.

Comment 18(s)(3)(i)(C)–2 provides guidance on how to determine the length of time for which mortgage insurance payments must be included in the estimate. Under the comment, the payment amount should reflect the consumer's mortgage insurance payments until the date on which the creditor must automatically terminate coverage under applicable law, even though the consumer may have a right to request that the insurance be canceled earlier. This guidance mirrors existing comment 18(g)–5. Comment 18(s)(3)(i)(C)–2 also states that periodic mortgage insurance payments should be included in the escrow line of the summary table even if they are not escrowed and even if there is no escrow account established for the transaction.

Credit insurance. The Board solicited comment on whether premiums or other amounts for credit life insurance, debt suspension and debt cancellation agreements, and other similar products ("credit protection products") should be included or excluded from the disclosure of escrows for taxes and insurance. The Board expressed concerns that inclusion of such amounts may cause some consumers to believe these products are required. Most commenters that addressed this question agreed with the Board's concern and favored excluding such amounts from the escrow amount disclosed. The Board is adopting the escrow disclosure requirement as proposed and is adding language to comment 18(s)(3)(i)(C)–1 to clarify that premiums or payments for credit protection products should not be included in the disclosed escrow amounts.

Total periodic payments. Section 226.18(s)(3)(i)(D) requires disclosure of the total estimated monthly payment. The total estimated monthly payment is the sum of the principal and interest payments required under § 226.18(s)(3)(i)(A) or (B), as applicable, and the estimated taxes and insurance payments required to be disclosed in § 226.18(s)(3)(i)(C).

18(s)(3)(ii) Interest-Only Payments

Like § 226.18(s)(3)(i), § 226.18(s)(3)(ii) requires the disclosure of regular periodic payments corresponding to the amortizing loan interest rates disclosed under § 226.18(s)(2)(i). In addition, under § 226.18(s)(3)(ii), special itemization of the payment is required if the loan permits the consumer to make any interest-only payments. Comment 18(s)(3)(ii)–1 clarifies, however, that these rules apply only if the loan is not also a negative amortization loan; if the loan is a negative amortization loan, even if it also has an interest-only feature, payments are disclosed under the rules in § 226.18(s)(4), discussed below.

Principal and interest payment itemization. Under § 226.18(s)(3)(ii), if any regular periodic payment amounts will include interest but not principal, all payments for the loan must be itemized into principal and interest. For a payment that includes no principal, § 226.18(s)(3)(ii)(A) requires the creditor to indicate that none of the payment amount will be applied to principal. The creditor must label the dollar amount to be applied to interest "interest payment." The Board requires this itemization and labeling to highlight for consumers the impact of making interest-only payments. Without this emphasis, many participants in the Board's consumer testing did not clearly understand that an "interest-only" loan was different from a loan in which all payments are applied to principal and interest. Thus, even for later payments that will be applied to both principal and interest, § 226.18(s)(3)(ii)(B) requires the creditor to itemize the payment between the two.

Escrows and total periodic payments. Section 226.18(s)(3)(ii)(C) requires disclosure of an estimate of the amount of taxes and insurance, including mortgage insurance. Section 226.18(s)(3)(ii)(D) requires disclosure of the estimated total payment including principal, interest, and taxes and insurance. These requirements parallel the escrow and total payment disclosures under § 226.18(s)(3)(i)(C) and (D). Accordingly, comment 18(s)(3)(ii)(C)–1 refers to the commentary under § 226.18(s)(3)(i)(C), discussed above, for guidance on escrows.

18(s)(4) Payments for Negative Amortization Loans

Under § 226.18(s)(4), for each interest rate disclosed under § 226.18(s)(2)(ii) for a loan with negative amortization, the creditor must disclose payments in two separate rows. One row of the table shows the fully amortizing payment for each interest rate; for purposes of calculating these payments the creditor would assume the interest rate reaches the maximum at the earliest possible date and that the consumer makes only fully amortizing payments. The other row of the table shows the minimum required payment for each rate, until the recast point. At the recast point, the minimum payment row shows the fully amortizing payment. For purposes of the minimum payment row, creditors must assume the interest rate reaches the maximum at the earliest possible date and that the consumer makes only the minimum required payment for as long as permitted under the terms of the legal obligation.

The interest rate and payment summary would display only two payment options, even if the terms of the legal obligation provide for others, such as an option to make interest-only payments. The table would show only the option to make minimum payments that would result in negative amortization, and the option to make fully amortizing payments. The Board believes that displaying all of the options in the table could cause confusion and information overload for consumers. Creditors would be free to provide information on options not displayed in the table, outside the segregated information required under this subsection.

Consumer advocates commented that the Board's proposed sample disclosure for payment option adjustable-rate mortgages ("payment option ARMs"), proposed sample H–19(I), would not show the maximum possible payment for a typical payment option ARM because the sample assumed the transaction's lifetime maximum interest rate of 10.5% would be reached at the second payment, which caused the loan to recast to fully amortizing payments at the earliest possible time. The commenters noted that a payment option ARM reaches the maximum possible payment when it applies an intervening rate for a period, so that the onset of fully amortizing payments is delayed as long as possible thus maximizing the principal balance to which the lifetime maximum rate is applied after the loan recasts. The proposed sample was intended to illustrate the maximum payment possible under certain assumed transaction terms, which did not include any rate adjustment caps other than the lifetime cap. Thus, while it did not show the maximum possible payment under any payment option

ARM, it showed the maximum payment under the type of product it was intended to illustrate. This interim rule is publishing only model clauses, not samples, thus it entails no assumptions regarding sample transaction terms. In all cases, however, these rules require that creditors reflect all applicable terms, including rate adjustment caps, maximum negative amortization amounts and periods, and maximum interest rates.

Minimum payment amounts. The rule requires a disclosure of the amount of the minimum required payment applicable for each interest rate required to be disclosed under § 226.18(s)(2)(ii) and the date on which that payment becomes applicable. Section 226.18(s)(4)(i)(A) requires disclosure of the minimum required payment at consummation.

Payment increases. As noted above, some payment option loans do not have interest rate adjustment caps, and thus the interest rate may reach its maximum at the first interest rate adjustment. Such loans may have limits, however, on the amount that the minimum payment may increase following an interest rate adjustment. For example, a minimum payment increase may be limited by a certain percentage, such as 7.5% greater than the previous minimum payment. (Such limits are generally subject to conditions and will apply only until a specific time, such as at the fifth year of the loan, or until the loan balance reaches a certain maximum.) Under § 226.18(s)(4)(i)(B), if adjustments in the minimum payment amount are limited such that the payment will not fully amortize the loan even after the interest rate has reached the maximum, a disclosure of the minimum payment amount at the first and second payment adjustments is required. That is, in cases where the *first* interest rate adjustment will be the *only* interest rate adjustment, but payment adjustments will continue to occur before the minimum payment recasts to a fully amortizing payment, a disclosure of up to two additional minimum payment adjustments is required.

Explanation of negative amortization. Under § 226.18(s)(4)(i)(C), the creditor must provide a statement that the minimum payment will cover only some of the accrued interest and none of the principal and will cause the principal balance to increase. Participants in the Board's consumer testing were unfamiliar with the concept of negative amortization and struggled to understand why a loan's balance would increase when payments were made. Thus, the Board is adopting this required statement to ensure that consumers are informed about the consequences of making such minimum payments.

Payment after recast. Section 226.18(s)(4)(ii) requires disclosure of the fully amortizing payment that will be required when the loan recasts, *i.e.,* when minimum payments no longer are permitted and fully amortizing payments are required under the terms of the legal obligation. This payment amount must reflect the maximum possible interest rate that will be applicable at that time, based on the terms of the legal obligation, as disclosed under § 226.18(s)(2)(ii)(B).

Fully amortizing payments. Section 226.18(s)(4)(iii) requires disclosure in a separate row of the table of the fully amortizing payment, assuming that the consumer makes only fully amortizing payments beginning at consummation. The fully amortizing payment row must be completed for each interest rate required to be disclosed under § 226.18(s)(2)(ii). The Board believes that contrasting the fully amortizing payment with the minimum required payment will help consumers to understand the implications of making the fully amortizing payment and the minimum payment. In consumer testing, participants understood from the table that if they made the fully amortizing payment each month they would pay their loan off, and that if they instead made the minimum payment they would not pay the loan off and in fact would increase the amount that they owe.

18(s)(5) Balloon Payments

Under § 226.18(s)(5)(i), if a loan's terms provide for a balloon payment, the payment must be disclosed in the last row of the table rather than in a column, unless it coincides with an interest rate adjustment or other payment increase such as the expiration of an interest-only option. Section 226.18(s)(5)(i) provides that a payment is a balloon payment if it is more than twice the amount of other payments. Under § 226.18(s)(5)(ii), if a balloon coincides with an interest rate adjustment or other payment increase, the balloon payment is disclosed in the table as that payment increase.

18(s)(6) Special Disclosures for Loans With Negative Amortization

Statement of balance increase and other information. Section 226.18(s)(6) requires a statement of the amount of the increase in the loan's principal balance if the consumer makes only minimum payments and the earliest month and year in which the minimum payment will recast to a fully amortizing payment under the terms of the legal obligation, assuming that the interest rate reaches its maximum at the earliest possible time. As noted, participants in testing expressed confusion about negative amortization; the Board believes this disclosure and the other required disclosures in the table will help consumers understand the risks of making such minimum payments. In addition, to help consumers navigate the information in the table, § 226.18(s)(6) requires a statement directly above the interest rate and payment summary table explaining that the loan offers payment options. The explanation preceding the table also must state the maximum possible interest rate and the smallest number of months or years in which the interest rate could reach its maximum.

The creditor also must disclose whether an escrow account will be established and, if so, an estimate of the amount for taxes and insurance included in each periodic payment. Comment 18(s)(6)-1 refers to the commentary under § 226.18(s)(3)(i)(C) for guidance on escrows. The comment notes that, under that guidance, mortgage insurance payments decline over a loan's term, and the payment amounts shown in the table should reflect the mortgage insurance payment that will be applicable at the time each disclosed periodic payment will be in effect. Accordingly, the disclosed mortgage insurance payment will be zero if it corresponds to a periodic payment that will occur after the creditor will be legally required to terminate mortgage insurance. On the other hand, because only one escrow amount is disclosed under § 226.18(s)(6) for negative amortization loans and escrows are not itemized in the payment amounts, the single escrow amount disclosed should reflect the mortgage insurance amount that will be collected as of the outset of the loan's term.

18(s)(7) Definitions

As noted above, § 226.18(s)(7) provides definitions for several terms used in § 226.18(s). Those definitions are discussed at the beginning of this section-by-section analysis to facilitate the subsequent discussion of this interim rule's requirements.

18(t) "No-Guarantee-to-Refinance" Statement

The MDIA also amended Section 128(b) of TILA to require creditors to disclose for variable rate transactions, in conspicuous type size and format, that there is no guarantee that the consumer will be able to refinance the transaction to lower the interest rate or monthly payments ("MDIA refinancing warning").[6] 15 U.S.C. 1638(b)(2)(C)(ii). To implement the disclosure required by the MDIA, the Board is adding a new § 226.18(t). Section 226.18(t)(1) requires creditors to disclose a statement that there is no guarantee that the consumer will be able to refinance the loan to obtain a lower interest rate and payment. The Board believes that including such a statement on the TILA disclosure form will alert consumers to consider the impact of future rate adjustments and increased monthly payments.

Although the MDIA requires this refinancing warning only for variable-rate transactions secured by a dwelling, the Board proposed in the 2009 Closed-End Proposal to expand the scope of the requirement to include fixed-rate transactions secured by a dwelling, as well as transactions secured by real property without a dwelling. The Board is now adopting this approach. The Board is concerned that some consumers may accept loan terms that could present possible payment shock concerns similar to variable-rate transactions, such as a three-year, fixed-rate mortgage with a balloon payment. Based on consumer testing, the Board believes all consumers, regardless of transaction-type, would benefit from a statement that encourages consideration of future possible market rate increases. Consistent with MDIA's provisions, however, § 226.18(t) does not apply to transactions secured by timeshare plans.

Section 226.18(t)(2) provides format requirements for the statement required by § 226.18(t)(1). The statement must be made in a form substantially similar to Model Clause H–4(K) in Appendix H. In the 2009 Closed-End Proposal, the Board proposed to require that the statement be made together with the security interest disclosure. The Board also proposed to modify the security interest disclosure to provide a more plain-language approach to the significant potential consequences of a creditor taking a security interest in a consumer's home. See 74 FR 43232, 43310, Aug. 26, 2009. The Board is not adopting the proposed changes to the security interest disclosure at this time because that is not necessary to implement the MDIA amendments that take effect on January 30, 2011. Accordingly, the Board also is not adopting the requirement to link the security interest disclosure to the new statement that there is no guarantee a consumer will be able to refinance.

Appendixes G and H Open-End and Closed-End Model Forms and Clauses

Comment App. G and H–1 discusses permissible changes to the model forms and clauses. It states that creditors may make certain changes to the format or content of the model forms without losing TILA's protection from liability for their use. It also indicates, however, that formatting changes may not be made to certain model forms and samples. This interim rule amends the comment to add new model clauses H–4(E), H–4(F), H–4(G), and H–4(H) to the list of models whose formatting may not be altered.

Appendix H Closed-End Model Forms and Clauses

As noted above, the Board is adopting several model clauses to illustrate the new requirements under this interim rule. Model Clause H–4(E) illustrates the interest rate and payment summary table required under § 226.18(s) for a fixed-rate mortgage transaction. Model Clause H–4(F) illustrates the table for an adjustable-rate or a step-rate mortgage transaction. Model Clause H–4(G) illustrates the table for a mortgage transaction with negative amortization. Model Clause H–4(H) illustrates the table for a fixed-rate loan with interest-only terms. Model Clause H–4(I) illustrates the introductory rate disclosure required by § 226.18(s)(2)(iii) if an adjustable-rate mortgage has an introductory rate. Model Clause H–4(J) illustrates the balloon payment disclosure required by § 226.18(s)(5) for a mortgage with a balloon payment term. Finally, Model Clause H–4(K) illustrates the no-guarantee-to-refinance statement required by § 226.18(t).

VI. Paperwork Reduction Act

In accordance with the Paperwork Reduction Act (PRA) of 1995 (44 U.S.C. 3506; 5 CFR Part 1320 Appendix A.1), the Board reviewed the interim rule under the authority delegated to the Board by the Office of Management and Budget (OMB). The collection of information that is required by this interim rule is found in 12 CFR part 226. The Board may not conduct or sponsor, and an organization is not required to respond to, this information collection unless the information collection displays a currently valid OMB control number. The OMB control number is 7100–0199.

This information collection is required to provide benefits for consumers and is mandatory (15 U.S.C. 1601 *et seq.*). Since the Board does not collect any information, no issue of confidentiality arises. The respondents/recordkeepers are creditors and other entities subject to Regulation Z.

TILA and Regulation Z are intended to ensure effective disclosure of the costs and terms of credit to consumers. For open-end credit, creditors are required, among other things, to disclose information about the initial costs and terms and to provide periodic statements of account activity, notice of changes in terms, and statements of rights concerning billing error procedures. Regulation Z requires specific types of disclosures for credit and charge card accounts and home-equity plans. For closed-end loans, such as mortgage and installment loans, cost disclosures are required to be provided prior to consummation. Special disclosures are required for certain products, such as reverse mortgages, certain variable-rate loans, and certain mortgages with rates and fees above specified thresholds. TILA and Regulation Z also contain rules concerning credit advertising. Creditors are required to retain evidence of compliance for two years, see § 226.25, but Regulation Z identifies only a few specific types of records that must be retained.[7]

Under the PRA, the Board accounts for the paperwork burden associated with Regulation Z for the state member banks and other creditors supervised by the Federal Reserve that engage in consumer credit activities covered by Regulation Z and, therefore, are respondents under the PRA. Appendix I of Regulation Z defines the Federal Reserve-regulated institutions as: State member banks, branches and agencies of foreign banks (other than federal branches, federal agencies, and insured state branches of foreign banks), commercial lending companies owned or controlled by foreign banks, and organizations operating under section 25 or 25A of the Federal Reserve Act. Other federal agencies account for the paperwork burden imposed on the entities for which they have administrative enforcement authority. The current total annual burden to comply with the provisions of Regulation Z is estimated to be 1,497,362 hours for the 1,138 Federal Reserve-regulated institutions that are deemed to be respondents for the purpose of the PRA. A detailed discussion of revised burden is presented in the following two paragraphs. To ease the burden and cost of complying with Regulation Z (particularly for small entities), the

[6] Specifically, the MDIA requires that the Board use consumer testing to develop disclosures for variable-rate transactions, including the fact that "there is no guarantee that the borrower will be able to refinance to a lower amount." Public Law 109–8, 119 Stat. 23, § 2502(a)(6).

[7] *See* comments 25(a)–3 and –4.

Board provides model forms, which are appended to the regulation.

As discussed in the preamble, the Board is adopting changes to format and content requirements for disclosures for closed-end mortgages that are required within three days after application and before consummation. The interim rule will impose a one-time increase in the total annual burden under Regulation Z for all respondents regulated by the Federal Reserve by 136,560 hours, from 1,497,362 to 1,633,922 hours. In addition, the Board estimates that the proposed revisions to the rules will increase the total annual burden on a continuing basis from 1,497,362 to 2,043,602 hours.

The Board estimates that 1,138 respondents regulated by the Federal Reserve would take, on average, 120 hours (three business weeks) to update their systems and internal procedure manuals and to provide training for relevant staff to comply with the new disclosure requirements in § 226.18(s) and (t). This one-time revision will increase the burden by 136,560 hours. On a continuing basis, the Board estimates that 1,138 respondents regulated by the Federal Reserve will take, on average, 40 hours a month to comply with the new disclosure requirements and that the new requirements will increase the ongoing burden from 304,756 hours to 546,240 hours. To ease the burden and cost of complying with the new requirements under Regulation Z the Board is adding several model clauses to Appendix H.

The total estimated burden increase represents averages for all respondents regulated by the Federal Reserve. The Board expects that the amount of time required to implement the changes for a given institution may vary based on the size and complexity of the respondent. Further, the estimated burden increase does not include the burden of complying with other proposed and final rules the Board is issuing simultaneously with this interim rule.

The other federal financial agencies, Office of the Comptroller of the Currency (OCC), Office of Thrift Supervision (OTS), the Federal Deposit Insurance Corporation (FDIC), and the National Credit Union Administration (NCUA), are responsible for estimating and reporting to OMB the total paperwork burden for the domestically chartered commercial banks, thrifts, and federal credit unions and U.S. branches and agencies of foreign banks for which they have primary administrative enforcement jurisdiction under TILA Section 108(a), 15. U.S.C. 1607(a). These agencies are permitted, but are not required, to use the Board's burden estimation methodology. Using the Board's method, the total current estimated annual burden for the approximately 16,200 domestically chartered commercial banks, thrifts, and federal credit unions and U.S. branches and agencies of foreign banks supervised by the Federal Reserve, OCC, OTS, FDIC, and NCUA under TILA will be approximately 19,610,245 hours. The interim rule will impose a one-time increase in the estimated annual burden for such institutions by 1,944,000 hours to 21,554,245 hours. On a continuing basis, the interim rule will impose an increase in the estimated annual burden by 7,776,000 to 27,386,245 hours. The above estimates represent an average across all respondents; the Board expects variations between institutions based on their size, complexity, and practices.

Comments are invited on: (1) Whether the new collection of information is necessary for the proper performance of the Board's functions; including whether the information has practical utility; (2) the accuracy of the Board's estimate of the burden of the information collection, including the cost of compliance; (3) ways to enhance the quality, utility, and clarity of the information to be collected; and (4) ways to minimize the burden of information collection on respondents, including through the use of automated collection techniques or other forms of information technology. Comments on the collection of information should be sent to Michelle Shore, Federal Reserve Board Clearance Officer, Division of Research and Statistics, Mail Stop 95–A, Board of Governors of the Federal Reserve System, Washington, DC 20551, with copies of such comments sent to the Office of Management and Budget, Paperwork Reduction Project (7100–0199), Washington, DC 20503.

VII. Regulatory Flexibility Analysis

In accordance with Section 4 of the Regulatory Flexibility Act (RFA), 5 U.S.C. 604, the Board is publishing a final regulatory flexibility analysis for the amendments to Regulation Z in this interim rule. The RFA generally requires an agency to perform an assessment of the impact a rule is expected to have on small entities.[8] Under Section 5(b) of the RFA, however, the regulatory flexibility analysis otherwise required under Section 4 of the RFA is not required if an agency certifies that the rule will not have a significant economic impact on a substantial number of small entities and states the factual basis for such certification. 5 U.S.C. 605(b). The Board believes that this interim rule will not have a significant economic impact on a substantial number of small entities. The amendments to Regulation Z's disclosure requirements implement revisions to TILA made by MDIA. Creditors must comply with MDIA's requirements when they become effective on January 30, 2011, whether or not the Board amends Regulation Z to conform the regulation to the statute. The Board's final rule is intended to facilitate compliance by eliminating inconsistencies between Regulation Z's existing requirements and the statutory requirements imposed by the MDIA, which are effective January 30, 2011.

A. Statement of the Need for, and Objectives of, the Interim Rule

Congress enacted the TILA based on findings that economic stability would be enhanced and competition among consumer credit providers would be strengthened by the informed use of credit resulting from consumers' awareness of the cost of credit. One of the stated purposes of TILA is to provide meaningful disclosure of credit terms to enable consumers to compare credit terms available in the marketplace more readily and avoid the uninformed use of credit. TILA also contains procedural and substantive protections for consumers. TILA directs the Board to prescribe regulations to carry out the purposes of the statute. The Board's Regulation Z implements TILA.

Congress enacted the MDIA in 2008 as an amendment to TILA. The MDIA amended TILA's disclosure requirements for closed-end mortgage transactions that are secured by a consumer's dwelling. In May 2009, the Board revised Regulation Z to implement those requirements. The MDIA also amended TILA to require disclosure of examples for variable-rate mortgage transactions of payment changes, including the maximum payment increase possible, and to require disclosure to ensure that consumers are aware that there is no guarantee they will be able to refinance to lower their payments in the future. As discussed in part V of the **SUPPLEMENTARY INFORMATION**, this interim rule implements those MDIA requirements by requiring disclosure of

[8] Under standards set by the U.S. Small Business Administration (SBA), an entity is considered "small" if it has $175 million or less in assets, for banks and other depository institutions, or $7 million or less in revenues, for non-bank mortgage lenders, mortgage brokers, and loan servicers. U.S. Small Business Administration, Table of Small Business Size Standards Matched to North American Industry Classification System Codes, *available at http://www.sba.gov/idc/groups/public/documents/sba_homepage/serv_sstd_tablepdf.pdf.*

the interest rate and payment summary and the no guarantee to refinance statement.

B. Summary of Issues Raised by Comments in Response to the Initial Regulatory Flexibility Analysis

The initial regulatory flexibility analysis published in the 2009 Closed-End Proposal (IRFA) related to the disclosure requirements being implemented by this interim rule, as well as a significant number of additional proposed requirements for mortgage transactions. Those additional requirements include the rest of the proposed changes to the TILA disclosure's content, timing, and format; proposed new requirements and changes to the format and content of disclosures given at application; proposed changes to the timing, content, and types of notices provided after consummation; and proposed new protections related to limits on loan originator compensation. Consequently, most comments to the 2009 Closed-End Proposal relating specifically to the IRFA addressed the overall proposal. Comments relating to specific burdens focused mainly on aspects of the proposal other than the interest rate and payment summary and the no-guarantee-to-refinance statement.

A few commenters opposed certain aspects of the interest rate and payment summary, such as its tabular format requirement, on the grounds that they would be technologically challenging. The Board believes, however, that software likely is readily available that is capable of tabular formatting, especially in light of the increasing use of tabular disclosures under various state and federal laws. More importantly, the formatting requirements are essential to the interim rule's purposes based on consumer testing, as discussed above. Some small depository institutions, mortgage brokers, and their trade associations also suggested exempting small creditors or delaying the implementation of the overall proposal by substantial time periods to allow time for other regulatory developments to take effect.

TILA exempts from coverage persons that do not "regularly extend" consumer credit. *See* TILA Section 103(f), 15 U.S.C. 1604(f) (definition of "creditor"). Regulation Z implements this provision in § 226.2(a)(17). Thus, lenders with limited activity (in the case of mortgage lending, five or fewer loans in a year) already are exempt from all TILA disclosure requirements. Limited lending activity likely correlates to a significant extent with being a small entity. The Board believes, however, that an exemption from certain TILA disclosure requirements for small creditors that otherwise are subject to TILA and Regulation Z generally would undermine the purposes of TILA by limiting the instances where consumers would receive the benefit of the disclosures. This would be especially true if the exemption were limited to the interest rate and payment summary implemented by this interim rule. Consumers also could be confused by receiving disclosures that differ in that one respect, solely based on which creditor they applied to for a mortgage loan. Accordingly, the Board is not exempting small entities from the requirements of this interim rule.

The Board intends to establish the implementation period for the new disclosures and other new TILA requirements when it publishes a final rule under the 2009 and 2010 Closed-End Proposals. At that time, the Board will take into consideration the impact on small businesses and the time needed for them to implement the new requirements. With respect to this interim rule, the Board is affording creditors the maximum possible time to implement the interest rate and payment summary and no-guarantee-to-refinance notice requirements, by making compliance optional until the statutory effective date of January 30, 2011.

The U.S. Small Business Administration Office of Advocacy (Advocacy) commented on the IRFA generally. Advocacy asserted that the Board's IRFA failed to satisfy the requirements of the RFA in two ways. First, Advocacy stated that the IRFA lacked adequate information about the economic impact of the proposal. Second, Advocacy stated that the Board failed to give full consideration to less burdensome alternatives to the proposal.

The Board acknowledged that the overall proposal would have a significant economic impact on a substantial number of small entities but also noted that the precise costs to small entities of updating their systems and disclosures are difficult to identify. The Board noted that the impact would depend on a number of unknown factors, including the specifications of the current systems used by such entities to prepare and provide disclosures and to administer and maintain accounts, the complexity of the terms of credit products that they offer, and the range of such product offerings. *See* 74 FR 43232, 43320, Aug. 26, 2009. The Board also recognizes that the impact also includes the cost of legal counsel to implement new disclosure requirements, but that cost also is difficult to quantify. Nevertheless, as Advocacy recognized in its comment letter, in preparing an IRFA an agency may provide general, descriptive statements of the effects of a proposed rule if quantification is not practicable or reliable. 5 U.S.C. 607. Because quantification of the impact was impracticable, the Board believes the descriptive discussion, referenced above, satisfied this standard.

Most alternatives raised by commenters specifically to reduce burdens related to the loan originator compensation proposal, which is not a part of this interim rule. The Board considered alternatives to the various disclosure proposals, and discussed them throughout the **SUPPLEMENTARY INFORMATION** to the 2009 Closed-End Proposal. Despite these discussions, Advocacy asserted that the Board did not consider alternatives that are specifically meant to reduce the economic impact on small entities. The Board stated, however, that a principal goal of the Regulation Z review is to produce revised and improved mortgage disclosures that consumers will be more likely to understand and use in their decisions, while at the same time not creating undue burdens for creditors. *See* 74 FR 43232, 43234, Aug. 26, 2009. In considering alternatives to the 2009 Closed-End Proposal, the Board sought to further both of these objectives, thus all alternatives were specifically considered at least in part as to how they might reduce the economic impact on small entities.

In proposing the specific parts of the proposal being implemented by this interim rule, the Board did not identify any alternatives that might reduce the economic impact on small entities while still achieving the purposes of the disclosure. As noted above, recent amendments to TILA require these disclosures, and extensive consumer testing led to the specifics of the requirements. The Board has concluded that the required content and format are necessary to meet the purposes of TILA as amended by MDIA, and it has not identified any less burdensome alternatives that would achieve the same purposes. Accordingly, the Board did not discuss any alternatives to the interest rate and payment summary or the no-guarantee-to-refinance statement requirements. As also noted above, the Board cannot quantify precisely the costs of complying with the requirements of this interim rule. The Board sought comment, however, on any costs, compliance requirements, or changes in operating procedures arising from the application of the overall proposal, including the requirements implemented by this interim rule, to small businesses. *See* 74 FR 43232, 43320, Aug. 26, 2009. As noted above, some commenters objected to the interest rate and payment summary as burdensome, but they gave no specific cost information.

C. Description and Estimate of Small Entities to Which the Interim Rule Will Apply

The interim rule will apply to all institutions and entities that engage in closed-end lending secured by real property or a dwelling. TILA and Regulation Z have broad applicability to individuals and businesses that originate even small numbers of home-secured loans. *See* § 226.1(c)(1). As discussed in the IRFA, through data from Reports of Condition and Income (Call Reports) of depository institutions and certain subsidiaries of banks and bank holding companies, as well as data reported under the Home Mortgage Disclosure Act (HMDA), the Board can estimate the approximate number of small depository institutions and non-depository institutions that would be subject to the rules. For the majority of HMDA respondents that are not depository institutions, exact revenue information is not available.

Based on the best information available, the Board makes the following estimate of small entities that will be affected by this interim rule: According to March 2010 Call Report data, approximately 8,848 small depository institutions would be subject to the rule. Approximately 15,899 depository institutions in the United States filed Call Report data, approximately 11,218 of which had total domestic assets of $175 million or less and thus were considered small entities for purposes of the RFA. Of the 3,898 banks, 523 thrifts, 6,727 credit unions, and 70 branches of foreign banks that filed Call Report data and were considered small entities, 3,776 banks, 496 thrifts, 4,573 credit unions, and 3 branches of foreign banks, totaling 8,848 institutions, extended mortgage credit. For purposes of this Call Report analysis, thrifts include savings banks, savings and loan entities, co-operative banks and industrial banks. Further, 1,507 non-depository institutions (independent mortgage companies, subsidiaries of a depository institution, or affiliates of a bank holding company) filed HMDA reports in 2009 for 2008 lending activities. Based on the small volume of lending activity reported by these institutions, most are likely to be small entities.

D. Reporting, Recordkeeping, and Other Compliance Requirements

The compliance requirements of the interim rule are described in part V of the SUPPLEMENTARY INFORMATION. To comply with the revised rules, small entities will be required to modify their procedures for making credit disclosures for mortgage loans. The precise costs to small entities of updating their systems and disclosures are difficult to estimate. These costs will depend on a number of unknown factors, including, among other things, the specifications of the current systems used by such entities to prepare and provide disclosures, the scope and complexity of their mortgage products, the extent to which they will require outside legal counsel to develop compliant disclosures, and their internal costs of training personnel.

E. Steps Taken To Minimize the Economic Impact on Small Entities

The Board generally prescribes model forms and clauses to facilitate compliance with its disclosure requirements under Regulation Z. In this interim rule, the Board is adopting model clauses to illustrate the interest rate and payment summary for fixed-rate mortgages, adjustable- or step-rate mortgages, mortgages with negative amortization, and mortgages with interest-only payments, as well as model clauses to illustrate the introductory rate disclosure, the balloon payment disclosure, and the no guarantee to refinance statement. In addition, as noted above, the Board is affording small creditors and other creditors the maximum possible time to implement this interim rule's requirements by making compliance optional until the statutory effective date. This regulatory flexibility analysis does not discuss alternatives to the interim rule because the Board is revising Regulation Z for the narrow purpose of carrying out its mandate to implement statutory amendments to TILA.

List of Subjects in 12 CFR Part 226

Advertising, Consumer protection, Federal Reserve System, Mortgages, Reporting and recordkeeping requirements, Truth in lending.

Authority and Issuance

■ For the reasons set forth in the preamble, the Board amends Regulation Z, 12 CFR Part 226, as set forth below:

PART 226—TRUTH IN LENDING

(Regulation Z)

■ 1. The authority citation for part 226 continues to read as follows:

Authority: 12 U.S.C. 3806; 15 U.S.C. 1604, 1637(c)(5), and 1639(l); Pub. L. 111–24 § 2, 123 Stat. 1734.

Subpart C—Closed-End Credit

■ 2. Section 226.18 is amended by revising paragraph (g) introductory text and adding new paragraphs (s) and (t) to read as follows:

§ 226.18 Content of disclosures.

* * * * *

(g) *Payment schedule.* Other than for a transaction that is subject to paragraph (s) of this section, the number, amounts, and timing of payments scheduled to repay the obligation.

* * * * *

(s) *Interest rate and payment summary for mortgage transactions.* For a closed-end transaction secured by real property or a dwelling, other than a transaction secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53D), the creditor shall disclose the following information about the interest rate and payments:

(1) *Form of disclosures.* The information in paragraphs (s)(2)–(4) of this section shall be in the form of a table, with no more than five columns, with headings and format substantially similar to Model Clause H–4(E), H–4(F), H–4(G), or H–4(H) in Appendix H to this part. The table shall contain only the information required in paragraphs (s)(2)–(4) of this section, shall be placed in a prominent location, and shall be in a minimum 10-point font.

(2) *Interest rates—(i) Amortizing loans.* (A) For a fixed-rate mortgage, the interest rate at consummation.

(B) For an adjustable-rate or step-rate mortgage—

(*1*) The interest rate at consummation and the period of time until the first interest rate adjustment may occur, labeled as the "introductory rate and monthly payment";

(*2*) The maximum interest rate that may apply during the first five years after consummation and the earliest date on which that rate may apply, labeled as "maximum during first five years"; and

(*3*) The maximum interest rate that may apply during the life of the loan and the earliest date on which that rate may apply, labeled as "maximum ever."

(C) If the loan provides for payment increases as described in paragraph (s)(3)(i)(B) of this section, the interest rate in effect at the time the first such payment increase is scheduled to occur and the date on which the increase will occur, labeled as "first adjustment" if the loan is an adjustable-rate mortgage or, otherwise, labeled as "first increase."

(ii) *Negative amortization loans.* For a negative amortization loan—

(A) The interest rate at consummation and, if it will adjust after consummation, the length of time until it will adjust, and the label "introductory" or "intro";

(B) The maximum interest rate that could apply when the consumer must begin making fully amortizing payments under the terms of the legal obligation;

(C) If the minimum required payment will increase before the consumer must begin making fully amortizing payments, the maximum interest rate that could apply at the time of the first payment increase and the date the increase is scheduled to occur; and

(D) If a second increase in the minimum required payment may occur before the consumer must begin making fully amortizing payments, the maximum interest rate that could apply at the time of the second payment increase and the date the increase is scheduled to occur.

(iii) *Introductory rate disclosure for amortizing adjustable-rate mortgages.* For an amortizing adjustable-rate mortgage, if the interest rate at consummation is less than the fully-indexed rate, placed in a box directly beneath the table required by paragraph (s)(1) of this section, in a format substantially similar to Model Clause H–4(I) in Appendix H to this part—

(A) The interest rate that applies at consummation and the period of time for which it applies;

(B) A statement that, even if market rates do not change, the interest rate will increase at the first adjustment and a designation of the place in sequence of the month or year, as applicable, of such rate adjustment; and

(C) The fully-indexed rate.

(3) *Payments for amortizing loans—(i) Principal and interest payments.* If all periodic payments will be applied to accrued interest and principal, for each interest rate disclosed under paragraph (s)(2)(i) of this section—

(A) The corresponding periodic principal and interest payment, labeled as "principal and interest;"

(B) If the periodic payment may increase without regard to an interest rate adjustment, the payment that corresponds to the first such increase and the earliest date on which the increase could occur;

(C) That an escrow account is required, if applicable, and an estimate of the amount of taxes and insurance, including any mortgage insurance; and

(D) The sum of the amounts disclosed under paragraphs (s)(3)(i)(A) and (C) of this section or (s)(3)(i)(B) and (C) of this section, as applicable, labeled as "total estimated monthly payment."

(ii) *Interest-only payments.* If the loan is an interest-only loan, for each interest rate disclosed under paragraph (s)(2)(i) of this section, the corresponding periodic payment and—

(A) If the payment will be applied to only accrued interest, the amount applied to interest, labeled as "interest payment," and a statement that none of the payment is being applied to principal;

(B) If the payment will be applied to accrued interest and principal, the earliest date that such payments will be required and an itemization of the amount applied to accrued interest and the amount applied to principal, labeled as "interest payment" and "principal payment," respectively;

(C) The escrow information described in paragraph (s)(3)(i)(C) of this section; and

(D) The sum of all amounts required to be disclosed under paragraphs (s)(3)(ii)(A) and (C) of this section or (s)(3)(ii)(B) and (C) of this section, as applicable, labeled as "total estimated monthly payment."

(4) *Payments for negative amortization loans.* For negative amortization loans:

(i)(A) The minimum periodic payment required until the first payment increase or interest rate increase, corresponding to the interest rate disclosed under paragraph (s)(2)(ii)(A) of this section;

(B) The minimum periodic payment that would be due at the first payment increase and the second, if any, corresponding to the interest rates described in paragraphs (s)(2)(ii)(C) and (D) of this section; and

(C) A statement that the minimum payment pays only some interest, does not repay any principal, and will cause the loan amount to increase;

(ii) The fully amortizing periodic payment amount at the earliest time when such a payment must be made, corresponding to the interest rate disclosed under paragraph (s)(2)(ii)(B) of this section; and

(iii) If applicable, in addition to the payments in paragraphs (s)(4)(i) and (ii) of this section, for each interest rate disclosed under paragraph (s)(2)(ii) of this section, the amount of the fully amortizing periodic payment, labeled as the "full payment option," and a statement that these payments pay all principal and all accrued interest.

(5) *Balloon payments.* (i) Except as provided in paragraph (s)(5)(ii) of this section, if the transaction will require a balloon payment, defined as a payment that is more than two times a regular periodic payment, the balloon payment shall be disclosed separately from other periodic payments disclosed in the table under this paragraph (s), outside the table and in a manner substantially similar to Model Clause H–4(J) in Appendix H to this part.

(ii) If the balloon payment is scheduled to occur at the same time as another payment required to be disclosed in the table pursuant to paragraph (s)(3) or (s)(4) of this section, then the balloon payment must be disclosed in the table.

(6) *Special disclosures for loans with negative amortization.* For a negative amortization loan, the following information, in close proximity to the table required in paragraph (s)(1) of this section, with headings, content, and format substantially similar to Model Clause H–4(G) in Appendix H to this part:

(i) The maximum interest rate, the shortest period of time in which such interest rate could be reached, the amount of estimated taxes and insurance included in each payment disclosed, and a statement that the loan offers payment options, two of which are shown.

(ii) The dollar amount of the increase in the loan's principal balance if the consumer makes only the minimum required payments for the maximum possible time and the earliest date on which the consumer must begin making fully amortizing payments, assuming that the maximum interest rate is reached at the earliest possible time.

(7) *Definitions.* For purposes of this § 226.18(s):

(i) The term "adjustable-rate mortgage" means a transaction secured by real property or a dwelling for which the annual percentage rate may increase after consummation.

(ii) The term "step-rate mortgage" means a transaction secured by real property or a dwelling for which the interest rate will change after consummation, and the rates that will apply and the periods for which they will apply are known at consummation.

(iii) The term "fixed-rate mortgage" means a transaction secured by real property or a dwelling that is not an adjustable-rate mortgage or a step-rate mortgage.

(iv) The term "interest-only" means that, under the terms of the legal obligation, one or more of the periodic payments may be applied solely to accrued interest and not to loan principal; an "interest-only loan" is a loan that permits interest-only payments.

(v) The term "amortizing loan" means a loan in which payment of the periodic payments does not result in an increase in the principal balance under the terms of the legal obligation; the term "negative amortization" means payment of periodic payments that will result in an increase in the principal balance under the terms of the legal obligation; the term "negative amortization loan" means a loan that permits payments resulting in negative amortization, other than a reverse mortgage subject to § 226.33.

(vi) The term "fully-indexed rate" means the interest rate calculated using the index value and margin at the time of consummation.

(t) "*No-guarantee-to-refinance*" *statement.* (1) *Disclosure.* For a closed-end transaction secured by real property or a dwelling, other than a transaction secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53D), the creditor shall disclose a statement that there is no guarantee the consumer can refinance the transaction to lower the interest rate or periodic payments.

(2) *Format.* The statement required by paragraph (t)(1) of this section must be in a form substantially similar to Model Clause H–4(K) in Appendix H to this part.

■ 3. Appendix H to Part 226 is amended by:

■ A. Adding entries for H–4(E) through H–4(K) to the table of contents at the beginning of the appendix; and

■ B. Adding new Model Clauses H–4(E) through H–4(K) in numerical order.

Appendix H to Part 226—Closed-End Model Forms and Clauses

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BILLING CODE P

H-4(E) Fixed Rate Mortgage Interest Rate and Payment Summary Model Clause

INTEREST RATE AND PAYMENT SUMMARY

	Rate & Monthly Payment
Interest Rate	____%
Principal + Interest Payment	$_____
Est. Taxes + Insurance (Escrow) • [Includes [Private] Mortgage Insurance]	$_____
Total Est. Monthly Payment	**$____**

H-4(F) Adjustable-Rate Mortgage or Step-Rate Mortgage Interest Rate and Payment Summary Model Clause

INTEREST RATE AND PAYMENT SUMMARY

	INTRODUCTORY Rate & Monthly Payment (for first (*period*))	[MAXIMUM during FIRST FIVE YEARS (*date*)]	MAXIMUM EVER (as early as (*date*))
Interest Rate	___%	[___%]	___%
Principal + Interest Payment	$_____	[$_____]	$_____
Est. Taxes + Insurance [(Escrow)] • [Includes [Private] Mortgage Insurance]	[$_____]	[$_____]	[$_____]
Total Est. Monthly Payment	**$_____**	**[$_____]**	**$_____**

H-4(G) Mortgage with Negative Amortization Interest Rate and Payment Summary Model Clause

INTEREST RATE AND PAYMENT SUMMARY

[This loan offers you several monthly payment options. The table below shows you what your payments would be under two of these options **if the interest rate reached its maximum of** ___% in the (*period*) of this loan.]

[All payments shown in the table include $___ for estimated taxes and insurance [(escrow)].

	(***Date***) [(*period*) [intro]]	[(***Date***) (1st adjustment)]	[(***Date***) (2nd adjustment)]	(***Date***) + every (*period*) after
Maximum Interest Rate	___% [(intro rate)]	**[___%]**	**[___%]**	___% (max. ever)
Full Payment Option *Monthly payments cover all principal and interest.*	**$_____**	**[$_____]**	**[$_____]**	**$_____**
Minimum Payment Option *Initial monthly payments cover no principal and only some interest and increase your loan amount.*	$_____	[$_____]	[$_____]	$_____

You will borrow an additional $_____ by (date) if you make only minimum payments on this loan.

H-4(H) Fixed Rate Mortgage with Interest Only Interest Rate and Payment Summary Model Clause

INTEREST RATE AND PAYMENT SUMMARY

	INTRODUCTORY Rate & Monthly Payment (for first ____ years)	MAXIMUM EVER (as early as ____)
Interest Rate	____%	____%
Principal Payment	- none -	$_____
Interest Payment	$_____	$_____
Est. Taxes + Insurance (Escrow)	$_____	$_____
Total Est. Monthly Payment	**$____**	**$____**

BILLING CODE C

H–4(I)—Introductory Rate Model Clause

[Introductory Rate Notice
You have a discounted introductory rate of ________ % that ends after (period).
In the (period in sequence), even if market rates do not change, this rate will increase to ____ %.]

H–4(J)—Balloon Payment Model Clause

[Final Balloon Payment due (date):
$________]

H–4(K)—"No-Guarantee-to-Refinance" Statement Model Clause

There is no guarantee that you will be able to refinance to lower your rate and payments.

* * * * *

■ 4. In Supplement I to Part 226:

■ A. Under *Section 226.17—General Disclosure Requirements, 17(a) Form of disclosures, Paragraph 17(a)(1),* paragraph 1 is revised.

■ B. Under *Section 226.18—Content of Disclosures, 18(g) Payment schedule,* paragraph 6 is added, and an entry for *18(s) Interest rate and payment summary for mortgage transactions* is added.

■ C. Under Appendixes G and H—Open-End and Closed-End Model Forms and Clauses, paragraph 1 is revised.

■ D. Under Appendix H—Closed-End Model Forms and Clauses, paragraph 7 is revised.

The additions and revisions read as follows:

Supplement I to Part 226—Official Staff Interpretations

* * * * *

Subpart C—Closed-End Credit

* * * * *

Section 226.17—General Disclosure Requirements

17(a) Form of disclosures.

Paragraph 17(a)(1).

1. *Clear and conspicuous.* This standard requires that disclosures be in a reasonably understandable form. For example, while the regulation requires no mathematical progression or format, the disclosures must be presented in a way that does not obscure the relationship of the terms to each other. In addition, although no minimum type size is mandated (except for the interest rate and payment summary for mortgage transactions required by § 228.18(s)), the disclosures must be legible, whether typewritten, handwritten, or printed by computer.

* * * * *

Section 226.18—Content of Disclosures

* * * * *

18(g) Payment schedule.

* * * * *

6. *Mortgage transactions.* Section 226.18(g) applies only to closed-end transactions other than transactions that are subject to § 226.18(s). Section 226.18(s) applies to closed-end transactions secured by real property or a dwelling. Thus, if a closed-end consumer credit transaction is secured by real property or a dwelling, the creditor discloses an interest rate and payment summary table in accordance with § 226.18(s) and does not observe the requirements of § 226.18(g). On the other hand, if a closed-end consumer credit transaction is not secured by real property or a dwelling, the creditor discloses a payment schedule in accordance with § 226.18(g) and does not observe the requirements of § 226.18(s).

* * * * *

18(s) Interest rate and payment summary for mortgage transactions.

1. *In general.* Section 226.18(s) prescribes format and content for disclosure of interest rates and monthly (or other periodic) payments for mortgage loans. The information in § 226.18(s)(2)–(4) is required to be in the form of a table, except as otherwise provided, with headings and format substantially similar to Model Clause H–4(E), H–4(F), H–4(G), or H–4(H) in Appendix H to this part. A disclosure that does not include the shading shown in a model clause but otherwise follows the model clause's headings and format is substantially similar to that model clause. In all cases, the table should have no more than five vertical columns corresponding to applicable interest rates at various times during the loan's term; corresponding payments would be shown in horizontal rows. Certain loan types and terms are defined for purposes of § 226.18(s) in § 226.18(s)(7).

2. *Amortizing loans.* Loans described as amortizing in §§ 226.18(s)(2)(i) and 226.18(s)(3) include interest-only loans if they do not also permit negative amortization. (For rules relating to loans with balloon payments, see § 226.18(s)(5)). If an amortizing loan is an adjustable-rate mortgage with an introductory rate (less than the fully-indexed rate), creditors must provide a special explanation of introductory rates. *See* § 226.18(s)(2)(iii).

3. *Negative amortization.* For negative amortization loans, creditors must follow the rules in §§ 226.18(s)(2)(ii) and 226.18(s)(4) in disclosing interest rates and monthly payments. Loans with negative amortization also require special explanatory disclosures about rates and payments. *See* § 226.18(s)(6). Loans with negative amortization include "payment option" loans, in which the consumer is permitted to make minimum payments that will cover only some of the interest accruing each month. *See also* comment 17(c)(1)–12, regarding graduated-payment adjustable-rate mortgages.

18(s)(2) Interest rates.

18(s)(2)(i) Amortizing loans.

Paragraph 18(s)(2)(i)(A).

1. *Fixed rate loans—payment increases.* Although the interest rate will not change after consummation for a fixed-rate loan, some fixed-rate loans may have periodic payments that increase after consummation. For example, the terms of the legal obligation may permit the consumer to make interest-only payments for a specified period such as the first five years after consummation. In such cases, the creditor must include the increased payment under § 226.18(s)(3)(ii)(B) in the payment row, and must show the interest rate in the column for that payment, even though the rate has not changed since consummation. See also comment 17(c)(1)–13, regarding growth equity mortgages.

Paragraph 18(s)(2)(i)(B).

1. *Adjustable-rate mortgages and step-rate mortgages.* Creditors must disclose more than one interest rate for adjustable-rate mortgages and step-rate mortgages, in accordance with § 226.18(s)(2)(i)(B). Creditors must assume that an adjustable-rate mortgage's interest rate will increase after consummation as rapidly as possible, taking into account the terms of the legal obligation.

2. *Maximum interest rate during first five years—adjustable-rate mortgages and step-rate mortgages.* The creditor must disclose the maximum rate that could apply during the first five years after consummation. If there are no interest rate caps other than the maximum rate required under § 226.30, then the creditor should disclose only the rate at consummation and the maximum rate. Such a table would have only two columns.

i. For an adjustable-rate mortgage, the creditor must take into account any interest rate caps when disclosing the maximum interest rate during the first five years. The creditor must also disclose the earliest date on which that adjustment may occur.

ii. If the transaction is a step-rate mortgage, the creditor should disclose the rate that will apply after consummation. For example, the legal obligation may provide that the rate is 6 percent for the first two years following consummation, and then increases to 7 percent for at least the next three years. The creditor should disclose the maximum rate during the first five years as 7 percent and the date on which the rate is scheduled to increase to 7 percent.

3. *Maximum interest rate at any time.* The creditor must disclose the maximum rate that could apply at any time during the term of the loan and the earliest date on which the maximum rate could apply.

i. For an adjustable-rate mortgage, the creditor must take into account any interest rate caps in disclosing the maximum interest rate. For example, if the legal obligation provides that at each annual adjustment the rate may increase by no more than 2 percentage points, the creditor must take this limit into account in determining the earliest date on which the maximum possible rate may be reached.

ii. For a step-rate mortgage, the creditor should disclose the highest rate that could apply under the terms of the legal obligation and the date on which that rate will first apply.

Paragraph 18(s)(2)(i)(C).

1. *Payment increases.* For some loans, the payment may increase following consummation for reasons unrelated to an interest rate adjustment. For example, an adjustable-rate mortgage may have an introductory fixed-rate for the first five years following consummation and permit the borrower to make interest-only payments for the first three years. Under § 226.18(s)(3)(ii)(B), the creditor must disclose the first payment that will be applied to both principal and interest. In such a case, § 226.18(s)(2)(i)(C) requires that the creditor also disclose the interest rate that corresponds to the first payment of principal and interest, even though the interest rate will not adjust at that time. The table would show, from left to right: The interest rate and payment at consummation with the payment itemized to show that the payment is being applied to interest only; the interest rate and payment when the interest-only option ends; the maximum interest rate and payment during the first five years; and the maximum possible interest rate and payment.

18(s)(2)(ii) Negative amortization loans.

1. *Rate at consummation.* In all cases the interest rate in effect at consummation must be disclosed, even if it will apply only for a short period such as one month.

2. *Rates for adjustable-rate mortgages.* The creditor must assume that interest rates rise as quickly as possible after consummation, in accordance with any interest rate caps under the legal obligation. For adjustable-rate mortgages with no rate caps except a life-time maximum, creditors must assume that the interest rate reaches the maximum at the first adjustment. For example, assume that the legal obligation provides for an interest rate at consummation of 1.5 percent. One month after consummation, the interest rate adjusts and will adjust monthly thereafter, according to changes in the index. The consumer may make payments that cover only part of the interest accrued each month, until the date the principal balance reaches 115 percent of its original balance, or until the end of the fifth year after consummation, whichever comes first. The maximum possible rate is 10.5 percent. No other limits on interest rates apply. The minimum required payment adjusts each year, and may increase by no more than 7.5 percent over the previous year's payment. The creditor should disclose the following rates and the dates when they are scheduled to occur: A rate of 1.5 percent for the first month following consummation and the minimum payment; a rate of 10.5 percent, and the corresponding minimum payment taking into account the 7.5 percent limit on payment increases, at the beginning of the second year; and a rate of 10.5 percent and the corresponding minimum payment taking into account the 7.5 percent payment increase limit, at the beginning of the third year. The creditor also must disclose the rate of 10.5 percent, the fully amortizing payment, and the date on which the consumer must first make such a payment under the terms of the legal obligation.

18(s)(2)(iii) Introductory rate disclosure for amortizing adjustable-rate mortgage.

1. *Introductory rate.* In some adjustable-rate mortgages, creditors may set an initial interest rate that is lower than the fully-indexed rate at consummation. For amortizing loans with an introductory rate, creditors must disclose the information required in § 226.18(s)(2)(iii) directly below the table.

Paragraph 18(s)(2)(iii)(B).

1. *Place in sequence.* "Designation of the place in sequence" refers to identifying the month or year, as applicable, of the change in the rate resulting from the expiration of an introductory rate by its place in the sequence of months or years, as applicable, of the transaction's term. For example, if a transaction has a discounted rate for the first three years, § 226.18(s)(2)(iii)(B) requires a statement such as, "In the fourth year, even if market rates do not change, this rate will increase to __%."

Paragraph 18(s)(2)(iii)(C).

1. *Fully-indexed rate.* The fully-indexed rate is defined in § 226.18(s)(7) as the index plus the margin at consummation. For purposes of § 226.18(s)(2)(iii)(C), "at consummation" refers to disclosures delivered at consummation, or three business days before consummation pursuant to § 226.19(a)(2)(ii); for early disclosures delivered within three business days after receipt of a consumer's application pursuant to § 226.19(a)(1), the fully-indexed rate disclosed under § 226.18(s)(2)(iii)(C) may be based on the index in effect at the time the disclosures are provided. The index in effect at consummation (or at the time of early disclosures) need not be used if a contract provides for a delay in the implementation of changes in an index value. For example, if the contract specifies that rate changes are based on the index value in effect 45 days before the change date, creditors may use any index value in effect during the 45 days before consummation (or any earlier date of disclosure) in calculating the fully-indexed rate to be disclosed.

18(s)(3) Payments for amortizing loans.

1. *Payments corresponding to interest rates.* Creditors must disclose the periodic payment that corresponds to each interest rate disclosed under § 226.18(s)(2)(i)(A)–(C). The corresponding periodic payment is the regular payment for each such interest rate, without regard to any final payment that differs from others because of the rounding of periodic payments to account for payment amounts including fractions of cents. Balloon payments, however, must be disclosed as provided in § 226.18(s)(5).

2. *Principal and interest payment amounts; examples.*

i. For fixed-rate interest-only transactions, § 226.18(s)(3)(ii)(B) requires scheduled increases in the regular periodic payment amounts to be disclosed along with the date of the increase. For example, in a fixed-rate interest-only loan, a scheduled increase in the payment amount from an interest-only payment to a fully amortizing payment must be disclosed. Similarly, in a fixed-rate balloon loan, the balloon payment must be disclosed in accordance with § 226.18(s)(5).

ii. For adjustable-rate mortgage transactions, § 226.18(s)(3)(i)(A) requires that for each interest rate required to be disclosed under § 226.18(s)(2)(i) (the interest rate at consummation, the maximum rate during the first five years, and the maximum possible rate) a corresponding payment amount must be disclosed.

iii. The format of the payment disclosure varies depending on whether all regular periodic payment amounts will include principal and interest, and whether there will be an escrow account for taxes and insurance.

Paragraph 18(s)(3)(i)(C).

1. *Taxes and insurance.* An estimated payment amount for taxes and insurance must be disclosed if the creditor will establish an escrow account for such amounts. The payment amount must include estimated amounts for property taxes and premiums for mortgage-related insurance required by the creditor, such as insurance against loss of or damage to property, or

against liability arising out of the ownership or use of the property, or insurance protecting the creditor against the consumer's default or other credit loss. Premiums for credit insurance, debt suspension and debt cancellation agreements, however, should not be included. Except for periodic mortgage insurance premiums included in the escrow payment under § 226.18(s)(3)(i)(C), amounts included in the escrow payment disclosure such as property taxes and homeowner's insurance generally are not finance charges under § 226.4 and, therefore, do not affect other disclosures, including the finance charge and annual percentage rate.

2. *Mortgage insurance.* Payment amounts under § 226.18(s)(3)(i) should reflect the consumer's mortgage insurance payments until the date on which the creditor must automatically terminate coverage under applicable law, even though the consumer may have a right to request that the insurance be cancelled earlier. The payment amount must reflect the terms of the legal obligation, as determined by applicable state or other law. For example, assume that under applicable law, mortgage insurance must terminate after the 130th scheduled monthly payment, and the creditor collects at closing and places in escrow two months of premiums. If, under the legal obligation, the creditor will include mortgage insurance premiums in 130 payments and refund the escrowed payments when the insurance is terminated, payment amounts disclosed through the 130th payment should reflect premium payments. If, under the legal obligation, the creditor will apply the amount escrowed to the two final insurance payments, payments disclosed through the 128th payment should reflect premium payments. The escrow amount reflected on the disclosure should include mortgage insurance premiums even if they are not escrowed and even if there is no escrow account established for the transaction.

Paragraph 18(s)(3)(i)(D).

1. *Total monthly payment.* For amortizing loans, each column should add up to a total estimated payment. The total estimated payment amount should be labeled. If periodic payments are not due monthly, the creditor should use the appropriate term such as "quarterly" or "annually."

18(s)(3)(ii) Interest-only payments.

1. *Interest-only loans that are also negative amortization loans.* The rules in § 226.18(s)(3)(ii) for disclosing payments on interest-only loans apply only if the loan is not also a negative amortization loan. If the loan is a negative amortization loan, even if it also has an interest-only feature, payments are disclosed under the rules in § 226.18(s)(4).

Paragraph 18(s)(3)(ii)(C).

1. *Escrows.* See the commentary under § 226.18(s)(3)(i)(C) for guidance on escrows for purposes of § 226.18(s)(3)(ii)(C).

18(s)(4) Payments for negative amortization loans.

1. *Table.* Section 226.18(s)(1) provides that tables shall include only the information required in § 226.18(s)(2)–(4). Thus, a table for a negative amortization loan must contain no more than two horizontal rows of payments and no more than five vertical columns of interest rates.

2. *Payment amounts.* The payment amounts disclosed under § 226.18(s)(4) are the minimum or fully amortizing periodic payments, as applicable, corresponding to the interest rates disclosed under § 226.18(s)(2)(ii). The corresponding periodic payment is the regular payment for each such interest rate, without regard to any final payment that differs from the rest because of the rounding of periodic payments to account for payment amounts including fractions of cents.

Paragraph 18(s)(4)(i).

1. *Minimum required payments.* In one row of the table, the creditor must disclose the minimum required payment in each column of the table, corresponding to each interest rate or adjustment required in § 226.18(s)(2)(ii). The payments in this row must be calculated based on an assumption that the consumer makes the minimum required payment for as long as possible under the terms of the legal obligation. This row should be identified as the minimum payment option, and the statement required by § 226.18(s)(4)(i)(C) should be included in the heading for the row.

Paragraph 18(s)(4)(iii).

1. *Fully amortizing payments.* In one row of the table, the creditor must disclose the fully amortizing payment in each column of the table, corresponding to each interest rate required in § 226.18(s)(2)(ii). The creditor must assume, for purposes of calculating the amounts in this row that the consumer makes only fully amortizing payments starting with the first scheduled payment.

18(s)(5) Balloon payments.

1. *General.* A balloon payment is one that is more than two times the regular periodic payment. In a reverse mortgage transaction, the single payment is not considered a balloon payment. A balloon payment must be disclosed outside and below the table, unless the balloon payment coincides with an interest rate adjustment or a scheduled payment increase. In those cases, the balloon payment must be disclosed in the table.

18(s)(6) Special disclosures for loans with negative amortization.

1. *Escrows.* See the commentary under § 226.18(s)(3)(i)(C) for guidance on escrows for purposes of § 226.18(s)(6). Under that guidance, because mortgage insurance payments decline over a loan's term, the payment amounts shown in the table should reflect the mortgage insurance payment that will be applicable at the time each disclosed periodic payment will be in effect. Accordingly, the disclosed mortgage insurance payment will be zero if it corresponds to a periodic payment that will occur after the creditor will be legally required to terminate mortgage insurance. On the other hand, because only one escrow amount is disclosed under § 226.18(s)(6) for negative amortization loans and escrows are not itemized in the payment amounts, the single escrow amount disclosed should reflect the mortgage insurance amount that will be collected at the outset of the loan's term, even though that amount will decline in the future and ultimately will be discontinued pursuant to the terms of the mortgage insurance policy.

* * * * *

Appendixes G and H—Open-End and Closed-End Model Forms and Clauses

1. *Permissible changes.* Although use of the model forms and clauses is not required, creditors using them properly will be deemed to be in compliance with the regulation with regard to those disclosures. Creditors may make certain changes in the format or content of the forms and clauses and may delete any disclosures that are inapplicable to a transaction or a plan without losing the act's protection from liability, except formatting changes may not be made to model forms and samples in H–18, H–19, H–20, H–21, H–22, H–23, G–2(A), G–3(A), G–4(A), G–10(A)–(E), G–17(A)–(D), G–18(A) (except as permitted pursuant to § 226.7(b)(2)), G–18(B)–(C), G–19, G–20, and G–21, or to the model clauses in H–4(E), H–4(F), H–4(G), and H–4(H). The rearrangement of the model forms and clauses may not be so extensive as to affect the substance, clarity, or meaningful sequence of the forms and clauses. Creditors making revisions with that effect will lose their protection from civil liability. Except as otherwise specifically required, acceptable changes include, for example:

i. Using the first person, instead of the second person, in referring to the borrower.

ii. Using "borrower" and "creditor" instead of pronouns.

iii. Rearranging the sequences of the disclosures.

iv. Not using bold type for headings.

v. Incorporating certain state "plain English" requirements.

vi. Deleting inapplicable disclosures by whiting out, blocking out, filling in "N/A" (not applicable) or "0," crossing out, leaving blanks, checking a box for applicable items, or circling applicable items. (This should permit use of multipurpose standard forms.)

vii. Using a vertical, rather than a horizontal, format for the boxes in the closed-end disclosures.

* * * * *

Appendix H—Closed-End Model Forms and Clauses

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7. *Models H–4(D) through H–4(J).* These model clauses illustrate certain notices, statements, and other disclosures required as follows:

i. Model H–4(D) illustrates the adjustment notice required under § 226.20(c), and provides examples of payment change notices and annual notices of interest rate changes.

ii. Model H–4(E) illustrates the interest rate and payment summary table required under § 226.18(s) for a fixed-rate mortgage transaction.

iii. Model H–4(F) illustrates the interest rate and payment summary table required under § 226.18(s) for an adjustable-rate or a step-rate mortgage transaction.

iv. Model H–4(G) illustrates the interest rate and payment summary table required under § 226.18(s) for a mortgage transaction with negative amortization.

v. Model H–4(H) illustrates the interest rate and payment summary table required under § 226.18(s) for a fixed-rate, interest-only mortgage transaction.

vi. Model H–4(I) illustrates the introductory rate disclosure required by § 226.18(s)(2)(iii) for an adjustable-rate mortgage transaction with an introductory rate.

vii. Model H–4(J) illustrates the balloon payment disclosure required by § 226.18(s)(5) for a mortgage transaction with a balloon payment term.

viii. Model H–4(K) illustrates the no-guarantee-to-refinance statement required by § 226.18(t) for a mortgage transaction.

* * * * *

By order of the Board of Governors of the Federal Reserve System, August 13, 2010.

Robert deV. Frierson,

Deputy Secretary of the Board.

[FR Doc. 2010–20663 Filed 9–23–10; 8:45 am]

BILLING CODE P

FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Docket No. R–1378]

Regulation Z; Truth in Lending

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule; official staff commentary.

SUMMARY: The Board is publishing final rules amending Regulation Z (Truth in Lending). The final rule implements Section 131(g) of the Truth in Lending Act (TILA), which was enacted on May 20, 2009, as Section 404(a) of the Helping Families Save Their Homes Act. TILA Section 131(g) became effective immediately upon enactment and established a new requirement for notifying consumers of the sale or transfer of their mortgage loans.

Consistent with the statute, the final rule requires a purchaser or assignee that acquires a loan to provide the disclosures in writing no later than 30 days after the date on which the loan was sold, transferred or assigned. Certain exceptions may apply if the covered person transfers or assigns the loan to another party on or before the 30th day.

DATES: *Effective Date.* This final rule is effective on January 1, 2011.

Mandatory Compliance Date. The mandatory compliance date is January 1, 2011. Covered persons may immediately comply with this amendment or continue to comply with 12 CFR 226.39 until the mandatory compliance date.

FOR FURTHER INFORMATION CONTACT: Jelena McWilliams, Attorney, or Paul Mondor, Senior Attorney; Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, DC 20551, at (202) 452–2412 or (202) 452–3667. For users of Telecommunications Device for the Deaf (TDD) only, contact (202) 263–4869.

SUPPLEMENTARY INFORMATION:

I. Background

The Truth in Lending Act (TILA), 15 U.S.C. 1601 *et seq.,* seeks to promote the informed use of consumer credit by requiring disclosures about its costs and terms. TILA requires additional disclosures for loans secured by consumers' homes and permits consumers to rescind certain transactions that involve their principal dwelling. TILA directs the Board to prescribe regulations to carry out its purposes. TILA specifically authorizes the Board, among other things, to issue regulations that contain such classifications, differentiations, or other provisions, or that provide for such adjustments and exceptions for any class of transactions, that in the Board's judgment are necessary or proper to effectuate the purposes of TILA, facilitate compliance with TILA, or prevent circumvention or evasion of TILA. 15 U.S.C. 1604(a). TILA is implemented by the Board's Regulation Z. 12 CFR part 226. An Official Staff Commentary interprets the requirements of the regulation and provides guidance to creditors in applying the rules to specific transactions. *See* 12 CFR part 226, Supp. I.

On May 20, 2009, the Helping Families Save Their Homes Act of 2009 (the "2009 Act") was signed into law. Public Law 111–22, 123 Stat. 1632. Section 404(a) of the 2009 Act amended TILA to establish a new requirement for notifying consumers of the sale or transfer of their mortgage loans. The purchaser or assignee that acquires the loan must provide the required disclosures no later than 30 days after the date on which it acquired the loan. This provision is contained in TILA Section 131(g), 15 U.S.C. 1641(g), which applies to any consumer credit transaction secured by the principal dwelling of a consumer. Consequently, the disclosure requirements in Section 131(g) apply to both closed-end mortgage loans and open-end home equity lines of credit.

Section 131(g) became effective immediately upon enactment on May 20, 2009, and did not require the issuance of implementing regulations. Mortgage loans sold, or otherwise transferred on or after that date became subject to the requirements of Section 131(g), and failure to comply can result in civil liability under TILA Section 130(a). *See* 15 U.S.C. 1640(a). In November 2009, the Board issued an interim rule that was effective immediately upon publication, so that parties subject to the rule would have guidance on how to interpret and comply with the statutory requirements. 74 FR 60143, Nov. 20, 2009.

Under the Real Estate Settlement Procedures Act (RESPA), consumers must be notified when the servicer of their mortgage loan has changed.[1] The 2009 Act's legislative history reflects that, in addition to the information provided under RESPA, the Congress intended to provide consumers with information about the identity of the owner of their mortgage loan. In some cases, consumers that have an extended right to rescind the loan under TILA Section 125, 15 U.S.C. 1635, can assert that right against the purchaser or assignee. *See* TILA Section 131(c), 15 U.S.C. 1641(c). Among other things, the 2009 Act seeks to ensure that consumers attempting to exercise this right know the identity of the assignee and how to contact the assignee or its agent for that purpose. *See* 155 Cong. Rec. S5098–99 (daily ed. May 5, 2009); 155 Cong. Rec. S5173–74 (daily ed. May 6, 2009). The legislative history indicates, however, that TILA Section 131(g) was not intended to require notice when a transaction "does not involve a change in the ownership of the physical note," such as when the note holder issues mortgage-backed securities but does not transfer legal title to the loan. 155 Cong. Rec. S5099.

II. Summary of the Final Rule

The final rule requires an acquiring party to provide the disclosures in writing no later than 30 days after the date on which the loan was sold, transferred or assigned. Under the final rule, the disclosures must state (1) The name, address, and telephone number of the new owner; (2) the transfer date; (3) the name, address, and telephone number of an agent or other party authorized to receive the consumer's rescission notice and resolves issues concerning the consumer's payments on the loan (if other than owner); and (4) where the transfer of ownership is recorded.

Consistent with the statute and legislative intent, the final rule implements Section 404(a) of the 2009 Act by applying the new disclosure requirements to any person or entity that acquires ownership of an existing consumer mortgage loan, whether the acquisition occurs as a result of a

[1] RESPA is implemented by Regulation X, 24 CFR part 3500, which is issued by the Department of Housing and Urban Development (HUD).