FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Regulation Z; Docket No. R–1366]

Truth in Lending

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule; request for public comment.

SUMMARY: The Board proposes to amend Regulation Z, which implements the Truth in Lending Act (TILA), and the staff commentary to the regulation, as part of a comprehensive review of TILA's rules for closed-end credit. This proposal would revise the rules for disclosures of closed-end credit secured by real property or a consumer's dwelling, except for rules regarding rescission and reverse mortgages, which the Board anticipates will be reviewed at a later date. Published elsewhere in today's Federal Register is the Board's proposal regarding rules for disclosures of open-end credit secured by a consumer's dwelling.

Disclosures provided at application would include a Board-published one-page ''*Key Questions to Ask About Your Mortgage*'' document that explains potentially risky loan features, and a Board-published one-page ''*Fixed* vs. *Adjustable Rate Mortgages*'' document. Transaction-specific disclosures required within three business days of application would summarize key loan terms. The calculation of the annual percentage rate and the finance charge would be revised to be more comprehensive, and their disclosures improved. Consumers would receive a ''final'' TILA disclosure at least three business days before consummation. Certain new post-consummation disclosures would be required. In addition, the proposed revisions would prohibit certain payments to mortgage brokers and loan officers that are based on the loan's terms or conditions, and prohibit steering consumers to transactions that are not in their interest to increase compensation received.

Rules regarding eligibility restrictions and disclosures for credit insurance and debt cancellation or debt suspension coverage would apply to all closed-end and open-end credit transactions.

DATES: Comments must be received on or before December 24, 2009.

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:* Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551.

All public comments are available from the Board's Web site at *http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm* as submitted, unless modified for technical reasons. Accordingly, your 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: Jamie Z. Goodson, Jelena McWilliams, Nikita M. Pastor, or Maureen C. Yap, Attorneys; Paul Mondor, Senior Attorney; or Kathleen C. Ryan, Senior Counsel. Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, at (202) 452–3667 or 452–2412; for users of Telecommunications Device for the Deaf (TDD) only, contact (202) 263–4869.

SUPPLEMENTARY INFORMATION:

I. Background on 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, or administrative sanction.

II. Summary of Major Proposed Changes

The goal of the proposed amendments to Regulation Z is to improve the effectiveness of disclosures that creditors provide to consumers in connection with an application and throughout the life of a mortgage. The proposed changes are the result of the Board's review of the provisions that apply to closed-end mortgage transactions. The proposal would apply to all closed-end credit transactions secured by real property or a dwelling, and would not be limited to credit secured by the consumer's principal dwelling. The Board is proposing changes to the format, timing, and content of disclosures for the four main types of closed-end credit information governed by Regulation Z: (1) disclosures at application; (2) disclosures within three days after application; (3) disclosures three days before consummation; and (4) disclosures after consummation. In addition, the Board is proposing additional protections related to limits on loan originator compensation.

Disclosures at Application. The proposal contains new requirements and changes to the format and content of disclosures given at application, to make them more meaningful and easier for consumers to use. The proposed changes include:

- Providing a new one-page Board publication, entitled ''*Key Questions to Ask About Your Mortgage*,'' which would explain the potentially risky features of a loan.
- Providing a new one-page Board publication, entitled ''*Fixed* vs. *Adjustable Rate Mortgages*,'' which would explain the basic differences between such loans and would replace the lengthy Consumer Handbook on Adjustable-Rate Mortgages (CHARM booklet) currently required under Regulation Z.
- Revising the format and content of the current adjustable-rate mortgage (ARM) loan program disclosure, including: a requirement that the disclosure be in a tabular question and answer format, a streamlined plain-language disclosure of interest rate and payment information, and a new disclosure of potentially risky features, such as prepayment penalties.

Disclosures within Three Days after Application. The proposal also contains revisions to the TILA disclosures provided within three days after application (the ''early TILA disclosure'') to make the information clearer and more conspicuous. The proposed changes include:

• Revising the calculation of the finance charge and annual percentage rate (APR) so that they capture most fees and costs paid by consumers in connection with the credit transaction.

• Providing a graph that would show consumers how their APR compares to the APRs for borrowers with excellent credit and for borrowers with impaired credit.

• Summarizing key loan features, such as the loan term, amount, and type, and disclosing total settlement charges, as is currently required for the good faith estimate of settlement costs (GFE) under the Real Estate Settlement Procedures Act (RESPA) and Regulation X.

• Requiring disclosure of potential changes to the interest rate and monthly payment.

• Adopting new format requirements, including rules regarding: type size and use of boldface for certain terms, placement of information, and highlighting certain information in a tabular format.

Disclosures Three Days before Consummation. The proposal would require creditors to provide a ''final'' TILA disclosure that the consumer must receive at least three business days before consummation. In addition, two proposed alternatives regarding redisclosure of the ''final'' TILA disclosure include:

• *Alternative 1:* If any terms change after the ''final'' TILA disclosures are provided, then another final TILA disclosure would need to be provided so that the consumer receives it at least three business days before consummation.

• *Alternative 2:* If the APR exceeds a certain tolerance or an adjustable-rate feature is added after the ''final'' TILA disclosures are provided, then another final TILA disclosure would need to be provided so that the consumer receives it at least three business days before consummation. All other changes could be disclosed at consummation.

Disclosures after Consummation. The proposal would change the timing, content and types of notices provided after consummation. The proposed changes include:

• For ARMs, increasing advance notice of a payment change from 25 to 60 days, and revising the format and content of the ARM adjustment notice.

• For payment option loans with negative amortization, requiring a monthly statement to provide information about payment options that include the costs and effects of negatively-amortizing payments.

• For creditor-placed property insurance, requiring notice of the cost and coverage at least 45 days before imposing a charge for such insurance.

Loan Originator Compensation. The proposal contains new limits on originator compensation for all closed-end mortgages. The proposed changes include:

• Prohibiting certain payments to a mortgage broker or a loan officer that are based on the loan's terms and conditions.

• Prohibiting a mortgage broker or loan officer from ''steering'' consumers to transactions that are not in their interest in order to increase the mortgage broker's or loan officer's compensation.

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

The Board has amended Regulation Z numerous times since TILA simplification in 1980. In 1987, the Board revised Regulation Z to require special disclosures for closed-end ARMs secured by the borrower's principal dwelling. 52 FR 48665; Dec. 24, 1987. In 1995, the Board revised Regulation Z to implement changes to TILA by the Home Ownership and Equity Protection Act (HOEPA). 60 FR 15463; Mar. 24, 1995. HOEPA requires special disclosures and substantive protections for home-equity loans and refinancings with APRs or points and fees above certain statutory thresholds. Numerous other amendments have been made over the years to address new mortgage products and other matters, such as abusive lending practices in the mortgage and home-equity markets.

The Board's current review of Regulation Z was initiated in December 2004 with an advance notice of proposed rulemaking.[1] 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.

Beginning in 2007, the Board proposed revisions to the rules for closed-end credit in several phases:

• *HOEPA.* In 2007, the Board proposed rules under HOEPA for higher-priced mortgage loans (2007 HOEPA Proposed Rule). The final rules, approved in July 2008 (2008 HOEPA Final Rule), prohibited certain unfair or deceptive lending and servicing practices in connection with closed-end mortgages. The Board also approved revisions to advertising rules for both closed-end and open-end home-secured loans to ensure that advertisements contain accurate and balanced information and do not contain misleading or deceptive representations. The final rules also required creditors to provide consumers with transaction-specific disclosures early enough to use while shopping for a mortgage. 73 FR 44522; July 30, 2008.

• *Timing of Disclosures for Closed-End Mortgages.* On May 7, 2009, the Board approved final rules implementing the Mortgage Disclosure Improvement Act of 2008 (the MDIA).[2] The MDIA adds to the requirements of the 2008 HOEPA Final Rule regarding transaction-specific disclosures. Among other things, the MDIA and the final rules require early, transaction-specific disclosures for mortgage loans secured by dwellings even when the dwelling is not the consumer's principal dwelling, and requires waiting periods between the time when disclosures are given and consummation of the transaction. 74 FR 23289; May 19, 2009.

This proposal would revise the rules for disclosures for closed-end credit secured by real property or a consumer's dwelling. The Board anticipates reviewing the rules for rescission and reverse mortgages in the next phase of the Regulation Z review.

A. Coordination With Disclosures Required Under the Real Estate Settlement Procedures Act

The Board anticipates working with the Department of Housing and Urban Development (HUD) to ensure that TILA and Real Estate Settlement Procedures Act of 1974 (RESPA) disclosures are compatible and complementary, including potentially developing a single disclosure form that creditors could use to combine the initial disclosures required under TILA and

[1] The review was initiated pursuant to requirements of section 303 of the Riegle Community Development and Regulatory Improvement Act of 1994, section 610(c) of the Regulatory Flexibility Act of 1980, and section 2222 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996. An advance notice of proposed rulemaking is published to obtain preliminary information prior to issuing a proposed rule or, in some cases, deciding whether to issue a proposed rule.

[2] 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.

RESPA. The two statutes have different purposes but have considerable overlap. Harmonizing the two disclosure schemes would ensure that consumers receive consistent information under both laws. It may also help reduce information overload by eliminating some duplicative disclosures. Consumer testing would be used to ensure consumers could understand and use the combined disclosures. In the meantime, the Board is proposing a revised model TILA form so that commenters can see how the Board's proposed revisions to Regulation Z might be applied in practice.

RESPA, which is implemented by HUD's Regulation X, seeks to ensure that consumers are provided with timely information about the nature and costs of the settlement process and are protected from unnecessarily high real estate settlement charges. To this end, RESPA mandates that consumers receive information about the costs associated with a mortgage loan transaction, and prohibits certain business practices. Under RESPA, creditors must provide a GFE within three business days after a consumer submits a written application for a mortgage loan, which is the same time creditors must provide the early TILA disclosure. RESPA also requires a statement of the actual costs imposed at loan settlement (HUD–1 settlement statement). In November 2008, HUD published revised RESPA rules, including new GFE and HUD–1 settlement statement forms, which lenders, mortgage brokers, and settlement agents must use beginning on January 1, 2010. 73 FR 68204; Nov. 17, 2008. In addition to revised disclosures of settlement costs, the revised GFE now includes loan terms, some of which would also appear on the TILA disclosure, such as whether there is a prepayment penalty and the borrower's interest rate and monthly payment. The revised GFE form was developed through HUD's consumer testing.

TILA, which is implemented by the Board's Regulation Z, governs the disclosure of the APR and certain loan terms. This proposal contains a revised model TILA form that was developed through consumer testing. In addition to a revised disclosure of the APR and loan terms, the revised TILA disclosure would include the total settlement charges that appear on the GFE required under RESPA. Total settlement charges would be added to the TILA form because consumer testing conducted by the Board found that consumers wanted to have settlement charges disclosed on the TILA form.

The proposed revised TILA form and HUD's revised GFE would represent significant improvements, but overlap between the two forms could be eliminated to reduce information overload and consistency issues. There have been previous efforts to develop a combined TILA and RESPA disclosure form, which were fueled by the amount, complexity, and overlap of information in the disclosures. Under a 1996 congressional directive, the Board and HUD studied ways to simplify and improve the disclosures. In July 1998, the Board and HUD submitted a joint report to Congress that provided a broad outline intended to be a starting point for consideration of legislative reform of the mortgage disclosure requirements (the 1998 Joint Report).[3] The 1998 Joint Report included a recommendation for combining and simplifying the RESPA and TILA disclosure forms to satisfy the requirements of both laws. In addition, The 1998 Joint Report recommended that the timing of the TILA and RESPA disclosures be coordinated. Recent regulatory changes addressed the timing issues so that initial disclosures required under TILA and RESPA would be delivered at the same time.

B. The Bankruptcy Act's Amendment to TILA

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (Bankruptcy Act) primarily amended the federal bankruptcy code, but also contained several provisions amending TILA. With respect to open-end and closed-end dwelling-secured credit, the Bankruptcy Act requires that the credit application disclosure contain a statement warning consumers that if the loan exceeds the fair market value of the dwelling, then the interest on that portion of the loan is not tax deductible, and the consumer should consult a tax advisor for further information on tax deductibility. This proposal would implement this Bankruptcy Act provision.

C. The MDIA's Amendments to TILA

On July 30, 2008, Congress enacted the MDIA.[4] The MDIA codified some of the requirements of the Board's 2008 HOEPA Final Rule, which required transaction-specific 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.[5] 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. In addition, the MDIA required 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 Board implemented these MDIA requirements in final rules published May 19, 2009, and effective July 30, 2009. 74 FR 23289; May 19, 2009.

The MDIA also requires payment examples if the interest rate or payments can change. Such disclosures are to be formatted in accordance with the results of consumer testing conducted by the Board. Those provisions of the MDIA will not become effective until January 30, 2011, or any earlier compliance date established by the Board. This proposal would implement those MDIA provisions.

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. Currently, Regulation Z requires creditors to provide at application an ARM loan program disclosure and the CHARM booklet. An early TILA disclosure is required within three business days of application and at least seven business days before consummation for closed-end mortgages.

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

[3] Bd. of Governors of the Fed. Reserve Sys. and U.S. Dep't of Hous. and Urban Dev., *Joint Report to the Congress Concerning Reform to the Truth in Lending Act and the Real Estate Settlement Procedures Act* (1998), *available at http://www.federalreserve.gov/boarddocs/rptcongress/tila.pdf.*

[4] As noted, Congress subsequently amended the MDIA with the Emergency Economic Stabilization Act of 2008.

[5] To ease discussion, the description of the closed-end mortgage disclosure scheme includes MDIA's recent amendments to TILA and the disclosure timing requirements of the 2008 HOEPA Final Rule that will be effective July 30, 2009.

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 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.

Specifically, the Board worked with ICF Macro to develop and test several types of closed-end disclosures, including:

- Two Board publications to be provided at application, entitled ''*Key Questions To Ask About Your Mortgage''* and ''*Fixed* vs. *Adjustable Rate Mortgages'';*
- An ARM loan program disclosure to be provided at application;
- An early TILA disclosure to be provided within three business days of application, and again so that the consumer receives it at least three business days before consummation;
- An ARM adjustment notice to be provided after consummation; and
- A payment option monthly statement to be provided after consummation.

Exploratory focus groups. In February and March 2008 the Board worked with ICF Macro to conduct four focus groups with consumers who had obtained a mortgage in the previous two years. Two of the groups consisted of subprime borrowers and two consisted of prime borrowers, with creditworthiness determined by their answers to questions about prior financial hardship, difficulties encountered in shopping for credit, and the rate on their current mortgage. Each focus group consisted of between seven and nine people that discussed issues identified by the Board and raised by a moderator from ICF Macro. Through these focus groups, the Board gathered information on how consumers shop for mortgages, what information consumers currently use in making decisions about mortgages, and what perceptions consumers had of TILA disclosures currently provided in the shopping and application process.

Cognitive interviews on existing disclosures. In 2008, the Board worked with ICF Macro to conduct five rounds of cognitive interviews with mortgage customers (seven to eleven participants per round). These cognitive interviews consisted of one-on-one discussions with consumers, during which consumers described their recent mortgage shopping experience and reviewed existing sample mortgage disclosures. In addition to learning about shopping behavior, the goals of these interviews were: (1) To learn more about what information consumers read when they receive current mortgage disclosures; (2) to research how easily consumers can find various pieces of information in these disclosures; and (3) to test consumers' understanding of certain mortgage related words and phrases.

1. Initial design of disclosures for testing. In the fall of 2008, the Board worked with ICF Macro to develop sample mortgage disclosures to be used in later rounds of testing, taking into account information learned through the focus groups and the cognitive interviews.

2. Additional cognitive interviews and revisions to disclosures. In late 2008 and early 2009, the Board worked with ICF Macro to conduct six additional rounds of cognitive interviews (nine or ten participants per round), where consumers were asked to view new sample mortgage disclosures developed by the Board and ICF Macro. The rounds of interviews were conducted sequentially to allow for revisions to the testing materials based on what was learned from the testing during each previous round.

Results of testing. Several of the model forms 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*.

Many consumer testing participants reported that they did not shop for a lender or a mortgage. Several stated that they were referred to a lender by a realtor, family member or friend, and that they relied on that lender to get them a loan. Participants who reported shopping for a mortgage relied on originators' oral quotes for interest rates, monthly payments, and closing costs. Most participants stated that once they had applied for a particular loan and received a TILA disclosure they ceased shopping. Some cited the time involved, and the amount of documentation required, as factors for limiting their shopping. These findings suggest that consumers need information early in the process and that information should not be limited to information about ARMs. Therefore, the proposal would require creditors to provide key information about evaluating loan terms at the time an application form is provided, as discussed below.

1. Disclosures provided to consumers before application. Currently, creditors must provide the CHARM booklet before a consumer applies or pays a nonrefundable fee, whichever is earlier. The booklet explains how ARMs generally work. Testing showed that participants found the CHARM booklet too lengthy to be useful, although some liked specific elements such as the glossary. In addition, creditors must provide an ARM loan program disclosure for each ARM loan program in which the consumer expresses an interest, before the consumer applies or has paid a nonrefundable fee. The ARM loan program disclosure currently must include either a 15-year historical example of rates and payments for a $10,000 loan, or the maximum interest rate and payment for a $10,000 loan originated at the interest rate in effect for the disclosure's identified month and year. Many testing participants found the narrative form of the current ARM loan program disclosure difficult to read and understand. Some participants mistook the historical examples to be their actual loan rate and payments. Participants also found the content of the disclosure too general to be useful to them when comparing between lenders or products, and noted the absence of key loan information, such as the interest rate.

Thus, the proposal would require creditors to provide, for all closed-end mortgages, a one-page document that explains the basic differences between fixed-rate mortgages and ARMs, and a one-page document that would explain potentially risky features of a mortgage in a plain-English question and answer format. In addition, the proposal would streamline the content of the ARM loan program disclosure to highlight in a table form information that participants found most useful, such as interest rate and payment adjustments, and to provide information about program-specific loan features that could pose greater risk, such as prepayment penalties. Consumer testing suggested that highlighting such information in a table form improved participants' ability to identify and understand the information provided about key loan features.

2. Disclosures provided to consumers after application. Currently, creditors must provide an early TILA disclosure within three business days after application and at least seven business days before consummation, and before the consumer has paid a fee other than a fee for obtaining the consumer's credit history. If the APR on the early TILA disclosure exceeds a certain tolerance before consummation, the creditor must provide corrected disclosures that the consumer must receive at least three days before consummation. If any term other than the APR becomes inaccurate, the creditor must give the corrected disclosure no later than at consummation.

The early TILA disclosure—and any corrected disclosure—must provide certain information, such as the loan's annual percentage rate (APR), finance charge, amount financed, and total of payments. Participants in consumer testing indicated that much of the information in the current TILA disclosure was of secondary importance to them when considering a loan. Participants consistently looked for the contract rate of interest, monthly payment, and in some cases, closing costs. Most participants assumed that the APR was the contract rate of interest, and that the finance charge was the total of all interest they would pay if they kept the loan to maturity. Most identified the amount financed as the loan amount. When asked to compare two loan offers using redesigned model forms that contained these disclosures, few participants used the APR and finance charge to compare the loans. In addition, some participants had difficulty determining whether the loan tested had a variable or fixed rate and understanding the payment schedule's relationship to the changing interest rate. Many did not understand what circumstances would trigger a prepayment penalty.

Thus, the proposal contains a number of revisions to the format and content of TILA disclosures to make them clearer and more conspicuous. To enhance the effectiveness of the finance charge as a disclosure of the true cost of credit, the proposal would require a simpler, more inclusive approach. The disclosure of the APR would be enhanced to improve consumers' comprehension of the cost of credit. In addition, to help consumers determine whether the loan offered is affordable for them, creditors would be required to summarize key loan terms and highlight interest rate and payment information in a table. Consumer testing showed that using special formatting requirements, consistent terminology and a minimum 10-point font, would ensure that consumers are better able to identify and review key loan terms.

3. Disclosures required after consummation. Currently, creditors must provide advance notice to a consumer before the interest rate and monthly payment adjust on an ARM. The ARM adjustment notice must provide certain information, including current and prior interest rates, the index values upon which the current and prior interest rates are based, and the payment that would be required to amortize the loan fully at the new interest rate. The Board worked with ICF Macro to develop a revised ARM adjustment notice that would enhance consumers' ability to identify and understand changes being made to their loan terms. Consumer testing of the revised ARM adjustment notice indicated that consumers understood the content and were able correctly to identify the amount and due date of the new payment. Thus, under the proposal, creditors would be required to provide the ARM adjustment notice in a revised format that would highlight changes being made to the interest rate and the monthly payment, and provide other important information, such as the due date of the new payment and the loan balance.

Currently, creditors are not required to provide disclosures after consummation for negatively-amortizing loans. The Board worked with ICF Macro to develop a monthly statement that compares the amount and the impact on the loan balance of a fully-amortizing payment, interest-only payment, and minimum payment. Consumer testing of the proposed monthly statement indicated that consumers understood the content, easily recognized the payment options highlighted in the table, and understood that by making only the minimum payment they would be borrowing more money and increasing their loan balance. Thus, to improve consumer understanding of the risks associated with payment option loans, the Board proposes to require, not later than 15 days before a periodic payment is due, a monthly statement of payment options that explains the impact of payment choice on the loan balance.

Additional testing during and after the comment period. During the comment period, the Board will work with ICF Macro to conduct additional testing of model disclosures. After receiving comments from the public on the proposal and the proposed disclosure forms, the Board will work with ICF Macro to further revise model disclosures based on comments received, and to conduct additional rounds of cognitive interviews to test the revised disclosures. After the cognitive interviews, quantitative testing will be conducted. The goal of the quantitative testing is to measure consumers' comprehension of the newly-developed disclosures with a larger and more statistically representative group of consumers.

E. Other Outreach and Research

The Board also solicited input from members of the Board's Consumer Advisory Council on various issues presented by the review of Regulation Z. During 2009, for example, the Council discussed ways to improve disclosures for home-secured credit. In addition, Board staff met or conducted conference calls with various industry and consumer group representatives throughout the review process leading to this proposal. Board staff also reviewed disclosures currently provided by creditors, the Federal Trade Commission's (FTC) report on consumer testing of mortgage disclosures,[6] HUD's report on consumer testing of the GFE,[7] and other information.

F. Reviewing Regulation Z in Stages

The Board is proceeding with a review of Regulation Z in stages. This proposal largely contains revisions to rules affecting closed-end credit transactions secured by real property or a dwelling. Published elsewhere in today's **Federal Register** is the Board's proposal regarding disclosures for open-end credit secured by a consumer's dwelling. Closed-end mortgages are distinct from other TILA-covered products, and conducting a review in stages allows for a manageable process. To minimize compliance burden for creditors offering other closed-end credit, as well as home-secured credit, the proposed rules that would apply only to closed-end home-secured credit are organized in sections separate from the general disclosure requirements for closed-end rules. Although this reorganization would increase the size of the regulation and commentary, the Board believes a clear delineation of rules for closed-end, home-secured loans pending the review of the remaining closed-end rules provides a clear compliance benefit to creditors.

[6] James M. Lacko and Janis K. Pappalardo, Fed. Trade Comm'n, *Improving Consumer Mortgage Disclosures: An Empirical Assessment of Current and Protoype Disclosure Forms* (2007), (''*Improving Consumer Mortgage Disclosures*'') *available at http://www2.ftc.gov/os/2007/06/P025505MortgageDisclosureReport.pdf.*

[7] U.S. Dep't. of Hous. and Urban Dev., *Summary Report: Consumer Testing of the Good Faith Estimate Form (GFE)* (2008), *available at http://www.huduser.org/publications/pdf/Summary_Report_GFE.pdf.*

G. Implementation Period

The Board contemplates providing creditors sufficient time to implement any revisions that may be adopted. The Board seeks comment on an appropriate implementation period.

IV. The Board's Rulemaking Authority

TILA Section 105. TILA mandates that the Board prescribe regulations to carry out the purposes of the act. TILA also 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 the act, or prevent circumvention or evasion. 15 U.S.C. 1604(a).
- Exempt from all or part of TILA any class of transactions if the Board determines that TILA coverage does not provide a meaningful benefit to consumers in the form of useful information or protection. The Board must consider factors identified in the act and publish its rationale at the time it proposes an exemption for comment. 15 U.S.C. 1604(f).

In the course of developing the proposal, the Board has considered the views of interested parties, its experience in implementing and enforcing Regulation Z, and the results obtained from testing various disclosure options in controlled consumer tests. For the reasons discussed in this notice, the Board believes this proposal is appropriate pursuant to the authority under TILA Section 105(a).

Also, as explained in this notice, the Board believes that the specific exemptions proposed are appropriate because the existing requirements do not provide a meaningful benefit to consumers in the form of useful information or protection. In reaching this conclusion with each proposed exemption, the Board considered (1) the amount of the loan and whether the disclosure provides a benefit to consumers who are parties to the transaction involving a loan of such amount; (2) the extent to which the requirement complicates, hinders, or makes more expensive the credit process; (3) the status of the borrower, including any related financial arrangements of the borrower, the financial sophistication of the borrower relative to the type of transaction, and the importance to the borrower of the credit, related supporting property, and coverage under TILA; (4) whether the loan is secured by the principal residence of the borrower; and (5) whether the exemption would undermine the goal of consumer protection. The rationales for these proposed exemptions are explained in part VI below.

TILA Section 129(l)(2). TILA also authorizes the Board to prohibit acts or practices in connection with:

- Mortgage loans that the board finds to be unfair, deceptive, or designed to evade the provisions of HOEPA; and
- Refinancing of mortgage loans that the Board finds to be associated with abusive lending practices or that are otherwise not in the interest of the borrower.

The authority granted to the Board under TILA Section 129(l)(2), 15 U.S.C. 1639(l)(2), is broad. It reaches mortgage loans with rates and fees that do not meet HOEPA's rate or fee trigger in TILA Section 103(aa), 15 U.S.C. 1602(aa), as well as mortgage loans not covered under that section, such as home purchase loans. Moreover, while HOEPA's statutory restrictions apply only to creditors and only to loan terms or lending practices, Section 129(l)(2) is not limited to acts or practices by creditors, nor is it limited to loan terms or lending practices. *See* 15 U.S.C. 1639(l)(2). It authorizes protections against unfair or deceptive practices ''in connection with mortgage loans,'' and it authorizes protections against abusive practices ''in connection with refinancing of mortgage loans.'' Thus, the Board's authority is not limited to regulating specific contractual terms of mortgage loan agreements; it extends to regulating loan-related practices generally, within the standards set forth in the statute.

HOEPA does not set forth a standard for what is unfair or deceptive, but the Conference Report for HOEPA indicates that, in determining whether a practice in connection with mortgage loans is unfair or deceptive, the Board should look to the standards employed for interpreting State unfair and deceptive trade practices statutes and the Federal Trade Commission Act (FTC Act), Section 5(a), 15 U.S.C. 45(a).[8]

Congress has codified standards developed by the Federal Trade Commission (FTC) for determining whether acts or practices are unfair under Section 5(a), 15 U.S.C. 45(a).[9] Under the FTC Act, an act or practice is unfair when it causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition. In addition, in determining whether an act or practice is unfair, the FTC is permitted to consider established public policies, but public policy considerations may not serve as the primary basis for an unfairness determination.[10]

The FTC has interpreted these standards to mean that consumer injury is the central focus of any inquiry regarding unfairness.[11] Consumer injury may be substantial if it imposes a small harm on a large number of consumers, or if it raises a significant risk of concrete harm.[12] The FTC looks to whether an act or practice is injurious in its net effects.[13] The FTC has also observed that an unfair act or practice will almost always reflect a market failure or market imperfection that prevents the forces of supply and demand from maximizing benefits and minimizing costs.[14] In evaluating unfairness, the FTC looks to whether consumers' free market decisions are unjustifiably hindered.[15]

The FTC has also adopted standards for determining whether an act or practice is deceptive (though these standards, unlike unfairness standards, have not been incorporated into the FTC Act).[16] First, there must be a representation, omission or practice that is likely to mislead the consumer. Second, the act or practice is examined from the perspective of a consumer acting reasonably in the circumstances. Third, the representation, omission, or practice must be material. That is, it must be likely to affect the consumer's conduct or decision with regard to a product or service.[17]

Many States also have adopted statutes prohibiting unfair or deceptive acts or practices, and these statutes employ a variety of standards, many of them different from the standards

[8] H.R. Rep. 103–652, at 162 (1994) (Conf. Rep.).

[9] *See* 15 U.S.C. 45(n); Letter from Commissioners of the FTC to the Hon. Wendell H. Ford, Chairman, and the Hon. John C. Danforth, Ranking Minority Member, Consumer Subcomm. of the H. Comm. on Commerce, Science, and Transp. (Dec. 17, 1980).

[10] 15 U.S.C. 45(n).

[11] Statement of Basis and Purpose and Regulatory Analysis, Credit Practices Rule, 42 FR 7740, 7743; Mar. 1, 1984 (*Credit Practices Rule*).

[12] Letter from Commissioners of the FTC to the Hon. Wendell H. Ford, Chairman, and the Hon. John C. Danforth, Ranking Minority Member, Consumer Subcomm. of the H. Comm. on Commerce, Science, and Transp., n.12 (Dec. 17, 1980).

[13] *Credit Practices Rule*, 42 FR at 7744.

[14] *Id.*

[15] *Id.*

[16] Letter from James C. Miller III, Chairman, FTC to the Hon. John D. Dingell, Chairman, H. Comm. on Energy and Commerce (Oct. 14, 1983) (*Dingell Letter*).

[17] *Dingell Letter* at 1–2.

currently applied to the FTC Act. A number of States follow an unfairness standard formerly used by the FTC. Under this standard, an act or practice is unfair where it offends public policy; or is immoral, unethical, oppressive, or unscrupulous; and causes substantial injury to consumers.[18]

In developing proposed rules under TILA Section 129(l)(2)(A), 15 U.S.C. 1639(l)(2)(A), the Board has considered the standards currently applied to the FTC Act's prohibition against unfair or deceptive acts or practices, as well as the standards applied to similar State statutes.

V. Discussion of Major Proposed Revisions

The goal of the proposed revisions is to improve the effectiveness of the Regulation Z disclosures that must be provided to consumers for closed-end credit transactions secured by real property or a dwelling. To shop for and understand the cost of home-secured credit, consumers must be able to identify and comprehend the key terms of mortgages. But the terms and conditions for mortgage transactions can be very complex. The proposed revisions to Regulation Z are intended to provide the most essential information to consumers when the information would be most useful to them, with content and formats that are clear and conspicuous. The proposed revisions are expected to improve consumers' ability to make informed credit decisions and enhance competition among creditors. Many of the changes are based on the consumer testing that was conducted in connection with the review of Regulation Z.

In considering the proposed revisions, the Board sought to ensure that the proposal would not reduce access to credit, and sought to balance the potential benefits for consumers with the compliance burdens imposed on creditors. For example, the proposed revisions seek to provide greater certainty to creditors in identifying what costs must be disclosed for mortgages, and how those costs must be disclosed. More effective disclosures may also reduce confusion and misunderstanding, which may also ease creditors' costs relating to consumer complaints and inquiries.

A. Disclosures at Application

Currently, Regulation Z requires pre-application disclosures only for variable-rate transactions. For these transactions, creditors are required to provide the CHARM booklet and a loan program disclosure that provides twelve items of information at the time an application form is provided or before the consumer pays a nonrefundable fee, whichever is earlier.

''Key Questions to Ask about Your Mortgage'' publication. Since 1987, the number of loan products and product features has grown, providing consumers with more choices. However, the growth in loan features and products has also made the decision-making process more complex for consumers. The proposal would require creditors to provide to consumers a one-page Board publication entitled, ''*Key Questions to Ask about Your Mortgage.''* Creditors would be required to provide this document for all closed-end loans secured by real property or a dwelling, not just variable-rate loans, before the consumer applies for a loan or pays a nonrefundable fee, whichever is earlier. The publication would inform consumers in a plain-English question and answer format about potentially risky features, such as interest-only, negative amortization, and prepayment penalties. To enable consumers to track the presence or absence of potentially risky features throughout the mortgage transaction process, the key questions and answers provided in this one-page document would also be included in the ARM loan program disclosure and the early and final TILA disclosures.

''Fixed vs. *Adjustable Rate Mortgages'' publication.* Instead of the CHARM booklet, the proposal would require creditors to provide a one-page Board publication entitled, ''*Fixed* vs. *Adjustable Rate Mortgages''* for all closed-end loans secured by real property or a dwelling, not just variable-rate loans. The publication would contain an explanation of the basic differences between fixed-rate mortgages and ARMs. Although the requirement to provide a CHARM booklet would be eliminated, the Board would continue to publish the CHARM booklet as a consumer-education publication.

ARM loan program disclosure. Currently, for each variable-rate loan program in which a consumer expresses an interest, creditors must provide certain information, including the index and margin to be used to calculate interest rates and payments, and either a 15-year historical example of rates and payments for a $10,000 loan, or the maximum interest rate and payment for a $10,000 loan originated at the interest rate in effect for the disclosure's identified month and year. Based on consumer testing, the proposal would simplify the ARM loan program disclosure to focus on the interest rate and payment and the potential risks associated with ARMs. Information on how to calculate payments, and the effect of rising interest rates on monthly payments would be moved to the early TILA disclosure provided after application. Placing the information there will allow the creditor to customize the information to the consumer's potential loan, making the information more useful to consumers. The proposed ARM loan program disclosure would be provided in a tabular question and answer format to enable consumers to easily locate the most important information.

B. Disclosures Within Three Days After Application

TILA and Regulation Z currently require creditors to provide an early TILA disclosure within three business days after application and at least seven business days before consummation, and before the consumer has paid a fee other than a fee for obtaining the consumer's credit history. If the APR on the early TILA disclosure exceeds a certain tolerance before consummation, the creditor must provide corrected disclosures that the consumer must receive at least three days before consummation. If any term other than the APR becomes inaccurate, the creditor must give the corrected disclosure no later than at consummation.

The early TILA disclosure, and any corrected disclosure, must include certain loan information, including the amount financed, the finance charge, the APR, the total of payments, and the amount and timing of payments. The finance charge is the sum of all credit-related charges, but excludes a variety of fees and charges. TILA requires that the finance charge and the APR be disclosed more conspicuously than other information. The APR is calculated based on the finance charge and is meant to be a single, unified number to help consumers understand the total cost of credit.

Calculation of the finance charge. The proposal contains a number of revisions to the calculation of the finance charge and the disclosure of the finance charge and the APR to improve consumers'

[18] *See, e.g., Kenai Chrysler Ctr., Inc.* v. *Denison*, 167 P.3d 1240, 1255 (Alaska 2007) (quoting *FTC* v. *Sperry & Hutchinson Co.*, 405 U.S. 233, 244–45 n.5 (1972)); *State* v. *Moran*, 151 N.H. 450, 452, 861 A.2d 763, 755–56 (N.H. 2004) (concurrently applying the FTC's former test and a test under which an act or practice is unfair or deceptive if ''the objectionable conduct * * * attain[s] a level of rascality that would raise an eyebrow of someone inured to the rough and tumble of the world of commerce.'') (citation omitted); *Robinson* v. *Toyota Motor Credit Corp.*, 201 Ill. 2d 403, 417–418, 775 N.E.2d 951, 961–62 (2002) (quoting 405 U.S. at 244–45 n.5).

understanding of the cost of credit. Currently, TILA and Regulation Z permit creditors to exclude several fees or charges from the finance charge, including certain fees or charges imposed by third party closing agents; certain premiums for credit or property insurance or fees for debt cancellation or debt suspension coverage, if the creditor meets certain conditions; security interest charges; and real-estate related fees, such as title examination or document preparation fees.

Consumer groups, creditors, and government agencies have long been dissatisfied with the ''some fees in, some fees out'' approach to the finance charge. Consumer groups and others believe that the current approach obscures the true cost of credit. They contend that this approach creates incentives for creditors to shift the cost of credit from the interest rate to ancillary fees excluded from the finance charge. They further contend that this approach undermines the purpose of the APR, which is to express in a single figure the total cost of credit. Creditors maintain that consumers are confused by the APR and that the current approach creates significant regulatory burdens. They contend that determining which fees are or are not included in the finance charge is overly complex and creates litigation risk.

The Board proposes to use its exception and exemption authority to revise the finance charge calculation for closed-end mortgages, including HOEPA loans. The proposal would maintain TILA's definition of a ''finance charge'' as a fee or charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to the extension of credit. However, the proposal would require the finance charge to include charges by third parties if the creditor requires the use of a third party as a condition of or incident to the extension of credit (even if the consumer chooses the third party), or if the creditor retains a portion of the third-party charge (to the extent of the portion retained). Charges that would be incurred in a comparable cash transaction, such as transfer taxes, would continue to be excluded from the finance charge. Under this approach, consumers would benefit from having a finance charge and APR disclosure that better represent the cost of credit, undiluted by myriad exclusions for various fees and charges. This approach would cause more loans to be subject to the special protections of the Board's 2008 HOEPA Final Rule, special disclosures and restrictions for HOEPA loans, and certain State anti-predatory lending laws. However, the proposal could also reduce compliance burdens, regulatory uncertainty, and litigation risks for creditors.

Disclosure of the finance charge and the APR. Currently, creditors are required to disclose the loan's ''finance charge'' and ''annual percentage rate,'' using those terms, more conspicuously than the other required disclosures. Consumer testing indicated that consumers do not understand the term ''finance charge.'' Most consumers believe the term refers to the total of all interest they would pay if they keep the loan to maturity, but do not realize that it includes the fees and costs associated with the loan. For these reasons, the proposal replaces the term ''finance charge'' with ''interest and settlement charges'' to make clear it is more than interest, and the disclosure would no longer be more conspicuous than the other required disclosures.

In addition, the disclosure of the APR would be enhanced to improve consumers' comprehension of the cost of credit. Under the proposal, creditors would be required to disclose the APR in 16-point font in close proximity to a graph that compares the consumer's APR to the HOEPA average prime offer rate for borrowers with excellent credit and the HOEPA threshold for higher-priced loans. This disclosure would put the APR in context and help consumers understand whether they are being offered a loan that comports with their creditworthiness.

Interest rate and payment summary. Currently, creditors are required to disclose the number, amount, and timing of payments scheduled to repay the loan. Under the MDIA's amendments to TILA, creditors will be required to provide examples of adjustments to the regularly required payment based on the change in interest rates specified in the contract. Consumer testing consistently indicated that consumers shop for and evaluate a mortgage based on the contract interest rate and the monthly payment, but consumers have difficulty understanding such terms using the current TILA disclosure. Under the proposal, creditors would be required to disclose in a tabular format the contract interest rate together with the corresponding monthly payment, including escrows for taxes and property and/or mortgage insurance. Special disclosure requirements would be imposed for adjustable-rate or step-rate loans to show the interest rate and payment at consummation, the maximum interest rate and payment at first adjustment, and the highest possible maximum interest rate and payment. Additional special disclosures would be required for loans with negatively-amortizing payment options, introductory interest rates, interest-only payments, and balloon payments.

Disclosure of other terms. In addition to the interest rate and monthly payment, consumer testing indicated that consumers benefit from the disclosure of other key terms in a clear format. Thus, the proposal would require creditors to provide in a tabular format information about the loan amount, the loan term, the loan type (such as fixed-rate), the total settlement charges, and the maximum amount of any prepayment penalty. In addition, creditors would be required to disclose in a tabular question and answer format the ''Key Questions about Risk,'' which would include information about potentially risky loan features such as prepayment penalties, interest-only payments, and negative amortization.

C. Disclosures Three Days Before Consummation

As noted above, the creditor is required to provide the early TILA disclosure to the consumer within three business days after receiving the consumer's written application and at least seven business days before consummation, and before the consumer has paid a fee other than a fee for obtaining the consumer's credit history. If the APR on the early TILA disclosure exceeds a certain tolerance before consummation, the creditor must provide corrected disclosures that the consumer must receive at least three days before consummation. If any term other than the APR becomes inaccurate, the creditor must give the corrected disclosure no later than at consummation. The consumer may waive the seven- and three-day waiting periods for a bona fide personal financial emergency.

There are, however, long-standing concerns about consumers facing different loan terms or increased settlement costs at closing. Members of the Board's Consumer Advisory Council, participants in public hearings, and commenters on prior Board rulemakings have expressed concern about consumers not learning of changes to credit terms or settlement charges until consummation. In addition, consumer testing indicated that consumers are often surprised at closing by changes in important loan terms, such as the addition of an adjustable-rate feature. Despite these changes, consumers report that they have proceeded with closing because they lacked alternatives (especially in the case of a home purchase loan), or were told that they could easily refinance with better terms in the near future.

For these reasons, the proposal would require the creditor to provide a final TILA disclosure that the consumer must receive at least three business days before consummation, even if no terms have changed since the early TILA disclosure was provided. In addition, the Board is proposing two alternative approaches to address changes to loan terms and settlement charges during the three-business-day waiting period. Under the first approach, if any terms change during the three-business-day waiting period, the creditor would be required to provide another final TILA disclosure and wait an additional three business days before consummation could occur. Under the second approach, creditors would be required to provide another final TILA disclosure, but would have to wait an additional three business days before consummation only if the APR exceeds a designated tolerance or the creditor adds an adjustable-rate feature. Otherwise, the creditor would be permitted to provide the new final TILA disclosure at consummation.

D. Disclosures After Consummation

Regulation Z requires certain notices to be provided after consummation. Currently, for variable-rate transactions, creditors are required to provide advance notice of an interest rate adjustment. There are no disclosure requirements for other post-consummation events.

ARM adjustment notice. Currently, for variable-rate transactions, creditors are required to provide a notice of interest rate adjustment at least 25, but no more than 120, calendar days before a payment at a new level is due. In addition, creditors must provide an adjustment notice at least once each year during which an interest rate adjustment is implemented without an accompanying payment change. These disclosures must include certain information, including the current and prior interest rates and the index values upon which the current and prior interest rates are based.

Under the proposal, creditors would be required to provide the ARM adjustment notice at least 60 days before payment at a new level is due. This proposal seeks to address concerns that consumers need more than 25 days to seek out a refinancing in the event of a payment adjustment. This notice is particularly critical for subprime borrowers who may be more vulnerable to payment shock and may have a more difficult time refinancing a loan.

Payment option statement. Currently, creditors are not required to provide disclosures after consummation for negatively amortizing loans, such as payment option loans. To ensure consumers receive information about the risks associated with payment option loans (*e.g.*, payment shock), the proposal would require creditors to provide a periodic statement for payment option loans that have negative amortization. The disclosure would contain a table with a comparison of the amount and impact on the loan balance and property equity of a fully-amortizing payment, interest-only payment, and minimum negatively-amortizing payment. This disclosure would be provided not later than 15 days before a periodic payment is due.

Creditor-placed property insurance notice. Creditors are not currently required under Regulation Z to provide notice before charging for creditor-placed property insurance. Industry reports indicate that the volume of creditor-placed property insurance has increased significantly. Consumers struggling financially may fail to pay required property insurance premiums unaware that creditors have the right to obtain such insurance on their behalf and add the premiums to their outstanding loan balance. Such premiums are often considerably more expensive than premiums for insurance obtained by the consumer. Thus, under the proposal, creditors would be required to provide notice to consumers of the cost and coverage of creditor-placed property insurance at least 45 days before a charge is imposed for such insurance. In addition, creditors would be required to provide consumers with evidence of such insurance within 15 days of imposing a charge for the insurance.

E. Prohibitions on Payments to Loan Originators and Steering

Currently, creditors pay commissions to loan originators in the form of ''yield spread premiums.'' A yield spread premium is the present dollar value of the difference between the lowest interest rate a lender would have accepted on a particular transaction and the interest rate a loan originator actually obtained for the lender. Some or all of this dollar value is usually paid to the loan originator by the creditor as a form of compensation, though it may also be applied to other closing costs.

Yield spread premiums can create financial incentives to steer consumers to riskier loans for which loan originators will receive greater compensation. Consumers generally are not aware of loan originators' conflict of interest and cannot reasonably protect themselves against it. Yield spread premiums may provide some benefit to consumers because consumers do not have to pay loan originators' compensation in cash or through financing. However, the Board believes that this benefit may be outweighed by costs to consumers, such as when consumers pay a higher interest rate or obtain a loan with terms the consumer may not otherwise have chosen, such as a prepayment penalty or an adjustable rate.

In response to these concerns, the 2007 HOEPA Proposed Rule attempted to address the potential unfairness through disclosure. The proposal would have prohibited a creditor from paying a mortgage broker more than the consumer had previously agreed in writing that the mortgage broker would receive. A mortgage broker would have had to enter into the written agreement with the consumer, before accepting the consumer's loan application and before the consumer paid any fee in connection with the transaction (other than a fee for obtaining a credit report). The agreement also would have disclosed (1) that the consumer ultimately would bear the cost of the entire compensation even if the creditor paid part of it directly; and (2) that a creditor's payment to a broker could influence the broker to offer the consumer loan terms or products that would not be in the consumer's interest or the most favorable the consumer could obtain.

Based on analysis of comments received on the 2007 HOEPA Proposed Rule, the results of consumer testing, and other information, the Board withdrew the proposed provisions relating to broker compensation in the 2008 HOEPA Final Rule. In particular, the Board's consumer testing raised concerns that the proposed agreement and disclosures would confuse consumers and undermine their decisionmaking rather than improve it. Participants often concluded, not necessarily correctly, that brokers are more expensive than creditors. Many also believed that brokers would serve their best interests notwithstanding the conflict resulting from the relationship between interest rates and brokers' compensation.[19] The proposed disclosures presented a significant risk of misleading consumers regarding both the relative costs of brokers and lenders and the role of brokers in their

[19] *See* Macro International, Inc., *Consumer Testing of Mortgage Broker Disclosures* (July 10, 2008), *available at http://www.federalreserve.gov/newsevents/press/bcreg/20080714regzconstest.pdf.*

transactions. In withdrawing the broker compensation provisions of the HOEPA proposal, the Board stated it would continue to explore options to address potential unfairness associated with loan originator compensation arrangements.

To address the concerns related to loan originator compensation, the Board proposes to prohibit payments to loan originators that are based on the loan's terms and conditions. This prohibition would not apply to payments that consumers make directly to loan originators. The Board solicits comment on an alternative that would allow loan originators to receive payments that are based on the principal loan amount, which is a common practice today. If a consumer directly pays the loan originator, the proposal would prohibit the loan originator from also receiving compensation from any other party in connection with that transaction. These rules would be proposed under the Board's HOEPA authority to prohibit unfair or deceptive acts or practices in connection with mortgage loans.

Under the proposal, a ''loan originator'' would include both mortgage brokers and employees of creditors who perform loan origination functions. The 2007 HOEPA Proposed Rule covered only mortgage brokers. However, a creditor's loan officers frequently have the same discretion as mortgage brokers to modify loans' terms to increase their compensation, and there is evidence that creditors' loan officers engage in such practices.

The Board also seeks comment on an optional proposal that would prohibit loan originators from directing or ''steering'' consumers to a particular creditor's loan products based on the fact that the loan originator will receive additional compensation even when that loan may not be in the consumer's best interest. The Board solicits comment on whether the proposed rule would be effective in achieving the stated purpose. In addition, the Board solicits comment on the feasibility and practicality of such a rule, its enforceability, and any unintended adverse effects the rule might have.

F. Additional Protections

Credit insurance or debt cancellation or debt suspension coverage eligibility for all loan transactions. Currently, creditors may exclude from the finance charge a premium or charge for credit insurance or debt cancellation or debt suspension coverage if the creditor discloses the voluntary nature and cost of the product, and the consumer signs or initials an affirmative request for the product. Concerns have been raised about creditors who sometimes offer products that contain eligibility restrictions, specifically age or employment restrictions, but do not evaluate whether applicants for the products actually meet the eligibility restrictions at the time of enrollment. Subsequently, consumers' claims for benefits may be denied because they did not meet the eligibility restrictions at the time of enrollment. Consumers are presumably unaware that they are paying for a product for which they will derive no benefit. Under the proposal, creditors would be required to determine whether the consumer meets the age and/or employment eligibility criteria at the time of enrollment in the product and provide a disclosure that such a determination has been made. The proposal is not limited to mortgage transactions and would apply to all closed-end and open-end transactions.

VI. Section-by-Section Analysis

Section 226.1 Authority, Purpose, Coverage, Organization, Enforcement, and Liability

1(b) Purpose

Section 226.1(b) would be revised to reflect the fact that § 226.35 prohibits certain acts or practices for transactions secured by the consumer's principal dwelling. In addition, § 226.1(b) would be revised to reflect the proposal to broaden the scope of § 226.36 (from transactions secured by the consumer's principal dwelling to all transactions secured by real property or a dwelling).

1(d) Organization

1(d)(5)

The Board proposes to revise § 226.1(d)(5) to reflect the scope of §§ 226.32, 226.34, and 226.35. The Board would also revise § 226.1(d)(5) to reflect the proposed change in the scope of § 226.36, and the addition of new §§ 226.37 and 226.38.

Section 226.2 Definitions and Rules

2(a) Definitions

2(a)(24) Residential Mortgage Transaction

Regulation Z, § 226.2(a)(24), defines a ''residential mortgage transaction'' as ''a transaction in which a mortgage, deed of trust, purchase money security interest arising under an installment sales contract, or equivalent consensual security interest is created or retained in the consumer's principal dwelling to finance the acquisition or initial construction of that dwelling.'' Currently, comment 2(a)(24)–1 states that the term is important in five provisions in Regulation Z, including assumption under §§ 226.18(q) and 226.20(b). However, the proposed rule would expand coverage of the assumption rules to cover any closed-end credit transaction secured by real property or a dwelling. Thus, the Board proposes to revise comments 2(a)(24)–1, –2, and –5 to reflect this change.

Section 226.3 Exempt Transactions

3(b) Credit Over $25,000 Not Secured by Real Property or a Dwelling

TILA and Regulation Z cover all credit transactions that are secured by real property or a principal dwelling in which the amount financed exceeds $25,000. 15 U.S.C. 1603(3). Section 226.3(b), which implements TILA Section 104(3), provides that credit transactions over $25,000 *not* secured by real property, or by personal property used or expected to be used as the principal dwelling of the consumer, are exempt from Regulation Z. 15 U.S.C. 1603(3).

As noted in the discussion under §§ 226.19 and 226.38, the Board proposes to require creditors to provide certain disclosures for all closed-end transactions secured by real property or a dwelling, not just principal dwellings. However, the Board recognizes that, if personal property that is a dwelling but not the borrower's principal dwelling secures a loan of over $25,000, it is not covered by TILA in the first instance. For example, Regulation Z does not apply to a $26,000 loan that is secured by a manufactured home that is not the consumer's second or vacation home. Notwithstanding this exemption, the Board solicits comment on whether consumers in these transactions receive adequate information regarding their loan terms and are afforded sufficient protections. The Board also seeks comment on the relative benefits and costs of applying Regulation Z to these transactions.

Section 226.4 Finance Charge

Background

Section 106(a) of TILA provides that the finance charge in a consumer credit transaction is ''the sum of all charges, payable directly or indirectly by the person to whom the credit is extended, and imposed directly or indirectly by the creditor as an incident to the extension of credit.'' 15 U.S.C. 1605(a). The finance charge does not include charges of a type payable in a comparable cash transaction. *Id.* The finance charge does not include fees or charges imposed by third party closing agents, such as settlement agents, attorneys, and title companies, if the creditor does not require the imposition of those charges or the services provided, and the creditor does not retain the charges. *Id.* Examples of finance charges include, among other things, interest, points, service or carrying charges, credit report fees, and credit insurance premiums. *Id.*

The finance charge is significant for two reasons. First, it is meant to represent, in dollar terms, the ''cost of credit'' in whatever form imposed by the creditor or paid by the borrower. Second, the finance charge is used in calculating the annual percentage rate (APR) for the loan, 15 U.S.C. 1606, which represents the ''cost of credit, expressed as a yearly rate.'' § 226.22(a)(1). Together, these two interrelated terms are among the most important terms disclosed to consumers under TILA.

While the test for determining what is included in a finance charge is very broad, TILA Section 106 excludes from the definition of the finance charge various fees or charges. The statute excludes from the finance charge: Premiums for credit insurance if coverage is not required to obtain credit, certain disclosures are provided to the consumer, and the consumer affirmatively requests the insurance in writing; and premiums for property and liability insurance written in connection with a consumer credit transaction if the insurance may be obtained from a person of the consumer's choice and certain disclosures are provided to the consumer. 15 U.S.C. 1605(b) and (c). Statutory exclusions also apply to certain security interest charges, including: (1) Fees or charges required by law and paid to public officials for determining the existence of, or for perfecting, releasing, or satisfying, any security related to the credit transaction; (2) premiums for insurance purchased instead of perfecting any security interest otherwise required by the creditor; and (3) taxes levied on security instruments or the documents evidencing indebtedness if payment of those taxes is required to record the instrument securing the evidence of indebtedness. 15 U.S.C. 1605(d). Finally, the statute excludes from the finance charge various fees in connection with loans secured by real property, such as title examination fees, title insurance premiums, fees for preparation of loan-related documents, escrows for future payment of taxes and insurance, notary fees, appraisal fees, pest and flood-hazard inspection fees, and credit report fees. 15 U.S.C. 1605(e).

Through the exclusions described above, the Congress has adopted a ''some fees in, some fees out'' approach to the finance charge with some fees automatically excluded from the finance charge and other fees excluded from the finance charge provided certain conditions are met. The regulation tracks this approach with a three-tiered approach to the classification of fees or charges: (1) Some fees or charges are finance charges; (2) some fees and charges are not finance charges; and (3) some fees and charges are not finance charges, but only if certain conditions are met. As a result, neither the finance charge nor the corresponding APR disclosed to the consumer reflect the consumer's total cost of credit.

Section 226.4(a) defines the finance charge as ''the cost of consumer credit as a dollar amount.'' Consistent with TILA Section 106(a), the finance charge includes ''any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit'' and does not include ''any charge of a type payable in a comparable cash transaction.'' § 226.4(a). The finance charge also includes fees and amounts charged by someone other than the creditor if the creditor requires the use of a third party as a condition of or incident to the extension of credit, even if the consumer can choose the third party, or if the creditor retains a portion of the third party charge (to the extent of the portion retained). § 226.4(a)(1).

The Board has adopted provisions in the regulation to give effect to each of the statutory exclusions and conditional exclusions from the finance charge. Closing agent charges are not included in the finance charge unless the creditor requires the particular services for which the consumer is charged, requires imposition of the charge, or retains a portion of the charge (to the extent of the portion retained). § 226.4(a)(2). Premiums for credit insurance may be excluded from the finance charge if insurance coverage is not required by the creditor, certain disclosures are provided to the consumer, and the consumer affirmatively requests the insurance coverage in a writing signed or initialed by the consumer. § 226.4(d)(1). Premiums for property and liability insurance may also be excluded from the finance charge if the insurance may be obtained from a person of the consumer's choice and certain disclosures are provided to the consumer. § 226.4(d)(2). Certain security interest charges enumerated in the statute, such as taxes and fees prescribed by law and paid to public officials for determining the existence of, or for perfecting, releasing, or satisfying, a security interest, are excluded from the finance charge. § 226.4(e). The regulation also excludes from the finance charge the real estate related fees enumerated in Section 106(e) of TILA. § 226.4(c)(7).

Over time, the Board, by regulation, has contributed to the ''some fees in, some fees out'' approach to the finance charge by determining that certain other charges not specifically excluded by the statute are not finance charges. These regulatory exclusions often sought to bring logical consistency to the treatment of fees that are similar to fees the statute excludes or conditionally excludes from the finance charge. Charges excluded from the finance charge by regulation include: Charges for debt cancellation or debt suspension coverage if the coverage is not required by the creditor, certain disclosures are provided to the consumer, and the consumer affirmatively requests the coverage in a writing signed or initialed by the consumer; and fees for verifying the information in a credit report. *See* § 226.4(d)(3) and comment 4(c)(7)–1. The additional fees the Board has excluded from the finance charge generally are closely analogous or related to fees that the statute excludes or conditionally excludes from the finance charge. For example, premiums for voluntary debt cancellation coverage are closely analogous to premiums for voluntary credit insurance, which TILA excludes from the finance charge. Likewise, charges for verifying a credit report are related to the credit report itself.

Concerns With the Current Approach to Finance Charges

The ''some fees in, some fees out'' approach to the finance charge has been problematic both for consumers and for creditors since TILA's inception. Many of these problems were described in the 1998 Joint Report.[20]

One fundamental problem is that there are two views of what is meant by the ''cost of credit.'' From the creditor's perspective, the cost of credit means the interest and fee income that the creditor receives or requires in exchange for providing credit to the consumer. From the consumer's perspective, however, the cost of credit means what the consumer pays for the credit, regardless of the persons to whom such amounts are paid.[21] The statute uses both of these approaches in designating which fees are and are not included in the finance charge.

The influence of the creditor's perspective on the cost of credit is evident in how the ''some fees in, some

[20] The *1998 Joint Report* at 8–16.

[21] *See* The *1998 Joint Report* at 10.

fees out'' approach to the finance charge has evolved and been applied to loans secured by real property. Many services provided in connection with real estate loans are performed by third parties, such as appraisers, closing agents, inspectors, public officials, attorneys, and title companies. Some of these services are required by the creditor, while others are not. In either case, the fees for these services generally are remitted in whole or in part to the third party. In some cases, the creditor may have little control over the fees imposed by these third parties. From the creditor's perspective, the creditor generally does not receive and retain these charges in connection with providing credit to the consumer. From the consumer's perspective, however, these third-party charges are part of what the consumer pays to obtain credit.[22]

Another problem with the ''some fees in, some fees out'' approach is that it undermines the effectiveness of the APR as an accurate measure of the cost of credit expressed as a yearly rate. The APR is designed to be a benchmark for consumer shopping. In consumer testing conducted for the Board, however, the APR appeared not to be fulfilling that objective in connection with mortgage loans.

A single figure such as the APR is simple to use, particularly if consumers can use it to evaluate and compare competing products, rather than having to evaluate multiple figures.[23] This is especially true for a figure such as the APR, which has a forty-year history in consumer disclosures, and thus is familiar to consumers. Nevertheless, if that single figure is not understood by consumers or does not fully represent what it purports to represent, the usefulness of that figure is undermined. Consumer testing shows that most consumers do not understand the APR, and many believe that the APR is the interest rate.

Under the current ''some fees in, some fees out'' approach to the finance charge, mortgage lenders also have an incentive to unbundle the cost of credit and shift some of the costs from the interest rate into ancillary fees that are excluded from the finance charge and not considered when calculating the APR, resulting in a lower APR than otherwise would have been disclosed. This further undermines the usefulness of the APR and has resulted in the proliferation of ''junk fees,'' such as fees for preparing loan-related documents. Such unbundling of the cost of credit, and the resulting pricing complexity, can have a detrimental impact on consumers. For example, research undertaken by HUD suggests that borrowers experience great difficulty when deciding whether the tradeoff between paying higher up-front costs or paying a higher interest rate is in their best interest, and that borrowers who do not pay up-front loan origination fees generally pay less than borrowers who do pay such fees.[24] To the extent that the APR calculation includes most or all fees, the APR can reduce the incentive for lenders to include junk fees in credit agreements.[25]

Based on extensive outreach conducted by Board staff, there appears to be a broad consensus that the ''some fees in, some fees out'' approach to the finance charge and corresponding APR calculation and disclosure is seriously flawed. Many industry representatives consider the finance charge definition overly complex. For creditors, this complexity creates significant regulatory burden and litigation risk. While some industry representatives generally favor a more inclusive measure, they have not advocated a specific test for determining the finance charge.

Consumer advocates believe that the exclusions from the finance charge undermine the purpose of the finance charge and the APR, which is to measure the cost of credit. Some consumer advocates have recommended a ''but for'' test that would include in the finance charge all fees except those that the consumer would pay if he or she were not ''obtaining, accessing, or repaying the extension of credit,'' such as fees paid in comparable cash transactions.[26]

In the 1998 Joint Report, the Board and HUD recommended that the Congress adopt a more comprehensive definition of the finance charge.[27] The Board and HUD recommended adopting a ''required-cost of credit'' test that would include in the finance charge ''the costs the consumer is required to pay to get the credit.''[28] Under this approach, the finance charge would include (and the APR would reflect) costs required to be paid by the consumer to obtain the credit, including many fees currently excluded from the finance charge, such as application fees, appraisal fees, document preparation fees, fees for title services, and fees paid to public officials to record security interests.[29] Under the ''required-cost of credit'' test, fees for optional services, such as premiums for voluntary credit insurance, would be excluded from the finance charge.[30]

The Board's Proposal

A simpler, more inclusive test for determining the finance charge. The Board believes consumers would benefit from having a disclosure that includes fees or charges that better represent the full cost of credit undiluted by myriad exclusions, the basis for which consumers cannot be expected to understand. In addition, having a single benchmark figure—the APR—that is simple to use should allow consumers to evaluate competing mortgage products by reviewing one variable. The Board also believes that such a disclosure would reduce compliance burdens, regulatory uncertainty, and litigation risks for creditors who must provide accurate TILA disclosures.

Thus, the Board would retain the APR as a benchmark for closed-end transactions secured by real property or a dwelling but is proposing certain revisions designed to make the APR more useful to consumers. First, as discussed below, the Board is proposing to provide consumers with more helpful explanation of the APR and what it represents. Second, the Board is proposing to require disclosure of the APR together with a new disclosure of the interest rate, as discussed below. Third, the Board is proposing to replace the ''some fees in, some fees out'' approach for determining the finance charge with a simpler, more inclusive approach for determining the finance charge that is based on TILA Section 106(a), 15 U.S.C. 1605(a). This approach is designed to ensure that the finance charge and the corresponding APR disclosed to consumers fulfills the basic purpose of TILA by providing a more complete and useful measure of the cost of credit.

Pursuant to its authority under TILA Sections 105(a) and (f) of TILA, 15 U.S.C. 1604(a) and (f), the Board is proposing to amend § 226.4 to make most of the current exclusions from the finance charge inapplicable to closed-end credit transactions secured by real property or a dwelling. For such loans, the Board is proposing to replace the ''some fees in, some fees out'' approach with a simpler, more inclusive test based on the definition of finance

[22] *See* The *1998 Joint Report* at 11.

[23] *See* The *1998 Joint Report* at 9.

[24] U.S. Department of Housing and Urban Development, *A Study of Closing Costs for FHA Mortgages* at x–xi and 2–4 (May 2008).

[25] *See* The *1998 Joint Report* at 9.

[26] Renuart, Elizabeth and Diane E. Thomson, *The Truth, the Whole Truth, and Nothing but the Truth: Fulfilling the Promise of Truth in Lending,* 25 Yale J. on Reg. 181, 230 (2008).

[27] The *1998 Joint Report* at 15–16.

[28] The *1998 Joint Report* at 13, 16.

[29] The *1998 Joint Report* at 13.

[30] The *1998 Joint Report* at 13.

charge in TILA Section 106(a), 15 U.S.C. 1605(a), for determining what fees or charges are included in the finance charge. The Board believes that the current patchwork of fee exclusions from the definition of the finance charge is not consistent with TILA's purpose of disclosing the cost of credit to the consumer. The Board believes that a more inclusive approach to determining the finance charge would be more consistent with TILA's purpose, enhance consumer understanding and use of the finance charge and APR disclosures, and reduce compliance costs. The Board also believes that the proposed revisions to the finance charge may enhance competition for third-party services since creditors would likely be more mindful of fees or charges that must be included in the finance charge and APR.

The proposed test for determining the finance charge tracks the language of current § 226.4 but excluding § 226.4(a)(2). Specifically, under this test, a fee or charge is included in the finance charge for closed-end credit transactions secured by real property or a dwelling if it is (1) ''payable directly or indirectly by the consumer'' to whom credit is extended, and (2) ''imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit.'' The finance charge would continue to exclude fees or charges paid in comparable cash transactions. *See* § 226.4(a). The finance charge also includes charges by third parties if the creditor: (1) Requires use of a third party as a condition of or incident to the extension of credit, even if the consumer can choose the third party; or (2) retains a portion of the third-party charge, to the extent of the portion retained. *See* § 226.4(a)(1). Other exclusions from the finance charge for closed-end credit transactions secured by real property or a dwelling would be limited to late fees and similar default or delinquency charges, seller's points, and premiums for property and liability insurance.

As new services are added, and new fees are charged, in connection with closed-end credit transactions secured by real property or a dwelling, creditors would have to apply the basic test in making judgments about whether or not new fees must be included in the finance charge. The Board requests comment on whether further guidance is needed to assist creditors in making these determinations, and, if so, what specific guidance would be helpful.

Loans covered. Section 226.4 is part of Subpart A, General, as opposed to Subpart C, Closed-End Credit. Nevertheless, the proposed amendments to § 226.4 would apply only to closed-end credit transactions secured by real property or a dwelling, consistent with the general scope of this proposed rule. The Board seeks comment on whether the same amendments should be made applicable to other closed-end credit and may consider such amendments under a future review of Regulation Z. Contemporaneous with this proposal, the Board is publishing separately proposed rules regarding home equity lines of credit (HELOCs). Accordingly, the Board is not proposing to apply the changes to the finance charge determination to HELOCs in this rulemaking. As discussed in the HELOC proposal, the Board believes that changing the definition of finance charge for HELOC accounts would not have a material effect on the HELOC disclosures and accordingly is unnecessary.

Impact on coverage of other rules. One potential consequence of adopting a more inclusive test for determining the finance charge is that more loans may qualify as ''HOEPA loans,'' as described in TILA Section 103(aa), and therefore be subject to the additional disclosures and prohibitions applicable to such loans under TILA Section 129. Similarly, more loans may be subject to the Board's recently adopted protections for higher-priced mortgage loans under § 226.35, which become effective on October 1, 2009. 73 FR 44522; Jul. 30, 2008. Finally, more loans may qualify as covered loans under certain State anti-predatory lending laws that use the APR as a coverage test. The Board has conducted some analysis to quantify these impacts.

To estimate representative charges, the Board obtained information from a 2008 survey conducted by Bankrate.com on closing costs for each state, based on a $200,000 hypothetical mortgage loan.[31] Using these estimates, and scaling those that are calculated as a percentage of loan amount as necessary, the Board estimated the effect on the APRs of first-lien loans in two databases: HMDA records, which include most closed-end home loans, and data obtained from Lender Processing Services, Inc. (LPS), which include mostly prime and near-prime home loans serviced by several large mortgage servicers.

On the basis of this analysis, the Board estimates that proposed § 226.4 would increase the share of first-lien refinance and home improvement loans covered by HOEPA, under § 226.32, by about 0.6 percent. While this increase is small, the Board also notes that, because very few HOEPA loans are originated overall, the absolute number of loans covered would increase markedly—more than 350 percent. Because the HMDA data do not include APRs for loans below the rate spread reporting thresholds, *see* 12 CFR 203.4(a)(12), 2006 LPS data were used to estimate the impact on coverage of § 226.35. Based on this analysis, the Board estimates that about 3 percent of the first-lien loans in the loan amount range of the typical home purchase or refinance loan ($175,000 to $225,000) that were below the § 226.35 APR threshold would have been above the threshold if proposed § 226.4 had been in effect at the time.

The Board also examined HMDA data for the impact of the proposed, more inclusive finance charge definition on APRs in certain states. Specifically, the Board considered the APR tests for coverage of first-lien mortgages under the anti-predatory lending laws in the District of Columbia (DC), Illinois, and Maryland. These laws are the only three State anti-predatory lending laws with APR coverage thresholds that are lower than the federal HOEPA APR threshold, for first-lien loans, of 800 basis points over the U.S. Treasury yield on securities with comparable maturities. DC and Illinois use a threshold of 600 basis points, and Maryland uses a threshold of 700 basis points, over the comparable Treasury yield.[32] Freddie Mac and Fannie Mae have policies under which they will not purchase loans that exceed the Illinois thresholds,[33] but they have no such policies with regard to DC or Maryland. The Board estimates that proposed § 226.4 would convert the following percentages of first-lien loans that are under the applicable APR threshold into loans that exceed that threshold and thus would become covered by the applicable State anti-predatory lending law: DC, 2.5%; Illinois, 4.0%; Maryland, 0.0%.

[31] To supplement the Bankrate.com survey with estimated recording fees and taxes, which the survey did not include, the Board used the Martindale-Hubbell service's digest of State laws. As discussed below, the Board is not proposing to revise comment 4(a)–5, which provides principles for determining the treatment of taxes based on the party on whom the law imposes the tax. For the sake of simplicity, the Board did not attempt to distinguish such laws on this basis and, instead, included all recording taxes in the finance charge under the proposal. The analysis thus may have included some recording taxes in the finance charge under the proposal that could have been excluded under comment 4(a)–5.

[32] DC Code Ann. 26–1151.01(7)(A)(i); Ill. Comp. Stat. ch. 815, 137/10; Md. Code Ann. Com. Law 12–1029(a)(2).

[33] *http://www.freddiemac.com/learn/pdfs/uw/Pred_requirements.pdf; https://www.efanniemae.com/sf/guides/ssg/annltrs/pdf/2003/03-12.pdf.*

The Board notes that the impact of the proposed finance charge definition on APRs varies among loans based on two significant factors. First, because many of the affected charges are fixed dollar amounts, the impact is significantly greater for smaller loans. Second, the impact likely would vary geographically because some charges, notably title insurance premiums and recording fees and taxes, vary considerably by state. The Board believes the proposal, on balance, would be in consumers' interests but seeks comment on these consequences of the proposal and the impact it may have on loans that could become subject to these various laws.

Legal authority. The Board is proposing to adopt the simpler, more inclusive test for determining the finance charge and corresponding APR pursuant to its general rulemaking, exception, and exemption authorities under TILA Section 105. Section 105(a) directs the Board to prescribe regulations to carry out the purposes of this title, 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). Section 105(a) generally authorizes the Board to make adjustments and exceptions to TILA to effectuate the statute's purposes, to prevent circumvention or evasion of the statute, or to facilitate compliance with the statute. 15 U.S.C. 1601(a), 1604(a).

The Board has considered the purposes for which it may exercise its authority under TILA Section 105(a) carefully and, based on that review, believes that the proposed adjustments and exceptions are appropriate. The proposal has the potential to effectuate the statute's purpose by better informing consumers of the total cost of credit and to prevent circumvention or evasion of the statute through the unbundling or shifting of the cost of credit from finance charges to fees or charges that are currently excluded from the finance charge. The Board believes that Congress did not anticipate how such unbundling would undermine the purposes of TILA, when it enacted the exceptions. For example, fees for preparation of loan-related documents are excluded from the finance charge by TILA Section 106(e), 15 U.S.C. 1605(e); in practice, document preparation fees have become a common vehicle used by creditors to enhance their revenue without having any impact on the finance charge or APR. A simpler, more inclusive approach to determining the finance charge also would facilitate compliance with the statute.

TILA Section 105(f) generally authorizes the Board to exempt any class of transactions from coverage under any part of TILA if the Board determines that coverage under that part does not provide a meaningful benefit to consumers in the form of useful information or protection. 15 U.S.C. 1604(f)(1). The Board is proposing to exempt closed-end transactions secured by real property or a dwelling from the complex exclusions in TILA Section 106(b) through (e), 15 U.S.C. 1605(b) through (e). TILA Section 105(f) directs the Board to make the determination of whether coverage of such transactions under those exclusions provides a meaningful benefit to consumers in light of specific factors. 15 U.S.C. 1604(f)(2). These factors are (1) the amount of the loan and whether the disclosure provides a benefit to consumers who are parties to the transaction involving a loan of such amount; (2) the extent to which the requirement complicates, hinders, or makes more expensive the credit process; (3) the status of the borrower, including any related financial arrangements of the borrower, the financial sophistication of the borrower relative to the type of transaction, and the importance to the borrower of the credit, related supporting property, and coverage under TILA; (4) whether the loan is secured by the principal residence of the borrower; and (5) whether the exemption would undermine the goal of consumer protection.

The Board has considered each of these factors carefully and, based on that review, believes that the proposed exemptions are appropriate. Mortgage loans generally are the largest credit obligation that most consumers assume. Most of these loans are secured by the consumer's principal residence. For many consumers, their mortgage loan is the most important credit obligation that they have. Consumer testing suggests that consumers find the finance charge and APR disclosures confusing and unhelpful when shopping for a mortgage. Along with other changes, replacing the patchwork ''some fees in, some fees out'' approach to determining the finance charge with a more inclusive approach that reflects the consumer's total cost of credit has the potential to further the goals of consumer protection and promote the informed use of credit for mortgage loans. Adoption of a more inclusive finance charge also would simplify compliance, reduce regulatory burden, and reduce litigation risk for creditors.

The Board's exception and exemption authority under Sections 105(a) and (f) does not apply in the case of a mortgage referred to in Section 103(aa), which are high-cost mortgages generally referred to as ''HOEPA loans.'' The Board does not believe that this limitation restricts its ability to apply the revised provisions regarding finance charges to all mortgage loans, including HOEPA loans. This limitation on the Board's general exception and exemption authority is a necessary corollary to the decision of the Congress, as reflected in TILA Section 129(*l*)(1), to grant the Board more limited authority to exempt HOEPA loans from the prohibitions applicable only to HOEPA loans in Section 129(c) through (i) of TILA. *See* 15 U.S.C. 1639(*l*)(1). Here, the Board is not proposing any exemptions from the HOEPA prohibitions. This limitation does raise a question as to whether the Board could use its exception and exemption authority under Sections 105(a) and (f) to except or exempt HOEPA loans, but not other types of mortgage loans, from other, generally applicable TILA provisions. That question, however, is not implicated by this proposal.

Here, the Board is proposing to apply its general exception and exemption authority to enhance the finance charge disclosure for all loans secured by real property or a dwelling, including both HOEPA and non-HOEPA loans, in order to fulfill the statute's purpose of having the finance charge and APR disclosures reflect the total cost of credit. It would not be consistent with the statute or with Congressional intent to interpret the Board's authority under Sections 105(a) and (f) in such a way that the proposed revisions could apply only to mortgage loans that are not subject to HOEPA. Reading the statute in a way that would deprive HOEPA borrowers of improved finance charge and APR disclosures is not a reasonable construction of the statute and contravenes the Congress's goal of ensuring ''that enhanced protections are provided to consumers who are most vulnerable to abuse.'' [34]

The Board solicits comment on all aspects of this proposal, including the cost, burden, and benefits to consumers and to industry regarding the proposed revisions to the determination of the finance charge. The Board also requests comment on any alternatives to the proposal that would further the purposes of TILA and provide consumers with more useful disclosures.

4(a) Definition

Comment 4(a)–5 contains guidance for determining whether taxes should be treated as finance charges. Generally, a tax imposed on the creditor is a finance

[34] H.R. Conf. Rept. 103–652 at 159 (Aug. 2, 1994).

charge if the creditor passes it through to the consumer. If applicable law imposes a tax solely on the consumer, on the creditor and consumer jointly, on the credit transaction itself without specifying a liable party, or on the creditor with direction or authorization to pass it through to the consumer, the tax is not a finance charge. Consequently, an examination of the law imposing each tax that is paid by the consumer is required to determine whether such taxes are finance charges. This examination of laws creates burden for creditors and may result in inconsistent treatment of similar taxes. The resulting disclosures likely are not as useful to consumers as they might be if all taxes were treated consistently. The Board seeks comment on whether the rules for determining the finance charge treatment of taxes imposed by State and local governments should be simplified and, if so, how. The Board also seeks comment on whether any such simplification should be for purposes of closed-end transactions secured by real property or a dwelling only or should have more general applicability.

Proposed new comment 4(a)–6 would clarify that there is no comparable cash transaction in a transaction where there is no seller, such as a refinancing, and thus the comparable cash transaction exclusion from the finance charge does not apply to such transactions.

4(a)(2) Special Rule; Closing Agent Charges

The Board is proposing to amend § 226.4(a)(2), which set out special rules for closing agent charges, in light of the proposed new § 226.4(g), discussed below. As a result, this provision would no longer apply to closed-end credit transactions secured by real property or a dwelling because the fees excluded by § 226.4(a)(2) meet the general definition of the finance charge in TILA Section 106(a). The Board also proposes certain conforming amendments to the staff commentary under this provision.

Under the general definition of ''finance charge'' in TILA Section 106(a), a charge is a finance charge if it is (1) ''payable directly or indirectly by the person to whom the credit is extended,'' and (2) ''imposed directly or indirectly by the creditor as an incident to the extension of credit.'' 15 U.S.C. 1605(a). Application of the basic statutory definition as the test for determining which charges are finance charges would result in many third-party charges being treated as finance charges because such third-party charges often are payable directly or indirectly by the consumer and imposed indirectly by the creditor. For instance, because real estate settlements are complex financial and legal transactions, creditors generally require a licensed closing agent (often an attorney) to conduct closings to ensure that the transaction is handled with professional skill and care. These closing agents typically impose fees on the consumer in the course of ensuring that the loan is consummated appropriately. In some cases, the creditor clearly requires the particular third-party service for which a fee is charged, such as where the creditor instructs the closing agent to send documents by overnight courier. In other cases, however, whether the creditor requires the particular service is not clear.

A rule that requires case-by-case factual determinations as to whether a particular third-party fee must be included in the finance charge results in complexity and inconsistent treatment of such fees. Such inconsistent treatment in turn undermines the utility of the finance charge and APR as comparison shopping tools and introduces uncertainty and litigation risk for creditors. For these reasons, the Board believes that fees charged by closing agents, both their own and those of other third parties they hire to perform particular services, should be treated uniformly as finance charges. The Board seeks comment on whether any such third-party charges do not fall within the basic test for determining the finance charge and could be excluded from the finance charge without requiring factual determination in each case.

Requiring third-party charges to be included in the finance charge creates some risk that a creditor may understate the finance charge if the creditor does not know that a particular charge was imposed by a third party. This risk is mitigated to some extent by TILA Section 106(f), which provides that a disclosed finance charge is treated as accurate if it does not vary from the actual finance charge by more than $100 or is greater than the amount required to be disclosed. 15 U.S.C. 1605(f). This tolerance has been incorporated into Regulation Z. *See* § 226.18(d)(1). The Board requests comment on whether it should increase the finance charge tolerance, for example to $200, in light of its proposal to require more third-party charges to be included in the finance charge. The Board also requests comment on whether the existing or any increased tolerance should be linked to an inflation index, such as the Consumer Price Index.

Excluding fees from the finance charge because they are voluntary or optional also is not consistent with the statutory purpose of disclosing the ''cost of credit,'' which includes charges imposed ''as an incident to the extension of credit.'' [35] 15 U.S.C. 1605(a). One basis for the current exclusions for voluntary or optional charges is an implicit assumption that they are not ''imposed directly or indirectly by the creditor'' on the consumer. However, charges may be imposed by a creditor even if the services for which the fee is imposed are not specifically required by the creditor. Moreover, a test that depends upon whether a service is ''voluntary'' inherently requires a factual determination. In the current provisions addressing credit insurance, the Board has identified certain objective criteria for determining when the consumer's purchase of such insurance is deemed to be voluntary. However, as discussed below, this approach has many problems and has not proven satisfactory. The Board believes that drawing a bright-line to include in the finance charge both voluntary and required charges that are imposed by the creditor would eliminate the difficulties posed by this type of fact-based analysis and provide a more consistent measure of the cost of credit.

Another basis for the current exclusions for voluntary or optional charges in connection with the credit transaction is an assumption that creditors cannot know the amounts of such charges at the time the disclosure must be provided to the consumer. The Board presumes that creditors know the amounts of their own voluntary charges, if any. The Board believes that creditors generally know or can readily determine voluntary third-party charges when providing TILA disclosures three business days before consummation, as proposed § 226.19(a)(2)(ii) would require. As a practical matter, the primary voluntary third-party charge in connection with a mortgage transaction of which the Board is aware (and that is not otherwise excluded from the finance charge) is the premium for voluntary credit insurance, and creditors generally solicit consumers for such insurance. In fact, under existing § 226.4(d)(1)(ii), creditors historically

[35] The Board has consistently interpreted the definition of finance charge as not dependent on whether a charge is voluntary or required. As a practical matter, most voluntary fees are excluded because they coincidentally are payable in a comparable cash transaction, not specifically because they are voluntary. *See, e.g.,* 61 FR 49237, 49239; Sept. 19, 1996 (charges for voluntary debt cancellation agreements).

have had to disclose the premium for voluntary credit insurance to exclude it from the finance charge. The Board nevertheless solicits comment on whether there are voluntary third-party charges the amounts of which cannot be determined three business days before consummation.

The Board recognizes that creditors may not know what voluntary or optional charges the consumer will incur when providing early TILA disclosures. When providing early TILA disclosures, creditors may rely on reasonable assumptions regarding voluntary or optional charges and label those amounts as estimates. The Board invites comment on whether further guidance is required regarding reasonable assumptions that may be made regarding voluntary or optional charges in early TILA disclosures.

4(b) Examples of Finance Charges

The Board is proposing technical amendments to comment 4(b)–1 to reflect the fact that the exclusions from the finance charge under § 226.4(c) through (e), other than §§ 226.4(c)(2), 226.4(c)(5) and 226.4(d)(2), would not apply to closed-end credit transactions secured by real property or a dwelling.

4(c) Charges Excluded From the Finance Charge

The Board proposes to amend § 226.4(c), which lists miscellaneous exclusions from the finance charge, to provide that § 226.4(c) is limited by proposed new § 226.4(g). Thus, except for late fees and similar default or delinquency charges and seller's points, the exclusions in § 226.4(c) would not apply to closed-end credit transactions secured by real property or a dwelling. The Board also proposes certain conforming amendments to the staff commentary under those provisions.

4(c)(2)

The exclusion of fees for actual unanticipated late payment, exceeding a credit limit, or for delinquency, default, or a similar occurrence in § 226.4(c)(2) would be retained for closed-end credit transactions secured by real property or a dwelling. The Board believes these charges should be excluded because they necessarily occur only after the finance charge is disclosed to consumers. At the time the TILA disclosures must be provided to consumers, a creditor cannot know whether it will impose such charges or their amounts.

4(c)(5)

The exclusion of seller's points from the finance charge in § 226.4(c)(5) would be retained for closed-end credit transactions secured by real property or a dwelling. Seller's points are not payable by the consumer. Comment 226.4(c)(5)–1 notes that seller's points may be passed on to the buyer in the form of a higher sales price for the property or dwelling. Even then, seller's points are excluded from the finance charge. A different rule would require a fact-specific determination in every transaction involving seller's points regarding whether and to what extent the seller shifted those costs to the borrower. The Board does not believe that such a rule is feasible. The Board seeks comment on the retention of the seller's points exclusion.

4(c)(7) Real-Estate Related Fees

The Board is proposing to amend § 226.4(c)(7), which currently excludes from the finance charge a number of fees charged in transactions secured by real property or in residential mortgage transactions if those fees are bona fide and reasonable. Under the proposal, the following fees currently excluded would be included in the finance charge for closed-end credit transactions secured by real property or a dwelling: fees for title examination, abstract of title, title insurance, property survey, and similar purposes; fees for preparing loan-related documents, such as deeds, mortgages, and reconveyance or settlement documents; notary and credit-report fees; property appraisal fees or fees for inspections to assess the value or condition of the property if the service is performed prior to closing, including fees related to pest-infestation or flood-hazard determinations; and amounts required to be paid into escrow or trustee accounts if the amounts would not otherwise be included in the finance charge. The commentary provisions under § 226.4(c)(7) would also be amended accordingly.

As amended, § 226.4(c)(7) and the commentary provisions under § 226.4(c)(7) would apply only to open-end credit plans secured by real property and open-end residential mortgage transactions. Thus, for HELOCs, the fees specified in § 226.4(c)(7) would continue to be excluded from the finance charge. The Board requests comment on whether it should retain § 226.4(c)(7), as proposed to be amended, or delete § 226.4(c)(7) altogether, in light of the proposed changes to the Regulation Z HELOC rules, published today in a separate Federal Register notice. *See* the discussion under § 226.4 in that notice.

4(d) Insurance and Debt Cancellation and Debt Suspension Coverage

The Board is proposing technical amendments to comment 4(d)–12 to reflect the fact that the exclusions from the finance charge under § 226.4(e) would not apply to closed-end transactions secured by real property or a dwelling.

4(d)(1) and (3) Voluntary Credit Insurance Premiums; Voluntary Debt Cancellation and Debt Suspension Fees

The Board is proposing to amend §§ 226.4(d)(1), exclusion for voluntary credit insurance premiums, and 226.4(d)(3), exclusion for voluntary debt cancellation and debt suspension fees, to limit their application consistently with proposed § 226.4(g). Thus, these exclusions would not apply to closed-end transactions secured by real property or a dwelling.

Age or employment eligibility criteria. Under TILA Section 106(a)(5), 15 U.S.C. 1605(a)(5), a premium or other charge for any guarantee or insurance protecting the creditor against the obligor's default or other credit loss is a finance charge. Under §§ 226.4(b)(7) and 226.4(b)(10), a premium or charge for credit life, accident, health, or loss-of-income insurance, or debt cancellation or debt suspension coverage is a finance charge if the insurance or coverage is written in connection with a credit transaction. TILA Section 106(b), 15 U.S.C. 1605(b), allows the creditor to exclude from the finance charge any charge or premium for credit life, accident, or health insurance written in connection with any consumer credit transaction if (1) the coverage is not a factor in the approval by the creditor of the extension of credit, and this fact is clearly disclosed in writing to the consumer; and (2) in order to obtain the insurance, the consumer specifically requests the insurance after getting the disclosures. Under §§ 226.4(d)(1) and 226.4(d)(3), the creditor may exclude from the finance charge any premium for credit life, accident, health or loss-of-income insurance; any charge or premium paid for debt cancellation coverage for amounts exceeding the value of the collateral securing the obligation; or any charge or premium for debt cancellation or debt suspension coverage in the event of loss of life, health, or income or in case of accident, whether or not the coverage is insurance, if (1) the insurance or coverage is not required by the creditor and the creditor discloses this fact in writing; (2) the creditor discloses the premium or charge for the initial term of the insurance or coverage,

(3) the creditor discloses the term of insurance or coverage, if the term is less than the term of the credit transaction, and (4) the consumer signs or initials an affirmative written request for the insurance or coverage after receiving the required disclosures. In addition, under § 226.4(d)(3)(iii), the creditor must disclose for debt suspension coverage the fact that the obligation to pay loan principal and interest is only suspended, and that interest will continue to accrue during the period of suspension.[36] Under proposed § 226.4(g), these provisions would not apply to closed-end credit transactions secured by real property or a dwelling.

Some creditors offer credit insurance or debt cancellation or debt suspension products with eligibility restrictions, but may not evaluate whether applicants for the products actually meet the eligibility criteria at the time the applicants request the product.[37] For instance, a consumer who is 70 at the time of enrollment could never receive the benefits of a product with a 65-year-old age limit.[38] Similarly, a consumer who is self-employed at the time of enrollment would not receive benefits if the product requires the consumer to be employed as a W–2 wage employee.[39]

Although age and employment eligibility criteria may be set forth in the product marketing materials and/or enrollment forms, the Board believes few consumers notice this information when they obtain credit and choose to purchase the voluntary credit insurance or debt cancellation or debt suspension coverage. Because the product is sold in connection with a credit transaction that is underwritten by the creditor, the consumer may reasonably believe that the creditor has determined that the consumer is eligible for the product. This may be especially true for age restrictions because that information is typically requested by the creditor on the credit application form. As a result, many consumers may not discover until they file a claim that they were paying for a product for which they were not eligible when they initially purchased it. Consumers that do not submit claims may never discover that they are paying for products that hold no value for them.

To address this problem, the Board proposes to add §§ 226.4(d)(1)(iv) and 226.4(d)(3)(v) to permit creditors to exclude a premium or charge from the finance charge only if the creditor determines at the time of enrollment that the consumer meets any applicable age or employment eligibility criteria for the credit insurance or the debt suspension or debt cancellation coverage. These provisions would apply to open-end as well as closed-end (non-real property) credit transactions. Proposed comment 4(d)–14 would state that a premium or charge for credit life, accident, health, or loss-of-income insurance, or debt cancellation or debt suspension coverage is voluntary and can be excluded from the finance charge only if the consumer meets the product's age or employment eligibility criteria at the time of enrollment. The proposed comment would further clarify that to exclude such a premium or charge from the finance charge, the creditor would have to determine at the time of enrollment that the consumer is eligible for the product under the product's age or employment eligibility restrictions.

Proposed comment 4(d)–14 would provide that the creditor could use reasonably reliable evidence of the consumer's age or employment status to satisfy the condition. Reasonably reliable evidence of a consumer's age would include using the date of birth on the consumer's credit application, on the driver's license or other government-issued identification, or on the credit report. Reasonably reliable evidence of a consumer's employment status would include the consumer's information on a credit application, Internal Revenue Service Form W–2, tax returns, payroll receipts, or other evidence such as a letter or e-mail from the consumer or the consumer's employer. A determination of age or employment eligibility at the time of enrollment should not be unduly burdensome because in most cases the creditor would already have information about the consumer's age and employment status as part of the credit underwriting process. The Board seeks comment on whether other examples of reasonably reliable evidence of the consumer's age or employment status should be included.

Proposed comment 4(d)–14 would clarify that, if the consumer does not meet the product's age or employment eligibility criteria, then the premium or charge is not voluntary and must be included in the finance charge. If the creditor offers a bundled product (such as credit life insurance combined with credit involuntary unemployment insurance) and the consumer does not meet the age and/or employment eligibility criteria for all of the bundled products, the proposed commentary would clarify that the creditor must either: (1) treat the entire premium or charge for the bundled product as a finance charge, or (2) offer the consumer the option of selecting only the products for which the consumer is eligible and exclude the premium or charge from the finance charge if the consumer chooses an optional product for which the consumer meets the age and/or employment eligibility criteria at the time of enrollment.

The Board proposes this rule and commentary to address concerns about the voluntary nature of this product. TILA Section 106(b), 15 U.S.C. 1605(b), states that ''[c]harges or premiums for credit life, accident, or health insurance written in connection with any consumer credit transaction shall be included in the finance charge unless (1) the coverage of the debtor by the insurance is not a factor in the approval by the creditor of the extension of credit, and this fact is clearly disclosed in writing to the person applying for or obtaining the extension of credit; and (2) in order to obtain the insurance in connection with the extension of credit, the person to whom the credit is extended must give specific affirmative written indication of his desire to do so after written disclosure to him of the cost thereof.'' Historically, § 226.4(d) has implemented this provision as a ''voluntariness'' standard. For example, in 1981, comment 4(d)–5 was adopted as part of the TILA simplification process. The comment stated that the credit insurance ''must be *voluntary* in order for the premium to be excluded from the finance charge.'' 46 FR 50288, 50301; Oct. 9, 1981 (emphasis added). In 1996, the Board amended Regulation Z to apply the rules for credit insurance to debt cancellation coverage. In adopting this provision, the Board

[36] The provisions regarding debt suspension coverage were in the December 2008 Open-End Final Rule. *See* 74 FR 5244, 5400; Jan. 29, 2009. These provisions will take effect on July 1, 2010.

[37] *See, e.g., Parker et al.* v. *Protective Life Ins. Co. of Ohio et al.,* Nos. 2004–T–0127 and 2004–T–0128, 2006 Ohio App. LEXIS 3983, at *28 (Ohio Ct. App. Aug. 4, 2006) (reversing summary judgment for defendants automobile dealership and insurer because the automobile dealership employee did not evaluate whether the plaintiffs were eligible for credit disability insurance and the plaintiffs were later denied benefits based on eligibility restrictions); *Stewart v. Gulf Guaranty Life Ins. Co.,* No. 2000–CA–01511–SCT, 2002 Miss. LEXIS 254, at *4 (Miss. Aug. 15, 2002) (affirming the jury award where the insurer did not require the bank employee to have the consumer fill out a credit life and disability insurance application regarding pre-existing conditions and the insurer later denied coverage based on a pre-existing condition).

[38] *See, e.g., Fed. Trade Comm'n* v. *Stewart Finance Holdings, Inc. et al.,* Civ. Action No. 103CV–2648, Final Judgment and Order at 13 (N.D. Ga. Nov. 9, 2005) (alleging that the finance company sold accidental death and dismemberment insurance to borrowers who were not eligible for the product due to age restrictions).

[39] *See, e.g., In the Matter of Providian Nat'l Bank,* OCC Docket No. 2000–53, Consent Order (June 28, 2000) (alleging that the bank marketed an involuntary unemployment credit protection program but failed to adequately disclose that such protection was unavailable to consumers who were self-employed).

stated: ''The new rule allows creditors to exclude fees for *voluntary* debt cancellation coverage from the finance charge when specified disclosures are made.'' 61 FR 49237, 49240; Sept. 19, 1996 (emphasis added). In the December 2008 Open-End Final Rule, the Board applied the rules for credit insurance and debt cancellation coverage to debt suspension coverage. In adopting this provision, the Board referred to the May 2007 Open-End Proposed Rule, which stated that the Board ''proposed to revise § 226.4(d)(3) to expressly permit creditors to exclude charges for *voluntary* debt suspension coverage from the finance charge when, after receiving certain disclosures, the consumer affirmatively requests such as product.'' 74 FR 5244, 5266; Jan. 29, 2009 (emphasis in original). Finally, the model forms currently contain the following statement emphasizing the voluntary nature of the product: ''Credit life insurance and credit disability insurance are not required to obtain credit, and will not be provided unless you sign and agree to pay the additional cost.'' *See* Appendix H–1 (Credit Sale Model Form) and Appendix H–2 (Loan Model Form). The Board believes that if the consumer was ineligible for the benefits of credit insurance or debt cancellation or debt suspension coverage at the time of enrollment, then the purchase cannot be voluntary because a reasonable consumer would not knowingly purchase a policy for which he or she can derive no benefit. For these reasons, the Board believes that the requirements of proposed §§ 226.4(d)(1)(iv) and 226.4(d)(3)(v) would help ensure that the purchase of credit insurance or debt cancellation or debt suspension coverage would, in fact, be voluntary.

The Board notes that although the proposed rule would require creditors to determine the consumer's age and/or employment eligibility for the product at the time of enrollment, the proposed rule would not affect the creditor's ability to deny coverage if the consumer misrepresented his or her age or employment status at the time of enrollment. Finally, the proposed rule does not require a creditor to determine if a consumer ceases to meet the age or employment eligibility criteria after enrollment. For example, the creditor has complied with the proposal if the consumer becomes ineligible for the policy or coverage after enrollment. State or other law may address these issues. However, the Board solicits comment on whether creditors should be required to determine whether the consumer meets the product's age or employment eligibility criteria after the product is sold (*e.g.,* before renewing an annual premium), or whether creditors should be required to provide notice when the consumer exceeds the age limit of the product after enrollment.

Revised disclosures. As discussed above, TILA Section 106(b), 15 U.S.C. 1605(b), and §§ 226.4(d)(1) and 226.4(d)(3) allow a creditor to exclude from the finance charge a credit insurance premium or debt cancellation or debt suspension fee if the creditor provides disclosures that inform the consumer of the voluntary nature and cost of the product. Currently, Regulation Z does not specifically mandate the format of these disclosures, but provides sample language in the model forms. For example, Appendix H–2 (Loan Model Form) contains the following language: ''Credit life insurance and credit disability insurance are not required to obtain credit, and will not be provided unless you sign and agree to pay the additional cost.'' The model form also shows the type of product (*e.g.,* credit life or credit disability); the cost of the premium; and a signature line. The signature area is accompanied by the following language: ''I want credit life insurance.''

Concerns have been raised about whether the current disclosures sufficiently inform consumers of the voluntary nature and costs of the product. To address these concerns, a disclosure was tested that included a charge for credit life insurance and listed the product under the title ''Optional Features.'' Only about half of the participants understood that accepting credit insurance was voluntary and that they could decline the product. Subsequently, a disclosure was tested that stated, ''STOP. You do *not* have to buy this insurance to get this loan.'' After reading this disclosure, all participants understood the voluntary nature of the product.

In addition, concerns have been raised about the product's cost. The product may be more costly than, for example, traditional life insurance, but may not provide additional benefits. To address this concern, the Board tested the following language: ''If you have insurance already, this policy may not provide you with any additional benefits. Other types of insurance can give you similar benefits and are often less expensive.'' Participant comprehension of the costs and benefits of the product was significantly increased by these plain-language disclosures.

Concerns have also been raised about eligibility restrictions. Consumers might not be aware that they may incur a cost for a product that provides no benefit to them if the eligibility criteria are not met at the time of enrollment. Accordingly, the Board tested the following language: ''Even if you pay for this insurance, you may not qualify to receive any benefits in the future.'' Participants were greatly surprised to learn that they might purchase the insurance only to later discover that they were not eligible for benefits. A few participants indicated that they did not understand how they could pay for the coverage and then receive no benefits. To address this issue and to conform to the requirements of proposed §§ 226.4(d)(1)(iv) and 226.4(d)(3)(v), the following statement was added to the disclosure: ''Based on our review of your age and/or employment status at this time, you would be eligible to receive benefits.'' However, if there are other eligibility restrictions, such as pre-existing health conditions, the creditor would be required to disclose the following statements: ''Based on our review of your age and/or employment status at this time, you may be eligible to receive benefits. However, you may not qualify to receive any benefits because of other eligibility restrictions.''

Finally, a sentence was added to the disclosure to refer consumers to the Board's Web site to learn more about the product, and the cost disclosure was streamlined to display more clearly the exact cost of the product. Most consumer testing participants indicated they would visit the Board's Web site to learn more about a credit insurance or debt cancellation or debt suspension product.

Based on this consumer testing, the Board proposes to add model clauses and samples that provide clearer information to consumers about the voluntary nature and costs of credit insurance or debt cancellation or debt suspension coverage. These model clauses and samples would apply in open-end or closed-end (not secured by real property) transactions, if the product is voluntary and the consumer qualifies for benefits based on age or employment. For closed-end transactions secured by real property or a dwelling, the model clause or sample would be required whether or not the product is voluntary. Model Clauses and Samples are proposed at Appendix G–16(C) and G–16(D) and H–17(C) and H–17(D). These Model Clauses and Samples would be in addition to the Debt Suspension Model Clauses and Samples found at Appendix G–16(A) and G–16(B) and H–17(A) and H–17(B).

Timing of disclosures. Currently, comment 4(d)–2 states that ''[i]f disclosures are given early, for example under § 226.17(f) or § 226.19(a), the creditor need not redisclose if the actual premium is different at the time of consummation. If insurance disclosures are not given at the time of early disclosure and insurance is in fact written in connection with the transaction, the disclosures under § 226.4(d) must be made in order to exclude the premiums from the finance charge.'' The Board proposes to delete the reference to § 226.19(a) to conform to the new timing and redisclosure requirements under proposed § 226.19(a).

4(d)(2) Property Insurance Premiums

The proposal would retain the exclusion from the finance charge of premiums for insurance against loss or damage to property or against liability arising out of the ownership or use of property under TILA Section 106(c) and § 226.4(d)(2). Consumers typically purchase property and liability insurance to protect against a variety of risks, including loss of or damage to the property, such as damage caused by fire, loss of or damage to personal property kept on the property, such as furniture, and owner liability for injuries incurred by visitors to the property. Although creditors generally require such insurance as a condition of extending closed-end credit secured by real property or a dwelling in order to protect the value of the collateral that is securing the loan, consumers who do not have mortgages regularly purchase this type of insurance to protect themselves from the risks described above. This type of insurance is best viewed as a hybrid product that protects not only the value of the creditor's collateral, but also protects the consumer from loss or impairment of the consumer's equity in the property, loss or impairment of the consumer's personal property, and personal liability if anyone is injured on the property. Consequently, it is impossible to segregate that portion of the insurance (and that portion of the premium) which protects the creditor from that portion which protects only the consumer.

In addition, the Board has not identified significant abuses in connection with the sale or marketing of insurance against loss or damage to property or against liability arising out of the ownership or use of property. The market for these products appears to be competitive. Consumers can purchase this type of insurance from many insurance companies, including companies not associated with mortgage lenders. In addition, policies generally are tailored to the particular risks faced by the consumer. Thus, consumers have choices with regard to how much insurance to purchase to cover various risks and, as a result, have some control over the premiums they pay.

The Board requests comment on the appropriateness of retaining the current exclusion from the finance charge of premiums for insurance against loss or damage to property or against liability arising out of the ownership or use of property. The Board notes that, under current § 226.4(d)(2), the category of property and liability insurance has been interpreted to include coverage against flood risks; the Board seeks comment on whether the reasons for retaining the exclusion discussed above are applicable to flood insurance specifically and, if not, whether it should be subject to separate treatment under Regulation Z. In addition, the Board requests comment on whether including such premiums in the finance charge could have adverse or unintended consequences for consumers and for creditors.

TILA Section 106(c) states that charges or premiums for property insurance must be included in the finance charge unless ''a clear and specific statement in writing is furnished by the creditor to the person to whom the credit is extended, setting forth the cost of the insurance if obtained *from or through the creditor,* and stating that the person to whom the credit is extended may choose the person through which the insurance is to be obtained.'' 15 U.S.C. 1605(c) (emphasis added). Section 226.4(d)(2) permits property insurance premiums to be excluded from the finance charge under the following conditions, among others: ''If the coverage is obtained *from or through the creditor,* the premium for the initial term of insurance coverage shall be disclosed. If the term of insurance is less than the term of the transaction, the term of insurance shall also be disclosed.'' (Emphasis added). Comment 4(d)–8 states, in relevant part, that ''[t]he premium or charge must be disclosed only if the consumer elects to purchase the insurance *from the creditor;* in such a case, the creditor must also disclose the term of the property insurance coverage if it is less than the term of the obligation.'' (Emphasis added.) Currently, the comment does not use the statutory language ''from or through the creditor'' and does not define the phrase. To conform to the statutory and regulatory language, the Board proposes to amend comment 4(d)–8 to clarify that the premium or charge and term (if less than the term of the obligation) must be disclosed if the consumer elects to purchase the insurance ''from or through the creditor.'' In addition, the proposed comment would clarify that insurance is available ''from or through a creditor'' if it is available from the creditor's ''affiliate,'' as that term is defined under the Bank Holding Company Act, 12 U.S.C. 1841(k). The Bank Holding Company Act defines an ''affiliate'' as ''any company that controls, is controlled by, or is under common control with another company.'' Thus, if the consumer elects to purchase property insurance from a company that controls, is controlled by, or is under common control with the creditor, then the creditor would be required to disclose the cost of the insurance, and the term, if it is less than the term of the obligation. The Board believes that this proposed rule would clarify for creditors the meaning of ''through the creditor'' and provide consumers with a clearer disclosure of the cost of property insurance.

4(d)(4) Telephone Purchases

Under §§ 226.4(d)(1) and 226.4(d)(3), creditors may exclude from the finance charge premiums for credit insurance or fees for debt cancellation or debt suspension coverage, if the creditor provides certain disclosures in writing and the consumer signs or initials an affirmative written request for the insurance or coverage. Over the years, the Board has received industry requests to permit creditors to provide the disclosures and obtain the affirmative consumer request orally in order to facilitate telephone purchases of these products. In addition, the OCC has issued telephone sales guidelines for national banks that sell debt cancellation and debt suspension coverage. 12 CFR 37.6(c)(3), 37.7(b).

In the December 2008 Open-End Final Rule, the Board created an exception to the requirement to provide prior written disclosures and obtain written signatures or initials for telephone purchases of credit insurance and debt cancellation or debt suspension coverage in connection with open-end (not home-secured) plans. 74 FR 5244, 5267; Jan. 29, 2009. This rule will take effect on July 1, 2010. Under new § 226.4(d)(4), for telephone purchases a creditor may make the disclosures orally and the consumer may affirmatively request the insurance or coverage orally, provided that the creditor (1) maintains evidence that the consumer, after being provided the disclosures orally, affirmatively elected to purchase the insurance or coverage, and (2) mails the required disclosures within three business days after the telephone purchase. New comment 226.4(d)(4)–1 provides that a creditor does not satisfy the requirement to obtain a consumer's affirmative request if the ''request'' was a response to a leading question or negative consent. The comment also provides an example of an acceptable enrollment question (''Do you want to enroll in this optional debt cancellation plan?'').

The Board promulgated this rule pursuant to its exception and exemption authorities under TILA Section 105. Section 105(a) authorizes the Board to make exceptions to TILA 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). In addition, the Board considered the exemption factors set forth in TILA Section 105(f)(2), 15 U.S.C. 1604(f)(2), and determined that an exemption for telephone purchases for open-end (not home-secured) plans was appropriate because the rule contained adequate safeguards to ensure that oral purchases are voluntary. 74 FR 5268. The Board emphasized that consumers in open-end (not home-secured) plans receive monthly statements that clearly disclose fees, including credit insurance and debt cancellation or debt suspension coverage charges. *Id.* Consumers who are billed for insurance or coverage they did not request can dispute the charge as a billing error. *Id.* The Board stated that as part of the closed-end review, it would consider whether to expand the telephone purchase rule to this type of credit. 74 FR 5267.

The Board believes that a telephone purchase rule for closed-end credit is not appropriate. Monthly statements are not required for closed-end credit, and it would be difficult for consumers who do not receive monthly statements to detect charges for unwanted coverage. Moreover, there is no billing error resolution process for closed-end loans.

Finally, the Board noted in the December 2008 Open-End Final Rule that an exception or exemption for the telephone purchase of credit insurance or debt cancellation or debt suspension coverage in connection with closed-end loans may be ''less necessary.'' 74 FR 5267. For open-end (not home-secured) credit, new comments 4(b)(7) and (8)–2 and 4(b)(10)–2 in the December 2008 Open-End Final Rule clarify that credit insurance and debt cancellation or debt suspension coverage is ''written in connection with a credit transaction'' if the consumer purchases it after the opening of an open-end (not home-secured) plan because the consumer retains the ability to obtain advances of funds. 74 FR 5265. Therefore, in such a transaction, the creditor must comply with the disclosure and consumer request requirements even if the credit insurance and debt cancellation or debt suspension coverage is sold after the opening of the plan. A creditor in an open-end (not home-secured) transaction may be more likely to market the product by telephone after the opening of the plan, and new § 226.4(d)(4) facilitates the telephone purchase. By contrast, a creditor in a closed-end transaction is more likely to have the opportunity to meet the consumer face-to-face at or before consummation to market the product, provide the disclosure, and obtain the consumer request. For these reasons, this proposal does not contain a telephone purchase rule for credit insurance or debt cancellation or debt suspension coverage sold in connection with a closed-end credit transaction. The Board seeks comment on this issue. For a discussion of the application of the telephone purchase rule to HELOCs, see the Board's proposal for such transactions published simultaneously with this proposal.

4(e) Certain Security Interest Charges

The Board proposes to amend § 226.4(e), which provides exclusions from the finance charge for certain government recording and related charges and insurance premiums incurred in lieu of such charges, as limited by proposed § 226.4(g). Thus, the exclusions listed in § 226.4(e) would not apply to closed-end credit transactions secured by real property or a dwelling. The Board also proposes certain conforming amendments to the staff commentary under this provision.

4(g) Special Rule; Closed-End Mortgage Transactions

The Board is proposing to add a new § 226.4(g) as a special rule for closed-end credit transactions secured by real property or a dwelling. Proposed § 226.4(g) would provide that the exclusions from the finance charge enumerated in §§ 226.4(a)(2) (closing agent charges), (c) (miscellaneous charges), (d) (premiums for certain insurance and debt cancellation coverage), and (e) (certain security-interest charges) do not apply to closed-end credit transactions secured by real property or a dwelling, except that the exclusions in § 226.4(c)(2) for late, over-limit, delinquency, default, and similar fees, § 226.4(c)(5) for seller's points, and § 226.4(d)(2) for property and liability insurance would continue to apply to such transactions. As noted above, a cross-reference to the special rule in § 226.4(g) would be added to each of the enumerated sections. With these changes, the following fees that currently are excluded from the finance charge would be included in the finance charge for closed-end mortgage transactions (unless otherwise excluded): Closing agent charges, application fees charged to all applicants for credit (whether or not credit is extended), voluntary credit insurance premiums, voluntary debt-cancellation charges or premiums, taxes or fees required by law and paid to public officials relating to security interests, premiums for insurance obtained in lieu of perfecting a security interest, taxes imposed as a condition of recording the instruments securing the evidence of indebtedness, and various real-estate related fees.

Proposed commentary to § 226.4(g) is included to clarify the rule for mortgage transactions. Proposed comment 4(g)–1 clarifies that the commentary for the exclusions identified above no longer applies to closed-end credit transactions secured by real property or a dwelling. Proposed comment 4(g)–2 clarifies that third-party charges that meet the definition under § 226.4(a) and are not otherwise excluded generally are finance charges, whether or not the creditor requires the services for which they are imposed. Proposed comment 4(g)–3 clarifies that charges payable in a comparable cash transaction, such as property taxes and fees or taxes imposed to record the deed evidencing transfer of title to the property from the seller to the buyer, are not finance charges because they would have to be paid even if no credit were extended to finance the purchase.

Request for Comment

The Board solicits comment on the benefits and costs of the proposed changes for determining the finance charge for closed-end credit transactions secured by real property or a dwelling. The Board requests comment specifically on whether this approach adequately or appropriately addresses the concerns raised by the ''some fees in, some fees out'' approach in light of the statute's purposes, the need for consumer protection and meaningful disclosures, and industry concerns regarding complexity and burden. The Board also seeks comment on the benefits and costs of the rules for insurance and related products under the proposed amendments to § 226.4(d).

Section 226.17 General Disclosure Requirements

The Board is proposing new rules governing format and content of disclosures for transactions secured by real property or a dwelling under new

§§ 226.37 and 226.38. Accordingly, the Board proposes conforming and technical amendments to current §§ 226.17 and 226.18, as discussed more fully below. In addition, in reviewing the rules for closed-end credit, regulatory text and associated commentary have been redesignated, and footnotes moved to the text of the regulation or commentary, as appropriate, to facilitate compliance with the regulation.

17(a) Form of Disclosures

17(a)(1)

The Board proposes special rules in new § 226.37 and associated commentary to govern the format of disclosures required under proposed §§ 226.38 and 226.20(d), and existing §§ 226.19(b) and 226.20(c). These new format rules would be in addition to the rules contained in current § 226.17(a)(1). Current § 226.17(a)(1) requires that closed-end credit disclosures be grouped together, segregated from everything else, and not contain any information not directly related to the disclosures. The Board proposes to revise § 226.17(a)(1) to clarify that the general disclosure standards continue to apply to transactions secured by real property or a dwelling, but under the proposal, creditors would also be required to meet the higher standards under proposed § 226.37. In addition, § 226.17(a)(1) would be revised to reflect the requirement of electronic disclosures in certain circumstances, as discussed under § 226.19(d). Under the proposal, the substance of footnotes 37 and 38 would be moved to the regulatory text of § 226.17(a)(1).

Footnotes 37 and 38 currently provide exceptions to the grouped and segregated requirement under § 226.17(a)(1). Footnote 37 allows creditors to include certain information not directly related to the required disclosures, such as the consumer's name, address, and account number. Footnote 38, which implements TILA Section 128(b)(1) in part, allows creditors to exclude certain required disclosures from the grouped and segregated requirement, such as the creditor's identity under § 226.18(a). 15 U.S.C. 1638(b)(1). The Board proposes to revise the substance of footnote 38 to require that the creditor's identity under § 226.18(a) be subject to the grouped together and segregated requirement for all closed-end credit disclosures. (See proposed § 226.37(a)(2), which parallels this approach for transactions secured by real property or a dwelling). The Board proposes to make this adjustment 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 to effectuate the statute's purposes, which include facilitating consumers' ability to compare credit terms, and avoiding the uninformed use of credit. 15 U.S.C. 1601(a).

The Board believes requiring the creditor's identity to be grouped together with required disclosures could assist consumers. The Board believes it is important for the disclosures to bear the creditor's identity so that consumers can more easily identify the appropriate entity. As a result, the Board believes the proposal would help serve TILA's purpose to provide meaningful disclosure of terms.

Commentary to § 226.17(a)(1) provides guidance to creditors regarding the general disclosures standards contained in § 226.17(a)(1). The Board proposes to clarify the applicability of comments 17(a)(1)–2, –5, –6, and –7 to transactions secured by real property or a dwelling.

Current comment 17(a)(1)–2 provides an exception to the grouped and segregated requirement for disclosures on variable rate transactions required under existing §§ 226.19(b) and 226.20(c). For the reasons discussed under proposed § 226.37(a)(2), the Board proposes to require that ARM loan program disclosures under proposed § 226.19(b), and ARMs adjustment notices under proposed § 226.20(c), be subject to the grouped and segregated requirement. As a result, the reference made to §§ 226.19(b) and 226.20(c) would be removed from comment 17(a)(1)–2.

Current comment 17(a)(1)–5, which addresses information considered directly related to the segregated disclosures, would be revised to clarify that it does not apply to transactions secured by real property or a dwelling, and to cross-reference proposed § 226.37(a)(2). Under the proposal, cross-references in comments 17(a)(1)–5(viii), (xi), (xii), and (xvi) would be updated; no substantive change is intended. In addition, as noted below, proposed revisions to § 226.18(f) regarding variable rate transactions, and proposed § 226.38(j)(6) regarding assumption disclosure for transactions secured by real property or a dwelling, render comments 17(a)(1)–5(xiii) and (xiv) unnecessary and therefore those comments would be deleted. Finally, comment 17(a)(1)–5(xvi) would be revised to update cross-references.

As discussed under proposed §§ 226.37(a)(2) and 226.38, the Board proposes to require that creditors make disclosures for transactions secured by real property or a dwelling only as applicable. Current comment 17(a)(1)–6, which permits creditors to design multi-purpose forms for closed-end credit disclosures as long as they are clear and conspicuous, would be revised to clarify that it does not apply to transactions secured by real property or a dwelling, as discussed more fully below under proposed § 226.37(a)(2).

Finally, the Board proposes to clarify in current comment 17(a)(1)–7 that transactions secured by real property or a dwelling and that have balloon payment financing with leasing characteristics are treated as closed-end credit under TILA and subject to its disclosure requirements.

17(a)(2)

Section 226.17(a)(2), which implements TILA Section 122(a), requires the terms finance charge and annual percentage rate, together with a corresponding amount or percentage rate, to be more conspicuous than any other disclosure, except the creditor's identity under § 226.18(a). The Board proposes new disclosure requirements under proposed § 226.38(e)(5)(ii) for the finance charge (renamed ''interest and settlement charges''), and under proposed §§ 226.37(a)(2) and 226.38(b) for the APR. As a result, the Board would revise § 226.17(a)(2) to be inapplicable to transactions secured by real property or a dwelling.

17(b) Time of Disclosures

Section 227.17(b) and comment 17(b)–1 require creditors to make closed-end credit disclosures before consummation of the transaction; special timing requirements apply to dwelling-secured transactions and variable-rate transactions. As discussed more fully under § 226.19, the Board is proposing to require creditors to make pre-consummation disclosures for transactions secured by real property or a dwelling in accordance with special timing requirements. As a result, the Board proposes to revise § 226.17(b) and comment 17(b)–1 to clarify that more specific timing rules would apply to transactions secured by real property or a dwelling. Current comment 17(b)–2, which addresses disclosure requirements for transactions converted from open-end to closed-end, would be revised to clarify that the special timing requirements under § 226.19(b) would apply for adjustable rate transactions secured by real property or a dwelling.

17(c) Basis of Disclosures and Use of Estimates

17(c)(1) Legal Obligation

Section 226.17(c)(1) requires that disclosures under subpart C reflect the terms of the legal obligation between the parties. Commentary to § 226.17(c)(1) provides guidance regarding disclosure of specific transaction types and loan features. The Board proposes to add new provisions in § 226.17(c)(1)(i) through (vi) to move certain content from commentary to the regulation, as discussed below. In addition, the Board would revise certain commentary to § 226.17(c)(1) to reflect the new disclosure regime for mortgages, and redesignate comments as appropriate. Each of these proposed subsections, and accompanying commentary, is discussed below.

Comments 17(c)(1)–1 and 17(c)(1)–2 generally address disclosure of the legal obligation and modification of such obligation. Comment 17(c)(1)–1 would be revised to include the general principle that the consumer is presumed to abide by the terms of the legal obligation. For example, proposed comment 17(c)(1)–1 states that creditors should assume that a consumer will make payments on time and in full. This proposed revision is consistent with existing comment 17(c)(2)(i)–3, which states that creditors may base all disclosures on the assumption that payments will be made on time, disregarding any possible inaccuracies resulting from consumers' payment patterns. Comment 17(c)(2)(i)–3 specifically addresses disclosures for simple-interest transactions that potentially may be affected by late payments. The proposed revisions to comment 17(c)(1)–1 would clarify that disclosures for all transactions subject to § 226.17 should be based on the assumption that the consumer will adhere to the terms of the legal obligation.

Comment 17(c)(1)–2 would be revised to clarify that transactions secured by real property or a dwelling are subject to the special disclosure rules under proposed § 226.38(a)(3) and (c). Under the proposal, preferred-rate loans with a fixed interest rate would not be considered ARMs, and therefore, comment 17(c)(1)–2 also would be revised to remove the cross-reference to § 226.19(b). Comment 17(c)(1)–2 would be redesignated as 17(c)(1)–2(i) through (iii). Comment 17(c)(1)–16, which addresses disclosure for credit extensions that may be treated as multiple transactions, would be moved and redesignated as comment 17(c)(1)–3; no substantive change is intended.

Comment 17(c)(1)–15 states that where a deposit account is created for the sole purpose of accumulating payments that are applied to satisfy the consumer's credit obligation—a practice used in Morris Plan transactions—payments to that account are treated the same as loan payments. Under the proposal, comment 17(c)(1)–15 would be removed. As discussed below, Morris Plan transactions are rare. In addition, the Board believes that such deposits clearly constitute loan payments and therefore comment 17(c)(1)–15 is unnecessary.

The remaining commentary to § 226.17(c)(1) would be revised and redesignated as discussed below under proposed subsections 17(c)(1)(i) through (vi).

17(c)(1)(i) Buydowns

Comments 17(c)(1)–3 through 17(c)(1)–5 address third-party buydowns, consumer buydowns, and split buydowns, respectively. The proposed rule would add a new provision in § 226.17(c)(1)(i) that reflects that existing commentary about buydowns. Proposed § 226.17(c)(1)(i) requires creditors to disclose an APR that is a composite rate, based on the rate in effect during the initial period and the rate in effect for the remainder of the loan's term, if the consumer's interest rate or payments are reduced for all or part of the loan term. Proposed § 226.17(c)(1)(i) applies to seller or third-party buydowns if they are reflected in the legal obligation, and to all consumer buydowns.

Comments 17(c)(1)–3 through 17(c)(1)–5 would be redesignated as comments 17(c)(1)(i)–1 through –4 and revised to reflect changes in the terminology used under the proposed rule to describe the finance charge, for transactions secured by real property or a dwelling.

17(c)(1)(ii) Wrap-Around Financing

Comment 17(c)(1)–6 provides guidance on disclosures for transactions that involve wrap-around financing; comment 17(c)(1)–7 provides guidance on disclosures for wrap-around transactions that include a balloon payment. Both comments state that, in transactions that involve wrap-around financing, the amount financed equals the sum of the new funds advanced by the wrap creditor and the remaining principal owed to the original creditor on the pre-existing loan. The proposed rule would incorporate this guidance into proposed § 226.17(c)(1)(ii). Comments 17(c)(1)–6 and 17(c)(1)–7 would be redesignated as comments 17(c)(1)(ii)–1 and 17(c)(1)(ii)–2, respectively; no substantive change is intended.

17(c)(1)(iii) Variable- or Adjustable-Rate Transactions

Comment 17(c)(1)–8 currently provides that creditors should base disclosures for variable- or adjustable-rate transactions on the full term of the transaction and the terms in effect at the time of consummation and should not assume that the rate will increase. The proposed rule would incorporate that guidance into proposed § 226.17(c)(1)(iii). Proposed § 226.17(c)(1)(iii) would require creditors to base disclosures for variable- or adjustable-rate transactions on the full loan term, and on the terms in effect at the time of consummation, except as otherwise provided under proposed §§ 226.17(c)(1)(iii) or 226.38(a)(3) and (c) for transactions secured by real property or a dwelling.

As discussed below under proposed § 226.38(c), creditors would be required to disclose specified rate and payment adjustments for adjustable-rate loans secured by real property or a dwelling. As a result, comment 17(c)(1)–8 would be revised to clarify that creditors must disclose specified rate and payment adjustments for adjustable-rate loans secured by real property or a dwelling in accordance with the requirements under proposed § 226.38(c). Current comment 17(c)(1)–8 would be redesignated as comment 17(c)(1)(iii)–1.

Current comment 17(c)(1)–9, which states that a variable-rate feature does not, by itself, make the disclosures estimates, would be redesignated as comment 17(c)(1)(iii)–2. No substantive change is intended.

17(c)(1)(iii)(A) and (B) Discounted and Premium Rates

Comment 17(c)(1)–10 provides that if the initial interest for a variable-rate transaction is not determined by the index or formula used to make later interest-rate adjustments, disclosures should reflect a composite APR based on the initial interest rate for as long as it is charged and, for the remainder of the term, the rate that would have been applied using the index or formula at the time of consummation. The proposed rule would incorporate that commentary into proposed § 226.17(c)(1)(iii)(B).

Proposed § 226.17(c)(1)(iii) contains two separate disclosure rules; which disclosure rule applies depends on whether or not the initial rate is determined using the same index or formula used to make subsequent rate adjustments. If the initial rate is determined using the same index or formula used for subsequent rate adjustments, then the general rule that disclosures must reflect the terms in effect at the time of consummation applies under proposed § 226.17(c)(1)(iii)(A). If the initial rate is set using a different index or formula, however, disclosures must reflect a composite APR under proposed § 226.17(c)(1)(iii)(B). The composite APR would be based on the initial rate for as long as it is charged and, for the remainder of the loan term, the rate that would have applied if such index or formula had been used at the time of consummation. Comments 17(c)(1)–10(i) through (vi) would be revised to reflect that, under the proposed rule, for transactions secured by real property or a dwelling, new terminology would be used for specified disclosures (for example, the term ''interest and settlement charges'' would be used in place of ''finance charge''), as discussed below. Comments 17(c)(1)–10(i) through (vi) also would be redesignated as comments 17(c)(1)(iii)–3(i) through (vi); no substantive change is intended. Finally, a cross-reference in comment 24(c)–4 would be updated to reflect the redesignation of comment 17(c)(1)–10.

Comment 17(c)(1)–11 provides that variable rate transactions include the following transaction types, even if initially they feature a fixed interest rate: balloon-payment loans where the creditor is unconditionally obligated to renew, but can increase the interest rate at the time of renewal; preferred-rate loans where the interest rate may increase upon some future event; and price-level adjusted mortgages that provide for periodic payment and loan balance adjustments. (But see the discussion under proposed § 226.19(b) on comment 19(b)–5, which clarifies that creditors need not provide the disclosures required by § 226.19(b) for specified balloon-payment, preferred-rate, and price-level adjusted mortgages.) As discussed below, proposed § 226.38(a)(3), which address disclosure of loan type for transactions secured by real property or a dwelling, would treat each of these transaction types as fixed-rate loans. As a result, comment 17(c)(1)–11 would be revised to clarify that balloon-payment, preferred-rate, and price-level adjusted mortgages secured by real property or a dwelling are considered fixed-rate transactions for the purposes of the loan type disclosure required under proposed § 226.38(a)(3). (See also the discussion under proposed § 226.38(c), which clarifies that the loan type attributed to transactions under proposed § 226.38(a)(3) applies for purposes of interest rate and payment summary disclosures under proposed § 226.38(c).)

Further, certain shared-equity or shared-appreciation mortgages are considered variable-rate transactions under comment 17(c)(1)–11. However, under the proposal, if a mortgage is secured by real property or a dwelling, the mortgage would not be considered an adjustable-rate loan solely because of a shared-equity or shared-appreciation feature. As discussed under proposed §§ 226.19(b)(2)(ii)(F) and 226.38(d)(2)(vi), the Board would require creditors to disclose shared-equity or shared-appreciation as a loan feature for transactions secured by real property or a dwelling. As a result, guidance in comment 17(c)(1)–11 relating to shared-equity and shared-appreciation mortgages would be deleted.

Comment 17(c)(1)–11 would be redesignated as comment 17(c)(1)(iii)–4(i) through (iii), except that guidance under current comment 17(c)(1)–11 regarding graduated payment mortgages and step-rate transactions without a variable-rate feature would be redesignated as comment 17(c)(1)(iii)–5. A cross-reference to comment 17(c)(1)–11 in comment 30–1 would be updated accordingly. Comment 17(c)(1)–12, which addresses graduated-payment ARMs, would be redesignated as comment 17(c)(1)(iii)–6(i) through (iii); no substantive change is intended.

Current comment 17(c)(1)–13 states that creditors may base disclosures for growth-equity mortgages (also referred to as ''payment-escalated mortgages'') on estimated payment increases, using the best information reasonably available, or may disclose by analogy to the variable-rate disclosures in § 226.18(f)(1). As discussed below, current § 226.18(f) contains disclosure requirements for variable-rate transactions that differ based on a loan's security interest and term. Under the proposed rule, § 226.18(f) would be revised so that a loan's security interest, not its term, would determine whether the creditor would provide variable- or adjustable-rate disclosures. Accordingly, under the proposal, the reference made in comment 17(c)(1)–13 to providing disclosures analogous to those under current § 226.18(f)(1) would be deleted, and comment 17(c)(1)–13 would be revised to require creditors to base disclosures for growth-equity mortgages using estimated payment increases. The reference to graduated-payment mortgages would be removed for clarity. Comment 17(c)(1)–13 would be redesignated as comment 17(c)(1)(iii)–7.

17(c)(1)(iv) Reverse Mortgages

Comment 17(c)(1)–14 provides that if a reverse mortgage has a specified period for disbursements but repayment is due only upon the occurrence of a future event such as the death of the consumer, the creditor must assume that repayment will occur when disbursements end. The proposed rule would incorporate this commentary into the regulation as proposed § 226.17(c)(1)(vi). Comment 17(c)(1)–14 would be revised to clarify that the disclosure requirements for reverse mortgage under § 226.33 apply only if the consumer's death is one of the conditions of repayment, as provided under § 226.33(a). Comment 17(c)(1)–14 also would be revised by removing the discussion of shared-equity and shared-appreciation features because under the proposed rule transactions with such features would not be deemed adjustable-rate loans solely because of such features, as discussed above. Further, comment 17(c)(1)–14 would be revised to state that, if a reverse mortgage has an adjustable interest rate and is secured by real property or a dwelling, the creditor must disclose the shared-equity or shared-appreciation feature as required under §§ 226.19(b)(2)(ii)(F) and 226.38(d)(2)(vi). Finally, under the proposed rule comment 17(c)(1)–14 would be redesignated as comment 17(c)(1)(iv)–1(i) through (iii).

17(c)(1)(v) Tax Refund-Anticipation Loans

Comment 17(c)(1)–17 clarifies that if a consumer is required to repay a tax refund-anticipation loan when the consumer receives a tax refund, disclosures are to be based on the creditor's estimate of the time the refund will be delivered. Comment 17(c)(1)–17 further clarifies that the finance charge includes any repayment amount that exceeds the loan amount that is not excluded from the finance charge under § 226.4. The proposed rule would incorporate this guidance into the regulation as proposed § 226.17(c)(1)(v). Comment 17(c)(1)–17 which would be redesignated as comments 17(c)(1)(v)–1(i) and –1(ii) under the proposed rule. No substantive change is intended.

17(c)(1)(vi) Pawn Transactions

For pawn transactions, proposed § 226.17(c)(1)(vi) would require creditors to: (1) Disclose the initial sum provided to the consumer as the amount financed; (2) include the difference between the initial sum provided to the consumer and the price at which the item is pledged or sold in the finance charge; and (3) determine the APR using the redemption date as the end of the loan term. Proposed § 226.17(c)(1)(vi) is consistent with comment 17(c)(1)–18, which would be redesignated as comment 17(c)(1)(vi)–1. No substantive change is intended.

17(c)(2) Estimates

Under the proposal, § 226.17(c)(2) would be revised to clarify that proposed § 226.19(a) would limit creditors' ability to provide estimated disclosures for transactions secured by real property or a dwelling. As discussed below, proposed § 226.19(a) requires creditors to provide disclosures that consumers must receive no later than three business days before consummation and which may not be estimated disclosures. Comments 17(c)(2)(i)–1 and 17(c)(2)(i)–2, which address the basis and labeling of estimates, respectively, also would be revised to reflect this limitation. In addition, comment 17(c)(2)(i)–3, which states that creditors may base all disclosures on the assumption that consumers will make timely payments, would be revised to clarify that creditors may also assume that consumers would make payments in the amounts required by the terms of the legal obligation. In technical revisions, a heading would be added to § 226.17(c)(2) for clarity; no substantive change is intended.

17(c)(3) Disregarded Effects

In technical revisions, a heading would be added to § 226.17(c)(3) for clarity, and guidance under current comment 17(c)(3)–1 would be redesignated as 17(c)(3)–1(i) and (ii). No substantive change is intended.

17(c)(4) Disregarded Irregularities

Under the proposal, § 226.17(c)(4) would be revised to clarify that creditors may disregard period irregularities when disclosing the payment summary table, as required under proposed § 226.38(c), for transactions secured by real property or a dwelling. No substantive change to the treatment of period irregularities is intended.

In technical revisions, a heading would be added to § 226.17(c)(4) for clarity. Also, comment 17(c)(4)–1 would be redesignated as comment 17(c)(4)–1(i) and (ii), and comment 17(c)(4)–2 would be redesignated as comment 17(c)(4)–2(i) through (iii). No substantive change is intended.

17(c)(5) Demand Obligations

Under the proposal, comment 17(c)(5)–1, which addresses demand obligation disclosures, would be revised to reflect that proposed §§ 226.19(b)(2)(ii)(D) and 226.38(d)(2)(iv) contain requirements for disclosing a demand feature in transactions secured by real property or a dwelling. Comment 17(c)(5)–2, which addresses future events such as the maturity date, would be revised to clarify that certain disclosures for transactions not secured by real property or a dwelling may not contain estimated disclosures, as discussed below under proposed § 226.19(a)(2). Comment 17(c)(5)–3, which addresses demand after a stated period, would be revised to delete obsolete references to specific loan programs and update cross-references. Comment 17(c)(5)–4, which addresses balloon payment mortgages, would be revised to reflect that creditors must disclose a payment summary table for transactions secured by real property or a dwelling under proposed § 226.38(c) (rather than a payment schedule, as required for transactions not secured by real property or a dwelling under § 226.18(g)) and to update a cross-reference. In technical revisions, a heading would be added to § 226.17(c)(5) for clarity; no substantive change is intended.

17(c)(6) Multiple Advance Loans

In technical revisions, a heading would be added to § 226.17(c)(6) for clarity; no substantive change is intended.

17(d) Multiple Creditors; Multiple Consumers

Section 226.17(d) addresses transactions that involve multiple creditors and consumers. The Board does not propose any changes to these provisions, except that the guidance contained in current comment 17(d)–1 would be redesignated as comment 17(d)–1(i) through (iii); no substantive change is intended.

17(e) Effect of Subsequent Events

Section 226.17(e) addresses whether a subsequent event makes a disclosure inaccurate or requires a new disclosure. Under proposed § 226.20(e), if a creditor obtains insurance on behalf of the consumer subsequent to consummation, the creditor would be required to provide notice before charging for such insurance. The Board proposes to revise comment 17(e)–1 to reflect this new requirement.

17(f) Early Disclosures

Under the proposal, in addition to providing early disclosures, creditors would be required to provide additional disclosures that a consumer must receive no later than three business days before consummation for transactions secured by real property or a dwelling. Accordingly, comments 17(f)–1 through –4 would be revised to clarify that the special disclosure timing requirements under § 226.19(a)(2) would apply to transactions secured by real property or a dwelling. In technical revisions, guidance in current comment 17(f)–1 would be renumbered and headings revised to clarify that some of the current guidance would not apply to transactions secured by real property or a dwelling under the proposed rule.

17(g) Mail or Telephone Orders—Delay in Disclosures

Section 226.17(g) and comment 17(g)–1 permit creditors to delay disclosures for transactions involving mail or telephone orders until the first payment is due if certain information, such as the APR or finance charge, is provided to the consumer in advance of any request. As discussed under § 226.19(a) and 226.20(c), the Board proposes special timing requirements for disclosures for transactions secured by real property or a dwelling and for adjustable rate transactions. As a result, the Board proposes to revise § 226.17(g) and comment 17(g)–1 to clarify that they do not apply to transactions secured by real property or a dwelling.

17(h) and 17(i) Series of Sales—Delay in Disclosures; Interim Student Credit Extensions

Sections 226.17(h) and (i) address delay in disclosures in transactions involving a series of sales and interim student credit extensions. The Board does not propose any substantive changes to these provisions. In technical revisions, a cross-reference is corrected.

Section 226.18 Content of Disclosures

As noted, the Board proposes to require creditors to provide new disclosures for transactions secured by real property or a dwelling under proposed § 226.38. Accordingly, the Board would clarify under § 226.18 that creditors must provide the new disclosures under § 226.38 for transactions secured by real property or a dwelling. In addition, the Board proposes conforming amendments to § 226.18 and associated commentary to reflect the new disclosure regime for mortgages, and would redesignate comments as appropriate.

18(a) Creditor

Currently, § 226.18(a), which implements TILA Section 128(a)(1), requires disclosure of the identity of the creditor making the disclosures. 15

U.S.C. 1638(a)(1). Comment 18(a)–1 states, in part, that this disclosure may, at the creditor's option, appear apart from the other required disclosures. As discussed above, currently, § 226.17(a)(1) footnote 38, which implements TILA Section 128(b)(1), allows creditors to exclude from the grouped and segregated requirement certain required disclosures, such as the creditor's identity. 15 U.S.C. 1638(b)(1). However, the Board proposes to revise the substance of footnote 38 to require the creditor's identity under § 226.18(a) to be subject to the grouped together and segregated requirement for all closed-end credit disclosures. Thus, the Board proposes to revise comment 18(a)–1 to reflect this change.

18(b) Amount Financed

Section 226.18(b) addresses the disclosure and calculation of the amount financed. The Board proposes to revise comment 18(b)–2, which provides guidance regarding treatment of rebates and loan premiums for the amount financed calculation required under § 226.18(b). Comment 18(b)–2 primarily addresses credit sales, such as automobile financing, and provides that creditors may choose whether to reflect creditor-paid premiums and seller- or manufacturer-paid rebates in the disclosures required under § 226.18. The Board believes that creditor-paid premiums and seller- or manufacturer-paid rebates are analogous to buydowns. Like buydowns, such premiums and rebates may or may not be funded by the creditor and reduce costs that otherwise would be borne by the consumer. Accordingly, their impact on the amount financed, like that of buydowns, properly depends on whether they are part of the legal obligation. *See* comments 17(c)(1)–1 through –5. The Board is proposing to revise comment 18(b)–2 to clarify that the disclosures, including the amount financed, must reflect loan premiums and rebates regardless of their source, but only if they are part of the terms of the legal obligation between the creditor and the consumer. As discussed below, proposed comment 38(e)(5)(iii)–2 would parallel this approach for transactions secured by real property or a dwelling.

In addition, the Board proposes to revise comment 18(b)(2)–1, which addresses amounts included in the amount financed calculation that are not otherwise included in the finance charge, to remove reference to real estate settlement charges for the reasons discussed more fully under § 226.4.

18(c) Itemization of Amount Financed

Section 226.18(c) requires a separate disclosure of the itemization of amount financed and provides guidance on the amounts that must be included in such itemization. As discussed below, the Board proposes new § 226.38(e)(5)(iii) to address the calculation and disclosure requirements of the amount financed for transactions secured by real property or a dwelling. Under the proposal, the substance of footnote 40, which permits creditors to substitute good faith estimates required under RESPA for the itemization of the amount financed for dwelling-secured transactions, would be moved to new § 226.38(j)(1)(iii).

Comment 18(c)–2 affords creditors flexibility in the information that may be included in the itemization of amount financed. Under the proposal, the Board would revise comment 18(c)–2(i) to remove references made to escrow items and to the commentary under § 226.18(g) because the proposal renders them unnecessary, and 18(c)–2(vi) to reflect a technical revision with no intended change in substance or meaning. The Board also proposes to move comment 18(c)–4 regarding the exemption afforded to RESPA transactions, and 18(c)(1)(iv)–2 regarding prepaid mortgage insurance premiums to proposed comments 38(j)(1)(iii)–1 and 38(j)(1)(i)(D)–2, respectively, because they apply only to dwelling-secured transactions.

18(d) Finance Charge

Section 226.18(d) requires disclosure of the finance charge for closed-end credit. As discussed below, the Board proposes new § 226.38(e)(5)(ii) to address disclosure of the finance charge (renamed ''interest and settlement charges'') for transactions secured by real property or a dwelling. As a result, reference to the finance charge tolerances for mortgage loans would be moved from § 226.18(d) to proposed § 226.38(e)(5)(ii); no substantive change is intended. Technical amendments to comment 18(d)(2) would reflect this revision.

18(e) Annual Percentage Rate

Section 226.18(e) requires disclosure of the annual percentage rate, using that term. The substance of footnote 42 would be moved to the regulatory text of § 226.18(e). Technical amendments to comment 18(e)–2 would reflect this revision; no substantive change is intended.

18(f) Variable Rate

Section 226.18(f)(1) contains disclosure requirements for variable-rate transactions not secured by a consumer's principal dwelling and variable-rate transactions secured by a consumer's principal dwelling if the loan term is one year or less. Section 226.18(f)(1) requires creditors to make the following disclosures within three business days after receiving the consumer's application: (1) Circumstances under which the APR may increase; (2) any limitations on the increase; (3) the effect of an increase; and (4) an example of the payment terms that would result from an increase. Section 226.18(f)(2) applies to variable-rate transactions secured by a consumer's principal dwelling with a loan term greater than one year, and requires creditors to disclose that the loan has a variable-rate feature together with a statement that variable-rate program disclosures (required by current § 226.19(b)) have been provided earlier.

The Board adopted § 226.18(f)(2) in 1987, at the same time that it adopted § 226.19(b) (disclosures for variable-rate mortgages with terms greater than one year). The Board adopted those provisions based on recommendations by the Federal Financial Institutions Examination Council (FFIEC). 52 FR 48665; Dec. 24, 1987. However, the Board applied the requirements of those provisions only to loans secured by a principal dwelling with a term greater than one year. Loans secured by a principal dwelling with a term of one year or less, and loans not secured by a principal dwelling remained subject to rules in § 226.18(f)(1). The Board did not apply the new variable-rate loan disclosure requirements to such loans because public comments expressed concern about potential compliance problems for creditors making short-term loans. 52 FR at 48666.

Proposed §§ 226.19(b) and 226.38(c) contain disclosure requirements for closed-end adjustable-rate loans secured by real property or a dwelling, and would apply the same rules to loans with a term of one year or less as for loans with a term greater than one year. Disclosures required by those provisions are discussed below. As a result, § 226.18(f)(2) and comment 18(f)(2)–1, which address requirements and guidance for closed-end adjustable-rate loans secured by real property or a dwelling, are unnecessary and would be deleted. The substance of footnote 43, which permits creditors to substitute information required under § 226.18(f)(2) and 226.19(b) for the disclosures required by § 226.18(f)(1), would also be deleted. Section 226.18(f)(1)(i) through (iv) would be redesignated as § 226.18(f)(1) through

(4), and references in comment 18(f)–1 would be updated.

As discussed below, proposed §§ 226.19(b)(3)(iii) and 226.38(d)(2)(iii) regarding disclosure of shared-equity or shared-appreciation loan features would render guidance about shared-equity or shared-appreciation mortgages in comment 18(f)–1 unnecessary, and therefore that comment would be deleted. Comment 18(f)(1)–1 regarding terms used in disclosures, and comment 18(f)(1)(i)–2 regarding conversion features would be redesignated as comments 18(f)–2 and –3, respectively. Finally, comments 18(f)(1)(i)–1, 18(f)(1)(ii)–1, 18(f)(1)(iii)–1, and 18(f)(1)(iv)–1 would be redesignated as comments 18(f)(1)–1, 18(f)(2)–1, 18(f)(3)–1, and 18(f)(4)–1, respectively.

18(g) Payment Schedule

Section 226.18(g) and associated commentary address the disclosure of the payment schedule for all closed-end credit. As discussed under proposed § 226.38(c), the Board would require creditors to provide disclosures regarding interest rates and monthly payments in a tabular format for transactions secured by real property or a dwelling. As a result, creditors would not need to comply with the disclosure requirements of § 226.18(g) for such transactions. However, as discussed under proposed § 226.38(e)(5)(i), creditors would be required to disclose the number and total amount of payments that the consumer would make over the full term of the loan for transactions secured by real property or a dwelling. Proposed comment 18(e)(5)(i)–1 would require creditors to calculate the total payments following the rules under § 226.18(g) and associated commentary. As a result, the Board proposes to revise comment 18(g)–3 to require creditors to disclose the total number of payments for all payment levels as a single figure for transactions secured by real property or a dwelling, and to cross-reference proposed § 226.38(e)(5)(i).

18(h) Total of Payments

In a technical revision, the substance of footnote 44 would be moved to the regulation text of § 226.18(e); technical amendments to comment 18(h)–3 would reflect this revision.

18(i) Demand Feature

Section 226.18(i) and associated commentary address the following for all closed-end credit: disclosure of a demand feature; the type of demand features covered; and the relationship to payment schedule disclosures. The Board does not propose any change to this provision, except that comments 18(i)–2 and –3 would be updated to cross-reference proposed §§ 226.38(d)(2)(iv) and 226.38(c), which address the disclosure requirements for a demand feature and payment schedule, respectively, for transactions secured by real property or a dwelling. No substantive change is intended.

18(k) Prepayment

Section 226.18(k)(1) provides that, when an obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance, the creditor must disclose a statement that indicates whether or not a penalty may be imposed if the obligation is prepaid in full. Comment 18(k)(1)–1 provides examples of charges considered penalties under § 226.18(k)(1). One such example is ''interest charges for any period after prepayment in full is made.'' When the loan is prepaid in full, there is no balance to which the creditor may apply the interest rate. Accordingly, the proposed rule would revise this example for clarity; no substantive change is intended. Proposed § 226.38(a)(5) contains requirements for disclosing prepayment penalties for transactions secured by real property or a dwelling. As discussed below, commentary on proposed § 226.38(a)(5) is consistent with the commentary on § 226.18(k), as proposed to be revised.

18(j) Through 18(m) Total Sale Price; Prepayment; Late Payment; Security Interest

Sections 226.18(j), (k), (l), and (m) address, respectively, disclosures regarding: total sale price; prepayment; late payment; and security interest. The Board does not propose any changes to these provisions, except for a minor technical amendment to comment 18(k)(1)–1, as discussed above. However, as noted below, the Board proposes new disclosure requirements under §§ 226.38(a)(5) and 226.38(d)(1)(iii) regarding prepayment penalties, § 226.38(j)(3) regarding late payment, and § 226.38(f)(2) regarding security interest, for transactions secured by real property or a dwelling.

18(n) Insurance and Debt Cancellation

Section 226.18(n) requires disclosure of insurance and debt cancellation in accordance with the requirements under § 226.4(d) to exclude such fees from the finance charge. For the reasons discussed under § 226.4(d), the Board proposes to revise § 226.18(n) and comment 18(n)–2 to clarify that this disclosure requirement also applies to debt suspension policies.

18(o) and 18(p) Certain Security-Interest Charges; Contract Reference

Sections 226.18(o) and (p) address, respectively, disclosures regarding certain security-interest charges and contract reference. The Board does not propose any changes to these provisions. However, as noted below, the Board would require creditors to provide parallel contract references for transactions secured by real property or a dwelling under proposed § 226.38(j)(5). No parallel disclosure for security-interest charges is proposed for transactions secured by real property or a dwelling because such disclosures would not apply to those transactions under the Board's proposed revisions to § 226.4, discussed above.

18(q) Assumption Policy

Section 226.18(q) and associated commentary require disclosure of assumption policies for residential mortgage transactions. Under the proposal, the Board proposes to move § 226.18(q) and comments 18(q)–1 and –2 to proposed § 226.38(j)(6) and comments 38(j)(6)–1 and –2, respectively, because assumption policies apply only to transactions secured by real property or a dwelling. No substantive change is intended.

18(r) Required Deposit

Section 226.18(r) addresses disclosure requirements when creditors require consumers to maintain deposits as a condition to the specific transaction. Footnote 45 provides additional guidance on such required deposits and includes a reference to payments made under Morris Plans. Although at least one Morris Plan bank remains active, Morris Plans essentially are obsolete today. Accordingly, the Board proposes to move the substance of footnote 45 to the regulation text but delete the reference to Morris Plans. Comments 18(r)–1, –3, and –5 would also be similarly revised. In addition, under the proposal, comment 18(r)–2 on pledged-account mortgages would be moved to comment 38(i)–2 because it applies only to transactions secured by real property. (See also comment 17(c)(1)–15 on Morris Plans, which the Board proposes to delete as unnecessary.) Comment 18(r)–6 would be redesignated as comment 18(r)–6(i) through (vii).

Section 226.19 Early Disclosures and Adjustable-Rate Disclosures for Transactions Secured by Real Property or a Dwelling

Section 226.19(a) currently contains timing requirements for providing disclosures for closed-end transactions secured by a dwelling and subject to RESPA. Section 226.19(b) contains disclosure timing and content requirements for variable-rate loans secured by a consumer's principal dwelling. The Board proposes to revise § 226.19(a) and (b) to apply the disclosures to any closed-end transaction secured by real property or a dwelling, for reasons discussed below. Section 226.19(a) also would be revised to require creditors to provide new disclosures that a consumer must receive at least three business days before consummation, in addition to the existing requirement to provide early disclosures within three business days of application. The Board also proposes to revise the content of disclosures for ARMs required under § 226.19(b), require new disclosures about risky loan features in proposed § 226.19(c), and to include existing rules about disclosures provided through an intermediary agent or broker, or by telephone or electronic communication, in proposed § 226.19(d).

19(a) Good Faith Estimates of Mortgage Transaction Terms and New Disclosures

TILA Section 128(b)(2), 15 U.S.C. 1638(b)(2), requires creditors to mail or deliver to consumers good faith estimates of disclosures required by TILA Section 128(a), 15 U.S.C. 1638(a) (early disclosures), for a transaction secured by a dwelling and subject to RESPA. As amended by the MDIA, TILA Section 128(b)(2) requires creditors to deliver or mail the early disclosures at least seven business days before consummation. Further, TILA Section 128(b)(2), as amended by the MDIA, requires that the creditor 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 Board implemented these MDIA requirements in § 226.19(a) through a final rule effective July 30, 2009 (MDIA Final Rule). 74 FR 23289; May 19, 2009.

The Board proposes to expand the coverage of § 226.19(a) so that the timing provisions would apply to closed-end mortgage transactions secured by real property or a dwelling, and would not be limited to RESPA-covered transactions. Thus, proposed § 226.19(a) would apply to transactions secured by real property that does not include a dwelling, such as vacant land, and transactions that are not subject to RESPA, such as construction loans.

The Board also proposes to revise § 226.19(a) so that, in addition to the early disclosures, the creditor must provide final disclosures that the consumer must receive no later than three business days before consummation. Under existing § 226.19(a), by contrast, a consumer must receive new disclosures at least three business days before consummation only if changes to the previously disclosed APR exceed a specified tolerance. The Board is proposing two alternative provisions to address circumstances where terms change after the consumer has received the final disclosures.

19(a)(1)(i) Time of Good Faith Estimates of Disclosures

TILA Section 128(b)(2), 15 U.S.C. 1638(b)(2), as amended by the MDIA, requires creditors to provide early disclosures if a transaction is secured by a dwelling and subject to RESPA. However, TILA's early disclosure requirements do not apply to mortgage transactions for personal, family, or household purposes if they are secured by real property that is not a dwelling, for example a consumer's business property. Creditors need not provide early disclosures for transactions secured by property of 25 acres or more, temporary financing (such as a construction loan), or transactions secured by vacant land because RESPA does not apply to such transactions. 24 CFR 3500.5(b)(1), (3), and (4).

The Board proposes to expand § 226.19(a) to cover transactions secured by real property, even if the property is not a dwelling and even if the transaction is not subject to RESPA. (Transactions secured by a consumer's interest in a timeshare plan would be treated differently, as discussed under § 226.19(a)(5) below.) Under TILA Section 128(b)(2), 15 U.S.C. 1638(b)(2), if the transaction is not secured by a dwelling, or is not covered by RESPA, the creditor is only required to provide disclosures before consummation. The Board proposes to require creditors to provide early disclosures under TILA for all closed-end transactions secured by real property or a dwelling to facilitate compliance.

Section 226.18 currently contains requirements for the content of transaction-specific disclosures secured by real property or a dwelling, whether or not creditors are required to provide that content in early disclosures. Although under the proposed rule § 226.38 rather than § 226.18 would contain requirements for disclosure content for transactions secured by real property or a dwelling, the content required in early disclosures is the same as the content of disclosures provided in cases where early disclosures are not required. Applying the requirement to provide early disclosures to all transactions secured by real property or a dwelling would simplify creditors' determination of the time by which creditors must make the disclosures required by § 226.38. The Board requests comment about operational or other issues involved in providing early disclosures for temporary loans, however. The Board also solicits comment on whether there are other types of loans exempt from RESPA to which it is not appropriate to apply proposed § 226.19(a).

Proposed new comment 19–1 states that proposed § 226.19 applies to transactions secured by real property or a dwelling even if such transactions are not subject to RESPA. The proposed comment clarifies that TILA does not apply to transactions that are primarily for business, commercial, or agricultural purposes, however. (Proposed comment 19–1 addresses the introductory text to proposed § 226.19, which provides that all of § 226.19, not only § 226.19(a), applies to closed-end transactions secured by real property or a dwelling.)

Comment 19(a)(1)(i)–1, which discusses the coverage of § 226.19(a), would be removed because proposed comment 19–1 would discuss the coverage of all of proposed § 226.19. Comment 19(a)(1)(i)–2 would be revised to clarify that under the proposed rule disclosures required by proposed § 226.19(a)(2) may not contain estimated disclosures, with limited exceptions. The comment also would be revised to reflect that proposed § 226.37 contains requirements for disclosure of estimates and contingencies, as discussed below. Comment 19(a)(1)(i)–3 would be revised to reflect that creditors may rely on RESPA and Regulation X to determine when an application is received, even for transactions not subject to RESPA. Comment 19(a)(1)(i)–5 would be revised to refer to the itemization of the amount financed disclosures in proposed § 226.38(j) rather than in § 226.18(c), as currently referenced. Finally, comments 19(a)(1)(i)–2 through –5 would be redesignated as comments 19(a)(1)(i)–1 through –4.

19(a)(1)(ii) Imposition of Fees

On July 30, 2008, the Board published the 2008 HOEPA Final Rule amending Regulation Z, which implements TILA and HOEPA. The July 2008 final rule requires creditors to give transaction-specific cost disclosures no later than three business days after receiving a consumer's application, for closed-end mortgage transactions secured by a consumer's principal dwelling, under § 226.19(a)(1)(i). Further, the 2008 HOEPA Final Rule prohibits creditors and other persons from imposing a fee on the consumer, other than a fee for obtaining the consumer's credit history, before the consumer receives the early disclosures, under § 226.19(a)(1)(ii) and (iii). Section 226.19(a)(1)(ii) provides that if the early disclosures are mailed to the consumer, the consumer is considered to have received them three business days after they are mailed. 73 FR 44522, 44600–44601.

The proposed rule would revise § 226.19(a)(1)(ii) to conform to the presumption of receipt provision the Board subsequently adopted in the MDIA Final Rule in § 226.19(a)(2)(ii).[40] Under the proposed rule § 226.19(a)(1)(ii) would be revised to provide that if the early disclosures are mailed to the consumer or delivered to the consumer by means other than delivery in person, the consumer is deemed to have received the corrected disclosures three business days after they are mailed or delivered. This is consistent with comment 19(a)(1)(ii)–1, which provides that creditors may impose a fee any time after midnight following the third business day after the creditor delivers or mails the early disclosures in all cases, regardless of the method the creditor uses to provide the early disclosures. The Board does not intend to make substantive changes by conforming the presumption of receipt provisions under §§ 226.19(a)(1)(ii) and 226.19(a)(2)(ii).

The Board also proposes to revise comment 19(a)(1)(ii)–1 to clarify that the three-business-day presumption of receipt applies in all cases, including where a creditor uses electronic mail or a courier to provide the early disclosures. Proposed comment 19(a)(1)(ii)–1 provides that creditors that use electronic mail or a courier other than the postal service may use the three-business-day presumption of receipt. This comment is consistent with existing comment 19(a)(2)(ii)–3 adopted through the MDIA Final Rule. (Comment 19(a)(2)(ii)–3 would be redesignated as comment 19(a)(2)(v)–1 and conforming edits would be made in connection with the proposed requirement that creditors provide final disclosures that the consumer must receive no later than three business days before consummation, as discussed below.)

An additional change would be made to comment 19(a)(1)(ii)–1 under the proposed rule. Currently, comment 19(a)(1)(ii)–1 provides that if the creditor places the early disclosures in the mail, the creditor may impose a fee in all cases ''after midnight on the third business day following mailing of the disclosures.'' The Board recognizes that the phrase ''after midnight on the third business day'' may be construed to mean *either* that the creditor may impose a fee at the beginning of the third business day after the creditor receives the consumer's application, *or* at the beginning of the fourth business day after the creditor receives the consumer's application. Thus, the Board proposes to revise comment 19(a)(1)(ii)–1 to provide that the creditor may impose a fee after the consumer receives the early disclosures or, in all cases, after midnight following the third business day after mailing the early disclosures. For example, proposed comment 19(a)(1)(ii)–1 provides that (assuming that there are no intervening legal public holidays) a creditor that receives the consumer's written application on Monday and mails the early mortgage loan disclosure on Tuesday may impose a fee on the consumer on Saturday.

19(a)(2)(ii) Three-Business-Day Waiting Period

Under § 226.19(a), as revised by the MDIA Final Rule, if changes to the APR disclosed for a closed-end transaction secured by a dwelling and subject to RESPA exceed a specified tolerance, creditors must provide corrected disclosures. The consumer must receive the corrected disclosures no later than three business days before consummation. The tolerance specified for closed-end ''regular transactions'' (those that do not involve multiple advances, irregular payment periods, or irregular payment amounts) is ⅛ of 1 percentage point and for closed-end ''irregular transactions'' (those that involve multiple advances, irregular payment periods, or irregular payment amounts, such as an ARM with a discounted initial interest rate) is ¼ of 1 percentage point. *See* § 226.22(a) and footnote 46; comment 17(c)(1)–10(iv).

Currently, if an APR stated in early disclosures for a closed-end transaction not subject to § 226.19(a) remains accurate but other terms that were not labeled as estimates change, the creditor must disclose those changed terms before consummation under § 226.17(f). Creditors also must provide corrected disclosures if a variable-rate feature is added to a closed-end transaction under § 226.17(f), whether or not the transaction is subject to § 226.19(a). *See* comment 17(f)–2. In practice, most creditors provide ''final'' disclosures to a consumer on the day of consummation, whether or not the loan terms stated in the early disclosures have changed.

Under the proposed rule, after providing early disclosures for a closed-end transaction secured by real property or a dwelling, creditors would provide a second set of disclosures in all cases, under § 226.19(a)(2)(ii). The consumer would have to receive these final disclosures no later than three business days before consummation. Proposed § 226.19(a)(2)(ii) is designed to address long-standing concerns that consumers may find out about different loan terms or increased settlement costs only at consummation. Members of the Board's Consumer Advisory Council and commenters on prior Board rulemakings have expressed concern about consumers not learning of changes to credit terms until consummation. Further, several participants in the Board's consumer testing stated that they had been surprised at closing by important changes in loan terms. For example, some participants said that they had been told at closing that a loan would have an adjustable rate even though previously they had been told they would receive a fixed-rate loan. Participants said that they closed despite unfavorable changes in loan terms because they lacked alternatives, especially in the case of a loan financing a home purchase. Some participants stated that they accepted changed terms because the loan originator advised them that they could easily obtain a refinance loan with better terms in the near future.

Terms or costs may change after early disclosures are given for a variety of reasons, including that the consumer did not lock the interest rate at application or an appraisal report developed after early disclosures are provided shows a different property value than the creditor assumed when providing the early disclosure. Regardless of the reason for the changed terms, a consumer who receives notice

[40] On the same day the July 2008 final rule was published, the Congress passed the MDIA. Under the MDIA, if the APR stated in the early disclosures changes in excess of a specified tolerance, the creditor must provide corrected disclosures that the consumer must receive no later than three business days before consummation. The MDIA provides that if the creditor mails the corrected disclosures, the consumer is considered to have received them three business days after they are mailed. These early disclosure rules are contained in TILA Section 128(b)(2)(E) (to be codified at 15 U.S.C. 1638(b)(2)(E)). Section 226.19(a)(2)(ii) implements these rules.

of changed loan terms at consummation that differ from those originally disclosed does not have a meaningful opportunity to make an informed credit decision.

To address concerns about changes to loan terms, proposed § 226.19(a)(2)(ii) requires creditors to provide final disclosures that a consumer would have to receive no later than the third business day before consummation. Under proposed § 226.38(a)(4), the early disclosures and final disclosures would contain total estimated settlement costs disclosed under RESPA and HUD's Regulation X, which implements RESPA. Regulation X permits final settlement charges to be disclosed at consummation; the consumer may request that final settlement charges be disclosed twenty-four hours in advance, however. 24 CFR 3500.10(a) and (b). Thus, under RESPA, creditors, settlement agents, and settlement service providers have until the day of consummation to determine the amounts of the various settlement costs. Effective January 1, 2010, Regulation X provides that the sum of most lender-required third party settlement costs may vary no more than 10 percent from the same costs disclosed on the good faith estimate (GFE) delivered earlier. Certain other changes, such as the lender's origination fee, cannot vary, unless the consumer did not lock the interest rate.

The Board believes that proposed § 226.19(a)(2) would not conflict with tolerance and timing rules under Regulation X—that is, creditors could comply with both Regulation Z and Regulation X. However, the Board's proposal would require creditors to finalize settlement costs earlier than RESPA does: At least three business days before consummation, and as much as a week before consummation if the creditor mails the disclosures to the consumer.[41] The Board recognizes that requiring that loan terms and costs be finalized several days before consummation would require significant changes to current settlement practices. These changes would generate costs that creditors and third-party service providers would pass on to consumers. The Board solicits comment on the operational and other practical effects of requiring that consumers receive final TILA disclosures for closed-end loans secured by real property or a dwelling no later than three business days before consummation.

Proposed comment 19(a)(2)(ii)–1 provides that creditors must provide final disclosures even if the terms disclosed have not changed since the creditor provided the early disclosures. Proposed comment 19(a)(2)(ii)–2 provides that disclosures made under § 226.19(a)(2)(ii) must contain each of the applicable disclosures required by § 226.38.

If escrows for taxes and insurance will be required, creditors may disclose periodic payments of taxes and insurance as estimates under § 226.38(c). If the creditor includes escrowed amounts when calculating the total of payments under § 226.38(e)(5)(i), then the total of payments also would be disclosed as estimated disclosures, as discussed in comment 38(e)(5)–1. Periodic payment disclosures that include escrowed amounts must be estimated disclosures because the creditor cannot know with certainty the amounts for property taxes and insurance after the first year of the loan. Proposed comment 19(a)(2)(ii)–3 clarifies that other disclosures may not be estimated under proposed § 226.19(a)(2)(ii). Finally, comment 19(a)(2)(ii)–4 provides an example that illustrates when consummation may occur after the consumer receives the final disclosures.

19(a)(2)(iii) Additional Three-Business-Day Waiting Period

The Board is proposing two alternative requirements for creditors to provide corrected disclosures after making the final disclosures required by § 226.19(a)(2)(ii), to be designated as § 226.19(a)(2)(iii). Consumers would have to receive the corrected disclosures required by proposed § 226.19(a)(2)(iii) no later than the third business day before consummation. Under both Alternative 1 and Alternative 2, comment 19(a)(2)–2 would be revised to reflect that there is more than one three-business-day waiting period under § 226.19(a).

Alternative 1. The first alternative would require that a creditor provide corrected disclosures if any terms stated in the final disclosures required by proposed § 226.19(a)(2)(ii) change. This would ensure that consumers are aware of the final loan terms and costs at least three business days before consummation. The consumer would have to receive the corrected disclosures no later than the third business day before consummation.

Under Alternative 1, proposed comment 19(a)(2)(iii)–1 clarifies that a disclosed APR is accurate for purposes of § 226.19(a)(2)(iii) if the disclosure is accurate under proposed § 226.19(a)(2)(iv). (Under proposed § 226.19(a)(2)(iv), an APR disclosed under proposed § 226.19(a)(2)(ii) or (iii) is considered accurate as provided by § 226.22, except that in certain circumstances the APR is considered accurate if the APR decreases from the APR disclosed previously, as discussed below.) Proposed comment 19(a)(2)(iii)–2 states that disclosures made under § 226.19(a)(2)(ii) must contain each of the disclosures required by § 226.38. Proposed comment 19(a)(2)(iii)–3 clarifies that creditors may rely on proposed comment 19(a)(2)(ii)–3 in determining which of the disclosures required by § 226.19(a)(2)(iii) may be estimated disclosures. Proposed comment 19(a)(2)(iii)–4 provides an example that shows when consummation may occur after the consumer receives corrected disclosures. Existing comments 19(a)(2)(ii)–1 through –4 would be removed under Alternative 1.

Alternative 2. It is not clear that it is always in a consumer's interest to delay consummation until three business days after the consumer receives corrected disclosures if any terms or costs change. Thus, the Board proposes an alternative § 226.19(a)(2)(iii) that incorporates the existing tolerance for APR changes under § 226.22 and incorporates an additional tolerance discussed under § 226.19(a)(iv). If the APR changes beyond the specified tolerances, creditors would be required to provide corrected disclosures that the consumer must receive no later than three business days before consummation.

Under the second alternative, after the creditor provides the final disclosures, only APR changes beyond the specified tolerances or the addition of a variable-rate feature to the loan would trigger a requirement that consumers receive corrected disclosures no later than three business days before consummation. In other cases, the creditor would have to disclose changed terms no later than the day of consummation, under existing § 226.17(f). Under this alternative, a consumer would be alerted to significant increases in loan costs and would have three business days to investigate the reason for the change or to consider other options. Smaller APR increases or other changes to loan terms would not trigger a three-day delay in consummation, however. This alternative is designed to prevent

[41] Under existing and proposed § 226.19(a)(2), a consumer is deemed to receive corrected disclosures three business days after a creditor mails them. Under existing and proposed § 226.19(a)(2), creditors may but need not rely on the presumption of receipt to determine when the three-business-day waiting period begins, whether creditors mail TILA disclosures using the postal service, use a courier other than the postal service, or provide disclosures electronically. Alternatively, creditors may rely on evidence of receipt. 74 FR at 23293; 73 FR 44522, 44593; July 30, 2008.

relatively minor changes in loan terms from repeatedly delaying consummation.

Under Alternative 2, comment 19(a)(2)(ii)–1 would be redesignated as comment 19(a)(2)(iii)–1 and revised to clarify that creditors must provide corrected disclosures if the APR disclosed pursuant to § 226.19(a)(ii) becomes inaccurate under proposed § 226.19(a)(2)(iv), which incorporates existing tolerances under § 226.22, or an adjustable-rate feature is added. Comment 19(a)(2)(ii)–2 would be redesignated as comment 19(a)(2)(iii)–2 and revised to: (1) Reflect that corrected disclosures must comply with the format requirements of proposed § 226.37 as well as those of § 226.17(a); (2) reflect that a different APR will almost always result in changes in ''interest and settlement charges'' and the ''payment summary'' (currently designated as the finance charge and payment schedule, respectively); (3) clarify that the addition of an adjustable-rate feature triggers the requirement to provide corrected disclosures, by moving a cross-reference to comment 17(f)–2; and (4) remove guidance on the timing and conditions of new disclosures from guidance on disclosure content, for clarity. Proposed comment 19(a)(2)(iii)–3 clarifies that creditors may rely on proposed comment 19(a)(2)(ii)–3 in determining which of the disclosures required by § 226.19(a)(2)(iii) creditors may estimate. Under the proposed rule, comment 19(a)(2)(iii)–4 would be revised to update a cross-reference consistent with the proposed rule and reflect that consumers must receive disclosures under § 226.19(a)(2)(ii) whether or not the disclosures correct the early disclosures.

The Board solicits comment on whether, under Alternative 2, changes other than APR changes in excess of the specified tolerance or the addition of an adjustable-rate feature after the creditor makes the new disclosures should trigger an additional three-business-day waiting period. For example, should the addition of a prepayment penalty, negative amortization, interest-only, or balloon payment feature trigger a waiting period requirement?

Proposed § 226.19(a)(2)(iii) (under Alternative 2) would require corrected disclosures and a new three-business-day waiting period if the previously disclosed APR has become inaccurate. Under current rules, a disclosed APR is considered accurate and does not trigger corrected disclosures if it results from a disclosed finance charge that is greater than the finance charge required to be disclosed (*i.e.,* the finance charge is ''overstated''). *See* §§ 226.22(a)(4) and 226.18(d)(1)(ii). In some transactions, the finance charge at consummation might be lower than the amount previously disclosed, for example, if the parties agree to a smaller principal loan amount after early disclosures were made. In the same transaction, the APR might increase because of an increase in the interest rate after the early disclosures were made. In this transaction, at consummation the previously disclosed finance charge would be overstated and the previously disclosed APR understated. In such a case, the question has been raised as to whether the previously disclosed APR, which was derived from the overstated finance charge, should be deemed accurate even though it is understated at consummation. The Board believes the APR in this case is not accurate. The Board believes an APR ''results from'' an overstated finance charge only if the APR also is overstated. The Board solicits comment on whether, should Alternative 2 be adopted, the Board also should adopt commentary under § 226.22(a)(4) to clarify this interpretation.

Proposed § 226.19(a)(2)(iv) contains APR tolerances, and proposed § 226.38(e)(5)(ii) contains tolerances for interest and settlement charges (as the finance charge would be referred to under the proposed rule), for transactions secured by real property or a dwelling. The Board solicits comment on whether, under § 226.38(e)(5)(ii), tolerances would be appropriate for numerical disclosures other than the APR and interest and settlement charges. For example, would dollar tolerances for overstatements of periodic payment disclosures required by § 226.38(c) be appropriate? What standards should be used to prevent overstated disclosures from undermining the integrity of the early disclosures and their usefulness as a shopping tool?

19(a)(2)(iv) Annual Percentage Rate Accuracy

Under proposed § 226.19(a)(2)(iv), an APR disclosed under proposed § 226.19(a)(2)(ii) or (iii) is considered accurate as provided by § 226.22, except that the APR also is considered accurate if the APR decreases due to a discount (1) the creditor gives the consumer to induce periodic payments by automated debit from a consumer's deposit account or (2) the title insurer gives the consumer on owner's title insurance. Thus, such APR changes would not trigger a new three-business-day waiting period. Comment 19(a)(2)(iv)–1 clarifies that if a change occurs that does not render the APR inaccurate under § 226.19(a)(iv), the creditor must disclose the changed terms before consummation, consistent with § 226.17(f). The Board solicits comment on whether a disclosed APR that is higher than the actual APR at consummation should be considered accurate in other circumstances.

19(a)(2)(v) Timing of Receipt

As adopted by the MDIA Final Rule, § 226.19(a)(2)(ii) provides that consumers must receive corrected disclosures, if required, no later than three business days before consummation. Further, § 226.19(a)(2)(ii) provides that if the corrected disclosures are mailed to the consumer or delivered to the consumer by means other than delivery in person, the consumer is deemed to have received the disclosures three business days after they are mailed or delivered. The proposed rule applies this presumption for purposes of both the waiting period under proposed § 226.19(a)(2)(ii) and the waiting period under proposed § 226.19(a)(2)(iii). The presumption would be moved to § 226.19(a)(2)(v) under the proposed rule.

Proposed comment 19(a)(2)(v)–1 states that whether the creditor provides disclosures by delivery, postal service, electronic mail, or courier other than the postal service, consumers are deemed to receive the disclosures three business days after the creditor so provides them, for purposes of determining when a three-business-day waiting period required by § 226.19(a)(2)(ii) or (iii) begins. Further, proposed comment 19(a)(2)(v)–1 clarifies that creditors may rely on evidence of earlier receipt, regardless of how the creditor provides disclosures to the consumer. This commentary is consistent with the Board's discussion of delivery and mailing under the MDIA Final Rule and the 2008 HOEPA Final Rule. *See* 74 FR at 23292–23293; 73 FR at 44593.

19(a)(3) Consumer's Waiver of Waiting Period

Section 226.19(a)(3) and comment 19(a)(3)–1 would be revised to reflect that under the proposed rule the disclosures required for transactions secured by real property or a dwelling are contained in § 226.38 rather than in § 226.18. Section 226.19(a)(3) also would be revised to reflect that there is more than one three-business-day waiting period under proposed § 226.19(a)(2); comment 19(a)(3)–1 would be revised to clarify that a separate waiver is required for each waiting period to be waived.

Section 226.19(a)(2)(ii) currently requires creditors to provide corrected disclosures to a consumer if changes to the disclosed APR exceed the specified tolerance (APR correction disclosures). The consumer must receive APR correction disclosures no later than three business days before consummation. Comment 19(a)(3)–2 provides examples that show whether or not the three-business-day waiting period would need to be waived to allow consummation to occur during the seven-business-day waiting period required by § 226.19(a)(2)(i), in the event of a *bona fide* personal financial emergency. This example would be removed because proposed § 226.19(a)(2)(ii) provides that, after the creditor provides the early disclosures, consumers must receive final disclosures no later than three business days before consummation in all cases. Comment 19(a)(3)–3 provides examples illustrating whether or not, after the seven-business-day waiting period required by § 226.19(a)(2)(i), the three-business-day waiting period triggered by APR correction disclosures would need to be waived to allow consummation to occur, in the event of a *bona fide* personal financial emergency. Comment 19(a)(3)–3 would be revised to reflect that in all cases consumers would have to receive final disclosures after the creditor provides the early disclosures under the proposed rule and that under proposed § 226.19(a)(2)(iv) a disclosed APR that is overstated is considered accurate in specified circumstances. Comment 19(a)(3)–3 would be redesignated as comment 19(a)(3)–2 under the proposed rule.

19(a)(4) Notice

Section 226.19(a)(4) currently requires creditors to disclose that a consumer need not enter into a loan agreement because the consumer has received disclosures or signed a loan application. This requirement would be moved to § 226.38(f)(1) under the proposed rule. Proposed § 226.38 contains all content requirements for disclosures for transactions secured by real property or a dwelling.

19(a)(5) Timeshare Transactions

Section 226.19(a)(5) excludes transactions secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53(D)) (timeshare transactions) from § 226.19(a)(1) through (a)(4), which address the following: (1) The period within which the creditor must provide the early disclosures and the fact that creditors and other persons cannot collect fees from the consumer before the consumer receives the early disclosures; (2) waiting periods after the creditor provides the early disclosures and after the consumer receives corrected disclosures (if any) and before consummation; (3) waiver of waiting periods; and (4) the requirement to disclose a statement that the consumer is not required to consummate a transaction merely because the consumer has received disclosures or signed a loan application.

Section 226.19(a)(5)(ii) contains timing requirements for early disclosures, and § 226.19(a)(5)(iii) contains timing requirements for corrected disclosures, for timeshare transactions. Waiting periods are not required for timeshare transactions, so § 226.19(a)(5) does not contain requirements similar to the requirements in § 226.19(a)(3) for waiving waiting periods for non-timeshare transactions. Section 226.19(a)(5) also does not contain a requirement similar to that in § 226.19(a)(4) that disclosures contain a statement that a consumer need not consummate a transaction simply because the consumer receives disclosures or signs a loan application. Section 226.19(a)(4) would be removed under the proposed rule, and a substantially similar requirement would apply under proposed § 226.38(f)(1). Proposed § 226.38(f)(1) requires creditors to disclose a statement that a consumer is not obligated to consummate a loan and that the consumer's signature only confirms receipt of a disclosure statement.

Proposed § 226.38(f)(1) applies to timeshare transactions. The MDIA exempts timeshare transactions from the requirements of TILA Section 128(b)(2)(C), which existing § 226.19(a)(4) implements. However, the Board does not believe that the Congress intended to exempt timeshare transactions from any requirement to disclose to a consumer that the consumer is not obligated to consummate a loan. Thus, the proposed rule does not exempt timeshare transactions from § 226.38(f)(1).

Section 226.19(a)(5) would be redesignated as § 226.19(a)(4) and cross-references adjusted accordingly under the proposed rule because § 226.19(a)(4) would be removed, as discussed above. Comment 19(a)(5)(ii)–1 would be revised to reflect that the coverage of § 226.19 has been expanded to include transactions not subject to RESPA, as discussed above. Comment 19(a)(5)(iii)–1 would be revised to clarify that timeshare transactions are subject to the general requirement to disclose changed terms under § 226.17(f). Further, comment 19(a)(5)(iii)–1 would be revised to reflect that cross-referenced commentary on variable- or adjustable-rate transactions would be incorporated into proposed § 226.17(c)(1)(iii). Finally, commentary on § 226.19(a)(5)(ii) and (iii) would be redesignated as commentary on § 226.19(a)(4)(ii) and (iii), respectively.

19(b) Adjustable-Rate Loan Program Disclosures

Section 226.19(b) currently requires creditors to provide detailed disclosures about adjustable-rate loan programs and a CHARM booklet if a consumer expresses an interest in ARMs. Section 226.19(b) applies to closed-end transactions secured by a consumer's principal dwelling with a term greater than one year. Creditors must provide these disclosures at the time an application form is provided or before the consumer pays a non-refundable fee, whichever is earlier. Creditors need not provide these disclosures, however, if a loan is secured by a dwelling other than a principal dwelling (such as a second home) or real property that is not a dwelling (such as vacant land) or with a term of one year or less. For such transactions, creditors instead must provide the less detailed variable-rate disclosures required by § 226.18(f)(1) within three business days after receiving the consumer's application, as discussed above.

The Board proposes to require creditors to provide ARM loan program disclosures, and additional disclosures discussed below, at the time an application form is provided, for all closed-end transactions secured by real property or a dwelling, regardless of the length of the loan's term. The ARM disclosures and the new disclosures are intended to alert consumers to certain risks before they apply for a loan. The Board believes that consumers should receive this information, even where the loan would be secured by a second home or unimproved real property, and where the loan term is one year or less. In these circumstances, the transaction likely involves a significant asset and consumers should receive information about risks, so that they can decide whether the program or loan feature is appropriate. The Board solicits comment on whether loan program disclosures should be given at the time an application form is provided to a consumer or before the consumer pays a non-refundable fee, whichever is earlier, for transactions other than ARMs.

The Board proposes to require creditors to provide the following disclosures at the time an application is provided:

- The ARM loan program disclosure, for each program in which the consumer expresses an interest (proposed § 226.19(b));
- The ''Key Questions about Risk'' document published by the Board (proposed § 226.19(c)); and
- The ''Fixed vs. Adjustable-Rate Mortgages'' document published by the Board (proposed § 226.19(c)).

Creditors no longer would be required to provide the CHARM booklet, as discussed under § 226.19(c).

Current content of ARM loan program disclosures. For adjustable-rate mortgage transactions secured by a consumer's principal dwelling with a term greater than one year, § 226.19(b)(2) requires the creditor to provide disclosures to consumers at the time an application form is provided or before the consumer pays a nonrefundable fee, whichever is earlier. Section 226.19(b)(2) requires creditors to provide the following disclosures, as applicable, for each adjustable-rate loan program in which the consumer expresses an interest: (1) The fact that interest rate, payment, or term of the loan can change, (2) the index or formula used in making adjustments, and a source of information about the index or formula, (3) an explanation of how the interest rate and payment will be determined, including an explanation of how the index is adjusted, such as by the addition of a margin, (4) a statement that the consumer should ask about the current margin value and current interest rate, (5) the fact that the interest rate will be discounted, and a statement that the consumer should ask about the amount of the interest rate discount, (6) the frequency of interest rate and payment changes, (7) any rules relating to changes in the index, interest rate, payment amount, and outstanding loan balance, (8) pursuant to TILA Section 128(a)(14), 15 U.S.C. 1638(a)(14), either (a) an historical example based on a $10,000 loan amount that illustrates how interest rate changes implemented according to the terms of the loan program would have affected payments and the loan balance over the past fifteen years or (b) the maximum interest rate and payment for a $10,000 loan originated at an initial interest rate in effect as of an identified month and year and a statement that the periodic payments may increase or decrease substantially, (9) an explanation of how the consumer may calculate the payments for the loan, (10) the fact that the loan program contains a demand feature, (11) the type of information that will be provided in notices of adjustments and the timing of such notices, and (12) a statement that the disclosure forms are available for the creditor's other variable-rate loan programs.

Amendments to maximum rate and historical example disclosures. TILA Section 128(a)(14), 15 U.S.C. 1638(a)(14), requires creditors to disclose at application (a) a statement that the periodic payments may increase or decrease substantially and the maximum interest rate and payment for a $10,000 loan originated at a recent interest rate, assuming the maximum periodic increases in rates and payments under the program or (b) an historical example illustrating the effects of interest rate changes implemented according to the loan program. Section 226.19(b)(2)(viii) implements TILA Section 128(a)(14). For the reasons discussed below, the Board proposes not to require creditors to provide either the historical example or the maximum interest rate and payment based on a $10,000 loan.

The Board proposes to eliminate the disclosure of the historical example or the maximum interest rate and payment based on a $10,000 loan pursuant to the Board's exception and exemption authorities in TILA Section 105. Section 105(a) authorizes the Board to make exceptions to TILA to effectuate the statute's purposes, which include facilitating consumers' ability to compare credit terms and helping consumers avoid the uniformed use of credit. *See* 15 U.S.C. 1601(a), 1604(a). Section 105(f) authorizes the Board to exempt any class of transactions from coverage under any part of TILA if the Board determines that coverage under that part does not provide a meaningful benefit to consumers in the form of useful information or protection. *See* 15 U.S.C. 1604(f)(1). The Board must make this determination in light of specific factors. *See* 15 U.S.C. 1604(f)(2). These factors are (1) the amount of the loan and whether the disclosure provides a benefit to consumers who are parties to the transaction involving a loan of such amount; (2) the extent to which the requirement complicates, hinders, or makes more expensive the credit process; (3) the status of the borrower, including any related financial arrangements of the borrower, the financial sophistication of the borrower relative to the type of transaction, and the importance to the borrower of the credit, related supporting property, and coverage under TILA; (4) whether the loan is secured by the principal residence of the borrower; and (5) whether the exemption would undermine the goal of consumer protection.

The Board has considered each of these factors carefully and based on that review believes that the proposed exemption is appropriate. Consumer testing conducted by the Board showed that examples based on hypothetical loan amounts and interest rates may be confusing to consumers and may not provide meaningful benefit. Several participants thought the historical example showed payments and rates that actually would apply if the participant chose the loan program described in the disclosure. Some participants mistakenly thought that the disclosures described an ARM with a fifteen-year term because the disclosure showed fifteen years' worth of index changes under an ARM program. Some consumer testing participants said that disclosures based on a hypothetical $10,000 loan amount are not useful to them; these consumers said they wanted to see information about rates and terms that would actually apply in the context of their own loan amount.

The Board's exception and exemption authority under Sections 105(a) and (f) does not apply in the case of a mortgage referred to in Section 103(aa), which are high-cost mortgages generally referred to as ''HOEPA loans.'' The Board does not believe that this limitation restricts its ability to apply the proposed changes to all mortgage loans, including HOEPA loans. This limitation on the Board's general exception and exemption authority is a necessary corollary to the decision of the Congress, as reflected in TILA Section 129(*l*)(1), to grant the Board more limited authority to exempt HOEPA loans from the prohibitions applicable only to HOEPA loans in Section 129(c) through (i) of TILA. *See* 15 U.S.C. 1639(*l*)(1). Here, the Board is not proposing any exemptions from the HOEPA prohibitions. This limitation does raise a question as to whether the Board could use its exception and exemption authority under Sections 105(a) and (f) to except or exempt HOEPA loans, but not other types of mortgage loans, from other, generally applicable TILA provisions. That question, however, is not implicated by this proposal.

Here, the Board is proposing to apply its general exception and exemption authority to eliminate information from the ARM loan program disclosure that consumers find confusing or not useful, for all loans secured by real property or a dwelling, including both HOEPA and non-HOEPA loans, in order to fulfill the statute's purpose of facilitating consumers' ability to compare credit terms and helping consumers avoid the uninformed use of credit. It would not be consistent with the statute or with

Congressional intent to interpret the Board's authority under Sections 105(a) and (f) in such a way that the proposed revisions could apply only to mortgage loans that are not subject to HOEPA. Reading the statute in a way that would deprive HOEPA borrowers of improved ARM loan program disclosures is not a reasonable construction of the statute and contravenes the Congress's goal of ensuring ''that enhanced protections are provided to consumers who are most vulnerable to abuse.'' [42]

The Board notes that proposed § 226.38(c) would require creditors to provide consumers with the maximum possible interest rate and payment within three business days after the consumer applies for an ARM or a loan in which payments may vary. *See* discussion of § 226.38(c). Consumer testing indicated that consumers find this information very useful when provided in the context of an actual loan offer, in contrast to the information for a hypothetical loan amount in relation to an historical interest rate or the interest rate or for a recently originated loan, as required by TILA Section 128(a)(14).

In addition to removing § 226.19(b)(2)(viii), the proposed rule would remove the related requirement under § 226.19(b)(2)(ix) that creditors explain how a consumer may calculate payments for the consumer's loan amount based on either the initial interest rate used to calculate the maximum interest rate and payment disclosure or the most recent payment shown in the historical example. The proposed rule also would eliminate commentary on § 226.19(b)(2)(viii) and (ix). Further, the proposed rule would eliminate comment 19(b)(2)–2(i)(I), which provides that if a loan feature must be taken into account in preparing the historical example of payment and loan balance movements required by § 226.19(b)(2)(viii), variable-rate loans that differ as to that feature constitute separate loan programs under § 226.19(b)(2).

Amendments to other regulations and comments. Comment 19(b)–1 currently provides that in an assumption of an adjustable-rate mortgage transaction secured by the consumer's principal dwelling with a term greater than one year, disclosures need not be provided under §§ 226.18(f)(2)(ii) or 226.19(b). Comment 19(b)–2(iv) currently provides that in cases where an open-end credit account will convert to a closed-end transaction subject to § 226.19(b), the creditor must provide the disclosures required by § 226.19(b). The proposed rule would integrate the foregoing commentary into § 226.19(b). Proposed § 226.19(b) would apply to all closed-end mortgage transactions secured by real property or a dwelling regardless of loan security or term, however, as discussed above.

The proposed rule would not require program disclosures to contain an explanation of how payments will be determined, a disclosure that creditors must make under existing § 226.19(b)(2)(iii). In general, consumer testing participants preferred to receive specific information about the amount of the payments they would have to make, which generally is not available at the time the consumer submits a loan application. Most participants found model loan program disclosures based on current requirements to be confusing because they contained complex terminology. Participants responded much more positively to revised model disclosures, which did not discuss technical issues about how payments are determined. If a creditor chooses to include an explanation of how payments will be determined, the explanation must be disclosed apart from the segregated disclosures that proposed § 226.19(b) requires, as a general rule under proposed § 226.37(a)(2), discussed below.

Footnote 45a to § 226.19(b) currently states that creditors may substitute information provided in accordance with variable-rate regulations of other federal agencies for the disclosures required by § 226.19(b). The proposed rule would remove and reserve that footnote and comment 19(b)–4. The footnote was designed to account for the fact that disclosure rules for variable-rate loans issued by HUD, the Federal Home Loan Bank Board, and the Office of the Comptroller of the Currency (OCC) were in effect when the Board adopted § 226.19(b). No comprehensive disclosure requirements for variable-rate loans currently are in effect under the rules of HUD, the OCC, or the Office of Thrift Supervision (OTS), the successor agency to the FHLBB. No such requirements are in effect under the rules of the Federal Deposit Insurance Corporation (FDIC) or the National Credit Union Administration (NCUA) either. Moreover, HUD and the OTS have incorporated the disclosure requirements for variable-rate loans under TILA and Regulation Z into their own regulations by cross-reference.[43] Accordingly, footnote 45a no longer appears to be necessary. The Board requests comment, however, on whether there are potential inconsistencies between any ARM loan disclosures required by other federal financial institution supervisory agencies that Regulation Z should specifically address.

Comment 19(b)–5 currently states that creditors must provide disclosures under § 226.19(b) for certain renewable balloon-payment, preferred-rate, and price-level adjusted mortgages with a fixed interest rate, if they are secured by a dwelling and have a term greater than one year. However, such mortgages lack most of the adjustable interest rate and payment features required to be disclosed under proposed § 226.19(b)(1). For example, the frequency of rate and payment changes for a preferred-rate loan with a fixed interest rate likely cannot be known because the loss of the preferred rate is based on factors other than a formula or a change in the value of an index. Accordingly, under the proposed rule creditors would not be required to provide ARM loan program disclosures under § 226.19(b) for such mortgages. Creditors would be required to provide ARM loan program disclosures for such mortgages if their interest rate is adjustable, however. Cross-references in comment 19(b)–5 would be updated and the comment would be redesignated as comment 19(b)–3 under the proposed rule.

Existing comment 19(b)(2)–2(i) provides examples of particular loan features that distinguish separate loan programs. That commentary would be redesignated as comment 19(b)–5(i) but generally would be unchanged under the proposal, with one exception. Differences among rules relating to loan balance changes would be removed as an example of a particular loan feature that distinguishes separate loan programs. However, differences in the possibility of negative amortization would continue to distinguish separate loan programs, as discussed above. Also, existing comment 19(b)(2)(vii)–2(i) on disclosing a negative amortization feature would be redesignated as comment 19(b)–5 under the proposal.

The requirement to provide loan program disclosures for each loan program in which a consumer expresses an interest generally would remain unchanged. However, comment 19(b)(2)–4 would be revised to state that a creditor ''must describe''—rather than

[42] H.R. Conf. Rept. 103–652 at 159 (Aug. 2, 1994).

[43] *See* 24 CFR 203.49(g) (HUD); 12 CFR 560.210 (OTS). Some of those agencies have issued regulations that apply to adjustable rate mortgages. *See, e.g.,* 12 CFR 34.22 (OCC) (requiring that an index specified in a national bank's loan documents for an ARM subject to § 226.19(b) be readily available to and verifiable by a borrower and beyond the bank's control). Those requirements do not establish comprehensive disclosure requirements, however.

''must fully describe''—an ARM loan program. The proposal would reduce some of the material that creditors must disclose about ARM loan programs to highlight information that is most important to consumers, as discussed above.

Use of term ''Adjustable-Rate Mortgage'' or ''ARM.'' Proposed § 226.19(b) requires the creditor to disclose the heading ''Adjustable-Rate Mortgage'' or ''ARM.'' Participants in the Board's consumer testing showed greater familiarity with the term ''adjustable-rate mortgage'' than with ''variable-rate mortgage.'' Format requirements in proposed § 226.19(b)(4)(iii) state that the statement must be more conspicuous than, and must precede, the other disclosures required by § 226.19(b) and must be located outside of the tables required by proposed § 226.19(b)(4)(iv). Finally, proposed § 226.19(b)(4)(iii) states that creditors may make the ''Adjustable-Rate Mortgage'' or ''ARM'' disclosure in a heading that states the name of the creditor and the name of the loan program, such as ''ABC Bank 3/1 Adjustable Rate Mortgage.''

19(b)(1) Interest Rate and Payment Disclosures

Proposed § 226.19(b)(1) requires the creditor to disclose the following information, as applicable, grouped together under the heading ''Interest Rate and Payment,'' using that term: (1) The introductory period, (2) the frequency of the rate and payment change, (3) the index, (4) the limit on rate changes, (5) the conversion feature, and (6) the preferred rate.

Introductory period. Proposed § 226.19(b)(1)(i) requires the creditor to disclose the period during which the interest rate or payment remains fixed and a statement that the interest rate may vary or the payment may increase after that period. This disclosure is similar to that required under existing § 226.19(b)(2)(i). Proposed § 226.19(b)(1)(i) also requires the creditor to provide an explanation of the effect on the interest rate of having an initial interest rate that is not determined using the index or formula that applies for interest rate adjustments, that is, of having a discounted or premium interest rate. This disclosure requirement is similar to that required under existing § 226.19(b)(2)(v). However, the proposed rule would eliminate the requirement that ARM loan program disclosures state that the consumer should ask about the amount of the interest rate discount.

Frequency of rate and payment change. Proposed § 226.19(b)(1)(ii) requires the creditor to disclose the frequency of interest rate and payment changes, as currently is required under § 226.19(b)(2)(vi).

Index. Proposed § 226.19(b)(1)(iii) requires the creditor to disclose the index or formula used in making adjustments and a source of information about the index or formula. Proposed § 226.19(b)(1)(iii) also requires the creditor to provide an explanation of how the interest rate will be determined, including an explanation of how the index is adjusted, such as by the addition of a margin. Those requirements are contained in existing § 226.19(b)(2)(ii) and (iii). However, the proposed rule eliminates § 226.19(b)(2)(iv), which requires the creditor to disclose that the consumer should ask about the current margin value and current interest rate.

Limit on rate changes. Currently, requirements for disclosing interest rate or payment limitations and carryover are contained in existing § 226.19(b)(2)(vii). The proposed rule would retain these requirements, under proposed § 226.19(b)(1)(iv). (Existing § 226.19(b)(2)(vii) also contains a requirement to disclose negative amortization. The proposed rule would retain that requirement as proposed § 226.19(b)(2)(ii)(B), as discussed below.)

Conversion feature. Existing comment 19(b)(2)(vii)–3 provides that if a loan program permits consumers to convert a variable-rate loan to a fixed-rate loan, the creditor must disclose that the fixed interest rate after conversion may be higher than the adjustable interest rate before conversion. Comment 19(b)(2)(vii)–3 further provides that the creditor must disclose any limitations on the period during which the loan may be converted, a statement that conversion fees may be charged, and any interest rate and payment limitations that apply if the consumer exercises the conversion option. The proposed rule would integrate this commentary into proposed § 226.19(b)(1)(v).

Preferred rate. Currently, if the variable-rate mortgage transaction is a preferred-rate loan, the creditor must disclose any event that would allow the creditor to increase the interest rate, for example, upon the termination of the consumer's employment with the creditor, whether voluntary or involuntary. *See* comment 19(b)(2)(vii)–4. The creditor also must disclose that fees may be charged when the preferred rate no longer is in effect, if applicable. The Board proposes to retain these requirements in proposed § 226.19(b)(1)(vi).

19(b)(2) Key Questions About Risk

Currently, TILA Section 128(a)(14), 15 U.S.C. 1638(a)(14), and § 226.19(b)(2), require the creditor to disclose only certain information about certain adjustable-rate mortgage features early in the mortgage application process. The Board believes, however, that the consumer should be aware early in the process of other risky features, in addition to adjustable-rate features. For this reason, the Board proposes to require ''Key Question'' disclosures several times during the process to allow consumers to become aware of and track potentially risky features of their loan. Consumer testing and document design principles suggest that keeping language and design elements consistent between forms improves consumers' ability to identify and track any changes in the information being disclosed. As discussed more fully below, proposed § 226.19(c)(1) would require the creditor to provide a Board publication entitled ''*Key Questions to Ask about Your Mortgage*'' at the time an application form is provided to the consumer or before the consumer pays a non-refundable fee, whichever is earlier. The content of this disclosure would be published by the Board and would address important terms related to any type of mortgage, whether fixed-rate or adjustable-rate. At the same time, if the consumer expresses an interest in an ARM loan program, proposed § 226.19(b)(2) would require the creditor to disclose the ''Key Questions about Risk'' as part of the ARM loan program disclosure. These ''Key Questions'' would be tailored to the specific ARM loan program in which the consumer has expressed an interest. Subsequently, within three days of the creditor receiving the consumer's application for a specific loan program, proposed § 226.38(d) would require the creditor to make a similar disclosure of ''Key Questions about Risk'' in the transaction-specific TILA disclosure. The list of the ''Key Questions about Risk'' for the transaction-specific TILA disclosure required under proposed § 226.38(d) would be the same as that required for the ARM loan program disclosure under proposed § 226.19(b)(2), but the information in the TILA disclosure would be specific to the loan program for which the consumer applied and would apply to fixed-rate or adjustable-rate loan programs. The Board believes that consistently using the ''Key Questions'' terminology would enhance consumers' ability to identify, review, and understand the disclosed terms across all disclosures, and, therefore, avoid the uninformed use of credit.

Key questions about risk. As discussed above, current § 226.19(b)(2) requires the creditor to disclose over 12 loan features. Consumer testing showed that the current format for these disclosures was very difficult for participants to understand. In addition, because the content was so general, participants felt the current disclosure would not help them shop for a mortgage. Therefore, the Board proposes to replace existing § 226.19(b)(2) with a new streamlined ARM loan program disclosure that would contain key information specific to that loan program. The proposed rule would require creditors to disclose certain information grouped together under the heading ''Key Questions about Risk,'' using that term, to draw the consumer's attention to information about the potential adverse impact that certain loan features could have on the consumer's ability to repay the loan. Proposed § 226.19(b)(2)(i) requires the creditor to always disclose information about the following three terms: (1) Rate increases, (2) payment increases, and (3) prepayment penalties. Proposed § 226.19(b)(2)(ii) would require the creditor to disclose information about the following six terms, but only if they are applicable to the loan program: (1) Interest-only payments, (2) negative amortization, (3) balloon payment, (4) demand feature, (5) no-documentation or low-documentation loans, and (6) shared-equity or shared-appreciation. The ''Key Questions about Risk'' disclosure would be subject to special format requirements, including a tabular format and a question and answer format, as described under proposed § 226.19(b)(4). The Board believes it is critical that consumers be alerted to certain risk factors before they have applied for an ARM, so that they can decide whether they want a loan with those terms. The Board solicits comment on whether there are other risk factors that loan program disclosures or publications should identify.

Required disclosures. As noted above, proposed § 226.19(b)(2)(i) requires the creditor to disclose information about the following three terms: (1) Rate increases, (2) payment increases, and (3) prepayment penalties. The Board believes that these three factors should always be disclosed. Rate and payment increases pose the most direct risk of payment shock. In addition, consumer testing showed that interest rate and monthly payment were by far the two most common terms that participants used to shop for a mortgage. The Board also believes that the prepayment penalty is a key risk factor because it is critical to the consumer's ability sell the home or to refinance the loan to obtain a lower rate and payments. While the other risk factors are important, those factors are only required to be disclosed as applicable to avoid information overload.

Rate and payment increases. With respect to rate increases, proposed § 226.19(b)(2)(i)(A) would require the creditor to disclose a statement that the interest rate on the loan may increase, along with a statement indicating when the first rate increase may occur and the frequency with which the interest rate may increase. With respect to payment increases, proposed § 226.19(b)(2)(i)(B) would require the creditor to disclose a statement indicating whether or not the periodic payment on the loan may increase. If the periodic payment on the loan may increase, then the creditor would disclose a statement indicating when the first payment may increase. For payment option loans, if the periodic payment may increase, the creditor would disclose a statement indicating when the first *minimum* payment would increase. Proposed comment 19(b)(2)(i)–1 would clarify that the requirement to disclose when the first rate or payment increase may occur refers to the time period in which the increase may occur, not the exact calendar date. For example, the disclosure may state, ''Your interest rate may increase at the end of the 3-year introductory period.''

Prepayment penalties. If the obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance, proposed § 226.19(b)(2)(i)(C) would require the creditor to disclose a statement indicating whether or not a penalty could be imposed if the obligation is prepaid in full. If the creditor could impose a prepayment penalty, the creditor would disclose the circumstances under which and the period in which the creditor could impose the penalty. Because of the importance of prepayment penalties, the proposed rule would also require disclosure of this feature under proposed § 226.38(a)(5). To avoid duplication, proposed comments 19(b)(2)(i)(C)–1 to –3 cross-reference proposed comments 38(a)(5)–1 to –3 for information about whether there is a prepayment penalty and examples of charges that are or are not prepayment penalties.

Some consumers take out ARM loans planning to refinance or sell the home securing the loan before the rate or payment increases. Consumer testing showed that while most participants understood the general meaning of the phrase ''prepayment penalty,'' they did not realize that the penalty would apply if they refinanced their loan or sold their home. The Board believes it is important for consumers to understand that a prepayment penalty may be imposed in various circumstances, including paying off the loan, refinancing, or selling the home early.

Additional disclosures. As noted above, proposed § 226.19(b)(2)(ii) requires the creditor to disclose information about the following six terms, as applicable: (1) Interest-only payments, (2) negative amortization, (3) balloon payment, (4) demand feature, (5) no-documentation or low-documentation loans, and (6) shared-equity or shared-appreciation. The Board proposes to require these disclosures only when the feature is present, in contrast to the required disclosures of proposed § 226.19(b)(2)(i). Proposed comment 19(b)(2)(ii)–1 would clarify that ''as applicable'' means that any disclosure not relevant to a particular ARM loan program may be omitted. Although consumer testing showed that some participants felt reassured by seeing all of the risk factors whether they were a feature of the loan or not, the Board is concerned about the potential for information overload if the entire list is included on every ARM loan program disclosure.

Interest-only payments. Proposed § 226.19(b)(2)(ii)(A) requires the creditor to disclose a statement that periodic payments will be applied only toward interest on the loan. The creditor would also disclose a statement of any limitation on the number of periodic payments that will be applied only toward interest on the loan and not towards the principal, that such payments will cover the interest owed each month, but none of the principal, and that making these periodic payments means the loan amount will stay the same and the consumer will not have paid any of the loan amount. For payment option loans, the creditor would disclose a statement that the loan gives the consumer the choice to make periodic payments that cover the interest owed each month, but none of the principal, and that making these periodic payments means the loan amount will stay the same and the consumer will not have paid any of the loan amount. Consumer testing showed that many participants did not understand that there are loans where the periodic payments do not pay down the mortgage principal. The Board believes it is important to alert consumers to this feature in order to avoid payment shock when the principal becomes due or the periodic payment increases.

Negative amortization. Proposed § 226.19(b)(2)(ii)(B) would require the creditor to disclose a statement that the loan balance may increase even if the consumer makes the required periodic payments. In addition, the creditor would disclose a statement that the minimum payment covers only a part of the interest the consumer owes each period and none of the principal, that the unpaid interest will be added to the consumer's loan amount, and that over time this will increase the total amount the consumer is borrowing and cause the consumer to lose equity in the home. The proposed requirement would replace existing § 226.19(b)(2)(vii), which requires the creditor to disclose any rules relating to changes in the outstanding loan balance, including an explanation of negative amortization. The Board believes that information regarding negative amortization should be disclosed because it is a complicated feature that significantly impacts a consumer's ability to repay the loan. Consumer testing showed that participants were generally unfamiliar with the term or concept. However, participants generally understood the revised transaction-specific plain-language explanation of negative amortization's causes and effects when disclosed in the ''Key Questions'' format.

Balloon payment. Proposed § 226.19(b)(2)(ii)(C) requires the creditor to disclose a statement that the consumer will owe a balloon payment, along with a statement of when it will be due. Proposed comment 19(b)(2)(ii)(C)–1 would clarify that the creditor must make this disclosure if the loan program includes a payment schedule with regular periodic payments that when aggregated do not fully amortize the outstanding principal balance. Proposed comment 19(b)(2)(ii)(C)–2 would clarify that the requirement to disclose when the balloon payment is due refers to the time period when it is due, not the exact calendar date. For example, the disclosure may state, ''You would owe a balloon payment due in seven years.'' The Board believes it is important for the consumer to be aware early in the process of any potential payment shock.

Demand feature. Proposed § 226.19(b)(2)(ii)(D) would require the creditor to disclose a statement that the creditor may demand full repayment of the loan, along with a statement of the timing of any advance notice the creditor will give the consumer before the creditor exercises such right. Proposed comment § 226.19(b)(2)(ii)(D)–1 would clarify that this requirement would apply not only to transactions payable on demand from the outset, but also to transactions that convert to a demand status after a stated period. Proposed comments § 226.19(b)(2)(ii)(D)–2 and –3 cross-reference comment 18(i)–2 regarding covered demand features and comment 18(i)–3 regarding the relationship to the payment schedule disclosures. The proposed rule replaces existing § 226.19(b)(2)(x). The Board believes that demand features are rare in consumer mortgage transactions, but pose a considerable risk when present and, therefore, should be brought to the consumer's attention. Consumer testing showed that participants understood the revised language regarding a demand feature and thought it was important information.

No-documentation or low-documentation loans. Proposed § 226.19(b)(2)(ii)(E) would require the creditor to disclose a statement that the consumer's loan could have a higher rate or fees if the consumer does not document employment, income, or other assets. In addition, the creditor would disclose a statement that if the consumer provides more documentation, the consumer could decrease the interest rate or fees. The Board is concerned that consumers who obtain loans with such features may not understand that they may pay a higher price for this feature.

Shared-equity or shared-appreciation. Proposed § 226.19(b)(2)(ii)(F) requires the creditor to disclose a statement that any future equity or appreciation in the real property or dwelling that secures the loan must be shared, along with a statement of the percentage of future equity or appreciation to which the creditor is entitled, and the events that may trigger such an obligation. The Board is aware that a number of shared-equity and shared-appreciation programs are being offered to consumers, including low- and moderate-income borrowers, on various terms. Consumer testing showed that participants were generally unfamiliar with the concept of shared-equity or shared-appreciation. However, to the extent that a shared-equity or a shared-appreciation feature is being offered as one of the loan terms, participants stated that they would want it disclosed clearly and prominently.

19(b)(3) Additional Information and Web Site

Currently, § 226.19(b)(2)(iv) and (v) require the creditor to disclose a statement that consumers should ask the creditor about the current margin value and current interest rate or the amount of any interest rate discount. Existing § 226.19(b)(2)(xii) requires a notice that disclosure forms are available for the creditor's other variable-rate programs. Consumer testing indicated that many consumers skim disclosures quickly and become frustrated if they cannot quickly locate the key information they seek. Reducing the number of non-specific notices in the loan program disclosures would increase the likelihood that consumers will read and understand specific disclosures. Under proposed § 226.19(b)(3), the creditor would be required to disclose that the consumer may visit the Web site of the Federal Reserve Board for more information about adjustable-rate mortgages and for a list of licensed housing counselors in the consumer's area that can help the consumer understand the risks and benefits of the loan. The Board believes that streamlining the notice will reduce information overload.

19(b)(4) Format Requirements

Proposed § 226.19(b)(4) contains format requirements for ARM loan program disclosures. As discussed more fully in proposed § 226.37, consumer testing showed that the location and order in which information was presented affected consumers' ability to locate and comprehend the information disclosed. Based on these findings, the Board proposes, under § 226.19(b)(4)(i), to require that creditors disclose the ''Key Questions about Risk'' using the format requirements for similar disclosures required by § 226.38, except as otherwise provided in proposed § 226.19(b)(4). Proposed § 226.19(b)(4)(ii) would require that the disclosures required by paragraphs (b)(1) through (b)(3) be grouped together and placed in a prominent location. Proposed § 226.19(b)(4)(iii) would require that the heading ''Adjustable Rate Mortgage'' or ''ARM'' required under § 226.19(b) be more conspicuous than and precede the other disclosures. The heading would be required to be outside the tables required under this paragraph. The creditor would be permitted to use a heading with the name of the loan program and the name of the creditor, such as ''XXX Bank 3/1 ARM.'' Proposed § 226.19(b)(4)(viii) would require the disclosure of the Board's Web site and list of licensed housing counselors to be disclosed outside of the required tables described below.

Proposed § 226.19(b)(4)(iv) to (vii) would require the following special formats for the ARM loan program disclosure: tabular format, question and answer format, highlighted answers, and special order of disclosures. Proposed § 226.19(b)(4)(iv) would require the creditor to provide the interest rate disclosure required under § 226.19(b)(1) and the ''Key Questions about Risk'' disclosure required under § 226.19(b)(2) in the form of two tables with headings, content and format substantially similar to Model Form H–4(B) in Appendix H. Consumer testing showed that using a tabular format improved participants' ability to readily identify and understand key information. Only the information required or permitted by paragraphs (b)(1) and (b)(2) would be in this table. In addition, under § 226.19(b)(4)(v), the ''Key Questions about Risk'' disclosures would be required to be grouped together and presented in the format of a question and answer in a manner substantially similar to Model Form H–4(B) in Appendix H. The table with interest rate information would precede the table with the ''Key Questions about Risk.'' Consumer testing showed that using a question and answer format improved participants' ability to recognize and understand potentially risky or costly features of a loan. Proposed § 226.19(b)(4)(vi) would require the creditor to disclose each affirmative answer in bold text and in all capitalized letters to highlight the fact that a risky feature is present in the loan. Negative answers (required under proposed § 226.19(b)(2)(i) but not under proposed § 226.(b)(2)(ii)) would be disclosed in non-bold text. Finally, proposed § 226.19(b)(4)(vii) would require the creditor to make the disclosures, as applicable, in the following order: Rate increases under § 226.19(b)(2)(i)(A), payment increases under § 226.19(b)(2)(i)(B), interest-only payments under § 226.19(b)(2)(ii)(A), negative amortization under § 226.19(b)(2)(ii)(B), balloon payments under § 226.19(b)(2)(ii)(C), prepayment penalties under § 226.19(b)(2)(i)(C), demand feature under § 226.19(b)(2)(ii)(D), no-documentation or low-documentation loans under § 226.19(b)(2)(ii)(E), and shared-equity or shared-appreciation under § 226.19(b)(2)(ii)(F). This order would ensure that consumers receive critical information about their payments first. Model Clauses and Samples are proposed at Appendix H–4(C) through H–4(F).

19(c) Publications for Transactions Secured by Real Property or a Dwelling

Based on the results of consumer testing, under the proposal creditors would be required to provide to consumers two Board publications for closed-end transactions secured by real property or a dwelling. The first publication, entitled ''*Key Questions to Ask about Your Mortgage,''* discusses loan terms and conditions that are important for consumers to consider when selecting a closed-end mortgage loan. The second publication, entitled ''*Fixed* vs. *Adjustable Rate Mortgages,''* discusses the respective costs and benefits of fixed-rate mortgages and ARMs.

Under existing § 226.19(b)(1), the creditor must provide to the consumer a copy of the CHARM booklet published by the Board, or a suitable substitute. The Board consumer tested the CHARM booklet and a sample current loan program disclosure. Few of the consumer testing participants who had obtained an ARM recalled having seen the CHARM booklet. Although many participants thought that the information in the CHARM booklet is useful, particularly the descriptions of ''payment shock,'' prepayment penalties, and negative amortization, most participants thought that the CHARM booklet is too long and that they likely would not read it.

The proposed rule would eliminate the requirement under § 226.19(b)(1) for creditors to provide the CHARM booklet to consumers who express interest in an ARM transaction, and instead, under proposed § 226.38(c)(2) require a brief Board publication showing the principal differences between a fixed-rate loan and an ARM. Comment 19(b)(1)– and –2 on the CHARM booklet would be removed accordingly. Also, proposed § 226.38(c)(1) would require creditors to provide to all consumers—regardless of whether they express interest in an ARM—two new single-page Board publications. These new disclosure forms would contain a notice stating where consumers may obtain additional information about ARMs. The Board believes that requiring that creditors provide the ''*Key Questions to Ask about Your Mortgage''* publication and the ''*Fixed versus Adjustable Rate Mortgages''* publication without modifications would promote consistency in the information consumers receive about ARMs. Accordingly, proposed § 226.19(c) would require creditors to provide this information ''as published.''

The Board proposes to require creditors to provide these publications at the time a consumer is given an application form or pays a non-refundable fee, whichever is earlier, for fixed-rate mortgage loans as well as variable-rate mortgage loans. Special rules for when a consumer accesses an application form electronically and when the creditor receives a consumer's application from an intermediary agent or broker are discussed below. The Board solicits comment on whether there are other loan types for which loan program publications should be given at the time an application form is provided to a consumer or before the consumer pays a non-refundable fee, whichever is earlier.

19(d) Timing of Disclosures

Proposed comment 19(c)–1 states that creditors are not required to provide disclosures under proposed § 226.19(c) in cases where an open-end credit account will convert to a closed-end transaction. The ''*Key Questions to Ask About Your Mortgage''* disclosure and the ''*Fixed vs. Adjustable Rate Mortgages''* disclosure would not be helpful at that time, because the creditor and consumer already will have entered into a written agreement. By contrast, transaction-specific disclosures are required in such cases under § 226.19(b), both as in effect (*see* comment 19(b)–2(iv)) and as proposed (*see* proposed § 226.19(b) and comment 19(b)–2).

Existing § 226.19(b) requires that creditors provide variable-rate loan program disclosures at the time an application form is provided to a consumer or before the consumer pays a non-refundable fee, whichever is earlier. Comment 19(b)–2 currently discusses when a creditor should provide such disclosures in cases where the creditor receives a consumer's application through an intermediary agent or broker or a consumer requests an application by telephone. The comment also clarifies that if the creditor solicits applications by mailing application forms, the creditor must send the ARM loan program disclosures with the application form. Existing § 226.19(c) contains requirements for providing variable-rate loan program disclosures when a consumer accesses an application form electronically. (Section 226.17(a)(1) currently permits creditors to provide the ARM loan program disclosures electronically, without regard to the consumer-consent or other provisions of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. 7001 *et seq.* (E-Sign Act)).

Under the Board's proposal, timing requirements for ARM loan program disclosures would be consolidated in proposed § 226.19(d). These timing requirements also would apply to the provision of the proposed new ''*Key Questions to Ask About Your Mortgage''* and ''*Fixed* vs. *Adjustable Rate*

Mortgages'' disclosures. Proposed § 226.19(d)(1) contains the general requirement to provide ARM loan program disclosures (if a consumer expresses interest in ARMs) at the time an application form is provided or before the consumer pays a non-refundable fee, whichever is earlier. Proposed § 226.19(d)(1) also specifies that creditors must provide ARM loan program disclosures before charging a fee for obtaining a consumer's credit report.

Proposed § 226.19(d)(2) states that if a consumer accesses an ARM loan application electronically, a creditor must provide the disclosures in electronic form, except as provided in § 226.19(d)(2). Proposed § 226.19(d)(2), in turn, states that if a consumer who is physically present in a creditor's office accesses an ARM loan application electronically, the creditor may provide disclosures in either electronic or paper form. These provisions are consistent with existing comment 19(c)–1(i) and (ii). Comment 19(c)–1 on the form of electronic disclosures would be redesignated as comment 19(d)(2)(i)–1. Commentary on the timing of electronic disclosures, currently contained in comment 19(b)–2(v), would be redesignated as comments 19(d)(2)(i)–2 and 19(d)(2)(ii)–1. Further, under the proposed rule existing § 226.17(a) would be revised to include the proposed new *Key Questions to Ask About Your Mortgage''* and ''*Fixed* vs. *Adjustable Rate Mortgages''* disclosures among the disclosures creditors may provide without regard to the consumer-consent or other provisions of the E-Sign Act.

Proposed § 226.19(d)(3) contains rules for applications made by telephone or through an intermediary. These rules are consistent with existing comment 19(b)–2. Existing comments 19(b)–2(i) through –2(iii) are redesignated as comments 19(d)(3)–1 through 19(d)(3)–3. Existing comment 19(b)–2(iii) states that the creditor must include the disclosures required by § 226.19(b) with any application form the creditor sends by mail to solicit consumers. This comment is redesignated as proposed comment 19(d)(3)–3 and revised to cover the *Key Questions* and *Fixed versus Adjustable Rate Mortgages* disclosures required by proposed § 226.19(c).

Proposed § 226.19(d)(4) provides that, where a consumer does not express interest in an ARM until after receiving or accessing an application form or paying a non-refundable fee, the creditor must provide an ARM loan program disclosure(s) within three business days after the consumer expresses such interest to the creditor or the creditor receives notice from an intermediary broker or agent that the consumer has expressed interest in an ARM. This is consistent with existing footnote 45b. Existing comment 19(b)–3 is redesignated as comments 19(d)(3)–1 through 19(d)(3)–3 under the proposed rule.

Proposed § 226.19(d)(5) provides that if the consumer expresses an interest in negotiating loan terms that are not generally offered, the creditor need not provide the disclosures required by § 226.19(b) before an application form is provided. Proposed § 226.19(d)(5) requires that the creditor provide such disclosures as soon as reasonably possible after the terms to be disclosed have been determined and not later than the time the consumer pays a non-refundable fee. Further, proposed § 226.19(d)(5) provides that in all cases the creditor must provide the disclosures required by § 226.19(c) of this section at the time an application form is provided or before the consumer pays a non-refundable fee, including a fee for obtaining a consumer's credit history, whichever is earlier.

Comment 19(b)(2)–1 currently provides that, if ARM loan program disclosures cannot be provided because a consumer expresses an interest in individually negotiating loan terms that the creditor generally does not offer, the creditor may provide disclosures reflecting those terms as soon as reasonably possible after the terms have been decided upon, but not later than the time the consumer pays a non-refundable fee. Proposed § 226.19(d)(5) incorporates that guidance into the regulation. Further, comment 19(b)(2)–1 provides that if, after an application form is provided or the consumer pays a non-refundable fee, a consumer expresses an interest in an adjustable-mortgage loan program for which the creditor has not provided the ARM loan program disclosures, the creditor must provide such disclosures as soon as reasonably possible. Proposed § 226.19(d)(6) incorporates that guidance into the regulation. The foregoing guidance is removed from comment 19(b)(2)–1 (which the proposed rule would redesignate as comment 19(b)–4) because under the proposed rule timing rules for ARM loan program disclosures are contained in § 226.19(d) rather than § 226.19(b).

Section 226.20 Subsequent Disclosure Requirements

20(b) Assumptions

Section 226.20(b) currently requires post-consummation disclosures if the creditor expressly agrees in writing with a subsequent consumer to accept that consumer as a primary obligator on an existing residential mortgage transaction. The Board proposes technical changes to § 226.20(b) and associated commentary to reflect the new format and content disclosure requirements for transactions secured by real property or a dwelling under §§ 226.37 and 226.38.

20(c) Rate Adjustments

For ARM transactions subject to § 226.19(b), § 226.20(c) currently requires creditors to mail or deliver to consumers a notice of interest rate adjustment at least 25, but no more than 120, calendar days before a payment at a new level is due. Section 226.20(c) also requires creditors to mail or deliver to consumers an adjustment notice at least once each year during which an interest rate adjustment is implemented without an accompanying payment change.

Those adjustment notices must state: (1) The current and prior interest rates for the loan; (2) the index values upon which the current and prior interest rates are based; (3) the extent to which the creditor has foregone any increase in the interest rate; (4) the contractual effects of the adjustment, including the payment due after the adjustment is made, and a statement of the loan balance; and (5) the payment, if different from the payment due after adjustment, that would be required to fully amortize the loan at the new interest rate over the remainder of the loan term. Model clauses in Appendix H–4(H) illustrate how creditors may comply with the requirements of § 226.20(c).

Discussion

The Board adopted the requirements for post-consummation disclosures (subsequent disclosures) in 1987. The minimum advance notice of a rate adjustment was set at 25 days to track the rules of the Office of the Comptroller of the Currency (OCC) and to provide creditors with flexibility in giving adjustment notices for a variety of ARMs. *See* 52 FR 48665, 48668; Dec. 24, 1987. Since 1987, ARMs have grown in popularity, especially from 2003 to 2007. Beginning in 2007, ARM growth began to slow as consumers experienced difficulty repaying such loans and concerns grew about the risk of payment shock ARMs pose.

Because ARMs pose the risk of payment shock, it is critical that consumers receive notice of ARM payment changes so they can prepare to make higher payments if necessary. If the new payments are unaffordable, borrowers need time to seek a refinance loan with lower payments or make other arrangements. Even if a consumer can afford a higher payment, the consumer may want to refinance into a fixed-rate loan for payment certainty or into another ARM loan with lower payments. It is particularly important that consumers with subprime loans receive adequate notice before a payment increase, as these borrowers tend to be more vulnerable to payment shock.

The Board believes the current 25-day notice is insufficient to allow many consumers to refinance into a loan with affordable payments or to make other arrangements. In the ''Subprime Mortgage Guidance'' issued in 2007, the Board, the OCC, FDIC, OTS, and NCUA stated that consumers should be given at least 60 days before an ARM adjustment in which to refinance without paying a prepayment penalty. Several consumer advocates who commented on the Board's 2008 HOEPA Final Rule stated that consumers with subprime ARMs may need significant time in which to seek out a refinancing, in some cases as much as 6 months.

The Board's Proposal

The Board proposes to require creditors to mail or deliver a notice of an interest rate adjustment at least 60 days before payment at a new level is due, instead of the current 25-day provision. Creditors would provide notice annually where interest rate changes are made without accompanying payment changes under the proposed. Proposed § 226.20(c)(1)(i) contains timing requirements for circumstances where a payment change accompanies an interest rate adjustment, and proposed § 226.20(c)(ii) contains timing requirements for circumstances where no payment change accompanies interest rate changes made during a year.

Proposed § 226.20(c)(2) contains content requirements for disclosures required where a payment change accompanies an interest rate adjustment. Proposed § 226.20(c)(3) contains content requirements for disclosures required once each year where no payment change accompanies an interest rate change. Whether or not a payment change is made, under proposed § 226.20(c)(4) creditors would disclose the following information: (1) The date until which the creditor may impose a prepayment penalty if the consumer prepays the obligation in full, if applicable; (2) a phone number the consumer may call to obtain additional information about the loan; and (3) a telephone number and Internet Web site for HUD-licensed housing counselors. Proposed § 226.20(c)(5) contains formatting requirements for discloses required by proposed § 226.20(c).

Section 226.20(c) currently provides that an adjustment to the interest rate with or without a corresponding adjustment to the payment in an adjustable-rate mortgage subject to § 226.19(b) is an event requiring new disclosures to the consumer. The proposed rule would retain this provision. Comment 20(c)–1 provides that the requirements of § 226.20(c) apply where the interest rate and payment change due to the conversion of an adjustable-rate mortgage subject to § 226.19(b) to a fixed-rate mortgage. The proposed rule would incorporate this guidance into proposed § 226.20(c). Further, the proposed rule would revise comment 20(c)–1 for clarity and to remove commentary on timing requirements, because timing requirements are contained in proposed § 226.20(c)(1).

The proposed rule would revise comment 20(c)–2 to clarify that price-level adjusted mortgages and similar mortgages are not subject to the disclosure requirements of § 226.20(c) because they are not subject to the disclosure timing requirements of § 226.19(b), as discussed above. The proposed rule would remove the commentary stating that ''shared-equity'' and ''shared-appreciation'' mortgages are not subject to the disclosure requirements of § 226.20(c) to conform with the removal of reference to such mortgages as examples of variable-rate transactions from comment 17(c)(1)–11 (redesignated as proposed comment 17(c)(1)(iii)–4), as discussed above. Under the proposed rule, whether or not creditors must provide ARM adjustment notices for a shared-equity or shared-appreciation mortgage depends on whether such mortgage has an adjustable rate or a fixed rate. Shared-equity and shared-appreciation mortgages with a fixed rate would not be considered adjustable-rate mortgages under the proposed rule.

20(c)(1) Timing of Disclosures

The Board proposes to require creditors to mail or deliver a notice of an interest rate adjustment for a closed-end ARM at least 60, but no more than 120, days before payment at a new level is due. This proposal is designed to provide borrowers with enough advance notice about an impending rate and payment change to enable them to refinance the loan if they cannot afford the adjusted payment. Even if consumers do not need or want to refinance a loan, they may need time to adjust other spending in order to afford higher mortgage loan payments.

The Board issued the current rule requiring 25 days' notice before a payment at a new level is due in 1987. Home Mortgage Disclosure Act (HMDA) data for the years 2004 through 2007 suggest that a requirement to provide ARM adjustment 60, rather than 25, days before payment at a new level is due more closely reflects the time needed for consumers to refinance a loan.[44] In each of those years, for first-lien refinance loans, the period between loan application and origination was 25 days or less for 50 percent of the loans originated, 45 days or less for 75 percent of the loans originated, and 65 days or less for 90 percent of the loans originated. (These data do not include time needed to compare available refinance loans.) Requiring creditors to provide an ARM adjustment notice at least 60 days before payment at a new level is due would better enable consumers to arrange to make a higher payment (if applicable) without missing a payment or paying less than the amount due.

The Board believes that a 60-day minimum notice requirement is consistent with many existing ARM agreements. For most ARMs, creditors base the calculation of interest rate changes on the value of an index 30 or 45 days prior to the effective date of a rate change (calculation date). Creditors generally refer to the period from the calculation date to the effective date of the interest rate change as the ''look-back period.'' (Interest rate change dates tend to be the first of a month to correspond with payment due dates.) In turn, payment in the new amount is due on the first day of the month following the month in which interest accrued at the new rate.

Thus, for most ARM loans creditors know what the new interest rate and payment will be well before payment at a new level is due, even assuming a week-long lag between publication of an index's level and the creditor's verification of that level. In fact, many creditors mail or deliver notice of an interest rate and payment change 60 or more days before payment at a new level is due.

[44] HMDA data consist of information reported by about 8,600 home lenders, including all of the nation's largest mortgage originators. Reported loans are estimated to represent about 80 percent of all home lending nationwide. Accordingly, HMDA data likely provide a broadly representative view of U.S. home lending. Robert B. Avery, Kenneth P. Brevoort, and Glenn B. Canner, *The 2007 HMDA Data*, 94 Fed. Reserve Bulletin A107 (Dec. 23, 2008).

However, some ARM agreements may provide for shorter look-back periods. For example, the calculation date for some ARM products is the first business day of the month that precedes the effective date of the interest rate change. The first day of that month may not be a business day, in which case the look-back period would be fewer than 30 days. In addition, it takes time for index levels to be reported and for creditors to confirm the index level and prepare disclosures for delivery or mailing.

Proposed § 226.20(c)(1) requires creditors to provide advance notice of an adjustment at least 60, but no more than 120, days before *payment* at a new level is due, not before the interest rate changes. Comment 20(c)–1 would be revised to reflect the increase in the required advance notice of a payment adjustment. Proposed comment 20(c)(1)–1 provides that if an adjustable-rate feature is added when an open-end credit account is converted to an adjustable-rate transaction, creditors must provide disclosures under § 226.20(c)(1) where payments change due to conversion of a transaction subject to § 226.19(b) to a fixed-rate transaction. Because relevant payment changes under existing and proposed § 226.20(c) are those due to interest changes, proposed comment 20(c)(1)–2 clarifies that payment changes due to adjustments in property tax obligations or premiums for mortgage-related insurance do not trigger requirements to disclose interest rate and payment adjustments.

The Board solicits comment on the operational changes creditors and servicers would need to make to provide disclosures at least 60 days before payment at a new level is due. Are there indices that are published at times that would make compliance with such a rule difficult? Are reported levels for particular indices difficult to confirm within a few days? The Board requests comment on whether requiring creditors to provide 45, rather than 60, days' advance notice of a payment change better balance concerns about providing sufficient notice to consumers and sufficient time for creditors to verify reported indices and prepare disclosures.

A look-back period of 45 days likely provides ample time for a creditor to determine a loan's new interest rate and provide disclosures at least 60 days before payment at a new level is due, as discussed above. Are there reasons why a look-back period of forty-five days is not feasible for certain loan types for which a shorter look-back period is common, for example, subordinate-lien loans? Also, where an interest rate and payment adjustment is due to the conversion of an adjustable-rate mortgage to a fixed-rate mortgage under a written agreement, should creditors continue to be required to provide an adjustment notice at least 25, rather than at least 60, days before payment at a new level is due?

Coverage. Section 226.20(c) currently applies to transactions subject to § 226.19(b), which applies to closed-end ARMs secured by a consumer's principal dwelling with a term greater than one year. The Board is proposing to apply § 226.19(b) to all closed-end ARMs secured by real property or a dwelling, as discussed above. Proposed § 226.20(c) would apply to the same category of transactions.

The Board recognizes that currently creditors need not provide ARM adjustment notices under existing § 226.20(c) for a short-term transaction, such as a construction loan, with an adjustable rate. The Board solicits comment on whether a 60-day notice period is appropriate for such loans and if not, what period would be appropriate and still provide consumers sufficient notice of a payment change.

Existing ARM loan agreements. The Board is aware that some ARM loan agreements may provide for a look-back period that is too short for the creditor to be able to provide an adjustment notice at least 60 days before payment at a new level is due. The Board seeks comment on the number or proportion of existing ARM loan agreements under which creditors or servicers could not comply with a minimum 60-day advance notice requirement.

20(c)(2)(i)

Where a payment change accompanies an interest rate change, proposed § 226.20(c)(2)(i) requires creditors to disclose a statement that changes are being made to the interest rate and the date such change is effective. Proposed § 226.20(c)(2)(i) also requires creditors to state that more detailed information is available in the loan agreements. Proposed § 226.20(c)(5)(ii) requires that these disclosures appear before the other required disclosures, as discussed below.

20(c)(2)(ii)

Proposed § 226.20(c)(2)(ii) requires creditors to provide the following disclosures for covered loans in the form of a table: (1) The current and new interest rates; (2) if payments are interest-only or negatively amortizing, the amount of the current and new payment allocated to pay interest, principal, and property taxes and mortgage-related insurance, as applicable; and (3) the current and new periodic payment amounts and the due date for the first new payment. This content is substantially similar to the content of the ''Payment Summary'' table in the TILA disclosures provided before consummation for most types of ARMs. (Under proposed § 226.38, the ''Payment Summary'' table for negatively amortizing ARMs differs from the ''Payment Summary'' table for other ARMs, as discussed below.) Under proposed § 226.20(c)(5)(iii), this table would have to contain headings, content, and format substantially similar to those in Appendix H–4(G), as discussed below.

Currently, ARM adjustment notices need not state how payments are allocated among principal, interest, and escrow accounts. The Board believes that a table showing payment allocations would benefit consumers with interest-only or negatively amortizing loans. Participants in the Board's consumer testing generally understood a sample form with a table showing the transition from interest-only payments to payments of both principal and interest. Further, all participants correctly identified the new payment and the due date of the first payment at the new level shown in the table. Almost all participants recognized the increase in the interest rate and amounts escrowed for taxes and property-related insurance and that part of the new payment would be allocated to pay principal.

Comment 20(c)(1)–1 on disclosing ''current'' and ''prior'' interest rates would be revised for clarity to refer instead to ''current'' and ''new'' interest rates. Under the proposed rule, § 226.20(c)(3) contains content requirements for annual notice disclosures and § 226.20(c)(2) contains content requirements for payment change notices. Accordingly, commentary on disclosure where no payment change has occurred during a year would be removed from comment 20(c)(1)–1.

20(c)(2)(iii)

Creditors currently must disclose the index values upon which the prior and new interest rates are based, under existing § 226.19(c)(2). Some consumer testing participants had difficulty understanding the relationship among an index, a margin, and an interest rate. Accordingly, proposed § 226.20(c)(2)(iii) substitutes a requirement that disclosures contain a description of the change in the index or formula for the disclosure required under existing § 226.20(c)(2). For example, rather than disclose that payments previously were based on a 1-year LIBOR rate of 3.75 and now would be based on a new rate of 5.75, a creditor might disclose the following: ''Your interest rate will change due to an increase in the 1-year LIBOR index.'' Further, proposed § 226.20(c)(2)(iii) requires creditors to disclose any application of previously foregone increases together with the description of the change in the index or formula.

A simple statement of the occurrence that caused the interest rate and payment to change likely conveys a level of information suitable for most consumers' needs. In consumer testing conducted for the Board, participants indicated that they found explanations of interest rates difficult to follow. Thus, providing more information would likely result in information overload. Consumers who prefer more information can review the loan agreement to determine the interaction between the interest rate and the index and margin or to learn more about the formula used to determine the interest rate. The loan agreement also will contain information about how the creditor may apply previously foregone interest. For these reasons, proposed § 226.20(c)(2)(ii) does not require creditors to disclose the current and prior index values. Comment 20(c)(2)–1 would be removed accordingly.

Comment 20(c)(4)–1, which discusses the types of contractual effects § 226.20(c) requires creditors to disclose—for example, effects on the loan term and balance—also would be removed under the proposed rule. Proposed comments 20(c)(2)(vi)–2, 20(c)(2)(vii)–1, and 20(c)(3)(v)–1 reflect the removed commentary, however.

20(c)(2)(iv)

Existing § 226.20(c)(3) requires that a creditor disclose the extent to which the creditor has foregone any increase in the interest rate. This requirement would be redesignated as proposed § 226.20(c)(2)(iv). Further, proposed § 226.20(c)(iv) would require creditors to disclose the earliest date a creditor may apply foregone interest to future adjustments, subject to any rate caps. Proposed comment 20(c)(3)(iv)–1 states that creditors may rely on proposed comment 20(c)(2)(iv)–1 in determining to which transactions the requirement to disclose foregone interest applies and how to disclose such increases. Proposed comment 20(c)(3)(iv)–1 clarifies that creditors need not disclose the earliest date the creditor may apply foregone interest in notices provided annually when no payment change occurs during a year.

20(c)(2)(v)

Proposed § 226.20(c)(2)(v) would require creditors to disclose limits on interest rate or payment increases at each adjustment, if any, and the maximum interest rate or payment over the life of the loan. This is consistent with the disclosure of rate change limits in the ''More Information about Your Payments'' section of the disclosures provided within three business days of application. *See* proposed § 226.38(e).

20(c)(2)(vi)

Currently, where the required loan payment is different from the payment disclosed under § 226.20(c)(4), § 226.20(c)(5) requires a creditor to disclose the payment required to fully amortize the loan over the remainder of the loan term. This requirement would be redesignated as proposed § 226.20(c)(2)(vi). Further, in all cases creditors would disclose a statement regarding whether or not part of the new payment will be allocated to pay the loan principal. This is consistent with the focus on the impact of loan payments on loan principal in the proposed new ''Key Questions'' disclosure in § 226.19(c) and the ''Key Questions about Risk'' section of the disclosure creditors provide within three business days of application in proposed § 226.38(d).

Existing comment 20(c)(5)–1, on fully amortizing payments, would be redesignated as comment 20(c)(2)(vi)–1. The comment also would be revised for clarity and to update cross-references. Consistent with existing comment 20(c)(4)–1, proposed comment 20(c)(2)(vi)–2 clarifies that the creditor must disclose any change in the term or maturity of the loan if the change resulted from the rate adjustment.

20(c)(2)(vii)

Existing § 226.20(c)(4) requires creditors to disclose the loan balance. This requirement would be redesignated as proposed § 226.20(c)(2)(vii) and would require creditors to disclose the loan balance as of the effective date of the interest rate adjustment. Proposed comment 20(c)(2)(vii)–1 clarifies that the balance required to be disclosed is the balance on which the new adjusted payment is based. This is consistent with existing comment 20(c)(4)–1.

20(c)(3) Content of Annual Interest Rate Notice

Existing § 226.20(c) requires creditors to provide ARM adjustment notices at least once each year during which an interest rate adjustment is implemented without an accompanying payment change. This requirement would be redesignated as proposed § 226.20(c)(3). Currently, § 226.20(c) contains a single list of required disclosures creditors must provide as applicable, in a payment change notice and an annual notice of interest rate changes without payment changes. Proposed § 226.20(c)(3) specifies the disclosures that are applicable for purposes of annual notices.

20(c)(3)(i)

Under proposed § 226.20(c)(3)(i), where no payment adjustment has been made during a year, the creditor must disclose that the interest rate on the loan has changed without changing the payments the consumer must make. Further, proposed § 226.20(c)(3)(i) requires creditors to disclose the specific time period for which the annual notice discloses interest rates that were not accompanied by payment changes. Proposed § 226.20(c)(5)(ii) requires that this disclosure appear before the other required disclosures, as discussed below.

20(c)(3)(ii)

Under proposed § 226.20(c)(3)(ii), a creditor must disclose the highest and lowest interest rates applied during the year in which no payment change has accompanied interest rate changes. Creditors would not disclose all interest rates applied to a transaction if the payment has not changed. By contrast, existing comment 20(c)–1 provides that creditors either may disclose all interest rates that applied or the highest and lowest rates. The Board believes that a simple and clear disclosure of the highest and lowest interest rates applied better conveys to consumers the impact of interest rate changes than does a list of all of the interest rates applied. This is especially true where interest rates change more frequently than monthly.

20(c)(3)(iii)

Creditors disclose the extent to which the creditor has foregone any increase in the interest rate under existing § 226.20(c)(3). This requirement would be contained in proposed § 226.20(c)(3)(iii) for notices where payment changes do not accompany interest rate changes made during a year.

20(c)(3)(iv)

Proposed § 226.20(c)(3)(iv) requires creditors to disclose the maximum interest rate that may apply over the life of the loan. This is consistent with the disclosure of rate change limits in the ''More Information about Your Payments'' section of the disclosures provided within three business days of application in proposed § 226.38(e).

20(c)(3)(v)

Existing § 226.20(c)(4) requires creditors to disclose the loan balance. Under the proposal, this requirement would be contained in proposed § 226.20(c)(3)(v) for purposes of annual notices where payment changes do not accompany interest rate changes. Creditors would disclose the loan balance as of the last date of the year covered by the disclosure. Proposed comment 20(c)(3)(v)–1 clarifies that the balance required to be disclosed is the balance on which the new adjusted payment is based. This is consistent with existing comment 20(c)(4)–1.

20(c)(4) Additional Information

Proposed § 226.20(c)(4) requires that ARM adjustment notices creditors provide information about prepayment penalties, contacting the creditor, and locating housing counseling resources. Proposed § 226.20(c)(5)(ii) requires that these additional disclosures be located directly below the required interest rate disclosures, as discussed below.

20(c)(4)(i)

Proposed § 226.20(c)(4)(i) requires creditors to disclose the last date the creditor may impose a penalty if the consumer prepays the obligation in full and the amount of the maximum penalty possible before that date, if applicable. Under proposed § 226.20(c)(4)(i), if an ARM has a prepayment penalty, the creditor must disclose the required information whether or not a payment change accompanies the interest rate change. The Board believes that disclosures regarding a prepayment penalty would assist consumers in determining when to seek a refinance loan. When presented with a sample ARM adjustment notice for a loan with a prepayment penalty, almost all consumer testing participants recognized that a prepayment penalty would apply if they obtained a refinance loan before a specified date.

Proposed § 226.20(c)(4)(i) provides that the creditor shall disclose the maximum prepayment penalty possible if the consumer prepays in full between the date the creditor delivers or mails the ARM adjustment notice and the last day the creditor may impose the penalty. The Board requests comment on whether creditors should determine the maximum prepayment penalty during some other period, for example between the date the creditor prepares the ARM adjustment notice and the last day the creditor may impose the penalty.

20(c)(4)(ii)

Proposed § 226.20(c)(4)(ii) requires creditors to disclose a phone number to call for additional information about the consumer's loan. Creditors must provide this information whether or not a payment change accompanies an interest rate change, under the proposed rule. Most consumer testing participants responded positively to tested disclosures stating how to contact their lender with questions and stated that they would call their lender if they realized they were unable to afford higher payments on an ARM.

20(c)(4)(iii)

Proposed § 226.20(c)(4)(iii) requires creditors to disclose a phone number and an Internet Web site consumers may use to obtain a list of HUD-licensed housing counselors. The proposed rule requires creditors to provide this disclosure whether or not a payment change accompanies an interest rate change. Most consumer testing participants thought that information about how to locate a HUD-licensed housing counselor would be useful to consumers. Some said that they would use the information themselves if they had difficulty affording payments.

20(c)(5) Format of Disclosures

20(c)(5)(i)

Proposed § 226.20(c)(5)(i) requires that the heading, content, and format of the disclosures required by § 226.20(c) be substantially similar to the heading, content, and format of the model form in Appendix H–4(G), where an interest rate adjustment is accompanied by a payment change, or the model form in Appendix H–4(K), where a creditor provides an annual notice of interest rate adjustments without an accompanying payment change. Proposed § 226.20(c)(5)(i) also requires that the disclosures required by § 226.20(c) be placed in a prominent location. (Comment 37(d)–1 states that disclosures meet the prominent location standard if they are located on the first page and on the front side of the disclosure statement.)

Further, under proposed § 226.20(c)(5)(i) the interest rate disclosures required by § 226.20(c)(2) (where a payment change accompanies an interest rate change) or § 226.20(c)(3) (where no payment change occurs during a year) must be grouped together with the additional disclosures on prepayment penalties, contacting the creditor or servicer for loan information, and locating housing counseling resources required by proposed § 226.20(c)(4). These grouped disclosures must be segregated from everything else.

20(c)(5)(ii)

Under proposed § 226.20(c)(5)(ii), the statement that changes are being made to the interest rate and payments (under proposed § 226.20(c)(2)(i)) or that the interest rate has changed without accompanying payments changes (under proposed § 226.20(c)(3)(i)) must precede the other required disclosures. The additional disclosures on information on prepayment penalties, contacting the creditor, and housing counseling resources required by proposed § 226.20(c)(4) must follow the interest rate disclosures, under proposed § 226.20(c)(5)(ii).

20(c)(5)(iii)

Under proposed § 226.20(c)(5)(iii), where a payment change accompanies an interest rate adjustment, the interest rate and payment change disclosures required by proposed § 226.20(c)(2)(ii) must contain headings, content, and format substantially similar to those in the table contained in Appendix H–4(G). The textual disclosures required by proposed § 226.20(c)(2)(iii) through (vii) must be located directly below the table. Further, the format requirements in § 226.37 apply to ARM adjustment notices, as discussed below.

Regulations of other agencies. Footnote 45c to § 226.20(c) currently states that creditors may substitute information provided in accordance with variable-rate subsequent disclosure regulations of other federal agencies for the disclosure required by § 226.20(c). The Board adopted footnote 45c in 1987, a time when OCC, FHLBB, and HUD regulations contained subsequent disclosure requirements for ARMs. *See* 52 FR 48665, 48671; Dec. 24, 1987. The proposed rule would remove footnote 45c. No comprehensive disclosure requirements for variable-rate mortgage transactions presently are in effect under the regulations of the other Federal financial institution supervisory agencies, as discussed above.

20(d) Periodic Statement for Negative Amortization Loans

The Board proposes to require creditors to provide periodic statements for payment option ARMs with a negative amortization feature that are secured by real property or a dwelling. Such ARMs permit consumers to choose the amount paid (above a specified minimum) each period. In 2006, the Board, the OCC, the OTS, the FDIC, and the NCUA expressed concerns about consumer understanding of how such loans function and of the effect of negative amortization on a loan's balance in the Interagency Guidance on Nontraditional Mortgage Product Risks issued in 2006. 71 FR 58609; October 4, 2006. The agencies issued related sample illustrations that include a payment summary table showing the impact of various payment options on the loan balance that creditors may include with periodic statements for payment option ARMs. 72 FR 31825, 31831; Jun. 8, 2007. The illustrations were not consumer-tested. The Board's proposed model table showing payment options is similar to the summary table the agencies issued but has been revised based on consumer testing.

Payment option ARMs are complex products. Most participants in the Board's consumer testing were unfamiliar with such loans and with negative amortization generally. These loans present consumers with choices each month, and how the consumer exercises his or her choice may result in negative amortization and much higher payments when the consumer must begin to make fully amortizing payments or a balloon payment. The Board believes that consumers should be informed of the consequences of making minimum payments on such a loan. Thus, the Board proposes to require creditors to provide a periodic statement that describes a consumer's payment options and the effects of making payments in those amounts.[45]

20(d)(1) Timing and Content of Disclosures

For closed-end transactions secured by real property or a dwelling that permit the consumer to select among multiple payment options that include an option that results in negative amortization, proposed § 226.20(d) requires creditors to provide a periodic statement that discloses payment options not later than fifteen business days before a payment is due. Where payment at a new level is due, however, proposed § 226.20(c) requires creditors to provide an ARM adjustment notice no later than 60 days beforehand, as discussed above.

20(d)(1)(i) Payment

Proposed § 226.20(d)(1)(i) would require creditors to disclose, based on the interest rate in effect at the time the disclosure is made, the payment amount required to: (1) Pay off the loan balance in full by the end of the term through regular periodic payments, without a balloon payment; (2) prevent negative amortization, if the legal obligation explicitly permits the consumer to elect to pay interest only without paying principal; and (3) pay the minimum payment required under the legal obligation. Under the proposed rule, creditors would provide each disclosure as applicable. For example, if the terms of the loan obligation did not provide the option for consumers to make interest-only payments, creditors would disclose only the required minimum payment and the fully amortizing payment.

In consumer testing conducted for the Board, participants generally understood the options presented in the table. Most were able to understand that making the minimum required payment would cause their loan balance to grow. They also understood that making a fully amortizing payment would be a safe choice and would pay their loan balance off over time.

Proposed comment 20(d)(1)–1 clarifies that creditors must provide a summary table under § 226.20(d) for covered loans that allow a consumer to choose to make a payment that results in negative amortization even if the initial payments required do not negatively amortize the loan. Proposed comment 20(d)(1)–1 states that a payment summary table need only contain those disclosures that apply to payment options available to a consumer, however. For example, the proposed comment states that if a negatively amortizing loan recasts and a consumer must begin to make fully amortizing payments, the payment summary table need not disclose payments other than the fully amortizing payment.

Proposed comment 20(d)(1)–2 states that creditors may base all disclosures on the assumption that payments will be made on time and in the amounts required by the terms of the legal obligation, disregarding any possible inaccuracies resulting from consumers' payment patterns. This is consistent with existing comment 17(c)(2)(i)–3 and proposed revisions to comment 17(c)(1)–1, discussed above. Proposed comment 20(d)(1)–2 clarifies, however, that creditors may not base disclosures for loans with a negatively amortizing feature on the fully amortizing, interest-only, or other payment unless that payment is the amount the consumer is required to pay under the legal obligation. Finally, proposed comment 20(d)(1)(i)–1 states that creditors may rely on comment 38(c)(5)–1 to determine whether a payment is a regular periodic payment or a balloon payment.

20(d)(1)(ii) Effects

Proposed § 226.20(d)(1)(ii) requires creditors to disclose the effects of making payments in the amounts required to be disclosed under proposed § 226.20(d). Appendix H – 4(L) contains a proposed model form with accessible language on fully amortizing payments, interest-only payments, and negatively amortizing minimum payments. First, the model form states that a fully amortizing payment will cover all the interest owed in a particular payment plus some principal and decrease the loan balance and that if the consumer regularly makes the fully amortizing payment the consumer will pay off the loan on schedule. Second, the model form states that an interest-only payment will cover all the interest owed in a particular payment but none of the principal, that the consumer's balance will remain the same, and that if the consumer regularly makes interest-only payments the consumer will have to make larger payments as early as a specified date. Third, the model form states that a minimum payment will cover only part of the interest owed in a particular payment and result in a specified amount of unpaid interest being added to the loan balance and that if the consumer makes a minimum payment the consumer in effect will be borrowing more money and will lose home equity. Further, the model form states that if a consumer regularly makes minimum payments the consumer will have to make significantly larger payments as early as a specified date.

Proposed comment 20(d)(1)(ii)–1 states that the disclosures required by § 226.20(d) must be consistent with the terms of the legal obligation. For example, the proposed comment clarifies that disclosures may not state that making fully amortizing payments on an interest-only loan will reduce a consumer's loan balance if the creditor will not apply payments that exceed the interest-only payment to principal.

[45] The Federal financial institution supervisory agencies (the Board, the OCC, the OTS, the FDIC, and the NCUA (collectively, the agencies)) expressed concerns about consumer understanding of how such loans function and of the effect of negative amortization on a loan's balance in the Interagency Guidance on Nontraditional Mortgage Product Risks issued in 2006. 71 FR 58609; October 4, 2006. The agencies issued related sample illustrations that include a payment summary table showing the impact of various payment options on the loan balance that creditors may include with periodic statements for payment option ARMs. 72 FR 31825, 31831; Jun. 8, 2007. Proposed § 226.20(d) requires creditors to provide periodic statements that disclose payment options in the form of a table. The proposed model table is similar to the summary table the agencies issued but has been revised based on consumer testing.

20(d)(1)(iii) Unpaid Interest

Proposed § 226.20(d)(1)(iii) requires creditors to disclose the amount that will be added to the loan balance due to unpaid interest, if the consumer elects to make a payment that results in negative amortization.

20(d)(2) Format of Disclosures

Proposed § 226.20(d)(2)(i) requires that periodic statements for loans with a negative amortization feature contain payment disclosures with content substantially similar to the content of Form H–4(L) in Appendix H. Further, the proposed provision requires creditors to make payment disclosures in a payment summary table with headings, content, and format substantially similar to Form H–4(L). Proposed § 226.20(d)(2)(ii) requires that disclosures be placed in a prominent location (that is, located on the first page and on the front side of the disclosure statement, as clarified by proposed comment 37(d)(1)–1), with one exception. Under proposed § 226.20(d)(2)(ii), if the payment disclosures required by § 226.20(d) are made together with the ARM adjustment disclosures required by § 226.20(c), the payment disclosures must be located directly below the ARM adjustment disclosures.

Proposed § 226.20(d)(2)(iii) requires that the table required by § 226.20(d)(2)(i) contain only the information required by § 226.20(d)(1). Other information may be presented with the table under the proposed rule, provided that such information appears outside of the required table.

Alternatives not proposed. The Board is proposing to apply the requirement to provide periodic statements that contain a payment summary table, for payment option ARMs with a negative amortization feature that are secured by real property or a dwelling. The Board considered requiring periodic statements for all loans secured by real property or a dwelling. The Board is not proposing such a requirement, however. It is not clear that a monthly statement on a fixed-rate mortgage or an ARM without payment options would provide sufficient benefits to consumers to offset the costs of providing statements. For these loans, the consumer cannot exercise any choice in payments. Moreover, creditors must give borrowers advance notice each time the required payment for a variable-rate transaction adjusts, under § 226.20(c), as discussed above. Servicers send borrowers with escrow accounts annual statements under RESPA. Some servicers send additional escrow notices more frequently, for example quarterly. Those statements assist consumers in monitoring account changes related to changes in taxes or property insurance costs.

20(e) Creditor-Placed Property Insurance

Creditor-placed property insurance requirements. The security instrument or promissory note typically contains a requirement that the consumer maintain insurance on the property securing the loan, such as the consumer's dwelling or automobile. If the consumer fails to maintain the insurance or the insurance is cancelled, the credit agreement typically authorizes the creditor to obtain such insurance at the consumer's expense. The premium becomes additional debt of the consumer. This practice is known as ''creditor-placed property insurance.''

Industry reports indicate that the volume of creditor-placed property insurance premiums has increased significantly in the past few years.[46] Consumers struggling financially may fail to pay required property insurance premiums unaware that the creditor has the right to obtain such insurance on their behalf and add the premiums to the outstanding loan balance.[47] In some instances, creditors have improperly obtained property insurance when they arguably knew or should have known that the consumer already had insurance.[48] Generally, creditor-placed insurance is more costly and provides less coverage than insurance that a consumer purchases through an insurance agent.[49]

Currently, there is no provision in Regulation Z or federal law that requires the creditor to provide notice of the cost to the consumer before charging the consumer for creditor-placed property insurance. It appears that only a few states require creditors to provide notice, and these requirements differ. Under Michigan law, for example, a creditor may not impose charges on a debtor for creditor-placed property insurance unless the creditor provides two notices and allows the borrower a total of 30 days to provide evidence of insurance.[50] New Mexico law, on the other hand, simply requires the insurer to provide notice to the debtor within 15 days *after* the placement or renewal of creditor-placed property insurance.[51] The majority of states have no notice requirement. The servicing guidelines of Fannie Mae and Freddie Mac also vary greatly. Fannie Mae's guidelines state that the servicer ''should'' provide the borrower with at least one written notice and a total of at least 60 days to provide evidence of insurance before charging for creditor-placed property insurance.[52] Freddie Mac's guidelines do not require the servicer to provide notice to the borrower.[53]

In order to ensure that consumers are informed of the cost of creditor-placed property insurance, the Board proposes to use its authority under TILA Section 105(a), 15 U.S.C. 1604(a), to add § 226.20(e) to require the creditor to provide notice of the cost and coverage of creditor-placed property insurance before charging the consumer for such insurance. In addition, proposed § 226.20(e)(4) would require the creditor to provide the consumer with evidence of creditor-placed property insurance within 15 days of imposing a charge for such insurance. Proposed § 226.20(e)(1) would define ''creditor-placed property insurance'' as ''property insurance coverage obtained by the creditor when the property insurance required by the credit agreement has lapsed.'' Section 226.20(e) would apply to secured closed-end loans, including mortgage and automobile loans. The Board solicits comment as to whether this rule should also apply to HELOCs.

Proposed § 226.20(e)(2) contains three conditions for charging for creditor-

[46] *See, e.g.,* Consumer Credit Industry Association, *Fact Book of Credit-Related Insurance* at 1 (2007) (finding that the 2007 volume of creditor-placed property insurance premiums was over twice the 2002 amount).

[47] *See* State of Wisconsin, Office of the Commissioner of Insurance, *''Force-Placed'' Insurance Surprises Those Who Let Policies Lapse* (May 30, 2002) *available at http://oci.wi.gov/pressrel/0502home.htm* (''Many people don't realize that if they let that [homeowner's] insurance lapse, banks and other lenders can legally re-insure their home loan by buying insurance to replace it and making the homebuyer pay for it.'').

[48] *See, e.g., United States of America* v. *Fairbanks Capital Corp.,* Civ. Action No. 03–12219–DPW, Complaint at ¶ 17 (D. Mass. Nov. 12, 2003) (finding that Fairbanks improperly obtained property insurance when it knew or should have known that borrowers already had insurance); *Ocwen Federal Bank FSB,* OTS Docket No. 04592, Supervisory Agreement, OTS Docket No. 04592 (Apr. 19, 2004) (requiring the bank to take reasonable actions to determine whether appropriate hazard insurance is already in place before it obtained creditor-placed property insurance).

[49] *See, e.g., Webb, et al.* v. *Chase Manhattan Mortgage Corp.,* No. 2:05–CV–0548, 2008 U.S. Dist. LEXIS 42559, at *15 (S.D. Ohio May 28, 2008) (finding that the creditor-placed property insurance premium was four times higher than the plaintiff's original premium and did not cover personal property or provide coverage for personal liability or medical payments to others).

[50] Mich. Comp. Laws § 500.1625 (2009).

[51] N.M. Admin. Code § 13.18.3.17 (2009).

[52] Fannie Mae Single-Family Servicing Guide, Part II, Ch. 6 Lender-Placed Property Insurance (2005).

[53] Freddie Mac Single-Family Seller/Servicer Guide, Vol. 2, § 58.9 Special Insurance Requirements and Changes in Insurance Requirements (2007).

placed property insurance. First, proposed § 226.20(e)(2)(i) would require the creditor to make a reasonable determination that the required property insurance had lapsed. Second, proposed § 226.20(e)(2)(ii) would require the creditor to mail or deliver to the consumer a written notice containing the information required by the proposed rule at least 45 days before a charge is imposed on the consumer for the creditor-placed property insurance. Finally, proposed § 226.20(e)(2)(iii) would permit the creditor to charge the consumer if, during the 45-day notice period, the consumer did not provide the creditor with evidence of adequate property insurance.

Notice period timing and charges. Under the proposed rule, the creditor would have to mail or deliver to the consumer the required written notice at least 45 days before charging the consumer for the cost of creditor-placed property insurance. This 45-day notice period is consistent with the 45-day notice period required by the Flood Disaster Protection Act of 1973 Section 102(e), 42 U.S.C. 4012a(e), and represents the midpoint between State law 30-day notice periods [54] and the 60-day Fannie Mae Servicing Guide recommendation.[55] The Board notes that the provision in the Fannie Mae Servicing Guide is stated as a recommendation, but not a requirement. The Board believes that a 45-day notice period would allow the consumer reasonable time to shop for and provide evidence of insurance. The Board recognizes that it may take several days for the consumer to receive a notice sent by mail, but the consumer would still have at least one calendar month in which to shop for and purchase property insurance. Comment is solicited, however, on whether a different time period would better serve the needs of consumers and creditors.

Proposed comment 20(e)–1 would make clear that if the creditor complies with § 226.20(e), the creditor could charge the consumer for creditor-placed insurance as of the 46th day after sending the notice to the consumer. For example, a creditor that mails the required notice on January 2, 2011, may begin to charge the consumer for the cost of the creditor-placed property insurance on February 18, 2011. Proposed comment 20(e)–1 would also clarify that the creditor may charge the consumer for the cost of any required property insurance obtained during the 45-day notice period if such charge is not prohibited by applicable State or other law.

Content and format of notice. Proposed § 226.20(e)(3) would require the creditor to provide the written notice clearly and conspicuously. Proposed § 226.20(e)(3)(i) would require that the notice contain the creditor's name and contact information, the loan number, and the address or description of the property securing the credit transaction. The Board solicits comment as to whether the creditor should be required to establish a local or toll-free telephone number for the consumer to contact the creditor.

Under proposed § 226.20(e)(ii)–(viii), the notice would also need to contain the following statements: (1) That the consumer is obligated to maintain insurance on the property securing the credit transaction; (2) that the required property insurance has lapsed; (3) that the creditor is authorized to obtain the property insurance on the consumer's behalf; (4) the date the creditor can charge the consumer for the cost of the creditor-placed property insurance; (5) how the consumer may provide evidence of property insurance; (6) the cost of the creditor-placed property insurance stated as an annual premium, and that this premium is likely significantly higher than a premium for property insurance purchased by the consumer; and (7) that the creditor-placed insurance may not provide as much coverage as homeowner's insurance. The Board solicits comment on whether the notice should also contain statements, if applicable, that the creditor will receive compensation for obtaining creditor-placed property insurance and that the creditor will establish an escrow account to pay for the creditor-placed insurance premium. Although such statements would be informative, the Board is concerned that providing these additional disclosures could result in information overload for the consumer. A Model Clause is proposed at Appendix H–18.

The Board proposes to use its authority under TILA Section 105(a), 15 U.S.C. 1604(a), to add § 226.20(e) to require the creditor to provide notice before charging the consumer for the cost of creditor-placed property insurance. TILA Section 105(a), 15 U.S.C. 1604(a), authorizes the Board to prescribe regulations to carry out the purposes of the act. TILA's purpose includes promoting ''the informed use of credit,'' which ''results from an awareness of the cost thereof by consumers.'' TILA Section 102(a), 15 U.S.C. 1601(a). Currently, few consumers are aware of the cost or coverage of creditor-placed property insurance, or that the premiums become additional debt of the consumer. The Board believes that this proposed rule would inform consumers of the cost and coverage of the creditor-placed property insurance and avoid the uninformed use of credit. In addition, this proposed rule would not prohibit the creditor from charging for creditor-placed property insurance, but would simply delay the charge until the consumer has been provided sufficient notice of the cost and sufficient time to shop for his or her own homeowner's insurance.

Section 226.25 Record Retention

25(a) General Rule

Section 226.25(a) provides that creditors must retain records to evidence compliance with Regulation Z for two years. As discussed in detail below, the Board is proposing to add a new comment to § 226.25(a) to provide guidance on record retention requirements relating to proposed § 226.36(d)(1), which would prohibit any person from paying compensation to a loan originator based on any of the terms or conditions of the transaction. Proposed comment 25(a)–5 would provide that, to evidence compliance with proposed § 226.36(d)(1), a creditor must retain for each covered transaction a record of the agreement between it and the loan originator that governs the originator's compensation and a record of the amount of compensation actually paid to the originator in connection with the transaction.

Section 226.27 Language of Disclosures

Currently, § 226.27, permits TILA disclosures in a language other than English as long as the disclosures are provided in English upon the consumer's request. Many consumers do not speak English or speak English as a second language. According to the 2000 Census, at least 18% of the population (47 million people) speak a language other than English at home.[56] To protect non-native English speakers from fraud and discrimination in credit transactions, recent enforcement actions have required that creditors or mortgage brokers provide translations of presentations, disclosures, or documents.[57] Moreover, several states

[54] *See* Ark. Code Ann. § 23–101–113 (2008); Mich. Comp. Laws § 500.1625 (2009); Miss. Code Ann. § 83–54–25 (2008); Tenn. Code Ann. § 56–49–113 (2009).

[55] Fannie Mae Single-Family Servicing Guide, Part II, Ch. 6 Lender-Placed Property Insurance (2005).

[56] U.S. Census Bureau, *Language Use and English-Speaking Ability: 2000* at 2 (Oct. 2003), *available at http://www.census.gov/prod/2003pubs/c2kbr-29.pdf.*

[57] *See, e.g., In the Matter of First Mariner Bank, Baltimore, Maryland,* FDIC–07–285b, FDIC–08–

have enacted laws to require credit disclosures or documents in Spanish or other foreign languages.[58] In 2006, Fannie Mae and Freddie Mac announced the availability of non-executable Spanish translations of the Fannie Mae/Freddie Mac Uniform Instrument to help the residential mortgage industry better serve Spanish-speaking consumers.[59] Finally, Congress recently asked the General Accounting Office to conduct a study examining the relationship between fluency in English and financial literacy, and the extent, if any, to which individuals whose native language is not English are impeded in the conduct of their financial affairs.[60]

Consumer advocates are concerned that consumers who do not speak English or speak English as a second language may be more susceptible to abusive credit practices or offered less favorable credit terms or products because they are not provided with disclosures they can understand. Industry representatives, on the other hand, raise concerns about the cost and burden of translating documents into multiple foreign languages and the potential liability for inaccurate translations. Both consumer advocates and industry representatives question whether consumers who speak minority languages will still have access to credit if creditors have to bear the cost and liability for translating documents into little-known languages. Creditors may be reluctant to engage in outreach to consumers who speak those languages.

The Board solicits comment on whether it should use its rulemaking authority to require creditors to provide translations of credit disclosures. Comment is requested on whether the failure to provide credit disclosure translations is unfair or deceptive, or impedes the informed use of credit. Comment is also requested on potential litigation issues, such as whether a translation would be admissible into evidence or whether an inaccurate translation would toll TILA's statute of limitations or extend the right of rescission. Finally, comment is requested on the effectiveness of State laws that require translations of disclosures or documents and whether the Board should adopt similar regulations.

The Board requests comment on the following translation issues:

- What is the scope of the problem? That is, approximately how many consumers do not understand TILA disclosures because of language barriers?
- Should creditors be required to provide consumers with translations of required TILA disclosures? If such translations were required, what should be the trigger for such disclosures (*e.g.,* the language of the negotiation, the language of the creditor's presentation, the language of the creditor's advertisement, a consumer request)?
- Should there be an exception for consumers who are accompanied by an interpreter?
- Would a translation requirement negatively affect consumers and the type and terms of credit offered because creditors would be reluctant to risk liability for engaging in transactions in a language other than English?

Finally, the Board solicits comment on the following coverage issues:

- Should a translation requirement apply only to mortgages loans, or also to other types of credit products, such as auto loans or credit cards?
- Should a translation requirement apply only to the TILA disclosures provided before or at consummation, or to any credit disclosures or documents provided before, at, or subsequent to consummation?
- Should a translation requirement apply to Web sites that provide early TILA disclosures?
- Should a translation requirement apply only to one or a few languages, or should it apply to any foreign language?

Section 226.32 Requirements for Certain Closed-End Mortgages

32(b) Definitions

32(b)(1)

Section 226.32(b)(1) defines the ''point and fees'' used to determine whether a loan is a HOEPA loan. That definition consists of four elements: (i) All items required to be disclosed under § 226.4(a) and 226.4(b), except interest or the time-price differential; (ii) All compensation paid to mortgage brokers; (iii) All items listed in § 226.4(c)(7) (other than amounts held for future payment of taxes) unless the charge is reasonable, the creditor receives no direct or indirect compensation in connection with the charge, and the charge is not paid to an affiliate of the creditor; and (iv) Premiums or other charges for credit life, accident, health, or loss-of-income insurance, or debt-cancellation coverage (whether or not the debt-cancellation coverage is insurance under applicable law) that provides for cancellation of all or part of the consumer's liability in the event of the loss of life, health, or income or in the case of accident, written in connection with the credit transaction. In light of the changes to the finance charge under proposed § 226.4, discussed above, the Board is proposing technical amendments to this provision.

The reference to ''items required to be disclosed under § 226.4(a) and 226.4(b), except interest or the time-price differential'' in § 226.32(b)(1)(i) implements TILA Section 103(aa)(4)(A). That provision includes in points and fees ''all items included in the finance charge, except interest or the time-price differential.'' 15 U.S.C. 1602(aa)(4)(A). Thus, ''items required to be disclosed under § 226.4(a) and 226.4(b)'' is intended to capture the finance charge. Section 226.32(b)(1)(ii) and (iii) parallel the additional elements in TILA Section 103(aa)(4)(B) and (C). *See* 15 U.S.C. 1602(aa)(4)(B) and (C). Finally, TILA Section 103(aa)(4)(D) provides for the inclusion of such other charges as the Board determines to be appropriate. 15 U.S.C. 1602(aa)(4)(D). Pursuant to that authority, in § 226.32(b)(1)(iv), the Board included credit insurance premiums and debt cancellation coverage fees. Thus, the statutory definition reflects Congress's intent to

358k, Consent Agreement at 5 (April 22, 2009) (alleging that the bank discriminated against Hispanics, African-Americans, and women by charging them higher prices for residential mortgage loans and requiring the bank to provide financial literacy courses in English and Spanish); *Fed. Trade Comm'n* v. *MortgagesParaHispanos.com and Daniel Moises Goldberg,* Civ. Action No. 4:06cv19, Final Judgment and Order at 5 (E.D. Tex. Sept. 27, 2006) (alleging that the mortgage broker misrepresented the mortgage terms to Spanish-speaking consumers and requiring the broker to provide a disclosure and consumer education brochure in Spanish to any consumer if they have reason to believe that the consumer's primary language is Spanish); *In re Ameriquest Mortgage Co., et al.,* Settlement Agreement at 17–18 (Jan. 23, 2006) (requiring documents and disclosures to be translated to Spanish or to any language in which Ameriquest advertises).

[58] Ariz. Rev. Stat. § 6–631 (requiring a consumer loan lender to provide a notice in English and Spanish that the consumer may request the TILA disclosure in Spanish); Cal. Civ. Code § 1632 (requiring any person engaged in a trade or business who negotiates certain transactions primarily in Spanish, Chinese, Tagalog, Vietnamese, or Korean to deliver a translation of the contract in the language in which the contract was negotiated); DC Code Ann. § 26–1113 (requiring a post-application mortgage disclosure to be provided in the language of the mortgage lender's presentation to the borrower); 815 Ill. Comp. Stat. Ann. 122/2–20 (requiring payday lenders to provide consumers with a written disclosure in English and in the language in which the loan was negotiated); Tex. Fin. Code Ann. § 341.502 (requiring that the TILA disclosure be provided in Spanish if the terms for the consumer loan, retail installment transaction, or home equity loan were negotiated in Spanish).

[59] News Release, *Fannie Mae and Freddie Mac Offer Mortgage Documents in Spanish to Aid Lenders and Industry Partners with Helping More Hispanics Become Homeowners; Collaborative Effort Aimed at Helping Close the Hispanic and Overall Minority Homeownership Gaps* (Sept. 25, 2006), *available at http://www.fanniemae.com/newsreleases/2006/3803.jhtml?p=Media&s=News+Releases.*

[60] Credit CARD Act of 2009, Public Law 111–24, § 513, 123 Stat. 1734, 1765 (2009).

include in points and fees mortgage broker compensation, certain real-estate related fees, and the insurance charges added by the Board, even if those items would be excluded from the finance charge under other applicable rules.

Under TILA Section 103(aa)(1), HOEPA applies to certain transactions that are secured by a consumer's principal dwelling. 15 U.S.C. 1602(aa)(1). Proposed § 226.4(g), and therefore the more inclusive definition of finance charge it would create, would apply to any transaction secured by real property or a dwelling. Consequently, all loans that are potentially subject to HOEPA would be subject to the proposed ''but for'' finance charge definition. Under that definition, the items included under the points and fees definition in addition to the finance charge (other than interest or the time-price differential) would never be excluded from the finance charge for transactions secured by real property or a dwelling.

The Board believes that proposed § 226.4 would render § 226.32(b)(1)(ii) through (iv) unnecessary because all items included in points and fees under those provisions already would be included as part of the finance charge. To eliminate unnecessary complexity, the Board proposes to streamline § 226.32(b)(1) by deleting those additional elements. The Board also proposes to revise § 226.32(b)(1) to provide that points and fees means all items included in the finance charge pursuant to § 226.4, except interest or the time-price differential, instead of § 226.32(b)(1)(i)'s reference to ''items required to be disclosed under § 226.4(a) and 226.4(b).'' This change would reflect the language of TILA more closely and is not meant to effect any substantive change to HOEPA's coverage.

32(c) Disclosures

32(c)(1) Notices

For HOEPA loans, TILA Sections 129(a)(1)(A) and (B), 15 U.S.C. 1639(a)(1)(A) and (B), and § 226.32(c)(1), require the creditor to provide the following disclosures in conspicuous type size: ''You are not required to complete this agreement merely because you have received these disclosures or have signed a loan application. If you obtain this loan, the lender will have a mortgage on your home. You could lose your home, and any money you have put into it, if you do not meet your obligations under the loan.'' The first sentence is a ''no obligation'' statement to inform the consumer that the space for the consumer's signature that may be on the credit application does not obligate the consumer to accept the terms of the loan. The next two sentences are ''security interest'' disclosures to inform the consumer of the potential consequences when the creditor takes a security interest in the consumer's home. Comment 32(c)(1)–1 states that these disclosures need not be in a particular format or part of the note or mortgage document. A Model Clause is currently provided at Appendix H–16.

As discussed more fully in § 226.38(f)(1), the MDIA amended TILA Section 128(b)(2), 15 U.S.C. 1638(b)(2), to require the creditor to provide the following ''no obligation'' statement on the TILA disclosure: ''You are not required to complete this agreement merely because you have received these disclosures or signed a loan application.'' Based on consumer testing, the Board proposes to use its adjustments and exception authority under TILA Section 105(a), 15 U.S.C. 1604(a), to modify the specific wording on the disclosure. Proposed § 226.38(f)(1) would require the creditor to provide a statement that the consumer has no obligation to accept the loan, and, if the creditor provides space for a consumer's signature, a statement that a signature by the consumer only confirms receipt of the disclosure statement. During consumer testing, participants' comprehension improved when they reviewed the plain-language version of the clause.

Similarly, based on consumer testing, the Board proposes to use its adjustments and exception authority under TILA Section 105(a), 15 U.S.C. 1604(a), to require the creditor under proposed § 226.32(c)(1) to provide the following ''no obligation'' statement in connection with a HOEPA loan: ''You have no obligation to accept this loan. Your signature below only confirms that you have received this form.'' TILA Section 105(a), 15 U.S.C. 1604(a), states that the Board ''may provide for such adjustments * * * as in the judgment of the Board are necessary or proper to effectuate the purposes of [TILA]''. One of the purposes of TILA is to promote the informed use of credit. TILA Section 102(a), 15 U.S.C. 1601(a). Consumer testing showed that the ''no obligation'' language improved participants' understanding of the key point that signing or accepting a disclosure did not obligate the consumer to accept the terms of the loan.

In addition, the Board proposes to use its adjustments and exception authority under TILA Section 105(a), 15 U.S.C. 1604(a), to require the creditor under proposed § 226.32(c)(1) to provide the following ''security interest'' statement in connection with a HOEPA loan: ''If you are unable to make the payments on this loan, you could lose your home.'' As discussed more fully in § 226.38(f)(2), consumer testing showed that participant comprehension of this disclosure improved when the plain-language version of the ''security interest'' disclosure was used. The Board believes that the plain-language versions of the ''no obligation'' and ''security interest'' disclosures will better inform consumers who are considering obtaining HOEPA loans.

The proposal would delete comment 32(c)(1)–1 and require these statements to be in bold text and a minimum 10-point font, consistent with proposed §§ 226.37 and 226.38. A revised Model Clause is proposed at Appendix H–16.

32(c)(5) Amount Borrowed

For HOEPA mortgage refinancing loans, § 226.32(c)(5) requires the creditor to disclose the amount borrowed, and states that ''where the amount borrowed includes premiums or other charges for optional credit insurance or debt-cancellation coverage, that fact shall be stated, grouped together with the disclosure of the amount borrowed.'' In the December 2008 Open-End Final Rule, the existing rules for credit insurance and debt cancellation coverage were applied to debt suspension coverage for purposes of excluding a charge for debt suspension coverage from the finance charge. *See* 74 FR 5244, 5255; Jan. 29, 2009. In the final rule, the Board stated that ''[d]ebt cancellation coverage and debt suspension coverage are fundamentally similar to the extent they offer a consumer the ability to pay in advance for the right to reduce the consumer's obligations under the plan on the occurrence of specified events that could impair the consumer's ability to satisfy those obligations.'' 74 FR 5266. The Board also noted that the two products are different because debt cancellation coverage cancels the debt while debt suspension merely suspends payment of the debt. *Id.* Despite this difference, the Board adopted a final rule treating the two products the same for purposes of the finance charge, but adding a special disclosure warning consumers of the risks of debt suspension coverage. *Id.* Consistent with this approach, the Board proposes to treat debt suspension coverage in the same manner as debt cancellation coverage for purposes of the disclosing the amount borrowed for a HOEPA mortgage refinancing loan. The Board proposes to revise § 226.32(c)(5) to clarify that where the amount borrowed includes charges for debt suspension coverage, that fact should be stated, grouped together with the disclosure of the amount borrowed. Proposed comment 32(c)(5)–1 would also be revised to include a reference to debt suspension coverage. Comment is solicited on this approach.

Section 226.35 Prohibited Acts or Practices in Connection With Higher-Priced Mortgage Loans

35(a) Higher-Priced Mortgage Loans

35(a)(2)

In its final rule implementing new requirements for higher-priced mortgage loans, 73 FR 44522; July 30, 2008, the Board adopted the ''average prime offer rate'' as the benchmark for coverage of new § 226.35. In so doing, the Board adopted commentary under new § 226.35(a)(2) regarding the calculation of the average prime offer rate and related guidance. Comment 35(a)(2)–4 indicated that the Board publishes average prime offer rates and the methodology for their calculation on the Internet. The Board is proposing to amend comment 35(a)(2)–4 to specify where on the Internet the table and methodology may be found (*http://www.ffiec.gov/hmda*).

The Board also is proposing new comment 35(a)(2)–5 to provide additional guidance on determination of applicable average prime offer rates for purposes of § 226.35. The comment would clarify that the average prime offer rate is defined identically under § 226.35 and under Regulation C (HMDA), 12 CFR 203.4(a)(12)(ii). Thus, for purposes of both coverage of § 226.35 and coverage of the rate spread reporting requirement under Regulation C, 12 CFR 203.4(a)(12)(i), the applicable average prime offer rate is identical. The comment would clarify further that guidance on the applicable average prime offer rate is provided in the staff commentary under Regulation C, the Board's *A Guide to HMDA Reporting: Getting it Right!*, and the relevant ''Frequently Asked Questions'' on HMDA compliance posted on the FFIEC's Web site referenced above.

Section 226.36 Prohibited Acts or Practices in Connection With Credit Secured by Real Property or a Consumer's Dwelling

The Board proposes to amend § 226.36 to extend the scope of the section's coverage to all closed-end transactions secured by real property or a dwelling. Currently, this section applies to closed-end credit transactions secured by a consumer's principal dwelling. As revised, § 226.36 would apply to closed-end transactions secured by any dwelling, not just a consumer's principal dwelling. This approach would be consistent with recent amendments to the TILA effected by the MDIA.

36(a) Loan Originator and Mortgage Broker Defined

As discussed below in more detail, the Board proposes to prohibit certain payments to loan originators that are based on a transaction's terms and conditions, and also proposes to prohibit loan originators from ''steering'' consumers to transactions that are not in their interest in order to increase the originator's compensation. Accordingly, the Board proposes to amend the regulation to provide a definition of ''loan originator'' in § 226.36(a)(1), which would include persons who are covered by the current definition of mortgage broker but also would include employees of the creditor, who are not considered ''mortgage brokers.'' Existing § 226.36(a) defines the term ''mortgage broker'' because mortgage brokers are subject to the prohibition on coercion of appraisers in § 226.36(b). A revised definition of mortgage broker would be designated as § 226.36(a)(2). The provision of existing § 226.36(a) stating that a creditor making a ''table funded'' transaction is considered a mortgage broker would be revised for clarity; no substantive change is intended other than the expansion of the definition from mortgage broker to loan originator. Thus, under proposed § 226.36(a)(1), a creditor that does not provide the funds for the transaction at consummation out of its own resources, out of deposits held by it, or by drawing on a bona fide warehouse line of credit would be considered a loan originator for purposes of § 226.36.

36(b) and (c) Misrepresentation of Value of Consumer's Dwelling; Servicing Practices

The Board proposes to amend § 226.36(b) and (c) to reflect the expanded scope of coverage of § 226.36, as noted above. Existing § 226.36(b) prohibits creditors and mortgage brokers and their affiliates from coercing, influencing, or otherwise encouraging appraisers to misstate or misrepresent the value of the consumer's principal dwelling in connection with a closed-end mortgage transaction. Section 226.36(c) currently prohibits certain practices of servicers of closed-end consumer credit transactions secured by a consumer's principal dwelling. Under this proposal, the rules relating to appraiser coercion and loan servicing would apply to all closed-end transactions secured by real property or a dwelling, for the reasons discussed above.

36(d) Prohibited Payments to Loan Originators

The Board is proposing to use its authority in HOEPA to prohibit unfair or deceptive acts or practices in mortgage lending to restrict certain practices related to the payment of loan originators. *See* TILA Section 129(*l*)(2)(A), 15 U.S.C. 1639(*l*)(2)(A). For this purpose, a ''loan originator'' includes both mortgage brokers and employees of creditors who perform loan origination functions.

Specifically, to address the potential unfairness that can arise with certain loan originator compensation practices, the proposed rule would prohibit a creditor or other party from paying compensation to a loan originator based on the credit transaction's terms or conditions. This prohibition would not apply to payments that consumers make directly to a loan originator. However, if a consumer directly pays the loan originator, the proposed rule would prohibit the originator from also receiving compensation from any other party in connection with that transaction.

The Board is soliciting comment on an alternative that would allow loan originators to receive payments that are based on the principal loan amount, which is a common practice today. The Board is also soliciting comment on whether it should adopt a rule that seeks to prohibit loan originators from directing or ''steering'' consumers to loans based on the fact that the originator will receive additional compensation, unless that loan is in the consumer's interest. The Board is expressly soliciting comment on whether the rule would be effective in achieving the stated purpose. Comment is also solicited on the feasibility and practicality of such a rule, its enforceability, and any unintended adverse effects the rule might have. These proposals and alternatives are discussed more fully below.

Background

In the summer of 2006, the Board held public hearings on home equity lending in four cities. During the hearings, consumer advocates urged the Board to ban ''yield spread premiums,'' payments that mortgage brokers receive from the creditor at closing for delivering a loan with an interest rate that is higher than the creditor's ''buy rate.'' The consumer advocates asserted that yield spread premiums provide brokers an incentive to increase consumers' interest rates unnecessarily. They argued that a prohibition would align reality with consumers' perception that brokers serve consumers' best interests.

In light of the information received at the 2006 hearings and the rise in defaults that began soon after, the Board held an additional hearing in June of 2007 to explore how it could use its authority under HOEPA to prevent abusive lending practices in the subprime mortgage market while still preserving responsible lending. Although the Board did not expressly solicit comment on mortgage broker compensation in its notice of the June 2007 hearing, a number of commenters and some hearing panelists raised the topic. Consumer and creditor representatives alike raised concerns about the fairness and transparency of creditors' payment of yield spread premiums to brokers. Several commenters and panelists stated that consumers are not aware of the payments creditors make to brokers, or that such payments increase consumers' interest rates. They also stated that consumers may mistakenly believe that a broker seeks to obtain the best interest rate available. Consumer groups have expressed particular concern about increased payments to brokers for delivering loans both with higher interest rates and prepayment penalties. Consumer groups suggested a variety of solutions, such as prohibiting creditors paying brokers yield spread premiums, imposing on brokers that accept yield spread premiums a fiduciary duty to consumers, imposing on creditors that pay yield spread premiums liability for broker misconduct, or including yield spread premiums in the points and fees test for loans subject to HOEPA. Several creditors and creditor trade associations advocated requiring brokers to disclose whether the broker represents the consumer's interests, and how and by whom the broker is to be compensated. Some of these commenters recommended that brokers be required to disclose their total compensation to the consumer and that creditors be prohibited from paying brokers more than the disclosed amount.

To address these concerns, the Board's January 2008 proposed rule would have prohibited a creditor from paying a mortgage broker any compensation greater than the amount the consumer had previously agreed in writing that the broker would receive. 73 FR 1672, 1698–1700; Jan. 9, 2008 (HOEPA proposal). In support of the rule, the Board explained its concerns about yield spread premiums, which are summarized below.

A yield spread premium is the present dollar value of the difference between the lowest interest rate the wholesale lender would have accepted on a particular transaction and the interest rate the broker actually obtained for the lender. This dollar amount is usually paid to the mortgage broker, though it may also be applied to reduce the consumer's upfront closing costs. The creditor's payment to the broker based on the interest rate is an alternative to the consumer paying the broker directly from the consumer's preexisting resources or from loan proceeds. Preexisting resources or loan proceeds may not be sufficient to cover the broker's total fee, or may appear to the consumer to be a more costly way to finance those costs if the consumer expects to prepay the loan in a relatively short period. Thus, consumers potentially benefit from having an option to pay brokers for their services indirectly by accepting a higher interest rate.

The Board shares concerns, however, that creditors' payments to mortgage brokers are not transparent to consumers and are potentially unfair to them. Creditor payments to brokers based on the interest rate give brokers an incentive to provide consumers loans with higher interest rates. Some brokers may refrain from acting on this incentive out of legal, business, or ethical considerations. Moreover, competition in the mortgage loan market may often limit brokers' ability to act on the incentive. The market often leaves brokers room to act on the incentive should they choose, however, especially as to consumers who are less sophisticated and less likely to shop among either loans or brokers.

Large numbers of consumers are simply not aware the incentive exists. Many consumers do not know that creditors pay brokers based on the interest rate, and the current legally required disclosures seem to have only limited effect. Some consumers may not even know that creditors pay brokers: A common broker practice of charging a small part of its compensation directly to the consumer, to be paid from the consumer's existing resources or loan proceeds, may lead consumers to believe, incorrectly, that this amount is all the consumer will pay or that the broker will receive. Consumers who do understand that the creditor pays the broker based on the interest rate may not fully understand the implications of the practice. They may not appreciate the full extent of the incentive the practice gives the broker to increase the rate because they do not know the dollar amount of the creditor's payment.

Moreover, consumers often wrongly believe that brokers have agreed, or are required, to obtain the best interest rate available. Several commenters in connection with the 2006 hearings suggested that mortgage broker marketing cultivates an image of the broker as a ''trusted advisor'' to the consumer. Consumers who have this perception may rely heavily on a broker's advice, and there is some evidence that such reliance is common. In a 2003 survey of older borrowers who had obtained prime or subprime refinancings, majorities of respondents with refinance loans obtained through both brokers and creditors' employees reported that they had relied ''a lot'' on their loan originators to find the best mortgage for them.[61] The Board's recent consumer testing also suggests that many consumers shop little for mortgages and often rely on one broker or lender because of their trust in the relationship.

If consumers believe that brokers protect consumers' interests by shopping for the lowest rates available, then consumers will be less likely to take steps to protect their interests when dealing with brokers. For example, they may be less likely to shop rates across retail and wholesale channels simultaneously to assure themselves the broker is providing a competitive rate. They may also be less likely to shop and negotiate brokers' services, obligations, or compensation upfront, or at all. For example, they may be less likely to seek out brokers who will promise in writing to obtain the lowest rate available.

In response to these concerns, the 2008 HOEPA proposal would have prohibited a creditor from paying a broker more than the consumer agreed in writing to pay. Under the proposal, the consumer and mortgage broker would have had to enter into a written agreement before the broker accepted the consumer's loan application and before the consumer paid any fee in connection with the transaction (other than a fee for obtaining a credit report). The agreement also would have disclosed (i) that the consumer ultimately would bear the cost of the entire compensation even if the creditor paid part of it directly; and (ii) that a creditor's payment to a broker could influence the broker to offer the consumer loan terms or products that would not be in the consumer's interest

[61] *See* Kellie K. Kim-Sung & Sharon Hermanson, *Experiences of Older Refinance Mortgage Loan Borrowers: Broker- and Lender-Originated Loans*, Data Digest No. 83 (AARP Public Policy Inst., Washington, DC, Jan. 2003, at 3, available at *http://assets.aarp.org/rgcenter/post-import/dd83_loans.pdf*.

or the most favorable the consumer could obtain.

Based on the Board's analysis of comments received on the HOEPA proposal, the results of consumer testing, and other information, the Board withdrew the proposed provisions relating to broker compensation. 73 FR 44522, 44563–65; July 30, 2008. The Board's withdrawal of those provisions was based on its concern that the proposed agreement and disclosures could confuse consumers and undermine their decision-making rather than improve it. The risks of consumer confusion arose from two sources. First, an institution can act as either creditor or broker depending on the transaction. At the time the agreement and disclosures would have been required, such an institution could be uncertain as to which role it ultimately would play. This could render the proposed disclosures inaccurate and misleading in some, and possibly many, cases. Second, the Board was concerned by the reactions of consumers who participated in one-on-one interviews about the proposed agreement and disclosures as part of the Board's consumer testing. These consumers often concluded, not necessarily correctly, that brokers are more expensive than creditors. Many also believed that brokers would serve their best interests notwithstanding the conflict resulting from the relationship between interest rates and brokers' compensation.[62] The proposed disclosures presented a significant risk of misleading consumers regarding both the relative costs of brokers and lenders and the role of brokers in their transactions.

In withdrawing the broker compensation provisions of the HOEPA proposal, the Board stated it would continue to explore options to address potential unfairness associated with loan originator compensation arrangements, such as yield spread premiums. The Board indicated it would consider whether disclosures or other approaches could effectively remedy this potential unfairness without imposing unintended consequences.

Potential for Unfairness in Loan Originator Compensation Practices

As noted above, the Board is now proposing rules to prohibit certain practices relating to payments made to compensate mortgage brokers and other loan originators. These rules would be adopted pursuant to the Board's authority under HOEPA, as contained in TILA Section 129(*l*), which authorizes the Board to prohibit acts or practice in connection with mortgage loans that the Board finds to be unfair or deceptive. As discussed in part IV above, in considering whether a practice is unfair or deceptive under TILA Section 129(*l*), the Board has generally relied on the standards that have been adopted for purposes of Section 5(a) of the FTC Act, 15 U.S.C. 45(a), which also prohibits unfair and deceptive acts and practices.

For purposes of the FTC Act, an act or practice is considered unfair when it causes or is likely to cause substantial injury to consumers that is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition. As explained below, the practice of basing a loan originator's compensation on the credit transaction's terms or conditions appears to meet these standards and constitute an unfair practice. Furthermore, based on its experience with consumer testing, particularly in connection with the HOEPA proposal, the Board believes that disclosure alone would be insufficient for most consumers to avoid the harm caused by this practice. Thus, the Board is proposing a rule that would remedy the practice through substantive regulations that prohibit particular practices.

Specifically, under proposed § 226.36(d)(1), compensation payments made to a mortgage broker or any other loan originator based on a mortgage transaction's terms or conditions would be prohibited. Unlike the 2008 HOEPA proposal, the rule would also apply to creditors' employees who originate loans. As noted above, such payments when made to a mortgage broker are commonly referred to as yield spread premiums. There are analogous payments made by creditors to their employees who originate loans at a higher interest rate than the minimum rate required by the creditor. This arrangement is frequently referred to as an ''overage.'' For convenience, the discussion below uses the term ''yield spread premium'' also to refer to these types of payments, which would be covered by the proposed rule as well.

Substantial injury. When loan originators receive compensation based on a transaction's terms and conditions, they have an incentive to provide consumers loans with higher interest rates or other less favorable terms. Yield spread premiums, therefore, present a significant risk of economic injury to consumers. Currently, such injury is common because consumers typically are not aware of the practice or do not understand its implications and cannot effectively negotiate its use.

Creditors' payments to mortgage brokers or their own employees that originate loans (''loan officers'') generally are not transparent to consumers. Brokers may impose a direct fee on the consumer which may lead consumers to believe that this is the sole source of the broker's compensation. While consumers expect the creditor to compensate its own loan officers, they do not necessarily understand that the loan originator may have the ability to increase the creditor's interest rate or include certain loan terms for the originator's own gain.

To guard effectively against this practice, a consumer would have to know the lowest interest rate the creditor would have accepted to ascertain that the offered interest rate represents a rate increase by the loan originator. Most consumers will not know the lowest rate the creditor would be willing to accept. The consumer also would need to understand the dollar amount of the yield spread premium that is generated by the rate increase to determine what portion, if any, is being applied to reduce the consumer's upfront loan charges. Although HUD recently adopted disclosures in Regulation X, implementing RESPA, that could enhance some consumers' understanding of mortgage broker compensation, the details of the compensation arrangements are complex and the disclosures are limited. A creditor may show the yield spread premium as a credit to the borrower that is applied to cover upfront costs, but is also permitted to add the amount of the yield spread to the total origination charges being disclosed. This would not necessarily inform the consumer that the rate has been increased by the originator and that a lower rate with a smaller origination charge was also available. In addition, the Regulation X disclosure concerning yield spread premiums would not apply to overages occurring when the loan originator is employed by the creditor. Thus, the Regulation X disclosure, while perhaps an improvement over previous rules, is not likely by itself to prevent consumers from incurring substantial injury from the practice.

Because consumers generally do not understand the yield spread premium mechanism, they are unable to engage in effective negotiation. Instead they are more likely to rely on the loan originator's advice and frequently obtain a higher rate or other unfavorable terms

[62] For more details on the consumer testing, see the report of the Board's contractor, Macro International, Inc., *Consumer Testing of Mortgage Broker Disclosures* (July 10, 2008), available at *http://www.federalreserve.gov/newsevents/press/bcreg/20080714regzconstest.pdf.*

solely because of greater originator compensation. These consumers suffer substantial injury by incurring greater costs for mortgage credit than they would otherwise be required to pay.

Injury not reasonably avoidable. Yield spread premiums create a conflict of interest between the loan originator and consumer. As noted above, many consumers are not aware of creditor payments to loan originators, especially in the case of mortgage brokers, because these arrangements lack transparency. Although consumers may reasonably expect creditors to compensate their own employees, consumers do not know how the loan officer's compensation is structured or that the loan officer can increase the creditor's interest rate or offer certain loan terms to increase their own compensation. Without this understanding, consumers cannot reasonably be expected to appreciate or avoid the risk of financial harm these arrangements represent.

Yield spread premiums are complex and may be counter-intuitive even to well-informed consumers. Based on the Board's experience with consumer testing, the Board believes that disclosures are insufficient to overcome the gap in consumer comprehension regarding this critical aspect of the transaction. Currently, the required disclosures of originator compensation under federal and State laws seem to have little, if any, effect on originators' incentive to provide consumers with increased interest rates or other unfavorable loan terms, such as a prepayment penalty, that can increase the originator's compensation.[63] The Board's consumer testing, discussed above, supported the finding that disclosures about yield spread premiums are ineffective; consumers in these tests did not understand yield spread premiums and did not grasp how they create an incentive for loan originators to increase consumers' costs.

Consumers' lack of comprehension of yield spread premiums is compounded where the originator also imposes a direct charge on the consumer. A mortgage broker might charge the consumer a direct fee, for example $500, for arranging the consumer's mortgage loan. This charge encourages consumers to infer that the broker accepts the consumer-paid fee to represent the consumer's financial interests. Consumers may believe that the fee they pay is the originator's sole compensation. This may lead reasonable consumers to believe, erroneously, that loan originators are working on their behalf and are under a legal or ethical obligation to help consumers obtain the most favorable loan terms and conditions. There is evidence that consumers often regard loan originators as ''trusted advisors'' or ''hired experts'' and consequently rely on originators' advice. Consumers who regard loan originators in this manner are far less likely to shop or negotiate to assure themselves that they are being offered competitive mortgage terms. Even for consumers who shop, the lack of transparency in originator compensation arrangements makes it unlikely consumers will avoid yield spread premiums that unnecessarily increase the cost of their loan.

Consumers generally lack expertise in complex mortgage transactions because they engage in such mortgage transactions infrequently. Their reliance on the loan originator is reasonable in light of the originator's greater experience and professional training in the area, the belief that originators are working on their behalf, and the apparent ineffectiveness of disclosures to dispel that belief.

Injury not outweighed by benefits to consumers or to competition. Yield spread premiums can represent a potential consumer benefit in cases where the amount is applied to reduce consumers' upfront closing costs, including originator compensation. A creditor's increase in the interest rate (or the addition of other loan terms) may be used to generate additional income that the creditor uses to compensate the originator, in lieu of adding origination points or fees that the consumer would be required to pay directly from the consumer's preexisting funds or the loan proceeds. This can benefit a consumer who lacks the resources to pay closing costs in cash, or who might have insufficient equity in the property to increase the loan amount to cover these costs. Further, some consumers prefer to fund closing costs, including origination fees, through a higher rate if the consumer expects to own the property or have the loan for a relatively short period, for example, less than five years. For those consumers who understand this trade-off there could be potential benefits. In such cases, however, the yield spread premium does not increase the amount of compensation paid by the creditor to the originator, who would receive the same amount whether the loan has a higher rate or a lower rate accompanied by higher upfront fees.

Nevertheless, without a clear understanding of yield spread premiums or effective disclosure, the majority of consumers are not equipped to police the market to ensure that yield spread premiums are in fact applied to reduce their closing costs, especially in the case of loan originator compensation. This would be particularly difficult because consumers are not likely to have any basis for determining a ''typical'' or ''reasonable'' amount for originator compensation. Accordingly, the Board is proposing a rule that prohibits any person from basing a loan originator's compensation on the loan's rate or terms but still affords creditors the flexibility to structure loan pricing to preserve the potential consumer benefit of compensating an originator through the interest rate.

The Board's Proposal

Under § 226.36(d)(1), the Board proposes to prohibit any person from compensating a loan originator, directly or indirectly, based on the terms or conditions of a loan transaction secured by real property or a dwelling. This prohibition would apply to any person, rather than only a creditor, to prevent evasion by structuring loan originator payments through non-creditors. For example, secondary market investors that purchase closed loans from creditors would not be permitted to pay compensation to loan originators that is based on the terms or conditions of their transactions.

Under the proposal, compensation that is based on the loan amount would be considered a payment that is based on a term or condition of the loan. The prohibition would not apply to consumers' direct payments to loan originators. Under § 226.36(d)(2), however, if the consumer compensates the loan originator directly, the originator would be prohibited from receiving compensation from the creditor or any other person.

Because the loan originator could not receive compensation based on the interest rate or other terms, the originator would have no incentive to alter the terms made available by the creditor to deliver a more expensive loan. For example, a company acting as a mortgage broker could not provide greater compensation to its employee acting as the loan originator for a transaction with a 7 percent interest rate than for a transaction with a 6 percent interest rate. A creditor would be under the same restriction in compensating its loan officer. For this purpose, the term ''compensation'' would not be limited to commissions, but would include

[63] Creditors may be willing to offer a loan with a lower interest rate in return for including a prepayment penalty. A loan originator that offers a loan with a prepayment penalty might not offer the lower rate, resulting in a premium interest rate and the payment of a yield spread premium.

salaries or any financial incentive that is tied to the transaction's terms or conditions, including annual or periodic bonuses or awards of merchandise or other prizes. *See* proposed comment 36(d)(1)–1.

Proposed comment 36(d)(1)–2 provides examples of compensation that is based on the transaction's terms or conditions, such as payments that are based on the interest rate, annual percentage rate, or the existence of a prepayment penalty. Examples of loan originator compensation that is not based on the transaction's terms or conditions are listed in proposed comment 36(d)(1)–3. These include compensation based on the originator's loan volume, the performance of loans delivered by the originator, or hourly wages.

The Board recognizes that loans originators may need to expend more time and resources in originating loans for consumers with limited or blemished credit histories. Because such loans are likely to carry higher rates, originators currently rely on higher yield spread premiums to compensate them for the additional time and efforts. Paying an originator based on the time expended would be permissible under the proposed rule.

Although the proposed rule would not prohibit a creditor from basing compensation on the originator's loan volume, such arrangements may raise concerns about whether it creates incentives for originators to deliver loans without proper regard for the credit risks involved. The Board expects creditors to exercise due diligence to monitor and manage such risks. Financial institution regulators generally will examine creditors they supervise to ensure they have systems in place to exercise such due diligence.

The proposed rule also would not prohibit compensation that differs by geographical area, but any such arrangements must comply with other applicable laws such as the Equal Credit Opportunity Act (15 U.S.C. 1691–1691f) and Fair Housing Act (42 U.S.C. 3601–3619). *See* proposed comment 36(d)(1)–4. Creditors that use geography as a criterion for setting originator compensation would need to be able to demonstrate that this reflects legitimate differences in the costs of origination and in the levels of competition for originators' services.

Under the proposed rule, creditors also may compensate their own loan officers differently than mortgage brokers. For instance, in light of the fact that mortgage brokers relieve creditors of certain overhead costs of loan originations, a creditor might pay brokers more than its own loan officers. Likewise, a creditor might pay one loan originator of either type more than it pays another, as long as each originator receives compensation that is not based on the terms of the transactions they deliver to the creditor.

Scope of coverage. The Board believes that the proposed rule should apply to creditors' employees who originate loans in addition to mortgage brokers. A creditor's loan officers frequently have the same discretion over loan pricing that mortgage brokers have to modify a loan's terms to increase their compensation, and there is evidence suggesting that loan officers engage in such practices.[64] Accordingly, the coverage of § 226.36(d)(1) is broader than the 2008 HOEPA proposal, which covered only mortgage brokers. Some commenters on the HOEPA proposal expressed concern that it would create an ''unlevel playing field'' by creating an unfair advantage for creditors that would not have to comply with the same requirements as brokers.

The proposed rule would apply to covered transactions whether or not they are higher-priced mortgage loans. A loan originator's financial incentive to deliver less favorable loan terms to a consumer could result in consumer injury whether or not the loan has a rate above the coverage threshold in § 226.35. The risks of harm could be reduced in the lower-priced segment of the market, however, where consumers historically have more choices. Comment is solicited on the relative costs and benefits of applying the rule to all segments of the market, and whether the costs would outweigh the benefits for loans below the higher-priced mortgage loan threshold.

Creditors' pricing flexibility. The proposed rule would not affect creditors' flexibility in setting rates or other loan terms. The rule does not limit the creditor's ability to adjust the loan terms it offers to consumers as a means of financing costs the consumer would otherwise be obligated to pay directly (in cash or out of the loan proceeds), including the originator's compensation, provided this does not affect the amount the originator receives for the transaction. Thus, a creditor could recoup costs by adding to the loan pricing terms an origination point (calculated as one percentage point of the loan amount) even though the creditor could not pay the originator's compensation on that basis. Similarly, a creditor could add a constant premium of, for instance, ¼ of one percent to the interest rates on all transactions for which the creditor will pay compensation to the loan originator, as a means of recouping the cost of the originator's compensation. The creditor would not recoup the same dollar amount in each transaction, however, because the present value of the premium in dollars would vary with the loan amount. Consequently, even though loan pricing could be set in this manner, this method could not be used to set the loan originator's compensation. *See* proposed comment 36(d)(1)–5.

Effect of modification of loan terms. The proposed rule is designed to prevent consumers from being harmed by loan originators making unfavorable modifications to loan terms, such as increasing the interest rate, to increase the originator's compensation. Currently, loan originators might also exercise discretion to make modifications in the consumer's favor. For example, to retain the consumer's business, today a loan originator might agree with the consumer to reduce the amount the consumer must pay in origination points on the loan, which would be funded by a reduction in the amount the originator receives from the creditor as compensation for delivering the loan. Under the proposed rule, however, a creditor would not be permitted to reduce the amount it pays to the loan originator based on such a change in loan terms. As a result, the reduction in origination points would be a cost borne by the creditor.

Thus, when the creditor offers to extend a loan with specified terms and conditions (such as the rate and points), the amount of the originator's compensation for that transaction is not subject to change, through either an increase or a decrease, even if different loan terms are negotiated. If this were not the case, a creditor generally could agree to compensate originators at a high level and then subsequently lower the compensation only in selective cases, such as when the consumer obtains a competing offer with a lower interest rate. This would have the same

[64] For example, the Federal Trade Commission's settlement with Gateway Funding, Inc. in December 2008 illustrates a case where a creditor's loan officers created ''overages,'' although the primary legal theory concerned disparate treatment by race in the imposition of overages. The FTC's complaint and the court's final judgment and order can be found on the FTC's web-site at *http://www.ftc.gov/os/caselist/0623063/index.shtm*. The FTC has since filed a complaint alleging similar patterns of overages in violation of fair lending laws, against Golden Empire Mortgage, Inc. The May 2009 complaint can be found at *http://www.ftc.gov/os/caselist/0623061/090511gemcmpt.pdf*. A similar pattern of overages was alleged in legal actions brought by the Department of Justice (DOJ), which resulted in settlement agreements with Huntington Mortgage Company (1995) and Fleet Mortgage Corp. (1996).

effect as increasing the originator's compensation for higher rate loans. Proposed comment 36(d)(1)–6 would address this issue.

Periodic changes in loan originator compensation. Under proposed § 226.36(d)(1) a creditor would not be prevented from periodically revising the compensation it agrees to pay a loan originator. However, a creditor may not revise a loan originator's compensation arrangement in connection with each transaction. This guidance is reflected in proposed comment 36(d)(1)–7. The revised compensation arrangement must result in payments to the loan originator that are not based on the terms or conditions of a credit transaction. A creditor might periodically review factors such as loan performance, transaction volume, as well as current market conditions for originator compensation, and prospectively revise the compensation it agrees to pay to a loan originator. For example, assume that during the first six months of the year, a creditor pays $3,000 to a particular loan originator for each loan delivered, regardless of the loan terms. After considering the volume of business produced by that originator, the creditor could decide that as of July 1, it will pay $3,250 for each loan delivered by that originator, regardless of the loan terms. The change in compensation would not be a violation even if the loans made by the creditor after July 1 generally carry higher interest rates than loans made before that date.

Alternative to permit compensation based on loan amount. The Board is also publishing for comment a proposed alternative that would allow loan originator compensation to be based on the loan amount, which would not be considered a transaction term or condition for purposes of the prohibition in § 226.36(d)(1). Currently, the compensation received by many mortgage originators is structured as a percentage of the loan amount. Other participants in the mortgage market, such as creditors, mortgage insurers, and other service providers, also receive compensation based on the loan amount. The Board is therefore seeking comment on whether prohibiting originator compensation on this basis might be unduly restrictive and unnecessary to achieve the purposes of the proposed rule.

On the other hand, prohibiting compensation based on the loan amount would eliminate an incentive for the originator to steer consumers to a larger loan amount. Such steering maximizes the originator's compensation but also increases the transaction's loan-to-value ratio and decreases the consumer's equity in the property. If the loan-to-value ratio increases sufficiently, the consumer may incur additional costs in the form of a higher interest rate or additional points and fees, including the cost of mortgage insurance premiums. Because the consumer's monthly payment would also be larger, the originator might direct the consumer to riskier loan products that have discounted initial rates but are subject to significant payment increases after the introductory period expires.

Because of the foregoing concerns, the Board is publishing two alternative versions of proposed § 226.36(d)(1). The first alternative would consider the loan amount as a term or condition of the loan, thereby prohibiting the payment of originator compensation as a percentage of the loan amount. The second alternative provides that the loan amount is not a term or condition of the loan, and would permit such payments. The second alternative would be accompanied by proposed comment 36(d)(1)–10 to provide further guidance. Under proposed comment 36(d)(1)–10, a loan originator could be paid a fixed percentage of the loan amount even though the dollar amount paid by a particular creditor would vary from transaction to transaction and would increase as the loan amount increases. Comment 36(d)(1)–10 also permits compensation paid as a fixed percentage of the loan amount to be subject to a specified minimum or maximum dollar amount. For example, a loan originator's compensation could be set at one percent of the principal loan amount but not less than $1,000 or greater than $5,000.

The Board seeks comment on the two alternatives. Further, if the final rule permits compensation based on the loan amount, should creditors be permitted to apply different percentages to loans of different amounts? Should creditors be allowed to pay a larger percentage for smaller loan amounts, which could be an incentive to originate loans in lower-priced neighborhoods that ensures that the originator receives an amount that is comparable to loans originated in high-priced neighborhoods? If so, should creditors also be permitted to pay originators a higher percentage for larger loan amounts?

Prohibition of compensation from both the consumer and another source. Proposed § 226.36(d)(2) would provide that, if a loan originator is compensated directly by the consumer for a transaction secured by real property or a dwelling, no other person may pay any compensation to the originator for that transaction. Direct compensation paid by a consumer to a loan originator would not be limited to ''origination fees,'' ''broker fees,'' or similarly labeled charges. Rather, compensation for this purpose includes any payment by the consumer that is retained by the loan originator. Thus, a creditor that is a loan originator by virtue of making a table funded transaction, as discussed above, would be subject to this prohibition if it imposes and retains any direct charge on the consumer for the transaction.

Consumers reasonably may believe that when they pay a loan originator directly, that amount is the only compensation the originator will receive. As discussed above, consumers generally are not aware of creditor payments to originators. If the consumer were aware of such payments, the consumer might reasonably expect that making a direct payment to an originator would reduce or eliminate the need for the creditor to fund the originator's compensation through the consumer's interest rate. Because the consumer is unaware of yield spread premiums, however, the consumer cannot effectively negotiate the originator's compensation. In fact, if consumers pay loan originators directly and creditors also pay originators through higher rates, consumers may be injured by unwittingly paying originators more in total compensation (directly and through the rate) than consumers believe they agreed to pay.

The Board believes that simply disclosing the yield spread premium would not address this injury to consumers. Consumer testing in connection with the Board's 2008 HOEPA Final Rule shows that, even with a disclosure, consumers do not understand how a creditor payment to a loan originator can result in a higher interest rate for the consumer. A disclosure therefore cannot inform consumers that they effectively are paying the loan originator more than they believe they agreed to pay. Without that knowledge, consumers cannot take steps to protect their own interests, such as by negotiating for a smaller direct payment, a lower rate, or both.

The Board also believes that this prohibition would increase transparency for consumers by requiring that all originator compensation come from the creditor or from the consumer, but not both. This additional consequence of proposed § 226.36(d)(2) would reduce the total number of loan pricing variables with which the consumer must contend. There is evidence that such simplification is consistent with TILA's purpose of promoting the informed use of consumer credit.[65] *See* TILA Section 102(a), 15 U.S.C. 1601(a).

Proposed § 226.36(d)(2) would prohibit only payments to an originator that are made in connection with the particular credit transaction, such as a commission for delivering the loan. The rule is not intended to prohibit payment of a salary to a loan originator who also receives direct compensation from a consumer in connection with that consumer's transaction. This guidance is contained in proposed comment 36(d)(2)–1.

Record retention requirements. Creditors are required by § 226.25(a) to retain evidence of compliance with Regulation Z for two years. Proposed staff comment 25(a)–5 would be added to clarify that, to demonstrate compliance with § 226.36(d)(1), a creditor must retain at least two types of records.

First, a creditor must have a record of the compensation agreement with the loan originator that was in effect on the date the transaction's rate was set. The Board believes this date is most likely when a loan originator's compensation was determined for a given transaction. The Board seeks comment, however, on whether some other time would be more appropriate, in light of the purposes of the proposed rule. Proposed comment 25(a)–5 would clarify that the rules in § 226.35(a) would govern in determining when a transaction's rate is set.

Second, proposed comment 25(a)–5 would state that a creditor must retain a record of the actual amount of compensation it paid to a loan originator in connection with each covered transaction. The proposed comment would clarify that, in the case of mortgage brokers, the HUD–1 settlement statement required under RESPA would be an example of such a record because it itemizes the compensation received by a mortgage broker. The Board solicits comment on whether any comparable record exists for loan officer compensation that should be referenced in proposed comment 25(a)–5. To facilitate compliance, a cross reference to the record retention requirement would be included in proposed comment 36(d)(1)–9.

The Board solicits comment on whether there are other records that should be subject to the retention requirements. The Board also seeks comment on whether the existing two-year record retention period is adequate for purposes of the rules governing loan originator compensation.

The current record retention requirements in § 226.25 apply only to creditors. Although loan originator compensation has historically been paid by creditors, the prohibitions in § 226.36(d) apply more broadly to any person to prevent evasion by restructuring of payments through non-creditors. Accordingly, the Board expects that payments to loan originators will continue to be made largely by creditors. The Board seeks comment on whether there is a need to adopt requirements for retaining records concerning originator compensation that would apply to persons other than creditors, including the relative costs and benefits of that approach.

36(e) Prohibition on Steering

Optional Proposal on Steering by Loan Originators

The Board is also soliciting comment on whether it should adopt a rule that seeks to prohibit loan originators from directing or ''steering'' consumers to loans based on the fact that the originator will receive additional compensation, when that loan may not be in the consumer's best interest. Under proposed § 226.36(d)(1), a loan originator would receive the same compensation from a particular creditor regardless of the transaction's rate or terms. That provision, however, would not prohibit a loan originator from directing a consumer to transactions from a single creditor that offers greater compensation to the originator, while ignoring possible transactions having lower interest rates that are available from other creditors.

Attempting to address this issue presents difficulties. Determining whether a loan originator was warranted in directing a consumer to a loan that resulted in greater compensation for the originator also involves a determination of whether that loan was in the consumer's best interest compared to other available loan products. There is, however, no uniform method for making that evaluation. Consumers and loan originators may choose from among possible loan offers for a variety of reasons. The annual percentage rate (APR) is a tool that facilitates comparison shopping among different loans, but it is imperfect for reasons that are well documented, including the fact that the APR is calculated by amortizing origination fees over the full loan term rather than the expected life of the loan. *See* the 1998 Joint Report to the Congress by the Board and HUD, cited above. In considering interest rates, consumers may view the economic trade-off between rates and points differently depending on their individual financial circumstances or the amount of time they expect to hold the loan. Moreover, consumers evaluate other factors in deciding whether a loan is in their best interest even if it is not represented as the lowest cost option among the possible loan offers available through the originator. Thus, some consumers may reasonably determine that the financial risk created by a loan's prepayment penalty is acceptable in light of the loan's lower interest rate, while other consumers may prefer to accept a higher rate to avoid the risk. Consumers and loan originators also may consider factors other than loan cost, such as the creditor's rate lock-in policies, or the creditor's reputation for delivering loans within the promised time-frame, especially for home-purchase loans.

The Board believes, however, that there is benefit in attempting to craft a rule that prohibits and deters the most egregious practices, even if such a rule cannot ensure that consumers always obtain the lowest cost loan. Under the proposal, a loan originator would have a duty not to steer a consumer to higher cost loans that pay more to the originator when the loan is not in the consumer's interest. Originators would violate the rule, for example, if they directed the consumer to a fixed-rate loan option from a creditor that maximizes the originator's compensation without providing the consumer with an opportunity to choose from other available loans that have lower fixed interest rates with the equivalent amount in origination and discount points.

The Board is publishing a proposal, designated as proposed § 226.36(e)(1), to reflect this optional approach. Specifically, the rule would prohibit loan originators from directing or ''steering'' a consumer to consummate a transaction secured by real property or a dwelling that is not in the consumer's interest, based on the fact that the originator will receive greater compensation from the creditor in that transaction than in other transactions the originator offered or could have offered to the consumer. The proposed rule seeks to preserve consumer choice by ensuring that consumers have appropriate loan options that reflect considerations other than the maximum amount of compensation that will be paid to the originator. Proposed comments 36(e)(1)–1 through –3 would provide additional guidance on the rule.

[65] *See, e.g.*, Woodward, Susan E., *A Study of Closing Costs for FHA Mortgages* at 70–73 (Urban Institute and U.S. Department of Housing and Urban Development 2008), available at *http://www.urban.org/UploadedPDF/411682_fha_mortgages.pdf*.

Proposed § 226.36(e) would not require a loan originator to direct a consumer to the transaction that will result in the least amount of compensation being paid to the originator by the creditor. However, if the loan originator reviews possible loan offers available from a significant number of the creditors with which the originator regularly does business and the originator directs the consumer to the transaction that will result in the least amount of creditor-paid compensation, the requirements of § 226.36(e) would be deemed to be satisfied. *See* proposed comment 36(e)(1)–2(ii).

Loan originators employed by the creditor in a transaction would be prohibited under § 226.36(d)(1) from receiving compensation based on the terms or conditions of the loan. Thus, when originating loans for the employer, the originator could not steer the consumer to a particular loan to increase compensation. Accordingly, in those cases, their compliance with § 226.36(d)(1) would be deemed to satisfy the requirements of proposed § 226.36(e). *See* proposed comment 36(e)(1)–2(ii). A creditor's employee, however, occasionally might act as a broker in forwarding a consumer's application to a creditor other than the originator's employer, such as when the employer does not offer any loan products for which the consumer would qualify. If the originator is compensated for arranging the loan with the other creditor, the originator would not be an employee of the creditor in that transaction and would be subject to proposed § 226.36(e).

The Board is also publishing provisions that would facilitate compliance with the prohibition in proposed § 226.36(e)(1). Under proposed § 226.36(e)(2) and (3), a safe harbor would be created, and there would be no violation if the loan was chosen by the consumer from at least three loan options for each type of transaction (fixed-rate or adjustable-rate loan) in which the consumer expressed an interest, provided the following conditions are met. The loan originator must obtain loan options from a significant number of creditors with which the originator regularly does business. For each type of transaction in which the consumer expressed an interest, the originator must present and permit the consumer to choose from at least three loans that include: the loan with the lowest interest rate, the loan with the second lowest interest rate, and the loan with the lowest total dollar amount for origination points or fees and discount points. The loan originator must have a good faith belief that these are loans for which the consumer likely qualifies. If the originator presents more than three loans to the consumer, the originator must highlight the three loans that satisfy the lowest rate and points criteria in the rule. Proposed comments 36(e)(2)–1 and 36(e)(3)–1 though –4 would provide guidance on the application of the rule.

Comment is expressly solicited on whether the proposed rule in § 226.36(e) and the accompanying commentary would be effective in achieving the stated purpose. Comment is also solicited on the feasibility and practicality of such a rule, its enforceability, and any unintended adverse effects the rule might have.

36(f)

The Board proposes to redesignate existing § 226.36(d) as § 226.36(f). Existing § 226.36(d) provides that § 226.36 does not apply to home-equity lines of credit (HELOCs). The redesignation would accommodate proposed new § 226.36(d) and (e), discussed above.

The Board proposed as part of the 2008 HOEPA proposal to exclude HELOCs from the coverage of § 226.36 because of two considerations, which suggested that the protections may be unnecessary for such transactions. First, the Board understood that most originators of HELOCs hold them in portfolio rather than sell them, which aligns these originators' interests in loan performance more closely with their borrowers' interests. Second, the Board understood that HELOCs are concentrated in the banking and thrift industries, where the federal banking agencies can use their supervisory authority to protect consumers. The Board sought comment on whether these considerations were valid or whether any or all of the protections in § 226.36 should apply to HELOCs. Although mortgage lenders and other industry representatives commented in support of the proposed exclusion and consumer advocates commented in opposition, neither group provided the Board with substantial evidence as to whether the kinds of problems § 226.36 addresses exist in the HELOC market.

In the July 2008 HOEPA Final Rule, the Board limited the scope of § 226.36 to closed-end mortgages. In the absence of clear evidence of abuse, the Board continued to believe the protections may be unnecessary for the reasons discussed above. Nevertheless, the Board remains aware of concerns that creditors may structure transactions as HELOCs solely to evade the protections of § 226.36. The Board also is aware that many of the same opportunities and incentives that underlie the abuses addressed by § 226.36 for closed-end mortgages may well exist for HELOCs. Reasons therefore exist for positing that such unfair practices either may or may not occur with HELOCs, but the Board lacks concrete evidence as to which is the case.

The Board requests comment on whether any or all of the protections in § 226.36 should apply to HELOCs. Specifically, what evidence exists that shows whether loan originators unfairly manipulate HELOC terms and conditions to receive greater compensation, injuring consumers as a result? What evidence is there as to whether appraisals obtained for HELOCs have been influenced toward misstating property values? To what extent do creditors contract out HELOC servicing to third parties, thus undermining the Board's premise regarding aligned interests between servicers and consumers? Whether third parties or the original creditors primarily service HELOCs, what evidence shows whether they engage in the abusive servicing practices addressed by § 226.36(c)?

Section 226.37 Special Disclosure Requirements for Closed-End Mortgages

Section 226.17(a), which implements Sections 122(a) and 128(b)(1) of TILA, addresses format and other disclosure standards for all closed-end credit. 15 U.S.C. 1632(a), 1638(b)(1). For closed-end credit, creditors must provide disclosures in writing in a form that the consumer may keep, grouped together and segregated from other information. In addition, the loan's ''finance charge'' and ''annual percentage rate,'' using those terms, must be more conspicuous than other required disclosures.

The Board proposes special rules in new § 226.37 to govern the format of required disclosures under TILA for transactions secured by real property or a dwelling. These new rules would be in addition to the rules in § 226.17. The proposed format rules are intended to (1) improve consumers' ability to identify disclosed loan terms more readily; (2) emphasize information that is most important to the consumer in the decision-making process; and (3) simplify the organization and structure of required disclosures to reduce complexity and ''information overload.'' Proposed § 226.37 would establish special format rules for disclosures required by proposed §§ 226.38 and 226.20(d), and existing §§ 226.19(b) and 226.20(c).

The Board is proposing § 226.37 and associated commentary to address the duty to provide ''clear and conspicuous'' disclosures that are grouped together and segregated from other information, and to require that certain information be highlighted in table form or in a graph. Proposed § 226.37 would also require creditors to use consistent terminology for all disclosures. The Board is proposing to revise the requirement that certain terms be used or disclosed more conspicuously, for transactions secured by real property or a dwelling. The general disclosure standards under § 226.17(a)(1) and associated commentary continue to apply transactions secured by real property or a dwelling but, under the proposal creditors would also be required to meet the higher standards under proposed § 226.37.

37(a) Form of Disclosures

37(a)(1) Clear and Conspicuous

Section 122(a) of TILA and § 226.17(a)(1) require that all closed-end credit disclosures be made clearly and conspicuously. 15 U.S.C. 1632(a). Currently, under comment 17(a)(1)–1, the Board interprets the clear and conspicuous standard to mean that disclosures must be in a ''reasonably understandable'' form. This standard does not require any mathematical progression or format, or that disclosures be provided in a particular type size, although disclosures must be legible whether typewritten, handwritten, or printed by computer. Comment 17(a)(1)–3 provides that the standard does not require disclosures to be located in a particular place.

Consumer testing conducted by the Board showed that information presented without any highlighting or other emphasis, and the use of small print led many participants to miss or disregard key information about the loan transaction. As discussed more fully under the following sections, consumer testing indicates that when certain information is presented and highlighted in a specific way consumers are able to identify and use key terms more easily: proposed § 226.38 for disclosures required on transactions secured by real property or a dwelling, § 226.19(b) for ARM loan program disclosures, § 226.20(c) for ARM adjustment notices, and § 226.20(d) for periodic statements on loans that are negatively amortizing.[66] For example, consumer testing of the current TILA model form indicated that participants viewed both the interest rate and monthly payment as important. Although participants generally understood that the interest rate on their loan could change, several arrived at this conclusion because of the payment schedule disclosure, which showed different monthly payment amounts, not because they understood the loan had a variable rate feature that would affect their monthly payments. In addition to testing the current TILA model form, the Board also tested variations of that form, including a form it developed in 1998 with HUD (''Joint Form'') that was submitted to Congress in the 1998 Joint Report.[67] Participants who reviewed the Joint Form also generally understood the loan had an adjustable rate, but less than half understood the rate was fixed only for the first three years and could vary only after that time period. However, when the Board consumer tested information about interest rates and monthly payments in a tabular form, participants could identify more readily that the loan had an adjustable rate feature, and comprehension of when interest rates would adjust and the impact that rate adjustments had on their monthly payments improved.

For these reasons, the Board proposes to require that creditors make disclosures for transactions secured by real property or a dwelling clearly and conspicuously, by highlighting certain information in accordance with the requirements in proposed §§ 226.38, 226.19(b), § 226.20(c), and § 226.20(d). Proposed comment 37(a)(1)–1 would clarify that to meet the clear and conspicuous standard, disclosures must be in a reasonably understandable form and readily noticeable to the consumer. Proposed comment 37(a)(1)–2 provides that to meet the readily noticeable standard, the disclosures under proposed §§ 226.38, 226.19(b), 226.20(c), and 226.20(d) generally must be provided in a minimum 10-point font. The approach of requiring a minimum of 10-point font for certain disclosures is consistent with the approach taken by the Board in revising disclosures required under TILA for certain open-end credit. 74 FR 5244; Jan. 29, 2009.

New comment 37(a)(1)–3 would clarify that disclosures under proposed §§ 226.38 and 226.19(b) must be provided on a document separate from other information, although these disclosures, as well as disclosures under proposed §§ 226.20(c) and 226.20(d), may be made on more than one page, on the front or back side of a page, and continued from one page to the next. Consumer testing suggests that consumers may not read information carefully if it is excessive in length, and if unable to identify relevant information quickly are likely to become frustrated and not read the disclosures. The Board believes that allowing creditors to combine disclosures with other information may increase the likelihood that consumers will not read the disclosures.

37(a)(2) Grouped Together and Segregated

Section 128(b)(1) of TILA and § 226.17(a)(1) currently require that, except for certain information, the disclosures required for closed-end credit must be grouped together, segregated from everything else, and not contain any information not directly related to the required disclosures. 15 U.S.C. 1638(b)(1). Comment 17(a)(1)–2 states that creditors can satisfy the grouped together and segregation requirement in a variety of ways, including combining segregated disclosures with other information as long as they are set off by a certain format type. Comment 17(a)(1)–2 further provides that the segregation requirement does not apply to disclosures for variable rate transactions required under current §§ 226.19(b) and 226.20(c). Comment 17(a)(1)–7 clarifies that balloon-payment financing with leasing characteristics is subject to the grouped together and segregation requirement.

Consumer testing conducted by the Board indicated that participants generally are overwhelmed by the amount of information presented for loan transactions, and as a result, do not read their mortgage disclosures carefully. Consumer testing showed that emphasizing terms and costs consumers find important, and separating out less useful information, is critical to improving consumers' ability to identify and use key information in their decision-making process.[68] Consumer testing also demonstrated that grouping related concepts and figures together, and presenting them in a particular format or structure can improve

[66] *See also Improving Consumer Mortgage Disclosures* (finding that incorporating white space, using clear headings, and using certain formatting and organization create a ''less intimidating appearance than many consumer financial disclosures, making it more likely that consumers will both want to read the form and be able to use it productively in their decisions.'').

[67] *See* the *1998 Joint Report,* App.A–6.

[68] *See also Improving Consumer Mortgage Disclosure* at 69 (consumer testing results showed that current mortgage disclosure forms failed to convey key cost disclosures, but that prototype disclosures, which removed less useful information, significantly improved consumers' recognition of key mortgage costs).

consumers' ability to identify, comprehend, or use disclosed terms.

For these reasons, the Board proposes to require that certain disclosures be grouped together and segregated in the manner discussed below, 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 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). Grouping and segregating information which is most useful and relevant to the loan transaction would facilitate consumers' ability to evaluate a loan offer.

Segregation of disclosures. Proposed § 226.37(a)(2) would implement TILA Section 128(b)(1) of TILA, in part, for transactions secured by real property or a dwelling. 15 U.S.C. 1604(a), 1638(b)(1). Proposed § 226.37(a)(2) would require that disclosures for such transactions be grouped together in accordance with the requirements under proposed § 226.38(a) through (j), segregated from other information, and not contain any information not directly related to the segregated disclosures. Based on consumer testing, the Board also is proposing to require that ARM loan program disclosures under proposed § 226.19(b), ARM adjustment notices under proposed § 226.20(c), and periodic notices for payment option loans that are negatively amortizing under proposed § 226.20(d), be subject to a grouped-together and segregation requirement. Thus, the reference to §§ 226.19(b) and 226.20(c) would be deleted from comment 17(a)(1)–2.

Proposed comment 37(a)(2)–1 would clarify that to be segregated, disclosures must be set off from other information. Based on consumer testing, the Board is concerned that allowing creditors to combine disclosures with other information, in any format, will diminish the clarity of key disclosures, potentially cause ''information overload,'' and increase the likelihood that consumers may not read the disclosures. Proposed comment 37(a)(2)–1 also would provide guidance on how creditors can group together and segregate the disclosures in accordance with proposed § 226.38(a)–(j), such as by using bold print dividing lines.

Content of segregated disclosures; directly related information. Footnotes 37 and 38 currently provide exceptions to the grouped-together and segregation requirement under § 226.17(a)(1). Footnote 37 allows creditors to include information not directly related to the required disclosures, such as the consumer's name, address, and account number. Footnote 38, which implements TILA Section 128(b)(1), 15 U.S.C. 1638(b)(1), allows creditors to exclude certain required disclosures from the grouped-together and segregation requirement, such as the creditor's identity under § 226.18(a), the variable-rate example under § 226.18(f)(1)(iv), insurance or debt cancellation disclosures under § 226.18(n), or certain security-interest charges under § 226.18(o). Comment 17(a)(1)–4 clarifies that creditors have flexibility in grouping the disclosures listed in footnotes 37 and 38 either together with or separately from segregated disclosures, and comment 17(a)(1)–5 addresses what is considered directly related to the segregated disclosures.

Proposed § 226.37(a)(2)(i) and (ii) would provide exceptions to the grouped-together and segregation requirement, and implement TILA Section 128(b)(1) for transactions secured by real property or a dwelling. 15 U.S.C. 1638(b)(1). Proposed § 226.37(a)(2)(i) replicates the content in current footnote 37 and would allow the following disclosures to be made together with the segregated disclosures: the date of the transaction, and the consumer's name, address and account number. Proposed § 226.37(a)(2)(ii) generally replicates the substance in current footnote 38, except that the Board proposes to remove the reference to the variable-rate example under § 226.18(f)(iv), which would be eliminated for mortgage loans as discussed under proposed § 226.19(b). Under proposed § 226.37(a)(2)(ii), creditors also would have flexibility to make the tax deductibility disclosure, as discussed under proposed § 226.38(f)(4), together with or separately from other required disclosures.

Proposed comment 37(a)(2)–2 clarifies that creditors may add or delete the disclosures listed in proposed § 226.37(a)(2)(i) and (ii) in any combination together with or separate from the segregated disclosures. Proposed comment 37(a)(2)–3 provides guidance on the type of information that would be considered directly related and that may be included with the segregated disclosures for transactions secured by real property or a dwelling. Information described in comments 17(a)(1)–5(i) through (xv) are not included in proposed comment 37(a)(2)–3 because they are not applicable to transactions secured by real property or a dwelling, or are unnecessary as a result of other proposed disclosures: grace periods for late fees; unsecured interest; demand features; instructions on multi-purpose forms; minimum finance charge statement; negative amortization; due-on-sale clauses; prepayment of interest statement; the hypothetical example disclosure required by current § 226.18(f)(1)(iv); the variable rate transaction disclosure required by current § 226.18(f)(1); assumption; and the late-payment fee disclosure for single-payment loans.

The Board also proposes to require that the disclosure of the creditor's identity be grouped together and segregated from other information, for all closed-end credit. The Board proposes to make this change 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 to effectuate the statute's purposes, which include facilitating consumers' ability to compare credit terms, and avoiding the uninformed use of credit. 15 U.S.C. 1601(a). The Board believes that the creditor's identity should be included with the grouped-together and segregated disclosures so that consumers can more easily identify the appropriate entity. Thus, current footnote 38 would be revised, and proposed § 226.37(a)(2) would implement this aspect of the proposal for transactions secured by real property or a dwelling.

In technical revisions, the Board proposes to move the substance of footnotes 37 and 38 to the regulatory text of § 226.17(a)(1). Current comment 17(a)(1)–7 would be revised to address disclosures for transactions secured by real property or a dwelling that have balloon payment financing with leasing characteristics; a cross-reference to comment 17(a)(1)–7 is proposed in new comment 37(a)(2)–4.

The Board seeks comment on whether it should continue to permit creditors to make the insurance or debt cancellation disclosures under proposed § 226.4(d) together with or separately from other required disclosures. Consumer testing showed that many participants found these disclosures too long and complex, and as a result they do not read or only skim the disclosures. The Board is concerned that adding the insurance information to the information about loan terms required by proposed § 226.38 will result in ''information overload.''

Multi-purpose forms. Comment 17(a)(1)–6 currently permits creditors to design multi-purpose forms for TILA-required closed-end credit disclosures as long as the clear and conspicuous requirement is met. The Board proposes to require that disclosures for transactions secured by real property or a dwelling be made only as applicable, as discussed more fully under proposed § 226.38. As noted, consumer testing indicates that consumers may not read information if it is excessive in length, and if unable to identify relevant information quickly are likely to become frustrated and not read the disclosures. The Board believes that allowing creditors to combine disclosures with other information that is not applicable to the transaction may contribute to ''information overload,'' and increase the likelihood that consumers will not read the disclosures.

For these reasons, under the proposal creditors would not be permitted to use forms for more than one type of mortgage transaction (*i.e.,* multi-purpose forms). The Board believes technology and form design software will allow creditors to prepare transaction-specific, customized disclosure forms at minimal cost. The Board seeks comment, however, on whether creditors already provide consumers with customized disclosures forms for mortgage loans in the regular course of business, or the extent to which creditors rely on multi-purpose forms. The Board seeks comment on potential operational changes, difficulties, or costs that would be incurred to implement the requirement to have transaction-specific disclosures for transactions secured by real property or a dwelling.

37(b) Separate Disclosures

Existing § 226.17(a)(1) requires certain disclosures to be provided separately from the segregated information, such as the itemization of amount financed required by § 226.18(c)(1) and TILA Section 128(a)(2)(A). 15 U.S.C. 1638(a)(2)(A). The Board is proposing to expand the list of disclosures that must be provided separately from the segregated information, based on consumer testing.

Consumer testing showed that certain disclosures, such as disclosures about assumption or property insurance, were confusing to participants, or were generally not as useful in the participants' decision-making process as other information. For example, with respect to assumption, few participants understood the current assumption policy model clause in Model Clause H–6 in Appendix H to Regulation Z; almost no one stated that the assumption was important information when applying for and obtaining a loan. With respect to property insurance, most participants understood that the borrower can obtain property insurance from anyone that is acceptable to the lender, but participants stated they were already aware of this fact and therefore this information was not useful. Regarding rebates, consumers understood that early payoff of the loan could result in a refund of interest and fees, and generally expressed interest in knowing this information. However, most also indicated that information about rebates would not have an impact on whether they accepted a loan and therefore, it was not as important or useful to the decision-making process as other information, such as interest rate or closing costs.

With respect to the contract reference, almost all participants understood already that they could read their contract to learn what could happen if they stopped making payments, defaulted, paid off or refinanced their loan early. In addition, other proposed disclosures, such as the prepayment penalty under proposed § 226.38(a)(5) or demand feature under proposed § 226.38(d)(2)(iv), would make the contract reference disclosure less important because such information would already be disclosed directly on the disclosure statement itself. Moreover, because creditors must provide disclosures within three business days after application for transactions secured by real property or a consumer's dwelling, consumers will not have a contract to reference at this point in time.

For these reasons, the Board proposes to require that certain information be disclosed separately from the grouped together and segregation information, to improve consumers' ability to focus on the terms that are most important for shopping and decision-making.[69] New § 226.37(b) would require that creditors provide the following disclosures separately from other information for transactions secured by real-property or a dwelling: Itemization of amount financed under proposed § 226.38(j)(1); rebates under proposed § 226.38(j)(2); late payment under proposed § 226.38(j)(3); property insurance under proposed § 226.38(j)(4); contract reference under proposed § 226.38(j)(5); and assumption under proposed § 226.38(j)(6).

The Board proposes this approach 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). In this case, the Board believes an exception from TILA's grouped together and segregation requirement is necessary to effectuate the Act's purposes for transactions secured by real property or a dwelling. As noted above, many consumers may not read information if it is excessive in length, and if unable to identify relevant information quickly are likely to become frustrated and not read the disclosures. The Board is concerned that allowing creditors to combine the information in proposed § 226.38(j) with other required information could contribute to ''information overload,'' distract from other important disclosures, such as the APR or monthly payments, and may increase the likelihood that consumers will not read the disclosures. Thus, the Board believes that requiring these disclosures to be separate from the other required disclosures will serve TILA's purpose to avoid the uninformed use of credit. 15 U.S.C. 1601(a).

37(c) Terminology

37(c)(1) Consistent Terminology

Currently, there is no requirement that TILA disclosures for closed-end credit use consistent terminology. Consumer testing showed that some participants were confused when different terms are used for the same information. For example, when the terms loan amount, principal, and loan balance were used, some participants attributed different meaning to each term used. Based on these findings, the Board proposes § 226.37(c)(1) to require the use of consistent terminology for the disclosures under proposed §§ 226.38, 226.19(b), 226.20(c) and 226.20(d). The Board believes that using consistent terminology will enhance a consumers' ability to identify, review, and comprehend disclosed terms across all disclosures and therefore, avoid the uninformed use of credit. Proposed comment 37(c)(1)–1 clarifies that terms do not need to be identical, unless otherwise specified, but must be close enough in meaning to enable the consumer to relate the disclosures to one another. Proposed comment 37(c)(1)–2 provides guidance on combining terms for transactions secured by real property or a dwelling when more than one numerical disclosure would be the same, and provides an example relating to the total payments and amount financed disclosures required under proposed

[69] *See also Improving Consumer Mortgage Disclosures* at 37–38, 59–60 (finding that streamlining disclosures improved consumer ability to identify and understand key terms of the loan transaction disclosed).

§§ 226.38(e)(5)(i) and 226.38(e)(5)(iii), respectively.

37(c)(2) Terms Required To Be More Conspicuous

Currently TILA Section 122(a) and § 226.17(a)(2) require creditors to disclose the terms ''finance charge'' and ''annual percentage rate,'' together with a corresponding dollar amount and percentage rate, more conspicuously than any other disclosure, except the creditor's identity under § 226.18(a). 15 U.S.C. 1632(a). Under TILA Section 103(u), the finance charge and the annual percentage rate are material disclosures; failure to disclose either term extends the right of rescission under TILA Section 125, and can result in actual and statutory damages under TILA Section 130(a). 15 U.S.C. 1602(u); 15 U.S.C. 1635, 1640(a).

Finance charge: interest and settlement charges. Section 226.18(d), which implements TILA Sections 128(a)(3) and (a)(8), requires creditors to disclose the ''finance charge,'' using that term, and a brief description such as ''the dollar amount the credit will cost you'' for closed-end credit. 15 U.S.C. 1638(a)(3), (a)(8). Consumer testing showed that participants could not correctly explain what the finance charge represented. Many consumers recognized that the finance charge included all of the interest they would pay over the loan's term, but did not know that it also included fees. Most participants did not find the finance charge to be useful in evaluating a loan offer. However, some participants expressed a general interest in knowing the information.

Based on these results, the Board tested a form with the finance charge disclosed as ''interest and settlement charges,'' to more closely represent the components of the finance charge. Participants generally understood the term, but still stated that they did not find the term very useful, particularly when compared to other information such as the interest rate or monthly payments. Consumer testing suggests that highlighting terms that are not useful in the decision-making process may generally diminish consumers' ability to understand other key terms.

For these reasons, and as discussed more fully in the discussion of proposed § 226.38(e)(5)(ii), the Board proposes to exercise its authority under TILA Section 105(a) to make certain exceptions to the disclosure of the finance charge under TILA Section 128(a)(3) and TILA Section 122(a). 15 U.S.C. 1604(a); 1632(a); 1638(a)(3). First, creditors would be required to disclose the finance charge as ''interest and settlement charges,'' not as the ''finance charge'' as required by TILA Section 128(a)(3). 15 U.S.C. 1638(a)(3). Second, the disclosure of interest and settlement charges would not have to be more conspicuous than other terms, as required by TILA Section 122(a). 15 U.S.C. 1632(a).

The exception to TILA's requirements that the finance charge be disclosed as the ''finance charge'' and that it be more conspicuous than other information is proposed pursuant to TILA Section 105(a). 15 U.S.C. 1604(a). The Board has authority under TILA Section 105(a) to adopt ''such adjustments and exceptions for any class of transactions as in the judgment of the Board are necessary or proper to effectuate the purposes of this title, to prevent circumvention or evasion thereof, or to facilitate compliance therewith.'' 15 U.S.C. 1601(a), 1604(a). The class of transactions that would be affected is closed-end transactions secured by real property or a dwelling. The Board believes an exception from TILA's requirements is necessary and proper to effectuate TILA's purposes to assure meaningful disclosure and informed credit use. Consumer testing showed that disclosing the finance charge as ''interest and settlement charges'' improved participants' understanding of the information, even though the figure may not include all interest and settlement charges applicable to the transaction. (See discussion under proposed § 226.4 regarding content and calculation of the interest and settlement charges.) Moreover, consumer testing showed that participants did not find the interest and settlement charges as useful, when choosing or evaluating a loan product, as other information, such as whether the loan has an adjustable rate or the monthly payment amount.

In addition, and for the reasons discussed more fully under proposed § 226.38(e)(5)(ii) regarding interest and settlement charges, the proposal would group the interest and settlement charges disclosure with other disclosures relating to the total cost of the loan offered, such as the total of payments and the amount financed. Consumer testing conducted by the Board, as well as basic document design principles, shows that grouping related concepts and figures makes it easier for consumers to identify, comprehend, or use disclosed terms.

Annual percentage rate. TILA Section 122(a) and § 226.17(a)(1) require that the term ''annual percentage rate,'' when disclosed with the corresponding percentage rate, be disclosed more conspicuously than any other required disclosure. 15 U.S.C. 1632(a). The Board is proposing to revise the description of the APR and require that creditors provide context for the APR by disclosing it on a scaled graph with explanatory text, as discussed more fully under proposed §§ 226.38(b). In addition, the Board is proposing § 226.37(c)(2) to implement TILA Section 122(a) for transactions secured by real property or a dwelling. 15 U.S.C. 1632(a). Section 226.37(c)(2) would require that creditors disclose the APR in a 16-point font, in a prominent location, and in close proximity to the scaled graph and explanations proposed under § 226.38(b)(2) through (4).

As discussed under proposed § 226.38(b), the APR is one of the most important terms disclosed about the loan; it is the only single, unified number available to help consumers understand the overall cost of a loan. To this end, the Board believes it is essential that consumers be able to identify the APR easily. Consumer testing and basic document design principles show that participants generally pay greater attention to figures, such as numbers, percentages and dollar signs, than to terminology that may accompany, describe or label any disclosed figure. However, the TILA disclosure contains many numerical figures that consumers must identify and review. Given that the Board is proposing to require a minimum 10-point font for disclosure of other terms on the TILA (see discussion under proposed comment 37(a)(1)–2), and based on document design principles, the Board consumer tested disclosing the APR figure in a larger font and in bold text to make it more readily noticeable as compared to other disclosed terms. When tested in this manner, participants were able to easily identify the APR. Based on consumer testing, the Board believes that a 16-point font requirement for the APR is sufficient to highlight the APR. The Board also notes that the approach of requiring at least a 16-point font for the APR disclosure is consistent with the approach taken by the Board in revising the purchase APR disclosure required under TILA for open-end credit. 74 FR 5244; Jan. 29, 2009.

Proposed comment 37(c)–3(i) through (iii) would provide further guidance on the more conspicuous requirement and would clarify that the APR must be more conspicuous only in relation to other required disclosures under proposed § 226.38, and only as required under proposed § 226.37(c)(2) and § 226.38(b). Proposed comment 37(c)–4 would provide guidance on how creditors can comply with the more conspicuous requirement for transactions secured by real property or a dwelling.

The Board seeks comment on whether the APR should be made more or less prominent using a larger or smaller font-size, and whether different graphs or visuals could be used to provide better context for the APR. The Board also seeks comment on the relative advantages and disadvantages of a graphic-based versus text-based approach to disclosing the APR, and the potential operational changes, difficulties, or costs that would be incurred to implement the graphic-based APR disclosure requirement for transactions secured by real property or a dwelling.

37(d) Specific Formats

Currently, § 226.17(a)(1) does not impose special format design or location requirements on disclosures for closed-end credit. However, as discussed more fully under proposed § 226.38, consumer testing showed that the current TILA form did not present key loan information in a manner that was noticeable and easy for consumers to understand. For example, the payment schedule required under current § 226.18(g) did not effectively demonstrate to participants the relationship between monthly payments and an adjustable interest rate feature. Consumer testing also showed that the current TILA form highlighted terms that confused many participants. For example, most participants incorrectly assumed the amount financed was the same as the loan amount, a term not required on the current TILA form. In other instances, the current TILA form emphasized information that participants generally understood, but did not find useful or important, such as the total of payments. Many participants also noted that the current TILA form failed to include information they would find useful when shopping or evaluating a loan offer, such as the contract interest rate and settlement charges.

As discussed under proposed § 226.19, consumer testing of the current ARM loan program disclosure and the CHARM booklet also revealed ineffective presentation of information relating to adjustable rate loan programs. Many participants found the narrative format and terminology used in the current ARM loan program disclosure complicated, dense, and difficult to read and understand. With respect to the CHARM booklet, many participants generally indicated that the information it contained was informative and educational, but they would be unlikely to read it because it was too long.

In addition, as noted previously, consumer testing suggests that consumers may not read information carefully if it is excessive in length, and if unable to identify relevant information quickly are likely to become frustrated and not read the disclosures. As discussed more fully under proposed § 226.37(a) through (c), this suggests highlighting and structuring disclosures in a particular manner to improve clarity, identification and comprehension of disclosed terms.

To address the problems with the current TILA form and ARM loan program disclosures, the Board used various formats to present key loan information, such as tabular forms and question and answer format. Consumer testing suggests that using tabular forms improved participants' ability to readily identify and understand key information, as discussed under proposed §§ 226.19(b) and 226.38(c). For example, current ARM loan program disclosures provide information in narrative form, which participants found difficult to read and understand. However, consumer testing showed that when information about interest rate, monthly payment and loan features was presented in tabular format, participants found the information easier to locate and their comprehension of the disclosed terms improved. The benefits of disclosing important information in a tabular format are consistent with the results of consumer testing conducted by the Board in revising credit card disclosures. 74 FR 5244; Jan. 29, 2009. Consumer testing also showed that using question and answer format improved participants' ability to recognize and understand potentially risky or costly features of a loan, as discussed under proposed §§ 226.19 and 226.38(d). Consumer testing and basic document design principles suggest that keeping language and design elements consistent between forms improves consumers' ability to identify and track changes in the information being disclosed. As a result, the Board also integrated the question and answer format used on the revised TILA model form into ARM loan program disclosures required under proposed § 226.19(b).

To present key loan terms more effectively, the Board also used specific location and structure requirements. Consumer testing suggests that the location and order in which information is presented impacts consumers' ability to find and comprehend the information disclosed. For example, as discussed under proposed § 226.38(a), disclosing key information, such as the loan term, amount, type, and settlement charges, before other required disclosures and in a tabular format improved participants' ability to quickly and accurately identify key loan terms. In another example, participants' ability to identify the frequency of rate adjustments after an introductory period expired also improved when this information was included both in the loan summary section at the top of the revised TILA model form, and then again below in the interest rate and payment summary section.

Based on consumer testing results, basic document design principles, and for the reasons discussed more fully under each of the following subsections, the Board is proposing to establish special format rules for: disclosures under proposed § 226.38 for transactions secured by real property or a dwelling; ARM loan program disclosures under proposed § 226.19(b) for adjustable rate transactions; ARM adjustment notices under proposed § 226.20(c); and periodic statements required for payment option loans that are negatively amortizing under proposed § 226.20(d). The special rules regarding format, structure and location of disclosures are noted in proposed § 226.37(d)(1) through (10). Proposed comments 37(d)–1 and –2 would provide guidance to creditors on how to comply with the special format rules noted in proposed § 226.37(d)(1) through (10) regarding prominence and close proximity of disclosed terms.

37(e) Electronic Disclosures

Currently, under § 226.17(a)(1) creditors are permitted to provide in electronic form any TILA disclosure for closed-end credit that is required to be provided or made available to consumers in writing if the consumer affirmatively consents to receipt of electronic disclosures in a prescribed manner. Electronic Signatures in Global and National Commerce Act (the E-Sign Act), 15 U.S.C. 7001 *et seq.* The Board proposes § 226.37(e) to allow creditors to provide required disclosures for transactions covered by proposed § 226.38 in electronic form in accordance with the requirements under § 226.17(a)(1).

Section 226.38 Content of Disclosures for Credit Secured by Real Property or a Dwelling

38(a) Loan Summary

To shop for and understand the cost of credit, consumers must be able to identify and understand the key credit terms offered to them. As discussed below, the Board's consumer testing suggested that loan amount, loan term and loan type are key terms that consumers are familiar with and expect to see on closed-end mortgage disclosures, together with settlement charges and whether a prepayment penalty would apply to their loan.

The Board's Proposal

The Board proposes to require creditors to provide the following key loan features in a loan summary section: loan amount, loan term, loan type, the total settlement charges, whether a prepayment penalty applies and, the maximum amount of the penalty. The purpose of the proposed disclosures is to improve their effectiveness and consumer comprehension. A concise loan summary would help consumers compare loan offers; a summary may also help consumers determine whether they can afford the loan they are offered, and whether the disclosure presents the same loan terms they discussed with their mortgage broker or lender.

The Board conducted consumer testing of loan summary disclosures. Participants were able to identify the exact loan amount, what type of a loan they were being offered, how long they would have to pay off their loan, how much they would have to pay in settlement charges, and whether a prepayment penalty would apply. A discussion of the items that would be included in the loan summary follows.

38(a)(1) Loan Amount

Currently creditors are not required to disclose the loan amount for closed-end mortgages, except for loans subject to HOEPA. Under § 226.32(c)(5), creditors are required to disclose the total amount borrowed. The Board is proposing to require a similar disclosure of the loan amount for all transactions secured by a real property or a dwelling. Proposed § 226.38(a)(1) would require creditors to disclose ''loan amount,'' which would be defined as the principal amount the consumer will borrow reflected in the note or loan contract. The loan amount is a core loan term that the consumer should be able to verify readily on the disclosure. Disclosing the loan amount may also alert the consumer to fees that are financed in addition to the principal balance.

38(a)(2) Loan Term

Currently, Regulation Z requires creditors to disclose the number of payments but not the term of the loan. The Board believes that the loan term is an important fact about the loan that consumers should know when evaluating a loan offer. Consumer testing of current model forms conducted by the Board indicated that some consumers are not able to readily identify the loan term from the number of payments disclosed in the current disclosures. Although some participants could determine the loan term by dividing by 12 the number of months shown in the payment schedule disclosed under § 226.18(g), other participants could not readily figure the term of the loan offered, particularly for loans that have multiple payment levels, such as discounted adjustable-rate mortgages. For these reasons, the Board is proposing to require disclosure of the loan term in the summary section for loans covered by § 226.38, and to define ''loan term'' for these purposes as the time to repay the obligation in full. For instance, instead of disclosing the number of months for each payment amount for variable interest rate loans and requiring the consumer to add up those months to determine the loan term, the proposed disclosure would state ''Loan term: 30 years.'' Likewise, for a 10-year loan with a balloon payment due in year 10 and an amortization schedule of 30 years, the proposed disclosure would state ''Loan term: 10 years.''

38(a)(3) Loan Type and Features

Regulation Z does not require the creditor to disclose the type of the loan, except in the case of loans with variable interest rates. Current § 226.18(f) requires a disclosure of a variable rate if the annual percentage rate may increase after consummation. The Board's consumer testing indicates that the current variable rate disclosures may not clearly convey whether the loan has a fixed or a variable interest rate. The Board believes that a specific disclosure of a loan type offered will assist consumers in better understanding whether a loan features a rate that may increase after consummation, so that the consumer may evaluate whether they want a loan in which the rate and payments can increase.

The Board is proposing to require a disclosure of the loan type in the loan summary section for loans covered by § 226.38. Proposed § 226.38(a)(3)(i) would require that a loan be classified as one of three types: an ''adjustable-rate mortgage (ARM),'' a ''step-rate mortgage,'' or a ''fixed-rate mortgage'' using those terms. The categories proposed in § 226.38(a)(3)(i) apply only to disclosures requires for closed-end transaction secured by real property or a dwelling, and are different from the categories in § 226.18(f) and commentary to § 226.17(c)(1). Proposed § 226.38(a)(3)(ii) would require an additional disclosure if the loan has one or more of the following three features: ''negative amortization,'' ''interest-only payments,'' or ''step-payments,'' using those terms. The related commentary would provide examples for each loan type and feature.

38(a)(3)(i) Loan Type

As discussed above, consumer testing indicated that the current variable rate disclosure is not sufficiently clear for many consumers. When presented with a current closed-end model form for an adjustable-rate mortgage, over half of the participants understood that the interest rate would change. However, several participants inferred this from the different monthly payments in the payment schedule, not because the check box on the form indicated that the loan had a ''variable rate.'' A few participants indicated that they did not know whether the rate would change. Some participants commented that although the current model form used the term ''variable rate,'' they were more familiar with the term ''adjustable rate.'' As a result, the Board tested revised disclosures using the term ''adjustable rate mortgage'' in the loan summary section. All participants who were shown a revised disclosure for a variable rate transaction using the term ''adjustable-rate mortgage'' understood that the interest rate and payments could change during the loan's term.

Proposed § 226.38(a)(3)(i) would define an adjustable-rate mortgage as a transaction in which the annual percentage rate may increase after consummation; a step-rate mortgage as a transaction in which the interest rate will change after consummation as specified in the legal obligation between the parties; and a fixed-rate mortgage as a transaction that is neither an adjustable-rate mortgage nor a step-rate mortgage. Proposed comment 38(a)(3)(i)(A)–2 would offer examples of adjustable-rate mortgages and clarify that some variable-rate transactions described in comment 17(c)(1)(iii)–4, such as certain renewable balloon-payment, preferred-rate and price-level-adjusted loans, would be considered fixed-rate mortgages for the purposes of the ''loan type'' disclosure in the loan summary required by § 226.38(a). This follows the current approach in comment 17(c)(1)–11 which provide that disclosures for certain variable-rate transactions should be based on the interest rate that applies at consummation.

Proposed § 226.38(a)(3)(i)(B) would require the creditor to disclose a loan as a ''step-rate mortgage'' if the interest rate will change after consummation, provided all such interest rates are specified in the legal obligation between the parties. Under existing guidance, such a loan would not be considered a variable rate loan. The Board believes that for the purposes of the loan summary, which is to alert the consumer to the possibility that their interest rate and payment could increase after consummation, step-rate loans should not be identified as fixed or variable rate loans, even though they share certain features with both loan types. Proposed comment 38(a)(3)(i)(B)–2 would clarify that certain preferred-rate loans would not be considered step-rate mortgages for the purposes of the ''loan type'' disclosures. Proposed comment 38(a)(3)(i)(C)–1 would offer examples of fixed-rate mortgages and explain which variable-rate transactions described in comment 17(c)(1)(iii)–4 would be considered fixed-rate mortgages for the purposes of the ''loan type'' disclosure.

38(a)(3)(ii) Loan Features

The general classification of loans as fixed rate, adjustable rate and step rate would enable consumers to understand what loan type they are being offered and to shop for loan products according to consumers' needs and preferences. However, these broad categories of loan types are not sufficient to warn consumers about the potential risks that a specific loan may carry. As discussed previously, nontraditional mortgage products with negatively amortizing or interest-only payments grew in popularity in recent years, subjecting consumers to the risk of payment shock. Disclosures should clearly alert consumers to these features before the consumer becomes obligated on the loan. To alert consumers to potentially risky loan features, the Board is proposing to require an additional disclosure for each loan type in the loan summary if the loan has step-payments, payment option or negative amortization features, or interest-only payments.

Proposed § 226.38(a)(3)(ii) would require creditors to disclose whether a loan would have one or more of the following features: Step-payments if the legal obligation permits the periodic monthly payment to increase by a set amount for a specified amount of time; a payment option feature if the legal obligation permits the consumer to make payments that result in negative amortization and other types of payments; a negative amortization feature if the legal obligation requires the consumer to make payments that result in negative amortization—that is, the legal obligation does not permit the consumer to make payments that would cover all interest accrued or all interest accrued and principal; or an interest-only feature if the legal obligation permits or requires the consumer to make one or more regular periodic payments of interest accrued and no principal, and the legal obligation does not require or permit any payments that would result in negative amortization.

Proposed comment 38(a)(3)(ii)(A)–1 would offer an example of a step-payment feature. For example, if the consumer is offered a fixed-rate mortgage with 24 monthly payments at $1,000 that will later increase to $1,200 and remain at that level for a specified period of time, and the loan amortizes fully over the loan term, the creditor would disclose ''Fixed-Rate Mortgage, step-payments'' for the loan type in the loan summary. Proposed comment 38(a)(3)(ii)(B) and (C)–1 would clarify that a creditor should disclose the loan feature as either ''payment option'' or ''negative amortization'' but not both, whereas a loan may have both a ''step-payment'' feature and either a ''payment option'' or a ''negative amortization'' feature. Moreover, for a loan to have a ''payment option'' feature, all periodic payment choices must be specified in the legal obligation and must include a choice to make payments that may result in negative amortization. Proposed comment 38(a)(3)(ii)(D)–1 would provide that a creditor should not disclose both an ''interest-only'' feature and a ''payment option'' feature or ''negative amortization'' feature in a single transaction, whereas a loan may have both an ''interest-only'' feature and a ''step-payment'' feature.

38(a)(4) Total Settlement Charges

Currently, TILA and Regulation Z disclose settlement charges through the finance charge. TILA Section 128(a)(3) and § 226.18(d) require the creditor to disclose the finance charge. 15 U.S.C. 1638(a)(3). TILA Section 106(a) defines the ''finance charge'' as the ''sum of all charges, payable directly or indirectly by the person to whom the credit is extended, and imposed directly or indirectly by the credit or as an incident to the extension of credit.'' 15 U.S.C. 1605(a). Section 226.4(a) further defines the ''finance charge'' as ''the cost of consumer credit as a dollar amount.'' The finance charge includes any interest due under the loan terms as well as other charges incurred in connection with the credit transaction. *See* § 226.4(a) and (b).

Consumer testing indicated that participants did not understand the term ''finance charge.'' Most participants believed the term referred only to the total amount of interest they would pay if they kept the loan to maturity, but did not always realize that it also includes the fees and costs incurred as part of the credit transaction. Most participants did not find the finance charge useful in evaluating a loan offer.

The disclosure of settlement charges is governed by RESPA, 12 U.S.C. 2601–2617, and implemented by HUD under Regulation X, 24 CFR part 3500. Under RESPA and Regulation X, creditors must provide a GFE of settlement costs within three business days of application for a mortgage, which is the same time creditors must provide the early TILA disclosure. RESPA and Regulation X also require a statement of the final settlement costs at loan closing (''HUD–1 or HUD–1A settlement statement''). Under the new final rule for Regulation X, effective January 1, 2010, the GFE is subject to certain accuracy requirements, absent changed circumstances. RESPA and Regulation X do not, however, provide any remedies for a violation of the accuracy requirements.

Consumer testing consistently demonstrated that participants wanted to see settlement charges on the revised TILA disclosure. Participants stated that including such a disclosure would help them confirm information that the loan originator told them about the cost of the loan during the mortgage application process. During consumer testing, participants indicated that they were often surprised at the closing table by substantial increases in the settlement charges. Despite these changes, consumers reported that they proceeded with closing because they lacked alternatives (especially in the case of a home purchase loan), or were told that they could easily refinance with better terms in the near future. Participants indicated that they would like an estimate of their settlement charges as early as possible in the loan process, and that it would be helpful to have the settlement charges displayed in the context of the other loan terms, rather than on a separate GFE or HUD–1 or HUD–1A settlement statement.

For these reasons, the Board proposes § 226.38(a)(4) to require creditors to disclose the ''total settlement charges,'' using that term, as those charges are disclosed under Regulation X, 12 CFR part 3500. The proposed rule would further require, as applicable, a statement of the amount of the charges already included in the loan amount. Finally, the proposed rule would require disclosure of a statement, as applicable, that the total amount does not include a down payment, along with a reference to the GFE or HUD–1 for more details.

Proposed comment 38(a)(4)–1 would clarify that on the early TILA disclosure required by § 226.19(a)(1)(i), the creditor must disclose the amount of the ''Total Estimated Settlement Charges'' as disclosed on the GFE under Regulation X, 12 CFR part 3500, Appendix C. For the final TILA disclosure required by proposed § 226.19(a)(2)(ii), the creditor would be required to disclose the sum of the final settlement charges. The creditor would be permitted to use the sum of the ''Charges That Cannot Increase,'' ''Charges That In Total Cannot Increase By More Than 10%,'' and ''Charges That Can Change'' as would be disclosed in the column entitled ''HUD–1'' on page three of the HUD–1 or on page two of the HUD–1A settlement statement under Regulation X, 12 CFR part 3500, Appendix A. Alternatively, the creditor would be permitted to provide the consumer with the final HUD–1 or HUD–1A settlement statement. For transactions in which a GFE, HUD–1 or HUD–1A are not required, the proposed comment would clarify that the creditor may look to such documents for guidance on how to comply with the requirements of this section.

The Board recognizes that creditors are not currently required to provide the final settlement charges before consummation. Regulation X, 24 CFR 3500.10(b), permits the settlement agent to provide the completed HUD–1 or HUD–1A at settlement. However, proposed § 226.19(a)(2)(ii) would require the creditor to provide the TILA disclosure required by proposed § 226.38, including the total settlement charges disclosed under proposed § 226.38(a)(4), so that the consumer receives it at least three business days before consummation. In addition, under proposed § 226.19(a)(2)(iii)–Alternative 1, if anything changes during the three-business-day waiting period, including total settlement charges, the creditor would be required to supply another final TILA disclosure and three-business-day waiting period before consummation could occur. Consumers could waive the three-day waiting periods for bona fide personal financial emergencies.

The Board recognizes that proposed §§ 226.19(a)(2)(ii), 226.19(a)(2)(iii)–Alternative 1, and 226.38(a)(4) would require the creditor to disclose final settlement charge information several days in advance of consummation. These requirements would impose a cost on creditors, which may be passed on to consumers. Operational procedures and systems would need to be changed significantly to determine several days before closing the precise total amount of settlement charges that the consumer would pay at settlement. The Board believes, however, that the cost would be outweighed by the benefit to consumers of knowing their final total settlement charges three business days before consummation. This proposal would enable consumers to review and verify cost information in advance of consummation, and contact the creditor with questions or take other action, as appropriate.

38(a)(5) Prepayment Penalty

Current Disclosure Requirements

Under TILA Section 128(a)(11) and existing § 226.18(k)(1), if an obligation includes a finance charge computed by applying a rate to the unpaid principal balance (a ''simple-interest obligation''), creditors must disclose whether or not a penalty may be imposed if the consumer prepays the obligation in full. Comment 18(k)(1)–1 states that the term ''penalty'' refers only to charges that are assessed because of the prepayment in full of a simple-interest obligation, in addition to other amounts.

The existing model form in Appendix H–2 contains checkboxes for creditors to indicate whether a consumer ''may'' or ''will not'' have to pay a penalty if the consumer prepays the obligation in full. The Board adopted these checkbox options in 1980, in response to concerns that a statement that a prepayment penalty ''will be imposed'' would be misleading. The Board noted that many credit contracts allow a penalty to be imposed only if the loan is paid off within a certain time period after consummation or under other specific circumstances. *See* 45 FR 80648, 80682; Dec. 5, 1980.

Discussion

Consumer testing of the current disclosure showed that participants had difficulty identifying whether a loan would have a prepayment penalty and in what circumstances it would apply. For example, in the Board's consumer testing, participants did not understand that refinancing a loan or paying off the loan with proceeds from the sale of the home securing the loan could trigger a prepayment penalty. Similarly, consumer testing conducted by FTC staff found that two-thirds of participants who looked at a sample of the existing TILA disclosure showing a loan with a two-year prepayment penalty did not understand that a prepayment penalty would be charged if the consumer refinanced the loan two years after origination.[70] Some participants thought that a prepayment penalty could be charged only if they paid off their entire loan from their own funds, such as with money obtained through a sudden financial windfall.[71]

The Board developed and tested a revised prepayment penalty disclosure. Participants in the Board's consumer testing generally understood that if they prepaid the loan within the time specified in the disclosure, a penalty could be imposed. Participants also understood that the penalty could be imposed if they refinanced or sold the home during the time the penalty was in effect.

The Board's Proposal

Under proposed § 226.38(a)(5), if the legal obligation permits a creditor to impose a prepayment penalty the creditor must disclose in the ''Loan Summary'' section the period during which the penalty provision applies, the maximum possible penalty, and the circumstances in which the creditor may impose the penalty. If the legal obligation does not allow the creditor to impose a prepayment penalty, the creditor would make no disclosure regarding prepayment penalties in the ''Loan Summary'' section. (However, proposed § 226.38(d)(1)(iii) requires the creditor to disclose whether or not the legal obligation permits the creditor to charge a prepayment penalty in the ''Key Questions about Risk'' section.)

Maximum penalty amount. The Board is proposing to require creditors to disclose the maximum penalty possible under the legal obligation. Prepayment penalties may be substantial. The existence of a prepayment penalty may make it difficult to refinance a loan or sell a home. This may be particularly difficult for consumers who have adjustable rate loans or other loans that pose the risk of payment shock, as these consumers may believe that they can refinance or sell the home to avoid the increased payments. Thus, it is important for consumers to know the maximum penalty amount before they are obligated on a loan.

Under proposed § 226.38(a)(5) and (d)(1)(iii), creditors could not disclose the method or formula they use to determine the penalty with the disclosures required by § 226.38. Although some consumers might benefit from knowing how a prepayment penalty will be determined, the Board is concerned that consumers may be overloaded with information if the

[70] *Improving Consumer Mortgage Disclosures* at 78.

[71] *Id.*

calculation method is included with the segregated information. Many consumers would not read the prepayment penalty disclosure at all if it contains mathematical procedures and terms. Creditors may, of course, disclose how a prepayment penalty will be determined, as long as the disclosure is not disclosed together with the segregated disclosures.

Creditors also could not disclose a range of possible prepayment penalties or give examples of penalty amounts assuming the consumer prepaid at a hypothetical point in time under proposed § 226.38(a)(5) or (d)(1)(iii). The Board believes that it is important that prepayment penalty disclosures simply and clearly convey to consumers the potential magnitude of the prepayment penalty. Disclosures based on assumptions or averages could undermine the impact of the maximum penalty disclosure.

Additional penalty disclosures. Consumer testing indicated that some consumers do not understand that paying off the loan with the proceeds of a refinance loan or a home sale can trigger a prepayment penalty provision, as discussed above. Therefore, the proposed rule would require creditors to disclose the conditions upon which and the period during which they may impose a prepayment penalty.

It is important for a consumer to know what actions will trigger a prepayment penalty provision before obtaining a loan with such a provision. Consumers likely will not receive the loan agreement containing the prepayment penalty provision until consummation and may have little opportunity to review the agreement before becoming obligated. Moreover, a prepayment penalty is but one of many loan terms for consumers to consider at closing. The Board believes that including key information about a prepayment penalty provision in transaction-specific disclosures would help consumers avoid the uninformed use of credit.

Coverage. Comment 226.18(k)(1)–1 clarifies that § 226.18(k)(1) applies to transactions in which interest calculations take into account all scheduled reductions in principal, whether interest calculations are made daily or at some other interval. Proposed comment 38(a)(5)–1 is consistent with comment 18(k)(1)–1. Proposed § 38(j)(2) reflects existing § 226.18(k)(2) on rebate disclosures, as discussed below. Existing comment 18(k)–2 discusses cases where a single transaction involves both a rebate and a penalty. Proposed comment 38(a)(5)–8 reflects this existing commentary.

Definition of prepayment penalty. Comment 18(k)(1)–1 states that under § 226.18(k)(1) the term ''penalty'' refers only to those charges that are assessed because of the prepayment in full of a simple-interest obligation, in addition to other amounts. Comment 18(k)(1)–1 clarifies that interest charges for any period after prepayment in full is made and minimum finance charges are examples of prepayment penalties. The Board is proposing to revise comment 18(k)(1)–1 for clarity by substituting ''charges determined by treating the loan balance as outstanding for a period after prepayment in full and applying the interest rate to such 'balance' '' for ''interest charges for any period after prepayment,'' as discussed above. Proposed comments 38(a)(5)–2(i) and (ii) are consistent with comment 18(k)(1)–1, as it is proposed to be amended.

Proposed comment 38(a)(5)–2(iii) states that origination or other charges that a creditor waives on the condition that the consumer does not prepay the loan are prepayment penalties, for transactions secured by real property or a dwelling. Fees imposed for a preparing a payoff statement and performing other services when a consumer prepays the obligation would not be considered a prepayment penalty under the proposed rule, however. Such fees are not strictly linked to a consumer's prepaying the obligation, as they are charged at the end of a loan's term as well. The Board solicits comment on this distinction.

For purposes of some State laws, a minimum finance charge is not considered a prepayment penalty. For purposes of disclosure under TILA, a minimum finance charge is considered a prepayment penalty. Existing comment 18(k)(1)–1 and proposed comment 38(a)(5)–2 are designed to promote clear, consistent disclosure of charges creditors may impose when a consumer prepays the obligation in full. The proposed rule would not preempt State laws unless State law disclosure requirements are inconsistent with the rule, and then only to the extent of any inconsistency.

Existing comment 17(a)(1)–5(vii) allows creditors to disclose that the borrower may pay a minimum finance charge as information directly related to the penalty disclosure. Further, if a State or federal law prohibits creditors from charging a prepayment penalty but permits the charging of interest for some period after the consumer prepays from that prohibition, existing comment 17(a)(1)–5(xi) permits creditors to disclose that a consumer may have to pay interest for some period after prepayment as information directly related to the prepayment penalty disclosure. Comments 17(a)(1)–5(vii) and (xi), together with other commentary in comment 17(a)(1)–5, would not apply to transactions secured by real property or a dwelling, as discussed above.

Existing comment 18(k)(1)–1 states that loan guarantee fees are examples of charges that are not penalties. The Board proposes to retain this example in comment 38(a)(5)–2. (In a separate rulemaking, the Board proposed to remove the example of interim interest on a student loan as an example of charges that are not penalties. *See* 74 FR 12464, 12469; Mar. 29, 2009.)

Disclosed as applicable; disclosure content. Proposed comment 38(a)(5)–4 clarifies that if no prepayment penalty applies, creditors need not disclose that fact in the ''Loan Summary'' section of transaction-specific disclosures. Proposed § 226.38(d)(1)(iii) requires creditors to disclose whether or not the legal obligation permits the creditor to charge a prepayment penalty in the ''Key Questions about Risk'' section, however. Proposed comment 38(a)(5)–5 clarifies that creditors must disclose the maximum penalty as a numerical amount. This is consistent with the general rule of construction of the word ''amount'' required by § 226.2(b)(5).

Basis of disclosure. Proposed comment 38(a)(5)–6 explains how creditors determine the maximum penalty amount and contains examples that illustrate how those principles are applied. (Proposed comment 38(d)(1)(iii) states that creditors may rely on proposed comment 38(a)(5)–6 in determining the maximum prepayment penalty to be disclosed as one of the ''Key Questions about Risk'' disclosures.) Proposed comment 38(a)(5)–6 states that in all cases, the creditor should assume that the consumer prepays at a time when the prepayment penalty may be charged. The comment also states that if more than one type of prepayment penalty applies (for example, if the loan includes a minimum finance charge and the creditor may collect interest after prepayment), the creditor should include the maximum amount of each type of prepayment penalty in determining the maximum penalty possible.

Existing comment 18(k)(1)–1 clarifies that interest charges for any period after a consumer prepays in full and a minimum finance charge in a simple interest transaction are deemed to be prepayment penalties. Proposed comment 38(a)(5)–6(i) and (ii) clarifies that the amount of such charges must be counted in determining the maximum penalty.

Proposed comment 38(a)(5)–6(iii) provides examples of how creditors may calculate a maximum prepayment penalty where the creditor determines the penalty by applying a constant rate to the loan balance at the time of prepayment. In such cases, the prepayment penalty amount is largest when the balance is as high as possible. Proposed comment 38(a)(5)–6(iv) illustrates a method creditors could use to approximate the maximum penalty where the penalty amount depends on both the loan balance and the time at which the consumer prepays (for example, where a prepayment penalty on an adjustable-rate loan equals six months' interest payments). If the penalty amount depends on both the loan balance and the time at which the consumer prepays, under the proposed rule creditors would disclose the greater of (1) the penalty charged when the balance is the highest possible and (2) the penalty charged when the penalty rate is the highest possible (two-stage penalty calculation).

The two-stage penalty calculation produces an amount that approximates, but does not necessarily equal, the maximum prepayment penalty. The Board believes, however, that the amount determined using the two-stage penalty calculation ordinarily will be sufficiently close to the actual maximum prepayment penalty that it would be appropriate for creditors to use the method in complying with § 226.38(a)(5) and (d)(1)(iii). The Board solicits comment on whether the Board should permit creditors to use the two-stage penalty calculation where the penalty rate increases. Will this ''two-stage penalty calculation'' method produce a prepayment penalty amount that sufficiently approximates the maximum prepayment penalty possible for a loan? Are there cases where there will be a significant disparity between the maximum penalty determined using the two-stage penalty calculation and the actual maximum penalty?

Neither the simple penalty calculation nor the two-stage penalty calculation will enable the creditor to determine the maximum penalty where the penalty rate on a negatively amortizing loan declines. In such a case, the creditor must determine the maximum prepayment penalty by determining what the penalty would be at each point during the loan term while the penalty is in effect.

Requiring all creditors to base maximum penalty disclosures on the foregoing rules ensures standardization of disclosures. Allowing creditors to select their own assumptions about when consumers are likely to prepay would result in inconsistencies among the disclosures given by different creditors. The Board considered other approaches, such as requiring creditors to disclose the maximum prepayment penalty based on a single hypothetical point in time (for example, one year after origination). However, this approach would understate the amount consumers who prepay earlier would have to pay.

Timely payment assumed. Proposed comment 38(a)(5)–7 states that creditors may assume that the consumer makes payments on time and may disregard any possible inaccuracies resulting from consumers' payment patterns. This is consistent with existing comment 17(c)(2)(i)–3 and proposed clarifications in comment 17(c)(1)–1. Proposed comment 38(a)(5)–7 further clarifies that where the payment required by a legal obligation's terms is not a fully amortizing payment, the creditor must base disclosures on the required periodic payment and may not assume that the consumer will make payments that exceed the required payment.

38(b) Annual Percentage Rate

The Board proposes to improve the APR's utility to consumers by making it a more inclusive measure of the cost of credit, as discussed under § 226.4, and also by improving the manner in which the APR is disclosed on the TILA statement. Proposed § 226.38(b)(1) would require the APR to be disclosed, using the term ''annual percentage rate'' and with the description, ''overall cost of this loan including interest and settlement charges.'' Proposed § 226.38(b)(2) would require creditors to show the APR plotted on a graph, relative to (1) the ''average prime offer rate'' (APOR) for borrowers with excellent credit for a comparable loan type, in the week in which the disclosure is provided, and (2) the higher-priced loan threshold under § 226.35(a).[72] Proposed § 226.38(b)(3) would require an explanation of the APOR and higher-priced threshold. Proposed § 226.38(b)(4) would require creditors to disclose the average per-period savings from a 1 percentage-point reduction in the disclosed APR. Certain loans, including construction loans, would be excluded from proposed § 226.38(b)(2) and (b)(3).

[72] The Board issued § 226.35(a) in its 2008 HOEPA Final Rule; compliance with § 226.35(a) is mandatory beginning on October 1, 2009.

Current Rules

For closed-end credit, TILA Section 128(a)(4) and (a)(8) require creditors to disclose the ''annual percentage rate,'' using that term, together with a brief description such as ''the cost of your credit as a yearly rate.'' 15 U.S.C. 1638(a)(4), (a)(8). Section 226.18(e) implements these requirements. As discussed in proposed § 226.37, TILA Section 122 and § 226.17(a) require the APR, with the finance charge, to be more conspicuous than other disclosures except the disclosure of the creditor's identity. Changes to the requirements of § 226.17(a) are discussed under § 226.37.

Discussion

The APR is the only single, unified number available to help consumers understand the overall cost of a loan.[73] 15 U.S.C. 1638(a)(4). Before enactment of TILA in 1968, creditors could advertise a 6 percent loan rate, but were allowed to calculate the interest charged to the consumer by using a simple interest, an add-on, or a discount rate method.[74] Although the advertised loan rate would appear the same, the amount of interest consumers actually would pay over the loan term would differ greatly under each of these calculation methods.[75] In addition, consumers were forced to evaluate different components of a loan's costs, such as interest rate, points, and closing costs, when comparing competing loan offers. The APR standardizes the interest rate calculation and seeks to capture the overall cost of the credit offered so that consumers can compare competing loan more easily than if they had to evaluate the relationship and impact of different loan costs themselves.[76]

Participants in the Board's consumer testing generally did not understand the APR and often mistook it for the loan's interest rate.[77] The Board tested alternative descriptive statements and formats for the APR, but consumers continued to be confused by the APR. For example, some participants thought the APR reflected future adjustments to the interest rate, or the maximum possible interest rate for a variable rate loan. A few participants recognized that

[73] The *1998 Joint Report* at 8; *see also* Bd. Of Governors of Fed. Res. Sys., *1996 Report to Congress: Finance Charges for Consumer Credit under the Truth in Lending Act* at (April 1996).

[74] The *1998 Joint Report* at 8.

[75] *Id.*

[76] *Id.*

[77] *See also Improving Consumer Mortgage Disclosures* at 35 (finding that most respondents in consumer testing did not understand or were confused by the APR and generally mistook it for the contract interest rate).

the APR differed from the interest rate, but were unable to articulate the reason. In addition, when presented with two hypothetical loan offers, participants did not use the APR to compare and choose between the offers. Instead, participants chose a loan based on one or more of the following pieces of information: the interest rate, monthly payment, and settlement costs.

The Board's Proposal

The Board proposes to retain the APR disclosure, with several changes designed to improve the APR's utility for consumers. These proposed changes would apply only to closed-end transactions secured by real property or a dwelling. First, the Board proposes to revise the description to use simpler terminology. Proposed § 226.38(b)(1) would require creditors to disclose the APR, expressed as a percentage, together with a statement that it represents the overall cost of the loan, including interest and settlement charges. As discussed under § 226.4, the Board also proposes to make the APR more inclusive of the cost of credit. Moreover, under § 226.38(c), the interest rate would be disclosed on the form, which would help some consumers understand that the APR does not represent the interest rate.

Second, the proposed rule also would require creditors to disclose the APR using a graph that shows the consumer how the APR for the loan offered would compare to the average prime offer rate and the threshold for higher-priced loans under § 226.35(a). This disclosure would help consumers understand how the APR on the loan offered to them compares to APRs offered to borrowers with excellent credit for a similar loan type, and higher-priced loans which generally are made to borrowers who present higher risk. Such borrowers include those with blemished credit histories, or with high loan-to-value ratios.

The Board's consumer testing shows that consumers do not understand the APR's utility. Testing the APR with different names and descriptions did not measurably increase consumers' understanding of the APR. Although the APR was designed in part to facilitate comparison of competing loan products, testing suggests that most consumers do not compare competing loans by APR, probably because they receive only one TILA disclosure before they consummate a loan. If consumers comparison shop for a loan, they do so before they apply for a loan and likely shop based on oral quotes of interest rates and points.

The Board's testing suggests that with little understanding of the APR and no ready and appropriate basis for comparison, many consumers ignore the APR in favor of information they find more accessible, such as the loan's monthly payment or settlement costs. Therefore, the Board is taking two steps to improve the disclosure of the APR. The first step is designed to draw consumers' attention to the APR. To do so, the Board proposes to require disclosure of the consumer's APR on a graph to highlight the APR and distinguish it from other numerical disclosures, including the interest rate. Consumers would be more likely to notice the APR plotted on the graph, in a prominent location on the disclosure statement. Principles of consumer design provide that a graphic device accommodates different learning styles. And, consumer research has shown that use of graphics or similar visual devices help consumers attend to or notice important information.[78]

The Board's next proposed step is to present the APR in a context that is designed to facilitate understanding of the APR. The Board believes that consumers would be more likely to use the APR if it is shown to them in context of other rates, rather than in isolation as is presently often the case. Research on consumer behavior suggests that consumer choice is affected by whether a consumer is presented with a single option for a product or multiple options. Consumers making a choice in the presence of more than one option are more likely to make a selection based on the relative merits of the options presented, rather than on their own existing ''references'' for the value of the product.[79] Here, the Board believes that presenting consumers with information about other rates, current as of the week of the consumer's application, would help consumers make more informed decisions about the loan offered.

Testing suggests that showing the consumer the APR in context of information about other APRs would result in consumer benefits. For example, the APR graph would cause consumers to ask the creditor questions about the rate offered to them and when applicable, why it differs from the average APR offered to borrowers with excellent credit histories. The proposed APR disclosure would enable consumers to determine whether they are being offered a loan that comports with their creditworthiness. A borrower who knows his or her credit history is excellent or very good would be informed that the loan offered is higher-priced. Participants in the Board's testing stated that if they knew they had excellent credit, they would ask the lender why they were being offered a higher-priced loan and what they would need to do to get a better offer. The Board notes that some participants indicated that the disclosed APR, even if higher-priced, was lower than the interest rate on their current loan and thus was attractive to them. Nevertheless, while some consumers may not be prompted by the APR graph to seek information about improved loan terms, testing suggests others may do so and benefit as a result.

The Board recognizes that not all consumers are aware of their credit history, and thus may not be able to assess whether the loan offered is consistent with their credit standing. The Board anticipates that the APR graph would cause some consumers to investigate their credit reports. If there are errors, these consumers could take steps to resolve the errors. If consumers in fact have impaired credit, some consumers might consider whether to delay seeking a loan until they could repair their credit standing.

In some instances the APR graph may be potentially confusing. That is, a loan may be a higher-priced loan for reasons other than the borrower's credit history. For example, a consumer might have little home equity, resulting in a high loan-to-value ratio and a higher APR. The Board believes that even in such cases, the APR graph nonetheless would be beneficial to consumers. It would prompt the consumer to ask questions, and creditors should be able to explain to consumers why the APR on a loan is higher-priced. In many cases the explanation may help the consumer determine whether they could take steps to get a lower APR. For example, if the creditor explains that the offered loan is a higher-priced loan because of a low down-payment, the borrower would be alerted that providing a larger down payment would result in a reduced APR and cost savings.

The Board also notes that certain loans may be higher-priced loans simply because of the loan type. For example, loans that exceed the threshold amount for eligibility for purchase by Fannie

[78] Kozup, John, Elizabeth Howlett, and Michael Pagano. 2008. ''The Effects of Summary Information on Consumer Perception of Mutual Fund Characteristics.'' *The Journal of Consumer Affairs*, vol. 42. *See also* Testimony of John Kozup, Assistant Professor, Department of Marketing, and Director, Center for Marketing and Public Policy, Villanova University; *http://www.federalreserve.gov/events/publichearings/hoepa/2006/20060711/transcript.pdf*.

[79] *See, e.g.*, Hsee, Christopher K. and France Leclerc. 1988. ''Will Products Look More Attractive When Presented Separately or Together?'' *Journal of Consumer Research*, vol. 25.

Mae and Freddie Mac, known as ''nonconforming'' or ''jumbo loans,'' may tend to be higher-priced loans because of the method for calculating the APOR. The APOR is the average APR for *conforming* loans offered to borrowers with excellent credit. In the case of such loans, creditors would have to explain to consumers why the loan's APR is higher-priced.

Third, the proposal would require the creditor to disclose the average per-period savings from a 1 percentage-point reduction in the disclosed APR. The Board believes that showing consumers the relationship between the APR and a concrete dollar figure would help make the possible benefits of obtaining better loan terms more concrete for consumers. Showing potential savings that could result from a lower APR would help encourage consumers to shop and negotiate for better loan terms, or as discussed, to increase their downpayment, resolve errors in their credit report, or seek to improve their credit standing.

38(b)(2)

Proposed § 226.38(b)(2) would require a graph indicating the consumer's APR within a range of APRs beginning with the average prime offer rate (''APOR''), as defined in § 226.35(a)(2), including the higher-priced mortgage loan threshold, as defined in § 226.35(a)(1), and terminating four percentage points greater than the higher-priced mortgage loan threshold. Proposed § 226.38(b)(3) would require a statement of the APOR as defined in § 226.35(a)(2), and the higher-priced mortgage loan threshold, as defined in § 226.35(a)(1), current as of the week the disclosure is produced. The graphic would contain different shaded areas using different scales for the range between the APOR and the higher-priced mortgage loan threshold, and for the range above the higher-priced mortgage loan threshold. The graphic would also label the range above the higher-priced mortgage loan threshold as the ''high-cost zone.''

Creditors would use the Board's table of average prime offer rates to find the APOR for the loan type that matches the loan being disclosed, for the week in which the creditor provides the disclosure. Creditors would follow the Board's guidance in commentary to § 226.35(a) in determining how to select the appropriate APOR. In the text explaining the APOR, creditors may include a statement clarifying that the APOR is for conforming loans only.

The Board requests comment on any potential operational difficulty in producing the graph proposed in § 226.38(b)(2) in an accurate and timely manner. Comment is also sought on whether a different graphical device would better draw consumers' attention to the APR and illustrate the APR's utility to consumers.

38(b)(3)

To help consumers navigate the information provided by the graph, proposed § 226.38(b)(3) would require an explanation of the average prime offer rate as defined in § 226.35(a)(2), and the higher-priced mortgage loan threshold, as defined in § 226.35(a)(1). Participants in the Board's consumer testing found this statement helpful in understanding the information in the graph.

38(b)(4)

Proposed § 226.38(b)(4) would provide how creditors must calculate the average per-period savings that would result from a 1 percentage-point reduction in the APR. (This discussion refers to monthly savings because most mortgage loans require monthly payments.) Creditors would calculate the average per-month savings by reducing the interest rate (or rates in the case of an ARM, as discussed in comment 34(b)(4)–1) by 1 percentage point, computing a hypothetical total of payments reflecting the payment schedule at the lower rate or rates. The creditor would divide the difference between (1) the total of payments disclosed under proposed § 226.38(e)(5)(i), and (2) the hypothetical total of payments by the number of payment periods required under the terms of the legal obligation. The creditor would report the results of this calculation as the average savings each month from a 1 percentage-point reduction in the APR. Proposed comment 38(b)(4)–1 would provide guidance on this method, and would include examples for fixed- and adjustable-rate mortgages.

The Board notes that the proposed method does not result in an exact 1 percentage-point reduction in APR, but is likely to be within a few basis points of a 1 percentage-point reduction. The results would be sufficiently accurate to show consumers that a lower APR will yield savings. Methods that might result in an actual 1 percentage-point reduction in the APR would likely be more complicated and would vary depending on the terms of the loan, such as whether the rate is variable and whether the payments amortize the loan. The Board believes that any additional consumer benefit from disclosing the precise 1 percentage-point APR reduction would not be sufficient to offset the costs of a more complex calculation method. The Board seeks comment, however, on its proposed method and whether another method would achieve the objectives of the disclosure without imposing undue compliance burdens.

38(b)(5) Exemptions

Proposed section 226.38(b)(5) would exempt construction loans, bridge loans, and reverse mortgages from the requirement to show the APR plotted on a graph (§ 226.38(b)(2)) and the statement of the APOR and the higher-priced loan threshold (§ 226.38(b)(3)). The exempted transactions are also exempt from the definition of a higher-priced mortgage, under § 226.35(a)(3) in the Board's 2008 HOEPA Final Rule. The Board does not publish an average prime offer rate for construction, bridge, or reverse mortgage loans. Thus, an exemption seems appropriate. The Board seeks comment, however, on whether these transactions should nevertheless be subject to § 226.38(b)(2) and (3).

38(c) Interest Rate and Payment Summary

Proposed § 226.38(c) provides requirements for disclosure of the contract interest rate and the periodic payment for transactions secured by real property or a dwelling. The information proposed to be required by this paragraph must be in the form of a table, as provided in § 226.38(c)(1), substantially similar to Model Forms H–19(A), H–19(B), or H–19(C) in Appendix H. Additional formatting requirements would be provided in § 226.37. The rules for disclosing the interest rate and periodic payments for an amortizing loan are provided in proposed §§ 226.38(c)(2)(i) and 226.38(c)(3). Rules for disclosing the interest rate and periodic payments for a loan with negative amortization are in proposed §§ 226.38(c)(2)(ii) and 226.38(c)(4). Special rules for disclosing balloon payments are found in proposed § 226.38(c)(5). Additional explanations of introductory rates and negative amortization are contained in proposed §§ 226.38(c)(2)(iii) and 226.38(c)(6), respectively. Proposed § 226.38(c)(7) provides definitions for certain terms used in § 226.38(c).

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. 1648(a)(6). Currently, § 226.18(g) implements TILA 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.[80] The creditor must provide these disclosures on the TILA statement within three business days of receiving the consumer's written application, as provided in § 226.19(a).

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. However, the disclosures must reflect a discounted or premium initial interest rate 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.''

TILA Section 128(b)(2)(C), as recently 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. * * *'' TILA Section 128(b)(2)(C), 15 U.S.C. 1638(b)(2)(C). Creditors must provide these disclosures within three business days of receipt of the consumer's written application, as provided in § 226.19(a). 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.'' 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).

The Board's Proposal

The Board proposes to add new § 226.38(c) to implement TILA Section 128(a)(6) and Section 128(b)(2)(C) for all closed-end transactions secured by real property or a dwelling.[81] (For all other closed-end credit transactions, § 226.18(g) would continue to provide the rules for disclosing payments). Section 226.38(c) would require 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 monthly payments would be 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 include an itemized 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 payments 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 would be required for loans with negative amortization. Creditors must provide the information about interest rates and payments in the form of a table, and creditors would not be permitted to include other unrelated information in the table.

Scope of proposed § 226.38(c). TILA Section 128(b)(2)(C) applies to all transactions secured by a dwelling. The Board proposes to expand the requirement in Section 128(b)(2)(C) to include loans secured by real property that do not include a dwelling. As discussed in § 226.19(a), 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 would 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 proposes 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 examples of increased interest rates and payments would help consumers understand the risks involved in certain loans. The Board also proposes to revise the label for the interest rate and payment information from the statutory language, ''Payment Schedule: Payments Will Vary Based on Interest Rate Changes,'' based on plain language principles, to make the disclosure more readily understandable.

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, by far the most common answers were that they wanted to obtain the lowest interest rate possible and that they wanted the loan with the lowest possible monthly payment. However, 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. Testing conducted on the current transaction-specific TILA disclosures indicated that consumers would like to see the interest rate disclosed on the form.

In addition, testing indicated that the current TILA payment schedule, which does not show the relationship between interest rate and payment, is ineffective at communicating to consumers what could happen to their payments over time on an ARM. Most participants said they liked the current presentation of the payments because it was specific and detailed. However, when shown a payment schedule for an ARM with an

[80] 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 proposing revisions to these disclosures.

[81] 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. Proposed § 226.38(f)(3) implements this aspect of Section 128(b)(2)(C).

introductory rate, 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 proposal, the interest rate and payment would be 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 would indicate changes in the adjustable interest rate over time. In addition, payment changes that are not based on adjustments to the interest rate would also be 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 a 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 would be better able to determine if a adjustable rate or payment loan will be affordable and appropriate for their individual circumstances.

Definitions for § 226.38(c). Proposed § 226.38(c) uses several terms that are defined in proposed § 226.38(c)(7). Under § 226.38(c)(7), the terms ''adjustable-rate mortgage,'' ''step-rate mortgage,'' and ''interest-only'' would have the same meanings as in § 226.38(a)(3). An ''amortizing loan'' would be defined as a loan in which the regular periodic payments cannot cause the principal balance to increase; the term ''negative amortization'' would mean a loan in which the regular periodic payments may cause the principal balance to increase. Finally, the tern ''fully-indexed rate'' would mean the interest rate calculated using the index value and margin.

Proposed § 226.38(c)(2)(i) and (c)(3) would require disclosure of interest rates and payment amounts for amortizing loans. Proposed § 226.38(c)(7) defines an amortizing loan as one in which the regular periodic payments cannot cause the principal balance to increase. Thus, loans with interest-only payments are amortizing loans. If an escrow account will be established for an amortizing loan, creditors would be required to itemize the payment to show amounts to be included for taxes and insurance. *See* proposed § 226.38(c)(3)(i)(C). Proposed §§ 226.38(c)(2)(ii) and 226.38(c)(4) would require a special table for disclosures of interest rates and payment amounts for negatively amortizing loans. For such loans in which the consumer may choose between several payment options, the table will show only two: the minimum required payment option, and the fully amortizing option. Creditors may, however, disclose other payment options to the consumer, outside the segregated information required by this section.

38(c)(1) Format

Proposed § 226.38(c)(1) would require the interest rate and payment information to be disclosed in the form of a table. This would 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 the proposal, all disclosures must be in a minimum 10 point font, including the table required under § 226.38(c), to ensure that they are clear and conspicuous. *See* proposed § 226.37(a).

The Board's proposal would prescribe the number of interest rates and payments that could be shown in a table. The number of columns and rows for the table required by this part would vary depending on whether the loan is an amortizing loan and whether it has adjustable rates. However, tables disclosed under this section would have no more than 5 columns across, and creditors would not include information in the table that is not required under 226.38(c), to avoid information overload. Model and Sample Forms would be provided in Appendix H.

38(c)(2) Interest Rates

38(c)(2)(i) Amortizing Loans

Proposed § 226.38(c)(2)(i) would provide disclosure of interest rates for amortizing loans. For a fixed-rate mortgage with no scheduled payment increases or balloon payments, the creditor would disclose only one interest rate. Fixed-rate loans with payment increases would require the creditor to disclose the interest rate with each increase. 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, proposed § 226.38(c)(2)(i)(A) would require creditors to disclose the interest rate applicable at consummation. If the transaction does not provide for any payment increases, only one interest rate would be disclosed. However, some fixed-rate mortgages will have scheduled payment increases and in those cases the creditor must show the interest rate again, even though it is redundant, as discussed under § 226.38(c)(2)(i)(C) below.

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

Interest rates at consummation, maximum possible at first adjustment, and maximum possible interest rate. As discussed, TILA Section 128(b)(2)(C) requires creditors to disclose examples of payment increases including the maximum possible payment, for adjustable-rate mortgages and mortgages where payments may vary. Under § 226.38(c)(2)(i), creditors would disclose more than one interest rate and corresponding monthly payment for adjustable-rate mortgages and step-rate mortgages. Under proposed § 226.38(c)(2)(i)A)(I), the creditor must provide the interest rate at consummation, and the period of time until the first adjustment. If the interest rate at consummation is less than the fully-indexed rate (the sum of the index and margin at consummation), the interest rate must be labeled as ''introductory.'' Additional explanation of discounted introductory rates is required in proposed § 226.38(c)(2)(iii), as discussed below.

Maximum at first adjustment. The Board proposes 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). Proposed § 226.38(c)(2)(i)(B)(1) requires 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 would be required to be disclosed. The creditor would take into account any limitations on interest rate increases when determining the interest rate to be disclosed under § 226.38(c)(2)(i)(B)(2). If the interest rate may reach the maximum possible at the first adjustment, the creditor should disclose the rate as the maximum possible as discussed below.

The Board proposes to require disclosure of the maximum interest rate at first adjustment because many consumers may take out adjustable-rate mortgages, planning to sell the home or refinance the loan before the first interest rate adjustment. It is important for consumers to know how much their rate and payment might increase at that point, if they are unable to refinance or sell the home before the first adjustment. The Board believes that for the same reason, the first interest rate increase should be shown for step-rate mortgages. Although such mortgages do not present the uncertainty that an adjustable-rate mortgage does, consumers need to be informed of what their rate will increase to at the first increase. Consumer testing conducted for the Board shows that most consumers would find this information useful in determining whether the loan is affordable and suitable to their needs.

Maximum possible interest rate. Proposed § 226.38(c)(2)(i)(B)(3) would require creditors to disclose the maximum interest rate that could apply, and the earliest possible year in which that rate could apply, as required by TILA Section 128(b)(2)(C). The Board proposes to require this disclosure for step-rate mortgages as well, because the rate and payment will increase in such loans. Consumer testing conducted for the Board 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 limitation on interest rate increases, then the table required by proposed § 226.38(c) would have at least three columns; if the transaction has no intermediate limitation on interest rates then the table would 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 this ''interest-only'' period, the borrower must begin making larger payments to cover both interest accrued and principal. Proposed § 226.38(c)(2)(i)(C) would provide that, where such an increase will not coincide with an interest rate adjustment or increase, 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 in which the increase would occur. The creditor must include a description such as ''first increase'' or ''first adjustment.'' Thus, for a fixed-rate mortgage, the creditor would show the same interest rate twice (and the corresponding payments as discussed in § 226.38(c)(4) below). The Board believes this would 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 proposed § 226.38(c)(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 would 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. Proposed comment 38(c)(2)(i)(C)–1 provides clarifying examples. The Board is not aware of step-rate loans with interest-only features; however, if such a loan is offered, creditors would disclose the payment increase in the same manner as for an adjustable-rate mortgage.

38(c)(2)(ii) Negative Amortization Loans

Proposed § 226.38(c)(2)(ii) would require disclosure of the interest rate applicable at consummation. Many payment option 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 payment option loans, the creditor would 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 would disclose that rate for the first and second scheduled payment increases, as explained more fully in § 226.38(c)(4) below, and in the last column, when the loan has recast and the consumer must first make a fully amortizing payment. The proposed 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 proposed rules for disclosing the interest rate on a loan with negative amortization are discussed under 38(c)(6) Special Disclosures for Loans with Negative Amortization, below.

38(c)(2)(iii) Introductory Rate Disclosure for Adjustable-Rate Mortgages

Many adjustable-rate mortgages have an introductory or teaser rate, set below the index and margin used for later adjustments. Proposed § 226.38(c)(2)(iii) would require a special disclosure in the case of an 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. However, 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 proposes to require an explanation of the introductory rate below the table itself. Proposed § 226.38(c)(2)(iii) would require 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 would also disclose the fully indexed rate that otherwise would apply at consummation. Proposed § 226.37(d)(4) would provide that this disclosure must be prominent and placed in a box under the table.

38(c)(3) Payments for Amortizing Loans

38(c)(3)(i) Principal and Interest Payments

Section 226.38(c)(3)(i) would require disclosure of the principal and interest payment that corresponds to each interest rate disclosed under proposed § 226.38(c)(2)(i). Special itemization of the payment is required, however, if the loan permits the consumer to make any payments that will be applied only to interest accrued. Proposed § 226.3(c)(3)(ii)(C) would require disclosure of an estimate of the amount of taxes and insurance, including mortgage insurance. Proposed § 226.3(c)(3)(i)(D) would require disclosure of the estimated total payment including principal, interest, and taxes and insurance.

Principal and interest payments. Proposed § 226.38(c)(3)(i) would require the disclosure of payment amounts that correspond to the interest rates disclosed under § 226.38(c)(2)(i). Proposed comment 38(c)(3)–1 would clarify that the interest rate and payment amount applicable at consummation are required to be disclosed for all loans. In addition, the comment would clarify that if a payment amount is required to be disclosed under more than one subparagraph, the payment should only be disclosed once. For example, in an adjustable-rate transaction with a balloon payment, if the balloon payment will occur at the same time the loan may reach its maximum interest rate, only one disclosure of the interest rate and payment is required. Proposed comment 38(c)(3)–2 provides examples of the types of loans that trigger additional payment disclosures.

Fixed-rate mortgages. Under proposed § 226.38(c)(3)(i)(A), for fixed-rate transactions where the regular periodic payment fully amortizes the loan and there are no scheduled payment increases (such as upon the expiration of an interest-only feature), the payment amount including both principal and interest would be required to be disclosed.

Fixed-rate interest-only loans. For fixed-rate transactions in which the consumer may make one or more interest-only payments, proposed § 226.38(c)(3)(i)(B) would require disclosure of the payment at any scheduled increase in the payment amount and the date on which the increase is scheduled to occur. 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 would be required to be disclosed. Similarly, in a fixed-rate balloon loan, the balloon payment must be disclosed, but it would be disclosed under the table pursuant to § 226.38(c)(5).

Adjustable-rate and step-rate transactions. Under proposed § 226.38(c)(3)(i), for adjustable-rate and step-rate transactions, a payment amount corresponding to each interest rate in § 226.38(c)(2) would be required to be disclosed.

Adjustable-rate interest-only and balloon loans. For adjustable-rate transactions in which the consumer may make interest-only payments, proposed § 226.38(c)(3)(ii) would require additional disclosures. Section 226.38(c)(3)(i)(B) would require 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. In addition, for an adjustable-rate balloon loan, if the balloon payment will not coincide with either the first interest rate adjustment or the time when the interest rate reaches its maximum, the balloon payment is required to be disclosed separately, below the table, in accordance with § 226.38(c)(5).

Principal and interest payment itemization. Under proposed § 226.38(c)(3)(i) and (ii), the format of the payment disclosure would vary depending on whether all regular periodic payment amounts will include principal and interest. If all regular periodic payments include principal and interest, under § 226.38(c)(3)(i) each payment amount would be listed in a single row in the table with a description such as principal and interest (except that a balloon payment would be disclosed in accordance with § 226.38(c)(5)). If any regular periodic payment amounts will include interest but not principal, under § 226.38(c)(3)(ii) all payments for the loan must be itemized into principal and interest. For a payment that includes no principal, the creditor must 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 proposes this itemization and labeling to emphasize for consumers the impact of making interest-only payments. 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 without this emphasis and the statement in the loan summary required in proposed § 226.38(a)(3).

Balloon payment. Under proposed § 226.38(c)(5)(i), if a payment amount is 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 226.38(c)(5)(i) would clarify that a payment is a balloon payment if it is more than twice the amount of other payments. This is consistent with how balloon payments are defined for purposes of restrictions on balloon payments for higher-priced and HOEPA loans.

Escrows; mortgage insurance premiums. Proposed § 226.38(c)(3)(i)(C) would provide that if an escrow account will be established, the creditor must disclose the estimated payment amount for taxes and insurance, including mortgage insurance. For transactions secured by real property or a dwelling, creditors would 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 in order for consumers to fully 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 would be included in the table to make it easier for consumers to identify whether there is an escrow and how much of their payment would apply to the escrow.

Proposed comment 38(c)(3)(i)(C)–1 would clarify the types of taxes and insurance that would be required to be included in the estimate. Proposed comment 38(c)(i)(C)–2 would provide guidance on how to determine the length of time for which mortgage insurance payments must be included in the estimate. Under the proposed comment, which is substantially similar to current comment 18(g)–5, 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.

The Board solicits comment on whether premiums or other amounts for credit life insurance, debt suspension and debt cancellation agreements and other similar products should be included or excluded from the disclosure of escrows for taxes and insurance. Including such amounts in the estimated escrow and monthly payment, particularly on the early TILA disclosures delivered within three days of application, may cause some consumers to believe these products are required as part of the loan agreement. This may affect consumers' ability to weigh the relative merits of credit insurance and other similar products and determine whether the product is appropriate for their circumstances.

Total periodic payments. Proposed § 226.38(c)(3)(i)(D) would require disclosure of the total estimated monthly payment. The total estimated monthly payment is the sum of the principal and interest payments and the estimated taxes and insurance payments required to be disclosed in § 226.38(c)(3)(i)(C).

38(c)(4) Periodic Payments for Loans With Negative Amortization

For each interest rate disclosed under § 226.38(c)(2)(ii), the creditor would disclose a corresponding payment. One row of the table would show 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 date, and that the consumer makes only fully amortizing payments. The other row of the table would show the minimum required payment for each rate, until the recast point. At the recast point, the minimum payment row would show the fully amortizing payment. For purposes of the minimum payment row, creditors must assume the interest rate reaches the maximum at the earliest date, and that the consumer makes only the minimum required payment for as long as permitted under the terms of the legal obligation.

Minimum payment amounts. Proposed § 226.38(c)(4)(i)(A) would require disclosure of the minimum required payment at consummation. The proposal would require a disclosure of the amount of the minimum payment applicable for each interest rate required to be disclosed under § 226.38(c)(2)(ii), and the date. Under proposed § 226.38(c)(4)(i)(C), the creditor must provide a statement that the minimum payment will cover only some of the interest accrued and none of the principal, and will cause the principal balance to increase. The Board proposes this required statement to ensure that consumers are informed about the consequences of making minimum payments. As stated above, 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.

Payment increases. As noted above, many payment option loans do not have interest rate caps, and thus the interest rate may reach its maximum possible amount at the first interest rate adjustment. However, such loans may have limits 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 not apply either at a specific time, such as at the fifth year of the loan, or when the loan balance reaches a certain maximum.) Under proposed § 226.38(c)(2)(ii)(D), 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 would be 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 one additional minimum payment adjustment would be required.

Fully amortizing payment amount. Proposed § 226.38(c)(4)(iii) would require disclosure of the amount of the fully amortizing payment, assuming that the consumer makes only fully amortizing payments beginning at consummation. The fully amortizing payment row must be filled in for each interest rate required to be disclosed under § 226.38(c)(4)(ii) and (iv). 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.

Statement of balance increase and other information. Proposed § 226.38(c)(4)(vi) would require 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 should help consumers understand the risks of making minimum payments.

In addition, the explanation preceding the table would provide the consumer's option to make fully amortizing payments or to make minimum payments, the maximum possible interest rate, the earliest number of months or years in which the interest rate could reach its maximum, and the amount of estimated taxes and insurance included in each payment disclosed. If the maximum interest rate may be reached in less than a year the statement would be required to provide the number of months after consummation in which the interest rate may reach its maximum, otherwise the statement would provide the number of years. In addition, the creditor would 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.

38(c)(6) Special Disclosures for Loans With Negative Amortization

Some mortgage transactions permit the borrower to make payments that are insufficient to cover all of the interest accrued, and the unpaid interest is added to the loan's balance. Thus, although the borrower is making payments, the loan balance is increasing instead of decreasing. Negative amortization could occur on a fixed-rate mortgage or an adjustable-rate mortgage. Mortgages with negative amortization were relatively rare until the early part of this decade, when the ''payment option'' loan began to grow in popularity.[82] Payment option loans have adjustable rates, and allow the borrower to choose among up to five monthly payment options, including a minimum payment that would result in negative amortization. Other options would include an interest-only option, a fully amortizing option, and the option to make extra payments of principal and pay the loan off early. Typically, payment option loans permit consumers to make minimum payments for a limited time, such as for the first five years following consummation or until the loan's principal balance reaches 115 percent of the original balance, whichever occurs first. Upon either event, the consumer must begin to make fully amortizing payments.

Payment option loans and other nontraditional mortgages can result in significant ''payment shock'' for borrowers, particularly when the loan ''recasts'' and a fully amortizing payment must be made. Concerns about payment shock led the Board, OCC, OTS, FDIC and NCUA to propose supervisory guidance on nontraditional mortgages in 2005, and issue final guidance in October 2006.[83] The guidance emphasizes that institutions should use prudence in underwriting nontraditional mortgages, and should provide accurate and balanced information to consumers before the consumer is obligated on such a mortgage. The agencies published illustrations to assist financial institutions in providing information that would help consumers understand the risks involved in nontraditional mortgages.[84] Those illustrations were not consumer tested.

The Board's consumer testing indicates that the unusual and complex nature of negative amortization loans requires a different approach to the

[82] Interagency Guidance on Nontraditional Mortgage Product Risks, 71 FR 58609; October 4, 2006.

[83] *Id.*

[84] 72 FR 31825, 318231; Jun. 8, 2007

disclosure of interest rates and payments than for amortizing loans. Nearly all participants in the Board's consumer testing were unfamiliar with the concept of negative amortization, and technical explanations of negative amortization proved challenging for them. The Board believes that selected information about payment option loans may be more effective in conveying the risks of such mortgages than extensive text explaining negative amortization and its impact.

Accordingly, the Board developed and tested an interest rate and payment summary table designed to inform consumers about the risks of a payment option loan. The proposed rules would also require disclosure of the interest rate and payment for a loan with negative amortization that is not an adjustable rate mortgage. However, the Board found no examples of such loans in the marketplace, and seeks comment on whether such loans are offered and if so, whether proposed § 226.38(c) provides sufficient guidance on disclosing such loans.

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 would have the unintended consequence of 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.

In addition, to help consumers navigate the information in the table, proposed § 226.38(c)(6) would require a statement directly above the interest rate and payment summary table explaining that the loan offers payment options. A disclosure of the maximum possible balance would also be required, directly below the table, to help ensure that consumers understand the nature and risks involved in loans with negative amortization.

38(d) Key Questions About Risk

Based on consumer testing, as discussed in greater detail in § 226.19(b)(2) above, the Board proposes to require creditors to disclose certain information grouped together under the heading ''Key Questions about Risk,'' using that term. This disclosure would be specific to the loan program for which the consumer applied. Proposed § 226.38(d)(1) would require the creditor to disclose information about the following three terms: (1) Rate increases, (2) payment increases, and (3) prepayment penalties. Proposed § 226.38(d)(2) would require the creditor to disclose information about the following six terms, but only if they are applicable to the loan program: (1) interest-only payments, (2) negative amortization, (3) balloon payment, (4) demand feature, (5) no-documentation or low-documentation loans, and (6) shared-equity or shared-appreciation. The ''Key Questions about Risk'' disclosure would be subject to special format requirements, including a tabular format and a question and answer format, as described under proposed § 226.38(d)(3).

38(d)(1) Required Disclosures

As noted above, proposed § 226.38(d)(1) would require the creditor to disclose information about the following three terms: (1) Rate increases, (2) payment increases, and (3) prepayment penalties. The Board believes that these three factors should always be disclosed. Rate and payment increases pose the most direct risk of payment shock. In addition, consumer testing consistently showed that interest rate and monthly payment were the two most common terms that participants used to shop for a mortgage. The Board also believes that the prepayment penalty is a key risk factor because it is critical to the consumer's ability to sell the home or refinance the loan to obtain a lower rate and payments. While the other risk factors are important if contained in the loan program, the Board believes it appropriate to include those factors only as applicable to avoid information overload.

Rate increases. Proposed § 226.38(d)(1)(i) would require the creditor to indicate whether or not the interest rate on the loan may increase. If the interest rate on the loan may increase, then the creditor would indicate the frequency with which the interest rate may increase and the date on which the first interest rate increase may occur. Proposed comment 38(d)(1)–1 would clarify that disclosing the date means that the creditor must disclose the calendar month and year.

Payment increases. Proposed § 226.38(d)(1)(ii) would require the creditor to indicate whether or not the periodic payment on the loan may increase. If the periodic payment on the loan may increase, then the creditor would be required to indicate the date on which the first payment increase may occur. For payment option loans, the creditor would be required to disclose the dates on which the full and *minimum* payments may increase. Proposed comment 38(d)(1)–1 would clarify that disclosing the date means that the creditor must disclose the calendar month and year.

Prepayment penalty. As currently required under TILA Section 128(a)(11), 15 U.S.C. 1638(a)(11), and § 226.18(k)(1), if the obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance, proposed § 226.38(d)(1)(iii) would require the creditor to indicate whether or not a penalty will be imposed if the obligation is prepaid in full. If the creditor may impose a prepayment penalty, the creditor would disclose the circumstances under which and period in which the creditor would impose the penalty and the amount of the maximum penalty. Because of the importance of prepayment penalties, the proposed rule would also require disclosure of prepayment penalties, if applicable, under proposed § 226.38(a)(5). To avoid duplication, proposed comments 38(d)(1)(iii)–1 to –3 would cross-reference proposed comments 38(a)(5)–1 to –3 for information about whether there is a prepayment penalty, and examples of charges that are or are not prepayment penalties. In addition, proposed comment 38(d)(1)(iii)–4 would cross-reference comment 38(a)(5)–6 to determine the maximum prepayment penalty. Proposed comment 38(d)(1)(iii)–5 would cross-reference comment 38(a)(5)–7 for information about any differences resulting from the consumer's payment patterns and basing disclosures on the required payment for a negative amortization loan. Although under proposed § 226.38(a)(5) the disclosure of the prepayment penalty would appear on the first page of the transaction-specific TILA disclosure only if this feature were present in the loan, the disclosure would always appear on the second page in the ''Key Questions'' disclosure in order for the consumer to verify whether or not there is a prepayment penalty associated with the loan.

38(d)(2) Additional Disclosures

As noted above, proposed § 226.38(d)(2) would require the creditor to disclose information about the following six terms, as applicable: (1) Interest-only payments, (2) negative amortization, (3) balloon payment, (4) demand feature, (5) no-documentation or low-documentation loans, and (6) shared-equity or shared-appreciation. Proposed comment 38(d)(2)–1 would clarify that ''as applicable'' means that any disclosure not relevant to a particular loan may be omitted. Although consumer testing showed that some participants felt reassured by seeing all of the risk factors whether the factors were a feature of the loan or not, the Board is concerned about the potential for information overload if the entire list is included.

Interest-only payments. Proposed § 226.38(d)(2)(i) would require the creditor to disclose that periodic payments will be applied only toward interest on the loan. The creditor would also disclose any limitation on the number of periodic payments that will be applied only toward interest on the loan, that such payments will cover the interest owed each month, but none of the principal, and that making these periodic payments means the loan amount will stay the same and the consumer will be not have paid any of the loan amount. For payment option loans, the creditor would disclose that the loan gives the consumer the choice to make periodic payments that cover the interest owed each month, but none of the principal, and that making these periodic payments means the loan amount will stay the same and the consumer will not have paid any of the loan amount.

Negative amortization. Proposed § 226.38(d)(2)(ii) would require the creditor to disclose that the loan balance may increase even if the consumer makes the periodic payments. In addition, the creditor would be required to disclose that the minimum payment covers only a part of the interest the consumer owes each period and none of the principal, that the unpaid interest will be added to the consumer's loan amount, and that over time this will increase the total amount the consumer is borrowing and cause the consumer to lose equity in the home.

Balloon payment. Proposed § 226.38(d)(2)(iii) would require the creditor to disclose that the consumer will owe a balloon payment, along with a statement of the amount that will be due and the date on which it will be due. Proposed comment 38(d)(2)(iii)–1 would clarify that the creditor must make this disclosure if the loan program includes a payment schedule with regular periodic payments that when aggregated do not fully amortize the outstanding principal balance.

Demand feature. As currently required under § 226.18(i), proposed § 226.38(d)(2)(iv) would require the creditor to disclose a statement that the creditor may demand full repayment of the loan, along with a statement of the timing of any advance notice the creditor is required to give the consumer before the creditor exercises such right. Proposed comment 38(d)(2)(iv)–1 would clarify that this requirement would apply not only to transactions payable on demand from the outset, but also to transactions that convert to a demand status after a stated period. Proposed comment 38(d)(2)(iv)–2 would cross-reference comment 18(i)–2 regarding covered demand features.

No-documentation or low-documentation loans. Proposed § 226.38(d)(2)(v) would require the creditor to disclose that the consumer's loan will have a higher rate or fees because the consumer did not document employment, income, or other assets. In addition, the creditor would disclose that if the consumer provides more documentation, the consumer could decrease the interest rate or fees.

Shared-equity or shared-appreciation. Proposed § 226.38(d)(2)(vi) would require the creditor to disclose a statement that any future equity or appreciation in the real property or dwelling that secures the loan must be shared, along with a statement of the events that may trigger such obligation.

38(d)(3) Format Requirements

Based on consumer testing, as discussed more fully in §§ 226.19(b)(2) and 226.37, proposed § 226.38(d)(3) would require the creditor to disclose the ''Key Questions about Risk'' using a special format. Proposed § 226.38(d)(3)(i) would require the creditor to provide the disclosures required in § 226.38(d)(1) and (d)(2), as applicable, in the form of a table with headings, content and format substantially similar to Model Forms H–19(A), H–19(B), or H–19(C) in Appendix H. Only the information required or permitted by § 226.38(d)(1) and (2) would be permitted in this table. In addition, under § 226.38(d)(3)(ii), the disclosures would be required to be grouped together and presented in the format of a question and answer in a manner substantially similar to Model Form H–19(A), H–19(B), or H–19(C) in Appendix H. Proposed § 226.38(d)(3)(iii) would further require the creditor to disclose each affirmative answer in bold text and in all capitalized letters, but negative answers would be disclosed in nonbold text. Finally, proposed 226.38(d)(3)(iv) would require the creditor to make the disclosures, as applicable, in the following order: rate increases under § 226.38(d)(1)(i), payment increases under § 226.38(d)(1)(ii), interest-only payments under § 226.38(d)(2)(i), negative amortization under § 226.38(d)(2)(ii), balloon payments under § 226.38(d)(2)(iii), prepayment penalties under § 226.38(d)(1)(iiii), demand feature under § 226.38(d)(2)(iv), no-documentation or low-documentation loans under § 226.38(d)(2)(v), and shared-equity or shared-appreciation under § 226.38(d)(2)(vi). This order would ensure that consumers receive critical information about their payments first.

38(e) Information About Payments

Proposed § 226.38(e) would require disclosure of additional information about interest rates and payments, including disclosure of the amount financed, the ''interest and settlement charges,'' (currently the ''finance charge''), the total of payments, and the number of payments. Proposed § 226.38(e) would also require disclosure of whether or not an escrow account for taxes and insurance is required, a disclosure about private mortgage insurance, if applicable, and information about limitations on rate and payment changes. In the consumer testing conducted by the Board, consumers did not find certain terms that are prominently disclosed on the current transaction-specific TILA form to be useful. Specifically, the amount financed, the total of payments, and the finance charge were less useful to consumers than other information such as information about the loan amount, interest rates, and monthly payments. The Board believes that it would enhance consumers' overall understanding of the disclosures if these items were placed less prominently on the form. In addition, by placing these terms in the context of a larger explanatory statement, some consumers may better be able to understand these terms. At the same time, consumer testing conducted for the Board has shown that there is other information about the loan terms that consumers find beneficial that is not currently disclosed on the transaction-specific form. Specifically, the Board believes that consumers would find it beneficial to have explanations of how the interest rate or payment amounts can change and whether there are limits on those changes, and notification of whether an escrow account or private mortgage insurance are required.

38(e)(1) and (2) Rate Calculation; Rate and Payment Change Limits

Proposed §§ 226.38(e)(1) and 226.38(e)(2) would require disclosures of how the consumer's variable interest rate is calculated, of any limitations on adjustments to the interest rate, and of any limitations on payment adjustments in negatively amortizing loans. The requirements under proposed §§ 226.38(e)(1) and 226.38(e)(2) to provide disclosures of how the rate is calculated and any limitations on adjustments to the interest rate are similar to the requirements of current §§ 226.18(f)(1)(i) and 226.18(f)(1)(ii) for transactions not secured by the consumer's principal dwelling or secured by the consumer's principal dwelling with a term of one year or less. Currently, for transactions secured by the consumer's principal dwelling with a term greater than one year, § 226.19(b)(2) requires information about the variable interest rate to be disclosed at the time an application form is provided to the consumer, or before the consumer pays a nonrefundable fee, whichever is earlier. However, under current § 226.18(f)(2), in the transaction-specific disclosures provided before consummation, only a statement that the transaction contains a variable-rate feature, and a statement that variable-rate disclosures have been provided earlier, are required. The Board believes that providing information about how the interest rate is calculated and about limitations on interest rate adjustments along with other transaction-specific disclosures would provide consumers with meaningful information about their particular interest rate in the context of the entire transaction being disclosed. For adjustable-rate mortgages, proposed § 226.38(e)(1) would require a statement of how the interest rate is calculated. In addition, if the interest rate at consummation is not based on the index and margin that will be used to make later interest rate adjustments, the statement would be required to include the time period when the initial interest rate expires.

Proposed comment 38(e)(1)–1 is similar to current comment 18(f)(1)(i)–1 for credit not secured by the consumer's principal dwelling, or secured by the consumer's principal dwelling with a term of one year or less. The proposed comment would clarify that if the interest rate is calculated based on the addition of a margin to an index the statement would have to identify the index to which the rate is tied and the margin that will be added to the index, as well as any conditions or events on which the increase is contingent. When no specific index is used, the factors used to determine whether to increase the rate would be required to be disclosed. When the increase in the rate is discretionary, the fact that any increase is within the creditor's discretion would be required to be disclosed. When the index is internal (for example, the creditor's prime rate), the creditor would be permitted to comply with the disclosure requirement by providing either a brief description of that index or a statement that any increase is in the discretion of the creditor. An external index, however, would be required to be identified.

Proposed § 226.38(e)(2) would require a statement of any limitations on the increase in the interest rate in a variable-rate transaction, and, for negatively amortizing loans, a statement of any limitations on the increase in the minimum payment amount and the circumstances under which the minimum payment required may recast to a fully amortizing payment. Proposed comment 38(e)(2)–1, covering variable-rate transactions, would be similar to current comment 18(f)(1)(ii)–1 and would clarify that the disclosure of limitations on adjustments to the interest rate must provide any maximum imposed on the amount of an increase in the rate at any time, as well as any maximum on the total increase over the transaction's term to maturity.

Proposed comment 38(e)(2)–2, covering negatively amortizing loans, would clarify that any limit imposed on the change of a minimum payment amount, whether or not the change follows an adjustment to the interest rate, would be required to be disclosed. In addition, any conditions to the limitation on payment increases would also be required to be disclosed. For example, some loan programs provide that the minimum payment will not increase by more than a certain percentage, regardless of the corresponding increase in the interest rate. However, there may be exceptions to the limitation on the payment increase, such as if the consumer's principal balance reaches a certain threshold, or if the legal obligation sets out a scheduled time when payment increases will not be limited.

38(e)(3) Escrow

Proposed § 226.38(e)(3) would require, if applicable, a statement substantially similar to the following: ''An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD–1 form for more details.'' If no escrow is required, the creditor would be required to state that fact and that the consumer must pay property taxes and insurance directly.

38(e)(4) Mortgage Insurance

Proposed § 226.38(e)(4) would require, if applicable, a statement substantially similar to the following: ''Private Mortgage Insurance (PMI) is required for this loan. It is included in your escrow.'' If other mortgage insurance is required, such as insurance or guaranty obtained from a government agency, the creditor would be required to omit the word ''private'' from the description.

38(e)(5) Total Payments

38(e)(5)(i) Total Payments

Section 226.18(h), which implements TILA Section 128(a)(5) and (8), requires creditors to disclose the total of payments, using that term, together with a descriptive statement that the disclosed amount reflects the sum of all scheduled payments disclosed under § 226.18(g).[85] 15 U.S.C. 1638(a)(5), (a)(8). Current comment 18(h)–1 allows creditors to revise the total of payments descriptive statement for variable rate transactions to convey that the disclosed amount is based on the annual percentage rate and may change. In addition, current comments 18(h)–3 and –4 permit creditors to omit the total of payments disclosure in certain single-payment transactions and for demand obligations that have no alternate maturity date.

Consumer testing conducted by the Board showed that participants did not find the total of payments to be helpful in evaluating a loan offer. Most participants understood that the total of payments generally represented the sum of scheduled payments and charges, including interest; several suggested that an explanation of how the total of payments is calculated would facilitate comprehension of the term. Some participants expressed interest in knowing the total of payments required to pay off the loan obligation, but regarded this information as marginally useful to their shopping and decision-making process. On the other hand, some participants commented that information about the total of payments was unnecessary and therefore, could be removed from the form entirely.

As part of consumer testing, the Board shortened the term ''total of payments'' to ''total payments'' because it is a more

[85] Section 128(a)(5) of TILA states that the total of payments should be disclosed as the sum of the amount financed and finance charge. 15 U.S.C. 1638(a)(5). Since 1969, the Board has required that the total of payments equal the sum of payments disclosed in the payment schedule under TILA Section 128(a)(6) and § 226.18(g), which can include amounts beyond the amount financed and the finance charge. 15 U.S.C. 1638(a)(6). Thus, if a creditor includes escrowed taxes and insurance in its disclosure of scheduled payments under § 226.18(g), it must also include those amounts in the total of payments disclosed under § 226.18(h). 34 FR 02002; Feb. 11, 1969.

direct and simple term to communicate to consumers what the dollar amount represented. In addition, an explanation of the assumptions underlying the total payments calculation was added with an explicit reference to whether the amount included escrowed amounts. The total payment amount was disclosed with a statement explaining that a portion of it goes towards interest and settlement charges. This approach enhanced consumer comprehension of the total payments and, as discussed more fully below, the interest and settlement charges disclosure.

The Board proposes to rename ''total of payments'' as ''total payments,'' and require that it be disclosed with a descriptive statement, for transactions secured by real property or a dwelling. The Board proposes to make this adjustment pursuant to its exception 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 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 Board believes that proposing the exception is appropriate. Consumer testing indicates that ''total payments'' is more understandable to consumers than ''total of payments.''

The Board proposes to add new § 226.38(e)(5)(i), which would implement TILA Sections 128(a)(5), 128(a)(6), in part, and 128(a)(8) for transactions secured by real property or a dwelling. 15 U.S.C. 1638(a)(5), (a)(6), and (a)(8). Proposed § 226.38(e)(5)(i) would require creditors to disclose for transactions secured by real property or a dwelling, the number and total amount of payments that the consumer would make over the full term of the loan. The Board proposes that this disclosure be made together with a brief statement that the amount is calculated assuming market rates will not change, and that the consumer will make all payments as scheduled for the full term of the loan. The Board believes that although the total payments disclosure is not critical to the shopping or decision-making process for many consumers, it provides information about the total cost of the loan that provides context for, and increases understanding of, other required disclosures, such as interest and settlement charges (formerly finance charge) and amount financed.

Proposed comments 38(e)(5)(i)–1 through –3 would be added to provide guidance to creditors on how to calculate and disclose the total payments amount and the number of payments. As discussed more fully under proposed § 226.38(c), the Board is proposing to require creditors to provide interest rate and monthly payment disclosures in a tabular format for transactions secured by real property or a dwelling. As a result, creditors would not be subject to the disclosure requirements for payment schedules under current § 226.18(g). However, proposed comment 38(e)(5)(i)–1 would clarify that creditors should continue to follow the rules in § 226.18(g) and associated commentary, and comments 17(c)(1)–8 and –10 for adjustable rate transactions, to calculate the total payments for transactions secured by real property or a dwelling. New comment 38(e)(5)(i)–2 would cross-reference to comment 18(g)–3, which the Board proposes to revise to require creditors to disclose the total number of payments for all payment levels as a single figure for transactions secured by real property or a dwelling. Proposed comment 38(e)(5)(i)–3 would provide guidance regarding demand obligations. In technical revisions, the text from current footnote 44 would be moved to the regulation text in § 226.18(h); however, this text is not included in proposed § 226.38(e)(5)(ii) because it is not applicable to transactions secured by real property or a dwelling.

As discussed more fully under proposed § 226.38(e)(5)(ii) for interest and settlement charges (formerly ''finance charge''), creditors would be required to group the total payments disclosure together with the interest and settlement charges and amount financed disclosures under proposed § 226.38(e)(5)(ii) and (iii), respectively.

38(e)(5)(ii) Finance Charge: Interest and Charges

Section 226.18(d), which implements TILA Sections 128(a)(3) and (a)(8), requires creditors to disclose the ''finance charge,'' using that term, and a brief description such as ''the dollar amount the credit will cost you.'' 15 U.S.C. 1638(a)(3), (a)(8). Current comment 18(d)–1 allows creditors to modify this description for variable rate transactions with a phrase that the disclosed amount is subject to change. In addition, § 226.17(a)(2), which implements TILA Section 122(a), requires creditors to disclose the finance charge, and the annual percentage rate, more conspicuously than any other required disclosure, except the creditor's identity. 15 U.S.C. 1633(a). The rules addressing which charges must be included in the finance charge are set forth under TILA Section 106 and § 226.4, and are discussed more fully under § 226.4 of this proposal. 15 U.S.C. 1605.

Consumer testing conducted by the Board indicated that many participants could not correctly explain the term ''finance charge.''[86] Most participants thought that the finance charge represented the amount of interest the borrower would pay over the life of the loan, but did not realize that it also included fees until directed to read a statement that explained fees were included. Consumer testing showed that comprehension of the finance charge improved when it was renamed to reflect the costs it actually represented—the interest and settlement charges paid over the life of the loan. However, even when participants understood what the finance charge signified they tended to disregard it, often because it was such a large dollar amount. Several participants commented that it is helpful to know the total amount of interest and fees that would be paid, but that they could not otherwise purchase a home, or refinance an existing obligation, in cash and therefore, already understood they would pay a significant amount in interest and fees when repaying the loan. Still, participants expressed an interest in knowing the total amount of interest and other charges they would pay over the full term of the loan.

The Board proposes to exercise its authority under TILA Section 105(a) to rename ''finance charge'' as ''interest and settlement charges,'' except it from the requirement under TILA Section 122(a) that it be disclosed more conspicuously, and require that it be disclosed with a descriptive statement. 15 U.S.C. 1632(a); 1604(a), (f). Section 105(a) authorizes the Board to make exceptions or 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). In this case, the Board believes an exception from TILA's requirements are necessary to effectuate the Act's purposes for transactions secured by real property or a dwelling. Although some consumers expressed interest in the finance charge when evaluating a loan offer, consumer testing showed that for most consumers it is not as useful in the shopping or decision-making process as other terms, and therefore, should be de-emphasized relative to other disclosed terms. Consumer testing also showed that

[86] *See also Improving Consumer Mortgage Disclosures* (stating that a number of respondents misinterpreted the finance charge).

participants had a better understanding of the finance charge when it was disclosed as a portion of the total payments amount, accompanied by a statement that explained the finance charge amount plus the amount financed is used to calculate the APR. Thus, based on consumer testing, the Board believes that consumers will find the finance charge disclosure more meaningful when described in a manner consistent with consumers' general understanding, and disclosed in context with other information that relate to loan payments, such as the total payments.

The Board proposes to add new § 226.38(e)(5)(ii), which would implement TILA Section 128(a)(3) and (8) for closed-end mortgage loans covered by § 226.38. 15 U.S.C. 1638(a)(3), (8). Section 226.38(e)(5)(ii) would require creditors to disclose the ''interest and settlement charges,'' using that term, together with a brief statement that the disclosed amount represents part of the total payments amount disclosed. Creditors would also be required to disclose the ''interest and settlement charges'' grouped together with the ''total payments'' and ''amount financed'' disclosures under proposed § 226.38(e)(5)(i) and (iii), respectively, under the subheading ''Total Payments,'' using that term. Based on consumer testing, the Board believes this approach is appropriate to help serve TILA's purpose of assuring a meaningful disclosure of credit terms. Consumer testing suggests that providing the disclosure of ''interest and settlement charges'' in context of the total payments improves consumers' ability to understand that this disclosure represents the cost (*i.e.,* interest and fees) of borrowing the loan amount.

The Board also proposes comment 38(e)(5)(ii)–1 to provide guidance on how creditors must calculate and disclose the interest and settlement charges. However, the proposed rule would not allow creditors to modify the description that accompanies the disclosure for variable-rate transactions. The Board proposes this restriction under TILA Section 105(a) to help serve TILA's purpose of meaningful disclosure of credit terms so that consumers will be able to compare more readily the various credit terms available, and avoid the uninformed use of credit. 15 U.S.C. 1601(a). Consumer testing showed that the simple disclosure aided consumer understanding. The Board believes that adding language that states the disclosed amount is subject to change could dilute the significance of the disclosure.

38(e)(5)(iii) Amount Financed

Disclosure of amount financed. Section 226.18(b), which implements TILA Section 128(a)(2)(A) and (a)(8), requires creditors to disclose the amount financed, using that term, together with a brief description that it represents the amount of credit of which the consumer has actual use. 15 U.S.C. 1638(a)(2)(A), (a)(8). Section 226.18(b) delineates how creditors should calculate the amount financed so that it reflects the net amount of credit being extended.

In consumer testing conducted for the Board, virtually no participant understood the disclosure of the amount financed.[87] The Board tested several versions of the amount financed disclosure, with alternative formatting and descriptions, to explain briefly that it represents the amount of credit of which the consumer has actual use to purchase a home or refinance an existing loan. However, these changes made no difference in participants' understanding of the term. In addition, consumer testing showed that the amount financed disclosure actually detracted from consumers' understanding of other disclosures. Many consumers mistook the amount financed for the loan amount. Some of these consumers were confused, however, because the amount financed was slightly lower than the amount borrowed in the hypothetical loan offer. Consumers offered various explanations regarding the difference in the disclosed amounts, including that the amount financed was the cost of purchasing a home less a down payment. Other participants stated that the amount financed represented escrowed amounts. Sample disclosures were used to try to explain that the difference between the loan amount and amount financed is attributable to prepaid finance charges, but this explanation did not appear to improve consumer comprehension. Consumer testing also indicated that participants would not consider the amount financed when shopping for a mortgage or evaluating competing loan offers.

For these reasons, the Board proposes to add new § 226.38(e)(5)(iii), which would implement TILA Section 128(a)(2)(A) and (a)(8) for transactions secured by real property or a dwelling. 15 U.S.C. 1638(a)(2)(A), (a)(8). Section 226.38(e)(5)(iii) would require creditors to disclose the amount financed with a brief statement that the amount financed, plus the interest and settlement charges, is the amount used to calculate the annual percentage rate. As noted above, creditors would be required to disclose the amount financed grouped together with the total payments and interest and settlement charges required under proposed § 226.38(e)(5)(i) and (ii).

The Board proposes this approach pursuant to its authority under TILA Section 105(a). 15 U.S.C. 1604(a). Section 105(a) authorizes the Board to prescribe regulations 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). Based on consumer testing, the Board believes this proposal is appropriate to help serve TILA's purpose of assuring a meaningful disclosure of credit terms. The Board believes that requiring creditors to disclose the amount financed in the loan summary with other key loan terms would add unnecessary complexity and result in ''information overload.'' Consumer testing showed that when the amount financed was disclosed with the total payments and interest and settlement charges, that consumer comprehension of the term improved slightly, and confusion over other key loan terms, such as the loan amount, was eliminated. The Board believes that disclosing the amount financed as one component in the APR calculation provided consumers with a better understanding of its significance to the loan transaction. The Board also proposes new comment 38(e)(5)(iii)–3 to provide guidance regarding disclosure of the ''amount financed.''

Calculation of amount financed. The Board proposes to simplify the calculation of the amount financed for transactions subject to the disclosure requirements of proposed § 226.38, pursuant to the Board's authority under TILA Section 105(a). The Board believes that the proposed simplification would improve understanding of the rules and facilitate compliance with Regulation Z. Under proposed § 226.38(e)(5)(iii), for a transaction secured by real property or a consumer's dwelling, the creditor would determine the amount financed by subtracting all prepaid finance charges from the loan amount as defined in proposed § 226.38(a)(1), discussed above. Under existing § 226.18(b) and its staff commentary, creditors may elect from among multiple alternatives in calculating the amount financed. All of

[87] *See also Improving Consumer Mortgage Disclosures* at 35 (finding that most respondents in consumer testing did not understand the term ''amount financed,'' and confused it for the loan amount, and discussing the risks of falling subject to predatory lending practices as a result of this confusion).

the permissible methods yield the same mathematical result.

The Board has received input from bank examiners and others that providing multiple approaches to calculation of the amount financed creates unnecessary complication. Examiners also indicate that, of the permissible approaches, mortgage lenders generally use the one that is simplest and most straightforward. The Board is now proposing to require that approach and to eliminate the alternatives. The Board also is proposing to make a conforming amendment to the staff commentary under § 226.18(b) to reflect the fact that it would not apply to mortgages.

TILA provides that the amount financed is calculated as follows:

(1) Take the principal amount of the loan (or cash price less downpayment);

(2) Add any charges that are not part of the finance charge or of the principal amount and that are financed by the consumer; and

(3) Subtract any prepaid finance charge.

TILA Section 128(a)(2)(A), 15 U.S.C. 1638(a)(2)(A). Regulation Z provides a substantially identical calculation. *See* § 226.18(b). Neither the statute nor Regulation Z defines ''principal amount of the loan.'' As a result, more than one understanding of that term is possible, and Regulation Z seeks to address several of those understandings rather than to define principal amount definitively.

Current Regulation Z permits non-finance charges and prepaid finance charges that are financed to be included in the principal loan amount under step (1) or not, at the creditor's option. The creditor then must add in under step (2) any financed non-finance charges that were not included under step (1). *See* comment 18(b)(2)–1. Similarly, the creditor must subtract under step (3) any financed prepaid finance charges only if they were included under step (1). *See* comment 18(b)(3)–1. Proposed § 226.38(e)(5)(iii) effectively would define ''principal loan amount'' as the loan amount, as that is defined in proposed § 226.38(a)(1), which would mean the principal amount the consumer will borrow reflected in the loan contract. Under that definition, all amounts that are financed necessarily would be included in step (1), whether they are finance charges or not. Consequently, no amount ever would be added under step (2). The new provision therefore would streamline the calculation to eliminate that step. Similarly, the current commentary providing that financed prepaid finance charges should be subtracted in step (3) only if they were included in step (1) would be unnecessary, as such finance charges always would be included in step (1). Proposed § 226.38(e)(5)(iii) would provide definitively that the amount financed is determined simply by subtracting the prepaid finance charge from the loan amount.

The Board also is proposing comment 38(e)(5)(iii)–2 to clarify how to treat creditor or third-party premiums and buy-downs for purposes of the amount financed calculation. This proposed comment is based on existing comment 18(b)–2, which relates to rebates and loan premiums. The discussion in comment 18(b)–2 was primarily intended to address situations that are more common in non-mortgage transactions, especially credit sales, such as automobile financing. It provides that creditor-paid premiums and seller- or manufacturer-paid rebates may be reflected in the disclosures under § 226.18 or not, at the creditor's option. Although such premiums and rebates are less likely to exist in mortgage transactions precisely as they are described in comment 18(b)–2, analogous situations can apply to mortgage financing. For example, real estate developers may offer to pay some or all closing costs or to buy down the consumer's interest rate, and creditors may agree to pay certain closing costs in return for a particular interest rate. Rather than permit any treatment at the creditor's option, however, proposed comment 38(e)(5)(iii)–2 would reflect the Board's belief that such situations are analogous to buydowns. Like buydowns, such premiums and rebates may or may not be funded by the creditor and reduce costs otherwise borne by the consumer. Accordingly, their impact on the amount financed, like that of buydowns, properly depends on whether they are part of the legal obligation. *See* comments 17(c)(1)–1 through –5. Proposed comment 38(e)(5)(iii)–2 would clarify that the disclosures, including the amount financed, must reflect loan premiums and rebates regardless of their source, but only if they are part of the terms of the legal obligation between the creditor and the consumer. As noted above, the Board also is proposing similar revisions to existing comment 18(b)–2.

38(f) Additional Disclosures

38(f)(1) No Obligation Statement

The MDIA amended Section 128(b)(2) of TILA to require creditors to disclose, in conspicuous type size and format, that receiving and signing a TILA disclosure does not obligate a consumer to accept the loan (''the MDIA statement''). 15 U.S.C. 1638(b)(2). The MDIA sets forth the following language for creditors to use in making this disclosure: ''You are not required to complete this agreement merely because you have received these disclosures or signed a loan application.'' [88] The Board proposes to modify this statutory language to facilitate consumers' use and understanding of the MDIA statement pursuant to its authority under TILA Section 105(a) to make adjustments that are necessary to effectuate the purposes of TILA. 15 U.S.C. 1604(a). Based on consumer testing, the Board believes that using plain language principles to revise the statutory language improves consumers' ability to understand the disclosure and would help serve TILA's purpose to provide meaningful disclosure of credit terms.

As part of consumer testing, the Board included the MDIA statement on the front page of the TILA, modified to replace legalistic phrasing with more common word usage. On the second page, the Board included a signature line and date, as most creditors require the consumer to sign the disclosure form to establish compliance with TILA. Most participants did not notice the MDIA statement, but indicated that they understood they were under no obligation to accept the loan; participants who did notice the text similarly understood they were under no obligation to accept the loan. However, upon seeing the signature line, some participants believed they would be obligated to accept the loan if they signed or initialized the disclosure. Based on consumer testing, the Board is concerned that although consumers may initially understand they are not obligated to accept a loan, this belief may be altered by creditors' practice of requiring consumers to sign or initial receipt of the disclosures. This may further discourage negotiation and shopping among loan products and lenders.

To implement the new disclosure required by the MDIA, the Board proposes to add new § 226.38(f)(1) for all transactions secured by real property or a dwelling. Proposed § 226.38(f)(1) would require a statement that a consumer is not obligated to accept the loan because he or she has signed the disclosure. In addition, the Board proposes that if a creditor provides space for the consumer to sign or initial the TILA disclosures, then the creditor

[88] Housing and Economic Recovery Act, Public Law 110–289, 122 Stat. 2655, § 2502(a)(6) (July 30, 2008).

must place the statement in close proximity to the space provided for the consumer's signature or initials. The statement must also specify that a signature only confirms receipt of the disclosure statement.

The Board proposes this approach pursuant to its authority under TILA Section 105(a) 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 Board believes that this proposal is necessary to encourage consumers to shop among available credit alternatives. The Board tested the disclosure as proposed under § 226.38(f)(1). Most participants understood they were not obligated to accept the loan and could refuse to accept the loan offer even after signing. As a result, the Board believes the disclosure proposed by new § 226.38(f)(1) is necessary to ensure that consumers are not discouraged from shopping or negotiating with the lender.

38(f)(2) Security Interest

TILA Section 128(a)(9), 15 U.S.C. 1638(a)(9), and § 226.18(m) require the creditor to disclose whether it has a security interest in the property securing the transaction. During consumer testing of the current TILA disclosure, participants were shown the following language: ''Security: You are giving a security interest in the real property, and fixtures and rents if indicated in the rider mortgage.'' Very few participants understood the current language regarding a security interest. The Board is concerned that consumers might not understand that the creditor can take the consumer's home if the consumer defaults on the loan agreement. To clarify the significance of the security interest disclosure to consumers, the Board proposes § 226.38(f)(2) to require the creditor to state that the consumer could lose the home if the consumer is unable to make the payments on the loan. This would provide a clearer disclosure regarding the effect of the lender taking a security interest in the home.

38(f)(3) No Guarantee to Refinance Statement

The MDIA also amended Section 128(b)(2) 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'').[89] 15 U.S.C. 1638(b)(2). To implement the disclosure required by the MDIA, the Board proposes to add § 226.38(f)(3) to require that creditors disclose 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 proposes to expand the scope of the requirement to also include fixed-rate transactions secured by a dwelling, as well as transactions secured by real property without a dwelling. The Board proposes this approach pursuant to its authority under TILA Section 105(a) 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 Board is concerned that some consumers may accept loan terms that could present refinancing 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.

38(f)(4) Tax Deductibility

The Board is also proposing changes to the closed-end disclosures to implement provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the ''Bankruptcy Act'') which requires disclosure of the tax implications for home-secured credit that may exceed the dwelling's fair market value. *See* Public Law 109–8, 119 Stat. 23. The Bankruptcy Act primarily amended the federal bankruptcy code, but also contained several provisions amending TILA. Section 1302 of the Bankruptcy Act amendments requires that advertisements and applications for credit (either open-end or closed-end) that may exceed the fair market value of the dwelling include a statement that the interest on the portion of the credit extension that exceeds the fair market value is not tax-deductible and a statement that the consumer should consult a tax advisor for further information on tax deductibility.

The Board stated its intent to implement the Bankruptcy Act amendments in an ANPR published in October 2005 as part of the Board's ongoing review of Regulation Z (October 2005 ANPR). 70 FR 60235; Oct. 17, 2005. The Board received approximately 50 comment letters: forty-five letters were submitted by financial institutions and their trade groups, and five letters were submitted by consumer groups. In general, creditors asked for flexibility in providing the disclosure regarding the tax implications for home-secured credit that may exceed the dwelling's fair market value, either by permitting the notice to be provided to all mortgage applicants, or to be provided later in the approval process after creditors have determined whether the disclosure is triggered. Creditor commenters asked for guidance on loan-to-value calculations and safe harbors for how creditors should determine property values. Consumer advocates favored triggering the disclosure when negative amortization could occur. A number of commenters stated that in order for the disclosure to be effective and useful to the borrower, it should be given when the new extension of credit, combined with existing credit secured by the dwelling (if any), may exceed the fair market value of the dwelling. A few industry comments took the opposite view that the disclosure should be limited only to when a new extension of credit itself exceeds fair market value, citing the difficulty in determining how much debt is already secured by the dwelling at the time of application.

The Board implemented section 1302 with regard to advertisements in its 2008 HOEPA Final Rule. *See* 73 FR 44522, 44600; July 30, 2008. In the supplementary information to that rule, the Board stated that it intends to implement the application disclosure portion of the Bankruptcy Act during its forthcoming review of closed-end and HELOC disclosures under TILA. Proposed § 226.38(f)(4) would implement provisions of the Bankruptcy Act by requiring creditors to include the disclosure of the tax implications for a loan secured by a dwelling, if extension of credit may, by its terms, exceed the fair market value of the dwelling. The text of the proposed disclosure is based on the Board's consumer testing of model HELOC disclosure forms. The disclosure would be segregated and located directly below the table.

The Board recognizes that creditors may not be able to determine whether the amount of credit extended exceeds

[89] 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).

the fair market value of the dwelling, especially three days after application when they are required to provide an early transaction-specific disclosures. The creditor may not be able to verify the value on the property until later in the loan underwriting process. The Board has considered whether the disclosure should be provided later in the approval process after the creditor has determined that the disclosure is triggered, for instance, after receiving the appraisal report or completing the underwriting process. However, such late timing of the disclosure would not satisfy the requirements of the Bankruptcy Act which requires that the disclosures be provided *at the time* of application. See 15 U.S.C. 1638(a)(15).

The Board also considered whether the disclosure should be provided to all mortgage applicants, regardless of whether the amount of credit extended exceeds the fair market value of the dwelling. To address the situations in which the creditor is not certain whether the credit extended may exceed the fair market value of the dwelling, comment 38(f)(4)–2 permits the disclosure to be provided to all mortgage applicants at creditors' discretion and provides model language.

The Board recognizes that the scope of the proposed § 226.38(f)(4) is limited to dwellings whereas proposed § 226.38 would apply to real property and dwellings. While the Bankruptcy Act amendment specifically references ''consumer's dwelling,'' the Board believes that it would be unnecessarily burdensome to require creditors to create separate disclosures for the transactions secured by real property and those secured by a dwelling solely for the purposes of the tax implications disclosure. For that reason, a creditor would be permitted, but not required, to provide the disclosures about the tax implications in connection with transactions secured by both real property and dwellings.

38(f)(5) Additional Information and Web Site

Consumer testing showed that many participants educated themselves about the mortgage process through informal networking with family, friends, and colleagues, while others relied on the Internet for information. To improve consumers' ability to make informed decisions about credit, the Board proposes § 226.38(f)(5) to require the creditor to disclose that if the consumer does not understand any of the disclosures, then the consumer should ask questions. The creditor would also disclose that the consumer may obtain additional information at the Web site of the Federal Reserve Board and disclose a reference to that Web site. The Board will enhance its Web site to further assist consumers in shopping for a mortgage. Although it is hard to predict from the results of the consumer testing how many consumers might use the Board's Web site, and recognizing that not all consumers have access to the Internet, the Board believes that this Web site may be helpful to some consumers as they shop for a mortgage. The Board seeks comment on the content for the Web site.

38(f)(6) Format

The Board is proposing to specify precise formatting requirements for the disclosures required by § 226.38(f)(1) through (5). Proposed § 226.38(f)(6)(i) would set forth location requirements, providing that the no obligation and confirmation of receipt statements must be disclosed together, the security interest and no guarantee to refinance statements must be disclosed together, and the recommendation to ask questions and statement regarding the Board's Web site must be disclosed together. Proposed § 226.38(f)(6)(ii) would set forth highlighting requirements, providing that the no obligation and security interest statements, and the advice to ask questions, must be disclosed in bold text.

38(g) Identification of Originator and Creditor

38(g)(1) Creditor

Currently, § 226.18(a), which implements TILA Section 128(a)(1), 15 U.S.C. 1638(a)(1), requires the creditor to disclose the identity of the creditor making the disclosure. Proposed § 226.38(g)(1) would require the same disclosure. In addition, proposed comment 38(g)(1)–1 would parallel existing comment 18(a)–1 to clarify that use of the creditor's name is sufficient, but the creditor may also include an address and/or telephone number. In transactions with multiple creditors, any one of them may make the disclosures, but the one doing so must be identified. The Board solicits comment on whether the creditor making the disclosures should be required to disclose its contact information, such as its address and/or telephone number.

Existing footnote 38 to § 226.17(a), which implements TILA Section 128(b)(1), 15 U.S.C. 1638(b)(1), states that the creditor's identity may be made together with or separately from the other required disclosures. The Board proposes to amend the substance of current footnote 38 to remove the reference to the creditor's identity disclosure required under § 226.18(a), thereby making it subject to the grouped-together and segregation requirement for all non-mortgage closed-end credit. Similarly, § 226.37(a)(2) would require the disclosure of the creditor's identity to be subject to the grouped-together and segregation requirement for closed-end credit transactions secured by real property or a dwelling.

The Board proposes to make this adjustment 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 to effectuate the statute's purposes, which include facilitating consumers' ability to compare credit terms, and avoid the uninformed use of credit. 15 U.S.C. 1604(a), 15 U.S.C. 1601(a). The Board believes it is important to disclose the creditor's identity so that consumers can more easily identify the appropriate entity. Thus, the Board believes this proposal would help serve TILA's purpose to provide meaningful disclosure of credit terms.

38(g)(2) Loan Originator

On July 30, 2008, the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act), 12 U.S.C. 5101–5116, was enacted to create a Nationwide Mortgage Licensing System and Registry of loan originators to increase uniformity, reduce fraud and regulatory burden, and enhance consumer protection. 12 U.S.C. 5102. Under the SAFE Act, a ''loan originator'' is defined as ''an individual who (I) takes a residential mortgage loan application; and (II) offers or negotiates terms of a residential mortgage loan for compensation or gain.'' 12 U.S.C. 5102(3)(A)(i). Each loan originator is required to obtain a unique identifier through the Nationwide Mortgage Licensing System and Registry. 12 U.S.C. 5103(a)(2). The term ''unique identifier'' is defined as ''a number or other identifier that (i) permanently identifies a loan originator; (ii) is assigned by protocols established by the Nationwide Mortgage Licensing System and Registry and the Federal banking agencies to facilitate electronic tracking of loan originators and uniform identification of, and public access to, the employment history of and the publicly adjudicated disciplinary and enforcement actions against loan originators; and (iii) shall not be used for purposes other than those set forth under this title.'' 15 U.S.C. 5102(12)(A). The system is intended to provide consumers with easily accessible information to research a loan originator's history of employment and any disciplinary or enforcement actions against that person. 12 U.S.C. 5101(7).

To facilitate the use of the Nationwide Mortgage Licensing System and Registry and promote the informed use of credit, the Board proposes § 226.38(g)(2) to require the loan originator to disclose his or her unique identifier on the TILA disclosure, as defined by the SAFE Act. Proposed comment 38(g)(2)–1 would clarify that in transactions with multiple loan originators, each loan originator's unique identifier must be listed on the disclosure. For example, in a transaction where a mortgage broker meets the SAFE Act definition of a loan originator, the identifiers for the broker and for its employee loan originator meeting that definition would be listed on the disclosure.

The Board notes that the Board, FDIC, OCC, OTS, NCUA, and Farm Credit Administration have published a proposed rule to implement the SAFE Act. *See* 74 FR 27386; June 9, 2009. In this proposed rule, the federal banking agencies have requested comment on whether there are mortgage loans for which there may be no mortgage loan originator. For example, the agencies query whether there are situations where a consumer applies for and is offered a loan through an automated process without contact with a mortgage loan originator. *See id.* at 27397. The Board solicits comments on the scope of this problem and its impact on the requirements of proposed § 226.38(g)(2).

38(h) Credit Insurance and Debt Cancellation and Debt Suspension Coverage

As discussed more fully in § 226.4(d)(1) and (3), concerns have been raised that consumers do not understand the voluntary nature, costs, and eligibility restrictions of credit insurance and debt cancellation and debt suspension coverage. For this reason, the Board proposes § 226.38(h) to require creditors to provide certain disclosures, which would be grouped together and substantially similar in headings, content and format to Model Clause H–17(C) in Appendix H to this part. Proposed comment 38(h)–1 would clarify that this disclosure may, at the creditor's option, appear apart from the other disclosures. It may appear with any other information, including the amount financed itemization, any information prescribed by State law, or other information. When this information is disclosed with the other segregated disclosures, however, no additional explanatory material may be included.

The proposed disclosures seek to address concerns that consumers may not understand that some products are voluntary and not required as a condition of receiving credit. If the product is optional, proposed § 226.38(h)(1)(i) would require the creditor to disclose the term ''OPTIONAL COSTS,'' in capitalized and bold letters, along with the name of the program in bold letters. If the product is required, then proposed § 226.38(h)(1)(ii) would require the creditor to disclose only the name of the program in bold letters. In addition, if the product is optional, proposed § 226.38(h)(2) would require the creditor to disclose the term ''STOP,'' in capitalized and bold letters, along with a statement that the consumer does not have to buy the product to get the loan. The term ''not'' would be in bold letters and underlined.

Concerns have also been raised that consumers may not realize that there are alternatives to the product. Therefore, under proposed § 226.38(h)(3), the creditor would disclose that if the consumer already has insurance, then the policy or coverage may not provide the consumer with additional benefits. Under proposed § 226.38(h)(4), the creditor would disclose that other types of insurance may give the consumer similar benefits and are often less expensive.

As described more fully in § 226.4(d)(1) and (3), concerns have been raised that consumers are not aware that they could incur a cost for a product that may offer no benefit if the eligibility criteria are not met at the time of enrollment. That is, consumers may not be aware that if they do not meet the eligibility criteria at the time of enrollment, the product would not pay off, cancel, or suspend the credit obligation. Although the creditor typically has information about the consumer's age or employment status, some creditors do not use this information to determine whether the consumer meets the age or employment eligibility restrictions at the time of enrollment. Some consumers are later denied benefits based on these eligibility restrictions.

For these reasons, the Board is proposing under § 226.38(h)(5)(i) to require the creditor to disclose a statement that based on the creditor's review of the consumer's age and/or employment status at the time of enrollment, the consumer would be eligible to receive benefits. However, if there are other eligibility restrictions, such as pre-existing health conditions, the creditor would be required to make certain other disclosures. Under proposed § 226.38(h)(5)(ii), the creditor would disclose that based on the creditor's review of the consumer's age and/or employment status at the time of enrollment, the consumer may be eligible to receive benefits. Under proposed § 226.38(h)(6), the creditor would also disclose that the consumer may not be eligible to receive any benefits because of other eligibility restrictions.

Proposed comment 38(h)(5)–1 would state that if, based on the creditor's review of the consumer's age and/or employment status at the time of enrollment in the product, the consumer would not qualify for the benefits of the product, then providing the disclosure under § 226.38(h)(5) would not comply with this provision. That is, if the consumer does not meet the age and/or employment eligibility criteria, then the creditor cannot state that the consumer may be eligible to receive benefits and cannot comply with this provision. In addition, the proposed comment would clarify that if the creditor offers a bundled product (such as credit life insurance combined with credit involuntary unemployment insurance) and the consumer is not eligible for all of the bundled products, then the disclosure under § 226.38(h)(5) would not comply with this provision. Finally, the proposed comment would clarify that the disclosure would still satisfy this provision if an event subsequent to enrollment, such as the consumer passing the age limit of the product, made the consumer ineligible for the product based on the product's age or employment eligibility restrictions.

Proposed comment 38(h)(5)–2 would clarify that the disclosure under § 226.38(h)(5) would be deemed to comply with this provision if the creditor used reasonably reliable evidence to determine whether the consumer met the age or employment eligibility criteria of the product. Reasonably reliable evidence of a consumer's age would include using the date of birth on the consumer's credit application, on the driver's license or other government-issued identification, or on the credit report. Reasonably reliable evidence of a consumer's employment status would include a consumer's statement on a credit application form, an Internal Revenue Service Form W–2, tax returns, payroll receipts, or other written evidence such as a letter or e-mail from the consumer or the consumer's employer.

Finally, the disclosure would contain the debt suspension coverage disclosure, a Web site reference, cost information, and a space for the consumer's signature and the date. To ensure consistency with the debt suspension coverage provisions of the December 2008 Open-End Final Rule, proposed § 226.38(h)(7) would require the creditor to disclose, as applicable, a statement that the obligation to pay loan principal and interest is only suspended, and that interest will continue to accrue during the period of suspension. To provide more information to consumers, proposed § 226.38(h)(8) would require the creditor to disclose a statement that the consumer may obtain additional information about credit insurance or debt suspension or debt cancellation coverage at the Web site of the Federal Reserve Board, and a reference to that Web site. If the product is optional, proposed § 226.38(h)(9)(i) would require the creditor to disclose a statement of the consumer's request to purchase or enroll in the optional product and a statement of the cost of the product expressed as a dollar amount per month or per year, as applicable, together with the loan amount and the term of the product in years. This disclosure parallels § 226.4(d)(1) and (3), which requires cost disclosures in order to exclude from the finance charge the credit insurance premium or debt cancellation or debt suspension coverage charge. If the product is required, proposed § 226.38(h)(9)(ii) would require the creditor to disclose that fact, along with a statement of the cost of the product expressed as a dollar amount per month or per year, as applicable, together with the loan amount and the term of the product in years. The cost, month or year, loan amount, and term of the product would be underlined. The provisions regarding required products would be applicable to the extent Regulation Y, 12 CFR part 225, or State or other law would not prohibit requiring the product. Finally, proposed § 226.38(h)(10) would require the creditor to provide a designation for the signature of the consumer and the date of the signing.

The Board proposes to require this disclosure using its authority under TILA Section 105(a), 15 U.S.C. 1604(a). Because proposed § 226.4(g) would treat a premium or charge for credit insurance or debt cancellation or debt suspension as a finance charge for closed-end credit transactions secured by real property or a dwelling, the creditor would not be required to provide the disclosure under § 226.4(d)(1) and (3) to exclude the premium or charge from the finance charge. The Board believes, however, that the consumer would still benefit from a disclosure of the voluntary nature, costs, and eligibility restrictions of credit insurance or debt cancellation or debt suspension coverage, and thus the proposal would require a substantially similar disclosure.

TILA Section 105(a), 15 U.S.C. 1604(a), authorizes the Board to prescribe regulations to carry out the purposes of the act. TILA's purpose includes promoting ''the informed use of credit,'' which ''results from an awareness of the cost thereof by consumers.'' TILA Section 102(a), 15 U.S.C. 1601(a). A premium or charge for credit insurance or debt cancellation or debt suspension coverage is a cost assessed in connection with credit. The credit transaction and the relationship between the creditor and the consumer are the reasons the product is offered or available. Because the merits of this product have long been debated,[90] the Board believes that consumers would benefit from clear and meaningful disclosures regarding the costs, benefits, and risks associated with this product. As discussed more fully in § 226.4(d)(1) and (3), consumer testing showed that without clear disclosures participants were unaware of the voluntary nature, costs, and eligibility restrictions. For these reasons, the Board believes that this proposed rule would serve to inform consumers of the cost of this credit product.

38(i) Required Deposit

Proposed § 226.38(i) addresses disclosure requirements when creditors require consumers to maintain deposits as a condition to the specific transaction, for transactions secured by real property or a dwelling. Proposed § 226.38(i) is consistent with § 226.18(r), which applies to transactions not secured by real property or a dwelling. The Board is proposing to revise § 226.18(r) and associated commentary, as discussed above, and proposed § 226.38(i) reflects the revised text and associated commentary.

38(j) Separate Disclosures

Consumer testing indicated that participants generally felt overwhelmed by the amount of information presented throughout the loan process and especially at consummation. As a result, the Board seeks to streamline the TILA disclosures and focus on the terms that participants stated were important for shopping and for understanding their loan terms. Currently, TILA and Regulation Z mandate that the following disclosures be grouped together with the required disclosures and segregated from everything else: rebate, late payment, property insurance, contract reference, and assumption policy. *See* TILA Sections 128(a)(9), (10), (11), (12), (13) and (b) and 106(c); 15 U.S.C. §§ 1638(a)(9), (10), (11), (12), (13) and (b) and 1605(c); §§ 226.4(d)(2), 226.17(a)(1), and 226.18(k)(2), (l), (n), (p), and (q). Consumer testing showed that these terms were not of primary importance to consumers in choosing a mortgage. With respect to assumption, for example, very few participants understood the language indicating that the loan was assumable, and even fewer felt it was important information. With respect to property insurance, most participants understood the language indicating that the borrower can obtain property insurance from anyone that is acceptable to the lender, but the participants felt that this was not important to their decision making.

TILA Section 105(a) authorizes the Board to make exceptions to TILA to effectuate the statute's purposes, which includes promoting the informed use of credit. 15 U.S.C. 1601(a), 1604(a). The Board believes that requiring these disclosures to appear separately from the other required disclosures would improve the consumer's ability to focus on the terms most useful to evaluating the proposed credit transaction.

TILA Section 105(f) authorizes the Board to exempt any class of transactions from coverage under any part of TILA if the Board determines that coverage under that part does not provide a meaningful benefit to consumers in the form of useful information or protection. 15 U.S.C. 1604(f)(1). TILA Section 105(f) directs the Board to make this determination in light of specific factors. 15 U.S.C. 1604(f)(2). These factors are (1) the amount of the loan and whether the disclosure provides a benefit to consumers who are parties to the transaction; (2) the extent to which the requirement complicates, hinders, or makes more expensive the credit process for the class of transactions; (3) the status of the borrower, including any related financial arrangements of the borrower, the financial sophistication of the borrower relative to the type of transaction, and the importance to the borrower of the credit, related supporting property, and coverage under TILA; (4) whether the loan is secured by the principal residence of

[90] *See, e.g.,* Credit CARD Act of 2009, Public Law No. 111–24, § 509; 123 Stat. 1734, 1763 (2009) (requiring the General Accounting Office to provide a report to Congress by December 31, 2010, of the suitability of credit insurance, debt cancellation agreements, and debt suspension agreements for target customers, the ''predatory nature'' of such offers, and the loss rates compared to more traditional insurance products).

the consumer; and (5) whether the exemption would undermine the goal of consumer protection. Although a credit transaction secured by real property or a dwelling is important to the borrower, the Board believes that removing these disclosures from the other segregated information would further, rather than undermine, the goal of consumer protection because consumers would then focus on the terms that are most important to their decision making process. The proposed rule would still require that the information be disclosed but would simply no longer require the disclosures to be provided with the segregated information.

38(j)(1) Itemization of Amount Financed

TILA Section 128(a)(2)(B), 15 U.S.C. 1638(a)(2)(B), and § 226.18(c) currently require that the creditor provide the consumer with a notice that an itemization of amount financed is available on request and to provide it when the consumer so requests. Regulation Z also provides that the good faith estimate of settlement costs (GFE) provided pursuant to RESPA suffices to satisfy the itemization of amount financed requirement. *See* § 226.18(c)(1), fn. 40. The staff commentary provides further that the HUD–1 settlement statement provided at settlement under RESPA also may be substituted for the itemization in connection with later disclosures made pursuant to § 226.19(a). *See* comment 18(c)–4.

Proposed § 226.38(j)(1) would mirror the rules currently found under § 226.l8(c) permitting a creditor to provide disclosures pursuant to RESPA in lieu of the itemization of amount financed. These rules originally were established by the Board pursuant to its authority under TILA Section 105(a) to make exceptions to facilitate compliance with TILA, and the Board is proposing to permit similar treatment under the same authority. Proposed § 226.38(j)(1) would differ from current § 226.18(c), as discussed below, to reflect recent changes to Regulation Z.

Under the proposal, the provisions permitting substitution of RESPA disclosures for the itemization of amount financed would be removed from § 226.18 and included under proposed § 226.38(j)(1). That section would govern the itemization disclosure contents for mortgage transactions, including all those subject to RESPA. As noted above, the Board also is proposing to make certain technical and conforming amendments under § 226.18(c).

Proposed § 226.38(j)(1)(i) would provide the same four categories of the itemization as currently appear in § 226.18(c)(1)—the amount of proceeds distributed directly to the consumer, the amount credited to the consumer's account, amounts paid to other persons on the consumer's behalf, and the prepaid finance charge. Proposed § 226.38(j)(1)(ii) similarly would provide to creditors the alternative under current § 226.18(c)(2) of disclosing the right to receive an itemization and providing it when the consumer so requests, instead of delivering the itemization routinely. Finally, proposed § 226.38(j)(1)(iii) would provide the alternative of substituting the RESPA GFE for the itemization. It also would state a parallel alternative of substituting the HUD–1 settlement statement for the itemization when a creditor provides later disclosures pursuant to § 226.19(a)(2), which currently is addressed only in the staff commentary under § 226.18(c). And proposed § 226.38(j)(1)(iii) would provide that the substitution is permissible for any transaction subject to § 226.38, whether subject to RESPA or not.

The Board notes that the timing of the HUD–1 settlement statement no longer is consistent with the timing of the TILA redisclosure under § 226.19(a)(2). Regulation X under RESPA requires the HUD–1 to be provided at settlement,[91] which generally corresponds with consummation of the transaction under Regulation Z. Under the MIDA final rule, and the proposed revisions to § 226.19 under this proposal, the redisclosure required under § 226.19(a)(2) must be received by the consumer at least three business days before consummation of the transaction. As current comment 18(c)–1 provides, and proposed § 226.38(j)(1) also would require, the itemization must be provided at the same time as the segregated disclosures. Accordingly, proposed § 226.38(j)(1)(iii) would provide that the HUD–1 settlement statement is a permissible substitute for the itemization of amount financed only if it is received by the consumer at least three business days prior to consummation, in accordance with § 226.19(a)(2).

The Board realizes that, in general, consumers currently receive a fully completed HUD–1 settlement statement only at consummation, in accordance with RESPA's requirements. For this reason, mortgage creditors might not take advantage of the alternative in proposed § 226.38(j)(1)(iii) as widely as they historically have done under § 226.18(c)(1), fn. 40. On the other hand, the Board notes that a creditor that does not avail itself of that alternative must follow one of the other two alternatives. Under proposed §§ 226.19(a) and 226.38(j)(1)(i), the creditor still must provide substantially the same information three business days before consummation. Under proposed §§ 226.19(a) and 226.38(j)(1)(ii), the creditor also must do so, at least in those cases where the consumer requests the itemization. Further, given the proposed expansion of the finance charge under § 226.4, discussed above, all of the information contained in either the good faith estimate or the itemization would have to be firmly established by three business days before consummation so that the creditor can comply with the timing requirements of proposed § 226.19(a)(2).

In any event, the Board believes that to permit substitution of the HUD–1 settlement statement for the itemization without requiring that it be delivered three business days before consummation would be inconsistent with the purposes of the MDIA amendments. The Board seeks comment on whether creditors would continue to make significant use of this alternative as proposed § 226.38(j)(1)(iii) would implement it and, if not, whether the alternative should be retained. If it should be retained, the Board seeks comment on how it might be structured without requiring that the HUD–1 settlement statement be received by the consumer earlier than RESPA requires while also preserving the purposes of the MDIA.

38(j)(2) Through (6) Rebate; Late Payment; Property Insurance; Contract Reference; Assumption Policy

The Board proposes to use its exception and exemption authorities under TILA Section 105(a), 15 U.S.C. 1604(a), to require creditors to provide the following disclosures separately from the other required disclosures: rebate under proposed § 226.38(j)(2), late payment under proposed § 226.38(j)(3), property insurance under proposed § 226.38(j)(4), contract reference under proposed § 226.38(j)(5), and assumption policy under proposed § 226.38(j)(6). The Board is not proposing to change the substantive content of these disclosures. Proposed § 226.38(j) would mirror § 226.18, except that the proposed requirement would be provided separately from the other required disclosures. The proposed comments for these

[91] 24 CFR 3500.10(b). The settlement agent must provide the borrower with an opportunity to inspect the HUD–1 during the business day preceding settlement, but only completed to reflect all information known to the settlement agent at the time. *Id.* 3500.10(a).

disclosures would also parallel the applicable comments under § 226.18.

In addition, the Board proposes Model Clauses at Appendix H–23 for the following non-segregated disclosures: rebate, late payment, property insurance, contract reference, and assumption policy. The Model Clauses are based on the Board's consumer testing and the Board believes that model clauses will enhance consumer understanding of the information, helping consumers to avoid the uninformed use of credit.

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

Appendices G and H set forth model forms, model clauses and sample forms that creditors may use to comply with the requirements of Regulation Z. Appendix G contains model forms, model clauses and sample forms applicable to open-end plans. Appendix H contains model forms, model clauses and sample forms applicable to closed-end loans. 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. As discussed above, the Board proposes to revise or add several model forms, model clauses and sample forms to Appendix H for transactions secured by real property or a dwelling. The revised or new model forms and clauses, and sample forms, are discussed above in the section-by-section analysis applicable to the regulatory provisions to which the forms or clauses relate. *See* discussion under §§ 226.19(b), 226.20(c)–(e), and 226.38(a)–(j). In addition, the Board proposes to add new model clauses and a sample form relating to credit insurance, debt cancellation and debt suspension coverage to both Appendix G and H for open-end and closed-end loans. These model clauses and sample forms are discussed under proposed § 226.4(d)(1) and (3) and 226.38(h). In Appendix H, all other existing forms and clauses applicable to transactions not secured by real property or a dwelling have been retained without revision.

The Board also proposes to revise or add commentary to the model forms, model clauses and sample forms in Appendix H, as discussed below. The Board solicits comments on the proposed revisions below, as well as whether any additional commentary should be added to explain the forms and clauses contained in Appendix H.

Permissible Changes

The commentary to appendices G and H currently states that creditors may make certain changes in the format and content of the model 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. However, certain formatting changes may not be made with respect to certain model and sample forms in Appendix G. *See* comment app. G and H–1. As discussed above, the Board is proposing format and content requirements with respect to disclosures for transactions secured by real property or a dwelling, such as a tabular requirement for ARM loan program disclosures and ARM adjustment notices, and transaction-specific disclosures required for loans secured by real property or a dwelling. *See* proposed §§ 226.19(b), 226.20(c), and 226.38(a)–(j). Accordingly, the Board would amend comment app. G and H–1 to indicate that certain formatting changes may not be made with respect to certain model forms, model clauses and sample forms in Appendix H. In addition, as discussed more fully under § 226.38, the Board proposes to require creditors to provide disclosures for transactions secured by real property or a dwelling only as applicable. As a result, the Board would not allow creditors to use multi-purpose forms; the Board would amend comment app. G and H–1(vi) to clarify that the use of multipurpose standard forms is not permitted for transactions secured by real property or a dwelling. *See* discussion under § 226.37(a)(2).

Debt Cancellation Coverage

Currently, commentary to appendices G and H states that creditors are not authorized to characterize debt-cancellation fees as insurance premiums for purposes of the regulation. The Board proposes to amend comment app. G and H–2 to clarify that the commentary also applies to debt suspension fees.

Appendix H—Closed-End Model Forms and Clauses

Model Forms, Model Clauses, and Sample Forms for Closed-End Disclosures

As noted above, the Board proposes a new disclosure regime under § 226.38 for transactions secured by real property or a dwelling. As a result, the following sample forms are rendered unnecessary and deleted: Sample H–13 (mortgage with demand feature sample); Sample H–14 (variable-rate mortgage sample); and Sample H–15 (graduated-payment mortgage sample). Comment app. H–1 would be revised to reflect the deletion of Samples H–13 through H–15. The Board would further amend comment app. H–1 to reflect that, under the proposal, new model clauses are added regarding credit life insurance, debt cancellation, or debt suspension disclosures, and creditor-placed property insurance disclosures. *See* discussion under §§ 226.4(d)(1) and (3), 226.38(h), and 226.20(e). These deleted samples forms and new model clauses are discussed more fully below.

Currently, comment app. H–2 addresses the flexibility given to creditors in providing the itemization of amount financed disclosure required under current § 226.18(c) and illustrated by Model Clause H–3. As discussed above, the Board is proposing new § 226.38(j)(1) regarding disclosure of the itemization of amount financed for transactions secured by real property or a dwelling. As a result, the Board would amend comment app. H–2 to update cross-references. In a technical revision, the Board would amend comment app. H–3 to clarify that the guidance applies to new Model Clauses H–4(B) and H–4(C), H–4(H), H–16, H–17(A) and H–17(C), H–18, and H–20 through H–23. These new model clauses are discussed more fully below.

Model Forms, Model Clauses, and Sample Forms for ARM Loan Program Disclosures

Currently, Appendix H contains several model clauses, and a sample form, related to variable-rate loan program disclosures required under current § 226.18(f)(1), 226.18(f)(2) and 226.19(b). Current Model Clause H–4(A) contains model clauses for variable-rate disclosures required under § 226.18(f)(1) for transactions not secured by a principal dwelling, or transactions secured by a dwelling with a term of one year or less. Current Model Clause H–4(B) contains model clauses for variable-rate disclosures for transactions that are secured by a principal dwelling with a term greater than one year. Current Model Clause H–4(C) contains model clauses related to variable-rate loan program disclosures required under § 226.19(b). Current Sample H–14 is a sample disclosure illustrating required disclosures under current § 226.19(b) of interest rate and monthly payment changes, as well as an historical example, for variable-rate loan programs.

Under the proposal, the Board would require new disclosures under § 226.19(b) for adjustable-rate loan programs, and would revise § 226.18(f)(1) and delete § 226.18(f)(2) to reflect such proposed changes to § 226.19(b). Accordingly, the Board proposes to delete current Model Clause H–4(B) and add new Model H–4(B) to illustrate, in the tabular format, the disclosures required under § 226.19(b) for adjustable-rate transactions secured by real property or a dwelling. The Board also would delete current Model Clause H–4(C) and add new Model Clauses H–4(C) to reflect the proposed changes to § 226.19(b), as discussed above, and to provide model clauses regarding interest rate carryover, conversion features, and preferred rates. The Board proposes to add Samples H–4(D) through H–4(F) to provide examples of how certain disclosures under § 226.19(b) may be provided, in the tabular format, for adjustable-rate loan programs that contain a hybrid, interest only, or payment option feature, respectively. In addition, the heading to Model Clause H–4(A) would be revised to update the cross-reference to § 226.18(f), and current Sample H–14 regarding variable-rate disclosures would be deleted and reserved.

The Board also proposes to revise existing commentary that provides guidance to creditors on how to use current Model Clauses H–4(A) through (C). Currently, comments app. H–4 through H–6 provide guidance regarding variable-rate loan program disclosures required under current §§ 226.18(f)(1)–(2) and 226.19(b). Under the proposal, the Board would delete guidance contained in current comment app. H–5 regarding disclosures under § 226.18(f)(2) as unnecessary, and instead provide that disclosures required under § 226.19(b) for adjustable-rate transactions be provided in the tabular format, as illustrated by Model H–4(B), and Samples H–4(D) through H–4(F). The Board also would delete guidance currently contained in comment app. H–6 relating to variable-rate disclosures, and instead provide guidance regarding model clauses on carryover interest, a conversion feature, or a preferred rate. In a technical revision, the Board would revise comment app. H–4 to update the cross-reference to § 226.18(f).

Model Forms, Model Clauses, and Sample Forms for ARM Adjustment Notices

Currently, Appendix H contains Model Clause H–4(D), which contains model clauses regarding interest rate and payment adjustment notices required for variable-rate transactions under current § 226.20(c). As discussed above under proposed§ 226.20(c), the Board proposes new timing and disclosure requirements regarding interest rate and payment changes for adjustable-rate transactions secured by real property or a dwelling. Accordingly, the Board would add a model form and two samples forms to illustrate, in the tabular format, the disclosures required under proposed § 226.20(c)(2) for ARM adjustment notices when there is an interest rate and payment change. *See* proposed Model H–4(G) and Samples H–4(I) and H–4(J). In addition, the Board proposes to add a model form to illustrate disclosures required under proposed § 226.20(c)(3) when there is an interest rate adjustment without any change to payment. *See* proposed Model H–4(K). Current Model Clause H–4(D) would be deleted and new Model Clauses H–4(H) would be added to reflect the proposed changes to § 226.20(c), as discussed above. The Board also proposes to revise current comment app. H–7 to provide that disclosures required under § 226.20(c) be provided in the tabular format, as illustrated by new Model H–4(G), and Samples H–4(I) and H–4(J).

Model Forms, Model Clauses, and Sample Forms for Periodic Statements

Currently, creditors are not required to provide certain disclosures with respect to periodic statements for loans that are negatively amortizing. As discussed under proposed § 226.20(d), the Board would require creditors to disclose periodic payment options on a monthly basis for transactions secured by real property or a dwelling that offer payment options and are negatively amortizing. Accordingly, the Board is proposing to add new Model Form H–4(L) that creditors may use to comply with the requirements in proposed § 226.20(d).

Model Clauses for Section 32 (HOEPA) Disclosures

Currently, Appendix H contains Mortgage Sample H–16, which provides model clauses for disclosures required under § 226.32(c), such as a notice to the borrower that he or she is not obligated to accept the terms of the loan and security interest disclosures. As discussed under proposed § 226.32(c)(1), the Board would require creditors to provide plain-language versions of the ''no obligation'' and ''security interest'' disclosures to better inform consumers who are considering obtaining HOEPA loans. The Board would revise Mortgage Sample H–16 accordingly. In addition, the Board proposes to revise commentary currently contained in comment app. H–20 to clarify that these disclosures are required for all HOEPA loans, and as noted below, would move this commentary to current comment app. H–17. In a technical revision, the Board would revise the heading to Mortgage Sample H–16 to reflect that it contains model clauses.

Model Clause for Credit Insurance, Debt Cancellation, or Debt Suspension

Currently, Appendix H contains a model clause and sample form that creditors may use to comply with the disclosure requirements under current § 226.4(d)(3) for debt suspension. *See* Model Clause H–17(A) and Sample H–17(B). As discussed above, the Board proposes new disclosure requirements for credit insurance, debt cancellation and debt suspension for all closed-end loans. *See* proposed §§ 226.4(d)(1), (d)(3) and 226.38(h). Accordingly, the Board proposes to add Model Clause H–17(C) and Sample H–17(D) that creditors may use to comply with the proposed requirements under §§ 226.4(d)(1), (d)(3) and 226.38(h).

Model Clause for Creditor-Placed Property Insurance

Currently, creditors are not required to provide any disclosures to the consumer with respect to creditor-placed property insurance. As discussed under proposed § 226.20(e), the Board would require creditors to provide notice of the cost and coverage of creditor-placed property insurance before charging the consumer for such insurance for transactions secured by real property or a dwelling. For all other closed-end loans, these disclosures would be required if creditors intend to exclude the creditor-placed property insurance fee from the finance charge under § 226.4(d). Accordingly, the Board proposes to add Model Clause H–18 that creditors may use to comply with the proposed requirements under § 226.20(e).

Model Forms, Model Clauses, and Sample Forms for Transaction-Specific Disclosures for Loans Secured by Real Property or a Dwelling

Currently, Appendix H contains several model forms, model clauses and samples that creditors may use to comply with the disclosures required under current § 226.18 for transactions secured by real property or a dwelling. Current Model H–2 illustrates the format and content of disclosures currently required under § 226.18 for mortgages. Current Model Clause H–6 contains a model clause for an assumption policy. Current Samples H–13 and H–15 are sample disclosures illustrating a mortgage with a demand feature and a graduated-payment mortgage, respectively.

As discussed under proposed § 226.38, the Board proposes a new disclosure regime for transactions secured by real property or a dwelling. Accordingly, the Board proposes to add new Model Forms, Model Clauses, and Sample Forms H–19 through H–23 that creditors may use to comply with the requirements in proposed § 226.38(a) through (j). The Board proposes to add Models H–19(A) through H–19(C) to illustrate the format and content of disclosures required under proposed § 226.38 for fixed-rate, hybrid adjustable-rate, and payment option mortgages, respectively. In addition, the Board would add Model Clauses H–20 and H–21 to provide guidance to creditors on how to disclose a balloon payment or introductory rate feature, respectively. Model Clause H–22 would be added to provide model clauses relating to key questions about risk disclosures required under proposed § 226.38(d)(2). Model Clause H–23 would be added to provide model clauses for the following disclosures required under proposed § 226.38(j)(2)–(6) for transactions secured by real property or a dwelling: rebate; late payment; property insurance; contract reference; and assumption policy. Under the proposal, current Samples H–13 and H–15 would be rendered unnecessary and therefore, are deleted and reserved. Model Clause H–6, which contains the current model clause for assumption, would be deleted because assumption policies are only applicable to transactions secured by real property or a dwelling; H–6 would be reserved.

In addition, the Board proposes to add several sample forms to provide examples of how creditors can provide certain disclosures required under proposed § 226.38 in the tabular format or scaled graph, as applicable, for various transaction types secured by real property or a dwelling. Specifically, proposed Samples H–19(D) through H–19(I) illustrate disclosures required under proposed § 226.38 for the following transaction-types, respectively: a fixed mortgage with balloon payment; an interest only, fixed mortgage; a step-payment mortgage; a hybrid adjustable-rate mortgage; an interest-only ARM; and a payment option ARM.

The Board also proposes to add or revise commentary to provide guidance to creditors on the purpose of the sample forms, and how to use Model Forms, Model Clauses, and Sample Forms H–19 through H–23 for transactions secured by real property or a dwelling. Current comment app. H–12 provides guidance to creditors regarding the purpose of sample forms generally. Under the proposal, the Board would update the cross-references contained in current comment app. H–12 to clarify that the commentary applies to proposed Sample H–4(D) through-4(F) for ARM loan program disclosures required under proposed § 226.19(b); Samples H–4(I) and H–4(J) for ARM adjustment notice disclosures required under § 226.20(c); Sample H–17(D) for credit insurance, debt cancellation or debt suspension disclosures required under § 226.4(d)(1), (d)(3) and 226.38(h); and Samples H–19(D) through H–19(I) for disclosures required under § 226.38 for transactions secured by real property or a dwelling.

Current comment app. H–16 provides guidance regarding the sample forms that creditors may use to illustrate required disclosures for mortgages subject to RESPA and would be updated to include cross-references to proposed Samples H–19(D) through H–19(I), and to the itemization of amount financed disclosure under proposed § 226.38(j)(1)(iii). Under the proposal, guidance contained in current comment app. H–17 regarding disclosure of a mortgage with a demand feature under § 226.18 would be deleted as unnecessary. As noted above, commentary regarding disclosures required under § 226.32(c) for HOEPA loans would be moved from comment app. H–20 to comment app. H–17.

In addition, under the proposal, current comment app. H–18, which contains guidance relating to variable-rate disclosures required under current § 226.19(b), would be deleted. New commentary would be added to comment app. H–18 to provide format details about proposed sample forms that illustrate the disclosures required for transactions secured by real property or a dwelling under proposed § 226.19(b) or 226.38, as applicable. For example, the commentary indicates that Samples H–4(D) through H–4(F), and H–19(D) through H–19(I) are designed to be printed on an 8½x11 inch sheet of paper. In addition, the following formatting techniques were used in presenting the information in the table to ensure that the information was readable:

1. A readable font style and font size (10-point Ariel font style, except for the APR which is shown in 16-point type).

2. Sufficient spacing between lines of the text. That is, words were not compressed to appear smaller than 10-point type, except for headings used to provide interest rate and payment summary disclosures required under proposed § 226.28(c), in the tabular format, which are shown in 9-point type.

3. Standard spacing between words and characters.

4. Sufficient white space around the text of the information in each row, by providing sufficient margins above, below and to the sides of the text.

5. Sufficient contrast between the text and the background. Black text was used on white paper.

Although the Board is not requiring creditors to use the above formatting techniques in presenting information in the table (except for the 10-point and 16-point font size), the Board encourages creditors to consider these techniques when disclosing information in the tabular format, or scaled graph, to ensure that the information is presented in a readable format.

Under the proposal, commentary currently contained in comment app. H–19 regarding the terms of a graduated-payment mortgage would be deleted, and would instead indicate the terms of the fixed-rate mortgage illustrated in Sample H–19(D). As noted above, guidance contained in current app. H–20 regarding disclosures required under § 226.32(c) would be moved to comment app. H–17. The Board proposes to add new commentary to comment app. H–20 to indicate the terms of the interest-only, fixed-rate mortgage illustrated in Sample H–19(E). The Board also proposes to add comments app. H–21 through –24 to indicate the terms of the following transaction types, which are illustrated in Samples H–19(F) through 19(I), respectively: a step-payment mortgage; a hybrid ARM; an interest-only ARM; and a payment option ARM. The transactions discussed in revised comments app. H–19 and H–20, and new comments app. H–21 through –24, all assume the average prime offer rates (APORs) that would be used in providing the disclosures required under proposed § 226.38(b), and are not representative of the actual APORs for the respective weeks.

Further, the Board proposes to add comments app. H–25 through –28 relating to the following, respectively: the disclosure required under proposed § 226.38(c) for a balloon payment feature; the disclosure required under proposed § 226.38(c)(2)(iii) for transactions that have an initial discounted rate that later adjusts; disclosures required under proposed § 226.19(d)(2) for key questions about risk that would be provided only as applicable; and disclosures required under proposed § 226.38(j)(2)–(6) that would be provided separately from disclosures required under proposed § 226.38(a)–(j). In a technical revision, current comments app. H–21 through –24, which contain guidance relating to forms issued by the U.S. Department of Health and Human Services and approved for certain student loans, would be redesignated as comments app. H–29 through –32, respectively; no substantive change is intended.

VII. 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 proposed 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 proposed 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 to, among other things, 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 in connection with 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, § 226.25, but Regulation Z identifies only a few specific types of records that must be retained.[92]

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 734,127 hours for the 1,138 Federal Reserve-regulated institutions that are deemed to be respondents for the purposes of the PRA. To ease the burden and cost of complying with Regulation Z (particularly for small entities), the Board provides model forms, which are appended to the regulation.

As discussed in the preamble, the Board proposes changes to format, timing, and content requirements for the four main types of credit disclosures for closed-end mortgages governed by Regulation Z: (1) Disclosures at or before application; (2) disclosures within three days after application; (3) disclosures before consummation; and (4) disclosures after consummation. The proposed rule would impose a one-time increase in the total annual burden under Regulation Z for all respondents regulated by the Federal Reserve by 227,600 hours, from 734,127 to 961,727 hours. In addition, the Board estimates that, on a continuing basis, the proposed revisions to the rules would increase the total annual burden on a continuing basis from 734,127 to 1,280,367 hours.

The total estimated burden increase, as well as the estimates of the burden increase associated with each major section of the proposed rule as set forth below, represents averages for all respondents regulated by the Federal Reserve. The Board expects that the amount of time required to implement each of the proposed changes for a given institution may vary based on the size and complexity of the respondent. Furthermore, the burden estimate for this rulemaking does not include the burden of complying with proposed disclosure and timing requirements that apply to private educational lenders making private education loans as announced in a separate proposed rulemaking (Docket No. R–1353) or the proposed disclosure and timing requirements of the Board's separate notice published simultaneously with this proposal for open-end credit plans secured by real property.

The Board estimates that 1,138 respondents regulated by the Federal Reserve would take, on average, 200 hours (five business weeks) to update their systems, internal procedure manuals, and provide training for relevant staff to comply with the proposed disclosure requirements in §§ 226.38 and 226.20(d), and revisions to existing disclosure requirements in §§ 226.19(b) and 226.20(c). This one-time revision would increase the burden by 227,600 hours. On a continuing basis the Board estimates that 1,138 respondents regulated by the Federal Reserve would take, on average, 40 hours a month to comply with the closed-end disclosure requirements and would increase the ongoing burden from 304,756 hours to 546,240 hours. To ease the burden and cost of complying with the new and proposed requirements under Regulation Z the Board proposes to revise or add several model forms, model clauses and sample forms to Appendix H.

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 17,200 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 would be approximately 13,568,725 hours. The proposed rule would impose a one-time increase in the estimated annual burden for such institutions by 3,440,000 hours to 17,765,525 hours. On a continuing basis the proposed rule would impose an increase in the estimated annual burden by 8,256,000 to 21,824,725 hours. The above estimates represent an average across all respondents; the Board expects

[92] *See* comments 25(a)–3 and –4 and proposed comment 25(a)–5.

variations between institutions based on their size, complexity, and practices.

Comments are invited on: (1) Whether the proposed 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 proposed 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 Cynthia Ayouch, Acting 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.

VIII. Initial Regulatory Flexibility Analysis

In accordance with section 3(a) of the Regulatory Flexibility Act (RFA), 5 U.S.C. 601–612, the Board is publishing an initial regulatory flexibility analysis for the proposed amendments to Regulation Z. The RFA requires an agency either to provide an initial regulatory flexibility analysis with a proposed rule or to certify that the proposed rule will not have a significant economic impact on a substantial number of small entities. Under regulations issued by the Small Business Administration, an entity is considered ''small'' if it has $175 million or less in assets for banks and other depository institutions; and $7 million or less in revenues for non-bank mortgage lenders and mortgage brokers.[93]

Based on its analysis and for the reasons stated below, the Board believes that this proposed rule will have a significant economic impact on a substantial number of small entities. A final regulatory flexibility analysis will be conducted after consideration of comments received during the public comment period. The Board requests public comment in the following areas.

A. Reasons for the Proposed Rule

Congress enacted 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 a 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. In this regard, the goal of the proposed amendments to Regulation Z is to improve the effectiveness of the disclosures that creditors provide to consumers beginning before application and throughout the life of a closed-end mortgage transaction. Accordingly, the Board is proposing changes to format, timing, and content requirements for closed-end disclosures required by Regulation Z: (1) Program and other educational information provided before application; (2) transaction-specific disclosures provided at or shortly after application; (3) transaction-specific disclosures provided at or three business days before consummation; and notices of changes to the transaction's terms and regarding certain payment options provided during the life of the credit.

Congress enacted HOEPA in 1994 as an amendment to TILA. TILA is implemented by the Board's Regulation Z. HOEPA imposed additional substantive protections on certain high-cost mortgage transactions. HOEPA also charged the Board with prohibiting acts or practices in connection with mortgage loans that are unfair, deceptive, or designed to evade the purposes of HOEPA, and acts or practices in connection with refinancing of mortgage loans that are associated with abusive lending or are otherwise not in the interest of borrowers.

The proposed regulations would revise and enhance many of the closed-end disclosure requirements of Regulation Z for transactions secured by real property or a dwelling. The Board's proposal also would require TILA disclosures for closed-end mortgages to be provided to the consumer earlier in the loan process and would expand on the post-consummation notification requirements concerning changes in mortgage terms. These amendments are proposed in furtherance of the Board's responsibility to prescribe regulations to carry out the purposes of TILA, including promoting consumers' awareness of the cost of credit and their informed use thereof. Finally, the proposal would restrict certain loan originator compensation practices for closed-end mortgage loans to address problems that have been observed in the mortgage market. These restrictions are proposed pursuant to the Board's statutory responsibility to prohibit unfair and deceptive acts and practices in connection with mortgage loans.

B. Statement of Objectives and Legal Basis

The **SUPPLEMENTARY INFORMATION** contains this information. In summary, the proposed amendments to Regulation Z are designed to achieve three goals: (1) Revise the disclosures required for closed-end mortgage loans; (2) restrict certain loan originator compensation practices for mortgage loans; and (3) require disclosures for closed-end mortgage loans to be provided earlier in the transaction and additional post-consummation disclosures for certain changes in terms.

The legal basis for the proposed rule is in Sections 105(a), 105(f), and 129(*l*)(2) of TILA. 15 U.S.C. 1604(a), 1604(f), and 1639(*l*)(2). A more detailed discussion of the Board's rulemaking authority is set forth in part IV of the **SUPPLEMENTARY INFORMATION.**

C. Description of Small Entities to Which the Proposed Rule Would Apply

The proposed regulations would apply to all institutions and entities that engage in originating or extending closed-end, home-secured credit. The Board is not aware of a reliable source for the total number of small entities likely to be affected by the proposal, and the credit provisions of TILA and Regulation Z have broad applicability to individuals and businesses that originate, extend and service even small numbers of home-secured credit. *See* § 226.1(c)(1).[94] All small entities that originate, extend, or service closed-end loans secured by real property or a dwelling potentially could be subject to at least some aspects of the proposed rule.

The Board can, however, identify through data from Reports of Condition and Income (''call reports'') approximate numbers of small depository institutions that would be subject to the proposed rules. Based on December 2008 call report data, approximately 9,418 small institutions would be subject to the proposed rule. Approximately 16,345 depository institutions in the United States filed call report data, approximately 11,907 of which had total

[93] 13 CFR 121.201.

[94] Regulation Z generally applies to ''each individual or business that offers or extends credit when four conditions are met: (i) The credit is offered or extended to consumers; (ii) the offering or extension of credit is done regularly, (iii) the credit is subject to a finance charge or is payable by a written agreement in more than four installments, and (iv) the credit is primarily for personal, family, or household purposes.'' § 226.1(c)(1).

domestic assets of $175 million or less and thus were considered small entities for purposes of the Regulatory Flexibility Act. Of 4,231 banks, 565 thrifts and 7,111 credit unions that filed call report data and were considered small entities, 4,091 banks, 530 thrifts, and 4,797 credit unions, totaling 9,418 institutions, extended mortgage credit. For purposes of this analysis, thrifts include savings banks, savings and loan entities, co-operative banks and industrial banks.

The Board cannot identify with certainty the number of small non-depository institutions that would be subject to the proposed rule. Home Mortgage Disclosure Act (HMDA) [95] data indicate that 1,752 non-depository institutions filed HMDA reports in 2007.[96] Based on the small volume of lending activity reported by these institutions, most are likely to be small.

The proposal's restrictions on compensation of loan originators would apply to mortgage brokers. Loan originators other than mortgage brokers that would be affected by the proposal are employees of creditors (or of brokers) and, as such, are not business entities in their own right. In its 2008 proposed rule under HOEPA, 73 FR 1672, 1720; Jan. 9, 2008, the Board noted that, according to the National Association of Mortgage Brokers (NAMB), in 2004 there were 53,000 mortgage brokerage companies that employed an estimated 418,700 people.[97] The Board estimated that most of these companies are small entities. On the other hand, the U.S. Census Bureau's 2002 Economic Census indicates that there were only 17,041 ''mortgage and nonmortgage loan brokers'' in the United States at that time.[98]

D. Projected Reporting, Recordkeeping, and Other Compliance Requirements

The compliance requirements of the proposed rules are described in parts V and VI of the **SUPPLEMENTARY INFORMATION**. The effect of the proposed revisions to Regulation Z on small entities is unknown. Some small entities would be required, among other things, to modify their home-secured credit disclosures and processes for delivery thereof to comply with the revised rules. The precise costs to small entities of updating their systems and disclosures are difficult to predict. 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 and to administer and maintain accounts, the complexity of the terms of credit products that they offer, and the range of such product offerings.

Additionally, the proposed rules could affect how loan originators are compensated and would impose certain related recordkeeping requirements on creditors. The precise costs that the proposed rule would impose on mortgage creditors and loan originators are also difficult to ascertain. Nevertheless, the Board believes that these costs will have a significant economic effect on small entities, including small mortgage creditors and brokers. The Board seeks information and comment on any costs, compliance requirements, or changes in operating procedures arising from the application of the proposed rule to small businesses.

E. Identification of Duplicative, Overlapping, or Conflicting Federal Rules

Other Federal Rules

The Board has not identified any federal rules that conflict with the proposed revisions to Regulation Z.

Overlap With SAFE Act

The proposed rule's required disclosure contents for closed-end mortgage transactions would overlap with the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act) by requiring that the disclosure include the loan originator's unique identifier, as defined by that Act, if applicable.

Overlap With RESPA

Certain terms defined in the proposed rule, such as ''total settlement charges'' cross-reference definitions under the U.S. Department of Housing and Urban Development's (HUD's) Regulation X under the Real Estate Settlement Procedures Act (RESPA). The proposed rule also would modify the existing prerequisites for use of the RESPA good faith estimate of settlement costs and HUD–1 settlement statement in lieu of the itemization of the amount financed under Regulation Z.

Overlap With HUD's Guidance

The Board recognizes that HUD has issued policy statements regarding creditor payments to mortgage brokers under RESPA and guidance as to disclosure of such payments on the Good Faith Estimate and HUD–1 Settlement Statement. HUD also has published revised disclosures for broker compensation under RESPA to become effective January 1, 2010. The Board intends that its proposal would complement HUD's final rule. The proposed provision regarding creditor payments to loan originators is intended to be consistent with HUD's existing guidance regarding broker compensation under Section 8 of RESPA. The proposed provision regarding record retention to evidence compliance with the provision regarding creditor payments to loan originators would cross-reference the HUD–1 settlement statement as an acceptable record of such compensation paid in a given transaction.

F. Identification of Duplicative, Overlapping, or Conflicting State Laws

State Laws Regulating Creditor Payments to Loan Originators

The Board is aware that many states regulate loan originators, especially mortgage brokers, and their compensation in various respects. Under TILA Section 111, the proposed rule would not preempt such State laws except to the extent they are inconsistent with the proposal's requirements. 15 U.S.C. 1610.

State Equivalents to TILA and HOEPA

Many states regulate consumer credit through statutory disclosure schemes similar to TILA. Similarly to State laws regulating loan originator compensation, such state disclosure laws would be preempted only to the extent they are inconsistent with the proposal's requirements. *Id.*

The Board also is aware that many states regulate ''high-cost'' or ''high-priced'' mortgage loans, under laws that

[95] The 8,610 lenders (both depository institutions and mortgage companies) covered by HMDA in 2007 accounted for an estimated 80% of all home lending in the United States (2008 HMDA data are not yet available). Under HMDA, lenders use a ''loan/application register'' (HMDA/LAR) to report information annually to their Federal supervisory agencies for each application and loan acted on during the calendar year. Lenders must make their HMDA/LARs available to the public by March 31 following the year to which the data relate, and they must remove the two date-related fields to help preserve applicants' privacy. Only lenders that have offices (or, for non-depository institutions, are deemed to have offices) in metropolitan areas are required to report under HMDA. However, if a lender is required to report, it must report information on all of its home loan applications and loans in all locations, including non-metropolitan areas.

[96] *The 2007 HMDA Data, http://www.federalreserve.gov/pubs/bulletin/2008/articles/hmda/default.htm.*

[97] *http://www.namb.org/namb/Industry_Facts.asp?SnID=719224934.* This page of the NAMB Web site, however, no longer provides an estimate of the number of mortgage brokerage companies.

[98] *http://www.census.gov/prod/ec02/ec0252a1us.pdf* (NAICS code 522310). Data on this industry sector are not yet available from the 2007 Economic Census.

resemble HOEPA. Many such State laws set their coverage tests in part on the APR of the transaction. The proposed rule would overlap with these laws indirectly by virtue of the proposal to modify the definition of the finance charge for closed-end mortgage transactions, which would result in APRs being higher generally and potentially more loans being covered under such State laws.

The Board seeks comment regarding any State or local statutes or regulations that would duplicate, overlap, or conflict with the proposed rule.

G. Discussion of Significant Alternatives

The Board considered whether improved disclosures could protect consumers against unfair loan originator compensation practices for mortgages as well as the proposed rule. While the Board is proposing improvements to mortgage loan disclosures, it does not appear that better disclosures would address loan originator compensation practices adequately.

The Board welcomes comments on any significant alternatives, consistent with the requirements of TILA, that would minimize the impact of the proposed rule on small entities.

List of Subjects in 12 CFR Part 226

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

Text of Proposed Revisions

Certain conventions have been used to highlight the proposed revisions. New language is shown inside bold arrows, and language that would be deleted is shown inside bold brackets.

Authority and Issuance

For the reasons set forth in the preamble, the Board proposes to amend 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); Public Law 111–24 § 2, 123 Stat. 1734.

Subpart A—General

2. Section 226.1, as amended on January 29, 2009 (74 FR 5397) is amended by revising paragraphs (b) and (d)(5) to read as follows:

§ 226.1 Authority, purpose, coverage, organization, enforcement and liability.

* * * * *

(b) *Purpose.* The purpose of this regulation is to promote the informed use of consumer credit by requiring disclosures about its terms and cost. The regulation also gives consumers the right to cancel certain credit transactions that involve a lien on a consumer's principal dwelling, regulates certain credit card practices, and provides a means for fair and timely resolution of credit billing disputes. The regulation does not govern charges for consumer credit. The regulation requires a maximum interest rate to be stated in variable-rate contracts secured by the consumer's dwelling. It also imposes limitations on home-equity plans that are subject to the requirements of § 226.5b and mortgages that are subject to the requirements of § 226.32. The regulation prohibits certain acts or practices in connection with credit secured by ►real property or◄ a consumer's [principal] dwelling ►in § 226.36, and credit secured by a consumer's principal dwelling in § 226.35.◄

* * * * *

(d) * * *

(5) Subpart E contains special rules for mortgage transactions. Section 226.32 requires certain disclosures and provides limitations for ►closed-end◄ loans that have rates and fees above specified amounts. Section 226.33 requires disclosures, including the total annual loan cost rate, for reverse mortgage transactions. Section 226.34 prohibits specific acts and practices in connection with ►closed-end◄ mortgage transactions that are subject to § 226.32. Section 226.35 prohibits specific acts and practices in connection with ►closed-end◄ higher-priced mortgage loans, as defined in § 226.35(a). Section 226.36 prohibits specific acts and practices in connection with ►extensions of◄ credit secured by ►real property or◄ a consumer's [principal] dwelling. ►Section 226.37 provides general disclosure requirements for closed-end extensions of credit secured by real property or a consumer's dwelling. Section 38 provides the content of disclosures for closed-end extensions of credit secured by real property or a consumer's dwelling.◄

* * * * *

3. Section 226.4, as amended on January 29, 2009 (74 FR 5399) is revised to read as follows:

§ 226.4 Finance charge.

(a) *Definition.* The finance charge is the cost of consumer credit as a dollar amount. It includes any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit. It does not include any charge of a type payable in a comparable cash transaction.

(1) *Charges by third parties.* The finance charge includes fees and amounts charged by someone other than the creditor, unless otherwise excluded under this section, if the creditor:

(i) Requires the use of a third party as a condition of or an incident to the extension of credit, even if the consumer can choose the third party; or

(ii) Retains a portion of the third-party charge, to the extent of the portion retained.

(2) *Special rule; closing agent charges.* ►Except as provided in § 226.4(g), fees◄ [Fees] charged by a third party that conducts the loan closing (such as a settlement agent, attorney, or escrow or title company) are finance charges only if the creditor:

(i) Requires the particular services for which the consumer is charged;

(ii) Requires the imposition of the charge; or

(iii) Retains a portion of the third-party charge, to the extent of the portion retained.

(3) *Special rule; mortgage broker fees.* Fees charged by a mortgage broker (including fees paid by the consumer directly to the broker or to the creditor for delivery to the broker) are finance charges even if the creditor does not require the consumer to use a mortgage broker and even if the creditor does not retain any portion of the charge.

(b) *Examples of finance charge.* The finance charge includes the following types of charges, except for charges specifically excluded by paragraphs (c) through (e) of this section:

(1) Interest, time price differential, and any amount payable under an add-on or discount system of additional charges.

(2) Service, transaction, activity, and carrying charges, including any charge imposed on a checking or other transaction account to the extent that the charge exceeds the charge for a similar account without a credit feature.

(3) Points, loan fees, assumption fees, finder's fees, and similar charges.

(4) Appraisal, investigation, and credit report fees.

(5) Premiums or other charges for any guarantee or insurance protecting the creditor against the consumer's default or other credit loss.

(6) Charges imposed on a creditor by another person for purchasing or accepting a consumer's obligation, if the consumer is required to pay the charges in cash, as an addition to the obligation,

or as a deduction from the proceeds of the obligation.

(7) Premiums or other charges for credit life, accident, health, or loss-of-income insurance, written in connection with a credit transaction.

(8) Premiums or other charges for insurance against loss of or damage to property, or against liability arising out of the ownership or use of property, written in connection with a credit transaction.

(9) Discounts for the purpose of inducing payment by a means other than the use of credit.

(10) Charges or premiums paid for debt cancellation or debt suspension coverage written in connection with a credit transaction, whether or not the debt cancellation coverage is insurance under applicable law.

(c) *Charges excluded from the finance charge.* ►Except as provided in § 226.4(g), the◄ [The] following charges are not finance charges:

(1) Application fees charged to all applicants for credit, whether or not credit is actually extended.

(2) Charges for actual unanticipated late payment, for exceeding a credit limit, or for delinquency, default, or a similar occurrence.

(3) Charges imposed by a financial institution for paying items that overdraw an account, unless the payment of such items and the imposition of the charge were previously agreed upon in writing.

(4) Fees charged for participation in a credit plan, whether assessed on an annual or other periodic basis.

(5) Seller's points.

(6) Interest forfeited as a result of an interest reduction required by law on a time deposit used as security for an extension of credit.

(7) *Real-estate related fees.* The following fees in ►an open-end credit plan◄ [a transaction] secured by real property or in ►an open-end◄ [a] residential mortgage transaction, if the fees are bona fide and reasonable in amount:

(i) Fees for title examination, abstract of title, title insurance, property survey, and similar purposes.

(ii) Fees for preparing loan-related documents, such as deeds, mortgages, and reconveyance or settlement documents.

(iii) Notary and credit report fees.

(iv) Property appraisal fees or fees for inspections to assess the value or condition of the property if the service is performed prior to closing, including fees related to pest infestation or flood hazard determinations.

(v) Amounts required to be paid into escrow or trustee accounts if the amounts would not otherwise be included in the finance charge.

(8) Discounts offered to induce payment for a purchase by cash, check, or other means, as provided in section 167(b) of the Act.

(d) *Insurance and debt cancellation and debt suspension coverage.* (1) *Voluntary credit insurance premiums.* ►Except as provided in § 226.4(g), premiums◄ [Premiums] for credit life, accident, health, or loss-of-income insurance may be excluded from the finance charge if the following conditions are met:

(i) The insurance coverage is not required by the creditor, and this fact is disclosed in writing.

(ii) The premium for the initial term of insurance coverage is disclosed in writing. If the term of insurance is less than the term of the transaction, the term of insurance also shall be disclosed. The premium may be disclosed on a unit-cost basis only in open-end credit transactions, closed-end credit transactions by mail or telephone under § 226.17(g), and certain closed-end credit transactions involving an insurance plan that limits the total amount of indebtedness subject to coverage.

(iii) The consumer signs or initials an affirmative written request for the insurance after receiving the disclosures specified in this paragraph, except as provided in paragraph (d)(4) of this section. Any consumer in the transaction may sign or initial the request.

►(iv) The creditor determines at the time of enrollment that the consumer meets any applicable age or employment eligibility criteria for insurance coverage.◄

(2) *Property insurance premiums.* Premiums for insurance against loss of or damage to property, or against liability arising out of the ownership or use of property, including single interest insurance if the insurer waives all right of subrogation against the consumer,[5] may be excluded from the finance charge if the following conditions are met:

(i) The insurance coverage may be obtained from a person of the consumer's choice,[6] and this fact is disclosed. (A creditor may reserve the right to refuse to accept, for reasonable cause, an insurer offered by the consumer.)

(ii) If the coverage is obtained from or through the creditor, the premium for the initial term of insurance coverage shall be disclosed. If the term of insurance is less than the term of the transaction, the term of insurance shall also be disclosed. The premium may be disclosed on a unit-cost basis only in open-end credit transactions, closed-end credit transactions by mail or telephone under § 226.17(g), and certain closed-end credit transactions involving an insurance plan that limits the total amount of indebtedness subject to coverage.

(3) *Voluntary debt cancellation or debt suspension fees.* ►Except as provided in § 226.4(g), charges◄ [Charges] or premiums paid for debt cancellation coverage for amounts exceeding the value of the collateral securing the obligation or for debt cancellation or debt suspension coverage in the event of the loss of life, health, or income or in case of accident may be excluded from the finance charge, whether or not the coverage is insurance, if the following conditions are met:

(i) The debt cancellation or debt suspension agreement or coverage is not required by the creditor, and this fact is disclosed in writing.

(ii) The fee or premium for the initial term of coverage is disclosed in writing. If the term of coverage is less than the term of the credit transaction, the term of coverage also shall be disclosed. The fee or premium may be disclosed on a unit-cost basis only in open-end credit transactions, closed-end credit transactions by mail or telephone under § 226.17(g), and certain closed-end credit transactions involving a debt cancellation agreement that limits the total amount of indebtedness subject to coverage.

(iii) The following are disclosed, as applicable, for debt suspension coverage: That the obligation to pay loan principal and interest is only suspended, and that interest will continue to accrue during the period of suspension.

(iv) The consumer signs or initials an affirmative written request for coverage after receiving the disclosures specified in this paragraph, except as provided in paragraph (d)(4) of this section. Any consumer in the transaction may sign or initial the request.

►(v) The creditor determines at the time of enrollment that the consumer meets any applicable age or employment eligibility criteria for the debt cancellation or debt suspension agreement or coverage.◄

(4) *Telephone purchases.* If a consumer purchases credit insurance or debt cancellation or debt suspension coverage for an open-end [(not home-secured)] plan by telephone, the creditor must make the disclosures under

[5] [Reserved].

[6] [Reserved].

paragraphs (d)(1)(i) and (ii) or (d)(3)(i) through (iii) of this section, as applicable, orally. In such a case, the creditor shall:

(i) Maintain evidence that the consumer, after being provided the disclosures orally, affirmatively elected to purchase the insurance or coverage; and

(ii) Mail the disclosures under paragraphs (d)(1)(i) and (ii) or (d)(3)(i) through (iii) of this section, as applicable, within three business days after the telephone purchase.

(e) *Certain security interest charges.* ►Except as provided in § 226.4(g), if◄ [If] itemized and disclosed, the following charges may be excluded from the finance charge:

(1) Taxes and fees prescribed by law that actually are or will be paid to public officials for determining the existence of or for perfecting, releasing, or satisfying a security interest.

(2) The premium for insurance in lieu of perfecting a security interest to the extent that the premium does not exceed the fees described in paragraph (e)(1) of this section that otherwise would be payable.

(3) *Taxes on security instruments.* Any tax levied on security instruments or on documents evidencing indebtedness if the payment of such taxes is a requirement for recording the instrument securing the evidence of indebtedness.

(f) *Prohibited offsets.* Interest, dividends, or other income received or to be received by the consumer on deposits or investments shall not be deducted in computing the finance charge.

►(g) *Special rule; closed-end mortgage transactions.* Paragraphs (a)(2) and (c) through (e) of this section, other than §§ 226.4(c)(2), 226.4(c)(5) and 226.4(d)(2), do not apply to closed-end transactions secured by real property or a dwelling.◄

Subpart C—Closed-End Credit

4. Section 226.17 is revised to read as follows:

§ 226.17 General disclosure requirements.

(a) *Form of disclosures.* (1) The creditor shall make the disclosures required by this subpart clearly and conspicuously in writing, in a form that the consumer may keep. ►In addition, transactions secured by real property or a dwelling are subject to the requirements under § 226.37.◄ The disclosures required by this subpart may be provided to the consumer in electronic form, subject to compliance with the consumer-consent and other applicable provisions of the Electronic Signatures in Global and National Commerce Act (E-Sign Act) (15 U.S.C. 7001 *et seq.*). ►For transactions secured by real property or a dwelling, disclosures required by § 226.19(b) or (c) must be provided in electronic form in specified circumstances.◄ The disclosures required by §§ 226.17(g), 226.19(b),► 226.19(c),◄ and 226.24 may be provided to the consumer in electronic form without regard to the consumer consent or other provisions of the E–Sign Act in the circumstances set forth in those sections. The disclosures ►required by § 226.18 or § 226.38◄ shall be grouped together, shall be segregated from everything else, and shall not contain any information not directly related [37] to the disclosures required under § 226.18 [38]►or § 226.38; however, the disclosures may include an acknowledgement of receipt, the date of the transaction, and the consumer's name, address, and account number. The following disclosures may be made together with or separately from other required disclosures: the variable-rate example under § 226.18(f)(4), insurance, debt cancellation, or debt suspension under § 226.18(n), and certain security interest charges under § 226.18(o)◄. The itemization of the amount financed under § 226.18(c)(1) must be separate from the other disclosures under that section.

(2)►Except for transactions secured by real property or a dwelling subject to § 226.38, t◄[T]he terms *finance charge* and *annual percentage rate,* when required to be disclosed under § 226.18(d) and (e) together with a corresponding amount or percentage rate, shall be more conspicuous than any other disclosure, except the creditor's identity under § 226.18(a).

(b) *Time of disclosures.* The creditor shall make disclosures before consummation of the transaction. [In certain mortgage transactions, special timing requirements are set forth in § 226.19(a). In certain variable-rate transactions, special timing requirements for variable-rate disclosures are set forth in § 226.19(b) and § 226.20(c).] ►Special disclosure timing requirements for transactions secured by real property or a dwelling are set forth in § 226.19(a). Additional disclosure timing requirements for adjustable-rate transactions secured by real property or a dwelling are set forth in § 226.19(b) and § 226.20(c).◄ In certain transactions involving mail or telephone orders or a series of sales, the timing of disclosures may be delayed in accordance with paragraphs (g) and (h) of this section.

(c) *Basis of disclosures and use of estimates.* (1) ►*Legal obligation.*◄ The disclosures ►required by this subpart◄ shall reflect the terms of the legal obligation between the parties.

►(i) *Buydowns.* The creditor shall disclose an annual percentage rate that is a composite rate based on the interest rate in effect during the initial period of the term of the loan and the interest rate in effect for the remainder of the term, if the consumer's interest rate or payments are reduced for all or part of the loan term based on payments made by:

(A) The seller or another third party, if the legal obligation reflects such an arrangement; or

(B) The consumer.

(ii) *Wrap-around financing.* If a transaction involves combining the outstanding balance on an existing loan with additional funds advanced to a consumer without paying off the outstanding balance, the amount financed shall equal the sum of the outstanding balance and the new funds advanced.

(iii) *Variable- or adjustable-rate transactions.* The creditor shall base disclosures for a variable- or adjustable-rate transaction on the full term of the transaction. Except as otherwise provided in § 226.38(a)(3) and (c) for adjustable-rate mortgage transactions secured by real property or a dwelling:

(A) If the initial interest rate for a transaction with a variable or adjustable rate is determined using the index or formula used to adjust the interest rate, the disclosures shall reflect the terms in effect at the time of consummation.

(B) If the initial interest rate for a transaction with a variable or adjustable rate is not determined using the index or formula used to adjust the interest rate, the disclosures shall reflect a composite annual percentage rate based on the initial rate for the time it is in effect and, for the remainder of the term, the rate that would have applied if such index or formula had been used at the time of consummation.

(iv) *Repayment upon occurrence of future event.* If disbursements for a transaction secured by real property or a dwelling are made during a specified period but repayment is required only upon the occurrence of a future event, the creditor shall base disclosures on

[37] ►[Reserved]◄[The disclosures may include an acknowledgment of receipt, the date of the transaction, and the consumer's name, address, and account number.]

[38] ►[Reserved]◄[The following disclosures may be made together with or separately from other required disclosures: the creditor's identity under § 226.18(a), the variable-rate example under § 226.18(f)(1)(iv), insurance or debt cancellation under § 226.18(n), and certain security interest charges under § 226.18(o).]

the assumption that repayment will occur when disbursements end.

(v) *Tax refund-anticipation loans.* For a tax refund-anticipation loan, the creditor shall estimate the time a tax refund will be delivered to the consumer and shall include in the finance charge any repayment amount that exceeds the loan amount that is not otherwise excluded from the finance charge under § 226.4.

(vi) *Pawn transactions.* For a pawn transaction, the creditor shall disclose:

(A) The initial sum paid to the consumer as the amount financed;

(B) A finance charge that includes the difference between the initial sum paid to the consumer and the price at which the item is pledged or sold; and

(C) The annual percentage rate is determined using the earliest date on which the item pledged or sold may be redeemed as the end of the loan term.◀

(2)▶*Estimates.*◀ (i) ▶*Reasonably available information.*◀ If any information necessary for an accurate disclosure is unknown to the creditor, the creditor shall make the disclosure based on the best information reasonably available at the time the disclosure is provided to the consumer[,] and shall state clearly that the disclosure is an estimate▶(except that § 226.19(a) limits the circumstances in which creditors may provide estimated disclosures, for mortgage transactions secured by real property or a dwelling)◀.

(ii)▶*Per-diem interest.*◀ For a transaction in which a portion of the interest is determined on a per-diem basis and collected at consummation, any disclosure affected by the per-diem interest shall be considered accurate if the disclosure is based on the information known to the creditor at the time that the disclosure documents are prepared for consummation of the transaction.

(3)▶*Disregarded effects.*◀ The creditor may disregard the effects of the following in making calculations and disclosures:

(i) That payments must be collected in whole cents.

(ii) That dates of scheduled payments and advances may be changed because the scheduled date is not a business day.

(iii) That months have different numbers of days.

(iv) The occurrence of leap year.

(4)▶*Disregarded irregularities.*◀ In making calculations and disclosures, the creditor may disregard any irregularity in the first period that falls within the limits described below and any [payment schedule] irregularity ▶in the payment schedule, in a transaction not secured by real property or a dwelling, or payment summary, in a transaction secured by real property or a dwelling,◀ that results from the irregular first period:

(i) For transactions in which the term is less than 1 year, a first period not more than 6 days shorter or 13 days longer than a regular period;

(ii) For transactions in which the term is at least 1 year and less than 10 years, a first period not more than 11 days shorter or 21 days longer than a regular period; and

(iii) For transactions in which the term is at least 10 years, a first period shorter than or not more than 32 days longer than a regular period.

(5)▶*Demand obligations.*◀ If an obligation is payable on demand, the creditor shall make the disclosures based on an assumed maturity of 1 year. If an alternate maturity date is stated in the legal obligation between the parties, the disclosures shall be based on that date.

(6) *Multiple advance loans.* (i)▶*Series of advances.*◀ A series of advances under an agreement to extend credit up to a certain amount may be considered as one transaction.

(ii)▶*Multiple-advance construction loan.*◀ When a multiple-advance loan to finance the construction of a dwelling may be permanently financed by the same creditor, the construction phase and the permanent phase may be treated as either one transaction or more than one transaction.

(d) *Multiple creditors; multiple consumers.* If a transaction involves more than one creditor, only one set of disclosures shall be given and the creditors shall agree among themselves which creditor must comply with the requirements that this regulation imposes on any or all of them. If there is more than one consumer, the disclosures may be made to any consumer who is primarily liable on the obligation. If the transaction is rescindable under § 226.23, however, the disclosures shall be made to each consumer who has the right to rescind.

(e) *Effect of subsequent events.* If a disclosure becomes inaccurate because of an event that occurs after the creditor delivers the required disclosures, the inaccuracy is not a violation of this regulation, although new disclosures may be required under paragraph (f) of this section, § 226.19, or § 226.20.

(f) *Early disclosures.* If disclosures required by this subpart are given before the date of consummation of a transaction and a subsequent event makes them inaccurate, the creditor shall disclose before consummation ([subject to the provisions of]▶except that additional timing requirements apply under◀ § 226.19(a)(2) and ▶alternative timing requirements apply under◀ § 226.19(a)[(5)]▶(4)◀(iii)): [39]

(1) Any changed term unless the term was based on an estimate in accordance with § 226.17(c)(2) and was labelled an estimate;

(2) All changed terms, if the annual percentage rate at the time of consummation varies from the annual percentage rate disclosed earlier by more than ⅛ of 1 percentage point in a regular transaction, or more than ¼ of 1 percentage point in an irregular transaction, as defined in § 226.22(a).

(g) *Mail or telephone orders—delay in disclosures.* ▶Except for transactions secured by real property or a dwelling subject to § 226.38, i◀[I]f a creditor receives a purchase order or a request for an extension of credit by mail, telephone, or facsimile machine without face-to-face or direct telephone solicitation, the creditor may delay the disclosures until the due date of the first payment, if the following information for representative amounts or ranges of credit is made available in written form or in electronic form to the consumer or to the public before the actual purchase order or request:

(1) The cash price or the principal loan amount.

(2) The total sale price.

(3) The finance charge.

(4) The annual percentage rate, and if the rate may increase after consummation, the following disclosures:

(i) The circumstances under which the rate may increase.

(ii) Any limitations on the increase.

(iii) The effect of an increase.

(5) The terms of repayment.

(h) *Series of sales—delay in disclosures.* If a credit sale is one of a series made under an agreement providing that subsequent sales may be added to an outstanding balance, the creditor may delay the required disclosures until the due date of the first payment for the current sale, if the following two conditions are met:

(1) The consumer has approved in writing the annual percentage rate or rates, the range of balances to which they apply, and the method of treating any unearned finance charge on an existing balance.

(2) The creditor retains no security interest in any property after the creditor has received payments equal to the cash price and any finance charge attributable to the sale of that property. For purposes of this provision, in the case of items purchased on different

[39] [Reserved.]

dates, the first purchased is deemed the first item paid for; in the case of items purchased on the same date, the lowest priced is deemed the first item paid for.

(i) *Interim student credit extensions.* For each transaction involving an interim credit extension under a student credit program, the creditor need not make the following disclosures: the finance charge under § 226.18(d), the payment schedule under § 226.18(g), the total of payments under § 226.18(h), or the total sale price under § 226.18(j).

5. Section 226.18 is revised to read as follows:

§ 226.18 General disclosure requirements.

For each transaction, the creditor shall disclose the following information as applicable►, except that for each transaction secured by real property or a dwelling, the creditor shall make the disclosures required by § 226.38◄:

(a) *Creditor.* The identity of the creditor making the disclosures.

(b) *Amount financed.* The amount financed, using that term, and a brief description such as the amount of credit provided to you or on your behalf. The amount financed is calculated by:

(1) Determining the principal loan amount or the cash price (subtracting any downpayment);

(2) Adding any other amounts that are financed by the creditor and are not part of the finance charge; and

(3) Subtracting any prepaid finance charge.

(c) *Itemization of amount financed.* (1) A separate written itemization of the amount financed, including:[40]

(i) The amount of any proceeds distributed directly to the consumer.

(ii) The amount credited to the consumer's account with the creditor.

(iii) Any amounts paid to other persons by the creditor on the consumer's behalf. The creditor shall identify those persons►,◄[.][41] ►except that the following payees may be described using generic or other general terms and need not be further identified: public officials or government agencies, credit reporting agencies, appraisers, and insurance companies.◄

(iv) The prepaid finance charge.

(2) The creditor need not comply with paragraph (c)(1) of this section if the creditor provides a statement that the consumer has the right to receive a written itemization of the amount financed, together with a space for the consumer to indicate whether it is desired, and the consumer does not request it.

(d) *Finance charge.* The *finance charge,* using that term, and a brief description such as ''the dollar amount the credit will cost you.''

[(1) *Mortgage loans.* In a transaction secured by real property or a dwelling, the disclosed finance charge and other disclosures affected by the disclosed finance charge (including the amount financed and the annual percentage rate) shall be treated as accurate if the amount disclosed as the finance charge—

(i) Is understated by no more than $100; or

(ii) Is greater than the amount required to be disclosed.

(2) *Other credit.* In any other transaction, the]►The◄ amount disclosed as the finance charge shall be treated as accurate if[,]►:

(1)◄In a transaction involving an amount financed of $1,000 or less, it is not more than $5 above or below the amount required to be disclosed; or[,]

►(2)◄ In a transaction involving an amount financed of more than $1,000, it is not more than $10 above or below the amount required to be disclosed.

(e) *Annual percentage rate.* The *annual percentage rate,* using that term, and a brief description such as ''the cost of your credit as a yearly rate.''[42] ►For any transaction involving a finance charge of $5 or less on an amount financed of $75 or less, or a finance charge of $7.50 or less on an amount financed of more than $75, the creditor need not disclose the annual percentage rate.◄

(f) *Variable-rate loan* [*with term of one year or less*]►*not secured by real property or a dwelling*◄.

[(1)] If the annual percentage rate may increase after consummation in a transaction not secured by [the consumer's principal dwelling or a transaction secured by the consumer's principal dwelling with a term of one year or less]►real property or a dwelling◄, the following disclosures:[43]

[(i)]►(1)◄ The circumstances under which the interest rate may increase.

[(ii)]►(2)◄ Any limitations on the increase.

[(iii)]►(3)◄ The effect of an increase.

[(iv)]►(4)◄ An example of the payment terms that would result from an increase.

[(2) If the annual percentage rate may increase after consummation in a transaction secured by the consumer's principal dwelling with a term greater than one year, a following disclosures:

(i) The fact that the transaction contains a variable-rate feature.

(ii) A statement that variable-rate disclosure have been provided earlier.]

(g) *Payment schedule.* The number, amounts, and timing of payments scheduled to repay the obligation.

(1) In a demand obligation with no alternate maturity date, the creditor may comply with this paragraph by disclosing the due dates or payment periods of any scheduled interest payments for the first year.

(2) In a transaction in which a series of payments varies because a finance charge is applied to the unpaid principal balance, the creditor may comply with this paragraph by disclosing the following information:

(i) The dollar amounts of the largest and smallest payments in the series.

(ii) A reference to the variations in the other payments in the series.

(h) *Total of payments.* The ''total of payments,'' using that term, and a descriptive explanation such as ''the amount you will have paid when you have made all scheduled payments.''[44] ►In any transaction involving a single payment, the creditor need not disclose the total of payments.◄

(i) *Demand feature.* If the obligation has a demand feature, that fact shall be disclosed. When the disclosures are based on an assumed maturity of 1 year as provided in § 226.17(c)(5), that fact shall also be disclosed.

(j) *Total sale price.* In a credit sale, the total sale price, using that term, and a descriptive explanation (including the amount of any downpayment) such as ''the total price of your purchase on credit, including your downpayment of $______.'' The total sale price is the sum of the cash price, the items described in paragraph (b)(2), and the finance charge disclosed under paragraph (d) of this section.

(k) *Prepayment.* (1) When an obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance, a statement indicating whether or not a penalty may

[40] ►[Reserved]◄[Good faith estimates of settlement costs provided for transactions subject to the Real Estate Settlement Procedures Act (12 U.S.C. 2601 *et seq.*) may be substituted for the disclosures required by paragraph (c) of this section.]

[41] ►[Reserved]◄[The following payees may be described using generic or other general terms and need not be further identified: public officials or government agencies, credit reporting agencies, appraisers, and insurance companies.]

[42] ►[Reserved]◄ [For any transaction involving a finance charge of $5 or less on an amount financed of $75 or less, or a finance charge of $7.50 or less on an amount financed of more than $75, the creditor need not disclose the annual percentage rate.]

[43] ►[Reserved]◄[Information provided in accordance with Sections 226.18(f)(2) and 226.19(b), may be substituted for the disclosures required by paragraph (f)(1) of this section.]

[44] ►[Reserved]◄ [In any transaction involving a single payment, the creditor need not disclose the total of payments.]

be imposed if the obligation is prepaid in full.

(2) When an obligation includes a finance charge other than the finance charge described in paragraph (k)(1) of this section, a statement indicating whether or not the consumer is entitled to a rebate of any finance charge if the obligation is prepaid in full.

(l) *Late payment.* Any dollar or percentage charge that may be imposed before maturity due to a late payment, other than a deferral or extension charge.

(m) *Security interest.* The fact that the creditor has or will acquire a security interest in the property purchased as part of the transaction, or in other property identified by item or type.

(n) *Insurance*►,◄ *[and] debt cancellation* ►*, and debt suspension*◄*.* The items required by § 226.4(d) in order to exclude certain insurance premiums►,◄ and debt-cancellation ►or debt suspension◄ fees from the finance charge.

(o) *Certain security interest charges.* The disclosures required by § 226.4(e) in order to exclude from the finance charge certain fees prescribed by law or certain premiums for insurance in lieu of perfecting a security interest.

(p) *Contract reference.* A statement that the consumer should refer to the appropriate contract document for information about nonpayment, default, the right to accelerate the maturity of the obligation, and prepayment rebates and penalties. At the creditor's option, the statement may also include a reference to the contract for further information about security interests and, in a residential mortgage transaction, about the creditor's policy regarding assumption of the obligation.

(q) [*Assumption policy.* In a residential mortgage transaction, a statement whether or not a subsequent purchaser of the dwelling from the consumer may be permitted to assume the remaining obligation on its original terms.] ►[Reserved.]◄

(r) *Required deposit.* If the creditor requires the consumer to maintain a deposit as a condition of the specific transaction, a statement that the annual percentage rate does not reflect the effect of the required deposit.[45] ►A required deposit need not include:

(1) An escrow account for items such as taxes, insurance or repairs; or

(2) A deposit that earns not less than 5 percent per year.◄

[45] ►[Reserved]◄ [A required deposit need not include, for example: (1) An escrow account for items such as taxes, insurance or repairs; (2) a deposit that earns not less than 5 percent per year; or (3) payments under a Morris Plan.]

6. Section 226.19 is revised to read as follows:

§ 226.19 [Certain mortgage and variable-rate transactions.]►Early disclosures and adjustable-rate disclosures for transactions secured by real property or a dwelling.

In connection with a closed-end transaction secured by real property or a dwelling, subject to paragraph (a)(4) of this section, the following requirements shall apply:◄

(a) *Mortgage transactions* [*subject to RESPA*]*—(1)(i) Time of* ►*good faith estimates of*◄ *disclosures.* [In a mortgage transaction subject to the Real Estate Settlement Procedures Act (12 U.S.C. 2601 *et seq.*) that is secured by the consumer's dwelling, other than a home equity line of credit subject to § 226.5b or mortgage transaction subject to paragraph (a)(5) of this section, t]►T◄he creditor shall make good faith estimates of the disclosures required by [§ 226.18]►§ 226.38◄ and shall deliver or place them in the mail not later than the third business day after the creditor receives the consumer's written application.

(ii) *Imposition of fees.* Except as provided in paragraph (a)(1)(iii) of this section, neither a creditor nor any other person may impose a fee on a consumer in connection with the consumer's application for a mortgage transaction subject to paragraph (a)(1)(i) of this section before the consumer has received the disclosures required by paragraph (a)(1)(i) of this section. If the disclosures are mailed to the consumer ►or delivered to the consumer by means other than delivery in person◄, the consumer is considered to have received them three business days after they are mailed ►or delivered◄.

(iii) *Exception to fee restriction.* A creditor or other person may impose a fee for obtaining the consumer's credit history before the consumer has received the disclosures required by paragraph (a)(1)(i) of this section, provided the fee is *bona fide* and reasonable in amount.

[(2) *Waiting periods for early disclosures and corrected disclosures.* (i)]►(2)(i) *Seven-business-day waiting period.*◄ The creditor shall deliver or place in the mail the good faith estimates required by paragraph (a)(1)(i) of this section not later than the seventh business day before consummation of the transaction.

►(ii) *Three-business-day waiting period.* After providing the disclosures required by paragraph (a)(1)(i) of this section, the creditor shall provide the disclosures required by § 226.38 before consummation. The consumer must receive the new disclosures no later than three business days before consummation. Only the disclosures required by §§ 226.38(c)(3)(i)(C), 226.38(c)(3)(ii)(C), 226.38(c)(6)(i) and 226.38(e)(5)(i) may be estimated disclosures.◄

Alternative 1—Paragraph (a)(2)(iii)

[(ii) If the annual percentage rate disclosed under paragraph (a)(1)(i) of this section becomes inaccurate, as defined in § 226.22, the creditor shall provide corrected disclosures with all changed terms.]►(iii) *Additional three-business-day waiting period.* If a subsequent event makes the disclosures required by paragraph (a)(2)(ii) inaccurate, the creditor shall provide corrected disclosures, subject to paragraph (a)(2)(iv) of this section.◄ The consumer must receive the corrected disclosures no later than three business days before consummation. ►Only the disclosures required by §§ 226.38(c)(3)(i)(C), 226.38(c)(3)(ii)(C), 226.38(c)(6)(i) and 226.38(e)(5)(i) may be estimated disclosures.◄ [If the corrected disclosures are mailed to the consumer or delivered to the consumer by means other than delivery in person, the consumer is deemed to have received the corrected disclosures three business days after they are mailed or delivered.]

Alternative 2—Paragraph (a)(2)(iii)

[(ii)]►(iii) *Additional three-business-day waiting period.*◄ If the annual percentage rate disclosed under paragraph [(a)(1)(i)]►(a)(2)(ii)◄ of this section becomes inaccurate, as defined in § 226.22, ►or a transaction that was disclosed as a fixed-rate transaction becomes an adjustable-rate transaction,◄ the creditor shall provide corrected disclosures with all changed terms►, subject to paragraph (a)(2)(iv) of this section◄. The consumer must receive the corrected disclosures no later than three business days before consummation. ►Only the disclosures required by §§ 226.38(c)(3)(i)(C), 226.38(c)(3)(ii)(C), 226.38(c)(6)(i) and 226.38(e)(5)(i) may be estimated disclosures.◄ [If the corrected disclosures are mailed to the consumer or delivered to the consumer by means other than delivery in person, the consumer is deemed to have received the corrected disclosures three business days after they are mailed or delivered.]

►(iv) *Annual percentage rate accuracy.* An annual percentage rate disclosed under paragraph (a)(2)(ii) or (a)(2)(iii) shall be considered accurate as provided by § 226.22, except that even if one of the following subsequent events makes the disclosed annual percentage rate inaccurate under

§ 226.22, the APR shall be considered accurate for purposes of paragraph (a)(2)(ii) and (a)(2)(iii) of this section:

(A) A decrease in the loan's annual percentage rate due to a discount the creditor gives the consumer to induce periodic payments by automated debit from a consumer's deposit or other account.

(B) A decrease in the loan's annual percentage rate due to a discount a title insurer gives the consumer on voluntary owners' title insurance.

(v) *Timing of receipt.* If the disclosures required by paragraph (a)(2)(ii) or paragraph (a)(2)(iii) of this section are mailed to the consumer or delivered by means other than delivery in person, the consumer is considered to have received the disclosures three business days after they are mailed or delivered.◄

(3) *Consumer's waiver of waiting period before consummation.* If the consumer determines that the extension of credit is needed to meet a *bona fide* personal financial emergency, the consumer may modify or waive the seven-business-day waiting period or [the]►a◄ three-business-day waiting period required by paragraph (a)(2) of this section, after receiving the disclosures required by [§ 226.18]►§ 226.38◄. To modify or waive a waiting period, the consumer shall give the creditor a dated written statement that describes the emergency, specifically modifies or waives the waiting period, and bears the signature of all the consumers who are primarily liable on the legal obligation. Printed forms for this purpose are prohibited.

[(4) *Notice.* Disclosures made pursuant to paragraph (a)(1) or paragraph (a)(2) of this section shall contain the following statement: ''You are not required to complete this agreement merely because you have received these disclosures or signed a loan application.'' The disclosure required by this paragraph shall be grouped together with the disclosures required by paragraph (a)(1) or (a)(2) of this section.]

[(5)]►(4)◄ *Timeshare plans.* In a mortgage transaction [subject to the Real Estate Settlement Procedures Act (12 U.S.C. 2601 *et seq.*)] that is secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53(D)):

(i) The requirements of paragraphs (a)(1) through [(a)(4)]►(a)(3)◄ of this section do not apply;

(ii) The creditor shall make good faith estimates of the disclosures required by [§ 226.18] ►§ 226.38◄ before consummation, or shall deliver or place them in the mail not later than three business days after the creditor receives the consumer's written application, whichever is earlier; and

(iii) If the annual percentage rate at the time of consummation varies from the annual percentage rate disclosed under paragraph (a)[(5)]►(4)◄(ii) of this section by more than ⅛ of 1 percentage point in a regular transaction or ¼ of 1 percentage point in an irregular transaction, the creditor shall disclose all the changed terms no later than consummation or settlement.

[(b) *Certain variable-rate transactions.*[45a] If the annual percentage rate may increase after consummation in a transaction secured by the consumer's principal dwelling with a term greater than one year, the following disclosures must be provided at the time an application form is provided or before the consumer pays a non-refundable fee, whichever is earlier:[45b]

(1) The booklet titled *Consumer Handbook on Adjustable Rate Mortgages* published by the Board and the Federal Home Loan Bank Board, or a suitable substitute.

(2) A loan program disclosure for each variable-rate program in which the consumer expresses an interest. The following disclosures, as applicable, shall be provided:

(i) The fact that the interest rate, payment, or term of the loan can change.

(ii) The index or formula used in making adjustments, and a source of information about the index or formula.

(iii) An explanation of how the interest rate and payment will be determined, including an explanation of how the index is adjusted, such as by the addition of a margin.

(iv) A statement that the consumer should ask about the current margin value and current interest rate.

(vii) Any rules relating to changes in the index, interest rate, payment amount, and outstanding loan balance including, for example, an explanation of interest rate or payment limitations, negative amortization, and interest rate carryover.

(viii) At the option of the creditor, either of the following:

(A) A historical example, based on a $10,000 loan amount, illustrating how payments and the loan balance would have been affected by interest rate changes implemented according to the terms of the loan program disclosure. The example shall reflect the most recent 15 years of index values. The example shall reflect all significant loan program terms, such as negative amortization, interest rate carryover, interest rate discounts, and interest rate and payment limitations, that would have been affected by the index movement during the period.

(B) The maximum interest rate and payment for a $10,000 loan originated at the initial interest rate (index value plus margin, adjusted by the amount of any discount or premium) in effect as of an identified month and year for the loan program disclosure assuming the maximum periodic increases in rates and payments under the program; and the initial interest rate and payment for that loan and a statement that the periodic payment may increase or decrease substantially depending on changes in the rate.

(ix) An explanation of how the consumer may calculate the payments for the loan amount to be borrowed based on either:

(A) The most recent payment shown in the historical example in paragraph (b)(2)(viii)(A) of this section; or

(B) The initial interest rate used to calculate the maximum interest rate and payment in paragraph (b)(2)(viii)(B) of this section.

(x) The fact that the loan program contains a demand feature.

(xi) The type of information that will be provided in notices of adjustments and the timing of such notices.

(xii) A statement that disclosure forms are available for the creditor's other variable-rate loan programs.]

►(b) *Adjustable-rate loan program disclosures.* For adjustable-rate mortgages described in § 226.38(a)(3) secured by real property or a consumer's dwelling, the creditor shall provide to the consumer an adjustable-rate loan program disclosure for each loan program in which the consumer expresses an interest. The creditor shall disclose the heading ''Adjustable-Rate Mortgage'' or ''ARM'' in accordance with § 226.19(b)(4)(iii). The creditor shall provide disclosures under this paragraph (b) in circumstances where an open-end credit account converts to a closed-end mortgage transaction under a written agreement with the consumer. The creditor need not provide such disclosures in circumstances where the consumer assumes an adjustable-rate mortgage originated to another consumer.

(1) *Interest rate and payment.* As applicable, the creditor shall disclose the information required in paragraph

[45a] ►Reserved.◄[Information provided in accordance with variable-rate regulations of other Federal agencies may be substituted for the disclosures required by paragraph (b) of this section.]

[45b] ►Reserved.◄[Disclosures may be delivered or placed in the mail not later than three business days following receipt of a consumer's application when the application reaches the creditor by telephone, or through an intermediary agent or broker.]

(b)(1) of this section, grouped together under the heading ''Interest Rate and Payment,'' using that term:

(i) *Introductory period.* The time period for which the interest rate or payment remains fixed, a statement that the interest rate or payment may increase after that period, and an explanation of the effect on the interest rate of having an initial interest rate that is not determined using the index or formula that applies for interest rate adjustments.

(ii) *Frequency of rate and payment change.* The frequency of interest rate and payment changes permitted under the legal obligation.

(iii) *Index.* The index or formula used in making adjustments, a source of information about the index or formula, and an explanation of how the interest rate will be determined ►when adjusted◄, including an explanation of how the index is adjusted, such as by the addition of a margin.

(iv) *Limit on rate changes.* An explanation of interest rate or payment limitations and interest rate carryover.

(v) *Conversion feature.* An explanation of any fixed-rate conversion feature that describes any limitations on the period during which the loan may be converted, a statement that the fixed interest rate may be higher than the adjustable rate at the time of conversion, a statement that conversion fees may be charged, and any interest rate and payment limitations that apply if the consumer exercises the conversion option.

(vi) *Preferred rate.* An explanation of the events that will cause the interest rate on an adjustable rate mortgage with a preferred rate to increase, a statement of the increase in the interest rate, and a statement that fees may be charged if one or more of the events occurs.

(2) *Key questions about risk.* The creditor shall disclose the information required in paragraphs (b)(2)(i) and (b)(2)(ii) of this section, grouped together under the heading ''Key Questions About Risk,'' using that term:

(i) *Required disclosures.* The creditor shall disclose the following information—

(A) *Rate increases.* A statement that the interest rate may increase, along with a statement indicating when the first interest rate increase may occur and the frequency with which the interest rate may increase.

(B) *Payment increases.* A statement indicating whether or not the periodic payment on the loan may increase. If the periodic payment may increase, a statement that if the interest rate increases, the periodic payment will increase. For a pay option loan, if the periodic payment may increase, a statement indicating when the first minimum payment may increase.

(C) *Prepayment penalty.* If the obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance, a statement indicating whether or not a penalty could be imposed if the obligation is prepaid in full. If the creditor could impose a prepayment penalty, a statement of the circumstances under which and period in which the creditor could impose the penalty.

(ii) *Additional disclosures.* The creditor shall disclose the following information as applicable:

(A) *Interest-only payments.* A statement that periodic payments will be applied only toward interest on the loan, along with a statement of any limitation on the number of periodic payments that will be applied only toward interest on the loan, that such payments will cover the interest owed each month, but none of the principal, and that making these periodic payments means the loan amount will stay the same and the consumer will not have paid any of the loan amount. For payment-option loans, a statement that the loan gives the consumer the choice to make periodic payments that cover the interest owed each month, but none of the principal, and that making these periodic payments means the loan amount will stay the same and the consumer will not have paid any of the loan amount.

(B) *Negative amortization.* A statement that the loan balance may increase even if the consumer makes the periodic payments, along with a statement that the minimum payment covers only a part of the interest the consumer owes each period and none of the principal, that the unpaid interest will be added to the consumer's loan amount, and that over time this will increase the total amount the consumer is borrowing and cause the consumer to lose equity in the home.

(C) *Balloon payment.* A statement that the consumer will owe a balloon payment, along with a statement of when it will be due.

(D) *Demand feature.* A statement that the creditor may demand full repayment of the loan, along with a statement of the timing of any advance notice the creditor will give the consumer before the creditor exercises such right.

(E) *No-documentation or low-documentation loans.* A statement that the consumer's loan could have a higher rate or fees if the consumer does not document employment, income or other assets, along with a statement that if the consumer provides more documentation, the consumer could decrease the interest rate or fees.

(F) *Shared-equity or shared-appreciation.* A statement that any future equity or appreciation in the real property or dwelling that secures the loan must be shared, along with a statement of the percentage of future equity or appreciation to which the creditor is entitled, and the events that may trigger such an obligation.

(3) *Additional information and Web site.* The creditor shall disclose a statement that the consumer may obtain additional information about adjustable-rate mortgages and a list of licensed housing counselors at the Web site of the Federal Reserve Board, and a reference to that Web site.

(4) *Format requirements.* (i) *Application of § 226.37.* Except as otherwise provided by this paragraph (b)(4), the format requirements in § 226.37 apply to loan program disclosures made under this section.

(ii) *Prominent location.* The disclosures required by paragraphs (b)(1) through (b)(3) of this section shall be grouped together and placed in a prominent location.

(iii) *Disclosure of heading.* The disclosure of the heading required by paragraph (b) of this section shall be more conspicuous than, and shall precede, the other disclosures required by paragraph (b) and shall be located outside of the tables required by paragraph (b)(4)(iv). The creditor may make the heading disclosure using the name of the creditor and the name of the loan program.

(iv) *Form of disclosures; tabular format.* The creditor shall provide the disclosures required by paragraphs (b)(1) and (b)(2) of this section in the form of two tables with headings, content, and format substantially similar to Form H–4(B) in Appendix H to this part. The table shall contain only the information required or permitted by paragraphs (b)(1) and (b)(2). The table containing the disclosures required by paragraph (b)(1) shall precede the table containing the disclosures required by paragraph (b)(2).

(v) *Question and answer format.* The creditor shall provide the disclosures required by paragraph (b)(2) of this section grouped together and presented in the format of question and answer, in a manner substantially similar to Form H–4(B) in Appendix H to this part.

(vi) *Highlighting.* Each affirmative answer for a feature required to be disclosed under paragraph (b)(2) shall be disclosed in bold text and in all capitalized letters. Any negative answer shall be in nonbold text.

(vii) *Order of key questions disclosure.* The key questions disclosure shall be provided, as applicable, in the following order: rate increases under § 226.19(b)(2)(i)(A), payment increases under § 226.19(b)(2)(i)(B), interest-only payments under § 226.19(b)(2)(ii)(A), negative amortization under § 226.19(b)(2)(ii)(B), balloon payment under § 226.19(b)(2)(ii)(C), prepayment penalty under § 226.19(b)(2)(i)(C), demand feature under § 226.19(b)(2)(ii)(D), no-documentation or low-documentation loans under § 226.19(b)(2)(ii)(E), shared-equity or shared-appreciation under § 226.19(b)(2)(ii)(F).

(viii) *Disclosure of additional information and Web site.* The disclosure and Web site information required by paragraph (b)(3) of this section shall be located outside and beneath the tables required by paragraph (b)(4)(iv).

(c) *Publications for transactions secured by real property or a dwelling.* In a closed-end consumer credit transaction secured by real property or a dwelling, the creditor shall provide the following Board publications:

(1) The publication entitled ''*Key Questions to Ask about Your Mortgage,''* as published by the Board.

(2) The publication entitled ''*Fixed vs. Adjustable Rate Mortgages,''* as published by the Board.

(d) *Timing of disclosures.* (1) *General.* Except as otherwise provided by this paragraph (d), the creditor shall provide the disclosures and publications required by paragraphs (b) and (c) of this section at the time an application form is provided to the consumer or before the consumer pays a non-refundable fee, including a fee for obtaining the consumer's credit history, whichever is earlier.◄

[(c)]►(2)◄ *Electronic disclosures.* For an application that is accessed by the consumer in electronic form, the disclosures and publications required by paragraph (b) ►and (c)◄ of this section may be provided to the consumer in electronic form on or with the application.

►(i) Except as provided in paragraph (d)(2)(ii), if a consumer accesses an ARM loan application electronically, the creditor shall provide the disclosures and publications required under paragraphs (b) and (c) of this section in electronic form.

(ii) If a consumer who is physically present in the creditor's office accesses a loan application electronically, the creditor may provide disclosures and publications required under paragraphs (b) and (c) of this section in either electronic or paper form.

(3) *Applications made by telephone or through intermediary.* If the creditor receives the consumer's application through an intermediary agent or broker or by telephone, the creditor satisfies the requirements of paragraph (b) or paragraph (c) of this section if the creditor delivers the disclosures and publications or places them in the mail not later than three business days after the creditor receives the consumer's application.

(4) *Adjustable-rate feature added after application.* If the consumer first expresses interest in an adjustable-rate mortgage transaction after an application form has been provided or accessed or the consumer has paid a non-refundable fee, the creditor shall provide to the consumer the disclosures required by paragraph (b) of this section within three business days after the creditor is informed of such interest by the consumer or by an intermediary broker or agent.

(5) *Terms not usually offered.* If the consumer expresses an interest in negotiating loan terms that are not generally offered, the creditor need not provide the disclosures required by paragraph (b) of this section before an application form is provided but shall provide such disclosures as soon as reasonably possible after the terms to be disclosed have been determined and not later than the time the consumer pays a non-refundable fee. In all cases the creditor shall provide the disclosures required by paragraph (c) of this section at the time an application form is provided or before the consumer pays a non-refundable fee, including a fee for obtaining a consumer's credit history, whichever is earlier.

(6) *Additional loan program disclosures.* If, after an application form is provided or the consumer pays a non-refundable fee, a consumer expresses an interest in an adjustable-mortgage loan program for which the creditor has not provided the disclosures required by paragraph (b) of this section, the creditor shall provide such disclosures within a reasonable time after the consumer expresses such interest. ◄

7. Section 226.20 is revised to read as follows:

§ 226.20 Subsequent disclosure requirements.

(a) *Refinancings.* A refinancing occurs when an existing obligation that was subject to this subpart is satisfied and replaced by a new obligation undertaken by the same consumer. A refinancing is a new transaction requiring new disclosures to the consumer. The new finance charge shall include any unearned portion of the old finance charge that is not credited to the existing obligation. The following shall not be treated as a refinancing:

(1) A renewal of a single payment obligation with no change in the original terms.

(2) A reduction in the annual percentage rate with a corresponding change in the payment schedule.

(3) An agreement involving a court proceeding.

(4) A change in the payment schedule or a change in collateral requirements as a result of the consumer's default or delinquency, unless the rate is increased, or the new amount financed exceeds the unpaid balance plus earned finance charge and premiums for continuation of insurance of the types described in § 226.4(d).

(5) The renewal of optional insurance purchased by the consumer and added to an existing transaction, if disclosures relating to the initial purchase were provided as required by this subpart.

(b) *Assumptions.* An assumption occurs when a creditor expressly agrees in writing with a subsequent consumer to accept that consumer as a primary obligor on an existing [residential mortgage transaction]►closed-end credit transaction secured by real property or a dwelling◄. Before the assumption occurs, the creditor shall make new disclosures to the subsequent consumer, based on the remaining obligation. If the finance charge originally imposed on the existing obligation was an add-on or discount finance charge, the creditor need only disclose:

(1) The unpaid balance of the obligation assumed.

(2) The total charges imposed by the creditor in connection with the assumption.

(3) The information required to be disclosed under [§ 226.18(k), (l), (m), and (n)] ►§ 226.38 (a)(5), (f)(2), (h), (j)(2), (j)(3), and (j)(4)◄.

(4) The annual percentage rate originally imposed on the obligation.

(5) The [payment schedule under § 226.18(g)] ►interest rate and payment summary under § 226.38(c)◄ and the total [of] payments under [§ 226.18(h)], ►§ 226.38(e)(5)◄ based on the remaining obligation.

(c) [*Variable-rate adjustments.]* ►*Rate adjustments.*◄[45c] An adjustment to the interest rate with or without a corresponding adjustment to the payment in [a variable-rate]►an adjustable-rate◄ mortgage subject to

[45c] ►Reserved.◄[Information provided in accordance with variable-rate subsequent disclosure regulations of other Federal agencies may be substituted for the disclosure required by paragraph (c) of this section.]

§ 226.19(b) is an event requiring new disclosures to the consumer. ►An adjustment to the interest rate with a corresponding adjustment to the payment due to the conversion of an adjustable-rate mortgage subject to § 226.19(b) to a fixed-rate mortgage also is an event requiring new disclosures to the consumer.◄[At least once each year during which an interest rate adjustment is implemented without an accompanying payment change, and at least 25, but no more than 120, calendar days before a payment at a new level is due, the following disclosures, as applicable, must be delivered or placed in the mail:

(1) The current and prior interest rates.

(2) The index values upon which the current and prior interest rates are based.

(3) The extent to which the creditor has foregone any increase in the interest rate.

(4) The contractual effects of the adjustment, including the payment due after the adjustment is made, and a statement of the loan balance.

(5) The payment, if different from that referred to in paragraph (c)(4) of this section, that would be required to fully amortize the loan at the new interest rate over the remainder of the loan term.]

►(1) *Timing of disclosures.* (i) *Payment change.* If an interest rate adjustment is accompanied by a payment change, the creditor shall deliver or place in the mail the disclosures required by paragraph (c)(2) of this section at least 60, but no more than 120, calendar days before a payment at a new level is due.

(ii) *No payment change.* At least once each year during which an interest rate adjustment is implemented without an accompanying payment change, the creditor shall deliver or place in the mail the disclosures required by paragraph (c)(3) of this section.

(2) *Content of payment change disclosures.* The creditor must provide the following information on the notice provided pursuant to paragraph (c)(1)(i) of this section:

(i) A statement that changes are being made to the interest rate, the date such change is effective, and a statement that more detailed information is available in the loan agreement(s).

(ii) A table containing the following disclosures—

(A) The current and new interest rates.

(B) If payments on the loan may be interest-only or negatively amortizing, the amount of the current and new payment allocated to pay principal, interest, and taxes and insurance in escrow, as applicable. The current payment allocation disclosed shall be based on the payment allocation in the last payment period during which the current interest rate applies. The new payment allocation disclosed shall be based on the payment allocation in the first payment period during which the new interest rate applies.

(C) The current and new payment and the due date for the new payment.

(iii) A description of the change in the index or formula and any application of previously foregone interest.

(iv) The extent to which the creditor has foregone any increase in the interest rate and the earliest date the creditor may apply foregone interest to future adjustments, subject to rate caps.

(v) Limits on interest rate or payment increases at each adjustment, if any, and the maximum interest rate or payment over the life of the loan.

(vi) A statement of whether or not part of the new payment will be allocated to pay the loan principal and a statement of the payment required to fully amortize the loan at the new interest rate over the remainder of the loan term or to fully amortize the loan without extending the loan term, if different from the new payment disclosed pursuant to paragraph (c)(2)(ii)(C) of this section.

(vii) A statement of the loan balance as of the date the interest rate change will become effective.

(3) *Content of annual interest rate notice.* The creditor shall provide the following information on the annual notice provided pursuant to paragraph (c)(1)(ii) of this section, as applicable:

(i) The specific time period covered by the disclosure, and a statement that the interest rate on the loan has changed during the past year without changing required payments.

(ii) The highest and lowest interest rates that applied during the period specified under paragraph (c)(3)(i) of this section.

(iii) Any foregone increase in the interest rate or application of previously foregone interest.

(iv) The maximum interest rate that may apply over the life of the loan.

(v) A statement of the loan balance as of the last day of the time period required to be disclosed by paragraph (c)(3)(i) of this section.

(4) *Additional information.* In addition to the disclosures provided under paragraph (c)(2) or (c)(3) of this section, the creditor shall provide the following information:

(i) If the creditor may impose a penalty if the obligation is prepaid in full, a statement of the circumstances under which and period in which the creditor may impose the penalty and the amount of the maximum penalty possible during the period between the date the creditor delivers or mails the disclosures required by this paragraph (c) and the last day the creditor may impose the penalty.

(ii) A telephone number the consumer may call to obtain additional information about the consumer's loan.

(iii) A telephone number and Internet Web site for housing counseling resources maintained by the Department of Housing and Urban Development.

(5) *Format of disclosures.* (i) The disclosures required by this paragraph (c) shall be provided in the form of tables with headings, content and format substantially similar to Form H−4(G) in Appendix H to this part, where an interest rate adjustment is accompanied by a payment change, or Form H−4(K) in Appendix H to this part, where a creditor provides an annual notice of interest rate adjustments without an accompanying payment change. The disclosures required by paragraph (c)(2) or (c)(3) of this section shall be grouped together with the disclosures required by paragraph (c)(4) of this section, and shall be in a prominent location.

(ii) The disclosures required by paragraph (c)(2)(i) or paragraph (c)(3)(i) of this section shall precede the other disclosures required by paragraph (c)(2) or (c)(3). The disclosures required by paragraph (c)(4) shall be located directly beneath the disclosures required by paragraph (c)(2) or (c)(3).

(iii) The disclosures required by paragraph (c)(2)(ii) shall be in the form of a table with headings, content, and format substantially similar to Form H–4(G) in Appendix H to this part. The disclosures required by paragraphs (c)(2)(iii) through (c)(2)(vii) of this section shall be located directly below the table required by paragraph (c)(2)(ii).

(d) *Periodic statement.* (1) *Timing and content of disclosures.* If a mortgage transaction secured by real property or a dwelling provides a consumer with multiple payment options that include a payment that results in negative amortization, for each period after consummation and not later than fifteen days before payment is due, subject to paragraph (c) of this section, the creditor shall mail or deliver to the consumer a periodic statement that discloses the following information, *as applicable:*

(i) *Payment.* Based on the interest rate in effect at the time the disclosure is made, the payment amount required to—

(A) Pay off the loan balance in full by the end of the term through regular periodic payments without a balloon payment, with a statement that the payment is ''recommended to reduce loan balance,'' using that term;

(B) Prevent negative amortization, if the legal obligation explicitly permits the consumer to elect to pay interest only without paying principal; and

(C) Pay the minimum amount required under the legal obligation.

(ii) *Effects.* A statement of the interest and principal, if any, covered by the payment amounts disclosed under paragraph (d)(1)(i) of this section, a statement describing the effects of making such payments, and the earliest date payments at a higher level may be due.

(iii) *Unpaid interest.* The amount that will be added to the loan balance each period due to unpaid interest.

(2) *Format of disclosures.* (i) *Form of a table.* The disclosures required by paragraph (d)(1) of this section shall be in the form of a table with headings, content and format substantially similar to Form H–4(L) in Appendix H to this part.

(ii) *Location of disclosures.* The disclosures required by this paragraph (d) shall be placed in a prominent location, except that if the disclosures are made concurrently with the disclosures required by paragraph (c) of this section, the disclosures required by paragraph (c) shall precede the disclosures required by this paragraph (d).

(iii) *Segregation of disclosures.* The table described in paragraph (d)(2)(i) of this section shall contain only the information required by paragraph (d)(1). Other information may be presented with the table, provided such information appears outside the required table.

(e) *Creditor-placed property insurance.* (1) ''Creditor-placed property insurance'' means property insurance coverage obtained by the creditor when the property insurance required by the credit agreement has lapsed.

(2) A creditor may not charge a consumer for obtaining property insurance on property securing a credit transaction, unless:

(i) The creditor has made a reasonable determination that the required property insurance has lapsed;

(ii) The creditor has mailed or delivered a written notice to the consumer with the disclosures set forth in paragraph (e)(3) of this section at least 45 days before a charge is imposed on the consumer for creditor-placed property insurance; and

(iii) During the 45-day notice period, the consumer has not provided the creditor with evidence of adequate property insurance.

(3) The creditor must provide the following information, clearly and conspicuously, on the notice required in paragraph (e)(2)(ii) of this section:

(i) The creditor's name and contact information, the loan number, and the address or description of the property securing the credit transaction;

(ii) That the consumer is obligated to maintain property insurance on the property securing the credit transaction;

(iii) That the required property insurance has lapsed;

(iv) That the creditor is authorized to obtain the property insurance on the consumer's behalf;

(v) The date the creditor can charge the consumer for the cost of creditor-placed property insurance;

(vi) How the consumer may provide evidence of property insurance;

(vii) The cost of creditor-placed property insurance stated as an annual premium, and that this premium is likely significantly higher than a premium for property insurance purchased by the consumer; and

(viii) That creditor-placed property insurance may not provide as much coverage as homeowner's insurance.

(4) Within 15 days after a creditor charges the consumer for creditor-placed property insurance, the creditor must mail or deliver to the consumer a copy of the individual policy, certificate or other evidence of the creditor-placed property insurance.◄

Subpart E—Special Rules for Certain Home Mortgage Transactions

8. Section 226.32 is amended by revising paragraphs (b)(1), (c)(1), and (c)(5), to read as follows:

§ 226.32 Requirements for certain closed-end home mortgages.

* * * * *

(b) * * *

(1) For purposes of paragraph (a)(1)(ii) of this section, *points and fees* means ►all items included in the finance charge, pursuant to § 226.4, except interest or the time-price differential.◄ [:]

(i) All items required to be disclosed under § 226.4(a) and 226.4(b), except interest or the time-price differential;

(ii) All compensation paid to mortgage brokers;

(iii) All items listed in § 226.4(c)(7) (other than amounts held for future payment of taxes) unless the charge is reasonable, the creditor receives no direct or indirect compensation in connection with the charge, and the charge is not paid to an affiliate of the creditor; and

(iv) Premiums or other charges for credit life, accident, health, or loss-of-income insurance, or debt-cancellation coverage (whether or not the debt-cancellation coverage is insurance under applicable law) that provides for cancellation of all or part of the consumer's liability in the event of the loss of life, health, or income or in the case of accident, written in connection with the credit transaction.]

* * * * *

(c) * * *

(1) *Notices.* The following statement ►in bold text and minimum 10-point font◄: [''You are not required to complete this agreement merely because you have received these disclosures or have signed a loan application. If you obtain this loan, the lender will have a mortgage on your home. You could lose your home, and any money you have put into it, if you do not meet your obligations under the loan.'']►''If you are unable to make the payments on this loan, you could lose your home. You have no obligation to accept this loan. Your signature below only confirms that you have received this form.''◄

* * * * *

(5) *Amount borrowed.* For a mortgage refinancing, the total amount the consumer will borrow, as reflected by the [face] amount of the note ►or other loan agreement◄; and where the amount borrowed includes premiums or other charges for optional credit insurance or debt-cancellation ►or debt suspension◄ coverage, that fact shall be stated, grouped together with the disclosure of the amount borrowed. The disclosure of the amount borrowed shall be treated as accurate if it is not more than $100 above or below the amount required to be disclosed.

* * * * *

9. Section 226.36, as added on July 30, 2008 (73 FR 44604), is amended by:

A. Revising the section heading,

B. Revising paragraph (a),

C. Revising paragraphs (b)(1) introductory text, (b)(1)(i)(A) through (D), (b)(1)(ii)(A) and (D), and (b)(2),

D. Revising the introductory text of paragraph (c)(1),

E. Redesignating paragraph (d) as paragraph (f), and

F. Adding new paragraphs (d) and (e).

The additions and revisions read as follows:

§ 226.36 Prohibited acts or practices in connection with credit secured by ►real property or a dwelling◄ [a consumer's principal dwelling].

(a) ►*Loan originator and*◄ *mortgage broker defined.* ►(1) *Loan originator.* For purposes of this section, the term ''loan originator'' means with respect to a particular transaction, a person◀ [For purposes of this section ''mortgage broker'' means a person, other than an employee of a creditor,] who for compensation or other monetary gain, or in expectation of compensation or other monetary gain, arranges, negotiates, or otherwise obtains an extension of consumer credit for another person. [The term includes a person meeting this definition, even if the consumer credit obligation is initially payable to such person, unless the person provides] ▶The term ''loan originator'' includes employees of the creditor. The term includes the creditor if the creditor does not provide◀ the funds for the transaction at consummation out of the ▶creditor's◀ [person's] own resources, out of deposits held by the ▶creditor◀ [person], or by drawing on a bona fide warehouse line of credit.

▶(2) *Mortgage broker.* For purposes of this section, a mortgage broker with respect to a particular transaction is any loan originator that is not an employee of the creditor.◀

(b) *Misrepresentation of value of consumer's dwelling*—(1) *Coercion of appraiser.* In connection with a consumer credit transaction secured by ▶real property or◀ a [consumer's principal] dwelling, no creditor or mortgage broker, and no affiliate of a creditor or mortgage broker, shall directly or indirectly coerce, influence, or otherwise encourage an appraiser to misstate or misrepresent the value of such dwelling.

(i) * * *

(A) Implying to an appraiser that current or future retention of the appraiser depends on the amount at which the appraiser values a [consumer's principal] dwelling;

(B) Excluding an appraiser from consideration for future engagement because the appraiser reports a value of a [consumer's principal] dwelling that does not meet or exceed a minimum threshold;

(C) Telling an appraiser a minimum reported value of a [consumer's principal] dwelling that is needed to approve the loan;

(D) Failing to compensate an appraiser because the appraiser does not value a [consumer's principal] dwelling at or above a certain amount; and

* * * * *

(ii) * * *

(A) Asking an appraiser to consider additional information about a [consumer's principal] dwelling or about comparable properties;

* * * * *

(D) Obtaining multiple appraisals of a [consumer's principal] dwelling, so long as the creditor adheres to a policy of selecting the most reliable appraisal, rather than the appraisal that states the highest value;

* * * * *

(2) *When extension of credit prohibited.* In connection with a consumer credit transaction secured by ▶real property or◀ a [consumer's principal] dwelling, a creditor who knows, at or before loan consummation, of a violation of paragraph (b)(1) of this section in connection with an appraisal shall not extend credit based on such appraisal unless the creditor documents that it has acted with reasonable diligence to determine that the appraisal does not materially misstate or misrepresent the value of such dwelling.

* * * * *

(c) *Servicing practices.* (1) In connection with a consumer credit transaction secured by ▶real property or◀ a [consumer's principal] dwelling, no servicer shall—

* * * * *

ALTERNATIVE 1—PARAGRAPH (d).

▶(d) *Prohibited payments to loan originators.* (1) *Payments based on transaction terms and conditions.* In connection with a consumer credit transaction secured by real property or a dwelling, no loan originator shall receive and no person shall pay to a loan originator, directly or indirectly, compensation in an amount that is based on any of the transaction's terms or conditions. For purposes of this paragraph, the principal amount of credit extended is deemed to be a transaction term. This paragraph (d)(1) shall not apply to any transaction in which paragraph (d)(2) of this section applies.

(2) *Payments by persons other than consumer.* If a loan originator receives compensation directly from the consumer in a transaction secured by real property or a dwelling:

(i) The loan originator shall not receive compensation, directly or indirectly, from any person other than the consumer in connection with the transaction; and

(ii) No person who knows or has reason to know of the consumer-paid compensation to the loan originator, other than the consumer, shall pay any compensation to the loan originator, directly or indirectly, in connection with the transaction.

(3) *Affiliates.* For purposes of paragraph (d) of this section, affiliated entities shall be treated as a single ''person.''◀

ALTERNATIVE 2—PARAGRAPH (d).

▶(d) *Prohibited payments to loan originators.* (1) *Payments based on terms and conditions.* In connection with a consumer credit transaction secured by real property or a dwelling, no loan originator shall receive and no person shall pay to a loan originator, directly or indirectly, compensation in an amount that is based on any of the transaction's terms or conditions. For purposes of this paragraph the principal amount of credit extended is not deemed to be a transaction term or condition. This paragraph (d)(1) shall not apply to any transaction in which paragraph (d)(2) applies.

(2) *Payments by persons other than consumer.* If a loan originator receives compensation directly from the consumer in a transaction secured by real property or a dwelling:

(i) The loan originator shall not receive compensation, directly or indirectly, from any person other than the consumer in connection with the transaction; and

(ii) No person who knows or has reason to know of the consumer-paid compensation to the loan originator, other than the consumer, shall pay any compensation to the loan originator, directly or indirectly, in connection with the transaction.

(3) *Affiliates.* For purposes of paragraph (d) of this section, affiliated entities shall be treated as a single ''person.''◀

OPTIONAL PROPOSAL—PARAGRAPH (e).

▶(e) *Prohibition on steering.* (1) *General.* In connection with a credit transaction secured by real property or a dwelling, a loan originator shall not direct or ''steer'' a consumer to consummate a transaction based on the fact that the originator will receive greater compensation from the creditor in that transaction than in other transactions the originator offered or could have offered to the consumer, unless the transaction is in the consumer's interest.

(2) *Permissible transactions.* A transaction does not violate paragraph (e)(1) of this section if the loan was chosen by the consumer from at least three loan options for each type of transaction in which the consumer expressed an interest, and the conditions specified in paragraph (e)(3) of this section are met. For purposes of paragraph (e) of this section, the phrase ''type of transaction'' refers to whether a loan has:

(i) An annual percentage rate that cannot increase after consummation, or

(ii) An annual percentage rate that may increase after consummation.

(3) *Loan options presented.* A transaction satisfies paragraph (e)(2) of this section only if the loan originator

presents the loan options required by that paragraph and all of the following conditions are met:

(i) The loan originator obtains loan options from a significant number of the creditors with which the originator regularly does business and, for each type of transaction in which the consumer expressed an interest the originator must present and permit the consumer to choose from at least three loans that include:

(A) The loan with the lowest interest rate;

(B) The loan with the second lowest interest rate; and

(C) The loan with the lowest total dollar amount for origination points or fees and discount points, as offered by the creditors.

(ii) The loan originator must have a good faith belief that the options presented to the consumer pursuant to paragraph (e)(3)(i) of this section are loans for which the consumer likely qualifies.

(iii) For each type of transaction, if the originator presents to the consumer more than three loans, the originator must highlight the loans that satisfy the criteria specified in paragraph (e)(3)(i) of this section.◄

►(f)◄ [(d)] This section does not apply to a home equity line of credit subject to § 226.5b.

10. A new § 226.37 is added to Subpart E to read as follows:

►§ 226.37 Special disclosure requirements for closed-end mortgages.

(a) *Form of disclosures*—(1) *General.* The creditor shall make the disclosures required by §§ 226.19, 226.20(c), 226.20(d) and 226.38 clearly and conspicuously in writing, in a form that the consumer may keep.

(2) *Grouped and segregated.* The disclosures required by § 226.19, as applicable, § 226.20(c), § 226.20(d), or § 226.38 shall be grouped together and segregated from everything else, except as provided in paragraph (b) of this section, and shall not contain any information not directly related to the disclosures required under §§ 226.19, 226.20(c), 226.20(d), or 226.38, except:

(i) The disclosures may include the date of the transaction and the consumer's name, address, and account number; and

(ii) The following disclosures may be made together with or separately from other required disclosures under § 226.38: the tax deductibility disclosure under § 226.38(f)(4); and insurance, debt cancellation, or debt suspension disclosure under § 226.38(h).

(b) *Separate disclosures.* The following disclosures must be provided separately from other required disclosures under § 226.38: itemization of amount financed under § 226.38(j)(1); rebate under § 226.38(j)(2); late payment under § 226.38(j)(3); property insurance under § 226.38(j)(4); contract reference under § 226.38(j)(5); and assumption under § 226.38(j)(6).

(c) *Terminology.* (1) Terminology used in providing the disclosures required by §§ 226.19, 226.20(c), 226.20(d) and 226.38 shall be consistent.

(2) The term *annual percentage rate,* when required to be disclosed under § 226.38(b)(1) together with a corresponding percentage rate, shall be more conspicuous than any other required disclosure, disclosed in at least a 16-point font, and be placed in a prominent location and in close proximity to a scaled graph in accordance with the requirements under § 226.38(b)(2).

(d) *Specific formats.* (1) The disclosures required by § 226.38(a)(1) through (5) shall be provided in accordance with the requirements of § 226.38(a), and precede all other disclosures, except the identification required by § 226.38(g) and the disclosures permitted under paragraph (a)(2)(i) of this section;

(2) The disclosures required by § 226.38(b)(2) shall be provided in the form of a graph with shading, scaling and content in accordance with the requirements of § 228.38(b)(2), placed in a prominent location and in close proximity to the disclosures required by §§ 226.38(b)(1), 226.38(b)(3) and 226.38(b)(4);

(3) The disclosures required by § 226.38(c), as applicable, shall be provided in a tabular format in accordance with the requirements of § 226.38(c), and placed in a prominent location;

(4) The disclosure required by § 226.38(c)(2)(iii) shall be outlined in a box and placed directly beneath the table required by § 226.38(c)(1) in accordance with the requirements of § 226.38(c)(2)(iii);

(5) The disclosures required by § 226.38(d) shall be provided in a question and answer format in a tabular format in accordance with the requirements of § 226.38(d), and shall not precede the disclosures required by § 226.38(a) through (c).

(6) The disclosures required by § 226.38(e) shall be provided in a tabular format in accordance with the requirements of § 226.38(e), and precede any information not directly related to the disclosures required by § 226.38.

(7) The disclosures required by § 226.38(f) shall be provided in accordance with the requirements of § 226.38(f), and precede the disclosures required by § 226.38(j).

(8) The loan program disclosures required by § 226.19(b) for an adjustable-rate mortgage shall be provided in a tabular format in accordance with the requirements of § 226.19(b).

(9) The disclosures required by § 226.20(c)(2)–(4) for an adjustable-rate adjustment notice shall be provided in a tabular format in accordance with the requirements of § 226.20(c)(2)–(5).

(10) The disclosures required by § 226.20(d)(1) for loans with negative amortization shall be provided in a tabular format in accordance with the requirements of § 226.20(d).

(e) *Electronic disclosures.* The disclosures required by § 226.38 may be provided to the consumer in electronic form in accordance with the requirements under § 226.17(a)(1).◄

11. A new § 226.38 is added to Subpart E to read as follows:

►§ 226.38 Content of disclosures for closed-end mortgages.

In connection with a closed-end transaction secured by real property or a dwelling, the creditor shall disclose the following information:

(a) *Loan summary.* A separate section, labeled "Loan Summary."

(1) *Loan amount.* The principal amount the consumer will borrow as reflected in the loan contract.

(2) *Loan term.* The period of time to repay the obligation in full.

(3) *Loan type and features.* The loan types and loan features described in this section.

(i) *Loan type.* The loan type, as applicable:

(A) *Adjustable-rate mortgage.* If the annual percentage rate may increase after consummation, the creditor shall disclose that the loan is an "adjustable-rate mortgage," using that term.

(B) *Step-rate mortgage.* If the interest rate will change after consummation, and the rates and periods in which they will apply are known, the creditor shall disclose that the loan is a "step-rate mortgage," using that term.

(C) *Fixed-rate mortgage.* If the transaction is not an adjustable-rate mortgage or a step-rate mortgage, the creditor shall disclose that the loan is a "fixed-rate mortgage," using that term.

(ii) *Loan features.* No more than two loan features, as applicable:

(A) *Step-payments.* If, under the terms of the legal obligation, the regular periodic payments will gradually increase by a set amount at predetermined times, the creditor shall disclose that the loan has a "step-payment" feature, using that term; and

(B) *Payment option.* If, under the terms of the legal obligation, the consumer may choose to make one or more regular periodic payments that may cause the loan balance to increase, the creditor shall disclose that the loan has a ''payment option'' feature, using that term;

(C) *Negative amortization.* If, under the terms of the legal obligation, the regular periodic payments will cause the loan balance to increase and the loan is not a loan described in paragraphs (a)(3)(ii)(B) or (a)(3)(ii)(D) of this section, the creditor shall disclose that the loan has a ''negative amortization'' feature, using that term; or

(D) *Interest-only payments.* If, under the terms of the legal obligation, one or more regular periodic payments may be applied to interest accrued only and not to loan principal, and the loan is not a loan described in paragraphs (a)(3)(ii)(A) or (a)(3)(ii)(B) of this section, the creditor shall disclose that the loan has an ''interest-only payment'' feature, using that term.

(4) *Total settlement charges.* The ''total settlement charges,'' using that term, as disclosed under Regulation X, 12 CFR part 3500. As applicable, a statement of the amount of the charges already included in the loan amount and a statement that the total does not include a down payment, with a reference to the Good Faith Estimate or HUD–1 for details.

(5) *Prepayment penalty.* If the obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance and permits the creditor to impose a penalty if the obligation is prepaid in full, a statement indicating the amount of the maximum penalty and the circumstances and period in which the creditor may impose the penalty.

(6) *Form of disclosures; tabular format.* The disclosures required by paragraphs (a)(1) through (5) of this section shall be in the form of a table, with headings, content and format substantially similar to Forms H–19(A), H–19(B), or H–19(C) in Appendix H to this part. The table shall contain only the information required or permitted by paragraphs (a)(1) through (5).

(b) *Annual percentage rate.* The disclosures specified in paragraph (b)(1)–(4) of this section shall be grouped together with headings, content and format substantially similar to Forms H–19(A), H–19(B), or H–19(C) in Appendix H to this part.

(1) The ''annual percentage rate,'' using that term, and the following description: ''overall cost of this loan including interest and settlement charges.''

(2) A graph depicting the annual percentage rate (APR) disclosed under paragraph (b)(1) of this section and how it relates to a range of rates including the average prime offer rate as defined in § 226.35(a)(2) for the week in which the disclosure required under this section is provided, and the higher-priced mortgage loan threshold as defined in § 226.35(a)(1).

(i) The graph shall consist of a horizontal line or axis, with a shaded bar extending above and below the line. The horizontal axis shall be used to depict a range of APRs and the shaded bar shall use lighter shading on the left and darker shading on the right to distinguish between the rates on the graph that are below and above the APR representing the higher-priced mortgage loan threshold.

(ii) The lighter shaded area shall comprise the first two-thirds of the graph to represent the rates that are below the higher-priced mortgage loan threshold. On the horizontal axis, a range of APRs shall be plotted in the lighter shaded area, starting with the average prime offer rate depicted as the lowest APR on the left, and increasing in increments of .50 percentage points, up to the APR that is the higher-priced mortgage loan threshold. The average prime offer rate shall be plotted as the lowest APR on the horizontal axis and shall be labeled as ''Average Best APR'' or ''Avg. Best APR.''

(iii) The darker shaded area to the right side of the APR representing the higher-priced mortgage loan threshold shall comprise the last third of the graph, shall contain the words ''high cost zone'' and the APR that is 4 percentage points higher than the higher-priced mortgage threshold shall be plotted as the highest APR on the horizontal axis. Ellipses shall separate the APR representing the higher-priced mortgage threshold and the highest APR on the graph.

(iv) The graph shall include the APR disclosed under paragraph (b)(1) of this section and:

(A) Identify its location on the horizontal axis, which shall be labeled ''this loan: __% APR,'' or

(B) If the APR disclosed under paragraph (b)(1) exceeds the highest APR on the axis, identify its location beyond the rightmost edge of the shaded graph, or

(C) If the APR disclosed under paragraph (b)(1) is below the average prime offer rate, identify its location beyond the leftmost edge of the shaded graph.

(v) The lighter and darker shaded areas shall each extend past the lowest and highest APRs depicted on the axis, with a left pointing arrow to the left of lowest APR and a right-pointing arrow to the right of the highest APR.

(3) A statement of the average prime offer rate as defined in § 226.35(a)(2), and the higher-priced mortgage loan threshold, as defined in § 226.35(a)(1), current as of the week the disclosure is produced.

(4) The average per-period savings from a 1 percentage point reduction in the APR, which shall be calculated as follows:

(i) Reduce the interest rate by 1 percentage point and compute the total of payments that would result from the reduced interest rate;

(ii) Compute the difference between the total of payments in paragraph (b)(4)(i) of this section and the total of payments for the loan disclosed under § 226.38(e)(5)(i), and divide the difference by the total number of payments required to pay the loan off by its maturity.

(5) *Exemptions.* The following transactions are exempt from the disclosures required under paragraphs (b)(2) and (b)(3) of this section:

(i) A transaction to finance the initial construction of a dwelling;

(ii) A temporary or ''bridge'' loan with a term of twelve months or less, such as a loan to purchase a new dwelling where the consumer plans to sell a current dwelling within twelve months; and

(iii) A reverse-mortgage transaction subject to § 226.33.

(c) *Interest rate and payment summary.* The creditor shall disclose the following information about the interest rate and periodic payments:

(1) The information in paragraphs (c)(2)–(4) of this section shall be in the form of a table, with no more than five columns, with headings, content and format substantially similar to Forms H–19(A), H–19(B), or H–19(C) in Appendix H to this part. The table shall contain only the information required in paragraphs (c)(2)–(4).

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

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

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

(*2*) The maximum possible interest rate at the first scheduled interest rate adjustment and the date on which the adjustment will occur, labeled as ''maximum at first adjustment''; and

(*3*) The maximum possible interest rate at any time and the earliest date on which that rate may apply, labeled as ''maximum ever.''

(C) If the loan provides for payment increases in paragraph (c)(3)(i)(B) of this section, the interest rate in effect at the time the first payment increase is scheduled to occur and the date on which the increase will occur.

(ii) *Negative amortization loans.* The creditor shall disclose—

(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'';

(B) The maximum possible 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 possible interest rate that would be in effect at the first payment increase and the date the increase is scheduled to occur; and

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

(iii) *Introductory rate disclosure for amortizing adjustable-rate mortgage.* If the interest rate at consummation is less than the fully-indexed rate—

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

(B) A statement that even if market rates do not change, the interest rate will increase at the first adjustment and the date of such rate adjustment; and

(C) The fully-indexed rate.

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

(A) The corresponding regular periodic payment of principal and interest, labeled as ''principal and interest;''

(B) If the regular periodic payment may increase without regard to an interest rate adjustment, the payment that corresponds to the first 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;

(D) The sum of the amounts disclosed under paragraph (c)(3)(i)(A)–(C) of this section, with a description such as ''total estimated monthly payment.''

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

(A) If the payment will be applied to only the interest accrued, the amount applied to interest and an indication that none of the payment is being applied to principal;

(B) If the payment will be applied to interest accrued and principal, the earliest date that payment will be required and the payment amount itemized by the amount applied to interest accrued and the amount applied to principal;

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

(D) The sum of all amounts required to be disclosed under paragraph (c)(3)(i)(A)–(C) of this section, with a description such as ''total estimated monthly payment.''

(4) *Payments for negative amortization loans.* (i) The minimum payment—

(A) Required until the first payment increase or interest rate increase;

(B) That would be due at the first payment increase and the second, if any, in paragraphs (c)(2)(ii)(C) and (D) of this section; and

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

(ii) The fully amortizing payment amount at the earliest time when such a payment must be made; and, if applicable,

(iii) In addition to the payments in paragraphs (c)(4)(i) and (ii) of this section, for each interest rate required under paragraph (c)(2)(ii) of this section, the amount of the fully amortizing payment, labeled as the ''full payment option,'' and a statement that payments cover all principal and interest.

(5) *Balloon payments.* (i) Except as provided in paragraph (c)(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 must be disclosed separately from other regular periodic payments disclosed under this paragraph (c), in a manner substantially similar to Model Clause H–20 in Appendix H to this part.

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

(6) *Special disclosures for loans with negative amortization.* The following information, in close proximity to the table required in paragraph (c)(1) of this section, with headings, content and format substantially similar to Form H–19(C) in Appendix H to this part:

(i) The maximum possible interest rate, the period of time in which the interest rate could reach its maximum, 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 make a fully amortizing payment, assuming that the interest rate reaches its maximum at the earliest possible time.

(7) *Definitions.* For the purposes of this paragraph (c):

(i) The terms ''adjustable-rate mortgage,'' ''step-rate mortgage,'' ''fixed-rate mortgage,'' and ''interest-only'' shall have the meaning given to them in paragraphs (a)(3)(i) and (a)(3)(ii)(D) of this section;

(ii) The term ''amortizing loan'' means a loan in which the regular periodic payments cannot cause the principal balance to increase under the terms of the legal obligation; the term ''negative amortization'' means a loan in which the regular periodic payments may or will cause the principal balance to increase under the terms of the legal obligation; and

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

(d) *Key questions about risk.* The creditor shall disclose the information required in paragraphs (d)(1) and (d)(2) of this section, grouped together under the heading ''Key Questions About Risk,'' using that term:

(1) *Required disclosures.* The creditor shall disclose the following information—

(i) *Rate increases.* A statement indicating whether or not the interest rate on the loan may increase. If the interest rate on the loan may increase, a statement indicating the frequency with which the interest rate may increase and the date on which the first interest rate increase may occur.

(ii) *Payment increases.* A statement indicating whether or not the periodic payment on the loan may increase. If the periodic payment on the loan may increase, a statement indicating the date on which the first payment increase may occur. For a payment option loan, if the periodic payment on the loan may increase, statements indicating the dates on which the full and minimum payments may increase.

(iii) *Prepayment penalty.* If the obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance, a statement indicating whether or not a penalty will be imposed if the obligation is prepaid in full. If the creditor may impose a prepayment penalty, a statement of the circumstances under which and period in which the creditor may impose the penalty and the amount of the maximum penalty.

(2) *Additional disclosures.* The creditor shall disclose the following information, as applicable—

(i) *Interest-only payments.* A statement that periodic payments will be applied only toward interest on the loan, along with a statement of any limitation on the number of periodic payments that will be applied only toward interest on the loan, that such payments will cover the interest owed each month, but none of the principal, and that making these periodic payments means the loan amount will stay the same and the consumer will not have paid any of the loan amount. For payment-option loans, a statement that the loan gives the consumer the choice to make periodic payments that cover the interest owed each month, but none of the principal, and that making these periodic payments means the loan amount will stay the same and the consumer will not have paid any of the loan amount.

(ii) *Negative amortization.* A statement that the loan balance may increase even if the consumer makes the periodic payments, along with a statement that the minimum payment covers only a part of the interest the consumer owes each period and none of the principal, that the unpaid interest will be added to the consumer's loan amount, and that over time this will increase the total amount the consumer is borrowing and cause the consumer to lose equity in the home.

(iii) *Balloon payment.* A statement that the consumer will owe a balloon payment, along with a statement of the amount that will be due and the date on which it will be due.

(iv) *Demand feature.* A statement that the creditor may demand full repayment of the loan, along with a statement of the timing of any advance notice the creditor will give the consumer before the creditor exercises such right.

(v) *No-documentation or low-documentation loans.* A statement that the consumer's loan will have a higher rate or fees because the consumer did not document employment, income or other assets, along with a statement that if the consumer provides more documentation, the consumer could decrease the interest rate or fees.

(vi) *Shared-equity or shared-appreciation.* A statement that any future equity or appreciation in the real property or dwelling that secures the loan must be shared, along with a statement of the percentage of equity or appreciation to which the creditor is entitled, and the events that may trigger such obligation.

(3) *Format requirements.* (i) *Form of disclosures; tabular format.* The creditor shall provide the disclosures required by paragraphs (d)(1) and (2) of this section, as applicable, in the form of a table with headings, content and format substantially similar to Forms H–19(A), H–19(B), or H–19(C) in Appendix H to this part. The table shall contain only the information required or permitted by paragraphs (d)(1) and (2).

(ii) *Question and answer format.* The creditor shall provide the disclosures required by paragraphs (d)(1) through (d)(2) of this section grouped together and presented in the format of question and answer, in a manner substantially similar to Forms H–19(A), H–19(B), or H–19(C) in Appendix H to this part.

(iii) *Highlighting.* Each affirmative answer for a feature required to be disclosed under paragraphs (d)(1) and (2) of this section shall be disclosed in bold text and in all capitalized letters. Any negative answer shall be in nonbold text.

(iv) *Order.* The disclosures shall be provided, as applicable, in the following order: rate increases under § 226.38(d)(1)(i), payment increases under § 226.38(d)(1)(ii), interest-only payments under § 226.38(d)(2)(i), negative amortization under § 226.38(d)(2)(ii), balloon payment under § 226.38(d)(2)(iii), prepayment penalty under § 226.38(d)(1)(iii), demand feature under § 226.38(d)(2)(iv), no-documentation or low-documentation loans under § 226.38(d)(2)(v), and shared-equity or shared-appreciation under § 226.38(d)(2)(vi).

(e) *Information about payments.* A creditor shall disclose the following information, grouped together under the heading ''More Information About Your Payments'':

(1) *Rate calculation.* For an adjustable-rate mortgage, a statement labeled ''Rate Calculation'' that describes the method used to calculate the interest rate and the frequency of interest rate adjustments. If the interest rate that applies at consummation is not based on the index and margin that will be used to make later interest rate adjustments, the statement must include the time period when the initial interest rate expires.

(2) *Rate and payment change limits.* (i) For an adjustable-rate mortgage, any limitations on the increase in the interest rate labeled in bold type ''Rate Change Limits,'' together with a statement of the maximum rate that may apply pursuant to such limitations during the transaction's term to maturity.

(ii) If the regular periodic payment required under the terms of the legal obligation may cause the principal balance to increase, any limitations on the increase in the minimum payment amount and an identification of the circumstances under which the minimum required payment may recast to a fully amortizing payment labeled, in bold type, ''Payment Change Limits.''

(3) *Escrow.* If applicable, a statement, labeled in bold type ''Escrow,'' that explains that an escrow account is required for property taxes and insurance, that the escrow payment is an estimate that can change at any time, and that the consumer should consult the good faith estimate of settlement costs and HUD–1 settlement statement for more details. If no escrow is required, a statement of that fact and that the consumer will have to pay property taxes, homeowners', and other insurance directly.

(4) *Mortgage insurance.* If applicable, a statement, labeled in bold type, ''Private Mortgage Insurance,'' that private mortgage insurance is required and, if applicable, whether such insurance is included in any escrow account. If other mortgage insurance is required, for example, for a transaction insured by a government entity, the statement shall be labeled, in bold type, ''Mortgage Insurance.''

(5) *Total payments.* A creditor shall disclose the following information, grouped together under the subheading ''Total Payments,'' using that term:

(i) *Total payments.* The total payments amount, calculated based on the number and amount of scheduled payments in accordance with the requirements of § 226.18(g), together with a statement that the total payments is calculated on the assumption that market rates do not change, if applicable, and that the consumer makes all payments as scheduled. The statement must also specify the total number of payments and whether the total payments amount includes estimated escrow.

(ii) *Interest and settlement charges.* The *interest and settlement charges,* using that term, calculated as the finance charge in accordance with the requirements of § 226.4 and expressed as a dollar figure, together with a brief statement that the interest and settlement charges amount represents part of the total payments amount. The disclosed interest and settlement charges, and other disclosures affected by the disclosed interest and settlement charges (including the amount financed and annual percentage rate), shall be treated as accurate if the amount disclosed as the interest and settlement charges—

(A) Is understated by no more than $100;

(B) Is greater than the amount required to be disclosed.

(iii) *Amount financed.* The *amount financed,* using that term and expressed as a dollar figure, together with a brief statement that the interest and settlement charges and the amount financed are used to calculate the annual percentage rate. The amount financed is calculated by subtracting all prepaid finance charges from the loan amount required to be disclosed under § 226.38(a)(1).

(6) *Form of disclosures; tabular format.* The creditor must provide the disclosures required by paragraphs (e)(1) through (5) of this section in the form of a table, with headings, content, and format substantially similar to Forms H–19(A), H–19(B), or H–19(C) in Appendix H to this part. The table shall contain only the information required or permitted by paragraphs (e)(1) through (e)(5).

(f) *Additional disclosures.* The creditor shall disclose the following information, grouped together:

(1) *No obligation statement.* A statement that the consumer has no obligation to accept the loan. If the creditor provides space for a consumer's signature, a statement that a signature by the consumer only confirms receipt of the disclosure statement.

(2) *Security interest.* A statement that the consumer could lose the home if he or she is unable to make payments on the loan.

(3) *No guarantee to refinance statement.* A statement that there is no guarantee the consumer can refinance the transaction to lower the interest rate or monthly payments.

(4) *Tax deductibility.* For a transaction secured by a dwelling, if the extension of credit may exceed the fair market value of the dwelling, the creditor shall disclose that:

(i) The interest on the portion of the credit extension that is greater than the fair market value of the dwelling may not be tax deductible for Federal income tax purposes; and

(ii) The consumer should consult a tax adviser for further information regarding the deductibility of interest and charges.

(5) *Additional information and Web site.* A statement that if the consumer does not understand any disclosure required by this section the consumer should ask questions, a statement that the consumer may obtain additional information at the Web site of the Federal Reserve Board, and a reference to that Web site.

(6) *Format*—(i) *Location.* The statements required by paragraph (f)(1) of this section must be disclosed together. The disclosure required by paragraph (f)(2) of this section must be made together with the disclosure paragraph (f)(3) of this section. The statements required by paragraph (f)(5) of this section must be made together.

(ii) *Highlighting.* The first statement required to be disclosed by paragraphs (f)(1) and (f)(5) of this section, and the statement required to be disclosed by paragraph (f)(2), must be disclosed in bold text.

(iii) *Form of disclosures.* The creditor must provide the disclosures required by paragraphs (f)(1) through (5) of this section in a manner substantially similar to Forms H–19(A), H–19(B), or H–19(C) in Appendix H to this part.

(g) *Identification of creditor and loan originator*—(1) *Creditor.* The identity of the creditor making the disclosures.

(2) *Loan originator.* The loan originator's unique identifier, as defined by the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 Sections 1503(3) and (12), 12 U.S.C. 5102(3) and (12).

(h) *Credit insurance and debt cancellation and debt suspension coverage.* The disclosures specified in paragraphs (h)(1)–(10) of this section, which shall be grouped together and substantially similar in headings, content and format to Model Clauses H–17(A) and H–17(C) in Appendix H to this part.

(1)(i) If the product is optional, the term ''OPTIONAL COSTS,'' in capitalized and bold letters, along with the name of the program, in bold letters; or

(ii) If the product is required, the name of the program, in bold letters.

(2) If the product is optional, the term ''STOP,'' in capitalized and bold letters, along with a statement that the consumer does not have to buy the product to get the loan. The term ''not'' shall be in bold text and underlined.

(3) A statement that if the consumer already has insurance, then the policy or coverage may not provide the consumer with additional benefits.

(4) A statement that other types of insurance may give the consumer similar benefits and are often less expensive.

(5) (i) If the eligibility restrictions are limited to age and/or employment, a statement that based on the creditor's review of the consumer's age and/or employment status at this time, the consumer would be eligible to receive benefits.

(ii) If there are other eligibility restrictions in addition to age and/or employment, a statement that based on the creditor's review of the consumer's age and/or employment status at this time, the consumer may be eligible to receive benefits.

(6) If there are other eligibility restrictions in addition to age and/or employment, such as pre-existing health conditions, a statement that the consumer may not qualify to receive any benefits because of other eligibility restrictions.

(7) If the product is a debt suspension agreement, a statement that the obligation to pay loan principal and interest is only suspended, and that interest will continue to accrue during the period of suspension.

(8) A statement that the consumer may obtain additional information about the product at the Web site of the Federal Reserve Board, and reference to that Web site.

(9)(i) If the product is optional, a statement of the consumer's request to purchase or enroll in the optional product and a statement of the cost of the product expressed as a dollar amount per month or per year, as applicable, together with the loan amount and the term of the product in years; or

(ii) If the product is required, a statement that the product is required, along with a statement of the cost of the product expressed as a dollar amount per month or per year, as applicable, together with the loan amount and the term of the product in years.

(iii) The cost, month or year, loan amount, and term of the product shall be underlined.

(10) A designation for the signature of the consumer and the date of the signing.

(i) *Required deposit.* If the creditor requires the consumer to maintain a deposit as a condition of the specific transaction, a statement that the annual percentage rate does not reflect the effect of the required deposit. A required deposit need not include:

(1) An escrow account for items such as taxes, insurance or repairs; or

(2) A deposit that earns not less than 5 percent per year.

(j) *Separate disclosures.* The following information must be provided separately from the other information required to be disclosed under this section.

(1) *Itemization of amount financed.* The creditor shall provide one of the following disclosures:

(i) A separate written itemization of the amount financed, including:

(A) The amount of any proceeds distributed directly to the consumer.

(B) The amount credited to the consumer's account with the creditor.

(C) Any amounts paid to other persons by the creditor on the consumer's behalf. The creditor shall identify those persons, except that the following payees may be described using general terms and need not be further identified: Public officials or government agencies, credit reporting agencies, appraisers, and insurance companies.

(D) The prepaid finance charge.

(ii) A statement that the consumer has the right to receive a written itemization of the amount financed, together with a space for the consumer to indicate whether it is desired. If the consumer requests it, the creditor shall provide an itemization that satisfies paragraph (j)(1)(i) of this section at the same time as the other disclosures required by this section.

(iii) A good faith estimate of settlement costs provided under the Real Estate Settlement Procedures Act, 12 U.S.C. 2601 *et seq.* (RESPA), in connection with disclosures under this section delivered within three business days of application pursuant to § 226.19(a)(1), or the HUD–1 settlement statement provided under RESPA, in connection with disclosures under this section delivered three business days before consummation pursuant to § 226.19(a)(2). The alternative provided by this paragraph (j)(1)(iii) is available whether or not those disclosures are required by RESPA, but the HUD–1 settlement statement satisfies this requirement only if it is provided to the consumer at the time required by § 226.19(a)(2).

(2) *Rebate.* If the obligation includes a finance charge other than one computed from time to time by application of a rate to the unpaid principal balance, a statement indicating whether or not the consumer is entitled to a rebate of any finance charge if the obligation is prepaid in full.

(3) *Late payment.* Any dollar or percentage charge that may be imposed before maturity due to a late payment, other than a deferral or extension charge.

(4) *Property insurance.* A statement that the consumer may obtain property insurance from any insurer that is acceptable to the creditor.

(5) *Contract reference.* A statement that the consumer should refer to the appropriate contract document for information about nonpayment, default, the right to accelerate the maturity of the obligation, and prepayment rebates and penalties. At the creditor's option, the statement may also include a reference to the contract for further information about security interests and about the creditor's policy regarding assumption of the obligation.

(6) *Assumption policy.* A statement whether or not a subsequent purchaser of the real property or dwelling from the consumer may be permitted to assume the remaining obligation on its original terms.

12. Appendix G to Part 226, as amended on January 29, 2009 (74 FR 5422) is amended by:

A. Adding entries for G–16(C) and G–16(D) to the table of contents at the beginning of the appendix; and

B. Adding new Model Clause G–16(C) and new Sample G–16(D) in numerical order.

Appendix G to Part 226—Open-End Model Forms and Clauses

* * * * *

►G–16(C) Credit Insurance, Debt Cancellation or Debt Suspension Model Clause (§ 226.4(d)(1) and (d)(3))

G–16(D) Credit Insurance, Debt Cancellation or Debt Suspension Sample (§ 226.4(d)(1) and (d)(3))◄

* * * * *

►G–16(C) Credit Insurance, Debt Cancellation or Debt Suspension Model Clause

OPTIONAL COSTS

(*Name of Program*)

STOP. You do *not* have to buy this product to get this loan.

• If you have insurance already, this policy may not provide you with any additional benefits.

• Other types of insurance can give you similar benefits and are often less expensive.

• Based on our review of your age and/or employment status at this time, you [would][may] be eligible to receive benefits.

• [However, you may not qualify to receive any benefits because of other eligibility restrictions.]

To learn more about [credit insurance][debt cancellation coverage][debt suspension coverage], go to (*Board's Web site*).

☐ Yes, I want to purchase optional (*name of program*) at an additional cost of (*cost*) per (*month or year*) for a loan of (*loan amount*) with a [policy/coverage] term of (*term in years*) years.

____

Signature of Borrower(s)

____

Date

G–16(D) Credit Insurance, Debt Cancellation or Debt Suspension Sample

OPTIONAL COSTS

Credit Life Insurance

STOP. You do *not* have to buy this product to get this loan.

• If you have insurance already, this policy may not provide you with any additional benefits.

• Other types of insurance can give you similar benefits and are often less expensive.

• Based on our review of your age and/or employment status at this time, you may be eligible to receive benefits.

• However, you may not qualify to receive any benefits because of other eligibility restrictions.

To learn more about credit insurance, go to *http://www.xxx.gov.*

☐ Yes, I want to purchase optional credit life insurance at an additional cost of *$72* per *month* for a loan of *$100,000* with a policy term of *10* years.

____

Signature of Borrower(s)

____

Date◄

13. Appendix H to Part 226, as amended on January 29, 2009 (74 FR 5441) is amended by:

A. Revising the table of contents at the beginning of the appendix;

B. Republishing H–4(A);

C. Removing H–4(B), H–4(C) and H–4(D);

D. Republishing H–5;

E. Removing and reserving H–6;

F. Republishing H–7;

G. Removing and reserving H–13 through H–15;

H. Revising H–16; and

I. Adding new H–4(B) through H–4(L), H–17(C) and H–17(D), and H–18 through H–23 in numerical order.

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

* * * * *

H–4(A)—Variable-Rate Model Clauses (§ 226.18(f)[(1)])

H–4(B)—[Variable-Rate Model Clauses (§ 226.18(f)(2)]►Adjustable-Rate Loan Program Model Form (§ 226.19(b))◄

H–4(C)—[Variable-Rate Model Clauses (§ 226.19(b))]►Adjustable-Rate Loan Program Model Clauses (§ 226.19(b))◄

H–4(D)—[Variable-Rate Model Clauses (§ 226.20(c))]►Adjustable-Rate Loan Program Sample (Hybrid ARM) (§ 226.19(b))◄

►H–4(E)—Adjustable-Rate Loan Program Sample (Interest Only ARM) (§ 226.19(b))

H–4(F)—Adjustable-Rate Loan Program Sample (Payment Option ARM) (§ 226.19(b))
H–4(G)—Adjustable-Rate Adjustment Notice Model Form (§ 226.20(c))
H–4(H)—Adjustable-Rate Adjustment Notice Model Clauses (§ 226.20(c))
H–4(I)—Adjustable-Rate Adjustment Notice Sample (Interest Only ARM) (§ 226.20(c))
H–4(J)—Adjustable-Rate Adjustment Notice Sample (Hybrid ARM) (§ 226.20(c))
H–4(K)—Adjustable-Rate Annual Notice Model Form (§ 226.20(c))
H–4(L)—Negative Amortization Monthly Disclosure Model Form (§ 226.20(d))◄

* * * * *

H–6—[Assumption Policy Model Clause (§ 226.18(q))]►Reserved◄

* * * * *

H–13—[Mortgage with Demand Feature Sample]►Reserved◄
H–14—[Variable-Rate Mortgage Sample (§ 226.19(b))]►Reserved◄
H–15—[Graduated-Payment Mortgage Sample]►Reserved◄
H–16—[Mortgage Sample (§ 226.32)]►Section 32 Loan Model Clauses (§ 226.32(c))◄

* * * * *

►H–17(C)—Credit Insurance, Debt Cancellation or Debt Suspension Model Clause (§ 226.4(d)(1), (d)(3) and § 226.38(h))
H–17(D)—Credit Insurance, Debt Cancellation or Debt Suspension Sample (§ 226.4(d)(1), (d)(3), and § 226.38(h))
H–18—Creditor-Placed Property Insurance Model Clause (§ 226.20(e))
H–19(A)—Fixed Rate Mortgage Model Form (§ 226.38)
H–19(B)—Adjustable-Rate Mortgage Model Form (§ 226.38)
H–19(C)—Mortgage with Negative Amortization Model Form (§ 226.38)
H–19(D)—Fixed Rate Mortgage with Balloon Payment Sample (§ 226.38)
H–19(E)—Fixed Rate Mortgage with Interest Only Sample (§ 226.38)
H–19(F)—Step-Payment Mortgage Sample (§ 226.38)
H–19(G)—Hybrid Adjustable-Rate Mortgage Sample (§ 226.38)
H–19(H)—Adjustable-Rate Mortgage with Interest Only Sample (§ 226.38)
H–19(I)—Adjustable-Rate Mortgage with Payment Options Sample (§ 226.38)
H–20—Balloon Payment Model Clause (§ 226.38(c)(5))
H–21—Introductory Rate Model Clause (§ 226.38(c)(2)(iii))
H–22—Key Questions About Risk Model Clauses (§ 226.38(d))
H–23—Separate Disclosure Model Clauses (§ 226.38(j)(2)–(6))◄

* * * * *

H–4(A)—Variable Rate Model Clauses

The annual percentage rate may increase during the term of this transaction if:

[the prime interest rate of (creditor) increases.]

[the balance in your deposit account falls below $________.]

[you terminate your employment with (employer).]

[The interest rate will not increase above____%.]

[The maximum interest rate increase at one time will be____%.]

[The rate will not increase more than once every (time period).]

Any increase will take the form of:

[higher payment amounts.]

[more payments of the same amount.]

[a larger amount due at maturity.]

Example based on the specific transaction

[If the interest rate increases by____% in (time period),

[your regular payments will increase to $________.]

[you will have to make____additional payments.]

[your final payment will increase to $________.]]

Example based on a typical transaction

[If your loan were for $________at____% for (term) and the rate increased to____% in (time period),

[your regular payments would increase by $________.]

[you would have to make____additional payments.]

[your final payment would increase by $________.]]

►H-4(B) Adjustable-Rate Loan Program Model Form

(Name of Creditor)
(Name of Loan Program)

INTEREST RATE AND PAYMENT	
Introductory Period	***(Length of Time)*** The interest rate [is discounted and] will stay the same for [a] *(length of time)* [introductory period]. After this initial period, [the interest rate could increase][even if market rates do not change, this rate will [increase][decrease] by ___%].
Frequency of Rate [and Payment] Change	***(Frequency)*** The interest rate [and payment] will adjust *(frequency)* [after the introductory period]. [The payment will adjust *(frequency)* [after the introductory period].]
[Index] [Formula]	**[*(Index)*][*(Formula)*]** After the initial *(length of time)* period, your interest rate will be based on [the *(index)* plus a margin. The *(index)* is published in the *(source of index)*] [*(formula)*. Information about this formula can be found at *(source of formula)*].
Limits on [Rate] [and Payment] Changes	**[___% *(Frequency)* Cap][;][___% Lifetime Cap]** Your [interest rate][payment] can increase [**no more than** ___**%** in any *(time period)*][, and] [**no more than** ___**%** over the life of the loan].]

KEY QUESTIONS ABOUT RISK	
Can my interest rate increase?	**YES.** Your interest rate could increase at the end of the *(length of time)* [introductory period], and *(frequency)* after that.
Can my monthly payment increase?	[No.] [**YES.** [If your interest rate increases, your monthly payment will increase.][Your minimum payment can increase after *(period)*.]]
[Will any of my monthly payments be interest-only?]	[**YES.** [Your *(frequency)* payments for the first *(period)* of the loan][This loan would give you the choice to make *(frequency)* payments that] cover the interest you owe each month, but **none** of the principal. Making these *(frequency)* payments means your loan amount will stay the same and you will be no closer to having it paid off.]
[Even if I make my monthly payments, could my loan balance increase?]	[**YES.** Your minimum payment covers only part of the interest you owe each *(period)* and **none** of the principal. The unpaid interest will be added to your loan amount, which over time will increase the total amount you are borrowing and cause you to lose equity in your home.]
[Will I owe a balloon payment?]	[**YES.** You would owe a balloon payment due *(period)*.]
Could I owe a prepayment penalty?	[No.][**YES.** If you pay off your loan, refinance, or sell your home within *(period)* you could pay a large penalty.]
[Can my lender demand full repayment at any time?]	[**YES.** We can demand that you pay off the **full** amount of your loan at any time. We would give you at least *(period)* notice.]
[Could my loan have a higher rate or fees if I do not document my employment, income or other assets?]	[**YES.** If you provide more documentation, you could decrease your interest rate or fees.]
[Do I have to share any equity I gain?]	[**YES.** We are entitled to ___% of any gain you make when you sell or refinance this property.]

For more information about ARMs, or for a list of licensed housing counselors in your area that can help you understand risks and benefits of this loan, visit *(Web site of the Federal Reserve Board)*.

H–4(C)—Adjustable-Rate Loan Program Model Clauses

Interest Rate and Payment

(a) Limits on rate or payment changes

[If a rate cap prevents us from adding part of an interest rate, we can add that increase at a later adjustment date.]

(b) Conversion feature

[Conversion Feature

You have the option to convert your loan to a fixed rate loan for (*length of time*). If you convert your loan to a fixed rate loan, the [rate] [payment] may not increase more than (*frequency*)[or ____% overall]. [You may have a higher interest rate when you convert to a fixed rate loan.]

[You may have to pay fees when you convert to a fixed rate loan.]]

(c) Preferred rate

[Preferred Rate

The interest rate is a preferred rate that could [increase] [decrease] by____% if (*description of event*).] [You could pay fees if [one or more] (*description of event(s)*) occur(s).]

H-4(D) Adjustable-Rate Loan Program Sample (Hybrid ARM)

XXX Bank
3/1 Adjustable Rate Mortgage (ARM)

INTEREST RATE AND PAYMENT	
Introductory Period	**3 Years** The interest rate is discounted and will stay the same for a 3-year introductory period. After this initial period, the interest rate could increase.
Frequency of Rate Change	**Annually** The interest rate will adjust once each year after the introductory period.
Index	**LIBOR Index** After the initial 3-year period, your interest rate will be based on the 1- year LIBOR Index plus a margin. The LIBOR is published daily in the Wall Street Journal.
Limits on Rate Changes	**2% Annual Cap; 6% Lifetime Cap** Your interest rate can increase **no more than 2%** in any one year, and **no more than 6%** over the life of the loan.

KEY QUESTIONS ABOUT RISK	
Can my interest rate increase?	**YES.** Your interest rate could increase at the end of the 3-year introductory period, and annually after that.
Can my monthly payment increase?	**YES.** If your interest rate increases, your monthly payment will increase.
Could I owe a prepayment penalty?	**YES.** If you pay off your loan, refinance, or sell your home within **2 years** you could pay a large penalty.

For more information about ARMs, or for a list of licensed housing counselors in your area that can help you understand the risks and benefits of this loan, visit www.xxx.gov.

H-4(E) Adjustable-Rate Loan Program Sample (Interest Only ARM)

XXX Bank
5/1 Interest-Only Adjustable Rate Mortgage (ARM)

INTEREST RATE AND PAYMENT	
Introductory Period	**5 Years** The interest rate is discounted and will stay the same for a 5-year introductory period. After this initial period, the interest rate could increase.
Frequency of Rate Change	**Annually** The interest rate will adjust once each year after the introductory period.
Index	**LIBOR Index** After the initial 5-year period, your interest rate will be based on the 1-year LIBOR Index plus a margin. The LIBOR is published daily in the Wall Street Journal.
Limits on Rate Changes	**2% Annual Cap; 6% Lifetime Cap** Your interest rate can increase **no more than 2%** in any one year, and **no more than 6%** over the life of the loan.

KEY QUESTIONS ABOUT RISK	
Can my interest rate increase?	**YES.** Your interest rate could increase at the end of the 5-year introductory period, and annually after that.
Can my monthly payment increase?	**YES.** If your interest rate increases, your monthly payment will increase.
Will any of my monthly payments be interest-only?	**YES.** Your monthly payments for the first 5 years of the loan cover the interest you owe each month, but **none** of the principal. Making these monthly payments means your loan amount will stay the same and you will be no closer to having it paid off.
Could I owe a prepayment penalty?	**YES.** If you pay off your loan, refinance, or sell your home within **2 years** you could pay a large penalty.

For more information about ARMs, or for a list of licensed housing counselors in your area that can help you understand the risks and benefits of this loan, visit www.xxx.gov.

H-4(F) Adjustable-Rate Loan Program Sample (Payment Option ARM)

XXX Bank
1-Month Payment Option Adjustable Rate Mortgage (ARM)

INTEREST RATE AND PAYMENT	
Introductory Period	**1 Month** The interest rate is discounted and will stay the same for a 1-month introductory period. After this initial period, the interest rate could increase.
Frequency of Rate Change	**Monthly** The interest rate will adjust once each month after the introductory period.
Index	**LIBOR Index** After the initial 1-month period, your interest rate will be based on the 1-year LIBOR Index plus a margin. The LIBOR is published daily in the Wall Street Journal.
Limits on Rate Changes	**10.5% Maximum Rate** Your interest rate can increase up to **a maximum of 10.5%** over the life of the loan.

KEY QUESTIONS ABOUT RISK	
Can my interest rate increase?	**YES.** Your interest rate could increase at the end of the 1-month introductory period, and monthly after that.
Can my monthly payment increase?	**YES.** Your minimum payment can increase after one year.
Will any of my monthly payments be interest-only?	**YES.** This loan would give you the choice to make monthly payments that cover the interest you owe each month, but **none** of the principal. Making these monthly payments means your loan amount will stay the same and you will be no closer to having it paid off.
Even if I make my monthly payments, could my loan balance increase?	**YES.** Your minimum payment covers only part of the interest you owe each month and **none** of the principal. The unpaid interest will be added to your loan amount, which over time will increase the total amount you are borrowing and cause you to lose equity in your home.
Could I owe a prepayment penalty?	No.

For more information about ARMs, or for a list of licensed housing counselors in your area that can help you understand the risks and benefits of this loan, visit www.xxx.gov.

H-4(G) Adjustable-Rate Adjustment Notice Model Form

Important Changes to Your Loan Terms

The following is a summary of changes that are being made to your loan terms as a result of changes to your interest rate, effective (*date*). For more detailed information, please refer to your loan agreement(s).

The changes are as follows:

	Current Rate and Monthly Payment	**New** Rate and Monthly Payment
Interest Rate	___%	___%
[Principal]	[$___]	[$___]
[Interest]	[$___]	[$___]
[Taxes + Insurance (Escrow)]	[$___]	[$___]
Total Monthly Payment	$___	$___ (due on (*date*))

Interest Rate: Your interest rate will change due to an [increase][decrease] in the (*index*). [(__%) is being added (interest carried over) to your interest rate because the rate cap prevented this increase at your last interest rate adjustment.] [We could have increased your interest rate another __% but did not because a rate cap applied. We can add this to your interest rate when the interest rate adjusts again on (*date*).]

[Maximum] [Rate] [Payment] [Limits]: [Your [rate] [payment] can change each (*frequency*), by no more than ___%.] [Your rate can not go higher than __% over the life of the loan.]

New Monthly Payment: [Your new payment will cover all of your interest and some of your loan's principal, and therefore will reduce your loan balance.]

Loan Balance: Your new loan balance as of (*date of rate adjustment*) is $______.

[**Prepayment Penalty:** If you pay off your loan, refinance or sell your home before (*date*) you could pay a penalty of up to $___.]

If you have trouble paying your mortgage, contact us at (*telephone number*) [or (*email address*)] as soon as possible.

If you would like to talk with a licensed housing counselor, you can find a list of counselors in your area on the (*Web site of the U.S. Department of Housing and Urban Development*).

H–4(H) Adjustable-Rate Adjustment Notice Model Clauses

Disclosure of New Monthly Payment

[Your new payment covers all of the interest that you owe this month, but none of the principal, and therefore will not reduce your loan balance. The payment needed to fully pay off your loan by the end of the loan term at the new interest rate is $____.]

[Your new payment covers only part of the interest that you owe this month, and therefore unpaid interest will be added to your loan balance. The payment needed to fully pay off your loan by the end of the loan term at the new interest rate is $____.]

[Your new payment covers only part of the interest that you owe this month, and therefore the term of your loan will increase. The payment needed to fully pay off your loan by the end of the previous loan term at the new interest rate is $____.]

H-4(I) Adjustable-Rate Adjustment Notice Sample (Interest Only ARM)

Important Changes to Your Loan Terms

The following is a summary of changes that are being made to your loan terms as a result of changes to your interest rate, effective April 1, 2009. For more detailed information, please refer to your loan agreement(s).

The changes are as follows:

	Current Rate and Monthly Payment	**New** Rate and Monthly Payment
Interest Rate	**6.875%**	**7.75%**
Principal	**- none -**	$218.99
Interest	$1,145.83	$1,291.67
Taxes + Insurance (Escrow)	$345.00	$400.00
Total Monthly Payment	**$1,490.83**	**$1,910.66** (due on May 1, 2009)

Interest Rate: Your interest rate will change due to an increase in the 1-year LIBOR index.

Rate Limits: Your rate can change each year, by no more than 2.00%. Your rate can not go higher than 12.875% over the life of the loan.

New Monthly Payment: Your new payment will cover all of your interest and some of your loan's principal, and therefore will reduce your loan balance.

Loan Balance: Your new loan balance as of April 1, 2009 is $200,000.

If you have trouble paying your mortgage, contact us at 1-800-XXX-XXXX or www.xxx.com as soon as possible.

If you would like to talk with a licensed housing counselor, you can find a list of counselors in your area on the U.S. Department of Housing and Urban Development's website at www.xxx.gov.

H-4(J) Adjustable-Rate Adjustment Notice Sample (Hybrid ARM)

Important Changes to Your Loan Terms

The following is a summary of changes that are being made to your loan terms as a result of changes to your interest rate, effective April 1, 2009. For more detailed information, please refer to your loan agreement(s).

The changes are as follows:

	Current Rate and Monthly Payment	**New** Rate and Monthly Payment
Interest Rate	**5.625%**	**5.125%**
Total Monthly Payment	**$1,151.31**	**$1,093.27** (due on May 1, 2009)

Interest Rate: Your interest rate will change due to a decrease in the 1-year LIBOR index.

Rate Limits: Your rate can change each year, by no more than 2.00%. Your rate can not go higher than 11.625% over the life of the loan.

New Monthly Payment: Your new payment will cover all of your interest and some of your loan's principal, and therefore will reduce your loan balance.

Loan Balance: Your new loan balance as of April 1, 2009 is $191,888.37.

Prepayment Penalty: If you pay off your loan, refinance or sell your home before May 1, 2010 you could pay a penalty of up to **$4,323.13**.

If you have trouble paying your mortgage, contact us at 1-800-XXX-XXXX as soon as possible.

If you would like to talk with a licensed housing counselor, you can find a list of counselors in your area on the U.S. Department of Housing and Urban Development's (HUD) website at www.xxx.gov.

H-4(K) Adjustable-Rate Annual Notice Model Form

Important Interest Rate Notice

Your interest rate changed between (*date period begins*) and (*date period ends*) without changing your payment.

Highest and Lowest Rates: The lowest interest rate this (*period*) was __% and the highest interest rate was __%. [This includes a __% interest rate increase we did not make previously because a rate cap applied.] [We could have increased your interest rate another __% but did not because a rate cap applied. We can add this to your interest rate when the interest rate adjusts again on (*date*).]

Maximum Rate: Your rate can not go higher than ___% over the life of the loan.

Loan Balance: Your new loan balance as of (*last date of period*) is $______.

[**Prepayment Penalty:** If you pay off your loan, refinance or sell your home before (*date*) you could pay a penalty of up to $___.]

If you have trouble paying your mortgage, contact us at (*telephone number*) [or (*email address*)] as soon as possible.

If you would like to talk with a licensed housing counselor, you can find a list of counselors in your area on the (*Web site of the U.S. Department of Housing and Urban Development*).

* * * * *

H-4(L) Negative Amortization Monthly Disclosure Model Form

Your Payment Options This Month

Payment Option	This Payment Covers	If you make this payment *this* month	If you make this payment *every* month
❑ **$___** Full Payment *(recommended to reduce loan balance)*	All the interest that you owe this month, plus some principal.	Your balance will decrease. You will be closer to having it paid off.	Your balance will steadily decrease and you will pay off your loan on schedule.
❑ **$___** Interest-Only Payment	All the interest that you owe this month, but none of the principal.	Your balance will stay the same. You will be no closer to having it paid off.	As early as (*date*), you will have to make monthly payments much larger than today's "Full Payment" amount.
❑ **$___** Minimum Payment	Just part of the interest that you owe this month.	**$___ in unpaid interest will be added to your loan balance this month.** You are borrowing more money, and you will be losing equity in your home.	As early as (*date*), you will have to make payments significantly larger than today's "Full Payment" amount to pay off your loan.

◄

* * * * *

H–5—Demand Feature Model Clauses

This obligation [is payable on demand.][has a demand feature.]

[All disclosures are based on an assumed maturity of one year.]

H–6—[Assumption Policy Model Clause]►Reserved◄

[Assumption: Someone buying your house [may, subject to conditions, be allowed to][cannot] assume the remainder of the mortgage on the original terms.]

H–7—Required Deposit Model Clause

The annual percentage rate does not take into account your required deposit.

* * * * *

H–13—[Mortgage With Demand Feature Sample]►Reserved◄

H–14—[Variable-Rate Mortgage Sample]►Reserved◄

H–15—[Graduated-Payment Mortgage Sample]►Reserved◄

H–16—[Mortgage Sample]►Section 32 Loan Model Clauses◄

[You are not required to complete this agreement merely because you have received these disclosures or have signed a loan application.

If you obtain this loan, the lender will have a mortgage on your home.

YOU COULD LOSE YOUR HOME, AND ANY MONEY YOU HAVE PUT INTO IT, IF YOU DO NOT MEET YOUR OBLIGATIONS UNDER THE LOAN.]

►IF YOU ARE UNABLE TO MAKE THE PAYMENTS ON THIS LOAN, YOU COULD LOSE YOUR HOME.

You have no obligation to accept this loan. Your signature below only confirms that you have received this form.◄

You are borrowing $________ (optional credit insurance is ☐ is not ☐ included in this amount).

The annual percentage rate on your loan will be:________%.

Your regular (*frequency*) payment will be: $________.

[At the end of your loan, will still owe use: $ (*balloon payment*).]

[Your interest rate may increase. Increase in the interest rate could increase your payment. The highest amount your payment could increase is to $________.]

* * * * *

►H–17(C)—Credit Insurance, Debt Cancellation or Debt Suspension Model Clause

[OPTIONAL COSTS]

(*Name of Program*)

[STOP. You do *not* have to buy this product to get this loan.]

- If you have insurance already, this policy may not provide you with any additional benefits.
- Other types of insurance can give you similar benefits and are often less expensive.
- Based on our review of your age and/or employment status at this time, you [would][may] be eligible to receive benefits.
- [However, you may not qualify to receive any benefits because of other eligibility restrictions.]

To learn more about [credit insurance][debt cancellation coverage][debt suspension coverage], go to (*Web site of the Federal Reserve Board*).

☐ [Yes, I want to purchase optional (*name of program*) at an additional cost of (*cost*) per (*month or year*) for a loan of (*loan amount*) with a (policy/coverage) term of (*term in years*) years.]

[(*Name of program*) is required and costs (*cost*) per (*month or year*) for a loan of (*loan amount*) with a [policy/coverage] term of (*term in years*) years.]

Signature of Borrower(s)

Date

H–17(D)—Credit Insurance, Debt Cancellation or Debt Suspension Sample

OPTIONAL COSTS

Credit Life Insurance

STOP. You do *not* have to buy this product to get this loan.

- If you have insurance already, this policy may not provide you with any additional benefits.
- Other types of insurance can give you similar benefits and are often less expensive.
- Based on our review of your age and/or employment status at this time, you may be eligible to receive benefits.
- However, you may not qualify to receive any benefits because of other eligibility restrictions.

To learn more about credit insurance, go to *www.xxx.gov.*

☐ Yes, I want to purchase optional credit life insurance at an additional cost of *$72* per *month* for a loan of *$100,000* with a policy term of *10* years.

Signature of Borrower(s)

Date

H–18—Creditor-Placed Property Insurance Model Clause

(Creditor name and contact information)

Re: (loan number) and (property address/ description)

Under our agreement, you must maintain adequate insurance coverage on the property. Our records show that your insurance policy has expired or been cancelled, and we do not have evidence that you have obtained new insurance coverage. Under our agreement, we can buy property insurance on your behalf and charge you for the cost as early as (*date*). Therefore, we request that you provide us with proof of insurance by (*description of procedure for providing proof of insurance*).

Please consider the following facts about the insurance policy that we buy:

- The cost of this insurance policy is $________ per year and is probably significantly higher than the cost of insurance you can buy through your own insurance agent.
- This insurance policy may not provide as much coverage as an insurance policy you buy through your own insurance agent].

If you have any questions, please contact us at (*contact information*).

H-19(A) Fixed Rate Mortgage Model Form

(Name of Creditor)
(Loan Originator Unique Identifier)

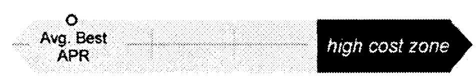
LOAN SUMMARY

Loan Amount:	**$_____**
Loan Term:	***(length of term)***
Loan Type and Features:	**Fixed Rate Mortgage** • [Includes [interest-only payments][step-payments]]
Total Settlement Charges:	**$_____** • [$_____ of these charges are already included in your loan amount above.] • [This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.]
[Prepayment Penalty:	Up to **$_____** if you pay off your loan, refinance, or sell this property within *(period)*.]

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges:

____% APR



How does this loan compare? For the week of *(date)*, the average APR on similar [but]conforming loans offered to applicants with excellent credit was ___%. Today, an APR of ___% or above is considered high cost and is usually available to applicants with poor credit history.

How much could I save by lowering my APR? For this loan, a __% reduction in the APR could save you an average of **$_____ each month.**

INTEREST RATE AND PAYMENT SUMMARY

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

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KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	No.
Can my monthly payment increase?	[No.][**YES.** Your payment can increase beginning in (*date*).]
Could I owe a prepayment penalty?	[No.][**YES.** If you pay off your loan, refinance, or sell your home within (***period***) you could pay a penalty of up to **$_____**.]

MORE INFORMATION ABOUT YOUR PAYMENTS

[Payment Change Limits]	[Your minimum payments due cannot increase more than ___% each (*period*) until (*description of recast event*). [When this happens][Beginning in (*period*)], you must make full monthly payments that cover all principal and interest owed on the loan.]
Escrow	[An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.][An escrow account is not required on this loan. You must pay your property taxes, homeowners, and other insurance on your own.]
[[Private]Mortgage Insurance]	[[Private]Mortgage Insurance [(PMI)] **is** required for this loan. It is included in your escrow.]
Total Payments	If you made all payments as scheduled, you would make (*number*) payments totaling $_____[, including estimated escrow]. Of this amount, $_____ would go to interest and settlement charges. This amount, and your amount financed of $_____, are used to calculate your APR.

➔ **You have no obligation to accept this loan.** [Your signature below only confirms that you have received this form.]

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ [If you borrow more than your home is worth, the interest on the extra amount may not be deductible for federal income tax purposes. Consult a tax advisor to find out whether the interest you pay is deductible.]

➔ **If you do not understand any part of this form, ask questions.** For more information, go to (*Web site of the Federal Reserve Board*).

H-19(B) Adjustable-Rate Mortgage Model Form

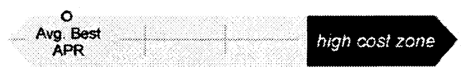
(Name of Creditor)
(Loan Originator Unique Identifier)

LOAN SUMMARY

Loan Amount:	**$_____**
Loan Term:	*(length of term)*
Loan Type and Features:	**[Step-Rate Mortgage][Adjustable Rate Mortgage]:** rate [is fixed for first (*period*), then] adjusts every (*frequency*).] • [Includes [interest-only payments][step-payments]]
Total Settlement Charges:	**$_____** • [$_____ of these charges are already included in your loan amount above.] • [This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.]
[Prepayment Penalty:	Up to **$_____** if you pay off your loan, refinance, or sell this property within (*period*).]

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges: **_____% APR**



How does this loan compare? For the week of (*date*), the average APR on similar [but] conforming loans offered to applicants with excellent credit was ____**%**. Today, an APR of ____**%** or above is considered high cost and is usually available to applicants with poor credit history.

How much could I save by lowering my APR? For this loan, a ___% reduction in the APR could save you an average of **$_____ each month**.

INTEREST RATE AND PAYMENT SUMMARY

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

KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	[No.][**YES.** Your interest rate can increase (***frequency***) beginning in (*date*).]
Can my monthly payment increase?	[No.][**YES.** Your payment can increase beginning in (*date*).]
Could I owe a prepayment penalty?	[No.][**YES.** If you pay off your loan, refinance, or sell your home within (***period***) you could pay a penalty of up to **$**_____.]

MORE INFORMATION ABOUT YOUR PAYMENTS

Rate Calculation	[When the (*length of time*) introductory period ends,] your rate will be determined (*frequency*) based on the (*identification of index*) (the market rate) plus ___%.]
[Rate Change Limits]	[When the (*length of time*) introductory period ends,] your interest rate can increase up to ___% from (*period*) to the next, and no more than ___% total for the life of the loan, which would result in a maximum ever rate of ___%.]
Escrow	[An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.][An escrow account is not required on this loan. You must pay your property taxes, homeowners, and other insurance on your own.]
[[Private]Mortgage Insurance]	[[Private] Mortgage Insurance [(PMI)] is required for this loan. It is included in your escrow.]
Total Payments	If [the market rate did not change and] you made all payments as scheduled, you would make (*number*) payments totaling $_____ [, including estimated escrow]. Of this amount, $_____ would go to interest and settlement charges. This amount, and your amount financed of $_____, are used to calculate your APR.

➔ **You have no obligation to accept this loan.** [Your signature below only confirms that you have received this form.]

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ [If you borrow more than your home is worth, the interest on the extra amount may not be deductible for federal income tax purposes. Consult a tax advisor to find out whether the interest you pay is deductible.]

➔ **If you do not understand any part of this form, ask questions.** For more information, go to (*Web site of the Federal Reserve Board*).

H-19(C) Mortgage with Negative Amortization Model Form

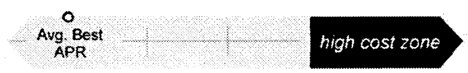
(Name of Creditor)
(Loan Originator Unique Identifier)

LOAN SUMMARY

Loan Amount	**$_____**
Loan Term:	***(length of term)***
Loan Type and Features:	**[Fixed Rate Mortgage][Step-Rate Mortgage][Adjustable Rate Mortgage]:** rate [is fixed for first (*period*), then] adjusts every (*frequency*).] • [includes [Step-Payments][Payment Options][Negative Amortization]]
Total Settlement Charges:	**$_____** • [$_____ of these charges are already included in your loan amount above.] • [This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.]
[Prepayment Penalty:	Up to **$_____** if you pay off your loan, refinance, or sell this property within (*period*).]

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges: **_____% APR**



How does this loan compare? For the week of (*date*), the average APR on similar [but]conforming loans offered to applicants with excellent credit was ___**%**. Today, an APR of ___**%** or above is considered high cost and is usually available to applicants with poor credit history.

How much could I save by lowering my APR? For this loan, a ___% reduction in the APR could save you an average of **$_____ each month.**

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.

KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	[No.] [**YES.** Your interest rate can increase (***frequency***) beginning in (*date*).]
Can my monthly payment increase?	[No.] [**YES.** Your [full] payment can increase beginning in (*date*). [Your minimum payment can increase beginning in (*date*).]]
Could I owe a prepayment penalty?	[No.][**YES.** If you pay off your loan, refinance, or sell your home within (***period***) you could pay a penalty of up to **$**_____.]

MORE INFORMATION ABOUT YOUR PAYMENTS

Rate Calculation	[When the (*length of time*) introductory period ends,] your rate will be determined (*frequency*) based on the (*identification of index*) (the market rate) plus ___%.]
[**Rate Change Limits**]	[When the (*period*) introductory period ends,] your interest rate can increase up to [___% from (*period*) to the next, and no more than ___% total][a maximum of __%] for the life of the loan[, which would result in a maximum ever rate of ___%].]
[Payment Change Limits]	Your minimum payments due [will increase][cannot increase more than] ___% each (*period*) until (*description of recast event*). [When this happens][Beginning in (*period*)], you must make full monthly payments that cover all principal and interest owed on the loan.]
Escrow	[An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.][An escrow account is not required on this loan. You must pay your property taxes, homeowners, and other insurance on your own.]
[[Private]Mortgage Insurance	[Private]Mortgage Insurance [(PMI)] **is** required for this loan. It is included in your escrow.]
Total Payments	If [the market rate did not change and] you made all payments as scheduled, you would make (*number*) payments totaling $_____ [, including estimated escrow]. Of this amount, $_____ would go to interest and settlement charges. This amount, and your amount financed of $_____, are used to calculate your APR.

➔ **You have no obligation to accept this loan.** [Your signature below only confirms that you have received this form.]

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ [If you borrow more than your home is worth, the interest on the extra amount may not be deductible for federal income tax purposes. Consult a tax advisor to find out whether the interest you pay is deductible.]

➔ **If you do not understand any part of this form, ask questions.** For more information, go to (*Web site of the Federal Reserve Board*).

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H-19(D) Fixed Rate Mortgage with Balloon Payment Sample

Jane Smith
1234 Main Street,
Anytown, ST 12345

March 26, 2009
XXX Bank
Loan Officer No. 12345-1234

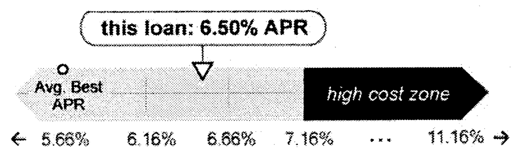
LOAN SUMMARY

Loan Amount:	**$210,000.00**
Loan Term:	**3 years**
Loan Type and Features:	**Fixed Rate Mortgage**
Total Settlement Charges:	**$7,472.00** • $3,000.00 of these charges are already included in your loan amount above. • This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges:

6.50% APR



How does this loan compare? For the week of March 23, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **5.66%**. Today, an APR of **7.16%** or above is considered high cost and is usually available to applicants with poor credit history.

How much could I save by lowering my APR? For this loan, a 1% reduction in the APR could save you an average of **$175 each month**.

INTEREST RATE AND PAYMENT SUMMARY

	Rate & Monthly Payment
Interest Rate	**5.50%**
Principal + Interest Payment	$1,192.36
Est. Taxes + Insurance (Escrow)	not included
Total Est. Monthly Payment	**$1,192.36**

Final Balloon Payment due March 2012: $202,217.84

Page 1 of 2

KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	No.
Can my monthly payment increase?	No.
Will I owe a balloon payment?	**YES.** You will owe a balloon payment of **$202,217.84**, due in March 2012.
Could I owe a prepayment penalty?	No.
Do I have to share any equity I gain?	**YES.** We are entitled to 50% of any gain you make when you sell or refinance this property.

MORE INFORMATION ABOUT YOUR PAYMENTS

Escrow	An escrow account is not required on this loan. You must pay your property taxes, homeowners, and other insurance on your own.
Total Payments	If you made all payments as scheduled, you would make 36 payments totaling $243,950.44. Of this amount, $39,530.44 would go to interest and settlement charges. This amount, and your amount financed of $204,420.00, are used to calculate your APR.

➔ **You have no obligation to accept this loan.** Your signature below only confirms that you have received this form.

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ If you borrow more than your home is worth, the interest on the extra amount may not be deductible for federal income tax purposes. Consult a tax advisor to find out whether the interest you pay is deductible.

➔ **If you do not understand any part of this form, ask questions.** For more information, go to www.xxx.gov.

Applicant's Signature **Date**

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H-19(E) Fixed Rate Mortgage with Interest Only Sample

Jane Smith
1234 Main Street
Anytown, ST 12345

February 26, 2009
XXX Bank
Loan Officer No. 12345-1234

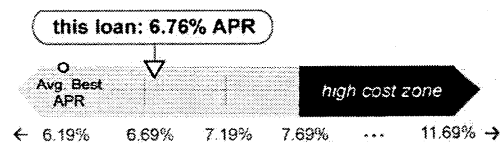
LOAN SUMMARY

Loan Amount:	**$200,000.00**
Loan Term:	**30 years**
Loan Type and Features:	**Fixed Rate Mortgage** • Includes interest-only payments
Total Settlement Charges:	**$7,654.00** • This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges:

6.76% APR



How does this loan compare? For the week of February 23, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **6.19%**. Today, an APR of **7.69%** or above is considered high cost and is usually offered to applicants with poor credit.

How much could I save by lowering my APR? For this loan, a 1% reduction in the APR could save you an average of **$132 each month.**

INTEREST RATE AND PAYMENT SUMMARY

	INTRODUCTORY Rate & Monthly Payment (for first 10 years)	MAXIMUM EVER (as early as 2019)
Interest Rate	**6.50%**	**6.50%**
Principal Payment	- none -	$407.82
Interest Payment	$1,083.33	$1,083.33
Est. Taxes + Insurance (Escrow)	$279.00	$279.00
Total Est. Monthly Payment	**$1,362. 33**	**$1,770.15**

KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	No.
Can my monthly payment increase?	**YES.** Your payment can increase beginning in April 2019.
Will any of my monthly payments be interest-only?	**YES.** Your monthly payments for the first 10 years of the loan cover the interest you owe each month, but **none** of the principal. Making these monthly payments means your loan amount will stay the same and you will be no closer to having it paid off.
Could I owe a prepayment penalty?	No.

MORE INFORMATION ABOUT YOUR PAYMENTS

Escrow	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
Total Payments	If you made all payments as scheduled, you would make 360 payments totaling $588,313.89, including estimated escrow. Of this amount, $293,757.89 would go to interest and settlement charges. This amount, and your amount financed of $194,116.00, are used to calculate your APR.

➔ **You have no obligation to accept this loan. Your signature below only confirms that you have received this form.**

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ **If you do not understand any part of this form, ask questions.** For more information, go to www.xxx.gov.

Applicant's Signature **Date**

Page 2 of 2

H-19(F) Step-Payment Mortgage Sample

Jane Smith
1234 Main Street,
Anytown, ST 12345

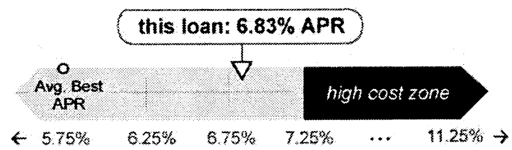
February 4, 2009
XXX Bank
Loan Officer No. 12345-1234

LOAN SUMMARY

Loan Amount:	**$200,000.00**
Loan Term:	**30 years**
Loan Type and Features:	**Fixed Rate Mortgage** • Includes Step-Payments • Includes Negative Amortization
Total Settlement Charges:	**$8,010.00** • This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges: **6.83% APR**



How does this loan compare? For the week of February 2, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **5.75%**. Today, an APR of **7.25%** or above is considered high cost and is usually available to applicants with poor credit history.

How much could I save by lowering my APR? For this loan, a 1% reduction in the APR could save you an average of **$138 each month**.

INTEREST RATE AND PAYMENT SUMMARY

All payments shown in the table include **$305** for estimated taxes and insurance (escrow).

	March 2009	March 2010 (1st adjustment)	March 2011 (2nd adjustment)	March 2017 + every month after
Interest Rate	6.5%	6.5%	6.5%	6.5%
Minimum Payment *Initial monthly payments cover no principal and only some interest and increase your loan amount.*	$1,318.37	$1,358.90	$1,401.06	$1,669.69

*You will borrow an additional **$1,286.87** by February 2011 if you make only minimum payments on this loan.*

Page 1 of 2

KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	No.
Can my monthly payment increase?	**YES.** Your payment can increase beginning in March 2010.
Even if I make my monthly payments, could my loan balance increase?	**YES.** Your minimum payment covers only part of the interest you owe each month and **none** of the principal. The unpaid interest will be added to your loan amount, which over time will increase the total amount you are borrowing and cause you to lose equity in your home.
Could I owe a prepayment penalty?	No.

MORE INFORMATION ABOUT YOUR PAYMENTS

Payment Change Limits	Your minimum payments due will increase 4% each year for the first 7 years. Beginning in year 8, you must make full monthly payments that cover all principal and interest owed on the loan.
Escrow	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
Total Payments	If you made all payments as scheduled, you would make 360 payments totaling $582,126.45, including estimated escrow. Of this amount, $279,444.45 would go to interest and settlement charges. This amount, and your amount financed of $192,882, are used to calculate your APR.

➔ **You have no obligation to accept this loan.** Your signature below only confirms that you have received this form.

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ If you borrow more than your home is worth, the interest on the extra amount may not be deductible for Federal income tax purposes. Consult a tax advisor to find out whether the interest you pay is deductible.

➔ **If you do not understand any part of this form, ask questions.** For more information, go to www.xxx.gov.

Applicant's Signature **Date**

H-19(G) Hybrid Adjustable-Rate Mortgage Sample

Jane Smith
1234 Main Street
Anytown, ST 12345

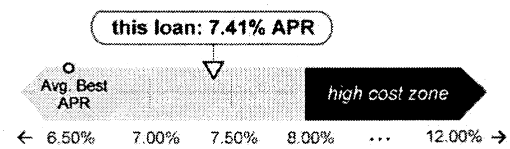
February 26, 2009
XXX Bank
Loan Officer No. 12345-1234

LOAN SUMMARY

Loan Amount:	**$200,000.00**
Loan Term:	**30 years**
Loan Type and Features:	**Adjustable Rate Mortgage:** rate is fixed for first 3 years, then adjusts every year.
Total Settlement Charges:	**$6,642.00** • $2,000.00 of these charges are already included in your loan amount above. • This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.
Prepayment Penalty:	Up to **$4,000.00** if you pay off your loan, refinance, or sell this property within 2 years.

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges: **7.41% APR**



How does this loan compare? For the week of February 23, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **6.50%**. Today, an APR of **8.00%** or above is considered high cost and is usually available to applicants with poor credit history.

How much could I save by lowering my APR? For this loan, a 1% reduction in the APR could save you an average of **$135 each month.**

INTEREST RATE AND PAYMENT SUMMARY

	INTRODUCTORY Rate & Monthly Payment (for first 3 years)	**MAXIMUM at FIRST ADJUSTMENT** (March 2012)	**MAXIMUM EVER** (as early as 2014)
Interest Rate	**5.625%**	**7.625%**	**11.625%**
Principal + Interest Payment	$1,151.31	$1,397.15	$1,924.97
Est. Taxes + Insurance (Escrow)	$241.00	$241.00	$241.00
Total Est. Monthly Payment	**$1,392.31**	**$1,638.15**	**$2,165.97**

Introductory Rate Notice
You have a discounted introductory rate of **5.625%** that ends after 3 years.
In the fourth year, even if market rates **do not** change, this rate will increase to **7.625%**.

Page 1 of 2

KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	**YES.** Your interest rate can increase **annually** beginning in March 2012.
Can my monthly payment increase?	**YES.** Your payment can increase beginning in March 2012.
Could I owe a prepayment penalty?	**YES.** If you pay off your loan, refinance, or sell your home within **2 years** you could pay a penalty of up to **$4,000**.

MORE INFORMATION ABOUT YOUR PAYMENTS

Rate Calculation	When the 3-year introductory period ends, your rate will be determined annually based on the one-year LIBOR index (the market rate) plus 2.125%.
Rate Change Limits	When the 3-year introductory period ends, your interest rate can increase up to 2.00% from one year to the next, and no more than 6.00% total for the life of the loan, which would result in a maximum ever rate of 11.625%.
Escrow	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
Total Payments	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling $585,778.09, including estimated escrow. Of this amount, $303,767.47 would go to interest and settlement charges. This amount, and your amount financed of $195,250.00, are used to calculate your APR.

➔ **You have no obligation to accept this loan.** Your signature below only confirms that you have received this form.

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ **If you do not understand any part of this form, ask questions.** For more information, go to www.xxx.gov.

Applicant's Signature **Date**

H-19(H) Adjustable-Rate Mortgage with Interest-Only Sample

Jane Smith
1234 Main Street
Anytown, ST 12345

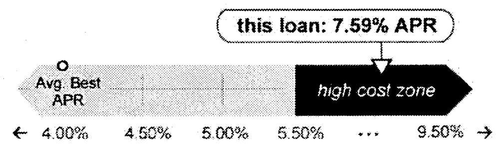
February 26, 2009
XXX Bank
Loan Officer No. 12345-1234

LOAN SUMMARY

Loan Amount:	**$200,000.00**
Loan Term:	**30 years**
Loan Type and Features:	**Adjustable Rate Mortgage:** rate is fixed for first 5 years, then adjusts every year. • includes interest-only payments
Total Settlement Charges:	**$8,625.00** • $2,000.00 of these charges are already included in your loan amount above. • This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.
Prepayment Penalty:	Up to **$4,000.00** if you pay off your loan, refinance, or sell this property within 2 years.

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges: **7.59% APR**



How does this loan compare? For the week of February 23, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **4.00%**. Today, an APR of **5.50%** or above is considered high cost and is usually available to applicants with poor credit history.

How much could I save by lowering my APR? For this loan, a 1% reduction in the APR could save you an average of **$133 each month.**

INTEREST RATE AND PAYMENT SUMMARY

	INTRODUCTORY Rate & Monthly Payment (for first 5 years)	**MAXIMUM at FIRST ADJUSTMENT** (April 2014)	**MAXIMUM EVER** (as early as 2016)
Interest Rate	**6.875%**	**8.875%**	**12.875%**
Principal Payment	-none-	$182.14	$116.64
Interest Payment	$1,145.83	$1,479.17	$2,101.91
Est. Taxes + Insurance (Escrow) • Includes Private Mortgage Insurance	$332.00	$332.00	$297.00
Total Est. Monthly Payment	**$1,477.83**	**$1,993.31**	**$2,515.55**

Introductory Rate Notice
You have a discounted introductory rate of **6.875%** that ends after 5 years.
In the sixth year, even if market rates do not change, this rate will increase to **7.00%**.

Page 1 of 2

KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	**YES.** Your interest rate can increase **annually** beginning in April 2014.
Can my monthly payment increase?	**YES.** Your payment can increase beginning in April 2014.
Will any of my monthly payments be interest-only?	**YES.** Your monthly payments for the first 5 years of the loan cover the interest you owe each month, but **none** of the principal. Making these monthly payments means your loan amount will stay the same and you will be no closer to having it paid off.
Could I owe a prepayment penalty?	**YES.** If you pay off your loan, refinance, or sell your home within **2 years** you could pay a penalty of up to **$4,000**.

MORE INFORMATION ABOUT YOUR PAYMENTS

Rate Calculation	When the 5-year introductory period ends, your rate will be determined annually based on the one-year LIBOR index (the market rate) plus 5.00%.
Rate Change Limits	When the 5-year introductory period ends, your interest rate can increase up to 2.00% from one year to the next, and no more than 6.00% total for the life of the loan, which would result in a maximum ever rate of 12.875%.
Escrow	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
Private Mortgage Insurance	Private Mortgage Insurance (PMI) **is** required for this loan. It is included in your escrow.
Total Payments	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling $589,385.69, including estimated escrow. Of this amount, $307,935.69 would go to interest and settlement charges. This amount, and your amount financed of $193,250.00, are used to calculate your APR.

➔ **You have no obligation to accept this loan. Your signature below only confirms that you have received this form.**

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ **If you do not understand any part of this form, ask questions.** For more information, go to www.xxx.gov.

Applicant's Signature **Date**

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H-19(I) Adjustable-Rate Mortgage with Payment Option Sample

Jane Smith
1234 Main Street,
Anytown, ST 12345

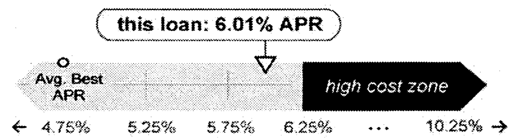
February 4, 2009
XXX Bank
Loan Officer No. 12345-1234

LOAN SUMMARY

Loan Amount:	**$200,000.00**
Loan Term:	**30 years**
Loan Type and Features:	**Adjustable Rate Mortgage**: rate is fixed for the first month, then adjusts every month. • includes Payment Options
Total Settlement Charges:	**$7,426.00** • $1,000.00 of these charges are already included in your loan amount above. • This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.

ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges: **6.01% APR**



How does this loan compare? For the week of February 2, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **4.75%**. Today, an APR of **6.25%** or above is considered high cost and is usually available to applicants with poor credit history.

How much could I save by lowering my APR? For this loan, a 1% reduction in the APR could save you an average of **$142 each month.**

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 10.5%** in the second month of this loan.

All payments shown in the table include **$280** for estimated taxes and insurance (escrow).

	March 2009 (1 month intro)	**April 2009** (1st adjustment)	**March 2010** (2nd adjustment)	**June 2011** + every month after
Maximum Interest Rate	**1.5%** (intro rate)	**10.5%**	**10.5%**	**10.5%** (max. ever)
Full Payment Option *Monthly payments cover all principal and interest.*	**$970.24**	**$2,106.18**	**$2,106.18**	**$2,106.18**
Minimum Payment Option *Initial monthly payments cover no principal and only some interest and increase your loan amount.*	$970.24	$970.24	$1,022.01	$2,402.54

*You will borrow an additional **$29,242.91** by June 2011 if you make only minimum payments on this loan.*

KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	**YES.** Your interest rate can increase **monthly** beginning in April 2009.
Can my monthly payment increase?	**YES.** Your full payment can increase beginning in April 2009. Your minimum payment can increase beginning in March 2010.
Will any of my monthly payments be interest-only?	**YES.** This loan gives you the choice to make monthly payments that cover the interest you owe each month, but **none** of the principal. Making these monthly payments means your loan amount will stay the same and you will be no closer to having it paid off.
Even if I make my monthly payments, could my loan balance increase?	**YES.** Your minimum payment covers only part of the interest you owe each month and **none** of the principal. The unpaid interest will be added to your loan amount, which over time will increase the total amount you are borrowing and cause you to lose equity in your home.
Could I owe a prepayment penalty?	No.

MORE INFORMATION ABOUT YOUR PAYMENTS

Rate Calculation	When the 1-month introductory period ends, your rate will be determined monthly based on the one-year LIBOR index (the market rate) plus 3.75%.
Rate Change Limits	When the 1-month introductory period ends, your interest rate can increase up to a maximum of 10.5% for the life of the loan.
Payment Change Limits	Your minimum payments due cannot increase more than 7.5% each year until the total loan amount has increased by 15%. When this happens, you must make full monthly payments that cover all principal and interest owed on the loan.
Escrow	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
Total Payments	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling $545,943.97, including estimated escrow. Of this amount, $251,893.97 would go to interest and settlement charges. This amount, and your amount financed of $193,250.00, are used to calculate your APR.

➔ **You have no obligation to accept this loan.** Your signature below only confirms that you have received this form.

➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.

➔ If you borrow more than your home is worth, the interest on the extra amount may not be deductible for Federal income tax purposes. Consult a tax advisor to find out whether the interest you pay is deductible.

➔ **If you do not understand any part of this form, ask questions.** For more information, go to www.xxx.gov.

Applicant's Signature **Date**

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BILLING CODE 6210–01–C

H–20—Balloon Payment Model Clause

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

H–21—Introductory Rate Model Clause

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

H–22—Key Questions About Risk Model Clauses

(a) Interest only feature

[Will any of my monthly payments be interest-only?]
[YES. Your (*frequency*) payments for the first (*period*) of the loan][This loan gives you the choice to make (*frequency*) payments that] cover the interest you owe each month, but none of the principal. Making these (*frequency*) payments means your loan amount will stay the same and you will be no closer to having it paid off.]

(b) Negative amortization feature

[Even if I make my monthly payments, could my loan balance increase?]

[YES. Your minimum payment covers only part of the interest you owe each (*period*) and none of the principal. The unpaid interest will be added to your loan amount, which over time will increase the total amount you are borrowing and cause you to lose equity in your home.]

(c) Balloon payment feature

[Will I owe a balloon payment?]

[YES. You will owe a balloon payment of $________, due in (*date of payment*).]

(d) Demand feature

[Can my lender demand full repayment at any time?]

[YES. We can demand that you pay off the full amount of your loan. We will give you at least (*period*) notice.]

(e) No-documentation or low-documentation feature

[Will my loan have a higher rate or fees because I did not document my employment, income or other assets?]

[YES. If you provide more documentation, you could decrease your interest rate or fees.]

(f) Shared-equity or shared-appreciation feature

[Do I have to share any equity I gain?]

[YES. We are entitled to ____% of any gain you make when you sell or refinance this property.]

H–23—Separate Disclosure Model Clauses

(a) Rebate

[If you pay off or refinance your loan, or sell this property early, you will receive a refund of some of the interest and fees you have paid on your loan.]

(b) Late Payment

[If you make a payment more than (*number of days*) days late, you may be charged a penalty equal to [$________][____%].]

(c) Property Insurance

[You may get property insurance from any insurer that is acceptable to us.]

(d) Contract Reference

Read your loan contract to find out what happens if you stop making payments, default, or pay off or refinance the loan early.

(e) Assumption Policy

[If you sell your home after you take out this loan, we may permit the new buyer to take over the payments on your mortgage.]◀

14. In Supplement I to Part 226, as amended on July 30, 2008 (73 FR 44604), and on January 29, 2009 (74 FR 5450):

A. Under *Section 226.2—Definitions and Rules of Construction, 2(a)(24) Residential mortgage transaction,* paragraphs 1, 2, and 5(ii) and 5(iii) are revised.

B. *Section 226.4—Finance Charge, Section 226.17—General Disclosure Requirements, Section 226.18—Content of Disclosures, Section 226.19—Certain Mortgage and Variable-Rate Transactions,* and *Section 226.20—Subsequent Disclosure Requirements* are revised.

C. Under *Section 226.24—Advertising, 24(c) Advertisement of rate of finance charge,* paragraph 4 is revised.

D. Under *Section 226.25—Record Retention, 25(a) General rule,* new paragraph 5 is added.

E. Under *Section 226.30—Limitation on Rates,* paragraph 1 is revised.

F. Under *Section 226.32—Requirements for Certain Closed-End Home Mortgages, 32(b) Definitions* is removed, *32(c) Disclosures,* paragraph 1 is removed, and *32(c)(5) Amount borrowed,* paragraph 1 is revised.

G. Under *Section 226.35—Prohibited Acts or Practices in Connection With Higher-Priced Mortgage Loans, 35(a) Higher-priced mortgage loans, Paragraph 35(a)(2),* paragraph 4 is revised and new paragraph 5 is added.

H. Under *Section 226.36—Prohibited Acts or Practices in Connection with Credit Secured by a Consumer's Principal Dwelling,* the heading is revised, *36(a) Mortgage broker defined,* the heading is revised, paragraph 1 is revised, and new paragraph 2 is added, *36(b) Misrepresentation of value of consumer's principal dwelling,* the heading is revised, and new *36(d) Prohibited payments to loan originators* and *36(e) Prohibition on steering* are added.

I. New *Section 226.37—Special Disclosure Requirements for Closed-End Mortgages* and *Section 226.38—Content of Disclosures for Closed-End Mortgages* are added.

J. Under Appendices G and H—Open-End and Closed-End Model Forms and Clauses, paragraphs 1 and 2 are revised.

K. Appendix H—Closed-End Model Forms and Clauses is revised.

Supplement I to Part 226—Official Staff Interpretations

* * * * *

SUBPART A—GENERAL

* * * * *

Section 226.2—Definitions and Rules of Construction

* * * * *

2(a)(24) Residential mortgage transaction.

1. *Relation to other sections.* This term is important in [five]▶three◀ provisions in the regulation:

i. Section 226.4(c)(7)—exclusions from the finance charge

ii. Section 226.15(f)—exemption from the right of rescission

[Section 226.18(q)—whether or not the obligation is assumable]

[Section 226.20(b)—disclosure requirements for assumptions]

iii. Section 226.23(f)—exemption from the right of rescission

2. *Lien status.* The definition is not limited to first-lien transactions. [For example, a consumer might assume a paid-down first mortgage (or borrow part of the purchase price) and borrow the balance of the purchase price from a creditor who takes a second mortgage. The second mortgage transaction is a ''residential mortgage transaction'' if the dwelling purchased is the consumer's principal residence.]

* * * * *

5. *Acquisition.* * * *

ii. Examples of new transactions involving a previously acquired dwelling include the financing of a balloon payment due under a land sale contract and an extension of credit made to a joint owner of property to buy out the other joint owner's interest. [In these instances, disclosures are not required under § 226.18(q (assumability policies). However, the]▶The◀ rescission rules of §§ 226.15 and 226.23 do apply to these new transactions.

[iii. In other cases, the disclosure and rescission rules do not apply. For example, where a buyer enters into a written agreement with the creditor holding the seller's mortgage, allowing the buyer to assume the mortgage, if the buyer had previously purchased the property and agreed with the seller to make the mortgage payments, § 226.20(b) does not apply (assumptions involving residential mortgages).]

* * * * *

§ 226.4—Finance Charge.

4(a) Definition.

1. *Charges in comparable cash transactions.* Charges imposed uniformly in cash and credit transactions are not finance charges. In determining whether an item is a finance charge, the creditor should compare the credit transaction in question with a similar cash transaction. A creditor financing the sale of property or services may compare charges with

those payable in a similar cash transaction by the seller of the property or service.

i. For example, the following items are not finance charges:

A. Taxes, license fees, or registration fees paid by both cash and credit customers.

B. Discounts that are available to cash and credit customers, such as quantity discounts.

C. Discounts available to a particular group of consumers because they meet certain criteria, such as being members of an organization or having accounts at a particular financial institution. This is the case even if an individual must pay cash to obtain the discount, provided that credit customers who are members of the group and do not qualify for the discount pay no more than the nonmember cash customers.

D. Charges for a service policy, auto club membership, or policy of insurance against latent defects offered to or required of both cash and credit customers for the same price.

ii. In contrast, the following items are finance charges:

A. Inspection and handling fees for the staged disbursement of construction-loan proceeds.

B. Fees for preparing a Truth in Lending disclosure statement, if permitted by law (for example, the Real Estate Settlement Procedures Act prohibits such charges in certain transactions secured by real property).

C. Charges for a required maintenance or service contract imposed only in a credit transaction.

iii. If the charge in a credit transaction exceeds the charge imposed in a comparable cash transaction, only the difference is a finance charge. For example:

A. If an escrow agent is used in both cash and credit sales of real estate and the agent's charge is $100 in a cash transaction and $150 in a credit transaction, only $50 is a finance charge.

2. *Costs of doing business.* Charges absorbed by the creditor as a cost of doing business are not finance charges, even though the creditor may take such costs into consideration in determining the interest rate to be charged or the cash price of the property or service sold. However, if the creditor separately imposes a charge on the consumer to cover certain costs, the charge is a finance charge if it otherwise meets the definition. For example:

i. A discount imposed on a credit obligation when it is assigned by a seller-creditor to another party is not a finance charge as long as the discount is not separately imposed on the consumer. (See § 226.4(b)(6).)

ii. A tax imposed by a State or other governmental body on a creditor is not a finance charge if the creditor absorbs the tax as a cost of doing business and does not separately impose the tax on the consumer. (For additional discussion of the treatment of taxes, see other commentary to § 226.4(a).)

3. *Forfeitures of interest.* If the creditor reduces the interest rate it pays or stops paying interest on the consumer's deposit account or any portion of it for the term of a credit transaction (including, for example, an overdraft on a checking account or a loan secured by a certificate of deposit), the interest lost is a finance charge. (See the commentary to § 226.4(c)(6).) For example:

i. A consumer borrows $5,000 for 90 days and secures it with a $10,000 certificate of deposit paying 15% interest. The creditor charges the consumer an interest rate of 6% on the loan and stops paying interest on $5,000 of the $10,000 certificate for the term of the loan. The interest lost is a finance charge and must be reflected in the annual percentage rate on the loan.

ii. However, the consumer must be entitled to the interest that is not paid in order for the lost interest to be a finance charge. For example:

A. A consumer wishes to buy from a financial institution a $10,000 certificate of deposit paying 15% interest but has only $4,000. The financial institution offers to lend the consumer $6,000 at an interest rate of 6% but will pay the 15% interest only on the amount of the consumer's deposit, $4,000. The creditor's failure to pay interest on the $6,000 does not result in an additional finance charge on the extension of credit, provided the consumer is entitled by the deposit agreement with the financial institution to interest only on the amount of the consumer's deposit.

B. A consumer enters into a combined time deposit/credit agreement with a financial institution that establishes a time deposit account and an open-end line of credit. The line of credit may be used to borrow against the funds in the time deposit. The agreement provides for an interest rate on any credit extension of, for example, 1%. In addition, the agreement states that the creditor will pay 0% interest on the amount of the time deposit that corresponds to the amount of the credit extension(s). The interest that is not paid on the time deposit by the financial institution is not a finance charge (and therefore does not affect the annual percentage rate computation).

4. *Treatment of transaction fees on credit card plans.* Any transaction charge imposed on a cardholder by a card issuer is a finance charge, regardless of whether the issuer imposes the same, greater, or lesser charge on withdrawals of funds from an asset account such as a checking or savings account. For example:

i. Any charge imposed on a credit cardholder by a card issuer for the use of an automated teller machine (ATM) to obtain a cash advance (whether in a proprietary, shared, interchange, or other system) is a finance charge regardless of whether the card issuer imposes a charge on its debit cardholders for using the ATM to withdraw cash from a consumer asset account, such as a checking or savings account.

ii. Any charge imposed on a credit cardholder for making a purchase or obtaining a cash advance outside the United States, with a foreign merchant, or in a foreign currency is a finance charge, regardless of whether a charge is imposed on debit cardholders for such transactions. The following principles apply in determining what is a foreign transaction fee and the amount of the fee:

A. Included are fees imposed when transactions are made in a foreign currency and converted to U.S. dollars; fees imposed when transactions are made in U.S. dollars outside the U.S.; and fees imposed when transactions are made (whether in a foreign currency or in U.S. dollars) with a foreign merchant, such as via a merchant's Web site. For example, a consumer may use a credit card to make a purchase in Bermuda, in U.S. dollars, and the card issuer may impose a fee because the transaction took place outside the United States.

B. Included are fees imposed by the card issuer and fees imposed by a third party that performs the conversion, such as a credit card network or the card issuer's corporate parent. (For example, in a transaction processed through a credit card network, the network may impose a 1 percent charge and the card-issuing bank may impose an additional 2 percent charge, for a total of a 3 percentage point foreign transaction fee being imposed on the consumer.)

C. Fees imposed by a third party are included only if they are directly passed on to the consumer. For example, if a credit card network imposes a 1 percent fee on the card issuer, but the card issuer absorbs the fee as a cost of doing business (and only passes it on to consumers in the general sense that the interest and fees are imposed on all its customers to recover its costs), then the fee is not a foreign transaction fee and need not be disclosed. In another example, if the credit card network imposes a 1 percent fee for a foreign transaction on the card issuer, and the card issuer imposes this same fee on the consumer who engaged in the foreign transaction, then the fee is a foreign transaction fee and a finance charge.

D. A card issuer is not required to disclose a fee imposed by a merchant. For example, if the merchant itself performs the currency conversion and adds a fee, this fee need not be disclosed by the card issuer. Under § 226.9(d), a card issuer is not obligated to disclose finance charges imposed by a party honoring a credit card, such as a merchant, although the merchant is required to disclose such a finance charge if the merchant is subject to the Truth in Lending Act and Regulation Z.

E. The foreign transaction fee is determined by first calculating the dollar amount of the transaction by using a currency conversion rate outside the card issuer's and third party's control. Any amount in excess of that dollar amount is a foreign transaction fee. Conversion rates outside the card issuer's and third party's control include, for example, a rate selected from the range of rates available in the wholesale currency exchange markets, an average of the highest and lowest rates available in such markets, or a government-mandated or government-managed exchange rate (or a rate selected from a range of such rates).

F. The rate used for a particular transaction need not be the same rate that the card issuer (or third party) itself obtains in its currency conversion operations. In addition, the rate used for a particular transaction need not be the rate in effect on the date of the transaction (purchase or cash advance).

5. *Taxes.*

i. Generally, a tax imposed by a State or other governmental body solely on a creditor is a finance charge if the creditor separately imposes the charge on the consumer.

ii. In contrast, a tax is not a finance charge (even if it is collected by the creditor) if applicable law imposes the tax:

A. Solely on the consumer;

B. On the creditor and the consumer jointly;

C. On the credit transaction, without indicating which party is liable for the tax; or

D. On the creditor, if applicable law directs or authorizes the creditor to pass the tax on to the consumer. (For purposes of this section, if applicable law is silent as to passing on the tax, the law is deemed not to authorize passing it on.)

iii. For example, a stamp tax, property tax, intangible tax, or any other State or local tax imposed on the consumer, or on the credit transaction, is not a finance charge even if the tax is collected by the creditor.

iv. In addition, a tax is not a finance charge if it is excluded from the finance charge by another provision of the regulation or commentary (for example, if the tax is imposed uniformly in cash and credit transactions).

►6. *Transactions with no seller.* In a transaction where there is no seller, such as a refinancing of an existing extension of credit described in § 226.20(a), there is no comparable cash transaction. Thus, the exclusion from the finance charge of charges of a type payable in a comparable cash transaction does not apply to such transactions.◄

4(a)(1) Charges by third parties.

1. *Choosing the provider of a required service.* An example of a third-party charge included in the finance charge is the cost of required mortgage insurance, even if the consumer is allowed to choose the insurer.

2. *Annuities associated with reverse mortgages.* Some creditors offer annuities in connection with a reverse-mortgage transaction. The amount of the premium is a finance charge if the creditor requires the purchase of the annuity incident to the credit. Examples include the following:

i. The credit documents reflect the purchase of an annuity from a specific provider or providers.

ii. The creditor assesses an additional charge on consumers who do not purchase an annuity from a specific provider.

iii. The annuity is intended to replace in whole or in part the creditor's payments to the consumer either immediately or at some future date.

4(a)(2) Special rule; closing agent charges.

1. *General.* This rule applies to charges by a third party serving as the closing agent for the particular loan. An example of a closing agent charge included in the finance charge is a courier fee where the creditor requires the use of a courier.

2. *Required closing agent.* If the creditor requires the use of a closing agent, fees charged by the closing agent are included in the finance charge only if the creditor requires the particular service, requires the imposition of the charge, or retains a portion of the charge. Fees charged by a third-party closing agent may be otherwise excluded from the finance charge under § 226.4. For example, a fee that would be paid in a comparable cash transaction may be excluded under § 226.4(a). A charge for conducting or attending a closing is a finance charge and may be excluded only if the charge is included in and is incidental to a lump-sum fee excluded under § 226.4(c)(7).

►3. *Closed-end mortgage transactions.* Comments 4(a)(2)–1 and 4(a)(2)–2 do not apply to closed-end transactions secured by real property or a dwelling, pursuant to § 226.4(g).◄

4(a)(3) Special rule; mortgage broker fees.

1. *General.* A fee charged by a mortgage broker is excluded from the finance charge if it is the type of fee that is also excluded when charged by the creditor. For example, to exclude an application fee from the finance charge under § 226.4(c)(1), a mortgage broker must charge the fee to all applicants for credit, whether or not credit is extended.

2. *Coverage.* This rule applies to charges paid by consumers to a mortgage broker in connection with a consumer credit transaction secured by real property or a dwelling.

3. *Compensation by lender.* The rule requires all mortgage broker fees to be included in the finance charge. Creditors sometimes compensate mortgage brokers under a separate arrangement with those parties. Creditors may draw on amounts paid by the consumer, such as points or closing costs, to fund their payment to the broker. Compensation paid by a creditor to a mortgage broker under an agreement is not included as a separate component of a consumer's total finance charge (although this compensation may be reflected in the finance charge if it comes from amounts paid by the consumer to the creditor that are finance charges, such as points and interest).

4(b) Examples of finance charges.

1. *Relationship to other provisions.* Charges or fees shown as examples of finance charges in § 226.4(b) may be excludable under § 226.4(c), (d), or (e). For example[:

i. Premiums]►, premiums◄ for credit life insurance, shown as an example of a finance charge under § 226.4(b)(7), may be excluded if the requirements of § 226.4(d)(1) are met. ►They may not be excluded, however, in transactions subject to § 226.4(g).◄

[ii. Appraisal fees mentioned in § 226.4(b)(4) are excluded for real property or residential mortgage transactions under § 226.4(c)(7).]

Paragraph 4(b)(2).

1. *Checking account charges.* A checking or transaction account charge imposed in connection with a credit feature is a finance charge under

§ 226.4(b)(2) to the extent the charge exceeds the charge for a similar account without a credit feature. If a charge for an account with a credit feature does not exceed the charge for an account without a credit feature, the charge is not a finance charge under § 226.4(b)(2). To illustrate:

i. A $5 service charge is imposed on an account with an overdraft line of credit (where the institution has agreed in writing to pay an overdraft), while a $3 service charge is imposed on an account without a credit feature; the $2 difference is a finance charge. (If the difference is not related to account activity, however, it may be excludable as a participation fee. See the commentary to § 226.4(c)(4).

ii. A $5 service charge is imposed for each item that results in an overdraft on an account with an overdraft line of credit, while a $25 service charge is imposed for paying or returning each item on a similar account without a credit feature; the $5 charge is not a finance charge.

Paragraph 4(b)(3).

1. *Assumption fees.* The assumption fees mentioned in § 226.4(b)(3) are finance charges only when the assumption occurs and the fee is imposed on the new buyer. The assumption fee is a finance charge in the new buyer's transaction.

Paragraph 4(b)(5).

1. *Credit loss insurance.* Common examples of the insurance against credit loss mentioned in § 226.4(b)(5) are mortgage guaranty insurance, holder in due course insurance, and repossession insurance. Such premiums must be included in the finance charge only for the period that the creditor requires the insurance to be maintained.

2. *Residual value insurance.* Where a creditor requires a consumer to maintain residual value insurance or where the creditor is a beneficiary of a residual value insurance policy written in connection with an extension of credit (as is the case in some forms of automobile balloon-payment financing, for example), the premiums for the insurance must be included in the finance charge for the period that the insurance is to be maintained. If a creditor pays for residual value insurance and absorbs the payment as a cost of doing business, such costs are not considered finance charges. (See comment 4(a)–2.)

Paragraphs 4(b)(7) and (b)(8).

1. *Pre-existing insurance policy.* The insurance discussed in § 226.4(b)(7) and (b)(8) does not include an insurance policy (such as a life or an automobile collision insurance policy) that is already owned by the consumer, even if the policy is assigned to or otherwise made payable to the creditor to satisfy an insurance requirement. Such a policy is not ''written in connection with'' the transaction, as long as the insurance was not purchased for use in that credit extension, since it was previously owned by the consumer.

2. *Insurance written in connection with a transaction.* Credit insurance sold before or after an open-end [(not home-secured)] plan is opened is considered ''written in connection with a credit transaction.'' Insurance sold after consummation in closed-end credit transactions [or after the opening of a home-equity plan subject to the requirements of § 226.5b] is not considered ''written in connection with'' the credit transaction if the insurance is written because of the consumer's default (for example, by failing to obtain or maintain required property insurance) or because the consumer requests insurance after consummation [or the opening of a home-equity plan subject to the requirements of § 226.5b] (although credit-sale disclosures may be required for the insurance sold after consummation if it is financed).

3. *Substitution of life insurance.* The premium for a life insurance policy purchased and assigned to satisfy a credit life insurance requirement must be included in the finance charge, but only to the extent of the cost of the credit life insurance if purchased from the creditor or the actual cost of the policy (if that is less than the cost of the insurance available from the creditor). If the creditor does not offer the required insurance, the premium to be included in the finance charge is the cost of a policy of insurance of the type, amount, and term required by the creditor.

4. *Other insurance.* Fees for required insurance not of the types described in § 226.4(b)(7) and (b)(8) are finance charges and are not excludable. For example:

i. The premium for a hospitalization insurance policy, if it is required to be purchased only in a credit transaction, is a finance charge.

Paragraph 4(b)(9).

1. *Discounts for payment by other than credit.* The discounts to induce payment by other than credit mentioned in § 226.4(b)(9) include, for example, the following situation:

i. The seller of land offers individual tracts for $10,000 each. If the purchaser pays cash, the price is $9,000, but if the purchaser finances the tract with the seller the price is $10,000. The $1,000 difference is a finance charge for those who buy the tracts on credit.

2. *Exception for cash discounts.*

i. Creditors may exclude from the finance charge discounts offered to consumers for using cash or another means of payment instead of using a credit card or an open-end plan. The discount may be in whatever amount the seller desires, either as a percentage of the regular price (as defined in section 103(z) of the act, as amended) or a dollar amount. Pursuant to section 167(b) of the act, this provision applies only to transactions involving an open-end credit plan or a credit card (whether open-end or closed-end credit is extended on the card). The merchant must offer the discount to prospective buyers whether or not they are cardholders or members of the open-end credit plan. The merchant may, however, make other distinctions. For example:

A. The merchant may limit the discount to payment by cash and not offer it for payment by check or by use of a debit card.

B. The merchant may establish a discount plan that allows a 15% discount for payment by cash, a 10% discount for payment by check, and a 5% discount for payment by a particular credit card. None of these discounts is a finance charge.

ii. Pursuant to section 171(c) of the act, discounts excluded from the finance charge under this paragraph are also excluded from treatment as a finance charge or other charge for credit under any State usury or disclosure laws.

3. *Determination of the regular price.*

i. The *regular price* is critical in determining whether the difference between the price charged to cash customers and credit customers is a *discount* or a *surcharge,* as these terms are defined in amended section 103 of the act. The *regular price* is defined in section 103 of the act as ''* * * the tag or posted price charged for the property or service if a single price is tagged or posted, or the price charged for the property or service when payment is made by use of an open-end credit plan or a credit card if either (1) no price is tagged or posted, or (2) two prices are tagged or posted * * *.''

ii. For example, in the sale of motor vehicle fuel, the tagged or posted price is the price displayed at the pump. As a result, the higher price (the open-end credit or credit card price) must be displayed at the pump, either alone or along with the cash price. Service station operators may designate separate pumps or separate islands as being for either cash or credit purchases and display only the appropriate prices at the various pumps. If a pump is capable of displaying on its meter either a cash or a credit price depending upon the consumer's means of payment, both the cash price and the credit price must be displayed at the pump. A service station operator may display the cash price of fuel by itself on a curb sign, as long as the sign clearly indicates that the price is limited to cash purchases.

4(b)(10) Debt cancellation and debt suspension fees.

1. *Definition.* Debt cancellation coverage provides for payment or satisfaction of all or part of a debt when a specified event occurs. The term ''debt cancellation coverage'' includes guaranteed automobile protection, or ''GAP,'' agreements, which pay or satisfy the remaining debt after property insurance benefits are exhausted. Debt suspension coverage provides for suspension of the obligation to make one or more payments on the date(s) otherwise required by the credit agreement, when a specified event occurs. The term ''debt suspension'' does not include loan payment deferral arrangements in which the triggering event is the bank's unilateral decision to allow a deferral of payment and the borrower's unilateral election to do so, such as by skipping or reducing one or more payments (''skip payments'').

2. *Coverage written in connection with a transaction.* Coverage sold after consummation in closed-end credit transactions [or after the opening of a home-equity plan subject to the requirements of § 226.5b] is not ''written in connection with'' the credit transaction if the coverage is written because the consumer requests coverage after consummation [or the opening of a home-equity plan subject to the requirements of § 226.5b] (although credit-sale disclosures may be required for the coverage sold after consummation if it is financed). Coverage sold before or after an open-end [(not home-secured)] plan is opened is considered ''written in connection with a credit transaction.''

4(c) Charges excluded from the finance charge.

Paragraph 4(c)(1).

1. *Application fees.* An application fee that is excluded from the finance charge is a charge to recover the costs associated with processing applications for credit. The fee may cover the costs of services such as credit reports, credit investigations, and appraisals. The creditor is free to impose the fee in only certain of its loan programs, such as ►automobile◄ [mortgage] loans. However, if the fee is to be excluded from the finance charge under § 226.4(c)(1), it must be charged to all applicants, not just to applicants who are approved or who actually receive credit.

Paragraph 4(c)(2).

1. *Late-payment charges.*

i. Late-payment charges can be excluded from the finance charge under § 226.4(c)(2) whether or not the person imposing the charge continues to extend credit on the account or continues to provide property or services to the consumer. In determining whether a charge is for actual unanticipated late payment on a 30-day account, for example, factors to be considered include:

A. The terms of the account. For example, is the consumer required by the account terms to pay the account balance in full each month? If not, the charge may be a finance charge.

B. The practices of the creditor in handling the accounts. For example, regardless of the terms of the account, does the creditor allow consumers to pay the accounts over a period of time without demanding payment in full or taking other action to collect? If no effort is made to collect the full amount due, the charge may be a finance charge.

ii. Section 226.4(c)(2) applies to late-payment charges imposed for failure to make payments as agreed, as well as failure to pay an account in full when due.

2. *Other excluded charges.* Charges for ''delinquency, default, or a similar occurrence'' include, for example, charges for reinstatement of credit privileges or for submitting as payment a check that is later returned unpaid.

Paragraph 4(c)(3).

1. *Assessing interest on an overdraft balance.* A charge on an overdraft balance computed by applying a rate of interest to the amount of the overdraft is not a finance charge, even though the consumer agrees to the charge in the account agreement, unless the financial institution agrees in writing that it will pay such items.

Paragraph 4(c)(4).

1. *Participation fees—periodic basis.* The participation fees described in § 226.4(c)(4) do not necessarily have to be formal membership fees, nor are they limited to credit card plans. The provision applies to any credit plan in which payment of a fee is a condition of access to the plan itself, but it does not apply to fees imposed separately on individual closed-end transactions. The fee may be charged on a monthly, annual, or other periodic basis; a one-time, nonrecurring fee imposed at the time an account is opened is not a fee that is charged on a periodic basis, and may not be treated as a participation fee.

2. *Participation fees—exclusions.* Minimum monthly charges, charges for nonuse of a credit card, and other charges based on either account activity or the amount of credit available under the plan are not excluded from the finance charge by § 226.4(c)(4). Thus, for example, a fee that is charged and then refunded to the consumer based on the extent to which the consumer uses the credit available would be a finance charge. (See the commentary to § 226.4(b)(2). Also, see comment 14(c)–2 for treatment of certain types of fees excluded in determining the annual percentage rate for the periodic statement.)

Paragraph 4(c)(5).

1. *Seller's points.* The seller's points mentioned in § 226.4(c)(5) include any charges imposed by the creditor upon the non-creditor seller of property for providing credit to the buyer or for providing credit on certain terms. These charges are excluded from the finance charge even if they are passed on to the buyer, for example, in the form of a higher sales price. Seller's points are frequently involved in real estate transactions guaranteed or insured by governmental agencies. A *commitment fee* paid by a non-creditor seller (such as a real estate developer) to the creditor should be treated as seller's points. Buyer's points (that is, points charged to the buyer by the creditor), however, are finance charges.

2. *Other seller-paid amounts.* Mortgage insurance premiums and other finance charges are sometimes paid at or before consummation or settlement on the borrower's behalf by a non-creditor seller. The creditor should treat the payment made by the seller as seller's points and exclude it from the finance charge if, based on the seller's payment, the consumer is not legally bound to the creditor for the charge. A creditor who gives disclosures before the payment has been made should base them on the best information reasonably available.

Paragraph 4(c)(6).

1. *Lost interest.* Certain federal and State laws mandate a percentage differential between the interest rate paid on a deposit and the rate charged on a loan secured by that deposit. In some situations, because of usury limits the creditor must reduce the interest rate paid on the deposit and, as a result, the consumer loses some of the interest that would otherwise have been earned. Under § 226.4(c)(6), such ''lost interest'' need not be included in the finance charge. This rule applies only to an interest reduction imposed because a rate differential is required by law and a usury limit precludes compliance by any other means. If the creditor imposes a differential that exceeds that required, only the lost interest attributable to the excess amount is a finance charge. (See the commentary to § 226.4(a).)

Paragraph 4(c)(7).

1. *[Real estate or residential mortgage transaction] ►Open-end real-property-secured credit◄charges.* The list of charges in § 226.4(c)(7) applies ►to open-end credit plans secured by real property and open-end residential mortgage transactions◄ [both to residential mortgage transactions (which may include, for example, the purchase of a mobile home) and to other transactions secured by real estate.] The fees are excluded from the finance charge even if the services for which the fees are imposed are performed by the creditor's employees rather than by a third party. In addition, the cost of verifying or confirming information connected to the item is also excluded. For example, credit-report fees cover not only the cost of the report but also the cost of verifying information in the report. In all cases, charges excluded under § 226.4(c)(7) must be bona fide and reasonable.

2. *Lump-sum charges.* If a lump sum charged for several services includes a charge that is not excludable, a portion of the total should be allocated to that service and included in the finance charge. However, a lump sum charged for conducting or attending a closing (for example, by a lawyer or a title company) is excluded from the finance charge if the charge is primarily for services related to items listed in § 226.4(c)(7) (for example, reviewing or completing documents), even if other incidental services such as explaining various documents or disbursing funds for the parties are performed. The entire charge is excluded even if a fee for the incidental services would be a finance charge if it were imposed separately.

3. *Charges assessed during the loan term.* ►Charges◄ [Real estate or residential mortgage transaction charges] excluded under § 226.4(c)(7) are those charges imposed solely in connection with the initial decision to grant credit. This would include, for example, a fee to search for tax liens on the property or to determine if flood insurance is required. The exclusion does not apply to fees for services to be performed periodically during the loan term, regardless of when the fee is collected. For example, a fee for one or more determinations during the loan term of the current tax-lien status or flood-insurance requirements is a finance charge, regardless of whether the fee is imposed at closing, or when the service is performed. If a creditor is uncertain about what portion of a fee to be paid at consummation or loan closing is related to the initial decision to grant credit, the entire fee may be treated as a finance charge.

4(d) Insurance and debt cancellation and debt suspension coverage.

1. *General.* Section 226.4(d) permits insurance premiums and charges and debt cancellation and debt suspension charges to be excluded from the finance charge. The required disclosures must be made in writing, except as provided in § 226.4(d)(4). The rules on location of insurance and debt cancellation and debt suspension disclosures for closed-end transactions are in § 226.17(a). For purposes of § 226.4(d), all references to insurance also include debt cancellation and debt suspension coverage unless the context indicates otherwise.

2. *Timing of disclosures.* If disclosures are given early, for example under § 226.17(f)[or § 226.19(a)], the creditor must redisclose if the actual premium is different at the time of consummation. If insurance disclosures are not given at the time of early disclosure and insurance is in fact written in connection with the transaction, the disclosures under § 226.4(d) must be made in order to exclude the premiums from the finance charge.

3. *Premium rate increases.* The creditor should disclose the premium amount based on the rates currently in effect and need not designate it as an estimate even if the premium rates may increase. An increase in insurance rates after consummation of a closed-end credit transaction or during the life of an open-end credit plan does not require redisclosure in order to exclude the additional premium from treatment as a finance charge.

4. *Unit-cost disclosures.*

i. *Open-end credit.* The premium or fee for insurance or debt cancellation or debt suspension for the initial term of coverage may be disclosed on a unit-cost basis in open-end credit transactions. The cost per unit should be based on the initial term of coverage, unless one of the options under comment 4(d)–12 is available.

ii. *Closed-end credit.* One of the transactions for which unit-cost disclosures (such as 50 cents per year for each $100 of the amount financed) may be used in place of the total insurance premium involves a particular kind of insurance plan. For example, a consumer with a current indebtedness of $8,000 is covered by a plan of credit life insurance coverage with a maximum of $10,000. The consumer requests an additional $4,000 loan to be covered by the same insurance plan. Since the $4,000 loan exceeds, in part, the maximum amount of indebtedness that can be covered by the plan, the creditor may properly give the insurance-cost disclosures on the $4,000 loan on a unit-cost basis.

5. *Required credit life insurance; debt cancellation or suspension coverage.* Credit life, accident, health, or loss-of-income insurance, and debt cancellation and suspension coverage described in § 226.4(b)(10), must be voluntary in order for the premium or charges to be excluded from the finance charge. Whether the insurance or coverage is in fact required or optional is a factual question. If the insurance or coverage is required, the premiums must be included in the finance charge, whether the insurance or coverage is purchased from the creditor or from a third party. If the consumer is required to elect one of several options—such as to purchase credit life insurance, or to assign an existing life insurance policy, or to pledge security such as a certificate of deposit—and the consumer purchases the credit life insurance policy, the premium must be included in the finance charge. (If the consumer assigns a preexisting policy or pledges security instead, no premium is included in the finance charge. The security interest would be disclosed under § 226.6(a)(4), § 226.6(b)(5)(ii), or § 226.18(m). See the commentary to § 226.4(b)(7) and (b)(8).)

6. *Other types of voluntary insurance.* Insurance is not credit life, accident, health, or loss-of-income insurance if the creditor or the credit account of the consumer is not the beneficiary of the insurance coverage. If the premium for such insurance is not imposed by the creditor as an incident to or a condition of credit, it is not covered by § 226.4.

7. *Signatures.* If the creditor offers a number of insurance options under § 226.4(d), the creditor may provide a means for the consumer to sign or initial for each option, or it may provide for a single authorizing signature or initial with the options selected designated by some other means, such as a check mark. The insurance authorization may be signed or initialed by any consumer, as defined in § 226.2(a)(11), or by an authorized user on a credit card account.

8. *Property insurance.* To exclude property insurance premiums or charges from the finance charge, the creditor must allow the consumer to choose the insurer and disclose that fact. This disclosure must be made whether or not the property insurance is available from or through the creditor. The requirement that an option be given does not require that the insurance be readily available from other sources. The premium or charge must be disclosed only if the consumer elects to purchase the insurance from ►or through◄ the creditor; in such a case, the creditor must also disclose the term of the property insurance coverage if it is less

than the term of the obligation. ►Insurance is available ''from or through a creditor'' if it is available from the creditor's affiliate, as defined under the Bank Holding Company Act, 12 U.S.C. 1841(k).◄

9. *Single-interest insurance.* Blanket and specific single-interest coverage are treated the same for purposes of the regulation. A charge for either type of single-interest insurance may be excluded from the finance charge if:

i. The insurer waives any right of subrogation.

ii. The other requirements of § 226.4(d)(2) are met. This includes, of course, giving the consumer the option of obtaining the insurance from a person of the consumer's choice. The creditor need not ascertain whether the consumer is able to purchase the insurance from someone else.

10. *Single-interest insurance defined.* The term *single-interest insurance* as used in the regulation refers only to the types of coverage traditionally included in the term *vendor's single-interest insurance* (or *VSI*), that is, protection of tangible property against normal property damage, concealment, confiscation, conversion, embezzlement, and skip. Some comprehensive insurance policies may include a variety of additional coverages, such as repossession insurance and holder-in-due-course insurance. These types of coverage do not constitute single-interest insurance for purposes of the regulation, and premiums for them do not qualify for exclusion from the finance charge under § 226.4(d). If a policy that is primarily VSI also provides coverages that are not VSI or other property insurance, a portion of the premiums must be allocated to the non-excludable coverages and included in the finance charge. However, such allocation is not required if the total premium in fact attributable to all of the non-VSI coverages included in the policy is $1.00 or less (or $5.00 or less in the case of a multiyear policy).

11. *Initial term.*

i. The initial term of insurance or debt cancellation or debt suspension coverage determines the period for which a premium amount must be disclosed, unless one of the options discussed under comment 4(d)–12 is available. For purposes of § 226.4(d), the initial term is the period for which the insurer or creditor is obligated to provide coverage, even though the consumer may be allowed to cancel the coverage or coverage may end due to nonpayment before that term expires.

ii. For example:

A. The initial term of a property insurance policy on an automobile that is written for one year is one year even though premiums are paid monthly and the term of the credit transaction is four years.

B. The initial term of an insurance policy is the full term of the credit transaction if the consumer pays or finances a single premium in advance.

12. *Initial term; alternative.*

i. *General.* A creditor has the option of providing cost disclosures on the basis of one year of insurance or debt cancellation or debt suspension coverage instead of a longer initial term (provided the premium or fee is clearly labeled as being for one year) if:

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

B. The consumer has agreed to pay a premium or fee that is assessed periodically but the consumer is under no obligation to continue the coverage, whether or not the consumer has made an initial payment.

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

iii. *Examples.* To illustrate:

A. A credit life insurance policy providing coverage for a ►seven-year automobile◄ [30-year mortgage] loan has an initial term of ►seven◄ [30] years, even though premiums are paid monthly and the consumer is not required to continue the coverage. Disclosures may be based on the initial term, but the creditor also has the option of making disclosures on the basis of coverage for an assumed initial term of one year.

13. *Loss-of-income insurance.* The loss-of-income insurance mentioned in § 226.4(d) includes involuntary unemployment insurance, which provides that some or all of the consumer's payments will be made if the consumer becomes unemployed involuntarily.

►14. *Age or employment eligibility criteria.* A premium or charge for credit life, accident, health, or loss-of-income insurance, or debt cancellation or debt suspension coverage is voluntary and can be excluded from the finance charge only if the consumer meets the product's age or employment eligibility criteria at the time of enrollment. To exclude such a premium or charge from the finance charge, the creditor must determine at the time of enrollment that the consumer is eligible for the product under the product's age or employment eligibility restrictions. The creditor may use reasonably reliable evidence of the consumer's age or employment status to satisfy this condition. Reasonably reliable evidence of a consumer's age would include using the date of birth on the consumer's credit application, on the driver's license or other government-issued identification, or on the credit report. Reasonably reliable evidence of a consumer's employment status would include the consumer's information on a credit application, an Internal Revenue Service Form W-2, tax returns, payroll receipts, or other evidence such as a letter or e-mail from the consumer or the consumer's employer. If the consumer does not meet the product's age or employment eligibility criteria at the time of enrollment, then the premium or charge is not voluntary. In such circumstances, the premium or charge is a finance charge. If the creditor offers a bundled product (such as credit life insurance combined with credit involuntary unemployment insurance) and the consumer is not eligible for all of the bundled products, then the creditor must either: (1) treat the entire premium or charge for the bundled product as a finance charge, or (2) offer the consumer the option of selecting only the products for which the consumer is eligible and exclude the premium or charge from the finance charge if the consumer chooses an optional product for which the consumer meets the age or employment eligibility criteria at the time of enrollment.◄

4(d)(3) Voluntary debt cancellation or debt suspension fees.

1. *General.* Fees charged for the specialized form of debt cancellation agreement known as guaranteed automobile protection (''GAP'') agreements must be disclosed according to § 226.4(d)(3) rather than according to § 226.4(d)(2) for property insurance.

2. *Disclosures.* Creditors can comply with § 226.4(d)(3) by providing a disclosure that refers to debt cancellation or debt suspension coverage whether or not the coverage is considered insurance. Creditors may use the model credit insurance disclosures only if the debt cancellation or debt suspension coverage constitutes insurance under State law. (See Model Clauses and Samples at G–16 and H–17 in Appendix G and Appendix H to part 226 for guidance on how to provide the disclosure required by § 226.4(d)(3)(iii) for debt suspension products.)

3. *Multiple events.* If debt cancellation or debt suspension coverage for two or more events is provided at a single charge, the entire charge may be excluded from the finance charge if at least one of the events is accident or loss

of life, health, or income and the conditions specified in § 226.4(d)(3) or, as applicable, § 226.4(d)(4), are satisfied.

4. *Disclosures in programs combining debt cancellation and debt suspension features.* If the consumer's debt can be cancelled under certain circumstances, the disclosure may be modified to reflect that fact. The disclosure could, for example, state (in addition to the language required by § 226.4(d)(3)(iii)) that ''In some circumstances, my debt may be cancelled.'' However, the disclosure would not be permitted to list the specific events that would result in debt cancellation.

4(d)(4) Telephone purchases.

1. *Affirmative request.* A creditor would not satisfy the requirement to obtain a consumer's affirmative request if the ''request'' was a response to a script that uses leading questions or negative consent. A question asking whether the consumer wishes to enroll in the credit insurance or debt cancellation or suspension plan and seeking a yes-or-no response (such as ''Do you want to enroll in this optional debt cancellation plan?'') would not be considered leading.

4(e) Certain security interest charges.

1. *Examples.*

i. *Excludable charges.* Sums must be actually paid to public officials to be excluded from the finance charge under § 226.4(e)(1) and (e)(3). Examples are charges or other fees required for filing or recording security agreements, mortgages ►(for open-end credit; but see § 226.4(g) regarding closed-end mortgage credit)◄, continuation statements, termination statements, and similar documents, as well as intangible property or other taxes even when the charges or fees are imposed by the state solely on the creditor and charged to the consumer (if the tax must be paid to record a security agreement). (See comment 4(a)–5 regarding the treatment of taxes, generally.)

ii. *Charges not excludable.* If the obligation is between the creditor and a third party (an assignee, for example), charges or other fees for filing or recording security agreements, mortgages, continuation statements, termination statements, and similar documents relating to that obligation are not excludable from the finance charge under this section.

2. *Itemization.* The various charges described in § 226.4(e)(1) and (e)(3) may be totaled and disclosed as an aggregate sum, or they may be itemized by the specific fees and taxes imposed. If an aggregate sum is disclosed, a general term such as security interest fees or filing fees may be used.

3. *Notary fees.* In order for a notary fee to be excluded under § 226.4(e)(1), all of the following conditions must be met:

i. The document to be notarized is one used to perfect, release, or continue a security interest.

ii. The document is required by law to be notarized.

iii. A notary is considered a public official under applicable law.

iv. The amount of the fee is set or authorized by law.

4. *Non-filing insurance.* The exclusion in § 226.4(e)(2) is available only if non-filing insurance is purchased. If the creditor collects and simply retains a fee as a sort of ''self-insurance'' against non-filing, it may not be excluded from the finance charge. If the non-filing insurance premium exceeds the amount of the fees excludable from the finance charge under § 226.4(e)(1), only the excess is a finance charge. For example:

i. The fee for perfecting a security interest is $5.00 and the fee for releasing the security interest is $3.00. The creditor charges $10.00 for non-filing insurance. Only $8.00 of the $10.00 is excludable from the finance charge.

4(f) Prohibited offsets.

1. *Earnings on deposits or investments.* The rule that the creditor shall not deduct any earnings by the consumer on deposits or investments applies whether or not the creditor has a security interest in the property.

►*4(g) Special rule; mortgage transactions.*

1. *Applicability of commentary to mortgages.* The staff commentary under §§ 226.4(a)(2) and 226.4(c) through (e) (other than that under §§ 226.4(c)(2), 226.4(c)(5), and 226.4(d)(2)) does not apply to closed-end transactions secured by real property or a dwelling. The staff commentary under §§ 226.4(a) (other than paragraph (2) of that section), 226.4(c)(2), 226.4(c)(5), and 226.4(d)(2), however, does apply to such transactions.

2. *Third-party charges.* Charges imposed by third parties are finance charges if they fit the general definition under § 226.4(a). Thus, if a third-party charge is payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to the extension of credit, it is a finance charge unless it would be payable in a comparable cash transaction. For example, appraisal and credit report fees are finance charges because they meet the definition in § 226.4(a). This test generally does not depend on whether the creditor requires the service for which the charge is imposed. In addition, charges imposed by closing agents required by the creditor, whether their own or those of third parties they retain, generally are finance charges unless otherwise excluded. (Note that § 226.4(a)(2) does not apply to closed-end transactions secured by real property or a dwelling, pursuant to § 226.4(g).) Insurance premiums generally are finance charges, whether imposed by a closing agent or another insurer, although premiums for property insurance are excluded if § 226.4(d)(2) is satisfied. Premiums for credit insurance (or fees for debt cancellation or debt suspension agreements) and premiums for lender's coverage under a title insurance policy are finance charges because they are imposed as an incident to the extension of credit. In contrast, premiums for owner's title insurance coverage are not finance charges because they are not imposed as an incident to the extension of credit.

3. *Charges in comparable cash transactions.* While the exclusions in § 226.4(c) through (e), other than §§ 226.4(c)(5) and 226.4(d)(2) are inapplicable to closed-end transactions secured by real property or a dwelling, charges in connection with such transactions that are payable in a comparable cash transaction are not finance charges. *See* comment 4(a)-1. For example, property taxes and fees or taxes imposed to record the deed evidencing transfer from the seller to the buyer of title to the property securing the transaction are not finance charges because they would be paid even if no credit were extended to finance the purchase. In contrast, fees or taxes imposed to record the mortgage, deed of trust, or other security instrument evidencing the creditor's security interest in the property securing the transaction are finance charges because they would not be incurred were it not for the extension of credit.

* * * * *

Subpart C—Closed-End Credit

§ 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, the disclosures must be legible, whether typewritten, handwritten, or printed by computer.

2. *Segregation of disclosures.* The disclosures may be grouped together and segregated from other information in a variety of ways. For example, the disclosures may appear on a separate sheet of paper or may be set off from other information on the contract or other documents:

[•]►i.◄ By outlining them in a box

[•]►ii.◄ By bold print dividing lines

[•]►iii.◄ By a different color background

[•]►iv.◄ By a different type style

[(The general segregation requirement described in this subparagraph does not apply to the disclosures required under §§ 226.19(b) and 226.20(c) although the disclosures must be clear and conspicuous.)]

3. *Location.* The regulation imposes no specific location requirements on the segregated disclosures. For example:

[•]►i.◄ They may appear on a disclosure statement separate from all other material.

[•]►ii.◄ They may be placed on the same document with the credit contract or other information, so long as they are segregated from that information.

[•]►iii.◄ They may be shown on the front or back of a document.

[•]►iv.◄ They need not begin at the top of a page.

[•]►v.◄ They may be continued from one page to another.

4. *Content of segregated disclosures.* Footnotes 37 and 38 contain exceptions to the requirement that the disclosures under § 226.18 be segregated from material that is not directly related to those disclosures. Footnote 37 lists the items that may be added to the segregated disclosures, even though not directly related to those disclosures. Footnote 38 lists the items required under § 226.18 that may be deleted from the segregated disclosures and appear elsewhere. Any one or more of these additions or deletions may be combined and appear either together with or separate from the segregated disclosures. The itemization of the amount financed under § 226.18(c), however, must be separate from the other segregated disclosures under § 226.18. If a creditor chooses to include the security interest charges required to be itemized under § 226.4(e) and § 226.18(o) in the amount financed itemization, it need not list these charges elsewhere.

5. *Directly Related.* ►Except in a transaction secured by real property or a dwelling, t◄[T]he segregated disclosures may, at the creditor's option, include any information that is directly related to those disclosures. ►(See the commentary to § 226.37(a)(2) for a discussion of directly related information for transactions secured by real property or a dwelling.)◄ The following is directly related information ►for a transaction not secured by real property or a dwelling◄:

i. A description of a grace period after which a late payment charge will be imposed. For example, the disclosure given under § 226.18(l) may state that a late charge will apply to ''any payment received more than 15 days after the due date.''

ii. A statement that the transaction is not secured. For example, the creditor may add a category labelled ''unsecured'' or ''not secured'' to the security interest disclosures given under § 226.18(m).

iii. The basis for any estimates used in making disclosures. For example, if the maturity date of a loan depends solely on the occurrence of a future event, the creditor may indicate that the disclosures assume that event will occur at a certain time.

iv. The conditions under which a demand feature may be exercised. For example, in a loan subject to demand after five years, the disclosures may state that the loan will become payable on demand in five years.

v. An explanation of the use of pronouns or other references to the parties to the transaction. For example, the disclosures may state, '''You' refers to the customer and 'we' refers to the creditor.''

vi. Instructions to the creditor or its employees on the use of a multiple-purpose form. For example, the disclosures may state, ''Check box if applicable.''

vii. A statement that the borrower may pay a minimum finance charge upon prepayment in a simple-interest transaction. For example, when State law prohibits penalties, but would allow a minimum finance charge in the event of prepayment, the creditor may make the § 226.18(k)(1) disclosure by stating, ''You may be charged a minimum finance charge.''

viii. A brief reference to negative amortization in variable-rate transactions. For example, in the variable-rate disclosures, the creditor may include a short statement such as ''Unpaid interest will be added to principal.'' (See the commentary to § 226.18(f)[(1)(iii)]►(3)◄.)

ix. A brief caption identifying the disclosures. For example, the disclosures may bear a general title such as ''Federal Truth in Lending Disclosures'' or a descriptive title such as ''Real Estate Loan Disclosures.''

x. A statement that a due-on-sale clause or other conditions on assumption are contained in the loan document. For example, the disclosure given under § 226.18(q) may state, ''Someone buying your home may, subject to conditions in the due-on-sale clause contained in the loan document, assume the remainder of the mortgage on the original terms.''

xi. If a State or Federal law prohibits prepayment penalties and excludes the charging of interest after prepayment from coverage as a penalty, a statement that the borrower may have to pay interest for some period after prepayment in full. The disclosure may state, for example, ''If you prepay your loan on other than the regular installment date, you may be assessed interest charges until the end of the month.''

xii. More than one hypothetical example under § 226.18(f)[(1)(iv)]►(4)◄ in transactions with more than one variable-rate feature. For example, in a variable-rate transaction with an option permitting consumers to convert to a fixed-rate transaction, the disclosures may include an example illustrating the effects of an increase resulting from conversion in addition to the example illustrating an increase resulting from changes in the index.

xiii. ►Reserved.◄[The disclosures set forth under section 226.18(f)(1) for variable-rate transactions subject to section 226.18(f)(2).]

xiv. ►[Reserved]◄[A statement whether or not a subsequent purchase of the property securing an obligation may be permitted to assume the remaining obligation on its original terms.]

xv. A late-payment fee disclosure under § 226.18(l) on a single payment loan.

xvi. The notice set forth in [§ 226.19(a)(4)]►§ 226.38(f)(1)◄, in a closed-end transaction not subject to § 226.19(a)(1)(i). In a mortgage transaction subject to § 19(a)(1)(i), the creditor must disclose the notice contained in [§ 226.19(a)(4)]►§ 226.38(f)(1)◄ grouped together with the disclosures made under [§ 226.18. *See* comment 19(a)(4)–1.]►§ 226.38.◄

6. *Multiple-purpose forms.* ►Except for transactions secured by real property or a dwelling, t◄[T]he creditor may design a disclosure statement that can be used for more than one type of transaction, so long as the required disclosures for individual transactions are clear and conspicuous. (See the Commentary to appendices G and H for a discussion of the treatment of disclosures that do not apply to specific transactions.) Any disclosure listed in § 226.18 (except the itemization of the amount financed under § 226.18(c)) may

be included on a standard disclosure statement even though not all of the creditor's transactions include those features. For example, the statement may include:

[•]►i.◄ The variable rate disclosure under § 226.18(f).

[•]►ii.◄ The demand feature disclosure under § 226.18(i).

[•]►iii.◄ A reference to the possibility of a security interest arising from a spreader clause, under § 226.18(m).

[• The assumption policy disclosure under § 226.18(q).]

[•]►iv.◄ The required deposit disclosure under § 226.18(r).

7. *Balloon payment financing with leasing characteristics.* In certain credit sale or loan transactions, a consumer may reduce the dollar amount of the payments to be made during the course of the transaction by agreeing to make, at the end of the loan term, a large final payment based on the expected residual value of the property. The consumer may have a number of options with respect to the final payment, including, among other things, retaining the property and making the final payment, refinancing the final payment, or transferring the property to the creditor in lieu of the final payment. Such transactions may have some of the characteristics of lease transactions subject to Regulation M, but are considered credit transactions where the consumer assumes the indicia of ownership, including the risks, burdens and benefits of ownership upon consummation. These transactions are governed by the disclosure requirements of this regulation instead of Regulation M. Creditors should not include in the segregated Truth in Lending disclosures additional information. Thus, disclosures should show the large final payment in the payment schedule and should not, for example, reflect the other options available to the consumer at maturity. ►For extensions of credit secured by real property or a dwelling, the large final payment in the payment schedule should be disclosed in accordance with the requirements under section 226.38(c), as applicable.◄

Paragraph 17(a)(2).

1. *When disclosures must be more conspicuous.* The following rules apply to the requirement that the terms *annual percentage rate* and *finance charge* be shown more conspicuously:

[•]►i.◄ The terms must be more conspicuous only in relation to the other required disclosures under § 226.18. For example, when the disclosures are included on the contract document, those 2 terms need not be more conspicuous as compared to the heading on the contract document or information required by State law.

[•]►ii.◄ The terms need not be more conspicuous except as part of the finance charge and annual percentage rate disclosures under § 226.18(d) and (e), although they may, at the creditor's option, be highlighted wherever used in the required disclosures. For example, the terms may, but need not, be highlighted when used in disclosing a prepayment penalty under § 226.18(k) or a required deposit under § 226.18(r).

[•]►iii.◄ The creditor's identity under § 226.18(a) may, but need not, be more prominently displayed than the finance charge and annual percentage rate.

[•]►iv.◄ The terms need not be more conspicuous than figures (including, for example, numbers, percentages, and dollar signs)

2. *Making disclosures more conspicuous.* The terms *finance charge* and *annual percentage rate* may be made more conspicuous in any way that highlights them in relation to the other required disclosures. For example, they may be:

[•]►i.◄ Capitalized when other disclosures are printed in capital and lower case.

[•]►ii.◄ Printed in larger type, bold print or different type face.

[•]►iii.◄ Printed in a contrasting color.

[•]►iv.◄ Underlined.

[•]►v.◄ Set off with asterisks.

17(b) Time of disclosures.

1. *Consummation.* As a general rule, disclosures must be made before "consummation" of the transaction. The disclosures ►for transactions not secured by real property or a dwelling◄ need not be given by any particular time before consummation[, except in certain mortgage transactions and variable-rate transactions secured by the consumer's principal dwelling with a term greater than one year under § 226.19.]► Pre-consummation disclosures for transactions secured by real property or a dwelling must be provided in accordance with the timing requirements in § 226.19.◄ (See the commentary to § 226.2(a)(13) regarding the definition of consummation.)

2. *Converting open-end to closed-end credit.* Except for home equity plans subject to § 226.5b in which the agreement provides for a repayment phase, if an open-end credit account is converted to a closed-end transaction under a written agreement with the consumer, the creditor must provide a set of closed-end credit disclosures before consummation of the closed-end transaction. (►See the commentary to § 226.19(a) for a discussion of disclosure timing requirements for closed-end transactions secured by real property or a dwelling.◄ See the commentary to § 226.19(b) for the timing rules for additional disclosures required upon the conversion to [a variable-rate transaction secured by a consumer's principal dwelling with a term greater than one year]►an adjustable-rate transaction secured by real property or a dwelling◄.) If consummation of the closed-end transaction occurs at the same time as the consumer enters into the open-end agreement, the closed-end credit disclosures may be given at the time of conversion. If disclosures are delayed until conversion and the closed-end transaction has a variable-rate feature, disclosures should be based on the rate in effect at the time of conversion. (See the commentary to § 226.5 regarding conversion of closed-end to open-end credit.)

3. *Disclosures provided on credit contracts.* Creditors must give the required disclosures to the consumer in writing, in a form that the consumer may keep, before consummation of the transaction. *See* § 226.17(a)(1) and (b). Sometimes the disclosures are placed on the same document with the credit contract. Creditors are not required to give the consumer two separate copies of the document before consummation, one for the consumer to keep and a second copy for the consumer to execute. The disclosure requirement is satisfied if the creditor gives a copy of the document containing the unexecuted credit contract and disclosures to the consumer to read and sign; and the consumer receives a copy to keep at the time the consumer becomes obligated. It is not sufficient for the creditor merely to show the consumer the document containing the disclosures before the consumer signs and becomes obligated. The consumer must be free to take possession of and review the document in its entirety before signing.

i. Example. To illustrate:

A. A creditor gives a consumer a multiple-copy form containing a credit agreement and TILA disclosures. The consumer reviews and signs the form and returns it to the creditor, who separates the copies and gives one copy to the consumer to keep. The creditor has satisfied the disclosure requirement.

17(c) Basis of disclosures and use of estimates.

[*Paragraph*]*17(c)(1)*►*Legal obligation*◄.

1. [*Legal obligation.*]►*General.*◄ The disclosures shall reflect the credit terms to which the parties are legally bound as of the outset of the transaction. In the case of disclosures required under

§ 226.20(c), the disclosures shall reflect the credit terms to which the parties are legally bound when the disclosures are provided. The legal obligation is determined by applicable State law or other law. ►The disclosures should be based on the assumption that the consumer will abide by the terms of the legal obligation throughout the term of the transaction. For example, the disclosures should be based on the assumption that the consumer makes payments on time and in full. In the case of an adjustable-rate mortgage described in § 226.38(a)(3)(i)(A), the creditor shall make the disclosure required by § 226.38(c) based on the assumption that the interest rate increases as fast as it can, taking into account any limitations on increases under the legal obligation.◄ (Certain transactions are specifically addressed in this commentary. See, for example, the discussion of buydown transactions elsewhere in the commentary to § 226.17(c).)

[•]►i.◄ The fact that a term or contract may later be deemed unenforceable by a court on the basis of equity or other grounds does not, by itself, mean that disclosures based on that term or contract did not reflect the legal obligation.

2. *Modification of obligation.* The legal obligation normally is presumed to be contained in the note or contract that evidences the agreement. But this presumption is rebutted if another agreement between the parties legally modifies that note or contract. If the parties informally agree to a modification of the legal obligation, the modification should not be reflected in the disclosures unless it rises to the level of a change in the terms of the legal obligation. For example:

[•]►i.◄ If the creditor offers a preferential rate, such as an employee preferred rate, the disclosures should reflect the terms of the legal obligation►, subject to special disclosure rules for transactions secured by real property or a dwelling in § 226.38(a)(3) and (c)◄. [(See the commentary to § 226.19(b) for an example of a preferred-rate transaction that is a variable-rate transaction.)]

[•]►ii.◄ If the contract provides for a certain monthly payment schedule but payments are made on a voluntary payroll deduction plan or an informal principal-reduction agreement, the disclosures should reflect the schedule in the contract.

[•]►iii.◄ If the contract provides for regular monthly payments but the creditor informally permits the consumer to defer payments from time to time, for instance, to take account of holiday seasons or seasonal employment, the disclosures should reflect the regular monthly payments.

►3. *Number of transactions.* Creditors have flexibility in handling credit extensions that may be viewed as multiple transactions. For example:

i. When a creditor finances the credit sale of a radio and a television on the same day, the creditor may disclose the sales as either 1 or 2 credit sale transactions.

ii. When a creditor finances a loan along with a credit sale of health insurance, the creditor may disclose in one of several ways: a single credit sale transaction, a single loan transaction, or a loan and a credit sale transaction.

iii. The separate financing of a downpayment in a credit sale transaction may, but need not, be disclosed as 2 transactions (a credit sale and a separate transaction for the financing of the downpayment).◄

[3. *Third-party buydown.*]►*17(c)(1)(i) Buydowns.*

1. *Third-party buydown.*◄ In certain transactions, a seller or other third party may pay an amount, either to the creditor or to the consumer, in order to reduce the consumer's payments or buy down the interest rate for all or a portion of the credit term. For example, a consumer and a bank agree to a mortgage with an interest rate of 15% and level payments over 25 years. By a separate agreement, the seller of the property agrees to subsidize the consumer's payments for the first 2 years of the mortgage, giving the consumer an effective rate of 12% for that period.

[•]►i.◄ If the lower rate is reflected in the credit contract between the consumer and the bank, the disclosures must take the buydown into account. For example, the annual percentage rate must be a composite rate that takes account of both the lower initial rate and the higher subsequent rate, and if the loan is not secured by real property or a dwelling, the payment schedule disclosures must reflect the 2 payment levels. However, the amount paid by the seller would not be specifically reflected in the disclosures given by the bank, since that amount constitutes seller's points and thus is not part of the finance charge.

[•]►ii.◄ If the lower rate is not reflected in the credit contract between the consumer and the bank and the consumer is legally bound to the 15% rate from the outset, the disclosures given by the bank must not reflect the seller buydown in any way. For example, the annual percentage rate and, in a transaction not secured by real property, the payment schedule, would not take into account the reduction in the interest rate and payment level for the first 2 years resulting from the buydown.

[4.]►2.◄ *Consumer buydowns.* In certain transactions, the consumer may pay an amount to the creditor to reduce the payments or obtain a lower interest rate on the transaction. Consumer buydowns must be reflected in the disclosures given for that transaction. To illustrate, in a mortgage transaction, the creditor and consumer agree to a note specifying a 14 percent interest rate. However, in a separate document, the consumer agrees to pay an amount to the creditor at consummation in return for a reduction in the interest rate to 12 percent for a portion of the mortgage term. The amount paid by the consumer may be deposited in an escrow account or may be retained by the creditor. Depending upon the buydown plan, the consumer's prepayment of the obligation may or may not result in a portion of the amount being credited or refunded to the consumer. In the disclosures given for the mortgage, the creditor must reflect the terms of the buydown agreement. For example:

[•]►i.◄ The amount paid by the consumer is a prepaid finance charge [(]►,◄ even if deposited in an escrow account[)]. ►(In transactions secured by real property or a dwelling, "finance charges" are referred to as "interest and settlement charges" under § 226.38(e)(5)(ii).)◄

[•]►ii.◄ A composite annual percentage rate must be calculated, taking into account both interest rates, as well as the effect of the prepaid finance charge.

[•]►iii.◄ The payment schedule must reflect the multiple payment levels resulting from a buydown►, in a transaction not secured by real property or a dwelling◄.

►3. *Lender buydown.*◄ The rules regarding consumer buydowns do not apply to transactions known as "lender buydowns." In lender buydowns. a creditor pays an amount (either into an account or to the party to whom the obligation is sold) to reduce the consumer's payments or interest rate for all or a portion of the credit term. Typically, these transactions are structured as a buydown of the interest rate during an initial period of the transaction with a higher than usual rate for the remainder of the term. The disclosures for lender buydowns should be based on the terms of the legal obligation between the consumer and the creditor. See comment [17(c)(1)–3]►17(c)(1)(i)–1◄ for the analogous rules concerning third-party buydowns.

[5.]►4.◄ *Split buydowns.* In certain transactions, a third party (such as a seller) and a consumer both pay an amount to the creditor to reduce the interest rate. The creditor must include the portion paid by the consumer in the finance charge and disclose the corresponding multiple payment levels and composite annual percentage rate. The portion paid by the third party and the corresponding reduction in interest rate, however, should not be reflected in the disclosures unless the lower rate is reflected in the credit contract. See the discussion on third-party and consumer buydown transactions [elsewhere in the commentary to § 226.17(c)]►in comments 17(c)(1)(i)–1 and 17(c)(1)(i)–2, respectively◄.

►*17(c)(1)(ii) Wrap-around financing.*◄

[6. *Wraparound financing.*]►1. *General.*◄ Wrap-around transactions, usually loans, involve the creditor's wrapping the outstanding balance on an existing loan and advancing additional funds to the consumer. The pre-existing loan, which is wrapped, may be to the same consumer or to a different consumer. In either case, the consumer makes a single payment to the new creditor, whom makes the payments on the pre-existing loan to the original creditor. Wrap-around loans or sales are considered new single-advance transactions, with an amount financed equaling the sum of the new funds advanced by the wrap creditor and the remaining principal owed to the original creditor on the pre-existing loan. In disclosing the itemization of the amount financed, the creditor may use a label such as ''the amount that will be paid to creditor X'' to describe the remaining principal balance on the pre-existing loan. This approach to Truth in Lending calculations has no effect on calculations required by other statutes, such as State usury laws.

[7.]►2.◄ *Wrap-around financing with balloon payments.* For wrap-around transactions involving a large final payment of the new funds before the maturity of the pre-existing loan, the amount financed is the sum of the new funds and the remaining principal on the pre-existing loan. The disclosures should be based on the shorter term of the wrap loan, with a large final payment of both the new funds and the total remaining principal on the pre-existing loan (although only the wrap loan will actually be paid off at that time).

►*17(c)(1)(iii) Variable- or adjustable-rate transactions.*◄

[8.]►1.◄ *Basis of disclosures* [*in variable-rate transactions*]. The disclosures for a variable-►or adjustable-◄ rate transaction must be given for the full term of the transaction and must be based on the terms in effect at the time of consummation. Creditors ►generally◄ should base the disclosures only on the initial rate and should not assume that this rate will increase ►(except as provided in § 226.38(c) for transactions secured by real property or a dwelling)◄. For example, in a ►a variable- or adjustable-rate◄ loan with an initial ►interest◄ rate of 10 percent and a 5 percentage points rate cap, creditors should base the disclosures on the initial rate and should not assume that the rate will increase 5 percentage points. However, in a variable-rate transaction with a seller buydown that is reflected in the credit contract, a consumer buydown, or a discounted or premium rate, disclosures should be a composite rate based on the rate in effect during the initial period and the rate that is the basis of the variable-rate feature for the remainder of the term. (See the commentary to section 226.17(c)►(1)◄ for a discussion of buydown, discounted, and premium transactions and the commentary to section 226.19(a)(2) for a discussion of [the] redisclosure in [certain mortgage transactions with a variable-rate] ►transactions secured by real property or a dwelling with an adjustable-rate◄ feature.

[9.]►2.◄ *Use of estimates in variable-►or adjustable-◄rate transactions.* The variable- ►or adjustable-◄ rate feature does not, by itself, make the disclosures estimates.

[10.]►3.◄ *Discounted and premium variable-►or adjustable-◄rate transactions.* In some variable-►or adjustable-◄rate transactions, creditors may set an initial interest rate that is not determined by the index or formula used to make later interest rate adjustments. Typically, this initial rate charged to consumers is lower than the rate would be if it were calculated using the index or formula. However, in some cases the initial rate may be higher. In a discounted transaction, for example, a creditor may calculate interest rates according to a formula using the six-month Treasury bill rate plus a 2 percent margin. If the Treasury bill rate at consummation is 10 percent, the creditor may forgo the 2 percent spread and charge only 10 percent for a limited time, instead of setting an initial rate of 12 percent.

i. When creditors use an initial interest rate that is not calculated using the index or formula for later rate adjustments, the disclosures should reflect a composite annual percentage rate based on the initial rate for as long as it is charged and, for the remainder of the term, the rate that would have been applied using the index or formula at the time of consummation. The interest rate at consummation 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 interest rate changes are based on the index value in effect 45 days before the ►interest rate◄ change date, creditors may use any index value in effect during the 45►-◄day period before consummation in calculating a composite annual percentage rate.

ii. The effect of the multiple rates must also be reflected in the calculation and disclosure of the finance charge, total of payments, and payment schedule. ►(In transactions secured by real property or a dwelling, creditors disclose the ''interest and settlement charges'' rather than the ''finance charge'' and the ''payment summary'' rather than the ''payment schedule.'' *See* § 226.38(c) and (e)(5).◄

iii. If a loan contains a rate or payment cap that would prevent the initial rate or payment, at the time of the first adjustment, from changing to the rate determined by the index or formula at consummation, the effect of that rate or payment cap should be reflected in the disclosures.

iv. Because these transactions involve irregular payment amounts, an annual percentage rate tolerance of [14]; of 1 percent applies, in accordance with § 226.22(a)(3).

v. Examples of discounted [variable]►adjustable◄-rate transactions ►secured by real property or a dwelling◄ include:

A. A 30-year loan for $100,000 with no prepaid [finance charges]►interest and settlement charges◄ and rates determined by the Treasury bill rate plus 2 percent. Rate and payment adjustments are made annually. Although the Treasury bill rate at the time of consummation is 10 percent, the creditor sets the interest rate for one year at 9 percent, instead of 12 percent according to the formula. The disclosures should reflect a composite annual percentage rate of 11.63 percent based on 9 percent for one year and 12 percent for 29 years. [Reflecting those two rate levels, the payment schedule should show 12 payments of $804.62 and 348 payments of $1,025.31.] The [finance charge]►interest and settlement charges◄ should be $266,463.32 and the total of payments $366,463.32.

B. Same loan as above, except with a 2 percent rate cap on periodic adjustments. The disclosures should reflect a composite annual percentage rate of 11.53 percent based on 9 percent for the first year, 11 percent for the second year, and 12 percent for the remaining 28 years. [Reflecting those three rate levels, the payment schedule should show 12 payments of $804.62, 12 payments of $950,09, and 336 payments of $365,234.76.] The [finance charge]►interest and settlement charges◄ should be $265,234.76 and the total of payments should be $365,234.76.

C. Same loan as above, except with a 7½; percent cap on payment adjustments. The disclosures should reflect a composite annual percentage rate of 11.64 percent, based on 9 percent for one year and 12 percent for 29 years. [Because of the payment cap, five levels of payments should be reflected.] The [finance charge]►interest and settlement charges◄ should be $277,040.60, and the total of payments $377,040.60.

vi. A loan in which the initial interest rate is set according to the index or formula used for later adjustments but is not set at the value of the index or formula at consummation is not a discounted or premium variable-►or adjustable-◄rate loan. For example, if a creditor commits to an initial rate based on the formula on a date prior to consummation, but the index has moved during the period between that time and consummation, a creditor should base its disclosures on the initial rate.

[11. *Examples of variable-rate transactions.*] ►4. *General.* In general, v◄[V]ariable-rate transactions include:

[•]►i.◄ Renewable balloon-payment instruments ►with a fixed interest rate◄ where the creditor is both unconditionally obligated to renew the balloon-payment loan at the consumer's option (or is obligated to renew subject to conditions within the consumer's control) and has the option of increasing the interest rate at the time of renewal. ►(However, a transaction secured by real property or a dwelling with a balloon payment and a fixed interest rate must be disclosed as a fixed-rate transaction under § 226.38(a)(3) whether or not the transaction is renewable.)◄ Disclosures must be based on the payment amortization (unless the specified term of the obligation with renewals is shorter) and on the rate in effect at the time of consummation of the transaction. (Examples of conditions within a consumer's control include requirements that a consumer be current in payments or continue to reside in the mortgaged property. In contrast, setting a limit on the rate at which the creditor would be obligated to renew or reserving the right to change the credit standards at the time of renewal are examples of conditions outside a consumer's control.) If, however, a creditor is not obligated to renew as described above, disclosures must be based on the term of the balloon-payment loan. Disclosures also must be based on the term of the balloon-payment loan in balloon-payment instruments in which the legal obligation provides that the loan will be renewed by a ''refinancing'' of the obligation, as that term is defined by § 226.20(a). If it cannot be determined from the legal obligation that the loan will be renewed by a ''refinancing,'' disclosures must be based either on the term of the balloon-payment loan or on the payment amortization, depending on whether the creditor is unconditionally obligated to renew the loan as described above. (This discussion does not apply to construction loans subject to § 226.17(c)(6).)

[• ''Shared-equity'' or ''shared-appreciation'' mortgages that have a fixed rate of interest and an appreciation share based on the consumer's equity in the mortgaged property, in a transaction not secured by real property or a dwelling. The appreciation share is payable in a lump sum at a specified time. Disclosures must be based on the fixed interest rate. (As discussed in the commentary to § 226.2, other types of shared-equity arrangements are not considered ''credit'' and are not subject to Regulation Z.)]

[•]►ii.◄ Preferred-rate loans where the terms of the legal obligation provide that the initial underlying rate is fixed but will increase upon the occurrence of some event, such as an employee leaving the employ of the creditor, and the note reflects the preferred rate. The disclosures are to be based on the preferred rate.

[• Graduated-payment mortgages and step-rate transactions without a variable-rate feature are not considered variable-rate transactions. ''Shared-equity'' or ''shared-appreciation'' mortgages are not considered variable-rate transactions.]

[•]►iii.◄ ''Price level adjusted mortgages'' or other indexed mortgages that have a fixed rate of interest but provide for periodic adjustments to payments and the loan balance to reflect changes in an index measuring prices or inflation. Disclosures are to be based on the fixed interest rate.

►5. *Not variable- or adjustable-rate transactions.* Graduated-payment mortgages and step-rate transactions without a variable-rate feature are not considered variable- or adjustable-rate transactions.◄

[12.]► 6.◄ *Graduated-payment adjustable-rate mortgage.* Graduated payment adjustable rate mortgages involve both [a variable]►an adjustable◄ interest rate and scheduled [variations]►adjustments◄ in payment amounts during the loan term. For example, under these plans, a series of graduated payments may be scheduled before rate adjustments affect payment amounts, or the initial scheduled payment may remain constant for a set period before rate adjustments affect the payment amount. In any case, the initial payment amount may be insufficient to cover the scheduled interest, causing negative amortization from the outset of the transaction. In these transactions, the disclosures should treat these features as follows:

[•]►i.◄ The finance charge includes the amount of negative amortization based on the assumption that the rate in effect at consummation remains unchanged.

[•]►ii.◄ The amount financed does not include the amount of negative amortization.

[•]►iii.◄ As in any variable- ►or adjustable-◄ rate transaction, the annual percentage rate is based on the terms in effect at consummation.

[• The schedule of payments discloses the amount of any scheduled initial payments followed by an adjusted level of payments based on the initial interest rate. Since some mortgage plans contain limits on the amount of the payment adjustment, the payment schedule in a transaction not secured by real property or a dwelling, or payment summary, in a transaction secured by real property or a dwelling may require several different levels of payments, even with the assumption that the original interest rate does not increase.]

[13.]►7.◄ *Growth-equity mortgages.* ►Growth-equity mortgages, a◄[A]lso referred to as payment-escalated mortgages, [these mortgage plans involve] scheduled payment increases to prematurely amortize the loan. The initial payment amount is determined as for a long-term loan with a fixed interest rate. Payment increases are scheduled periodically, based on changes in an index. The larger payments result in accelerated amortization of the loan. In disclosing these mortgage plans, creditors [may either—

• Estimate]►must estimate◄ the amount of payment increases, based on the best information reasonably available[, or

• Disclose by analogy to the variable-rate disclosures in section 226.18(f)(1)]. (This discussion does not apply to growth-equity mortgages in which the amount of payment increases can be accurately determined at the time of disclosure. For these mortgages, [as for graduated-payment mortgages,] disclosures should reflect the scheduled increases in payments.)

[14. *Reverse mortgages.*]►*17(c)(1)(iv) Repayment upon occurrence of future event.*◄

►1. *General.*◄ Reverse mortgages, also known as reverse annuity or home equity conversion mortgages, typically involve the disbursement of monthly advances to the consumer for a fixed period or until the occurrence of an event such as the consumer's death. Repayment of the loan (generally a single payment of principal and accrued interest) may be required to be made at the end of the disbursements or, for example, upon the death of the consumer. ►(However, a reverse mortgage is covered by § 226.33 only if the consumer's death is one of the conditions of repayment, as provided under § 226.33(a).)◄ In disclosing these transactions, creditors must apply the following rules, as applicable:

[•]►i.◄ If the reverse mortgage has a specified period for disbursements but repayment is due only upon the occurrence of a future event such as the death of the consumer, the creditor must assume that disbursements will be made until they are scheduled to end. The creditor must assume repayment will occur when disbursements end (or within a period following the final disbursement which is not longer than the regular interval between disbursements). This assumption should be used even though repayment may occur before or after the disbursements are scheduled to end. In such cases, the creditor may include a statement such as ''The disclosures assume that you will repay the loan at the time our payments to you end. As provided in your agreement, your repayment may be required at a different time.''

[•]►ii.◄ If the reverse mortgage has neither a specified period for disbursements nor a specified repayment date and these terms will be determined solely by reference to future events including the consumer's death, the creditor may assume that the disbursements will end upon the consumer's death (estimated by using actuarial tables, for example) and that repayment will be required at the same time (or within a period following the date of the final disbursement which is not longer than the regular interval for disbursements). Alternatively, the creditor may base the disclosures upon another future event it estimates will be most likely to occur first. (If terms will be determined by reference to future events which do not include the consumer's death, the creditor must base the disclosures upon the occur►r◄ence of the event estimated to be most likely to occur first.)

[•]►iii.◄ In making the disclosures, the creditor must assume that all disbursements and accrued interest will be paid by the consumer. For example, if the note has a nonrecourse provision providing that the consumer is not obligated for an amount greater than the value of the house, the creditor must nonetheless assume that the full amount to be disbursed will be repaid. In this case, however, the creditor may include a statement such as ''The disclosures assume full repayment of the amount advanced plus accrued interest, although the amount you may be required to pay is limited by your agreement.''

[•]►iv.◄ Some reverse mortgages provide that some or all of the appreciation in the value of the property will be shared between the consumer and the creditor. [Such loans are considered variable-rate mortgages, as described in comment 17(c)(1)–11, and the appreciation feature must be disclosed in accordance with § 226.18(f)(1). If the reverse mortgage has a variable interest rate, is written for a term greater than one year, and is secured by the consumer's principal dwelling, the shared appreciation feature must be described under § 226.19(b)(2)(vii).]►If the reverse mortgage has an adjustable interest rate and is secured by real property or a dwelling, the creditor must disclose the shared-equity or shared-appreciation feature as required by §§ 226.19(b)(3)(iii) and 226.38(d)(2)(iii).◄

[15. *Morris Plan transactions.* When a deposit account is created for the sole purpose of accumulating payments and then is applied to satisfy entirely the consumer's obligation in the transaction, each deposit made into the account is considered the same as a payment on a loan for purposes of making disclosures.

16. *Number of transactions.* Creditors have flexibility in handling credit extensions that may be viewed as multiple transactions. For example:

• When a creditor finances the credit sale of a radio and a television on the same day, the creditor may disclose the sales as either 1 or 2 credit sale transactions.

• When a creditor finances a loan along with a credit sale of health insurance, the creditor may disclose in one of several ways: a single credit sale transaction, a single loan transaction, or a loan and a credit sale transaction.

• The separate financing of a downpayment in a credit sale transaction may, but need not, be disclosed as 2 transactions (a credit sale and a separate transaction for the financing of the downpayment).]

[17. *Special rules for tax refund anticipation loans.*]►*17(c)(1)(v) Tax refund-anticipation loan.*◄

►1. *General.*◄ Tax refund loans, also known as refund anticipation loans (RALs), are transactions in which a creditor will lend up to the amount of a consumer's expected tax refund. RAL agreements typically require repayment upon demand, but also may provide that repayment is required when the refund is made. The agreements also typically provide that if the amount of the refund is less than the payment due, the consumer must pay the difference. Repayment often is made by a preauthorized offset to a consumer's account held with the creditor when the refund has been deposited by electronic transfer. Creditors may charge fees for RALs in addition to fees for filing the consumer's tax return electronically. In RAL transactions subject to the regulation the following special rules apply:

[•]►i.◄ If, under the terms of the legal obligation, repayment of the loan is required when the refund is received by the consumer (such as by deposit into the consumer's account), the disclosures should be based on the creditor's estimate of the time the refund will be delivered even if the loan also contains a demand clause. The practice of a creditor to demand repayment upon delivery of refunds does not determine whether the legal obligation requires that repayment be made at that time; this determination must be made according to applicable State or other law. (See comment 17(c)(5)–1 for the rules regarding disclosures if the loan is payable solely on demand or is payable either on demand or on an alternate maturity date.)

[•]►ii.◄ If the consumer is required to repay more than the amount borrowed, the difference is a finance charge unless excluded under § 226.4. In addition, to the extent that any fees charged in connection with the loan (such as for filing the tax return electronically) exceed those fees for a comparable cash transaction (that is, filing the tax return electronically without a loan), the difference must be included in the finance charge.

[18.]►*17(c)(1)(vi)*◄ *Pawn transactions.*

►1. *General.*◄ When, in connection with an extension of credit, a consumer pledges or sells an item to a pawnbroker creditor in return for a sum of money and retains the right to redeem the item for a greater sum (the redemption price) within a specified period of time, disclosures are required. In addition to other disclosure requirements that may be applicable under § 226.18, for purposes of pawn transactions:

i. The amount financed is the initial sum paid to the consumer. The pawnbroker creditor need not provide a separate itemization of the amount financed if that entire amount is paid directly to the consumer and the disclosed description of the amount financed is ''the amount of cash given directly to you'' or a similar phrase.

ii. The finance charge is the difference between the initial sum paid to the consumer and the redemption price plus any other finance charges paid in connection with the transaction. (See § 226.4.)

iii. The term of the transaction, for calculating the annual percentage rate, is the period of time agreed to by the pawnbroker creditor and the consumer. The term of the transaction does not include a grace period (including any statutory grace period) after the agreed redemption date.

Paragraph 17(c)(2)(i).

1. *Basis for estimates.* Disclosures may be estimated when the exact information is unknown at the time disclosures are made►, except that creditors may not provide estimated disclosures in disclosures required by § 226.19(a)(2)(ii) and (iii)◄. Information is unknown if it is not reasonably available to the creditor at the time the disclosures are made. The ''reasonably available'' standard requires that the creditor, acting in good faith, exercise due diligence in obtaining information. For example, the creditor must at a minimum utilize generally accepted calculation tools, but need not invest in the most sophisticated computer program to make a particular type of calculation. The creditor normally may rely on the representations of other parties in obtaining information. For example, the creditor might look to the consumer for the time of consummation, to insurance companies for the cost of insurance, or to realtors for taxes and escrow fees. The creditor may utilize estimates in making disclosures even though the creditor knows that more precise information will be available by the point of consummation. However, new disclosures may be required under § 226.17(f) or § 226.19.

2. *Labelling estimates.* Estimates must be designated as such in the segregated disclosures►, except that creditors may not provide estimated disclosures in the disclosures required by § 226.19(a)(2)(ii) and (iii)◄. Even though other disclosures are based on the same assumption on which a specific estimated disclosure was based, the creditor has some flexibility in labelling the estimates. Generally, only the particular disclosure for which the exact information is unknown is labelled as an estimate. However, when several disclosures are affected because of the unknown information, the creditor has the option of labelling either every affected disclosure or only the disclosure primarily affected. For example, when the finance charge is unknown because the date of consummation is unknown, the creditor must label the finance charge as an estimate and may also label as estimates the total of payments and the payment schedule. When many ►numerical◄ disclosures are estimates, the creditor may use a general statement, such as ''all numerical disclosures except the late payment disclosure are estimates,'' as a method to label those disclosures as estimates.

3. *Simple-interest transactions.* If consumers do not make timely payments in a simple-interest transaction, some of the amounts calculated for Truth in Lending disclosures will differ from amounts that consumers will actually pay over the term of the transaction. Creditors may label disclosures as estimates in these transactions[.]►except as otherwise provided by § 226.19(a)(2). (See the commentary on § 226.19(a)(2) for a discussion of circumstances where creditors may not disclose estimates for transactions secured by real property or a dwelling.)◄ For example, because the finance charge and total of payments may be larger than disclosed if consumers make late payments, creditors may label the finance charge and total of payments as estimates. On the other hand, creditors may choose not to label disclosures as estimates►. In all cases, creditors◄ [and] may base [all] disclosures on the assumption that payments will be made on time ►and in the amounts required by the terms of the legal obligation,◄ disregarding any possible [inaccuracies]►differences◄ resulting from consumers' payment patterns.

Paragraph 17(c)(2)(ii)

1. *Per diem interest.* This paragraph applies to any numerical amount (such as the finance charge, annual percentage rate, or payment amount) that is affected by the amount of the per-diem interest charge that will be collected at consummation. If the amount of per-diem interest used in preparing the disclosures for consummation is based on the information known to the creditor at the time the disclosure document is prepared, the disclosures are considered accurate under this rule, and affected disclosures are also considered accurate, even if the disclosures are not labeled as estimates. For example, if the amount of per-diem interest used to prepare disclosures is less than the amount of per-diem interest charged at consummation, and as a result the finance charge is understated by $200, the disclosed finance charge is considered accurate even though the understatement is not within the $100 tolerance of § 226.18(d)(1), and the finance charge was not labeled as an estimate. In this example, if in addition to the understatement related to the per-diem interest, a $90 fee is incorrectly omitted from the finance charge, causing it to be understated by a total of $290, the finance charge is considered accurate because the $90 fee is within the tolerance in § 226.18(d)(1).

Paragraph 17(c)(3)

1. *Minor variations.* Section 226.17(c)(3) allows creditors to disregard certain factors in calculating and making disclosures. For example:

[•]►i.◄ Creditors may ignore the effects of collecting payments in whole cents. Because payments cannot be collected in fractional cents, it is often difficult to amortize exactly an obligation with equal payments; the amount of the last payment may require adjustment to account for the rounding of the other payments to whole cents.

[•]►ii.◄ Creditors may base their disclosures on calculation tools that assume that all months have an equal number of days, even if their practice is to take account of the variations in months for purposes of collecting interest. For example, a creditor may use a calculation tool based on a 360-day year, when it in fact collects interest by applying a factor of 1/365 of the annual rate to 365 days. This rule does not, however, authorize creditors to ignore, for disclosure purposes, the effects of applying 1/360 of an annual rate to 365 days.

2. *Use of special rules.* A creditor may utilize the special rules in § 226.17(c)(3) for purposes of calculating and making all disclosures for a transaction or may, at its option, use the special rules for some disclosures and not others.

Paragraph 17(c)(4).

1. *Payment schedule irregularities.* When one or more payments in a transaction differ from the others because of a long or short first period, the variations may be ignored in disclosing the payment schedule,

finance charge, annual percentage rate, and other terms. For example:

[•]►i.◄ A 36-month auto loan might be consummated on June 8 with payments due on July 1 and the first of each succeeding month. The creditor may base its calculations on a payment schedule that assumes 36 equal intervals and 36 equal installment payments, even though a precise computation would produce slightly different amounts because of the shorter first period.

[•]►ii.◄ By contrast, in the same example, if the first payment were not scheduled until August 1, the irregular first period would exceed the limits in § 226.17(c)(4); the creditor could not use the special rule and could not ignore the extra days in the first period in calculating its disclosures.

2. *Measuring odd periods.* In determining whether a transaction may take advantage of the rule in § 226.17(c)(4), the creditor must measure the variation against a regular period. For purposes of that rule:

[•]►i.◄ The first period is the period from the date on which the finance charge begins to be earned to the date of the first payment.

[•]►ii.◄ The term is the period from the date on which the finance charge begins to be earned to the date of the final payment.

[•]►iii.◄ The regular period is the most common interval between payments in the transaction.

In transactions involving regular periods that are monthly, semimonthly or multiples of a month, the length of the irregular and regular periods may be calculated on the basis of either the actual number of days or an assumed 30-day month. In other transactions, the length of the periods is based on the actual number of days.

3. *Use of special rules.* A creditor may utilize the special rules in § 226.17(c)(4) for purposes of calculating and making some disclosures but may elect not to do so for all of the disclosures. For example, the variations may be ignored in calculating and disclosing the annual percentage rate but taken into account in calculating and disclosing the finance charge and payment schedule.

4. *Relation to prepaid finance charges.* Prepaid finance charges, including ''odd-days'' or ''per-diem'' interest, paid prior to or at closing may not be treated as the first payment on a loan. Thus, creditors may not disregard an irregularity in disclosing such finance charges.

Paragraph 17(c)(5).

1. *Demand disclosures.* Disclosures for demand obligations are based on an assumed 1-year term, unless an alternate maturity date is stated in the legal obligation. Whether an alternate maturity date is stated in the legal obligation is determined by applicable law. An alternate maturity date is not inferred from an informal principal reduction agreement or a similar understanding between the parties. However, when the note itself specifies a principal reduction schedule (for example, ''payable on demand or $2,000 plus interest quarterly''), an alternate maturity is stated and the disclosures must reflect that date. ►See §§ 226.19(b)(2)(ii)(D) and 226.38(d)(2)(iv) and associated commentary to determine how to disclose a demand feature for a transaction secured by real property or a dwelling.◄

2. *Future event as maturity date.* An obligation whose maturity date is determined solely by a future event, as for example, a loan payable only on the sale of property, is not a demand obligation. Because no demand feature is contained in the obligation, demand disclosures under § 226.18(i) are inapplicable. The disclosures should be based on the creditor's estimate of the time at which the specified event will occur, and ►in a transaction not secured by real property or a dwelling◄ may indicate the basis for the creditor's estimate, as noted in the commentary to § 226.17(a).

3. *Demand after stated period.* Most demand transactions contain a demand feature that may be exercised at any point during the term, but [certain transactions]►a transaction may◄ convert to demand status only after a fixed period. [For example, in States prohibiting due-on-sale clauses, the Federal National Mortgage Association (FNMA) requires mortgages that it purchases to include a call option rider that may be exercised after 7 years. These mortgages are generally written as long-term obligations, but contain a demand feature that may be exercised only within a 30-day period at 7 years.] The disclosures for [these transactions]►a transaction that converts to demand status after a fixed period◄ should be based upon the legally agreed-upon maturity date. Thus, ►for example,◄ if a mortgage containing [the 7-year FNMA call option] ►a call option the creditor may exercise during the first 30 days of the eighth year after loan origination◄ is written as a 20-year obligation, the disclosures should be based on the 20-year term, with the demand feature disclosed under [§ 226.18(i)]► § 226.38(d)(2)(iv)◄.

4. *Balloon mortgages.* Balloon payment mortgages, with payments based on a long-term amortization schedule and a large final payment due after a shorter term, are not demand obligations unless a demand feature is specifically contained in the contract. For example, a mortgage with a term of 5 years and a payment [schedule]►summary◄ based on 20 years would not be treated as a mortgage with a demand feature, in the absence of any contractual demand provisions. [In this type of mortgage, disclosures should be based on the 5-year term.]►(See § 226.38(c)(3) for requirements for interest rate and payment summary disclosures for balloon payment mortgages.)◄

Paragraph 17(c)(6).

1. *Series of advances.* Section 226.17(c)(6)(i) deals with a series of advances under an agreement to extend credit up to a certain amount. A creditor may treat all of the advances as a single transaction or disclose each advance as a separate transaction. If these advances are treated as 1 transaction and the timing and amounts of advances are unknown, creditors must make disclosures based on estimates, as provided in § 226.17(c)(2). If the advances are disclosed separately, disclosures must be provided before each advance occurs, with the disclosures for the first advance provided by consummation.

2. *Construction loans.* Section 226.17(c)(6)(ii) provides a flexible rule for disclosure of construction loans that may be permanently financed. These transactions have 2 distinct phases, similar to 2 separate transactions. The construction loan may be for initial construction or subsequent construction, such as rehabilitation or remodelling. The construction period usually involves several disbursements of funds at times and in amounts that are unknown at the beginning of that period, with the consumer paying only accrued interest until construction is completed. Unless the obligation is paid at that time, the loan then converts to permanent financing in which the loan amount is amortized just as in a standard mortgage transaction. Section 226.17(c)(6)(ii) permits the creditor to give either one combined disclosure for both the construction financing and the permanent financing, or a separate set of disclosures for the 2 phases. This rule is available whether the consumer is initially obligated to accept construction financing only or is obligated to accept both construction and permanent financing from the outset. If the consumer is obligated on both phases and the creditor chooses to give 2 sets of disclosures, both sets must be given to the consumer initially, because both

transactions would be consummated at that time. (Appendix D provides a method of calculating the annual percentage rate and other disclosures for construction loans, which may be used, at the creditor's option, in disclosing construction financing.)

3. *Multiple-advance construction loans.* Section 226.17(c)(6)(i) and (ii) are not mutually exclusive. For example, in a transaction that finances the construction of a dwelling that may be permanently financed by the same creditor, the construction phase may consist of a series of advances under an agreement to extend credit up to a certain amount. In these cases, the creditor may disclose the construction phase as either 1 or more than 1 transaction and also disclose the permanent financing as a separate transaction.

4. *Residential mortgage transaction.* See the commentary to § 226.2(a)(24) for a discussion of the effect of § 226.17(c)(6) on the definition of a residential mortgage transaction.

5. *Allocation of points.* When a creditor utilizes the special rule in § 226.17(c)(6) to disclose credit extensions as multiple transactions, buyers points or similar amounts imposed on the consumer must be allocated for purposes of calculating disclosures. While such amounts should not be taken into account more than once in making calculations, they may be allocated between the transactions in any manner the creditor chooses. For example, if a construction-permanent loan is subject to 5 points imposed on the consumer and the creditor chooses to disclose the 2 phases separately, the 5 points may be allocated entirely to the construction loan, entirely to the permanent loan, or divided in any manner between the two. However, the entire 5 points may not be applied twice, that is, to both the construction and the permanent phases.

17(d) Multiple creditors; multiple consumers.

1. *Multiple creditors.* If a credit transaction involves more than one creditor:

[•]►i.◄ The creditors must choose which of them will make the disclosures.

[•]►ii.◄ A single, complete set of disclosures must be provided, rather than partial disclosures from several creditors.

[•]►iii.◄ All disclosures for the transaction must be given, even if the disclosing creditor would not otherwise have been obligated to make a particular disclosure. For example, if one of the creditors is the seller, the total sale price disclosure under § 226.18(j) must be made, even though the disclosing creditor is not the seller.

2. *Multiple consumers.* When two consumers are joint obligors with primary liability on an obligation, the disclosures may be given to either one of them. If one consumer is merely a surety or guarantor, the disclosures must be given to the principal debtor. In rescindable transactions, however, separate disclosures must be given to each consumer who has the right to rescind under § 226.23, although the disclosures required under § 226.19(b) need only be provided to the consumer who expresses an interest in a variable-rate loan program.

17(e) Effect of subsequent events.

1. *Events causing inaccuracies.* Inaccuracies in disclosures are not violations if attributable to events occurring after the disclosures are made. [For example, when the consumer fails to fulfill a prior commitment to keep the collateral insured and the creditor then provides the coverage and charges the consumer for it, such a change does not make the original disclosures inaccurate.] The creditor may, however, be required to make new disclosures under § 226.17(f) or § 226.19 if the events occurred between disclosure and consummation or under § 226.20 if the events occurred after consummation.► For example, when the consumer fails to fulfill a prior commitment to keep the collateral insured and the creditor then provides the coverage and charges the consumer for it, such a change does not make the original disclosures inaccurate. However, the creditor would be required to provide the notice required under § 226.20(e).◄

17(f) Early disclosures.

1. *Change in rate or other terms.* Redisclosure is required for changes that occur between the time disclosures are made and consummation if the annual percentage rate in the consummated transaction exceeds the limits prescribed in this section, even if the [initial]►prior◄ disclosures would be considered accurate under the tolerances in § 226.18(d) or ►§◄ 226.22(a). To illustrate:

i. [*General.*]►*Non-mortgage loan.*◄ A. If disclosures are made in a regular transaction ►not secured by real property or a dwelling◄ on July 1, the transaction is consummated on July 15, and the actual annual percentage rate varies by more than ⅛ of 1 percentage point from the disclosed annual percentage rate, the creditor must either redisclose the changed terms or furnish a complete set of new disclosures before consummation. Redisclosure is required even if the disclosures made on July 1 are based on estimates and marked as such.

B. In a regular transaction ►not secured by real property or a dwelling◄, if early disclosures are marked as estimates and the disclosed annual percentage rate is within ⅛ of 1 percentage point of the rate at consummation, the creditor need not redisclose the changed terms (including the annual percentage rate).

[ii. *Nonmortgage loan.*]►C.◄ If disclosures ►for a transaction not secured by real property or a dwelling◄ are made on July 1, the transaction is consummated on July 15, and the finance charge increased by $35 but the disclosed annual percentage rate is within the permitted tolerance, the creditor must at least redisclose the changed terms that were not marked as estimates. (See § 226.18(d)(2) of this part.)

[iii.]►ii.◄ *Mortgage loan.* At the time [TILA disclosures]►the disclosures required by § 226.19(a)(2)(ii)◄ are prepared in July, the loan closing is scheduled for July 31 and the creditor does not plan to collect per-diem interest at consummation. Consummation actually occurs on August 5, and per-diem interest for the remainder of August is collected as a prepaid finance charge. [Assuming there were no other changes requiring redisclosure, t]►T◄he creditor may rely on the disclosures prepared in July that were accurate when they were prepared. However, if the creditor prepares new disclosures in August that will be provided at consummation, the new disclosures must take into account the amount of the per-diem interest known to the creditor at that time.

2. *Variable ►or adjustable◄ rate.* The addition of a variable ►or adjustable◄ rate feature to the credit terms, after early disclosures are given, requires new disclosures. ►(See § 226.19(a)(2) to determine when new disclosures are required for transactions secured by real property or a dwelling.◄

3. *Content of new disclosures.* ►Subject to § 226.19(a), i◄[I]f redisclosure is required ►in a transaction not secured by real property or a dwelling◄, the creditor has the option of either providing a complete set of new disclosures, or providing disclosures of only the terms that vary from those originally disclosed. ►If the creditor chooses to provide a complete set of new disclosures, the creditor may but need not highlight the new terms, provided that the disclosures comply with the format requirements of § 226.17(a). If the creditor chooses to disclose only the new terms, all the new

terms must be disclosed. For example, a different annual percentage rate will almost always produce a different finance charge, and often a new schedule of payments; all of these changes would have to be disclosed. If, in addition, unrelated terms such as the amount financed or prepayment penalty vary from those originally disclosed, the accurate terms must be disclosed. However, no new disclosures are required if the only differences involve estimates other than the annual percentage rate, and no variable rate feature has been added (see comment 17(f)-2). If a transaction is secured by real property or a dwelling, the creditor must provide a complete set of new disclosures in all cases, however.◀ (See the commentary to § 226.19(a)(2).)

4. *Special rules.* [In mortgage transactions subject to § 226.19, the creditor must redisclose if, between the delivery of the required early disclosures and consummation, the annual percentage rate changes by more than a stated tolerance.]▶Special disclosure timing and content requirements apply under § 226.19(a)(2) to disclosures provided before consummation for mortgage transactions secured by real property or a dwelling.◀ When subsequent events occur after consummation, new disclosures are required only if there is a refinancing or an assumption within the meaning of § 226.20.

Paragraph 17(f)(2).

1. *Irregular transactions.* For purposes of this paragraph, a transaction is deemed to be ''irregular'' according to the definition in footnote 46 of § 226.22(a)(3).

17(g) Mail or telephone orders—delay in disclosures.

1. *Conditions for use.* When the creditor receives a mail or telephone request for credit▶, except for extensions of credit covered by sections 226.19(a) and 226.19(b),◀ the creditor may delay making the disclosures until the first payment is due if the following conditions are met:

[•]▶i.◀ The credit request is initiated without face-to-face or direct telephone solicitation. (Creditors may, however, use the special rule when credit requests are solicited by mail.)

[•]▶ii.◀ The creditor has supplied the specified credit information about its credit terms either to the individual consumer or to the public generally. That information may be distributed through advertisements, catalogs, brochures, special mailers, or similar means.

2. *Insurance.* The location requirements for the insurance disclosures under § 226.18(n) permit them to appear apart from the other disclosures. Therefore, a creditor may mail an insurance authorization to the consumer and then prepare the other disclosures to reflect whether or not the authorization is completed by the consumer. Creditors may also disclose the insurance cost on a unit-cost basis, if the transaction meets the requirements of § 226.17(g).

17(h) Series of sales—delay in disclosures.

1. *Applicability.* The creditor may delay the disclosures for individual credit sales in a series of such sales until the first payment is due on the current sale, assuming the 2 conditions in this paragraph are met. If those conditions are not met, the general timing rules in [§ 266.17(b)] ▶§ 226.17(b)◀ apply.

2. *Basis of disclosures.* Creditors structuring disclosures for a series of sales under § 226.17(h) may compute the total sale price as either:

[•]▶i.◀ The cash price for the sale plus that portion of the finance charge and other charges applicable to that sale; or

[•]▶ii.◀ The cash price for the sale, other charges applicable to the sale, and the total finance charge and outstanding principal.

17(i) Interim student credit extensions.

1. *Definition.* Student credit plans involve extensions of credit for education purposes where the repayment amount and schedule are not known at the time credit is advanced. These plans include loans made under any student credit plan, whether government or private, where the repayment period does not begin immediately. (Certain student credit plans that meet this definition are exempt from Regulation Z. *See* § 226.3(f).) Creditors in interim student credit extensions need not disclose the terms set forth in this paragraph at the time the credit is actually extended but must make complete disclosures at the time the creditor and consumer agree upon the repayment schedule for the total obligation. At that time, a new set of disclosures must be made of all applicable items under § 226.18.

2. *Basis of disclosures.* The disclosures given at the time of execution of the interim note should reflect two annual percentage rates, one for the interim period and one for the repayment period. The use of § 226.17(i) in making disclosures does not, by itself, make those disclosures estimates. Any portion of the finance charge, such as statutory interest, that is attributable to the interim period and is paid by the student (either as a prepaid finance charge, periodically during the interim period, in one payment at the end of the interim period, or capitalized at the beginning of the repayment period) must be reflected in the interim annual percentage rate. Interest subsidies, such as payments made by either a State or the Federal government on an interim loan, must be excluded in computing the annual percentage rate on the interim obligation, when the consumer has no contingent liability for payment of those amounts. Any finance charges that are paid separately by the student at the outset or withheld from the proceeds of the loan are prepaid finance charges. An example of this type of charge is the loan guarantee fee. The sum of the prepaid finance charges is deducted from the loan proceeds to determine the amount financed and included in the calculation of the finance charge.

3. *Consolidation.* Consolidation of the interim student credit extensions through a renewal note with a set repayment schedule is treated as a new transaction with disclosures made as they would be for a refinancing. Any unearned portion of the finance charge must be reflected in the new finance charge and annual percentage rate, and is not added to the new amount financed. In itemizing the amount financed under § 226.18(c), the creditor may combine the principal balances remaining on the interim extensions at the time of consolidation and categorize them as the amount paid on the consumer's account.

4. *Approved student credit forms.* See the commentary to appendix H regarding disclosure forms approved for use in certain student credit programs.

§ 226.18—Content of Disclosures.

1. *As applicable.* ▶i.◀ The disclosures required by this section need be made only as applicable. Any disclosure not relevant to a particular transaction may be eliminated entirely. For example:

[•]▶A.◀ In a loan transaction, the creditor may delete disclosure of the total sale price.

[•]▶B.◀ In a credit sale requiring disclosure of the total sale price under § 226.18(j), the creditor may delete any reference to a downpayment where no downpayment is involved.

▶ii.◀ Where the amounts of several numerical disclosures are the same, the ''as applicable'' language also permits creditors to combine the terms, so long as it is done in a clear and conspicuous manner. For example:

[•]▶A.◀ In a transaction in which the amount financed equals the total of payments, the creditor may disclose ''amount financed/total of payments,'' together with descriptive language, followed by a single amount.

[•]►B.◄ However, if the terms are separated on the disclosure statement and separate space is provided for each amount, both disclosures must be completed, even though the same amount is entered in each space.

2. *Format.* See the commentary to § 226.17 and appendix H for a discussion of the format to be used in making these disclosures, as well as acceptable modifications.

18(a) Creditor.

1. *Identification of creditor.* The creditor making the disclosures must be identified. [This disclosure may, at the creditor's option, appear apart from the other disclosures.] Use of the creditor's name is sufficient, but the creditor may also include an address and/or telephone number. In transactions with multiple creditors, any one of them may make the disclosures; the one doing so must be identified.

18(b) Amount financed.

1. *Disclosure required.* The net amount of credit extended must be disclosed using the term amount financed and a descriptive explanation similar to the phrase in the regulation.

2. *Rebates and loan premiums.* In a loan transaction, the creditor may offer a premium in the form of cash or merchandise to prospective borrowers. Similarly, in a credit sale transaction, a seller's or manufacturer's rebate may be offered to prospective purchasers of the creditor's goods or services. ►Such premiums and rebates must be reflected in accordance with the terms of the legal obligation between the parties. *See* § 226.17(c)(1) and its commentary. Thus, if the creditor is legally obligated to provide the premium or rebate to the consumer as part of the credit transaction, the disclosures should reflect its value in the manner and at the time the creditor is obligated to provide it.◄ [At the creditor's option, these amounts may be either reflected in the Truth in Lending disclosures or disregarded in the disclosures. If the creditor chooses to reflect them in the § 226.18 disclosures, rather than disregard them, they may be taken into account in any manner as part of those disclosures.]

Paragraph 18(b)(1).

1. *Downpayments.* A downpayment is defined in § 226.2(a)(18) to include, at the creditor's option, certain deferred downpayments or pick-up payments. A deferred downpayment that meets the criteria set forth in the definition may be treated as part of the downpayment, at the creditor's option.

[•]►i.◄ Deferred downpayments that are not treated as part of the downpayment (either because they do not meet the definition or because the creditor simply chooses not to treat them as downpayments) are included in the amount financed.

[•]►ii.◄ Deferred downpayments that are treated as part of the downpayment are not part of the amount financed under § 226.18(b)(1).

Paragraph 18(b)(2).

1. *Adding other amounts.* Fees or other charges that are not part of the finance charge and that are financed rather than paid separately at consummation of the transaction are included in the amount financed. Typical examples are [real estate settlement charges and] premiums for voluntary credit life and disability insurance excluded from the finance charge under § 226.4. This paragraph does not include any amounts already accounted for under § 226.18(b)(1), such as taxes, tag and title fees, or the costs of accessories or service policies that the creditor includes in the cash price.

Paragraph 18(b)(3).

1. *Prepaid finance charges.* ►i.◄ Prepaid finance charges that are paid separately in cash or by check should be deducted under § 226.18(b)(3) in calculating the amount financed. To illustrate[• A]►, a◄ consumer applies for a loan of $2,500 with a $40 loan fee. The face amount of the note is $2,500 and the consumer pays the loan fee separately by cash or check at closing. The principal loan amount for purposes of § 226.18(b)(1) is $2,500 and $40 should be deducted under § 226.18(b(3), thereby yielding an amount financed of $2,460.

►ii.◄ In some instances, as when loan fees are financed by the creditor, finance charges are incorporated in the face amount of the note. Creditors have the option, when the charges are not add-on or discount charges, of determining a principal loan amount under § 226.18(b)(1) that either includes or does not include the amount of the finance charges. (Thus the principal loan amount may, but need not, be determined to equal the face amount of the note.) When the finance charges are included in the principal loan amount, they should be deducted as prepaid finance charges under § 226.18(b)(3). When the finance charges are not included in the principal loan amount, they should not be deducted under § 226.18(b)(3). The following examples illustrate the application of § 226.18(b) to this type of transaction. Each example assumes a loan request of $2,500 with a loan fee of $40; the creditor assesses the loan fee by increasing the face amount of the note to $2,540.

[•]►A.◄ If the creditor determines the principal loan amount under § 226.18(b)(1) to be $2,540, it has included the loan fee in the principal loan amount and should deduct $40 as a prepaid finance charge under § 226.18(b)(3), thereby obtaining an amount financed of $2,500.

[•]►B.◄ If the creditor determines the principal loan amount under § 226.18(b)(1) to be $2,500, it has not included the loan fee in the principal loan amount and should not deduct any amount under § 226.18(b)(3), thereby obtaining an amount financed of $2,500.

►iii.◄ The same rules apply when the creditor does not increase the face amount of the note by the amount of the charge but collects the charge by withholding it from the amount advanced to the consumer. To illustrate, the following examples assume a loan request of $2,500 with a loan fee of $40; the creditor prepares a note for $2,500 and advances $2,460 to the consumer.

[•]►A.◄ If the creditor determines the principal loan amount under § 226.18(b)(1) to be $2,500, it has included the loan fee in the principal loan amount and should deduct $40 as a prepaid finance charge under § 226.18(b)(3), thereby obtaining an amount financed of $2,460.

[•]►B.◄ If the creditor determines the principal loan amount under § 226.18(b)(1) to be $2,460, it has not included the loan fee in the principal loan amount and should not deduct any amount under § 226.18(b)(3), thereby obtaining an amount financed of $2,460.

►iv.◄ Thus in the examples where the creditor derives the net amount of credit by determining a principal loan amount that does not include the amount of the finance charge, no subtraction is appropriate. Creditors should note, however, that although the charges are not subtracted as prepaid finance charges in those examples, they are nonetheless finance charges and must be treated as such.

2. *Add-on or discount charges.* All finance charges must be deducted from the amount of credit in calculating the amount financed. If the principal loan amount reflects finance charges that meet the definition of a prepaid finance charge in § 226.2, those charges are included in the § 226.18(b)(1) amount and deducted under § 226.18(b)(3). However, if the principal loan amount includes finance charges that do not meet the definition of a prepaid finance charge, the § 226.18(b)(1) amount must exclude those finance charges. The following examples illustrate the application of § 226.18(b) to these types of transactions. Each example assumes a loan request of $1000 for 1 year, subject

to a 6 percent precomputed interest rate, with a $10 loan fee paid separately at consummation.

[•]►i.◄ The creditor assesses add-on interest of $60 which is added to the $1000 in loan proceeds for an obligation with a face amount of $1060. The principal for purposes of § 226.18(b)(1) is $1000, no amounts are added under § 226.18(b)(2), and the $10 loan fee is a prepaid finance charge to be deducted under § 226.18(b)(3). The amount financed is $990.

[•]►ii.◄ The creditor assesses discount interest of $60 and distributes $940 to the consumer, who is liable for an obligation with a face amount of $1000. The principal under § 226.18(b)(1) is $940, which results in an amount financed of $930, after deduction of the $10 prepaid finance charge under § 226.18(b)(3).

[•]►iii.◄ The creditor assesses $60 in discount interest by increasing the face amount of the obligation to $1060, with the consumer receiving $1000. The principal under § 226.18(b)(1) is thus $1000 and the amount financed $990, after deducting the $10 prepaid finance charge under § 226.18(b)(3).

18(c) Itemization of amount financed.

1. *Disclosure required.* ►i.◄ The creditor has 2 alternatives in complying with § 226.18(c):

[•]►A.◄ The creditor may inform the consumer, on the segregated disclosures, that a written itemization of the amount financed will be provided on request, furnishing the itemization only if the customer in fact requests it.

[•]►B.◄ The creditor may provide an itemization as a matter of course, without notifying the consumer of the right to receive it or waiting for a request.

►ii.◄ Whether given as a matter of course or only on request, the itemization must be provided at the same time as the other disclosures required by § 226.18, although separate from those disclosures.

2. *Additional information.* Section 226.18(c) establishes only a minimum standard for the material to be included in the itemization of the amount financed. Creditors have considerable flexibility in revising or supplementing the information listed in § 226.18(c) and shown in model form H–3, although no changes are required. The creditor may, for example, do one or more of the following:

i. Include amounts that reflect payments not part of the amount financed. For example, [escrow items and] certain insurance premiums may be included, ►even though they are neither part of the amount financed nor prepaid finance charges.◄ [as discussed in the commentary to § 226.18(g).]

ii. Organize the categories in any order. For example, the creditor may rearrange the terms in a mathematical progression that depicts the arithmetic relationship of the terms.

iii. Add categories. For example, in a credit sale, the creditor may include the cash price and the downpayment. If the credit sale involves a trade-in of the consumer's car and an existing lien on that car exceeds the value of the trade-in amount, the creditor may disclose the consumer's trade-in value, the creditor's payoff of the existing lien, and the resulting additional amount financed.

iv. Further itemize each category. For example, the amount paid directly to the consumer may be subdivided into the amount given by check and the amount credited to the consumer's savings account.

v. Label categories with different language from that shown in § 226.18(c). For example, an amount paid on the consumer's account may be revised to specifically identify the account as ''your auto loan with us.''

vi. Delete, leave blank, mark ''N/A,'' or otherwise ►note◄ [not] inapplicable categories in the itemization. For example, in a credit sale with no prepaid finance charges or amounts paid to others, the amount financed may consist of only the cash price less downpayment. In this case, the itemization may be composed of only a single category and all other categories may be eliminated.

3. *Amounts appropriate to more than one category.* When an amount may appropriately be placed in any of several categories and the creditor does not wish to revise the categories shown in § 226.18(c), the creditor has considerable flexibility in determining where to show the amount. For example[:] ►,◄ [•][I]►i◄ n a credit sale, the portion of the purchase price being financed by the creditor may be viewed as either an amount paid to the consumer or an amount paid on the consumer's account.

[4. *RESPA transactions.* The Real Estate Settlement Procedures Act (RESPA) requires creditors to provide a good faith estimate of closing costs and a settlement statement listing the amounts paid by the consumer. Transactions subject to RESPA are exempt from the requirements of § 226.18(c) if the creditor complies with RESPA's requirements for a good faith estimate and settlement statement. The itemization of the amount financed need not be given, even though the content and timing of the good faith estimate and settlement statement under RESPA differ from the requirements of §§ 226.18(c) and 226.19(a)(2). If a creditor chooses to substitute RESPA's settlement statement for the itemization when redisclosure is required under § 226.19(a)(2), the statement must be delivered to the consumer at or prior to consummation. The disclosures required by §§ 226.18(c) and 226.19(a)(2) may appear on the same page or on the same document as the good faith estimate or the settlement statement, so long as the requirements of § 226.17(a) are met.]

Paragraph 18(c)(1)(i).

1. *Amounts paid to consumer.* This encompasses funds given to the consumer in the form of cash or a check, including joint proceeds checks, as well as funds placed in an asset account. It may include money in an interest-bearing account even if that amount is considered a required deposit under § 226.18(r). For example, in a transaction with total loan proceeds of $500, the consumer receives a check for $300 and $200 is required by the creditor to be put into an interest-bearing account. Whether or not the $200 is a required deposit, it is part of the amount financed. At the creditor's option, it may be broken out and labeled in the itemization of the amount financed.

Paragraph 18(c)(1)(ii).

1. *Amounts credited to consumer's account.* The term consumer's account refers to an account in the nature of a debt with that creditor. It may include, for example, an unpaid balance on a prior loan, a credit sale balance or other amounts owing to that creditor. It does not include asset accounts of the consumer such as savings or checking accounts.

Paragraph 18(c)(1)(iii).

1. *Amounts paid to others.* This includes, for example, tag and title fees; amounts paid to insurance companies for insurance premiums; security interest fees, and amounts paid to credit bureaus, appraisers or public officials. When several types of insurance premiums are financed, they may, at the creditor's option, be combined and listed in one sum, labeled ''insurance'' or similar term. This includes, but is not limited to, different types of insurance premiums paid to one company and different types of insurance premiums paid to different companies. Except for insurance companies and other categories noted in footnote 41, third parties must be identified by name.

2. *Charges added to amounts paid to others.* A sum is sometimes added to the amount of a fee charged to a consumer for a service provided by a third party (such as for an extended warranty or a

service contract) that is payable in the same amount in comparable cash and credit transactions. In the credit transaction, the amount is retained by the creditor. Given the flexibility permitted in meeting the requirements of the amount financed itemization (see the commentary to § 226.18(c)), the creditor in such cases may reflect that the creditor has retained a portion of the amount paid to others. For example, the creditor could add to the category ''amount paid to others'' language such as ''(we may be retaining a portion of this amount).''

Paragraph 18(c)(1)(iv).

1. *Prepaid finance charge.* Prepaid finance charges that are deducted under § 226.18(b)(3) must be disclosed under this section. The prepaid finance charges must be shown as a total amount but may, at the creditor's option, also be further itemized and described. All amounts must be reflected in this total, even if portions of the prepaid finance charge are also reflected elsewhere. For example, if at consummation the creditor collects interim interest of $30 and a credit report fee of $10, a total prepaid finance charge of $40 must be shown. At the creditor's option, the credit report fee paid to a third party may also be shown elsewhere as an amount included in § 226.18(c)(1)(iii). The creditor may also further describe the 2 components of the prepaid finance charge, although no itemization of this element is required by § 226.18(c)(1)(iv).

[2. *Prepaid mortgage insurance premiums.* RESPA requires creditors to give consumers a settlement statement disclosing the costs associated with mortgage loan transactions. Included on the settlement statement are mortgage insurance premiums collected at settlement, which are prepaid finance charges. In calculating the total amount of prepaid finance charges, creditors should use the amount for mortgage insurance listed on the line for mortgage insurance on the settlement statement (line 1002 on HUD–1 or HUD 1–A), without adjustment, even if the actual amount collected at settlement may vary because of RESPA's escrow accounting rules. Figures for mortgage insurance disclosed in conformance with RESPA shall be deemed to be accurate for purposes of Regulation Z.]

18(d) Finance charge.

1. *Disclosure required.* The creditor must disclose the finance charge as a dollar amount, using the term ''finance charge,'' and must include a brief description similar to that in § 226.18(d). The creditor may, but need not, further modify the descriptor for variable rate transactions with a phrase such as ''which is subject to change.'' The finance charge must be shown on the disclosures only as a total amount; the elements of the finance charge must not be itemized in the segregated disclosures, although the regulation does not prohibit their itemization elsewhere.

[2. [Reserved]]

[18(d)(2) Other Credit]

[1]►2◄. *Tolerance.* When a finance-charge error results in a misstatement of the amount financed, or some other dollar amount for which the regulation provides no specific tolerance, the misstated disclosure does not violate the act or the regulation if the finance-charge error is within the permissible tolerance in this paragraph.

18(e) Annual percentage rate.

1. *Disclosure required.* The creditor must disclose the cost of the credit as an annual rate, using the term ''annual percentage rate,'' plus a brief descriptive phrase comparable to that used in § 226.18(e). For variable rate transactions, the descriptor may be further modified with a phrase such as ''which is subject to change.'' Under § 226.17(a), the terms ''annual percentage rate'' and ''finance charge'' must be more conspicuous than the other required disclosures.

2. *Exception.* [Footnote 42]►Section 226.18(e)◄ provides an exception for certain transactions in which no annual percentage rate disclosure is required.

18(f) Variable rate.

1. *Coverage.* The requirements of § 226.18(f) apply to [all] transactions ►not secured by real property or a dwelling◄ in which the terms of the legal obligation allow the creditor to increase the rate [originally disclosed to the consumer. It includes]►charged when the transaction is consummated. Increases in rate include◄ not only increases in the interest rate but also increases in other components, such as the rate of required credit life insurance. [The provisions, however, do not apply to]►However, increases in rate do not include◄ increases resulting from delinquency (including late payment), default, assumption, acceleration or transfer of the collateral ►, because creditors may assume that consumers abide by the terms of the legal obligation. *See* comment 17(c)(1)–1.◄ [Section 226.18(f)(1) applies to variable-rate transactions that are not secured by the consumer's principal dwelling and to those that are secured by the principal dwelling but have a term of one year or less. Section 226.18(f)(2) applies to variable-rate transactions that are secured by the consumer's principal dwelling and have a term greater than one year. Moreover, transactions subject to section 226.18(f)(2) are subject to the special early-disclosure requirements of section 226.19(b). (However, ''shared-equity'' or ''shared-appreciation'' mortgages are subject to the disclosure requirements of section 226.18(f)(1) and not to the requirements of sections 226.18(f)(2) and 226.19(b) regardless of the general coverage of those sections.) Creditors are permitted under footnote 43 to substitute in any variable-rate transaction the disclosures required under Section 226.19(b) for those disclosures ordinarily required under Section 226.18(f)(1). Creditors who provide variable-rate disclosures under section 226.19(b) must comply with all of the requirements of that section, including the timing of disclosures, and must also provide the disclosures required under section 226.18(f)(2). Creditors utilizing footnote 43 may, but need not, also provide disclosures pursuant to section 226.20(c). (Substitution of disclosures under section 226.18(f)(1) in transactions subject to section 226.19(b) is not permitted under the footnote.)]

[*Paragraph 18(f)(1).*]

[1.]►2.◄ *Terms used in disclosure.* In describing the variable rate feature, the creditor need not use any prescribed terminology. For example, limitations and hypothetical examples may be described in terms of interest rates rather than annual percentage rates. The model forms in appendix H provide examples of ways in which the variable rate disclosures may be made.

[2.]►3.◄ *Conversion feature.* In variable-rate transactions with an option permitting consumers to convert to a fixed-rate transaction, the conversion option is a variable-rate feature that must be disclosed. In making disclosures under § 226.18(f)[(1)], creditors should disclose the fact that the rate may increase upon conversion; identify the index or formula used to set the fixed rate; and state any limitations on and effects of an increase resulting from conversion that differ from other variable-rate features. Because § 226.18(f)[(1)(iv)]►(4)◄ requires only one hypothetical example (such as an example of the effect on payments resulting from changes in the index), a second hypothetical example need not be given.

Paragraph 18(f)(1)[(i)].

1. *Circumstances.* The circumstances under which the rate may increase include identification of any index to which the rate is tied, as well as any conditions or events on which the increase is contingent.

i. When no specific index is used, any identifiable factors used to determine whether to increase the rate must be disclosed.

ii. When the increase in the rate is purely discretionary, the fact that any increase is within the creditor's discretion must be disclosed.

iii. When the index is internally defined (for example, by that creditor's prime rate), the creditor may comply with this requirement by either a brief description of that index or a statement that any increase is in the discretion of the creditor. An externally defined index, however, must be identified.

Paragraph 18(f)[(1)(ii)]►(2)◄.

1. *Limitations.* This includes any maximum imposed on the amount of an increase in the rate at any time, as well as any maximum on the total increase over the life of the transaction. When there are no limitations, the creditor may, but need not, disclose that fact. Limitations do not include legal limits in the nature of usury or rate ceilings under State or Federal statutes or regulations. (See § 226.30 for the rule requiring that a maximum interest rate be included in certain variable-rate transactions.)

Paragraph 18(f)[(1)(iii)]►(3)◄.

1. *Effects.* Disclosure of the effect of an increase refers to an increase in the number or amount of payments or an increase in the final payment. In addition, the creditor may make a brief reference to negative amortization that may result from a rate increase. (See the commentary to § 226.17(a)(1) regarding directly related information.) If the effect cannot be determined, the creditor must provide a statement of the possible effects. For example, if the exercise of the variable-rate feature may result in either more or larger payments, both possibilities must be noted.

Paragraph 18(f)[(1)(iv)]►(4)◄.

1. *Hypothetical example.* The example may, at the creditor's option appear apart from the other disclosures. The creditor may provide either a standard example that illustrates the terms and conditions of that type of credit offered by that creditor or an example that directly reflects the terms and conditions of the particular transaction. In transactions with more than one variable-rate feature, only one hypothetical example need be provided. (See the commentary to § 226.17(a)(1) regarding disclosure of more than one hypothetical example as directly related information.)

2. *Hypothetical example not required.* The creditor need not provide a hypothetical example in the following transactions with a variable-rate feature:

i. Demand obligations with no alternate maturity date.

ii. Interim student credit extensions.

iii. Multiple-advance construction loans disclosed pursuant to appendix D, Part I.

[*Paragraph 18(f)(2).*

1. *Disclosure required.* In variable-rate transactions that have a term greater than one year and are secured by the consumer's principal dwelling, the creditor must give special early disclosures under section 226.19(b) in addition to the later disclosures required under section 226.18(f)(2). The disclosures under section 226.18(f)(2) must state that the transaction has a variable-rate feature and that variable-rate disclosures have been provided earlier. (See the commentary to section 226.17(a)(1) regarding the disclosure of certain directly related information in addition to the variable-rate disclosures required under section 226.18(f)(2).)]

18(g) Payment schedule.

1. *Amounts included in repayment schedule.* The repayment schedule should reflect all components of the finance charge, not merely the portion attributable to interest. A prepaid finance charge, however, should not be shown in the repayment schedule as a separate payment. The payments may include amounts beyond the amount financed and finance charge. For example, the disclosed payments may, at the creditor's option, reflect certain insurance premiums where the premiums are not part of either the amount financed or the finance charge, as well as real estate escrow amounts such as taxes added to the payment in mortgage transactions.

2. *Deferred downpayments.* As discussed in the commentary to § 226.2(a)(18), deferred downpayments or pick-up payments that meet the conditions set forth in the definition of downpayment may be treated as part of the downpayment. Even if treated as a downpayment, that amount may nevertheless be disclosed as part of the payment schedule, at the creditor's option.

3. *Total number of payments.* ►Except for transactions secured by real property or a dwelling, i◄[I]n disclosing the number of payments for transactions with more than one payment level, creditors may but need not disclose as a single figure the total number of payments for all levels. For example, in a transaction calling for 108 payments of $350, 240 payments of $335, and 12 payments of $330, the creditors need not state that there will be a total of 360 payments. ►For transactions secured by real property or a dwelling, creditors must disclose as a single figure the total number of payments for all levels. See § 226.38(e)(5)(i).◄

4. *Timing of payments.* i. *General rule.* Section 226.18(g) requires creditors to disclose the timing of payments. To meet this requirement, creditors may list all of the payment due dates. They also have the option of specifying the ''period of payments'' scheduled to repay the obligation. As a general rule, creditors that choose this option must disclose the payment intervals or frequency, such as ''monthly'' or ''bi-weekly,'' and the calendar date that the beginning payment is due. For example, a creditor may disclose that payments are due ''monthly beginning on July 1, 1998.'' This information, when combined with the number of payments, is necessary to define the repayment period and enable a consumer to determine all of the payment due dates.

ii. *Exception.* In a limited number of circumstances, the beginning-payment date is unknown and difficult to determine at the time disclosures are made. For example, a consumer may become obligated on a credit contract that contemplates the delayed disbursement of funds based on a contingent event, such as the completion of home repairs. Disclosures may also accompany loan checks that are sent by mail, in which case the initial disbursement and repayment dates are solely within the consumer's control. In such cases, if the beginning-payment date is unknown the creditor may use an estimated date and label the disclosure as an estimate pursuant to § 226.17(c). Alternatively, the disclosure may refer to the occurrence of a particular event, for example, by disclosing that the beginning payment is due ''30 days after the first loan disbursement.'' This information also may be included with an estimated date to explain the basis for the creditor's estimate. See comment 17(a)(1)–5(iii).

5. *Mortgage insurance.* The payment schedule 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 schedule must reflect 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, the payment schedule

should reflect 130 premium payments. If, under the legal obligation, the creditor will apply the amount escrowed to the two final insurance payments, the payment schedule should reflect 128 monthly premium payments. (For assumptions in calculating a payment schedule that includes mortgage insurance that must be automatically terminated, see comments [17(c)(1)–8 and 17(c)(1)–10]►17(c)(1)(iii)–1 and 17(c)(1)(iii)–3◄.)

[*Paragraph*]*18(h) Total of payments.*

1. *Disclosure required.* The total of payments must be disclosed using that term, along with a descriptive phrase similar to the one in the regulation. The descriptive explanation may be revised to reflect a variable rate feature with a brief phrase such as ''based on the current annual percentage rate which may change.''

2. *Calculation of total of payments.* The total of payments is the sum of the payments disclosed under § 226.18(g). For example, if the creditor disclosed a deferred portion of the downpayment as part of the payment schedule, that payment must be reflected in the total disclosed under this paragraph.

3. *Exception.* [Footnote 44]►Section 226.18(h)◄ permits creditors to omit disclosure of the total of payments in single-payment transactions. This exception does not apply to a transaction calling for a single payment of principal combined with periodic payments of interest.

4. *Demand obligations.* In demand obligations with no alternate maturity date, the creditor may omit disclosure of payment amounts under § 226.18(g)(1). In those transactions, the creditor need not disclose the total of payments.

[Paragraph] 18(i) Demand feature.

1. *Disclosure requirements.* The disclosure requirements of this provision apply not only to transactions payable on demand from the outset, but also to transactions that are not payable on demand at the time of consummation but convert to a demand status after a stated period. In demand obligations in which the disclosures are based on an assumed maturity of 1 year under § 226.17(c)(5), that fact must also be stated. Appendix H contains model clauses that may be used in making this disclosure.

2. *Covered demand features.* The type of demand feature triggering the disclosures required by section 226.18(i)►, or section 226.38(d)(2)(iv) for transactions secured by real property or a dwelling, ◄includes only those demand features contemplated by the parties as part of the legal obligation. For example, [this provision]►section 226.18(i), or section 226.38(d)(2)(iv) for transactions secured by real property or a dwelling,◄ do[es] not apply to transactions that convert to a demand status as a result of the consumer's default. A due-on-sale clause is not considered a demand feature. A creditor may, but need not, treat its contractual right to demand payment of a loan made to its executive officers as a demand feature to the extent that the contractual right is required by Regulation O (12 CFR 215.5) or other federal law.

3. *Relationship to payment schedule disclosures.* As provided in section 226.18(g)(1), ►or section 226.38(c) for transactions secured by real property or a dwelling,◄ in demand obligations with no alternate maturity date, the creditor need only disclose the due dates or payment periods of any scheduled interest payments for the first year. If the demand obligation states an alternate maturity, however, the disclosed payment schedule must reflect that stated term; the special rule in section 226.18(g)(1)►, or section 226.38(c) for transactions secured by real property or a dwelling,◄ is not available.

[Paragraph]18(j) Total sale price.

1. *Disclosure required.* In a credit sale transaction, the total sale price must be disclosed using that term, along with a descriptive explanation similar to the one in the regulation. For variable rate transactions, the descriptive phrase may, at the creditor's option, be modified to reflect the variable rate feature. For example, the descriptor may read: ''The total cost of your purchase on credit, which is subject to change, including your downpayment of * * *.'' The reference to a downpayment may be eliminated in transactions calling for no downpayment.

2. *Calculation of total sale price.* The figure to be disclosed is the sum of the cash price, other charges added under § 226.18(b)(2), and the finance charge disclosed under § 226.18(d).

3. *Effect of existing liens.* When a credit sale transaction involves property that is being used as a trade-in (an automobile, for example) and that has a lien exceeding the value of the trade-in, the total sale price is affected by the amount of any cash provided. (See comment 2(a)(18)–3.) To illustrate, assume a consumer finances the purchase of an automobile with a cash price of $20,000. Another vehicle used as a trade-in has a value of $8,000 but has an existing lien of $10,000, leaving a $2,000 deficit that the consumer must finance.

i. If the consumer pays $1,500 in cash, the creditor may apply the cash first to the lien, leaving a $500 deficit, and reflect a downpayment of $0. The total sale price would include the $20,000 cash price, an additional $500 financed under § 226.18(b)(2), and the amount of the finance charge. Alternatively, the creditor may reflect a downpayment of $1,500 and finance the $2,000 deficit. In that case, the total sale price would include the sum of the $20,000 cash price, the $2,000 lien payoff amount as an additional amount financed, and the amount of the finance charge.

ii. If the consumer pays $3,000 in cash, the creditor may apply the cash first to extinguish the lien and reflect the remainder as a downpayment of $1,000. The total sale price would reflect the $20,000 cash price and the amount of the finance charge. (The cash payment extinguishes the trade-in deficit and no charges are added under § 226.18(b)(2).) Alternatively, the creditor may elect to reflect a downpayment of $3,000 and finance the $2,000 deficit. In that case, the total sale price would include the sum of the $20,000 cash price, the $2,000 lien payoff amount as an additional amount financed, and the amount of the finance charge.

[Paragraph]18(k) Prepayment.

1. *Disclosure required.* The creditor must give a definitive statement of whether or not a penalty will be imposed or a rebate will be given.

[•]►iii.◄ The fact that no penalty will be imposed may not simply be inferred from the absence of a penalty disclosure; the creditor must indicate that prepayment will not result in a penalty.

[•]►ii.◄ If a penalty or refund is possible for one type of prepayment, even though not for all, a positive disclosure is required. This applies to any type of prepayment, whether voluntary or involuntary as in the case of prepayments resulting from acceleration.

[•]►iii.◄ Any difference in rebate or penalty policy, depending on whether prepayment is voluntary or not, must not be disclosed with the segregated disclosures.

2. *Rebate-penalty disclosure.* A single transaction may involve both a precomputed finance charge and a finance charge computed by application of a rate to the unpaid balance (for example, mortgages with mortgage-guarantee insurance). In these cases, disclosures about both prepayment rebates and penalties are required. Sample form H–15 in appendix H illustrates a mortgage transaction in which both rebate and penalty disclosures are necessary.

3. *Prepaid finance charge.* The existence of a prepaid finance charge in a transaction does not, by itself, require a disclosure under § 226.18(k). A prepaid finance charge is not considered a penalty under § 226.18(k)(1), nor does it require a disclosure under § 226.18(k)(2). At its option, however, a creditor may consider a prepaid finance charge to be under § 226.18(k)(2). If a disclosure is made under § 226.18(k)(2) with respect to a prepaid finance charge or other finance charge, the creditor may further identify that finance charge. For example, the disclosure may state that the borrower ''will not be entitled to a refund of the prepaid finance charge'' or some other term that describes the finance charge.

Paragraph 18(k)(1).

1. *Penalty.* [This]►Section 226.18(k)(1)◄ applies only to those transactions in which the interest calculation takes account of all scheduled reductions in principal, as well as transactions in which interest calculations are made daily. The term *penalty* as used here encompasses only those charges that are assessed strictly because of the prepayment in full of a simple-interest obligation, as an addition to all other amounts. Items which are penalties include, for example:

[• Interest charges for any period after prepayment in full is made.]►i. Charges determined by treating the loan balance as outstanding for a period after prepayment in full and applying the interest rate to such ''balance.''◄ (See the commentary to § 226.17(a)(1) regarding disclosure of [interest]►such◄ charges assessed for periods after prepayment in full as directly related information►, for transactions not secured by real property or a dwelling◄.)

[•]►ii.◄ A minimum finance charge in a simple-interest transaction. (See the commentary to § 226.17(a)(1) regarding the disclosure of a minimum finance charge as directly related information.) Items which are not penalties include, for example[:]►,◄

[• L]►l◄oan guarantee fees►.◄

[• Interim interest on a student loan.]

Paragraph 18(k)(2).

1. *Rebate of finance charge.* This applies to any finance charges that do not take account of each reduction in the principal balance of an obligation. This category includes, for example:

[•]►i.◄ Precomputed finance charges such as add-on charges.

[•]►ii.◄ Charges that take account of some but not all reductions in principal, such as mortgage guarantee insurance assessed on the basis of an annual declining balance, when the principal is reduced on a monthly basis.

►2.◄ *Methodology of computing.* No description of the method of computing earned or unearned finance charges is required or permitted as part of the segregated disclosures under this section.

[Paragraph]18(l) Late payment.

1. *Definition.* This paragraph requires a disclosure only if charges are added to individual delinquent installments by a creditor who otherwise considers the transaction ongoing on its original terms. Late payment charges do not include:

[•]►i.◄ The right of acceleration.

[•]►ii.◄ Fees imposed for actual collection costs, such as repossession charges or attorney's fees.

[•]►iii.◄ Deferral and extension charges.

[•]►iv.◄ The continued accrual of simple interest at the contract rate after the payment due date. However, an increase in the interest rate is a late payment charge to the extent of the increase.

2. *Content of disclosure.* Many State laws authorize the calculation of late charges on the basis of either a percentage or a specified dollar amount, and permit imposition of the lesser or greater of the 2 charges. The disclosure made under § 226.18(l) may reflect this alternative. For example, stating that the charge in the event of a late payment is 5% of the late amount, not to exceed $5.00, is sufficient. Many creditors also permit a grace period during which no late charge will be assessed; this fact may be disclosed as directly related information. (See the commentary to § 226.17(a).)

[Paragraph]18(m) Security interest.

1. *Purchase money transactions.* When the collateral is the item purchased as part of, or with the proceeds of, the credit transaction, section 226.18(m) requires only a general identification such as ''the property purchased in this transaction.'' However, the creditor may identify the property by item or type instead of identifying it more generally with a phrase such as ''the property purchased in this transaction.'' For example, a creditor may identify collateral as ''a motor vehicle,'' or as ''the property purchased in this transaction.'' Any transaction in which the credit is being used to purchase the collateral is considered a purchase money transaction and the abbreviated identification may be used, whether the obligation is treated as a loan or a credit sale.

2. *Nonpurchase money transactions.* In nonpurchase money transactions, the property subject to the security interest must be identified by item or type. This disclosure is satisfied by a general disclosure of the category of property subject to the security interest, such as ''motor vehicles,'' ''securities,'' ''certain household items,'' or ''household goods.'' (Creditors should be aware, however, that the Federal credit practices rules, as well as some State laws, prohibit certain security interests in household goods.) At the creditor's option, however, a more precise identification of the property or goods may be provided.

3. *Mixed collateral.* In some transactions in which the credit is used to purchase the collateral, the creditor may also take other property of the consumer as security. In those cases, a combined disclosure must be provided, consisting of an identification of the purchase money collateral consistent with comment 18(m)–1 and a specific identification of the other collateral consistent with comment 18(m)–2.

4. *After-acquired property.* An after-acquired property clause is not a security interest to be disclosed under § 226.18(m).

5. *Spreader clause.* The fact that collateral for pre-existing credit with the institution is being used to secure the present obligation constitutes a security interest and must be disclosed. (Such security interests may be known as ''spreader'' or ''dragnet'' clauses, or as ''cross-collateralization'' clauses.) A specific identification of that collateral is unnecessary but a reminder of the interest arising from the prior indebtedness is required. The disclosure may be made by using language such as ''collateral securing other loans with us may also secure this loan.'' At the creditor's option, a more specific description of the property involved may be given.

6. *Terms used in disclosure.* No specified terminology is required in disclosing a security interest. Although the disclosure may, at the creditor's option, use the term security interest, the creditor may designate its interest by using, for example, pledge, lien, or mortgage.

7. *Collateral from third party.* In certain transactions, the consumer's obligation may be secured by collateral belonging to a third party. For example, a loan to a student may be secured by an interest in the property of the student's parents. In such cases, the security interest is taken in connection with the transaction and must be disclosed, even though the property encumbered is owned by someone other than the consumer.

18(n) Insurance►,◄ [and] debt cancellation ►, and debt suspension◄.

1. *Location.* This disclosure may, at the creditor's option, appear apart from the other disclosures. It may appear with any other information, including the amount financed itemization, any information prescribed by State law, or other supplementary material. When this information is disclosed with the other segregated disclosures, however, no additional explanatory material may be included.

2. *Debt cancellation ►and debt suspension◄.* Creditors may use the model credit-insurance disclosures only if the debt-cancellation ►or debt suspension◄ coverage constitutes insurance under State law. Otherwise, they may provide a parallel disclosure that refers to debt-cancellation ►or debt suspension◄ coverage.

[Paragraph]18(o) Certain security interest charges.

1. *Format.* No special format is required for these disclosures; under § 226.4(e), taxes and fees paid to government officials with respect to a security interest may be aggregated, or may be broken down by individual charge. For example, the disclosure could be labeled ''filing fees and taxes'' and all funds disbursed for such purposes may be aggregated in a single disclosure. This disclosure may appear, at the creditor's option, apart from the other required disclosures. The inclusion of this information on a statement required under the Real Estate Settlement Procedures Act is sufficient disclosure for purposes of Truth in Lending.

[Paragraph]18(p) Contract reference.

1. *Content.* Creditors may substitute, for the phrase ''appropriate contract document,'' a reference to specific transaction documents in which the additional information is found, such as ''promissory note'' or ''retail installment sale contract.'' A creditor may, at its option, delete inapplicable items in the contract reference, as for example when the contract documents contain no information regarding the right of acceleration.

[18(q) Assumption policy

1. *Policy statement.* In many mortgages, the creditor cannot determine, at the time disclosure must be made, whether a loan may be assumable at a future date on its original terms. For example, the assumption clause commonly used in mortgages sold to the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation conditions an assumption on a variety of factors such as the creditworthiness of the subsequent borrower, the potential for impairment of the lender's security, and execution of an assumption agreement by the subsequent borrower. In cases where uncertainty exists as to the future assumability of a mortgage, the disclosure under § 226.18(q) should reflect that fact. In making disclosures in such cases, the creditor may use phrases such as ''subject to conditions,'' ''under certain circumstances,'' or ''depending on future conditions.'' The creditor may provide a brief reference to more specific criteria such as a due-on-sale clause, although a complete explanation of all conditions is not appropriate. For example, the disclosure may state, ''Someone buying your home may be allowed to assume the mortgage on its original terms, subject to certain conditions, such as payment of an assumption fee.'' See comment 17(a)(1)–5 for an example of a reference to a due-on-sale clause.

2. *Original terms.* The phrase *original terms* for purposes of § 226.18(q) does not preclude the imposition of an assumption fee, but a modification of the basic credit agreement, such as a change in the contract interest rate, represents different terms.]

[Paragraph]18(r) Required deposit.

1. *Disclosure required.* The creditor must inform the consumer of the existence of a required deposit. (Appendix H provides a model clause that may be used in making that disclosure.) [Footnote 45 describes three]►§ 226.18(r)(1) and (2) describe two◄ types of deposits that need not be considered required deposits. Use of the phrase ''need not'' permits creditors to include the disclosure even in cases where there is doubt as to whether the deposit constitutes a required deposit.

[2. *Pledged-account mortgages.* In these transactions, a consumer pledges as collateral funds that the consumer deposits in an account held by the creditor. The creditor withdraws sums from that account to supplement the consumer's periodic payments. Creditors may treat these pledged accounts as required deposits or they may treat them as consumer buydowns in accordance with the commentary to section 226.17(c)(1).]

3. *Escrow accounts.* The escrow exception in [footnote 45]►§ 226.18(r)(1)◄ applies, for example, to accounts for such items as maintenance fees, repairs, or improvements, whether in a realty or a nonrealty transaction. (See the commentary to section 226.17(c)(1) regarding the use of escrow accounts in consumer buydown transactions.)

4. *Interest-bearing accounts.* When a deposit earns at least 5 percent interest per year, no disclosure is required under § 226.18(r). This exception applies whether the deposit is held by the creditor or by a third party.

5. *[Morris Plan transactions]►Deposits applied solely to pay obligation◄.* A deposit [under a Morris Plan, in which]►to◄ a deposit account [is] created for the sole purpose of accumulating payments and [this is] applied to satisfy entirely the consumer's obligation in the transaction[,] is not a required deposit.

[6.] *Examples of amounts excluded.* The following are among the types of deposits that need not be treated as required deposits:

[•]►i.◄ Requirement that a borrower be a customer or a member even if that involves a fee or a minimum balance.

[•]►ii.◄ Required property insurance escrow on a mobile home transaction.

[•]►iii.◄ Refund of interest when the obligation is paid in full.

[•]►iv.◄ Deposits that are immediately available to the consumer.

[•]►v.◄ Funds deposited with the creditor to be disbursed (for example, for construction) before the loan proceeds are advanced.

[•]►vi.◄ Escrow of condominium fees.

[•]►vii.◄ Escrow of loan proceeds to be released when the repairs are completed.

§ 226.19—Certain Mortgage and Variable-Rate Transactions.

►*19 Coverage.*

1. *General.* Section 226.19 applies to transactions secured by real property or a dwelling, other than home equity lines of credit subject to § 226.5b. Creditors must make the disclosures required by § 226.19 even if the transaction is not subject to the Real Estate Settlement Procedures Act (RESPA), 12 U.S.C. 2602 *et seq.,* and its implementing Regulation X, 24 CFR 3500.1 *et seq.,* administered by the Department of Housing and Urban Development (HUD). For example, disclosures are required for construction loans that are not covered by RESPA or Regulation X because they are not considered ''federally related mortgage loans.'' *See* 12 U.S.C. 2602(1); 15 CFR 3500.2(b). However, § 226.19 only applies to transactions that are offered or extended to a consumer primarily for personal, family, or household purposes, even if the transactions are secured by real property or a dwelling. TILA and Regulation Z do not apply to transactions that are primarily for business, commercial, or agricultural purposes. *See* 15 U.S.C. 1603(1); § 226.3(a)(2). *See also* § 226.2(a)(12) and (b)(2). Section 226.19(a)(4) contains special disclosure

timing requirements for mortgage transactions secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53(D)).◀

19(a)(1)(i) Time of disclosure.

[1. *Coverage.* This section requires early disclosure of credit terms in mortgage transactions that are secured by a consumer's dwelling (other than home equity lines of credit subject to § 226.5b or mortgage transactions secured by an interest in a timeshare plan) that are also subject to the Real Estate Settlement Procedures Act (RESPA) and its implementing Regulation X, administered by the Department of Housing and Urban Development (HUD). To be covered by § 226.19, a transaction must be a Federally related mortgage loan under RESPA. ''Federally related mortgage loan'' is defined under RESPA (12 U.S.C. 2602) and Regulation X (24 CFR 3500.2), and is subject to any interpretations by HUD.]

[2.]▶1.◀ *Timing and use of estimates.* The disclosures required by § 226.19(a)(1)(i) must be delivered or mailed not later than three business days after the creditor receives the consumer's written application. The general definition of ''business day'' in § 226.2(a)(6)—a day on which the creditor's offices are open to the public for substantially all of its business functions—is used for purposes of § 226.19(a)(1)(i). *See* comment 2(a)(6)–1. This general definition is consistent with the definition of ''business day'' in HUD's Regulation X—a day on which the creditor's offices are open to the public for carrying on substantially all of its business functions. *See* 24 CFR 3500.2. Accordingly, the three-business-day period in § 226.19(a)(1)(i) for making early disclosures coincides with the time period within which creditors [subject to RESPA] must provide good faith estimates of settlement costs ▶for transactions subject to RESPA◀. If the creditor does not know the precise credit terms, the creditor must base the disclosures ▶required by § 226.19(a)(1)(i)◀ on the best information reasonably available and indicate that the disclosures are estimates under § 226.17(c)(2). If many of the disclosures are estimates, the creditor may include a statement to that effect (such as ''all numerical disclosures [except the late-payment disclosure] are estimates'') instead of separately labelling each estimate. In the alternative, the creditor may label as an estimate only the items primarily affected by unknown information. (*See* the commentary to § 226.17(c)(2).) The creditor may provide explanatory material concerning the estimates and the contingencies that may affect the actual terms, in accordance with the commentary to § 226.17(a)(1)[.]▶and § 226.37. The disclosures required by § 226.19(a)(2) may not contain estimates, however, with limited exceptions. See the commentary on § 226.19(a)(2) for a discussion of limitations on estimates in disclosures made under that subsection.◀

[3.]▶2.◀ *Written application.* Creditors may rely on RESPA and Regulation X (including any interpretations issued by HUD) in deciding whether a ''written application'' has been received. In general, Regulation X defines an ''application'' to mean the submission of a borrower's financial information in anticipation of a credit decision relating to a [F]▶f◀ederally related mortgage loan. *See 24* CFR 3500.2(b). ▶Creditors may rely on RESPA and Regulation X even for a transaction not subject to RESPA.◀ An application is received when it reaches the creditor in any of the ways applications are normally transmitted—by mail, hand delivery, or through an intermediary agent or broker. (*See* [comment 19(b)–3]▶the commentary on § 19(d)(3)◀ for guidance in determining whether or not the transaction involves an intermediary agent or broker.) If an application reaches the creditor through an intermediary agent or broker, the application is received when it reaches the creditor, rather than when it reaches the agent or broker.

[4.]▶3.◀ *Denied or withdrawn application.* The creditor may determine within the three-business-day period that the application will not or cannot be approved on the terms requested, as, for example, when a consumer applies for a type or amount of credit that the creditor does not offer, or the consumer's application cannot be approved for some other reason. In that case, or if the consumer withdraws the application within the three-business-day waiting period, the creditor need not make the disclosures under this section. If the creditor fails to provide early disclosures and the transaction is later consummated on the original terms, the creditor will be in violation of this provision. If, however, the consumer amends the application because of the creditor's unwillingness to approve it on its original terms, no violation occurs for not providing disclosures based on the original terms. But the amended application is a new application subject to § 226.19(a)(1)(i).

[5.]▶4.◀ *Itemization of amount financed.* In many mortgage transactions ▶subject to RESPA◀, the itemization of the amount financed required by [§ 226.18(c)]▶§ 226.38(j)◀ will contain items, such as origination fees or points, that also must be disclosed as part of the good faith estimates of settlement costs required under RESPA. Creditors furnishing the RESPA good faith estimates need not give consumers any itemization of the amount financed▶, whether or not a transaction is subject to RESPA◀.

19(a)(1)(ii) Imposition of fees.

1. *Timing of fees.* The consumer must receive the disclosures required by this section before paying or incurring any fee imposed by a creditor or other person in connection with the consumer's application for a mortgage transaction that is subject to § 226.19(a)(1)(i), except as provided in § 226.19(a)(1)(iii). If the creditor delivers the disclosures to the consumer in person, a fee may be imposed anytime after delivery. If the creditor places the disclosures in the mail, the creditor may impose a fee after the consumer receives the disclosures or, in all cases, after midnight [on the third business day] following ▶ the third business day after◀ mailing of the disclosures. ▶Creditors that use electronic mail or a courier to provide disclosures may also follow this approach. Whatever method is used to provide disclosures, creditors may rely on documentation of receipt in determining when a fee may be imposed.◀ For purposes of § 226.19(a)(1)(ii), the term ''business day'' means all calendar days except Sundays and legal public holidays referred to in § 226.2(a)(6). *See* [C]▶c◀omment 2(a)(6)–2. For example, assuming that there are no intervening legal public holidays, a creditor that receives the consumer's written application on Monday and mails the early mortgage loan disclosure on Tuesday may impose a fee on the consumer [after midnight on Friday]▶on Saturday◀.

19(a)(2) Waiting period(s) required

1. *Business day definition.* For purposes of § 226.19(a)(2), ''business day'' means all calendar days except Sundays and the legal public holidays referred to in § 226.2(a)(6). *See* comment 2(a)(6)–2.

2. *Consummation after* [*both*]▶*all*◀ *waiting periods expire.* Consummation may not occur until both the seven-business-day waiting period and the three-business-day waiting period▶(s)◀ have expired. For example, assume a creditor delivers the early disclosures to the consumer in person or places them in the mail on Monday, June 1, and the creditor then delivers [corrected]▶new◀ disclosures in person to the consumer on Wednesday, June 3. Although Saturday,

June 6 is the third business day after the consumer received the [corrected]►new◄ disclosures, consummation may not occur before Tuesday, June 9, the seventh business day following delivery or mailing of the early disclosures.

19(a)(2)(i) Seven-business-day waiting period.

1. *Timing.* The disclosures required by § 226.19(a)(1)(i) must be delivered or placed in the mail no later than the seventh business day before consummation. The seven-business-day waiting period begins when the creditor delivers the early disclosures or places them in the mail, not when the consumer receives or is deemed to have received the early disclosures. For example, if a creditor delivers the early disclosures to the consumer in person or places them in the mail on Monday, June 1, consummation may occur on or after Tuesday, June 9, the seventh business day following delivery or mailing of the early disclosures.

►*19(a)(2)(ii) Three-business-day waiting period.*

1. *New disclosures in all cases.* The creditor must provide new disclosures under § 226.38 so that the consumer receives them not later than the third business day before consummation, even if the new disclosures are identical to the early disclosures provided under § 226.19(a)(1)(i).

2. *Content of disclosures.* Disclosures made under § 226.19(a)(2)(ii) must contain each of the applicable disclosures required by § 226.38.

3. *Estimates.* Section 226.19(a)(2)(ii) provides that only the disclosures required by §§ 226.38(c)(3)(i)(C), 226.38(c)(3)(ii)(C), 226.38(c)(6)(i), and 226.38(e)(5)(i) may be estimated disclosures. Because estimated amounts of escrowed taxes and insurance premiums and mortgage insurance premiums disclosed (as applicable) under §§ 226.38(c)(3)(i)(C), 226.38(c)(3)(ii)(C), and 226.38(c)(6)(i) are components of the total periodic payments disclosure required by §§ 226.38(c)(3)(i)(D) and 226.38(c)(3)(ii)(D) and the total payments disclosure required by § 226.38(e)(5)(i), those disclosures are estimated disclosures. (A total payments disclosure is not required for loans with a negative amortization feature subject to § 226.38(c)(6).) Creditors may estimate components of the total periodic payments disclosures required by §§ 226.38(c)(3)(i)(C), 226.38(c)(3)(ii)(C) and 226.38(c)(6)(i) and the total payment disclosure required by § 226.38(e)(5)(i) only to the extent the estimated escrowed amounts and mortgage insurance premiums affect those disclosures.

4. *Timing.* The creditor must provide final disclosures so that the consumer receives them not later than the third business day before consummation. For example, for consummation to occur on Thursday, June 11, the consumer must receive the disclosures on or before Monday, June 8.◄

ALTERNATIVE 1—PARAGRAPH 19(a)(2)(iii)

►*19(a)(2)(iii) Corrected disclosures.*

1. *Conditions for corrected disclosures.* A disclosed annual percentage rate is accurate for purposes of § 226.19(a)(2)(iii) if the disclosure is accurate under § 226.19(a)(2)(iv). If a change occurs that does not render the annual percentage rate inaccurate, the creditor must disclose the changed terms before consummation, consistent with § 226.17(f).

2. *Content of corrected disclosures.* Disclosures made under § 226.19(a)(2)(iii) must contain each of the applicable disclosures required by § 226.38.

3. *Estimates.* In disclosures provided under § 226.19(a)(2)(iii), only the disclosures required by §§ 226.38(c)(3)(i)(C), 226.38(c)(3)(ii)(C), 226.38(c)(6)(i) and 226.38(e)(5)(i) may be estimates. *See* comment 19(a)(2)(ii)-3 for a discussion of which of the disclosures required under § 226.38 creditors may estimate.

4. *Timing.* The creditor must provide the corrected disclosures so that the consumer receives them not later than the third business day before consummation. For example, for consummation to occur on Saturday, June 13, the consumer must receive the disclosures on or before Wednesday, June 10.◄

[*19(a)(2)(ii) Three-business-day waiting period.*

1. *Conditions for redisclosure.* If, at the time of consummation, the annual percentage rate disclosed is accurate under § 226.22, the creditor does not have to make corrected disclosures under § 226.19(a)(2). If, on the other hand, the annual percentage rate disclosed is not accurate under § 226.22, the creditor must make corrected disclosures of all changed terms (including the annual percentage rate) so that the consumer receives them not later than the third business day before consummation. For example, assume consummation is scheduled for Thursday, June 11 and the early disclosures for a regular mortgage transaction disclose an annual percentage rate of 7.00%.

i. On Thursday, June 11, the annual percentage rate will be 7.10%. The creditor is not required to make corrected disclosures under § 226.19(a)(2).

ii. On Thursday, June 11, the annual percentage rate will be 7.15%. The creditor must make corrected disclosures so that the consumer receives them on or before Monday, June 8.

2. *Content of new disclosures.* If redisclosure is required, the creditor may provide a complete set of new disclosures, or may redisclose only the changed terms. If the creditor chooses to provide a complete set of new disclosures, the creditor may but need not highlight the new terms, provided that the disclosures comply with the format requirements of § 226.17(a). If the new creditor chooses to disclose only the new terms, all the new terms must be disclosed. For example, a different annual percentage rate will almost always produce a different finance charge, and often a new schedule of payments; all of these changes would have to be disclosed. If, in addition, unrelated terms such as the amount financed or prepayment penalty vary from those originally disclosed, the accurate terms must be disclosed. However, no new disclosures are required if the only inaccuracies involve estimates other than the annual percentage rate, and no variable-rate feature has been added. *See* § 226.17(f). For a discussion of the requirement to redisclose when a variable-rate feature is added, see comment 17(f)-2. For a discussion of redisclosure requirements in general, see the commentary on § 226.17(f).

3. *Timing.* When redisclosures are necessary because the annual percentage rate has become inaccurate, they must be received by the consumer no later than the third business day before consummation. (For redisclosures triggered by other events, the creditor must provide corrected disclosures before consummation. *See* § 226.17(f).) If the creditor delivers the corrected disclosures to the consumer in person, consummation may occur any time on the third business day following delivery. If the creditor provides the corrected disclosures by mail, the consumer is considered to have received them three business days after they are placed in the mail, for purposes of determining when the three-business-day waiting period required under § 226.19(a)(2)(ii) begins. Creditors that use electronic mail or a courier other than the postal service may also follow this approach.

4. *Basis for annual percentage rate comparison.* To determine whether a creditor must make corrected disclosures under § 226.22, a creditor compares (a) what the annual percentage rate will be at consummation to (b) the annual percentage rate stated in the most recent disclosures the creditor made to the consumer. For example, assume consummation for a regular mortgage transaction is scheduled for Thursday, June 11, the early disclosures provided in May stated an annual percentage rate of 7.00%, and corrected disclosures received by the consumer on Friday, June 5 stated an annual percentage rate of 7.15%:

1. On Thursday, June 11, the annual percentage rate will be 7.25%, which exceeds the most recently disclosed annual percentage rate by less than the applicable tolerance. The creditor is not required to make additional corrected disclosures or wait an additional three business days under § 226.19(a)(2).

ii. On Thursday, June 11, the annual percentage rate will be 7.30%, which exceeds the most recently disclosed annual percentage rate by more than the applicable tolerance. The creditor must make corrected disclosures such that the consumer receives them on or before Monday, June 8.]

ALTERNATIVE 2—PARAGRAPH 19(a)(2)(iii)

►*19(a)(2)(iii) Corrected disclosures.* 1. *Conditions for corrected disclosures.* If the annual percentage rate disclosed under § 226.19(a)(2)(ii) changes so that it is not accurate under § 226.19(a)(2)(iv) or an adjustable-rate feature is added (*see* comment 17(f)–2), the creditor must make corrected disclosures of all changed terms (including the annual percentage rate) so that the consumer receives them not later than the third business day before consummation. (If a change occurs that does not render the annual percentage rate on the early disclosures inaccurate, the creditor must disclose the changed terms before consummation, consistent with § 226.17(f).) For example, assume consummation is scheduled for Thursday, June 11 and the early disclosures for a regular mortgage transaction disclose an annual percentage rate of 7.00%:◄

[*19(a)(2)(ii) Three-business-day waiting period.* 1. *Conditions for redisclosure.* If, at the time of consummation, the annual percentage rate disclosed is accurate under § 226.22, the creditor does not have to make corrected disclosures under § 226.19(a)(2). If, on the other hand, the annual percentage rate disclosed is not accurate under § 226.22, the creditor must make corrected disclosures of all changed terms (including the annual percentage rate) so that the consumer receives them no later than the third business day before consummation. For example, assume consummation is scheduled for Thursday, June 11 and the early disclosures for a regular mortgage transaction disclose an annual percentage rate of 7.00%:]

i. On Thursday, June 11, the annual percentage rate will be 7.10%. The creditor is not required to make corrected disclosures under § 226.19(a)(2).

ii. On Thursday, June 11, the annual percentage rate will be 7.15%. The creditor must make corrected disclosures so that the consumer receives them on or before Monday, June 8.

2. *Content of* [*new*]►*corrected*◄ *disclosures.* If redisclosure is required ►under § 226.19(a)(2)(iii)◄, the creditor may provide a complete set of new disclosures, or may redisclose only the changed terms. If the creditor chooses to provide a complete set of new disclosures, the creditor may but need not highlight the new terms, provided that the disclosures comply with the format requirements of § 226.17(a) ►and § 226.37◄. If the new creditor chooses to disclose only the new terms, all the new terms must be disclosed. For example, a different annual percentage rate will almost always produce [a different finance charge, and often a new schedule of payments]►different interest and settlement charges, and often a new payment summary◄; all of these changes would have to be disclosed. If, in addition, unrelated terms such as the amount financed or prepayment penalty vary from those originally disclosed ►or an adjustable-rate feature is added (*see* comment 17(f)–2)◄, the accurate terms must be disclosed. [However, no new disclosures are required if the only inaccuracies involve estimates other than the annual percentage rate, and no variable-rate feature has been added. For a discussion of the requirement to redisclose when a variable-rate feature is added, see comment 17(f)–2. For a discussion of redisclosure requirements in general, see the commentary on § 226.17(f).]

[3. *Timing.* When redisclosures are necessary because the annual percentage rate has become inaccurate, they must be received by the consumer no later than the third business day before consummation. (For redisclosures triggered by other events, the creditor must provide corrected disclosures before consummation. *See* § 226.17(f).) If the creditor delivers the corrected disclosures to the consumer in person, consummation may occur any time on the third business day following delivery. If the creditor provides the corrected disclosures by mail, the consumer is considered to have received them three business days after they are placed in the mail, for purposes of determining when the three-business-day waiting periods required under § 226.19(a)(2)(ii) begins. Creditors that use electronic mail or a courier other than the postal service may also follow this approach.]

►3. *Estimates.* In disclosures provided under § 226.19(a)(2)(iii), only the disclosures required by §§ 226.38(c)(3)(i)(C), 226.38(c)(3)(ii)(C), 226.38(c)(6)(i) and 226.38(e)(5)(i) may be estimates. *See* comment 19(a)(2)(ii)–3 for a discussion of which of the disclosures required under § 226.38 creditors may estimate.◄

4. *Basis for annual percentage rate comparison.* To determine whether a creditor must make corrected disclosures under [§ 226.22]►§ 226.19(a)(2)(iii)◄, a creditor compares (a) what the annual percentage rate will be at consummation to (b) the annual percentage rate stated in the most recent disclosures the creditor made to the consumer. For example, assume consummation for a regular mortgage transaction is scheduled for Thursday, June 11, the early disclosures provided in May stated an annual percentage rate of 7.00%, and [corrected]►new◄ disclosures received by the consumer on Friday, June 5 stated an annual percentage rate of 7.15%:

i. On Thursday, June 11, the annual percentage rate will be 7.25%, which exceeds the most recently disclosed annual percentage rate by less than the applicable tolerance. The creditor is not required to make additional corrected disclosures or wait an additional three business days under § 226.19(a)(2).

ii. On Thursday, June 11, the annual percentage rate will be 7.30%, which exceeds the most recently disclosed annual percentage rate by more than the applicable tolerance. The creditor must make corrected disclosures such that the consumer receives them on or before Monday, June 8.

►*19(a)(2)(iv) Annual percentage rate accuracy.*

1. *Other changed terms.* If a change occurs that does not render the APR inaccurate under § 226.19(a)(iv), the creditor must disclose the changed terms before consummation, consistent with § 226.17(f).

19(a)(2)(v) Timing.

1. *General.* If the creditor delivers the disclosures required by § 226.19(a)(2)(ii)

or (a)(2)(iii) to the consumer in person, consummation may occur any time on the third business day following delivery. If the creditor provides the disclosures required by § 226.19(a)(2)(ii) or (a)(2)(iii) of this section by mail, the consumer is considered to have received them three business days after they are placed in the mail, for purposes of determining when the three-business-day waiting periods required under § 226.19(a)(2)(ii) and (iii) begin. Creditors that use electronic mail or a courier to provide disclosures may also follow this approach. Whatever method is used to provide disclosures, creditors may rely on documentation of receipt in determining when the three-business-day waiting period begins.◄

19(a)(3) Consumer's waiver of waiting period before consummation.

1. *Modification or waiver.* A consumer may modify or waive the right to a waiting period required by § 226.19(a)(2) only after the creditor makes the disclosures required by [§ 226.18]►§ 226.38. A separate waiver is required for each waiting period to be waived.◄ The consumer must have a *bona fide* personal financial emergency that necessitates consummating the credit transaction before the end of the waiting period. Whether these conditions are met is determined by the facts surrounding individual situations. The imminent sale of the consumer's home at foreclosure, where the foreclosure sale will proceed unless the loan proceeds are made available to the consumer during the waiting period, is one example of a *bona fide* personal financial emergency. Each consumer who is primarily liable on the legal obligation must sign the written statement for the waiver to be effective.

[2. *Examples of waivers within the seven-business-day waiting period.* Assume the early disclosures are delivered to the consumer in person on Monday, June 1, and at that time the consumer executes a waiver of the seven-business-day waiting period (which would end on Tuesday, June 9) so that the loan can be consummated on Friday, June 5:

i. If the annual percentage rate on the early disclosures is inaccurate under § 226.22, the creditor must provide a corrected disclosure to the consumer before consummation, which triggers the three-business-day waiting period in § 226.19(a)(2)(ii). After the consumer receives the corrected disclosure, the consumer must execute a waiver of the three-business-day waiting period in order to consummate the transaction on Friday, June 5.

ii. If a change occurs that does not render the annual percentage rate on the early disclosures inaccurate under § 226.22, the creditor must disclose the changed terms before consummation, consistent with § 226.17(f). Disclosure of the changed terms does not trigger the additional waiting period, and the transaction may be consummated on June 5 without the consumer giving the creditor an additional modification or waiver.]

[3. *Examples of waivers made after the seven-business-day waiting period.* Assume the early disclosures are delivered to the consumer in person on Monday, June 1 and consummation is scheduled for Friday, June 19.]►2. *Examples.* Assume consummation is scheduled for Friday, June 19, the disclosures required by § 226.19(a)(1)(i) are delivered to the consumer in person on Monday, June 1, and the consumer receives the disclosures required by § 226.19(a)(2)(ii) on Monday, June 15.◄ On Wednesday, June 17, a change in the annual percentage rate occurs:

i. If the annual percentage rate on the [early] disclosures ►required by § 226.19(a)(2)(ii)◄ is [inaccurate under § 226.22]►not accurate under § 226.22 nor accurate under § 226.19(a)(2)(iv)◄, the creditor must provide a corrected disclosure before consummation, which triggers the three-business-day-waiting period in § 226.19(a)(2)►(iii)◄. After the consumer receives the corrected disclosure, the consumer must execute a waiver of the three-business-day waiting period in order to consummate the transaction on Friday, June 19.

ii. If a change occurs that does not render the annual percentage rate on the [early] disclosures ►required by § 226.19(a)(2)(ii)◄ inaccurate under § 226.22, the creditor must disclose the changed terms before consummation, consistent with § 226.17(f). Disclosure of the changed terms does not trigger an additional waiting period, and the transaction may be consummated on Friday, June 19 without the consumer giving the creditor an additional modification or waiver.

[*19(a)(4) Notice.*

1. *Inclusion in other disclosures.* The notice required by § 226.19(a)(4) must be grouped together with the disclosures required by § 226.19(a)(1)(i) or § 226.19(a)(2). See comment 17(a)(1)–2 for a discussion of the rules for segregating disclosures. In other cases, the notice set forth in § 226.19(a)(4) may be disclosed together with or separately from the disclosures required under § 226.18. *See* comment 17(a)(1)–5(xvi).]

19(a)[(5)]►(4)◄(ii) Time of disclosures for timeshare plans.

1. *Timing.* A mortgage transaction secured by a consumer's interest in a "timeshare plan," as defined in 11 U.S.C. 101(53D), [that is also a Federally related mortgage loan under RESPA] is subject to the requirements of § 226.19(a)[(5)]►(4)◄ instead of the requirements of § 226.19(a)(1) through § 226.19(a)[(4)]►(3)◄. *See* comment 19(a)(1)(i)–1. Early disclosures for transactions subject to § 226.19(a)[(5)]►(4)◄ must be given (a) before consummation or (b) within three business days after the creditor receives the consumer's written application, whichever is earlier. The general definition of "business day" in § 226.2(a)(6)—a day on which the creditor's offices are open to the public for substantially all of its business functions—applies for purposes of § 226.19(a)(5)(ii). *See* comment 2(a)(6)–1. These timing requirements are different from the timing requirements under § 226.19(a)(1)(i). Timeshare transactions covered by § 226.19(a)[(5)] may be consummated any time after the disclosures required by § 226.19(a)[(5)]►(4)◄(ii) are provided.

2. *Use of estimates.* If the creditor does not know the precise credit terms, the creditor must base the disclosures on the best information reasonably available and indicate that the disclosures are estimates under § 226.17(c)(2). If many of the disclosures are estimates, the creditor may include a statement to that effect (such as "all numerical disclosures [except the late-payment disclosure] are estimates") instead of separately labelling each estimate. In the alternative, the creditor may label as an estimate only the items primarily affected by unknown information. (*See* the commentary to § 226.17(c)(2).) The creditor may provide explanatory material concerning the estimates and the contingencies that may affect the actual terms, in accordance with the commentary to § 226.17(a)(1)[.]►and § 226.37. The disclosures required by § 226.19(a)(2) may not contain estimates, however, with limited exceptions. See the commentary on § 226.19(a)(2) for a discussion of limitations on estimates in disclosures made under that subsection.◄

3. *Written application.* For timeshare transactions, creditors may rely on comment 19(a)(1)(i)–[3]►2◄ in determining whether a "written application" has been received.

4. *Denied or withdrawn applications.* For timeshare transactions, creditors may rely on comment 19(a)(1)(i)–[4]►3◄ in determining that disclosures are not required by § 226.19(a)[(5)]►(4)◄(ii) because the consumer's application will not or cannot be approved on the terms

requested or the consumer has withdrawn the application.

5. *Itemization of amount financed.* For timeshare transactions, creditors may rely on comment 19(a)(1)(i)–[5]►4◄ in determining whether providing the good faith estimates of settlement costs required by RESPA satisfies the requirement of § 226.18(c) to provide an itemization of the amount financed.

19(a)[*(5)*]►*(4)*◄*(iii) Redisclosure for timeshare plans.*

1. *Consummation or settlement.* For extensions of credit secured by a consumer's timeshare plan, when corrected disclosures are required, they must be given no later than ''consummation or settlement.'' ''Consummation'' is defined in § 226.2(a). ''Settlement'' is defined in Regulation X (24 CFR 3500.2(b)) and is subject to any interpretations issued by HUD. In some cases, a creditor may delay redisclosure until settlement, which may be at a time later than consummation. If a creditor chooses to redisclose at settlement, disclosures may be based on the terms in effect at settlement, rather than at consummation. For example, in a variable-rate transaction, a creditor may choose to base disclosures on the terms in effect at settlement, despite the general rule in comment [17(c)(1)–8]►§ 226.17(c)(1)(iii)◄ that variable-rate disclosures ►generally◄ should be based on the terms in effect at consummation.

2. *Content of new disclosures.* Creditors may rely on comment 19(a)(2)(ii)–2 in determining the content of corrected disclosures required under § 226.19(a)[(5)]►(4)◄(iii).

19(b) [Certain variable-rate transactions]►*Adjustable-rate mortgages*◄.

[1. *Coverage.* Section 226.19(b) applies to all closed-end variable-rate transactions that are secured by the consumer's principal dwelling and have a term greater than one year. The requirements of this section apply not only to transactions financing the initial acquisition of the consumer's principal dwelling, but also to any other closed-end variable-rate transaction secured by the principal dwelling. Closed-end variable-rate transactions that are not secured by the principal dwelling, or are secured by the principal dwelling but have a term of one year or less, are subject to the disclosure requirements of § 226.18(f)(1) rather than those of § 226.19(b). (Furthermore, ''shared-equity'' or ''shared-appreciation'' mortgages are subject to the disclosure requirements of § 226.18(f)(1) rather than those of § 226.19(b) regardless of the general coverage of those sections.) For purposes of this section, the term of a variable-rate demand loan is determined in accordance with the commentary to § 226.17(c)(5). In determining whether a construction loan that may be permanently financed by the same creditor is covered under this section, the creditor may treat the construction and the permanent phases as separate transactions with distinct terms to maturity or a single combined transaction. For purposes of the disclosures required under § 226.18, the creditor may nevertheless treat the two phases either as separate transactions or as a single combined transaction in accordance with § 226.17(c)(6). Finally, in any assumption of a variable-rate transaction secured by the consumer's principal dwelling with a term greater than one year, disclosures need not be provided under §§ 226.18(f)(2)(ii) or 226.19(b).]

►1. *Coverage.* Section 226.19(b) applies to all closed-end adjustable-rate mortgages described in § 226.38(a)(i) that are secured by real property or a dwelling. Closed-end adjustable-rate transactions that are not secured by real property or a dwelling are subject to the disclosure requirements of § 226.18(f) rather than those of § 226.19(b). In determining whether a construction loan that may be permanently financed by the same creditor is covered under this section, the creditor may treat the construction and the permanent phases as separate transactions with distinct terms to maturity or a single combined transaction. *See* comment 17(c)(6)–2. In any assumption of an adjustable-rate transaction secured by real property or a dwelling, disclosures need not be provided under § 226.19(b).◄

[2. *Timing.* A creditor must give the disclosures required under this section at the time an application form is provided or before the consumer pays a nonrefundable fee, whichever is earlier.

i. *Intermediary agent or broker.* In cases where a creditor receives a written application through an intermediary agent or broker, however, footnote 45b provides a substitute timing rule requiring the creditor to deliver the disclosures or place them in the mail not later than three business days after the creditor receives the consumer's written application. (See comment 19(b)–3 for guidance in determining whether or not the transaction involves an intermediary agent or broker.) This three-day rule also applies where the creditor takes an application over the telephone.

ii. *Telephone request.* In cases where the consumer requests an application form over the telephone, the creditor must include the early disclosures required under this section with the application that is sent to the consumer.

iii. *Mail solicitations.* In cases where the creditor solicits applications through the mail, the creditor must also send the disclosures required under this section if an application form is included with the solicitation.

iv. *Conversion.*]►2. *Disclosure at the time of conversion.*◄ In cases where an open-end credit account will convert to a closed-end transaction subject to this section under a written agreement with the consumer, disclosures under this section [may be given at the time of conversion.]►must be given at or before the time of conversion.◄ (See the commentary to § 226.20(a) for information on the timing requirements for § 226.19(b)[(2)] disclosures when [a variable-rate]►an adjustable-rate◄ feature is later added to a transaction.)

[v. *Form of electronic disclosures provided on or with electronic applications.* Creditors must provide the disclosures required by this section (including the brochure) on or with a blank application that is made available to the consumer in electronic form, such as on a creditor's Internet Web site. Creditors have flexibility in satisfying this requirement. Methods creditors could use to satisfy the requirement include, but are not limited to, the following examples:

A. The disclosures could automatically appear on the screen when the application appears;

B. The disclosures could be located on the same web page as the application (whether or not they appear on the initial screen), if the application contains a clear and conspicuous reference to the location of the disclosures and indicates that the disclosures contain rate, fee, and other cost information, as applicable;

C. Creditors could provide a link to the electronic disclosures on or with the application as long as consumers cannot bypass the disclosures before submitting the application. The link would take the consumer to the disclosures, but the consumer need not be required to scroll completely through the disclosures; or

D. The disclosures could be located on the same web page as the application without necessarily appearing on the initial screen, immediately preceding the button that the consumer will click to submit the application.

Whatever method is used, a creditor need not confirm that the consumer has read the disclosures.

3. *Intermediary agent or broker.* In certain transactions involving an ''intermediary agent or broker,'' a creditor may delay providing

disclosures. A creditor may not delay providing disclosures in transactions involving either a legal agent (as determined by applicable law) or any other third party that is not an ''intermediary agent or broker.'' In determining whether or not a transaction involves an ''intermediary agent or broker'' the following factors should be considered:

• The number of applications submitted by the broker to the creditor as compared to the total number of applications received by the creditor. The greater the percentage of total loan applications submitted by the broker in any given period of time, the less likely it is that the broker would be considered an ''intermediary agent or broker'' of the creditor during the next period.

• The number of applications submitted by the broker to the creditor as compared to the total number of applications received by the broker. (This factor is applicable only if the creditor has such information.) The greater the percentage of total loan applications received by the broker that is submitted to a creditor in any given period of time, the less likely it is that the broker would be considered an ''intermediary agent or broker'' of the creditor during the next period.

• The amount of work (such as document preparation) the creditor expects to be done by the broker on an application based on the creditor's prior dealings with the broker and on the creditor's requirements for accepting applications, taking into consideration the customary practice of brokers in a particular area. The more work that the creditor expects the broker to do on an application, in excess of what is usually expected of a broker in that area, the less likely it is that the broker would be considered an ''intermediary agent or broker'' of the creditor. An example of an ''intermediary agent or broker'' is a broker who, customarily within a brief period of time after receiving an application, inquires about the credit terms of several creditors with whom the broker does business and submits the application to one of them. The broker is responsible for only a small percentage of the applications received by that creditor. During the time the broker has the application, it might request a credit report and an appraisal (or even prepare an entire loan package if customary in that particular area).

4. *Other variable-rate regulations.* Transactions in which the creditor is required to comply with and has complied with the disclosure requirements of the variable-rate regulations of other Federal agencies are exempt from the requirements of § 226.19(b), by virtue of footnote 45a, and are exempt from the requirements of § 226.20(c), by virtue of footnote 45c. Those variable-rate regulations include the regulations issued by the Federal Home Loan Bank Board and those issued by the Department of Housing and Urban Development. The exception in footnotes 45a and 45c is also available to creditors that are required by State law to comply with the federal variable-rate regulations noted above and to creditors that are authorized by title VIII of the Depository Institutions Act of 1982 (12 U.S.C. 3801 et seq.) to make loans in accordance with those regulations. Creditors using this exception should comply with the timing requirements of those regulations rather than the timing requirements of Regulation Z in making the variable-rate disclosures.

5. *Examples of variable-rate transactions.*

(i) The following transactions, if they have a term greater than one year and are secured by the consumer's principal dwelling, constitute variable-rate mortgages subject to the disclosure requirements of § 226.19(b).]

►3. *Non-adjustable-rate mortgages.* The following transactions, if they are secured by real property or a dwelling, do not constitute adjustable-rate mortgages subject to the disclosure requirements of § 226.19(b).◄

[(A)]►(i)◄ Renewable balloon-payment instruments [where]►that have a fixed rate of interest, even if◄ the creditor is both unconditionally obligated to renew the balloon-payment loan at the consumer's option (or is obligated to renew subject to conditions within the consumer's control) and has the option of increasing the interest rate at the time of renewal. (See comment [17(c)(1)–11]►17(c)(1)(iii)–4◄ for a discussion of conditions within a consumer's control in connection with renewable balloon-payment loans.)

[(B)]►(ii)◄ Preferred-rate loans where the terms of the legal obligation provide that the initial underlying rate is fixed but will increase upon the occurrence of some event, such as an employee leaving the employ of the creditor, and the note reflects the preferred rate. [The disclosures under §§ 226.19(b)(1) and 226.19(b)(2)(v), (viii), (ix), and (xii) are not applicable to such loans.]

[(C)]►(iii)◄ ''Price-level-adjusted mortgages'' or other indexed mortgages that have a fixed rate of interest but provide for periodic adjustments to payments and the loan balance to reflect changes in an index measuring prices or inflation. [The disclosures under § 226.19(b)(1) are not applicable to such loans, nor are the following provisions to the extent they relate to the determination of the interest rate by the addition of a margin, changes in the interest rate, or interest rate discounts: Section 226.19(b)(2)(i), (iii), (iv), (v), (vi), (vii), (viii), and (ix).] (See comments 20(c)-2 and 30–1 regarding the inapplicability of variable-rate adjustment notices and interest rate limitations to price-level-adjusted or similar mortgages.)

[(ii)]►(iv)◄ Graduated-payment mortgages and step-rate transactions without ►an adjustable-rate feature.◄[a variable-rate feature are not considered variable-rate transactions].

[*Paragraph 19(b)(1).*

1. *Substitute.* Creditors who wish to use publications other than the *Consumer Handbook on Adjustable Rate Mortgages* must make a good faith determination that their brochures are suitable substitutes to the *Consumer Handbook.* A substitute is suitable if it is, at a minimum, comparable to the *Consumer Handbook* in substance and comprehensiveness. Creditors are permitted to provide more detailed information than is contained in the *Consumer Handbook.*

2. *Applicability.* The *Consumer Handbook* need not be given for variable-rate transactions subject to this section in which the underlying interest rate is fixed. (See comment 19(b)–5 for an example of a variable-rate transaction where the underlying interest rate is fixed.)]

[*Paragraph 19(b)(2).*

1.]►4. ◄ *Disclosure for each [variable]►adjustable◄-rate mortgage program.* A creditor must provide disclosures to the consumer that [fully] describe each of the creditor's [variable]►adjustable◄-rate mortgage programs in which the consumer expresses an interest. If a program is made available only to certain customers of an institution, a creditor need not provide disclosures for that program to other consumers who express a general interest in a creditor's ARM programs. [Disclosures must be given at the time an application form is provided or before the consumer pays a nonrefundable fee, whichever is earlier. If program disclosures cannot be provided because a consumer expresses an interest in individually negotiating loan terms that are not generally offered, disclosures reflecting those terms may be provided as soon as reasonably possible after the terms have been decided upon, but not later than the time a non-refundable fee is paid. If a consumer who has received program disclosures subsequently expresses an interest in other available variable-rate mortgage programs subject to 226.19(b)(2), or the creditor and consumer decide on a program for which the consumer has not received disclosures, the creditor must provide appropriate disclosures as soon as reasonably possible. The creditor, of course, is permitted to give the consumer information about additional programs subject to § 226.19(b) initially.]

[2. *Variable-rate loan program disclosure defined.*]►5. *Adjustable-rate mortgage loan program defined.* ◄ i. Generally, if the identification, the presence or absence, or the exact value of a loan feature must be disclosed under this section, [variable]►adjustable◄-rate mortgage loans that differ as to such features constitute separate loan programs. For example, separate loan programs would exist based on differences in any of the following loan features:

A. The index or other formula used to calculate interest rate adjustments.

B. The rules relating to changes in the index value, interest rate, ►and◄ payments[, and loan balance].

C. The presence or absence of, and the amount of, rate or payment caps.

D. The presence of a demand feature.

E. The possibility of negative amortization.

F. The possibility of interest rate carryover.

G. The frequency of interest rate and payment adjustments.

H. The presence of a discount ►or premium◄ feature.

I. [In addition, if a loan feature must be taken into account in preparing the disclosures required by § 226.19(b)(2)(viii), variable-rate mortgage loans that differ as to that feature constitute separate programs under § 226.19(b)(2).]►The presence of a prepayment penalty provision.

J. The possibility of making interest-only payments.

K. The presence of a balloon payment feature.

L. The presence of a shared-equity or shared-appreciation feature.

M. The possibility of providing less than full documentation of income or assets.

N. The presence of a demand feature.◄

ii. If, however, [a representative value may be given for a loan feature or the feature need not be disclosed under § 226.19(b)(2), variable-rate]►a feature is not required or permitted to be disclosed under § 226.19(b), adjustable-rate◄ mortgage loans that differ as to such features do not constitute separate loan programs. For example, separate programs would not exist based on differences in the following loan features:

A. The amount of a discount ►or premium◄.

B. The amount of a margin.

[3. *Form of program disclosures.* A creditor may provide separate program disclosure forms for each ARM loan program it offers or a single disclosure form that describes multiple programs. A disclosure form may consist of more than one page. For example, a creditor may attach a separate page containing the historical payment example for a particular program. A disclosure form describing more than one program need not repeat information applicable to each program that is described. For example, a form describing multiple programs may disclose the information applicable to all of the programs in one place with the various program features (such as options permitting conversion to a fixed rate) disclosed separately. The form, however, must state if any program feature that is described is available only in conjunction with certain other program features. Both the separate and multiple program disclosures may illustrate more than one loan maturity or payment amortization—for example, by including multiple payment and loan balance columns in the historical payment example. Disclosures may be inserted or printed in the *Consumer Handbook* (or a suitable substitute) as long as they are identified as the creditor's loan program disclosures.

4. *As applicable.* The disclosures required by this section need only be made as applicable. Any disclosure not relevant to a particular transaction may be eliminated. For example, if the transaction does not contain a demand feature, the disclosure required under § 226.19(b)(2)(x) need not be given. As used in this section, payment refers only to a payment based on the interest rate, loan balance and loan term, and does not refer to payment of other elements such as mortgage insurance premiums.]

►6. *Payment.* As used in this section, payment refers only to a payment based on the interest rate, loan balance and loan term, and does not refer to payment of other elements such as mortgage insurance premiums.◄

[5.]►7.◄ *Revisions.* A creditor must revise the disclosures required under this section [once a year] as soon as reasonably possible [after the new index value becomes available. Revisions to the disclosures also are required] when the loan program changes.

[*Paragraph 19(b)(2)(i).*

1. *Change in interest rate, payment, or term.* A creditor must disclose the fact that the terms of the legal obligation permit the creditor, after consummation of the transaction, to increase (or decrease) the interest rate, payment, or term of the loan initially disclosed to the consumer. For example, the disclosures for a variable-rate mortgage loan program in which the interest rate and payment (but not loan term) can change might read, ''Your interest rate and payment can change yearly.'' In transactions where the term of the loan may change due to rate fluctuations, the creditor must state that fact.

Paragraph 19(b)(2)(ii).

1. *Identification of index or formula.* If a creditor ties interest rate changes to a particular index, this fact must be disclosed, along with a source of information about the index. For example, if a creditor uses the weekly average yield on U.S. Treasury Securities adjusted to a constant maturity as its index, the disclosure might read, ''Your index is the weekly average yield on U.S. Treasury Securities adjusted to a constant maturity of one year published weekly in the Wall Street Journal.'' If no particular index is used, the creditor must briefly describe the formula used to calculate interest rate changes.

2. *Changes at creditor's discretion.* If interest rate changes are at the creditor's discretion, this fact must be disclosed. If an index is internally defined, such as by a creditor's prime rate, the creditor should either briefly describe that index or state that interest rate changes are at the creditor's discretion.

Paragraph 19(b)(2)(iii).

1. *Determination of interest rate and payment.* This provision requires an explanation of how the creditor will determine the consumer's interest rate and payment. In cases where a creditor bases its interest rate on a specific index and adjusts the index through the addition of a margin, for example, the disclosure might read, ''Your interest rate is based on the index plus a margin, and your payment will be based on the interest rate, loan balance, and remaining loan term.'' In transactions where paying the periodic payments will not fully amortize the outstanding balance at the end of the loan term and where the final payment will equal the periodic payment plus the remaining unpaid balance, the creditor must disclose this fact. For example, the disclosure might read, ''Your periodic payments will not fully amortize your loan and you will be required to make a single payment of the periodic payment plus the remaining unpaid balance at the end of the loan term.'' The creditor, however, need not reflect any irregular final payment in the historical example or in the disclosure

of the initial and maximum rates and payments. If applicable, the creditor should also disclose that the rate and payment will be rounded.

Paragraph 19(b)(2)(iv).

1. *Current margin value and interest rate.* Because the disclosures can be prepared in advance, the interest rate and margin may be several months old when the disclosures are delivered. A statement, therefore, is required alerting consumers to the fact that they should inquire about the current margin value applied to the index and the current interest rate. For example, the disclosure might state, ''Ask us for our current interest rate and margin.'']

►*19(b)(1) Interest rate and payment disclosures*

1. *As applicable.* The disclosures required by § 226.19(b)(1) need only be made as applicable. Any disclosure not relevant to a particular loan program may be omitted.◄

[*Paragraph 19(b)(2)(v).*]►*Paragraph 19(b)(1)(i)*◄

1. *Discounted and premium interest rate.* In some [variable]►adjustable◄-rate mortgage loan transactions, creditors may set an initial interest rate that is not determined by the index or formula used to make later interest rate adjustments. Typically, this initial rate charged to consumers is lower than the rate would be if it were calculated using the index or formula. However, in some cases the initial rate may be higher. If the initial interest rate will be a discount or a premium rate, creditors must alert the consumer to this fact. For example, if a creditor discounted a consumer's initial rate, the disclosure might state, [''Your initial interest rate is not based on the index used to make later adjustments.'']►''The interest rate is discounted and will stay the same for a 5-year introductory period. After this initial period, the interest rate will increase, even if market rates do not change.''◄ (See the commentary to § 226.17(c)(1) for a further discussion of discounted and premium variable-rate transactions.) [In addition, the disclosure must suggest that consumers inquire about the amount that the program is currently discounted. For example, the disclosure might state, ''Ask us for the amount our adjustable rate mortgages are currently discounted.''] In a transaction with a consumer buydown or with a third-party buydown that will be incorporated in the legal obligation, the creditor should disclose the program as a discounted [variable]►adjustable◄-rate mortgage transaction, but need not disclose additional information regarding the buydown in its program disclosures. [(See the commentary to § 226.19(b)(2)(viii) for a discussion of how to reflect the discount or premium in the historical example or the maximum rate and payment disclosure).]

[*Paragraph 19(b)(2)(vi)*]►*Paragraph 19(b)(1)(ii)*◄.

1. *Frequency.* The frequency of interest rate and payment adjustments must be disclosed. If interest rate changes will be imposed more frequently or at different intervals than payment changes, a creditor must disclose the frequency and timing of both types of changes. For example, in [a variable]►an adjustable◄-rate mortgage transaction where interest rate changes are made monthly, but payment changes occur on an annual basis, this fact must be disclosed. In certain ARM transactions, the interval between loan closing and the initial adjustment is not known and may be different than the regular interval for adjustments. In such cases, the creditor may disclose the initial adjustment period as a range of the minimum and maximum amount of time from consummation or closing. For example, the creditor might state: ''The first adjustment to your interest rate and payment will occur no sooner than 6 months and no later than 18 months after closing. Subsequent adjustments may occur once each year after the first adjustment.'' [(See comments 19(b)(2)(viii)(A)–7 and 19(b)(2)(viii)(B)–4 for guidance on other disclosures when this alternative disclosure rule is used.)]

►*Paragraph 19(b)(1)(iii).*

1. *Identification of index or formula.* If a creditor ties interest rate changes to a particular index, this fact must be disclosed, along with a source of information about the index. If no particular index is used, the creditor must briefly describe the formula used to calculate interest rate changes. To describe the index used, the disclosure might state, for example:

i. ''Your interest rate will be based on the '1-year CMT' (Constant Maturity Treasury) index plus a margin we determine upon application. That index is published weekly in the *Wall Street Journal* and is available on the Web site of the Federal Reserve Board.''

ii. ''Your interest rate is based on the 1-year LIBOR Index plus a margin that is determined at application. This index is published daily in the *Wall Street Journal.''*

iii. ''The interest rate is based on the 11th District COFI Index (Cost of Funds Index for 11th District Federal Home Loan Bank (FHLB)) plus a margin determined upon application. The 11th District COFI Index is published monthly on the Web site of the San Francisco FHLB.''

2. *Changes at creditor's discretion.* If interest rate changes are at the creditor's discretion, this fact must be disclosed. If an index is internally defined, such as by a creditor's prime rate, the creditor should either briefly describe that index or state that interest rate changes are at the creditor's discretion.◄

[*Paragraph 19(b)(2)(vii)*]►*Paragraph 19(b)(1)(iv)*◄.

1. *Rate and payment caps.* The creditor must disclose limits on changes (increases or decreases) in the interest rate or payment. If an initial discount is not taken into account in applying overall or periodic rate limitations, that fact must be disclosed. If separate overall or periodic limitations apply to interest rate increases resulting from other events, such as [the exercise of a fixed-rate conversion option or] leaving the creditor's employ, those limitations must also be stated. ►If separate overall periodic limitations apply to interest rate increases resulting from the consumer's exercise of a fixed-rate conversion option, those limitations must be stated with the disclosures about the option required by § 226.19(b)(1)(v).◄ Limitations do not include legal limits in the nature of usury or rate ceilings under State or Federal statutes or regulations. (See § 226.30 for the rule requiring that a maximum interest rate be included in certain [variable]►adjustable◄-rate mortgage transactions.) The creditor need not disclose each periodic or overall rate limitation that is currently available. As an alternative, the creditor may disclose the range of the lowest and highest periodic and overall rate limitations that may be applicable to the creditor's ARM transactions. For example, the creditor might state: ►''Your interest rate can increase between 1 and 2 percentage points in any one year and between 4 and 7 percentage points over the life of the loan.◄[''The limitation on increases to your interest rate at each adjustment will be set at an amount in the following range: Between 1 and 2 percentage points at each adjustment. The limitation on increases to your interest rate over the term of the loan will be set at an amount in the following range: Between 4 and 7 percentage points above the initial interest rate.'' A creditor using this alternative rule must include a statement in its program disclosures suggesting that the consumer ask about the overall rate limitations currently offered for the creditor's ARM loan programs. (See comments 19(b)(2)(viii)(A)–6 and 19(b)(2)(viii)(B)–3 for an explanation of

the additional requirements for a creditor using this alternative rule for disclosure of periodic and overall rate limitations.)

2. *Negative amortization and interest rate carryover.* A creditor must disclose, where applicable, the possibility of negative amortization. For example, the disclosure might state, ''If any of your payments is not sufficient to cover the interest due, the difference will be added to your loan amount.'' Loans that provide for more than one way to trigger negative amortization are separate variable-rate mortgage programs requiring separate disclosures. (See the commentary to § 226.19(b)(2) for a discussion on the definition of a variable-rate mortgage loan program and the format for disclosure.) If a consumer is given the option to cap monthly payments that may result in negative amortization, the creditor must fully disclose the rules relating to the option, including the effects of exercising the option (such as negative amortization will occur and the principal loan balance will increase); however, the disclosure in § 226.19(b)(2)(viii) need not be provided.

3. *Conversion option.* If a loan program permits consumers to convert their variable-rate mortgage loans to fixed-rate loans, the creditor must disclose that the interest rate may increase if the consumer converts the loan to a fixed-rate loan. The creditor must also disclose the rules relating to the conversion feature, such as the period during which the loan may be converted, that fees may be charged at conversion, and how the fixed rate will be determined. The creditor should identify any index or other measure or formula used to determine the fixed rate and state any margin to be added. In disclosing the period during which the loan may be converted and the margin, the creditor may use information applicable to the conversion feature during the six months preceding preparation of the disclosures and state that the information is representative of conversion features recently offered by the creditor. The information may be used until the program disclosures are otherwise revised. Although the rules relating to the conversion option must be disclosed, the effect of exercising the option should not be reflected elsewhere in the disclosures, such as in the historical example or in the calculation of the initial and maximum interest rate and payments.

4. *Preferred-rate loans.* Section 226.19(b) applies to preferred-rate loans, where the rate will increase upon the occurrence of some event, such as an employee leaving the creditor's employ, whether or not the underlying rate is fixed or variable. In these transactions, the creditor must disclose the event that would allow the creditor to increase the rate such as that the rate may increase if the employee leaves the creditor's employ. The creditor must also disclose the rules relating to termination of the preferred rate, such as that fees may be charged when the rate is changed and how the new rate will be determined.

Paragraph 19(b)(2)(viii).

1. *Historical example and initial and maximum interest rates and payments.* A creditor may disclose both the historical example and the initial and maximum interest rates and payments.

Paragraph 19(b)(2)(viii)(A).

1. *Index movement.* This section requires a creditor to provide an historical example, based on a $10,000 loan amount originating in 1977, showing how interest rate changes implemented according to the terms of the loan program would have affected payments and the loan balance at the end of each year during a 15-year period. (In all cases, the creditor need only calculate the payments and loan balance for the term of the loan. For example, in a five-year loan, a creditor would show the payments and loan balance for the five-year term, from 1977 to 1981, with a zero loan balance reflected for 1981. For the remaining ten years, 1982–1991, the creditor need only show the remaining index values, margin and interest rate and must continue to reflect all significant loan program terms such as rate limitations affecting them.) Pursuant to this section, the creditor must provide a history of index values for the preceding 15 years. Initially, the disclosures would give the index values from 1977 to the present. Each year thereafter, the revised program disclosures should include an additional year's index value until 15 years of values are shown. If the values for an index have not been available for 15 years, a creditor need only go back as far as the values are available in giving a history and payment example. In all cases, only one index value per year need be shown. Thus, in transactions where interest rate adjustments are implemented more frequently than once per year, a creditor may assume that the interest rate and payment resulting from the index value chosen will stay in effect for the entire year for purposes of calculating the loan balance as of the end of the year and for reflecting other loan program terms. In cases where interest rate changes are at the creditor's discretion (see the commentary to § 226.19(b)(2)(ii)), the creditor must provide a history of the rates imposed for the preceding 15 years, beginning with the rates in 1977. In giving this history, the creditor need only go back as far as the creditor's rates can reasonably be determined.

2. *Selection of index values.* The historical example must reflect the method by which index values are determined under the program. If a creditor uses an average of index values or any other index formula, the history given should reflect those values. The creditor should select one date or, when an average of single values is used as an index, one period and should base the example on index values measured as of that same date or period for each year shown in the history. A date or period at any time during the year may be selected, but the same date or period must be used for each year in the historical example. For example, a creditor could use values for the first business day in July or for the first week ending in July for each of the 15 years shown in the example.

3. *Selection of margin.* For purposes of the disclosure required under § 226.19(b)(2)(viii)(A), a creditor may select a representative margin that has been used during the six months preceding preparation of the disclosures, and should disclose that the margin is one that the creditor has used recently. The margin selected may be used until a creditor revises the disclosure form.

4. *Amount of discount or premium.* For purposes of the disclosure required under § 226.19(b)(2)(viii)(A), a creditor may select a discount or premium (amount and term) that has been used during the six months preceding preparation of the disclosures, and should disclose that the discount or premium is one that the creditor has used recently. The discount or premium should be reflected in the historical example for as long as the discount or premium is in effect. A creditor may assume that a discount that would have been in effect for any part of a year was in effect for the full year for purposes of reflecting it in the historical example. For example, a 3-month discount may be treated as being in effect for the entire first year of the example; a 15-month discount may be treated as being in effect for the first two years of the example. In illustrating the effect of the discount or premium, creditors should adjust the value of the interest rate in the historical example, and should not adjust the margin or index values. For example, if during the six months preceding preparation of the disclosures the fully indexed rate would have been 10% but the first year's rate under the program was 8%, the creditor would discount the first interest rate in the

historical example by 2 percentage points.

5. *Term of the loan.* In calculating the payments and loan balances in the historical example, a creditor need not base the disclosures on each term to maturity or payment amortization that it offers. Instead, disclosures for ARMs may be based upon terms to maturity or payment amortizations of 5, 15 and 30 years, as follows: ARMs with terms or amortizations from over 1 year to 10 years may be based on a 5-year term or amortization; ARMs with terms or amortizations from over 10 years to 20 years may be based on a 15-year term or amortization; and ARMs with terms or amortizations over 20 years may be based on a 30-year term or amortization. Thus, disclosures for ARMs offered with any term from over 1 year to 40 years may be based solely on terms of 5, 15 and 30 years. Of course, a creditor may always base the disclosures on the actual terms or amortizations offered. If the creditor bases the disclosures on 5-, 15- or 30-year terms or payment amortization as provided above, the term or payment amortization used in making the disclosure must be stated.

6. *Rate caps.* A creditor using the alternative rule described in comment 19(b)(2)(vii)–1 for disclosure of rate limitations must base the historical example upon the highest periodic and overall rate limitations disclosed under section 226.19(b)(2)(vii). In addition, the creditor must state the limitations used in the historical example. (See comment 19(b)(2)(viii)(B)–3 for an explanation of the use of the highest rate limitation in other disclosures.)

7. *Frequency of adjustments.* In certain transactions, creditors may use the alternative rule described in comment 19(b)(2)(vi)–1 for disclosure of the frequency of rate and payment adjustments. In such cases, the creditor may assume for purposes of the historical example that the first adjustment occurred at the end of the first full year in which the adjustment could occur. For example, in an ARM in which the first adjustment may occur between 6 and 18 months after closing and annually thereafter, the creditor may assume that the first adjustment occurred at the end of the first year in the historical example. (See comment 19(b)(2)(viii)(B)–4 for an explanation of how to compute the maximum interest rate and payment when the initial adjustment period is not known.)

Paragraph 19(b)(2)(viii)(B).

1. *Initial and maximum interest rates and payments.* The disclosure form must state the initial and maximum interest rates and payments for a $10,000 loan originated at an initial interest rate (index value plus margin adjusted by the amount of any discount or premium) in effect as of an identified month and year for the loan program disclosure. (See comment 19(b)(2)–5 on revisions to the loan program disclosure.) In calculating the maximum payment under this paragraph, a creditor should assume that the interest rate increases as rapidly as possible under the loan program, and the maximum payment disclosed should reflect the amortization of the loan during this period. Thus, in a loan with 2 percentage point annual (and 5 percentage point overall) interest rate limitations or ''caps,'' the maximum interest rate would be 5 percentage points higher than the initial interest rate disclosed. Moreover, the loan would not reach the maximum interest rate until the fourth year because of the 2 percentage point annual rate limitations, and the maximum payment disclosed would reflect the amortization of the loan during this period. If the loan program includes a discounted or premium initial interest rate, the initial interest rate should be adjusted by the amount of the discount or premium.

2. *Term of the loan.* In calculating the initial and maximum payments, the creditor need not base the disclosures on each term to maturity or payment amortization offered under the program. Instead, the creditor may follow the rules set out in comment 19(b)(2)(viii)(A)–5. If a historical example is provided under § 226.19(b)(2)(viii)(A), the terms to maturity or payment amortization used in the historical example must be used in calculating the initial and maximum payment. In addition, creditors must state the term or payment amortization used in making the disclosures under this section.

3. *Rate caps.* A creditor using the alternative rule for disclosure of interest rate limitations described in comment 19(b)(2)(vii)–1 must calculate the maximum interest rate and payment based upon the highest periodic and overall rate limitations disclosed under § 226.19(b)(2)(vii). In addition, the creditor must state the rate limitations used in calculating the maximum interest rate and payment. (See comment 19(b)(2)(viii)(A)–6 for an explanation of the use of the highest rate limitation in other disclosures.)

4. *Frequency of adjustments.* In certain transactions, a creditor may use the alternative rule for disclosure of the frequency of rate and payment adjustments described in comment 19(b)(2)(vi)–1. In such cases, the creditor must base the calculations of the initial and maximum rates and payments upon the earliest possible first adjustment disclosed under § 226.19(b)(2)(vi). (See comment 19(b)(2)(viii)(A)–7 for an explanation of how to disclose the historical example when the initial adjustment period is not known.)

5. *Periodic payment statement.* The statement that the periodic payment may increase or decrease substantially may be satisfied by the disclosure in paragraph 19(b)(2)(vi) if it states for example, ''your monthly payment can increase or decrease substantially based on annual changes in the interest rate.''

Paragraph 19(b)(2)(ix).

1. *Calculation of payments.* A creditor is required to include a statement on the disclosure form that explains how a consumer may calculate his or her actual monthly payments for a loan amount other than $10,000. The example should be based upon the most recent payment shown in the historical example or upon the initial interest rate reflected in the maximum rate and payment disclosure. In transactions in which the latest payment shown in the historical example is not for the latest year of index values shown (such as in a five-year loan), a creditor may provide additional examples based on the initial and maximum payments disclosed under § 226.19(b)(2)(viii)(B). The creditor, however, is not required to calculate the consumer's payments. (See the model clauses in appendix H–4(C).)

Paragraph 19(b)(2)(x).

1. *Demand feature.* If a variable-rate mortgage loan subject to § 226.19(b) requirements contains a demand feature as discussed in the commentary to § 226.18(i), this fact must be disclosed. (Pursuant to § 226.18(i), creditors would also disclose the demand feature in the standard disclosures given later.)

Paragraph 19(b)(2)(xi).

1. *Adjustment notices.* A creditor must disclose to the consumer the type of information that will be contained in subsequent notices of adjustments and when such notices will be provided. (See the commentary to § 226.20(c) regarding notices of adjustments.) For example, the disclosure might state, ''You will be notified at least 25, but no more than 120, days before the due date of a payment at a new level. This notice will contain information about the index and interest rates, payment amount, and loan balance.'' In transactions where there may be interest rate adjustments without accompanying payment adjustments in a year, the disclosure might read, ''You will be notified once each year during which interest rate adjustments, but no payment adjustments, have been made to your loan. This notice will contain

information about the index and interest rates, payment amount, and loan balance.''

Paragraph 19(b)(2)(xii).

1. *Multiple loan programs.* A creditor that offers multiple variable-rate mortgage loan programs is required to have disclosures for each variable-rate mortgage loan program subject to § 226.19(b)(2). Unless disclosures for all of its variable-rate programs are provided initially, the creditor must inform the consumer that other closed-end variable-rate programs exist, and that disclosure forms are available for these additional loan programs. For example, the disclosure form might state, ''Information on other adjustable rate mortgage programs is available upon request.'']

►*19(b)(2) Key questions about risk.*

19(b)(2)(i) Required disclosures.

1. *Disclosure of first rate or payment increase.* The requirement under § 226.19(b)(2)(i)(A) and (B) to disclose when the first interest rate or payment increase may occur refers to the time period in which the increase may occur, not the exact calendar date. For example, the disclosure may state, ''Your interest rate may increase at the end of the 3-year introductory period.''

19(b)(2)(i)(C) Prepayment penalty as risk factor.

1. *Coverage.* See comment 38(a)(5)–1 to determine whether there is a prepayment penalty.

2. *Penalty.* See comment 38(a)(5)–2 for examples of charges that are prepayment penalties.

3. *Not penalty.* See comment 38(a)(5)–3 for examples of charges that are not prepayment penalties.

19(b)(2)(ii) Additional disclosures.

1. *As applicable.* The disclosures required by § 226.19(b)(2)(ii) need only be made as applicable. Any disclosure not relevant to a particular loan program may be omitted.

19(b)(2)(ii)(C) Balloon payment.

1. *Coverage.* The creditor must make the disclosure required by § 226.19(b)(ii)(B) if the loan program includes a payment schedule with regular periodic payments that when aggregated do not fully amortize the outstanding principal balance.

2. *Time period.* The requirement to disclose when the balloon payment is due refers to the time period when it is due, not the exact calendar date. For example, the disclosure may state, ''You would owe a balloon payment due in seven years.''

19(b)(2)(ii)(D) Demand feature.

1. *Disclosure requirements.* The disclosure requirements of § 226.19(b)(2)(ii)(D) apply not only to transactions payable on demand from the outset, but also to transactions that convert to a demand status after a stated period.

2. *Covered demand features.* See comment 18(i)–2 for examples of covered demand features.

19(c) Conversion to closed-end credit.

1. *Disclosure at the time of conversion.* In cases where an open-end credit account will convert to a closed-end transaction under a written agreement with the consumer, disclosures are not required under § 226.19(c). By contrast, disclosures are required in such cases under § 226.19(b). *See* comment 19(b)–2.

19(d) Timing of disclosures.

19(d)(1) General timing.

1. *Oral application.* Creditors may rely on RESPA and Regulation X (including any interpretations issued by HUD) in deciding whether they have made a written record of a consumer's oral application, even for a transaction not subject to RESPA. In general, Regulation X defines ''application'' to mean the submission of a borrower's financial information in anticipation of a credit decision relating to a federally related mortgage loan and states that an application may either be in writing or electronically submitted, including a written record of an oral application. *See* 24 CFR 3500.2(b).◄

[*19(c)*]►*19(d)(2)*◄ *Electronic disclosures.*

►*Paragraph 19(d)(2)(i).*◄

[1. *Form of disclosures.* Whether disclosures must be in electronic form depends upon the following:]

[i.]►1. *Electronic disclosures required.*◄ If a consumer accesses [an ARM]►a◄ loan application electronically (other than as described under [ii. below]►§ 226.19(d)(ii)◄), such as online at a home computer, the creditor must provide the disclosures in electronic form (such as with the application form on its Web site) in order to meet the requirement to provide disclosures in a timely manner on or with the application. If the creditor instead mailed paper disclosures to the consumer, this requirement would not be met.

►2. *Timing of electronic disclosures provided on or with electronic applications.* Creditors have flexibility in satisfying the requirement under § 226.19(d) (subject to § 226.19(d)(1)(ii)) to provide disclosures required by § 226.19(b) and (c) in electronic form if a consumer accesses an application electronically. Methods creditors could use to satisfy the requirement include, but are not limited to, the following examples:

i. The disclosures could automatically appear on the screen when the application appears;

ii. The disclosures could be located on the same web page as the application (whether or not they appear on the initial screen), if the application contains a clear and conspicuous reference to the location of the disclosures and indicates that the disclosures contain rate, fee, and other cost information, as applicable;

iii. Creditors could provide a link to the electronic disclosures on or with the application as long as consumers cannot bypass the disclosures before submitting the application. The link would take the consumer to the disclosures, but the consumer need not be required to scroll completely through the disclosures; or

iv. The disclosures could be located on the same web page as the application without necessarily appearing on the initial screen, immediately preceding the button that the consumer will click to submit the application.◄

►*Paragraph 19(d)(2)(ii)*◄

[ii. In contrast, if]►1. *Electronic disclosures optional.* If◄ a consumer is physically present in the creditor's office, and accesses an ARM loan application electronically, such as via a terminal or kiosk (or if the consumer uses a terminal or kiosk located on the premises of an affiliate or third party that has arranged with the creditor to provide applications to consumers), the creditor may provide disclosures in either electronic or paper form, provided the creditor complies with the timing, delivery, and retainability requirements of the regulation.

►*Paragraph 19(d)(3)*

1. *Telephone request.* Where a creditor takes a written application by telephone, the creditor must deliver the disclosures or place them in the mail not later than three business days after the creditor receives the consumer's written application. In cases where the consumer only requests an application over the telephone, the creditor must include the early disclosures required under this section with the application that is sent to the consumer.

2. *Mail solicitations.* In cases where the creditor solicits applications through the mail, the creditor must also send the disclosures required under § 226.19(b) and (c) if an application form is included with the solicitation.

3. *Intermediary agent or broker.* i. Where a creditor receives a written application through an intermediary agent or broker the creditor must deliver the disclosures or place them in the mail not later than three business days after the creditor receives the consumer's written application.

However, a creditor must provide disclosures at the time an application form is provided or the consumer pays a non-refundable fee, whichever is earlier, in a transaction that involves a legal agent, as determined under applicable law, or any other third party that is not an ''intermediary agent or broker.'' In determining whether or not a transaction involves an ''intermediary agent or broker'' the creditor should consider the following factors:

A. The number of applications submitted by the broker to the creditor as compared to the total number of applications received by the creditor. The greater the percentage of total loan applications submitted by the broker in any given period of time, the less likely it is that the broker would be considered an ''intermediary agent or broker'' of the creditor during the next period.

B. The number of applications submitted by the broker to the creditor as compared to the total number of applications received by the broker. (This factor is applicable only if the creditor has such information.) The greater the percentage of total loan applications received by the broker that is submitted to a creditor in any given period of time, the less likely it is that the broker would be considered an ''intermediary agent or broker'' of the creditor during the next period.

C. The amount of work (such as document preparation) the creditor expects to be done by the broker on an application based on the creditor's prior dealings with the broker and on the creditor's requirements for accepting applications, taking into consideration the customary practice of brokers in a particular area. The more work that the creditor expects the broker to do on an application, in excess of what is usually expected of a broker in that area, the less likely it is that the broker would be considered an ''intermediary agent or broker'' of the creditor.

ii. An example of an ''intermediary agent or broker'' is a broker who, customarily within a brief period of time after receiving an application, inquires about the credit terms of several creditors with whom the broker does business and submits the application to one of them. The broker is responsible for only a small percentage of the applications received by that creditor. During the time the broker has the application, it might request a credit report and an appraisal (or even prepare an entire loan package if customary in that particular area).◄

§ 226.20—Subsequent Disclosure Requirements.

20(a) Refinancings.

1. *Definition.* A refinancing is a new transaction requiring a complete new set of disclosures. Whether a refinancing has occurred is determined by reference to whether the original obligation has been satisfied or extinguished and replaced by a new obligation, based on the parties' contract and applicable law. The refinancing may involve the consolidation of several existing obligations, disbursement of new money to the consumer or on the consumer's behalf, or the rescheduling of payments under an existing obligation. In any form, the new obligation must completely replace the prior one.

i. Changes in the terms of an existing obligation, such as the deferral of individual installments, will not constitute a refinancing unless accomplished by the cancellation of that obligation and the substitution of a new obligation.

ii. A substitution of agreements that meets the refinancing definition will require new disclosures, even if the substitution does not substantially alter the prior credit terms.

2. *Exceptions.* A transaction is subject to § 226.20(a) only if it meets the general definition of a refinancing. Section 226.20(a) (1) through (5) lists 5 events that are not treated as refinancings, even if they are accomplished by cancellation of the old obligation and substitution of a new one.

3. *Variable-rate.* i. If a variable-rate feature was properly disclosed under the regulation, a rate change in accord with those disclosures is not a refinancing. For example, no new disclosures are required when the variable-rate feature is invoked on a renewable balloon-payment mortgage that was previously disclosed as a variable-rate transaction.

ii. Even if it is not accomplished by the cancellation of the old obligation and substitution of a new one, a new transaction subject to new disclosures results if the creditor either:

A. Increases the rate based on a variable-rate feature that was not previously disclosed; or

B. Adds a variable-rate feature to the obligation. A creditor does not add a variable-rate feature by changing the index of a variable-rate transaction to a comparable index, whether the change replaces the existing index or substitutes an index for one that no longer exists.

iii. If either of the events in paragraph 20(a)3.ii.A. or ii.B. occurs in a transaction secured by a principal dwelling with a term longer than one year, the disclosures required under § 226.19(b) also must be given at that time.

4. *Unearned finance charge.* In a transaction involving precomputed finance charges, the creditor must include in the finance charge on the refinanced obligation any unearned portion of the original finance charge that is not rebated to the consumer or credited against the underlying obligation. For example, in a transaction with an add-on finance charge, a creditor advances new money to a consumer in a fashion that extinguishes the original obligation and replaces it with a new one. The creditor neither refunds the unearned finance charge on the original obligation to the consumer nor credits it to the remaining balance on the old obligation. Under these circumstances, the unearned finance charge must be included in the finance charge on the new obligation and reflected in the annual percentage rate disclosed on refinancing. Accrued but unpaid finance charges are included in the amount financed in the new obligation.

5. *Coverage.* Section 226.20(a) applies only to refinancings undertaken by the original creditor or a holder or servicer of the original obligation. A ''refinancing'' by any other person is a new transaction under the regulation, not a refinancing under this section.

Paragraph 20(a)(1).

1. *Renewal.* This exception applies both to obligations with a single payment of principal and interest and to obligations with periodic payments of interest and a final payment of principal. In determining whether a new obligation replacing an old one is a renewal of the original terms or a refinancing, the creditor may consider it a renewal even if:

i. Accrued unpaid interest is added to the principal balance.

ii. Changes are made in the terms of renewal resulting from the factors listed in § 226.17(c)(3).

iii. The principal at renewal is reduced by a curtailment of the obligation.

Paragraph 20(a)(2).

1. *Annual percentage rate reduction.* A reduction in the annual percentage rate with a corresponding change in the payment schedule is not a refinancing. If the annual percentage rate is subsequently increased (even though it remains below its original level) and the increase is effected in such a way that the old obligation is satisfied and replaced, new disclosures must then be made.

2. *Corresponding change.* A corresponding change in the payment schedule to implement a lower annual percentage rate would be a shortening of the maturity, or a reduction in the

payment amount or the number of payments of an obligation. The exception in § 226.20(a)(2) does not apply if the maturity is lengthened, or if the payment amount or number of payments is increased beyond that remaining on the existing transaction.

Paragraph 20(a)(3).

1. *Court agreements.* This exception includes, for example, agreements such as reaffirmations of debts discharged in bankruptcy, settlement agreements, and post-judgment agreements. (See the commentary to § 226.2(a)(14) for a discussion of court-approved agreements that are not considered ''credit.'')

Paragraph 20(a)(4).

1. *Workout agreements.* A workout agreement is not a refinancing unless the annual percentage rate is increased or additional credit is advanced beyond amounts already accrued plus insurance premiums.

Paragraph 20(a)(5).

1. *Insurance renewal.* The renewal of optional insurance added to an existing credit transaction is not a refinancing, assuming that appropriate Truth in Lending disclosures were provided for the initial purchase of the insurance.

20(b) Assumptions.

1. *General definition.* An assumption as defined in § 226.20(b) is a new transaction and new disclosures must be made to the subsequent consumer. An assumption under the regulation requires the following three elements:

i. [A residential mortgage transaction.]►A closed-end credit transaction secured by real property or a dwelling.◄

ii. An express acceptance of the subsequent consumer by the creditor.

iii. A written agreement.

The assumption of a nonexempt consumer credit obligation requires no disclosures unless all three elements are present. For example, an automobile dealer need not provide Truth in Lending disclosures to a customer who assumes an existing obligation secured by an automobile. However, [a residential mortgage transaction]►closed-end credit transaction secured by real property or a dwelling◄ with the elements described in § 226.20(b) is an assumption that calls for new disclosures; the disclosures must be given whether or not the assumption is accompanied by changes in the terms of the obligation. [(See comment 2(a)(24)–5 for a discussion of assumptions that are not considered residential mortgage transactions.)]

[2. *Existing residential mortgage transaction.* A transaction may be a residential mortgage transaction as to one consumer and not to the other consumer. In that case, the creditor must look to the assuming consumer in determining whether a residential mortgage transaction exists. To illustrate:

i. The original consumer obtained a mortgage to purchase a home for vacation purposes. The loan was not a residential mortgage transaction as to that consumer. The mortgage is assumed by a consumer who will use the home as a principal dwelling. As to that consumer, the loan is a residential mortgage transaction. For purposes of § 226.20(b), the assumed loan is an ''existing residential mortgage transaction'' requiring disclosures, if the other criteria for an assumption are met.]

[3.]►2.◄ *Express agreement.* Expressly agrees means that the creditor's agreement must relate specifically to the new debtor and must unequivocally accept that debtor as a primary obligor. The following events are not construed to be express agreements between the creditor and the subsequent consumer:

i. Approval of creditworthiness.

ii. Notification of a change in records.

iii. Mailing of a coupon book to the subsequent consumer.

iv. Acceptance of payments from the new consumer.

[4.]►3.◄ *Retention of original consumer.* The retention of the original consumer as an obligor in some capacity does not prevent the change from being an assumption, provided the new consumer becomes a primary obligor. But the mere addition of a guarantor to an obligation for which the original consumer remains primarily liable does not give rise to an assumption. However, if neither party is designated as the primary obligor but the creditor accepts payment from the subsequent consumer, an assumption exists for purposes of § 226.20(b).

[5.]►4.◄ *Status of parties.* Section 226.20(b) applies only if the previous debtor was a consumer and the obligation is assumed by another consumer. It does not apply, for example, when an individual takes over the obligation of a corporation.

[6.]►5.◄ *Disclosures.* For transactions that are assumptions within this provision, the creditor must make disclosures based on the ''remaining obligation.'' For example:

i. The amount financed is the remaining principal balance plus any arrearages or other accrued charges from the original transaction.

ii. If the finance charge is computed from time to time by application of a percentage rate to an unpaid balance, in determining the amount of the finance charge and the annual percentage rate to be disclosed, the creditor should disregard any prepaid finance charges paid by the original obligor, but must include in the finance charge any prepaid finance charge imposed in connection with the assumption.

iii. If the creditor requires the assuming consumer to pay any charges as a condition of the assumption, those sums are prepaid finance charges as to that consumer, unless exempt from the finance charge under § 226.4. If a transaction involves add-on or discount finance charges, the creditor may make abbreviated disclosures, as outlined in section 226.20(b)(1) through (5). [Creditors providing disclosures pursuant to this section for assumptions of variable-rate transactions secured by the consumer's principal dwelling with a term longer than one year need not provide new disclosures under sections 226.18(f)(2)(ii) or. In such transactions, a creditor may disclose the variable-rate feature solely in accordance with section 226.18(f)(1).

7. *Abbreviated disclosures.* The abbreviated disclosures permitted for assumptions of transactions involving add-on or discount finance charges must be made clearly and conspicuously in writing in a form that the consumer may keep. However, the creditor need not comply with the segregation requirement of § 226.17(a)(1). The terms *annual percentage rate* and *total of payments,* when disclosed according to § 226.20(b)(4) and (5), are not subject to the description requirements of § 226.18 (e) and (h). The term *annual percentage rate* disclosed under § 226.20(b)(4) need not be more conspicuous than other disclosures.

Paragraph 20(c) Variable-rate adjustments]►20(c) Rate adjustments.◄

1. [*Timing of adjustment notices*]►*General*◄. This section requires a creditor (or a subsequent holder) to provide certain disclosures in cases where an adjustment to the interest rate is made in an [variable-rate] ►adjustable-rate◄ mortgage transaction subject to § 226.19(b). [There are two timing rules, depending on whether payment changes accompany interest rate changes. A creditor is required to provide at least one notice each year during which interest-rate adjustments have occurred without accompanying payment adjustments. For payment adjustments, a creditor must deliver or place in the mail notices to borrowers at least 25, but not more than 120, calendar days before a payment at a new level is due. The timing rules also apply to the notice

required to be given in connection with the adjustment to the rate and payment that follows conversion of a transaction subject to § 226.19(b) to a fixed-rate transaction.]►This section also requires that notice be given where a transaction subject to § 226.19(b) is converted to a fixed-rate transaction.◄ (In cases where an open-end account is converted to a closed-end transaction subject to § 226.19(b), the requirements of this section do not apply until adjustments are made following conversion.)

2. [*Exceptions.*]►*Not applicable.*◄ Section 226.20(c) does not apply to [''shared-equity,'' ''shared-appreciation,'' or] ''price level adjusted'' or similar mortgages►, because such mortgages are not adjustable-rate mortgages subject to the disclosure requirements of § 226.19(b). *See* comment 19(b)–3◄.

3. *Basis of disclosures.* The disclosures required under this section shall reflect the terms of the parties' legal obligation, as required under § 226.17(c)(1).

►*20(c)(1) Timing of disclosures.*

1. *When required.* Payment changes due to changes in property tax obligations or mortgage-related insurance premiums do not trigger the requirement to make disclosures under § 226.20(c)(1)(i).◄

[*Paragraph 20(c)(1)*]►*Paragraph 20(c)(2)(ii)*◄.

1. *Current and* [*prior*]►*new*◄ *interest rates.* The requirements under this paragraph are satisfied by disclosing the interest rate used to compute the new adjusted payment amount [(''current rate'')]►(''new rate'')◄ and the adjusted interest rate that was disclosed in the last adjustment notice[, as well as all other interest rates applied to the transaction in the period since the last notice (''prior rates'')]►(''current rate'')◄. (If there has been no prior adjustment notice, the [prior rates are]►current rate is◄ the interest rate applicable to the transaction at consummation►.)◄[, as well as all other interest rates applied to the transaction in the period since consummation.) If no payment adjustment has been made in a year, the current rate is the new adjusted interest rate for the transaction, and the prior rates are the adjusted interest rate applicable to the loan at the time of the last adjustment notice, and all other rates applied to the transaction in the period between the current and last adjustment notices. In disclosing all other rates applied to the transaction during the period between notices, a creditor may disclose a range of the highest and lowest rates applied during that period.]

[*Paragraph 20(c)(2).*

1. *Current and prior index values.* This section requires disclosure of the index or formula values used to compute the current and prior interest rates disclosed in § 226.20(c)(1). The creditor need not disclose the margin used in computing the rates. If the prior interest rate was not based on an index or formula value, the creditor also need not disclose the value of the index that would otherwise have been used to compute the prior interest rate.]

[*Paragraph 20(c)(3)*]►*Paragraph 20(c)(2)(iv)*◄.

1. *Unapplied index increases.* The requirement that the consumer receive information about the extent to which the creditor has foregone any increase in the interest rate ►and the earliest date a creditor may apply foregone interest to future adjustments, subject to rate caps,◄ is applicable only to those transactions permitting interest rate carryover. The amount of increase that is foregone at an adjustment is the amount that, subject to rate caps, can be applied to future adjustments independently to increase, or offset decreases in, the rate that is determined according to the index or formula.

[*Paragraph 20(c)(4).*

1. *Contractual effects of the adjustment.* The contractual effects of an interest rate adjustment must be disclosed including the payment due after the adjustment is made whether or not the payment has been adjusted. A contractual effect of a rate adjustment would include, for example, disclosure of any change in the term or maturity of the loan if the change resulted from the rate adjustment. In transactions where paying the periodic payments will not fully amortize the outstanding balance at the end of the loan term and where the final payment will equal the periodic payment plus the remaining unpaid balance, the amount of the adjusted payment must be disclosed if such payment has changed as a result of the rate adjustment. A statement of the loan balance also is required. The balance required to be disclosed is the balance on which the new adjusted payment is based. If no payment adjustment is disclosed in the notice, the balance disclosed should be the loan balance on which the payment disclosed under § 226.20(c)(5) is based, if applicable, or the balance at the time the disclosure is prepared.]

Paragraph 20(c)(5)]►*Paragraph 20(c)(2)(vi)*◄.

1. *Fully-amortizing payment.* This paragraph requires a disclosure ►of the fully amortizing payment◄ only when negative amortization occurs as a result of the adjustment. A disclosure is not required simply because a loan calls for non-amortizing or partially amortizing payments. For example, in a transaction with a five-year term and payments based on a longer amortization schedule, and where the final payment will equal the periodic payment plus the remaining unpaid balance, the creditor would not have to disclose the payment necessary to fully amortize the loan in the remainder of the five-year term. A disclosure is required, however, if the ►new◄ payment disclosed under [§ 226.20(c)(4)] ►§ 226.20(c)(2)(ii)(C)◄ is not sufficient to prevent negative amortization in the loan. The adjustment notice must state the payment required to prevent negative amortization. (This paragraph does not apply if the payment disclosed in [§ 226.20(c)(4)] ►§ 226.20(c)(2)(ii)(C)◄ is sufficient to prevent negative amortization in the loan but the final payment will be a different amount due to rounding.)

►2. *Effect on loan term.* The creditor must disclose any change in the term or maturity of the loan if the change resulted from the rate adjustment. The creditor need not make that disclosure if the loan term or maturity has not changed.

20(c)(2)(vii) Loan balance in payment change notice.

1. *Basis of disclosure.* A statement of the loan balance must be disclosed. The balance required to be disclosed is the balance on which the new adjusted payment is based.

Paragraph 20(c)(3)(iii).

1. *Unapplied index increases.* Creditors may rely on comment 20(c)(2)(iv)–1 in determining which transactions the requirement to disclose foregone interest increases applies to and how to disclose such increases. Although creditors must disclose the earliest date the creditor may apply foregone interest to future adjustments under § 226.20(c)(2)(iv), creditors need not disclose this information in the disclosures required by § 226.20(c)(3)(iv), which are made when interest rate changes do not cause payment changes during a year.

Paragraph 20(c)(3)(v).

1. *Basis of disclosure.* A statement of the loan balance must be disclosed. The balance required to be disclosed is the balance on the last day of the period for which the creditor discloses the highest and lowest interest rates.

20(d) Periodic statement.

20(d)(1) Timing and content of disclosures.

1. *Timing and content.* Creditors must provide payment summary tables under § 226.20(d) starting with the first period after consummation, even if the initial

payments required do not negatively amortize the loan. However, payment summary tables need contain only those disclosures that apply to payment options actually available to a consumer. For example, if a consumer has been making the minimum required payments but must begin making fully amortizing payments because the creditor has recast the loan, the payment summary table need not disclose payments other than the fully amortizing payment.

2. *Assumptions.* Creditors may base all disclosures on the assumption that payments will be made on time and in the amounts required by the terms of the legal obligation, disregarding any possible inaccuracies resulting from consumers' payment patterns. *See* comment 17(c)(1)–1 and comment 17(c)(2)(i)–3. Creditors may not assume that consumers make payments greater than the minimum payment required by the legal obligation. That is, creditors may not base disclosures for loans with a payment option that results in negative amortization on the fully amortizing, interest-only, or other payment unless that payment is the amount the consumer is required to pay under the terms of the legal obligation.

20(d)(1)(i) Payment.

1. *Payment type.* Creditors may rely on comment 38(c)(5)–1 to determine whether a payment is a regular periodic payment or a balloon payment.

20(d)(1)(ii) Effects.

1. *Legal obligation.* The disclosures required by § 226.20(d) must reflect the terms of the legal obligation. For example, the disclosures may not state that making fully amortizing payments on an interest-only loan will reduce a consumer's loan balance if the creditor will not apply payments that exceed the interest-only payment to principal.

20(e) Creditor-placed property insurance.

1. *Notice period timing and charges.* The notice period begins on the day that the creditor mails or delivers the notice to the consumer and expires 45 days later. The creditor may begin to charge the consumer for creditor-placed property insurance on the 46th calendar day after sending the notice if the creditor has fulfilled the requirements of section 226.20(e)(1)–(3). For example, a creditor that mails the required notice on January 2, 2011, may begin to charge the consumer for the cost of the creditor-placed property insurance on February 18, 2011. After expiration of the 45-day notice period, a creditor may retroactively charge a consumer for the cost of any required property insurance obtained during the 45-day notice period if such charge is not prohibited by applicable State or other law.◀

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§ 226.24—Advertising.

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24(c) Advertisement of rate of finance charge.

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4. *Discounted variable-rate transactions.* The advertised annual percentage rate for discounted variable-rate transactions must be determined in accordance with comment [17(c)(1)–10] ▶17(c)(1)(iii)–3◀ regarding the basis of transactional disclosures for such financing.

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ii. Limits or caps on periodic rate or payment adjustments need not be stated. To illustrate using the second example in comment [17(c)(1)–10] ▶17(c)(1)(iii)–3◀, the fact that the rate is presumed to be 11 percent in the second year and 12 percent for the remaining 28 years need not be included in the advertisement.

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Subpart D—Miscellaneous

§ 226.25—Record Retention.

25(a) General rule.

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▶5. *Prohibited payments to loan originators.* For each transaction secured by real property or a dwelling subject to the loan originator compensation provisions in § 226.36(d)(1), a creditor should maintain records of the compensation it provided to the loan originator for the transaction as well as the compensation agreement in effect on the date the interest rate was set for the transaction. *See* § 226.35(a) and comment 35(a)(2)–3 for additional guidance on when a transaction's rate is set. Where a loan originator is a mortgage broker, a copy of the HUD–1 settlement statement required by the Real Estate Settlement Procedures Act (RESPA) would be presumed to be a record of the amount actually paid to the loan originator in connection with the transaction.◀

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§ 226.30—Limitation on Rates.

1. *Scope of coverage.* ▶i.◀ The requirement of this section applies to consumer credit obligations secured by a dwelling (as dwelling is defined in § 226.2(a)(19)) in which the annual percentage rate may increase after consummation (or during the term of the plan, in the case of open-end credit) as a result of an increase in the interest rate component of the finance charge—whether those increases are tied to an index or formula or are within a creditor's discretion. The section applies to credit sales as well as loans. Examples of credit obligations subject to this section include:

[•]▶A.◀ Dwelling-secured credit obligations that require variable-rate disclosures under the regulation because the interest rate may increase during the term of the obligation.

[•]▶B.◀ Dwelling-secured open-end credit plans entered into before November 7, 1989 (the effective date of the home equity rules) that are not considered variable-rate obligations for purposes of disclosure under the regulation but where the creditor reserves the contractual right to increase the interest rate—periodic rate and corresponding annual percentage rate—during the term of the plan.

▶ii.◀ In contrast, credit obligations in which there is no contractual right to increase the interest rate during the term of the obligation are not subject to this section. Examples include:

[•]▶A.◀ "Shared-equity" or "shared-appreciation" mortgage loans that have a fixed rate of interest and a shared-appreciation feature based on the consumer's equity in the mortgaged property. (The appreciation share is payable in a lump sum at a specified time.)

[•]▶B.◀ Dwelling-secured fixed-rate closed-end balloon-payment mortgage loans and dwelling-secured fixed-rate open-end plans with a stated term that the creditor may renew at maturity. (Contrast with the renewable balloon-payment mortgage instrument described in comment [17(c)(1)–11.)]▶17(c)(1)(iii)–4.◀

[•]▶C.◀ Dwelling-secured fixed rate closed-end multiple advance transactions in which each advance is disclosed as a separate transaction.

[•]▶D.◀ "Price level adjusted mortgages" or other indexed mortgages that have a fixed rate of interest but provide for periodic adjustments to payments and the loan balance to reflect changes in an index measuring prices or inflation.

▶iii.◀ The requirement of this section does not apply to credit obligations entered into prior to December 9, 1987. Consequently, new advances under open-end credit plans existing prior to December 9, 1987, are not subject to this section.

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Subpart E—Special Rules for Certain Home Mortgage Transactions

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§ 226.32—Requirements for Certain Closed-End Home Mortgages.

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[*32(b) Definitions.*

Paragraph 32(b)(1)(i).

1. *General.* Section 226.32(b)(1)(i) includes in the total ''points and fees'' items defined as finance charges under §§ 226.4(a) and 226.4(b). Items excluded from the finance charge under other provisions of § 226.4 are not included in the total ''points and fees'' under paragraph 32(b)(1)(i), but may be included in ''points and fees'' under paragraphs 32(b)(1)(ii) and 32(b)(1)(iii). Interest, including per-diem interest, is excluded from ''points and fees'' under § 226.32(b)(1).

Paragraph 32(b)(1)(ii).

1. *Mortgage broker fees.* In determining ''points and fees'' for purposes of this section, compensation paid by a consumer to a mortgage broker (directly or through the creditor for delivery to the broker) is included in the calculation whether or not the amount is disclosed as a finance charge. Mortgage broker fees that are not paid by the consumer are not included. Mortgage broker fees already included in the calculation as finance charges under § 226.32(b)(1)(i) need not be counted again under § 226.32(b)(1)(ii).

2. *Example.* Section 226.32(b)(1)(iii) defines ''points and fees'' to include all items listed in § 226.4(c)(7), other than amounts held for the future payment of taxes. An item listed in § 226.4(c)(7) may be excluded from the ''points and fees'' calculation, however, if the charge is reasonable, the creditor receives no direct or indirect compensation from the charge, and the charge is not paid to an affiliate of the creditor. For example, a reasonable fee paid by the consumer to an independent, third-party appraiser may be excluded from the ''points and fees'' calculation (assuming no compensation is paid to the creditor). A fee paid by the consumer for an appraisal performed by the creditor must be included in the calculation, even though the fee may be excluded from the finance charge if it is bona fide and reasonable in amount.

Paragraph 32(b)(1)(iv).

1. *Premium amount.* In determining ''points and fees'' for purposes of this section, premiums paid at or before closing for credit insurance are included whether they are paid in cash or financed, and whether the amount represents the entire premium for the coverage or an initial payment.]

32(c) Disclosures.

[1. *Format.* The disclosures must be clear and conspicuous but need not be in any particular type size or typeface, nor presented in any particular manner. The disclosures need not be a part of the note or mortgage document.]

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32(c)(5) Amount borrowed.

1. *Optional insurance; debt-cancellation ►or debt-suspension◄coverage.* This disclosure is required when the amount borrowed in a refinancing includes premiums or other charges for credit life, accident, health, or loss-of-income insurance►;◄[or] debt-cancellation coverage (whether or not the debt-cancellation coverage is insurance under applicable law) that provides for cancellation of all or part of the consumer's liability in the event of the loss of life, health, or income or in the case of accident►; or debt-suspension coverage that provides for suspension of the obligation to make one or more payments on the date(s) otherwise required by the credit agreement in the event of loss of life, health, or income or in the case of accident◄. See comment 4(d)(3)–2 and comment app. G and H–2 regarding terminology for debt-cancellation ►and debt-suspension◄ coverage.

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§ 226.35—Prohibited Acts or Practices in Connection With Higher-Priced Mortgage Loans.

35(a) Higher-priced mortgage loans.

Paragraph 35(a)(2).

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4. *Board table.* The Board publishes on the ►FFIEC's Web site,◄ [Internet,] in table form, average prime offer rates for a wide variety of transaction types. ►*See http://www.ffiec.gov/hmda.*◄ The Board calculates an annual percentage rate, consistent with Regulation Z (see § 226.22 and appendix J), for each transaction type for which pricing terms are available from a survey. The Board estimates annual percentage rates for other types of transactions for which direct survey data are not available based on the loan pricing terms available in the survey and other information. The Board publishes on the ►FFIEC's Web site◄ [Internet] the methodology it uses to arrive at these estimates.

►5. *Additional guidance on determination of average prime offer rates.* The average prime offer rate has the same meaning in this section as under Regulation C, 12 CFR part 203. *See* 12 CFR 203.4(a)(12)(ii). Guidance on the average prime offer rate under § 226.35(a)(2), such as when a transaction's rate is set and determination of the comparable transaction, is provided in the staff commentary under Regulation C, the Board's *A Guide to HMDA Reporting: Getting it Right!,* and the relevant ''Frequently Asked Questions'' on HMDA compliance posted on the FFIEC's Web site at *http://ffiec.gov/hmda.*◄

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§ 226.36—Prohibited Acts or Practices in Connection with Credit Secured by ►Real Property or a Dwelling◄ [a Consumer's Principal Dwelling].

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36(a) ►Loan originator and◄ mortgage broker defined.

1. *Meaning of ►loan originator◄ [mortgage broker].* Section 226.36(a) provides that a ►loan originator◄ [mortgage broker] is any person who for compensation or other monetary gain arranges, negotiates, or otherwise obtains an extension of consumer credit for another person. ►The term ''loan originator'' includes employees of the creditor◄ [but is not an employee of a creditor]. In addition, this definition expressly includes any ►creditor◄ [person] that satisfies this definition but makes use of ''table funding.'' Table funding occurs when a transaction is consummated with the debt obligation initially payable by its terms to one person, but another person provides the funds for the transaction at consummation and receives an immediate assignment of the note, loan contract, or other evidence of the debt obligation. Although § 226.2(a)(17)(i)(B) provides that a person to whom a debt obligation is initially payable on its face generally is a creditor, § 226.36(a) provides that, solely for the purposes of § 226.36, such a person is ►also considered a loan originator◄ [considered a mortgage broker]. ►The creditor is not considered a loan originator unless table funding occurs.◄ In addition, although consumers themselves often arrange, negotiate, or otherwise obtain extensions of consumer credit on their own behalf, they do not do so for compensation or other monetary gain or for another person and, therefore, are not ►loan originators◄ [mortgage brokers] under this section.

►2. *Mortgage broker.* For purposes of § 226.36, with respect to a particular transaction, the term ''mortgage broker'' refers to a loan originator who is not an employee of the creditor. Accordingly, the term ''mortgage broker'' includes companies that engage in the activities described in § 226.36(a) and also includes employees of such companies that engage in these activities. Section 226.36(d) prohibits certain payments to a loan originator. These prohibitions apply to payments made to all loan originators, including payments made to mortgage brokers, and payments made by a company acting as a mortgage broker to its employees who are loan originators.◀

36(b) Misrepresentation of value of consumer's [principal] dwelling.

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▶*36(d) Prohibited payments to loan originators.*

1. *Persons covered.* Section 226.36(d) prohibits any person (including the creditor) from paying compensation to a loan originator in connection with a covered credit transaction, if the amount of the payment is based on any of the transaction's terms or conditions. For example, a person that purchases a loan from the creditor may not compensate the loan originator in a manner that violates this section.

2. *Mortgage brokers.* The payments made by a company acting as a mortgage broker to its employees who are loan originators are subject to the section's prohibitions. For example, a mortgage broker may not pay its employee more for a transaction with a 7 percent interest rate than for a transaction with a 6 percent interest rate.

36(d)(1) Payments based on transaction terms and conditions.

1. *Compensation.* For purposes of § 226.36(d)(1) and (e) the term ''compensation'' is not limited to commissions; it includes salaries and any financial or similar incentive provided to a loan originator that is based on any of the terms and conditions of the loan originator's transactions. (*See* comment 36(d)(1)–2 for examples of types of compensation that are not covered by § 226.36(d) and (e)). For example, the term ''compensation'' includes:

i. An annual or other periodic bonus; or

ii. Awards of merchandise, services, trips, or similar prizes.

2. *Examples of compensation that is based on transaction terms or conditions.* Section 226.36(d)(1) prohibits loan originator compensation that is based on a transaction's terms or conditions. For example, the rule prohibits compensation based on the transaction's interest rate, annual percentage rate, loan-to-value ratio, or the existence of a prepayment penalty. A consumer's credit score or similar representation of credit risk is not one of the transaction's terms and conditions, but a creditor does not necessarily avoid having based a loan originator's compensation on the interest rate or the annual percentage rate solely because the originator's compensation happens to vary with the consumer's credit score as well.

3. *Examples of compensation not based on transaction terms or conditions.* Compensation would not be based on the transaction's terms or conditions if it were based on, for example:

i. The loan originator's overall loan volume delivered to the creditor.

ii. The long-term performance of the originator's loans.

iii. A fixed hourly rate of pay to compensate the originator for the actual number of hours worked.

iv. Whether the consumer is an existing customer of the creditor or a new customer.

4. *Geographic differences.* Section 226.36(d)(1) does not prohibit the payment of compensation to a loan originator that differs by geographical area, provided such compensation is not based on the transaction's terms or conditions. Any such arrangement must comply with other applicable laws, such as the Equal Credit Opportunity Act, 15 U.S.C. 1691–1691f, and Fair Housing Act, 42 U.S.C. 3601–3619.

5. *Creditor's flexibility in setting loan terms.* Section 226.36(d)(1) does not limit the creditor's ability to offer a higher interest rate in a transaction as a means for the consumer to finance the payment of the loan originator's compensation or other costs that the consumer would otherwise be required to pay directly (either in cash or out of the loan proceeds). Thus, a creditor may charge a higher interest rate to a consumer who will pay fewer of the costs of the transaction directly, or the creditor may offer the consumer a lower rate if the consumer pays more of the costs directly. For example, if the consumer pays half of the transaction costs directly, the creditor may charge an interest rate of 6% but, if the consumer pays none of the transaction costs directly, may charge an interest rate of 6.5%. Section 226.36(d)(1) also does not limit a creditor from offering or providing different loan terms to the consumer based on the creditor's assessment of the credit risk involved. A creditor also may set loan terms by offering varying interest rates to different consumers that include a constant interest rate premium to recoup the loan originator's compensation through increased interest paid by the consumer (such as by adding a constant ¼ of one percent to the interest rate on each loan).

6. *Effect of modification of loan terms.* Under § 226.36(d)(1), a loan originator's compensation may not vary based on any of a credit transaction's terms and conditions. Thus, a creditor and originator could not agree to set the originator's compensation at a higher level and then subsequently lower it in selective cases (such as where the consumer is able to obtain a lower rate from another creditor). When the creditor offers to extend a loan with specified terms and conditions (such as the rate and points) the amount of the originator's compensation for that transaction is not subject to change (increase or decrease) based on whether different loan terms are negotiated. For example, if the creditor agrees to lower the rate that was initially offered, the new offer may not be accompanied by a reduction in the loan originator's compensation.

7. *Periodic changes in loan originator compensation and transactions' terms and conditions.* This section does not limit a creditor from periodically revising the compensation it agrees to pay a loan originator. However, the revised compensation arrangement must result in payments to the loan originator that do not vary based on the terms or conditions of a credit transaction. A creditor might periodically review factors such as loan performance, transaction volume, as well as current market conditions for originator compensation, and prospectively revise the compensation it agrees to pay to a loan originator. For example, assume that during the first 6 months of the year, a creditor pays $3,000 to a particular loan originator for each loan delivered, regardless of the loan terms. After considering the volume of business produced by that originator, the creditor could decide that as of July 1, it will pay $3,250 for each loan delivered by that particular originator, regardless of the loan terms. No violation occurs even if the loans made by the creditor after July 1 generally carry a higher interest rate than loans made before that date, to reflect the higher compensation.

8. *Compensation received directly from a consumer.* The prohibition in § 226.36(d)(1) does not apply to transactions in which the loan originator receives compensation directly from the consumer, in which case no other person may provide any compensation to the loan originator, directly or indirectly, in connection with that particular transaction pursuant to § 226.36(d)(2).

9. *Record retention.* See comment 25(a)–5 for guidance on complying with the record retention requirements of § 226.25(a) as they apply to this section.◀

ALTERNATIVE COMMENT 36(d)(1)–10, TO ACCOMPANY ALTERNATIVE 2—PARAGRAPH (d):

►10. *Principal loan amount.* A loan originator's compensation may be based on the loan amount. Thus, an arrangement that pays a loan originator a fixed percentage of the loan amount does not violate this section even though the dollar amount received by the originator will vary from transaction to transaction and will be greater as the loan amount increases. Section 226.36(d)(1) does not prohibit an arrangement under which a loan originator is paid a fixed percentage of the loan amount, subject to specified minimum or maximum dollar amount. For example, a loan originator's compensation may be set at one percent of the principal loan amount but not less than $1,000 or greater than $5,000.◄

►*36(d)(2) Payments by persons other than consumer.*

1. *Compensation in connection with a particular transaction.* Under § 226.36(d)(2), if a loan originator receives compensation directly from a consumer in a transaction, no other person may provide any compensation to the loan originator, directly or indirectly, in connection with that particular credit transaction. The restrictions imposed under § 226.36(d)(2) relate only to payments, such as commissions, that are specific to, and paid solely in connection with, the transaction in which the consumer has paid compensation directly to the loan originator. Thus, compensation paid by a mortgage broker company to an employee in the form of a salary or hourly wage, which is not tied specifically to a single transaction, does not violate § 226.36(d)(2) even if the consumer directly pays a broker a fee in connection with a specific transaction.

2. *Compensation received directly from a consumer.* Under Regulation X, which implements the Real Estate Settlement Procedures Act (RESPA), a yield spread premium paid by a creditor to the loan originator may be characterized on the RESPA disclosures as a ''credit'' that will be applied to reduce the consumer's settlement charges, including origination fees. A yield spread premium disclosed in this manner is not considered to be received by the loan originator directly from the consumer for purposes of § 226.36(d)(2).◄

►*36(d)(3) Affiliates.*

1. For purposes of § 226.36(d), affiliated entities are treated as a single ''person.'' For example, assume a parent company has two mortgage lending subsidiaries. Under § 226.36(d)(1), subsidiary ''A'' could not pay a loan originator greater compensation for a loan with an interest rate of 8 percent than it would pay for a loan with an interest rate of 7 percent. If the loan originator may deliver loans to both subsidiaries, they must compensate the loan originator in the same manner. Accordingly, if the loan originator delivers the loan to subsidiary ''B'' and the interest rate is 8 percent, the originator must receive the same compensation that would have been paid by subsidiary A for a loan with a rate of either 7 or 8 percent.◄

COMMENTS 36(e)–1, 36(e)(1)–1 THROUGH 36(e)(1)–3, 36(e)(2)–1 AND 36(e)(2)–2, and 36(e)(3)–1 THROUGH 36(e)(3)–4, TO ACCOMPANY OPTIONAL PROPOSAL—PARAGRAPH (e).

►*36(e) Prohibition on steering.*

1. *Compensation.* See comment 36(d)(1)–1 for guidance on compensation that is subject to § 226.36(e).

Paragraph 36(e)(1).

1. *Steering.* For purposes of § 226.36(e), directing or ''steering'' a consumer to a particular credit transaction means advising, counseling, or otherwise influencing a consumer to accept that transaction. For such actions to constitute steering, the consumer must actually consummate the transaction in question. Thus § 226.36(e)(1) does not address the actions of a loan originator if the consumer does not actually obtain a loan through that originator.

2. *Prohibited conduct.* Under § 226.36(e)(1), a loan originator may not direct or steer a consumer to a loan to increase the amount of compensation that the originator will receive for the transaction unless the loan is in the consumer's interest.

i. In determining whether a consummated transaction is in the consumer's interest, that transaction must be compared to other possible loan offers available through the originator, and for which the consumer was likely to qualify, at the time the consummated transaction was offered to the consumer. Possible loan offers are available through the loan originator if they could be obtained from a creditor with which the loan originator regularly does business. Section 226.36(e)(1) does not require a loan originator to establish a business relationship with any creditor with which the loan originator does not already do business. To be considered a ''possible loan offer,'' an offer need not be extended by the creditor; it need only be an offer that the creditor likely would extend upon receiving an application from a qualified applicant, based on the creditor's current rate sheets or other, similar means of communicating its current credit terms to the loan originator. An originator need not inform the consumer about a possible loan offer if the originator is able to make a good faith determination that the consumer is not likely to qualify for the loan.

ii. Section 226.36(e)(1) does not require a loan originator to direct a consumer to the transaction that will result in a creditor paying the least amount of compensation to the originator. However, if the loan originator reviews possible loan offers available from a significant number of the creditors with which the originator regularly does business, and the originator directs the consumer to the transaction that will result in the least amount of creditor-paid compensation for the loan originator, the requirements of § 226.36(e)(1) are deemed to be satisfied. A loan originator who is an employee of the creditor may not obtain compensation that is based on the transaction's terms or conditions pursuant to § 226.36(d)(1), and compliance with that provision by such a loan originator also satisfies the requirements of § 226.36(e)(1).

iii. See the commentary under § 226.36(e)(3) for additional guidance on what constitutes a ''significant number of creditors with which a loan originator regularly does business'' and guidance on the determination about transactions for which ''the consumer likely qualifies.''

3. *Examples.* Assume the originator determines that a consumer likely qualifies for a loan from Creditor A that has a fixed interest rate of 7.00 percent, but the loan originator directs the consumer to a loan from Creditor B having a rate of 7.50 percent. If the loan originator receives more in compensation from Creditor B than the amount that would have been paid by Creditor A, the prohibition in § 226.36(e) is violated unless the higher-rate loan is in the consumer's interest. For example, a higher rate loan might be in the consumer's interest if the lower rate loan has a prepayment penalty, or if the lower rate loan requires the consumer to pay more in up-front charges that the consumer is unable or unwilling to pay or finance as part of the loan amount.

36(e)(2) Permissible transactions.

1. *Safe harbors.* A loan originator that complies with § 226.36(e)(2) is deemed to comply with § 226.36(e)(1). A loan originator that does not comply with § 226.36(e)(2) is not subject to any presumption regarding the originator's compliance or noncompliance with § 226.36(e)(1).

2. *Minimum number of loan options.* To obtain the safe harbor, § 226.36(e)(2)

requires that the loan originator present at least three loan options for each type of transaction in which the consumer expressed an interest. As required by § 226.36(e)(3)(ii), the loan originator must have a good faith belief that the options presented are loans for which the consumer likely qualifies. If the loan originator is not able to form such a good faith belief for at least three options for a given type of transaction, the loan originator may satisfy the minimum number of loan options set forth in § 226.36(e)(2) by presenting all loan options for which the consumer likely qualifies and that meet the other requirements of § 226.36(e)(3).

36(e)(3) Loan options presented.

1. *Significant number of creditors.* A significant number of the creditors with which a loan originator regularly does business is three or more of those creditors. If the loan originator regularly does business with fewer than three creditors, the originator is deemed to comply by obtaining loan options from all the creditors with which it regularly does business. Under § 226.36(e)(3)(i), the loan originator must obtain loan options from a significant number of creditors with which the loan originator regularly does business, but the loan originator need not present loan options from all such creditors to the consumer to satisfy § 226.36(e)(2). For example, if three loan options available from one of the creditors with which the loan originator regularly does business satisfy § 226.36(e)(3)(i), presenting those and no options from any other creditor satisfies § 226.36(e)(2).

2. *Creditors with which loan originator regularly does business.* To qualify for the safe harbor in § 226.36(e)(2), the loan originator must obtain and review loan options from a significant number of the creditors with which the loan originator regularly does business. For this purpose, a loan originator regularly does business with a creditor if:

i. There is a written agreement between the originator and the creditor governing the originator's submission of mortgage loan applications to the creditor;

ii. The creditor has extended credit secured by real property or a dwelling to one or more consumers during the current or previous calendar month based on an application submitted by the loan originator; or

iii. The creditor has extended credit secured by real property or a dwelling 25 or more times during the previous twelve calendar months based on applications submitted by the loan originator. For this purpose the previous twelve calendar months begins with the calendar month that precedes the month in which the loan originator accepted the consumer's application.

3. *Lowest interest rate.* To qualify under the safe harbor in § 226.36(e)(2), for each type of transaction in which the consumer has expressed an interest, the loan originator must present the consumer with at least three loans that include the loan with the lowest interest rate, the loan with the second lowest rate, and the loan with the lowest total dollar amount for discount points and origination points. To determine the loan with the lowest interest rate, for any loan that has an initial rate that is fixed for at least five years, the loan originator shall use the initial rate that would be in effect at consummation. For a loan with an initial rate that is not fixed for at least five years:

i. If the interest rate varies based on changes to an index, the originator shall use the fully-indexed rate that would be in effect at consummation without regard to any initial discount.

ii. For a step-rate loan the originator shall use the highest rate that would apply during the first five years.

4. *Transactions for which the consumer likely qualifies.* To qualify under the safe harbor in § 226.36(e)(2), the loan originator must have a good faith belief that the loan options presented to the consumer pursuant to § 226.36(e)(3) are transactions for which the consumer likely qualifies. The loan originator's belief that the consumer likely qualifies should be based on all information reasonably available to the loan originator at the time the loan options are being presented. The loan originator may rely on information provided by the consumer, even if it subsequently is determined to be inaccurate. For purposes of § 226.36(e)(3), a loan originator is not expected to know all aspects of each creditor's underwriting criteria. But pricing or other information that is routinely communicated by creditors to loan originators is considered to be reasonably available to the loan originator, for example, rate sheets showing creditors' current pricing and the required minimum credit score or other eligibility criteria.◄

►*Section 226.37—Special Disclosure Requirements for Closed-End Mortgages*

37(a) Form of disclosures.

1. *Controlling standard.* Transactions subject to this part are also subject to the clear and conspicuous standard under § 226.17(a)(1). In some instances, § 226.17(a)(1) provides creditors more flexibility in meeting the clear and conspicuous standard. For example, disclosures for transactions subject only to § 226.17(a)(1) may be grouped together and segregated in a variety of ways and need not be given in a particular type size. In contrast, disclosures required for transactions secured by real property or a dwelling, and therefore, also subject to § 226.37, must be segregated from all other material and be provided in a minimum 10-point font. For such disclosures, creditors must use the standards set forth under § 226.37(a) through (d).

37(a)(1) General.

1. *Clear and conspicuous standard.* The clear and conspicuous standard generally requires that disclosures be in a reasonably understandable form and readily noticeable to the consumer.

2. *Clear and conspicuous standard—readily noticeable.* To meet the readily noticeable standard, disclosures required by §§ 226.19, 226.20(c), 226.20(d), and 226.38 must be given in a minimum 10-point font.

3. *Location.* The disclosures required under §§ 226.19 or 226.38 must appear on a document separate from all other material. The disclosures required under §§ 226.19, 226.20(c), 226.20(d) or 226.38 may be made on more than one page, continued from one page to another, and made on the front or back side of a page, except as otherwise specifically required.

37(a)(2) Grouped and Segregated.

1. *Segregation of disclosures.* The disclosures required by §§ 226.19, 226.20(c), 226.20(d) or 226.38 must be segregated from other information. The disclosures under § 226.38 may be grouped together, in accordance with the requirements under § 226.38(a)–(j), and segregated from other required disclosures under § 226.38

i. By outlining them in a box.

ii. By bold print dividing lines.

iii. By a different color background.

iv. By a different type style.

2. *Content of segregated disclosures.* Section 226.37(a)(2)(i)–(ii) contains exceptions to the requirement that the disclosures required under § 226.38 be grouped together and segregated from material that is not directly related to those disclosures. Section 226.37(a)(2)(i) lists the items that may be added to the segregated disclosures, even though not directly related to those disclosures. Section 226.37(a)(2)(ii) lists the items required under § 226.38 that may be deleted from the segregated disclosures and appear elsewhere. Any of these additions or deletions may be combined and appear either together with or separate from the segregated disclosures.

3. *Directly related.* The segregated disclosures may, at the creditor's option, include any information that is directly related to those disclosures. The

following is directly related information:

i. The basis for any estimates used in making disclosures. For example, if the maturity date of a loan depends solely on the occurrence of a future event, the creditor may indicate that the disclosures assume that event will occur at a certain time.

ii. An explanation of the use of pronouns or other references to the parties to the transaction. For example, the disclosures may state, "'You' refers to the customer and 'we' refers to the creditor."

iii. A brief caption identifying the disclosures. For example, the disclosures may bear a general title such as "Federal Truth in Lending Disclosures" or a descriptive title such as "Real Estate Loan Disclosures."

4. *Balloon payment financing with leasing characteristics.* See comment 17(a)(1)–7.

37(c) Terminology.

1. *Consistent Terminology.* Language used in disclosures required by §§ 226.19, 226.20(c), 226.20(d), and 226.38 must be close enough in meaning to enable the consumer to relate the different disclosures; however, the language need not be identical, unless the use of specific terminology is required.

2. *Combining terminology.* Where the amounts of several numerical disclosures are the same, creditors may combine the terms, so long as it is done in a clear and conspicuous manner and in accordance with the requirements under § 226.38. For example, in a transaction in which the amount financed equals the total payments, the creditor may disclose a single dollar amount together with the descriptive statement required for total payments under § 226.38(e)(5)(i) and an explanation that the figure represents both the total payments and the amount financed, and is used to calculate the annual percentage rate. However, if the terms are required to be disclosed separately, both disclosures must be completed even though the same amount is entered into each space.

3. *When disclosures must be more conspicuous.* The following rules apply to the requirement that the annual percentage rate for the loan transaction, when disclosed with the term *annual percentage rate,* be shown more conspicuously:

i. the annual percentage rate, expressed as a percentage, must be more conspicuous only in relation to other required disclosures under § 226.38.

ii. the annual percentage rate, expressed as a percentage, need not be more conspicuous except as part of the annual percentage rate disclosure required under §§ 226.37(c)(2) and 226.38(b)(1).

iii. the term "annual percentage rate" must not be more conspicuous than the annual percentage rate, expressed as a percentage and disclosed as required under §§ 226.37(c)(2) and 226.38(b)(1).

iv. the creditor's identity under § 226.38(g)(1) may, but need not, be more prominently displayed than the annual percentage rate.

4. *Making disclosures more conspicuous.* The annual percentage rate for the loan transaction, expressed as a percentage, may be made more conspicuous in any way that highlights it in relation to the other required disclosures. For example, it may be:

i. Printed in bold print or different type face; or

ii. Underlined.

37(d) Specific Formats.

1. *Prominent Location.* Disclosures meet the prominent location standard if located on the first page and on the front side of the disclosure statement.

2. *Close Proximity.* If the required disclosures are located immediately next to or directly above or below each other, without any intervening text or graphical displays, the disclosures are deemed to be in close proximity.

Section 226.38—Content of Disclosures for Closed-End Mortgages

1. *As applicable.* The disclosures required by this section should be provided only as applicable. Any provision not relevant to a particular transaction should not be disclosed, except as otherwise required under § 226.38(d)(1).

2. *Format.* See the commentary to §§ 226.17(a)(1) and 226.37 for a discussion of the format to be used in making these disclosures, as well as acceptable modifications.

38(a) Loan summary.

38(a)(3) Loan type and features.

1. *General.* The disclosure of loan type and features should reflect the terms of the legal obligation between the parties.

38(a)(3)(i) Loan type.

1. *General.* Creditors must identify the loan type as required in § 226.38(a)(3)(i). Only one loan type may be disclosed. The categories used in § 226.38(a)(3)(i) are different from the categories in § 226.18(f) and commentary to § 226.17(c)(1).

38(a)(3)(i)(A) Adjustable-rate mortgages.

1. *General.* A transaction is an adjustable-rate mortgage for the purposes of this section if the annual percentage rate may increase after consummation. However, a transaction in which the annual percentage rate may change after consummation solely because of a shared-equity or shared-appreciation feature is not an adjustable-rate mortgage for the purposes of this section. *See* § 226.38(d)(2)(vi). Also, a step-rate mortgage is not an adjustable-rate mortgage for purposes of this section unless the interest rate or the applicable period for each interest rate can change other than as specified in the terms of the legal obligation between the parties. *See* § 226.38(a)(3)(i)(B). A fixed interest rate loan with a renewable balloon payment is not an adjustable-rate mortgage for purposes of this section. See comment 38(a)(3)(i)(C)–1(v).

2. *Examples.* The following transactions, for which the interest rate is variable, are examples of adjustable-rate mortgages for purposes of this section.

i. the seller or a 3rd party pays an amount either to the creditor or to the consumer to buy down the interest rate for all or a portion of the credit term as described in comment 17(c)(1)(i)–1, regardless of whether the disclosures take the buydown into account.

ii. the consumer pays an amount to the creditor to buy down the interest rate for all or a portion of the credit term as described in comment 17(c)(1)(i)–2.

iii. a third party (such as a seller) and a consumer both pay an amount to the creditor to buy down the interest rate for all or a portion of the credit term as described in comment 17(c)(1)(i)–4.

iv. a rate reduction option permits the consumer to adjust the existing variable interest rate to a lower variable interest rate under certain conditions, in accordance with the terms of the legal obligation between the parties.

v. the renewable balloon-payment option permits the consumer to renew the loan as described in comment 17(c)(1)(iii)–4(i).

vi. the terms of the legal obligation provide that the rate will increase upon the occurrence of some event, such as an employee leaving the employ of the creditor, as described in comment 17(c)(1)(iii)–4(ii).

vii. the terms of the legal obligation provide for periodic adjustments to payments and the loan balance, such as "price-level-adjusted mortgages" or other indexed mortgages that have a variable rate of interest and provide for periodic adjustments to payments and the loan balance to reflect changes in an index measuring prices or inflation, as described in comment 17(c)(1)(iii)–4(iii).

viii. if the interest rate or the applicable period for each interest rate can change other than as specified in the terms of the legal obligation between the parties, such as certain step-rate mortgages, as described in comment 38(a)(3)(i)(B)–1.

ix. the terms of the legal obligation provide for scheduled adjustments in payment amounts during the loan term, such as certain graduated-payment adjustable-rate mortgages, as described in comment 17(c)(1)(iii)–6.

x. the terms of the legal obligation give the consumer an option to convert the variable interest rate into a fixed interest rate at a designated time or upon satisfaction of certain conditions.

38(a)(3)(i)(B) Step-rate mortgages.

1. *General.* A step-rate mortgage is a transaction for which the annual percentage rate will change after consummation, and all of the interest rates that will apply throughout the term of the loan, including the applicable period for each interest rate, are specified in the terms of the legal obligation between the parties. As discussed in comment 38(a)(3)(i)(A)–1, if the interest rate or the applicable period for each interest rate can change other than as specified in the terms of the legal obligation between the parties, such mortgage is considered an adjustable-rate mortgage and not a step-rate mortgage for purposes of this section.

2. *Exclusion.* Preferred-rate loans where the terms of the legal obligation provide that the initial interest rate is fixed but will increase upon the occurrence of some event, such as an employee leaving the employ of the creditor, as described in comment 17(c)(1)(iii)–4, are considered *fixed-rate* mortgages and not *step-rate mortgages* for purposes of this section. See comment 38(a)(3)(i)(C)–1(vi).

38(a)(3)(i)(C) Fixed-rate mortgages.

1. *Examples.* The following transactions, for which the interest rate is fixed, are examples of fixed-rate mortgages for purposes of this section.

i. the seller or a third party pays an amount either to the creditor or to the consumer to buy down the interest rate for all or a portion of the credit term as described in comment 17(c)(1)(i)–1, regardless of whether the disclosures take the buydown into account.

ii. the consumer pays an amount to the creditor to buy down the interest rate for all or a portion of the credit term as described in comment 17(c)(1)(i)–2.

iii. a third party (such as a seller) and a consumer both pay an amount to the creditor to buy down the interest rate for all or a portion of the credit term as described in comment 17(c)(1)(i)–4.

iv. a rate reduction option permits the consumer to adjust the existing fixed interest rate to a lower fixed interest rate under certain conditions, in accordance with the terms of the legal obligation between the parties.

v. the renewable balloon-payment option permits the consumer to renew the loan as described in comment 17(c)(1)(iii)–4(i).

vi. the terms of the legal obligation provide that the rate will increase upon the occurrence of some event, such as an employee leaving the employ of the creditor, as described in comment 17(c)(1)(iii)–4(ii).

vii. the terms of the legal obligation provide for periodic adjustments to payments and the loan balance, such as ‘‘price-level-adjusted mortgages’’ or other indexed mortgages that have a fixed rate of interest but provide for periodic adjustments to payments and the loan balance to reflect changes in an index measuring prices or inflation, as described in comment 17(c)(1)(iii)–4(iii).

38(a)(3)(ii) Loan features.

1. *General.* Creditors must indicate whether a loan has the features specified in § 226.38(a)(3)(ii). Under § 226.38(a)(3)(ii), a creditor should disclose no more than two features for a single loan. A loan may have both a ‘‘step-payment’’ feature in § 226.38(a)(3)(ii)(A) and one of the features in § 226.38(a)(3)(ii)(B)–(D).

38(a)(3)(ii)(A) Step-payments.

1. *General.* If, under the terms of the legal obligation, a periodic monthly payment may increase by a set amount for a specified amount of time, the creditor must disclose that the loan has a ‘‘step-payment’’ feature. For instance, if the consumer is offered a fixed-rate mortgage with 24 monthly payments at $1,000 that will later increase to $1,200 and remain at that level for a specified period of time, and the loan amortizes fully over the loan term, the creditor would disclose ‘‘Fixed-rate mortgage, step-payments’’ for the loan type in the loan summary. See comment 17(c)(1)(iii)–5 clarifying that graduated-payment mortgages and step-rate transactions without an adjustable-rate mortgage feature are not considered adjustable-rate mortgage transactions. However, if the consumer is offered an adjustable-rate mortgage loan with scheduled variations in payment amounts during the loan term, the creditor would disclose ‘‘Adjustable-rate mortgage, step-payments.’’ See comment 17(c)(1)(iii)–6 for a discussion of graduated-payment adjustable-rate mortgages. Also see comment 38(a)(3)(ii)–2 regarding loans with multiple features.

Paragraphs 38(a)(3)(ii)(B) and (C)

1. *‘‘Payment option’’ and ‘‘negative amortization’’ features—loans with negative amortization.*

i. Negative amortization occurs when one or more regular periodic payments is not sufficient to cover interest accrued and the unpaid interest is added to the loan balance. For purposes of the loan feature disclosure in § 226.38(a)(3)(ii), features that result in negative amortization are divided into two types:

A. ‘‘Payment option’’ features, in which the terms of the legal obligation *permit* the consumer to make payments that result in negative amortization and other types of payments; and

B. ‘‘Negative amortization’’ features, in which the terms of the legal obligation require the consumer to make payments that result in negative amortization—that is, the legal obligation does not permit the consumer to make payments that would cover all interest accrued or all interest accrued and principal.

ii. Under § 226.38(a)(3)(ii)(B) and (C), a creditor should disclose the loan feature as either ‘‘payment option’’ or ‘‘negative amortization’’ but not both. Under § 226.38(a)(3)(ii)(A), however, a loan may have both a ‘‘step-payment’’ feature and either a ‘‘payment option’’ or a ‘‘negative amortization’’ feature.

2. *Consumer's choice.* For a loan to have a ‘‘payment option’’ feature, all periodic payment choices must be specified in the legal obligation and must include a choice to make payments that may result in negative amortization. For example, if the consumer is offered a loan with minimum monthly payments that will not reduce the loan balance to remain the same (i.e., interest-only payments), but the terms of the legal obligation do not prevent the consumer from making payments that will decrease the loan balance, such a loan would be disclosed as having an ‘‘interest-only’’ feature and not a ‘‘payment option’’ feature for purposes of this section.

Paragraph 38(a)(3)(ii)(D)

1. *Interest-only feature.* The creditor must disclose an ‘‘interest-only’’ feature if the terms of the legal obligation permit or require the consumer to make one or more regular periodic payments of interest accrued and no principal, and the legal obligation does not require or permit any payments that would result in negative amortization. Thus, a creditor should not disclose both an ‘‘interest-only’’ feature and a ‘‘payment option’’ feature or ‘‘negative amortization’’ feature in a single

transaction. Under § 226.38(a)(3)(ii)(A), however, a loan may have both an ''interest-only'' feature and a ''step-payment'' feature.

38(a)(4) Total settlement charges.

1. *Disclosure required.* For the good faith estimate required by § 226.19(a)(1)(i), the creditor must disclose the amount of the ''Total Estimated Settlement Charges'' as disclosed on the Good Faith Estimate under Regulation X, 12 CFR part 3500, Appendix C. For the final disclosure required by § 226.19(a)(2)(ii), the creditor must disclose the sum of the final settlement charges. For the final disclosure, the creditor may use the sum of the ''Charges That Cannot Increase,'' ''Charges That In Total Cannot Increase By More Than 10%,'' and ''Charges That Can Change'' as would be disclosed in the column entitled ''HUD–1'' on page three of the HUD–1 or on page two of the HUD–1A settlement statement under Regulation X, 12 CFR part 3500, Appendix A. Alternatively, for the final disclosure, the creditor may provide the consumer with the final HUD–1 or HUD–1A settlement statement. For transactions in which a Good Faith Estimate, HUD–1 or HUD–1A are not required, the creditor may look to such documents for guidance on how to comply with the requirements of this section.

38(a)(5) Prepayment penalty.

1. *Coverage.* Section 226.38 (a)(5) applies only to those transactions in which the interest calculation takes account of all scheduled reductions in principal, as well as transactions in which interest calculations are made daily.

2. *Penalty.* The term ''penalty'' as used in § 226.38(a)(5) encompasses only those charges that are assessed solely because of the prepayment in full of a transaction in which the interest calculation takes account of all scheduled reductions in principal. Charges which are penalties include, for example:

i. Charges determined by treating the loan balance as outstanding for a period after prepayment in full and applying the interest rate to such ''balance.''

ii. A minimum finance charge in a simple-interest transaction.

iii. Fees, such as loan closing costs, that are waived unless the consumer prepays the obligation.

3. *Fees that are not prepayment penalties.* Charges which are not penalties include, for example:

i. Loan guarantee fees.

ii. Fees imposed for preparing and providing documents in connection with prepayment, such as a loan payoff statement, a reconveyance, or other document releasing the creditor's security interest in the property securing the loan.

4. *As applicable.* When the legal obligation includes a finance charge computed from time to time by application of a rate to the unpaid principal balance and no penalty may be imposed, disclosures made under § 226.38(a)(5) need not be made. In such a case, however, § 226.38(d)(1)(iii) requires the creditor to indicate whether or not the legal obligation permits the creditor to impose a prepayment penalty.

5. *Content of disclosure.* Section 226.38(a)(5) requires creditors to disclose the amount of the maximum penalty, the circumstances under which the creditor may impose the penalty, and the period during which the creditor may impose the penalty. The creditor must state the maximum penalty as a dollar numerical amount. *See* § 226.2(b)(5) and comment 2(b)(5)–2.

6. *Basis of disclosure.* The creditor should assume that the consumer prepays at a time when the prepayment penalty may be charged. For example, if the prepayment penalty on a negatively amortizing loan equals 2% of the amount prepaid during the first two years after loan origination, the creditor should disclose the maximum penalty using the maximum loan balance during those years even if the loan balance, and thus the amount prepaid, may increase thereafter. If more than one type of prepayment penalty applies, the creditor should include the maximum amount of each type of prepayment penalty in the maximum penalty disclosed.

i. If the legal obligation permits the creditor to treat the loan balance as outstanding for a period after prepayment in full and charge amounts determined by applying the interest rate to the ''balance'' deemed outstanding during that period, the maximum the creditor should include is the maximum such charges in calculating the maximum prepayment penalty.

ii. If a minimum finance charge applies, the creditor should include the minimum finance charge in calculating the maximum prepayment penalty.

iii. If a prepayment penalty is determined by applying to the loan balance at the time of prepayment a rate that does not change, the prepayment penalty amount should be calculated assuming the highest balance possible. For amortizing loans and interest-only loans, the balance is highest at consummation, assuming the consumer makes timely payments in full. However, for loans with negative amortization, the loan's balance may be higher after consummation. For example, assume the principal balance of a negatively amortizing loan is $200,000 at consummation. The terms of the legal obligation allow the creditor to impose a fee equal to 3% of the amount prepaid if the consumer prepays during the first three years after consummation. The legal obligation provides that the interest rate for the loan is 1.50% for the first month, the maximum interest rate is 10.50%, and there are no limitations on how much the interest rate can increase on any adjustment date. Initial minimum payment amounts are based on the 1.5% initial rate. Payment amounts are adjusted yearly, but payments may not increase by more than 7.5% on any adjustment date, except that the consumer must make fully amortizing payments starting with the period in which the principal balance reaches 115% of the original principal balance. Assuming that the interest rate increases to 10.50% in the second month and remains at that rate and that the consumer makes minimum payments, the highest principal balance is $229,243, reached in the twenty-eighth month following origination. For purposes of this disclosure, the creditor should assume the consumer prepays in the 28th month, and the maximum prepayment penalty is $6,877.29.

iv. In some cases, the legal obligation may allow the creditor to determine the penalty using a penalty rate that may change over time (such as where a prepayment penalty on an adjustable-rate loan equals six months' interest payments.) In such cases, the creditor should disclose (1) the penalty charged when the penalty rate is the highest possible or (2) the penalty charged when the balance is the highest possible, whichever is greater. For example, assume that the interest rate for an adjustable-rate mortgage will remain fixed for the first 3 years after consummation and will adjust annually thereafter. The principal balance will be $200,000 at consummation and the loan amortizes. The initial interest rate on the loan is 5.625% and the maximum amount the interest rate can increase upon any rate adjustment is 2 percentage points. The terms of the legal obligation permit the creditor to impose a fee equal to 6 months' interest if the consumer prepays within the first 4 years. To determine the maximum prepayment penalty, the creditor must disclose (1) the penalty when the balance is highest or (2) the penalty when the penalty rate is highest, whichever is greater. The balance would be highest at consummation because the loan amortizes. The interest due the 1st month after consummation is $937.50. Six times the interest due in the first month is $5,625.00. The penalty rate would be highest in the 37th month after consummation, the first time the interest rate may increase during the period in which a prepayment penalty may be charged. Assuming the interest rate increased as much as possible, by 2 percentage points, the monthly interest due in the 37th month is $1,218.69. Six times the interest due in the 37th month is $7,312.14. The maximum penalty is the maximum penalty when the balance is highest, or $7,312.14, which is greater than the maximum penalty when the penalty rate is highest, or $5,625.00.

7. *Timely payment assumed.* The creditor may assume that the consumer makes payments on time and in the amount required by the terms of the legal obligation and may disregard any possible differences resulting from the consumer's payment patterns. *See* comment 17(c)(2)(i)–3. Where the terms of the obligation require a periodic payment that is not a fully amortizing payment, such as an interest only payment or a minimum payment that causes the loan balance to increase, the creditor must base disclosures on the required periodic payment and may not assume that the consumer will make payments that exceed the required payment.

8. *Rebate-penalty disclosure.* A single transaction may involve both a finance charge computed by application of a rate to the unpaid balance and a finance charge that is precomputed or otherwise does not take into account each reduction in the principal balance (for example, mortgages with mortgage-guarantee insurance for which premiums are calculated on an annual basis and do not take into account monthly declines in the principal balance). *See* comment 36(j)(6)–1. In these cases, disclosures about both prepayment rebates and penalties are required. Sample form H–15 in appendix H illustrates a mortgage transaction in which both rebate and penalty disclosures are necessary, and associated commentary explains the assumptions used in generating the sample.

38(b) Annual percentage rate.

Paragraph 38(b)(1).

1. *Disclosure required.* The creditor must disclose the cost of the credit as an annual rate, expressed as a percentage and using the term ''annual percentage rate,'' plus a brief descriptive phrase as required under § 226.38(b)(1). Under § 226.37(c)(2), the annual rate, expressed as a percentage, must be more conspicuous than the other required disclosures and in at least 16 point font.

Paragraph 38(b)(3).

1. *Applicable average prime offer rate and higher-priced loan threshold.* Creditors must disclose the APR on the loan offered, the average prime offer rate for a comparable transaction, and the higher priced loan threshold, for the week in which the creditor provides the disclosure. The higher-priced loan threshold is 1.5 percentage points above the comparable average prime offer rate for first lien loans, and 3.5 percentage points above the comparable average prime offer rate for subordinate lien loans. The Board publishes a table at least weekly with average prime offer rates by transaction type and loan term. Creditors should follow the guidance on how to determine the average prime offer rate and the higher-priced loan threshold in § 226.35(a)(2) and comments 35(a)(2)–1 through –4.

Paragraph 38(b)(4).

1. *Average per-period saving for 1 percentage-point reduction in the APR.* Section 226.38(b)(4) requires creditors to disclose the average per-period savings of a 1 percentage-point reduction in the APR disclosed in paragraph (b)(1). The creditor should base this disclosure on the terms of the legal obligation, except that the creditor must reduce the interest rate by one percentage point. If the legal obligation requires monthly payments, the creditor should identify the savings as the ''average per-month'' savings.

2. *Examples.* In both examples, assume the loan amount is $200,000 and the loan has a 30 year term with a total of 360 payments due monthly.

i. *Fixed-rate interest-only mortgage.* Assume that the loan is a fixed-rate mortgage with the option to make interest-only payments for the first 10 years of the loan. The interest rate is 6.5 percent. The total of payments disclosed under § 226.38(e)(5)(i) is $588,313.89. To calculate the average per-month savings, the creditor would reduce the interest rate to 5.5 percent for the full 30 year term of the loan and calculate a hypothetical total of payments of $540,627.21. The difference between the total of payments disclosed under § 226.38(e)(5)(i) and the hypothetical total of payments is $47,686.68. The creditor would divide $47,686.68 by the number of periods (360) and disclose an average per-month savings of $132.

ii. *Adjustable-rate mortgage.* Assume the loan is an ARM with a three-year introductory rate of 5.625 percent; the fully-indexed rate is 7.75 percent. At the end of the three year period, the interest rate will adjust, subject to a 2 percent rate cap. Thus, the interest rate in effect for year 4 is 7.625 percent. In year 5 the rate adjusts to the fully-indexed rate of 7.75 percent. The creditor should assume that the rate does not increase after it reaches the fully-indexed rate. The total of payments disclosed under § 226.38(e)(5)(i) is $585,778.09. To calculate the average per-month savings, the creditor would assume interest rates of 4.625 percent for the first 3 years; 6.625 percent for year 4; and 6.75 percent for the remainder of the loan. Thus, the rates are reduced by 1 percentage point, but the margin, periodic caps and other loan terms remain the same. The hypothetical total of payments is $537,087.61. The difference between the total of payments disclosed under § 226.38(e)(5)(i) and the hypothetical total of payments is $48,690.48. The creditor would divide $48,690.48 by the number of periods (360) and disclose an average per-month savings of $135.

38(c) Interest rate and payment summary.

1. *In general.* Section 226.38(c) prescribes format and content for disclosure of interest rates and monthly payments. The information in paragraph (c)(2)–(4) is required to be in the form of a table, except as provided otherwise. The required format and content of the table vary depending primarily on whether the loan has negative amortization. In all cases, however, the table should have no more than five vertical columns, showing applicable interest rates; payments would be shown in horizontal rows. Certain loan types and terms are defined for purposes of § 226.38(c) in § 226.38(c)(7).

2. *Amortizing loans.* Loans described as amortizing in § 226.38(c)(2)(i) and 226.38(c)(3) include loans with interest-only features that do not also have negative amortization features. (For rules relating to loans with balloon payments, *see* § 226.38(c)(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 § 226.38(c)(2)(iii).

3. *Negative amortization.* For loans with negative amortization, creditors should follow the rules in §§ 226.38(c)(2)(ii) and 226.38(c)(4) in disclosing interest rates and monthly payments. Loans with negative amortization also require special explanatory disclosures about rates and payments. See § 226.38(c)(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)(iii)–6, regarding graduated-payment adjustable-rate mortgages.

38(c)(2) Interest rates.

38(c)(2)(i) Amortizing loans.

Paragraph 38(c)(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 § 226.38(c)(4)(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)(iii)–7, regarding growth equity mortgages.

Paragraph 38(c)(2)(i)(B).

1. *ARMs and step-rate mortgages.* Creditors must disclose more than one interest rate for ARMs and step-rate mortgages, in accordance with paragraph (c)(2)(i)(B). Creditors must assume that interest rates rise after consummation, taking into account the terms of the legal obligation.

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

i. For an adjustable rate mortgage, the creditor must take into account any interest rate caps when disclosing the maximum interest rate at the first adjustment. The creditor must also disclose the date on which the first scheduled adjustment occurs.

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. The creditor should disclose the rate at first adjustment 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 interest rate could apply.

i. For an adjustable-rate mortgage, the creditor must take into account any interest rate caps in disclosing the maximum possible 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 loan, the creditor should disclose the highest rate that could apply under the terms of the legal obligation.

Paragraph 38(c)(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 § 26.38(c)(3)(ii)(B), the creditor must disclose the first payment of principal and interest. In such a case, the creditor must also disclose the interest rate that corresponds to the first payment of principal and interest, even though the interest rate will not adjust after consummation. 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 at first adjustment; and the maximum possible interest rate and payment.

38(c)(2)(ii) Loans with negative amortization.

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 ARMs with no interest rate caps except a maximum possible rate cap, creditors must assume that the interest rate reaches the maximum possible interest rate at 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 accruing each month, until the date the principal balance reaches 115 percent of its original balance, or until the 5th year after consummation, whichever comes first. The maximum possible rate is 10.5 percent. No other limits on interest rate changes 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 transaction as follows. 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, at the beginning of the second year; the rate of 10.5 percent and the corresponding minimum payment taking into account the 7.5 percent limit, at the beginning of the third year. The creditor must also 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.

Paragraph 38(c)(2)(iii).

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 226.38(c)(2)(iii) directly below the table.

38(c)(3) Payments for amortizing loans.

1. *Payments corresponding to interest rates.* Creditors must disclose a payment that corresponds to each interest rate disclosed under § 226.38(c)(2)(i)(A)–(C). Balloon payments, however, must be disclosed as provided in § 226.38(c)(5).

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

i. For fixed-rate interest-only transactions, § 226.38(c)(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 § 226.38(c)(5).

ii. For adjustable-rate mortgage transactions, § 226.38(c)(3)(i)(A) requires that for each interest rate required to be disclosed under § 226.38(c)(2)(i) (the interest rate at consummation, the maximum rate at the first adjustment, 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.

38(c)(3)(i)(C) Estimated amounts for taxes and insurance.

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.

2. *Mortgage insurance.* Payment amounts under § 226.38(c)(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 up to 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 up to the 128th payment should reflect premium payments.

Paragraph 38(c)(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.''

38(c)(4) Payments for negative amortization loans.

1. *Table.* Section 226.38(c)(1) provides that tables shall include only the information required in paragraph (c)(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.

Paragraph 38(c)(4)(i).

1. *Minimum required payments.* In one row of the table, the creditor must show the minimum required payment in each column, for each interest rate or adjustment required in § 226.38(c)(2)(ii), except that under the last column the fully amortizing payment must be shown and must be identified as the ''full payment.'' 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 § 226.38(c)(4)(i)(C) should be included in the heading for the row.

Paragraph 38(c)(4)(iii).

1. *Fully amortizing payments.* In one row of the table, the creditor must show the fully amortizing payment for every interest rate required in § 226.38(c)(2)(ii). The creditor must assume, for purposes of calculating the amounts in this row that the consumer makes only fully amortizing payments.

38(c)(5) Balloon payment.

1. *General.* A balloon payment is one that is more than two times the regular periodic payment. A balloon payment must be disclosed in a row under 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.

38(d) Key Questions About Risk.

38(d)(1) Required disclosures.

1. *Disclosure of first rate or payment increase.* Under § 226.38(d)(1)(i) and (ii), the creditor must disclose the calendar month and year in which the first interest rate or payment increase may occur.

38(d)(1)(iii) Prepayment penalty.

1. *Coverage.* See comment 38(a)(5)–1 to determine whether there is a prepayment penalty.

2. *Penalty.* See comment 38(a)(5)–2 for examples of charges that are prepayment penalties.

3. *Not penalty.* See comment 38(a)(5)–3 for examples of charges that are not prepayment penalties.

4. *Basis of disclosure.* Creditors may rely on comment 38(a)(5)–6 in determining the maximum prepayment penalty.

5. *Timely payment assumed.* In accordance with comment 38(a)(5)–7, creditors may disregard any possible differences resulting from the consumer's payment patterns and may base disclosures on the required payment and not an amortizing payment, if the loan has a negative amortization feature.

38(d)(2) Additional disclosures.

1. *As applicable.* The disclosures required by § 226.38(d)(2) need only be made as applicable. Any disclosure not relevant to the loan may be omitted.

38(d)(2)(iii) Balloon payment.

1. The creditor must make the balloon payment disclosure if the loan program includes a payment schedule with regular periodic payments that when aggregated do not fully amortize the outstanding principal balance.

38(d)(2)(iv) Demand feature.

1. *Disclosure requirements.* The disclosure requirements of § 226.38(d)(2)(iv) apply not only to transactions payable on demand from the outset, but also to transactions that convert to a demand status after a stated period.

2. *Covered demand features.* See comment 18(i)–2 for examples of covered demand features.

38(e) Information about payments.

38(e)(1) Rate calculation.

1. *Calculation.* If the interest rate will be calculated based on an index, an identification of the index to which the rate is tied, the amount of any margin that will be added to the index, and any conditions or events on which the increase is contingent must be disclosed. When no specific index is used, the factors used to determine any rate increase must be disclosed. When the increase in the rate is discretionary, the fact that any increase is within the creditor's discretion must be disclosed. When the index is internally defined (for example, by that creditor's prime rate), the creditor may comply with this requirement by providing either a brief description of that index or a statement that any increase is in the discretion of the creditor.

38(e)(2) Rate and payment change limits.

1. *Limitations on interest rate increases.* Limitations include any maximum imposed on the amount of an increase in the rate at any time, as well as any maximum on the total increase over the loan's term to maturity.

2. *Limitations on payment increases; negatively amortizing loans.* Limitations include any limit imposed on the change of a minimum payment amount whether or not the change is

accompanied by an adjustment to the interest rate. Any conditions on the limitation on payment increases must also be disclosed. For example, some loan programs provide that the minimum payment will not increase by more than a certain percentage, regardless of the corresponding increase in the interest rate. However, there may be exceptions to the limitation on the payment increase, such as if the consumer's principal balance reaches a certain threshold, or if the legal obligation sets out a scheduled time when payment increases will not be limited.

38(e)(5)(i) Total payments.

1. *Calculation of total payments scheduled.* Creditors should use the rules under § 226.18(g) and associated commentary, and comments 17(c)(1)(iii)–1 and –3 for adjustable-rate transactions, to calculate the total payments amount, except that the calculation of the total payments amount must include any amount required to be disclosed under § 226.38(c)(3)(i)(C).

2. *Number of payments.* See comment 18(g)–3.

3. *Demand obligations.* In demand obligations with no alternate maturity date, the creditor must make disclosure of total payments scheduled described in § 226.17(c)(5).

38(e)(5)(ii) Interest and settlement charges.

1. *Calculation of interest and settlement charges.* The interest and settlement charges disclosure is identical to the finance charge, as calculated under § 226.4.

2. *Disclosure required.* The creditor must disclose the interest and settlement charges as a dollar amount, using the term *interest and settlement charges,* together with a brief statement as required by § 226.38(e)(5)(ii). The interest and settlement charges must be disclosed only as a total amount; the components of the interest and settlement charges amount may not be itemized in the segregated disclosures, except as permitted under § 226.38(a)(4), although the regulation does not prohibit itemization elsewhere.

38(e)(5)(iii) Amount financed.

1. *Principal loan amount.* In a mortgage transaction subject to § 226.38, the principal loan amount is the same as the loan amount disclosed under § 226.38(a)(1). As provided in that section, the loan amount is the principal amount the consumer will borrow reflected in the loan contract. Thus the principal loan amount includes all amounts financed as part of the transaction, whether they are finance charges or not.

2. *Loan premiums and buydowns.* In a mortgage transaction, the creditor may offer a premium in the form of cash or merchandise to prospective borrowers. Similarly, a third party, such as a real estate developer or other seller, may offer to pay some portion of the consumer's costs of the credit transaction or to pay the creditor to ''buy down'' the consumer's interest rate. Such premiums and buydowns must be reflected in accordance with the terms of the legal obligation between the creditor and consumer. *See* § 226.17(c)(1) and comments 17(c)(1)–1, –2 and 17(c)(1)(i)–1 through –4. Thus, if the creditor is legally obligated by the terms of the credit obligation to charge a reduced interest rate or reduced costs as a consequence of the premium or buydown, regardless of its source, the disclosures, including the amount financed, should reflect those credit terms. Otherwise, the disclosures should be calculated without regard to any such premium or buydown.

3. *Disclosure required.* The net amount of credit extended must be disclosed using the term ''amount financed'' together with a descriptive statement as required by § 226.38(e)(5)(iii).

38(f)(4) Tax deductibility.

1. *Example.* The creditor can use the following language to satisfy the requirements of this section: ''If you borrow more than your home is worth, the interest on the extra amount may not be deductible for federal income tax purposes. Consult a tax advisor to find out whether the interest you pay is deductible.''

2. *Applicability.* If the creditor is not certain at the time of application whether the credit extended may exceed the fair market value of the dwelling, the creditor may, at its discretion, provide the disclosure required by this section in connection with all applications for closed-end credit secured by a dwelling or real property.

38(g) Identification of loan originator and creditor.

38(g)(1) Creditor.

1. *Identification of creditor.* The creditor making the disclosures must be identified. Use of the creditor's name is sufficient, but the creditor may also include an address and/or telephone number. In transactions with multiple creditors, any one of them may make the disclosures; the one doing so must be identified.

38(g)(2) Loan originator.

1. *Multiple loan originators.* In transactions with multiple loan originators, each loan originator's unique identifier must be disclosed. For example, in a transaction where a mortgage broker meets the definition of a loan originator under the Secure and Fair Enforcement for Mortgage Licensing Act of 2008, Section 1503(3), 12 U.S.C. 5102(3), the identifiers for the broker and for its employee originator meeting that definition must be disclosed.

38(h) Credit insurance and debt cancellation and debt suspension coverage.

1. *Location.* This disclosure may, at the creditor's option, appear apart from the other disclosures. It may appear with any other information, including the amount financed itemization, any information prescribed by State law, or other information. When this information is disclosed with the other segregated disclosures, however, no additional explanatory material may be included.

Paragraph 38(h)(5).

1. *Compliance.* If, based on the creditor's review of the consumer's age and/or employment status at the time of enrollment in the product, the consumer would not be eligible to receive the benefits of the product, then providing the disclosure required under § 226.38(h)(5) would not comply with this provision. That is, if the consumer does not meet the age and/or employment eligibility criteria, then the creditor cannot state that the consumer may be eligible to receive benefits and cannot comply with this requirement. If the creditor offers a bundled product (such as credit life insurance combined with credit involuntary unemployment insurance) and the consumer is not eligible for all of the bundled products, then providing the disclosure required under § 226.38(h)(5) would not comply with this provision. However, the disclosure still satisfies the requirements of this section if an event subsequent to enrollment, such as the consumer passing the age limit of the product, makes the consumer ineligible for the product based on the product's age or employment eligibility restrictions.

2. *Reasonably reliable evidence.* A disclosure under § 226.38(h)(5) shall be deemed to comply with this section if the creditor used reasonably reliable evidence to determine whether the consumer met the age or employment eligibility criteria of the product. Reasonably reliable evidence of a consumer's age would include using the date of birth on the consumer's credit application, on the driver's license or other government-issued identification, or on the credit report. Reasonably reliable evidence of a consumer's employment status would include a consumer's statement on a credit

application form, an Internal Revenue Service Form W–2, tax returns, payroll receipts, or other written evidence such as a letter or e-mail from the consumer or the consumer's employer.

38(i) Required deposit.

1. *Disclosure required.* The creditor must inform the consumer of the existence of a required deposit. (Appendix H provides a model clause that may be used in making that disclosure.) Section 226.38(i)(1) and (2) describe two types of deposits that need not be considered required deposits. Use of the phrase ''need not'' permits creditors to include the disclosure even in cases where there is doubt as to whether the deposit constitutes a required deposit.

2. *Pledged-account mortgages.* In these transactions, a consumer pledges as collateral funds that the consumer deposits in an account held by the creditor. The creditor withdraws sums from that account to supplement the consumer's periodic payments. Creditors may treat these pledged accounts as required deposits or they may treat them as consumer buydowns in accordance with the commentary to § 226.17(c)(1).

3. *Escrow accounts.* The escrow exception in § 226.38(i) applies, for example, to accounts for such items as maintenance fees, repairs, or improvements. (See the commentary to § 226.17(c)(1) regarding the use of escrow accounts in consumer buydown transactions.)

4. *Interest-bearing accounts.* When a deposit earns at least 5 percent interest per year, no disclosure is required. This exception applies whether the deposit is held by the creditor or by a third party.

5. *Examples of amounts excluded.* The following are among the types of deposits that need not be treated as required deposits:

i. Requirement that a borrower be a customer or a member even if that involves a fee or a minimum balance.

ii. Required property insurance escrow on a mobile home transaction.

iii. Refund of interest when the obligation is paid in full.

iv. Deposits that are immediately available to the consumer.

v. Funds deposited with the creditor to be disbursed (for example, for construction) before the loan proceeds are advanced.

vi. Escrow of condominium fees.

vii. Escrow of loan proceeds to be released when the repairs are completed.

38(j) Separate disclosures.

38(j)(1) Itemization of amount financed.

1. *Compliance alternatives.* The creditor has three alternatives in complying with § 226.38(j)(1). Under all three alternatives, the itemization (or its substitute) must be provided at the same time as the other disclosures required by § 226.38, although separate from those disclosures. The three alternatives are as follows:

i. The creditor may provide an itemization as a matter of course, without notifying the consumer of the right to receive the itemization.

ii. The creditor may inform the consumer, as part of the segregated disclosures, that a written itemization of the amount financed will be provided on request, furnishing the itemization only if the consumer in fact requests it.

iii. The creditor may substitute the GFE or HUD–1 settlement statement for the itemization. See comment 38(j)(1)(iii)–1 for additional guidance on this alternative.

Paragraph 38(j)(1)(i).

1. *Additional information.* Section 226.38(j)(1)(i) establishes a minimum standard for the information to be included in the itemization of the amount financed. Creditors have considerable flexibility in revising or supplementing the information listed in § 226.38(j)(1)(i). The creditor may, for example, do one or more of the following:

i. Include amounts that reflect payments not part of the amount financed. For example, costs of the transaction that the consumer pays directly, rather than out of loan proceeds, may be included.

ii. Organize the categories in any order. For example, the creditor may rearrange the terms in a mathematical progression that depicts the arithmetic relationship of the terms.

iii. Further itemize each category. For example, the amount paid directly to the consumer may be subdivided into the amount given by check and the amount credited to the consumer's savings account.

iv. Label categories with different language from that shown in § 226.38(j)(1)(i). For example, an amount paid on the consumer's account may be revised to identify the account specifically as ''your existing mortgage loan with us.''

v. Delete, leave blank, mark ''N/A,'' or otherwise note inapplicable categories in the itemization. For example, in a mortgage transaction to finance the purchase of a dwelling with no proceeds distributed directly to the consumer or amount credited to the consumer's account with the creditor, the amount financed may consist of only the amounts paid to others and the prepaid finance charge. In this case, the itemization may be composed of only those categories, and the other categories may be eliminated.

2. *Amounts appropriate to more than one category.* When an amount may appropriately be placed in any of several categories and the creditor does not wish to revise the categories shown in § 226.38(j)(1)(i), the creditor has considerable flexibility in determining where to reflect the amount. For example, in a mortgage transaction to refinance an existing mortgage held by the same creditor with additional proceeds paid to the consumer, the portion of the proceeds used to pay off the existing mortgage debt may be treated as either an amount paid to the consumer or an amount paid on the consumer's account. If the existing mortgage is held by another creditor, the portion of the proceeds used to pay it off may be treated as either an amount paid to the consumer or an amount paid to others on the consumer's behalf.

Paragraph 38(j)(1)(i)(A).

1. *Amounts paid to consumer.* This category encompasses funds given to the consumer in the form of cash or a check, including joint proceeds checks, as well as funds placed in an asset account. It may include money in an interest-bearing account even if that amount is considered a required deposit under § 226.38(i). For example, in a transaction with total loan proceeds of $50,000, assume the consumer receives a check for $30,000 and $20,000 is required by the creditor to be put into an interest-bearing account. Whether or not the $20,000 is a required deposit, it is part of the amount financed. At the creditor's option, it may be broken out and labeled in the itemization of the amount financed.

Paragraph 38(j)(1)(i)(B).

1. *Amounts credited to consumer's account.* The term *consumer's account* refers to an account in the nature of a debt with that creditor. It may include, for example, an unpaid balance on a prior loan or other amounts owing to that creditor. It does not include asset accounts of the consumer such as savings or checking accounts.

Paragraph 38(j)(1)(i)(C).

1. *Amounts paid to others.* This category includes, for example, title fees; amounts paid to insurance companies for insurance premiums; security interest fees; and amounts paid to credit bureaus, appraisers, and public officials. When several types of insurance premiums are financed, they may, at the creditor's option, be combined and listed in one sum, labeled ''insurance'' or similar term. This includes, but is not limited to, different types of insurance premiums paid to one company and different types of

insurance premiums paid to different companies. Except for insurance companies and other categories noted in § 226.38(j)(1)(i)(C), third parties must be identified by name.

Paragraph 38(j)(1)(i)(D).

1. *Prepaid finance charge.* Prepaid finance charges that are subtracted from the loan amount to calculate the amount financed, under § 226.38(e)(5)(iii), must be disclosed under § 226.38(j)(1)(i)(D). The prepaid finance charges must be shown as a total amount but, at the creditor's option, also may be further itemized and described. All amounts must be reflected in this total, even if portions of the prepaid finance charge are also reflected elsewhere. For example, if at consummation the creditor collects interim interest of $30 and an underwriting fee of $100, a total prepaid finance charge of $130 must be shown. At the creditor's option, the underwriting fee paid to a third party also may be shown elsewhere as an amount included in § 226.38(j)(1)(i)(C). The creditor also may further describe the two components of the prepaid finance charge, although no itemization of this element is required by § 226.38(j)(1)(i)(D).

2. *Prepaid finance charges placed in escrow.* RESPA requires creditors to give consumers a settlement statement disclosing the costs associated with mortgage loan transactions. Included on the settlement statement are payments into an escrow account for items that are prepaid finance charges. In calculating the total amount of prepaid finance charges, creditors should use the amounts listed on the respective lines of the settlement statement for each of those items, without adjustment, even if the actual amount collected at settlement may vary because of RESPA's escrow accounting rules. Figures for such items disclosed in conformance with RESPA shall be deemed to be accurate for purposes of Regulation Z.

Paragraph 38(j)(1)(iii).

1. *RESPA disclosures.* RESPA requires creditors to provide a good faith estimate of closing costs and a settlement statement listing the amounts paid by the consumer. For transactions subject to § 226.38, whether or not they are subject to RESPA, the creditor can satisfy § 226.38(j)(1) if the creditor complies with RESPA's requirements for a good faith estimate and settlement statement. The itemization of the amount financed need not be given, even though the content of the good faith estimate and HUD–1 settlement statement under RESPA differs from the requirements of § 226.38(j)(1)(i). If a creditor chooses to substitute RESPA's settlement statement for the itemization when redisclosure is required under § 226.19(a)(2), however, the statement must be provided to the consumer at the time required by that section.

38(j)(2) Rebate.

1. *Disclosure required.* The creditor must give a definitive statement of whether or not a rebate will be given. If a refund is possible for one type of prepayment, even though not for all, a positive disclosure is required. This applies to any type of prepayment, whether voluntary or involuntary as in the case of prepayments resulting from acceleration.

2. *Rebate-penalty disclosure.* Creditors may rely on comment 38(a)(5)–8 in determining how to disclose both a prepayment penalty and a rebate in a single transaction. Sample form H–15 in Appendix H illustrates a mortgage transaction in which both rebate and penalty disclosures are necessary.

3. *Prepaid finance charge.* The existence of a prepaid finance charge in a transaction does not, by itself, require a disclosure under § 226.38(j)(2). A prepaid finance charge is not considered a rebate under § 226.38(j)(2). At its option, however, a creditor may consider a prepaid finance charge to be a rebate under § 226.38(j)(2). If a disclosure is made under § 226.38(j)(2) with respect to a prepaid finance charge or other finance charge, the creditor may further identify that finance charge. For example, the disclosure may state that the borrower ''will not be entitled to a refund of the prepaid finance charge'' or some other term that describes the finance charge.

4. *Rebate of finance charge.* This applies to any finance charges that do not take account of each reduction in the principal balance of an obligation.

i. This category includes, for example:

A. Precomputed finance charges such as add-on charges.

B. Charges that take account of some but not all reductions in principal, such as mortgage guarantee insurance assessed on the basis of an annual declining balance, when the principal is reduced on a monthly basis.

ii. No description of the method of computing earned or unearned finance charges is required or permitted as part of the segregated disclosures under this section.

38(j)(3) Late payment.

1. *Definition.* This paragraph requires a disclosure only if charges are added to individual delinquent installments by a creditor who otherwise considers the transaction ongoing on its original terms. Late payment charges do not include:

i. The right of acceleration.

ii. Fees imposed for actual collection costs, such as repossession charges or attorney's fees.

iii. Deferral and extension charges.

iv. The continued accrual of simple interest at the contract rate after the payment due date. However, an increase in the interest rate is a late payment charge to the extent of the increase.

2. *Content of disclosure.* Many State laws authorize the calculation of late charges on the basis of either a percentage or a specified dollar amount, and permit imposition of the lesser or greater of the 2 charges. The disclosure made under § 226.38(j)(3) may reflect this alternative. For example, stating that the charge in the event of a late payment is 5% of the late amount, not to exceed $5.00, is sufficient.

38(j)(5) Contract reference.

1. *Content.* Creditors may substitute, for the phrase ''loan contract,'' a reference to specific transaction documents in which the additional information is found, such as ''promissory note.'' A creditor may, at its option, delete inapplicable items in the contract reference.

38(j)(6) Assumption policy.

1. *Policy statement.* In many mortgages, the creditor cannot determine, at the time disclosure must be made, whether a loan may be assumable at a future date on its original terms. For example, the assumption clause commonly used in mortgages sold to the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation conditions an assumption on a variety of factors such as the creditworthiness of the subsequent borrower, the potential for impairment of the lender's security, and execution of an assumption agreement by the subsequent borrower. In cases where uncertainty exists as to the future assumability of a mortgage, the disclosure under § 226.38(j)(6) should reflect that fact. In making disclosures in such cases, the creditor may use phrases such as ''subject to conditions,'' ''under certain circumstances,'' or ''depending on future conditions.'' The creditor may provide a brief reference to more specific criteria such as a due-on-sale clause, although a complete explanation of all conditions is not appropriate. For example, the disclosure may state, ''If you sell your home after you take out this loan, we may permit the new buyer to take over the payments on your mortgage, subject to certain conditions, such as payment of an assumption fee.'' See comment 17(a)(1)–5 for an example of a reference to a due-on-sale clause.

2. *Original terms.* The phrase ''original terms'' for purposes of section

226.38(j)(6) does not preclude the imposition of an assumption fee, but a modification of the basic credit agreement, such as a change in the contract interest rate, represents different terms.

* * * * *

Appendices 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] ►However,◄ formatting changes may not be made to ►to the following◄ model forms►, model clauses,◄ and samples► in Appendices G and H:◄ G–2[(A)], G–3[(A)], G–4[(A)], G–10(A)–(E), ►G–14(A)–(E), G–15(A)–(D),◄ 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►, G–22(A)–(B), G–23(A)–(B), G–24(A) (except as permitted pursuant to § 226.7(a)(2)), G–25, and G–26; and H–4(B) through H–4(L), H–17(A) through (D), H–19(A)–(I), and H–20 through H–22.◄ 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 ►for transactions not secured by real property or a dwelling◄.)

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

2. *Debt cancellation coverage.* This regulation does not authorize creditors to characterize debt cancellation ►or debt suspension◄ fees as insurance premiums for purposes of this regulation. Creditors may provide a disclosure that refers to debt cancellation ►or debt suspension◄ coverage whether or not the coverage is considered insurance. Creditors may use the model credit insurance disclosures only if the debt cancellation ►or debt suspension◄ coverage constitutes insurance under State law.

* * * * *

Appendix H—Closed-End Model Forms and Clauses

1. *Models H–1 and H–2.* Creditors may make several types of changes to closed-end model forms H–1 (credit sale) and H–2 (loan) and still be deemed to be in compliance with the regulation, provided that the required disclosures are made clearly and conspicuously. Permissible changes include the addition of the information permitted by [footnote 37 to] section 226.17 and ''directly related'' information as set forth in the commentary to section 226.17(a).

The creditor may also delete, or on multi-purpose forms, indicate inapplicable disclosures, such as:

- The itemization of the amount financed option (See sample[s] H–12[through H–15].)
- The credit [life and disability] insurance► or debt cancellation or debt suspension coverage◄ disclosures (See ►model clauses and◄ samples H-[11]►17(A) and H–17(C)◄ and H-[12]►17(B) and H–17(D)◄.)
- The property insurance disclosures (See ►model clause H–18, and ◄samples H–10 through H–12[, and H–14].)
- The ''filing fees'' and ''nonfiling insurance'' disclosures (See samples H–11 and H–12.)
- The prepayment penalty or rebate disclosures (See sample[s] H–12[and H–14].)
- The total sale price (See samples H–11 through H-[15]►12◄.)

Other permissible changes include:

- Adding the creditor's address or telephone number. (See the commentary to § 226.18(a).)
- Combining required terms where several numerical disclosures are the same, for instance, if the ''total of payments'' equals the ''total sale price.'' (See the commentary to § 226.18.)
- Rearranging the sequence or location of the disclosures—for instance, by placing the descriptive phrases outside the boxes containing the corresponding disclosures, or by grouping the descriptors together as a glossary of terms in a separate section of the segregated disclosures; by placing the payment schedule at the top of the form; or by changing the order of the disclosures in the boxes, including the annual percentage rate and finance charge boxes.
- Using brackets, instead of checkboxes, to indicate inapplicable disclosures.
- Using a line for the consumer to initial, rather than a checkbox, to indicate an election to receive an itemization of the amount financed.
- Deleting captions for disclosures.
- Using a symbol, such as an asterisk, for estimated disclosures, instead of an ''e.''
- Adding a signature line to the insurance disclosures to reflect joint policies.
- Separately itemizing the filing fees.
- Revising the late charge disclosure in accordance with the commentary to § 226.18(l).

2. *Model H–3.* ►Except as otherwise specifically provided,◄[C]►c◄reditors have considerable flexibility in filling out model H–3 (itemization of the amount financed). Appropriate revisions, such as those set out in the commentary to section 226.18(c)►, or section 226.38(j)(1) for transactions secured by real property or a dwelling◄, may be made to this form without loss of protection from civil liability for proper use of the model forms.

3. *Models H–4►(A)◄[through]►, H–4(C), H–4(H), H–5,◄ H–7►, H–16, H–17(A), H–17(C), H–18, and H–20 through H–23◄.* The model clauses are not included in the model forms although they are mandatory for certain transactions. Creditors using the model clauses when applicable to a transaction are deemed to be in compliance with the regulation with regard to that disclosure.

4. *Model H–4(A).* This model contains the variable-rate model clauses applicable to transactions subject to section 226.18(f)[(1)] and is intended to give creditors considerable flexibility in structuring variable-rate disclosures to fit individual plans. The information about circumstances, limitations, and effects of an increase may be given in terms of the contract interest rate or the annual percentage rate. Clauses are shown for hypothetical examples based on the specific amount of the transaction and based on a representative amount. Creditors may preprint the variable-rate disclosures based on a representative amount for similar types of transactions, instead of constructing an individualized example for each transaction. In both representative examples and transaction-specific examples, creditors may refer either to the incremental change in rate, payment amount, or number of payments, or to the resulting rate, payment amount, or number of payments. For example, creditors may state that the rate will increase by 2 percent, with a corresponding $150 increase in the payment, or creditors may state that the rate will increase to 16 percent, with a corresponding payment of $850.

5. *Model H–4(B)► and Samples H–4(D) through (F)◄.* [This model clause illustrates the variable-rate disclosure required under section 226.18(f)(2), which would alert consumers to the fact that the transaction contains a variable-rate feature and that disclosures were provided earlier]►Model H–4(B) illustrates, in the tabular format, the disclosures required under section 226.19(b) for adjustable-rate transactions secured by real property or a dwelling. The model form alerts consumers to risky features of the specific adjustable-rate mortgage program, and includes information on how the interest rate is determined and how it can change over time. The model form also directs the consumer to a Web site to obtain additional information on adjustable-rate programs or to

find a list of licensed housing counselors. Samples H–4(D) through (F) illustrate how to adapt the model form and clauses contained in appendix H–4(B) and H–4(C) to the creditor's own particular adjustable-rate program. Except as otherwise permitted, disclosures must be substantially similar in sequence and format to Model H–4(B). *See* comment app. H–18 regarding formatting details for samples H–4(D) through H–4(F).◀

6. *Model H–4(C).* Th[is]▶e◀ model clause▶s◀ illustrate[s] ▶certain◀[the] early disclosures required generally under 226.19(b). [It]▶They◀ include[s] information on how the consumer's interest rate is determined and how it can change over the term of the loan▶ when there is carryover interest, a conversion feature, or a preferred rate◀[, and explains changes that may occur in the borrower's monthly payment. It contains an example of how to disclose historical changes in the index or formula values used to compute interest rates for the preceding 15 years. The model clause also illustrates the disclosure of the initial and maximum interest rates and payments based on an initial interest rate (index value plus margin, adjusted by the amount of any discount or premium) in effect as of an identified month and year for the loan program disclosure and illustrates how to provide consumers with a method for calculating the monthly payment for the loan amount to be borrowed].

7. *Model▶s◀ H–4[D]▶(G), (H), and (K), and Samples H–4(I) and (J)◀.* [This model]▶Model H–4(G), and◀ model clause▶s contained in H–4(H),◀ illustrate[s]▶, in the tabular format, the disclosures◀ [the adjustment notice] required under section 226.20(c) [and provides] ▶regarding interest rate adjustment notices for adjustable rate transactions secured by real property or a dwelling. Model H–4(K) illustrates an annual notice of interest rate change without any corresponding change to payment. Samples H–4(I) and (J) provide◀ examples of payment-change notices [and annual notices of interest-rate changes]▶ for an interest-only, adjustable rate transaction and a hybrid adjustable rate transaction, respectively. Except as otherwise permitted, disclosures must be substantially similar in sequence and format to Models H–4(G) or H–4(K).◀

8. *Model H–5.* This contains the demand feature clause.

9. *Model H–6.* [This contains the assumption clause.]▶Reserved◀

10. *Model H–7.* This contains the required deposit clause.

11. *Models H–8 and H–9.* These models contain the rescission notices for a typical closed-end transaction and a refinancing, respectively. The last paragraph of each model form contains a blank for the date by which the consumer's notice of cancellation must be sent or delivered. A parenthetical is included to address the situation in which the consumer's right to rescind the transaction exists beyond 3 business days following the date of the transaction, for example, where the notice or material disclosures are delivered late or where the date of the transaction in paragraph 1 of the notice is an estimate. The language of the parenthetical is not optional. See the commentary to section 226.2(a)(25) regarding the specificity of the security interest disclosure for model form H–9. The prior version of model form H–9 is substantially similar to the current version and creditors may continue to use it, as appropriate. Creditors are encouraged, however, to use the current version when reordering or reprinting forms.

12. *Sample forms.* [The sample forms]▶Samples◀ [(]▶H–4(D) through H-(F), H4(I) and H–4(J),◀H–10 through H-[15]▶12, H–17(B) and H–17(D), and H–19(D) through (I)◀[)] serve a different purpose than the model forms▶ and model clauses◀. The samples illustrate various ways of adapting the model forms to the individual transactions described in the commentary to appendix H. The deletions and rearrangements shown relate only to the specific transactions described. As a result, the samples do not provide the general protection from civil liability provided by the model forms and clauses.

13. *Sample H–10.* This sample illustrates an automobile credit sale. The cash price is $7,500 with a downpayment of $1,500. There is an 8% add-on interest rate and a term of 3 years, with 36 equal monthly payments. The credit life insurance premium and the filing fees are financed by the creditor. There is a $25 credit report fee paid by the consumer before consummation, which is a prepaid finance charge.

14. *Sample H–11.* This sample illustrates an installment loan. The amount of the loan is $5,000. There is a 12% simple interest rate and a term of 2 years. The date of the transaction is expected to be April 15, 1981, with the first payment due on June 1, 1981. The first payment amount is labelled as an estimate since the transaction date is uncertain. The odd days' interest ($26.67) is collected with the first payment. The remaining 23 monthly payments are equal.

15. *Sample H–12.* This sample illustrates a refinancing and consolidation loan. The amount of the loan is $5,000. There is a 15% simple interest rate and a term of 3 years. The date of the transaction is April 1, 1981, with the first payment due on May 1, 1981. The first 35 monthly payments are equal, with an odd final payment. The credit disability insurance premium is financed. In calculating the annual percentage rate, the U.S. Rule has been used. Since an itemization of the amount financed is included with the disclosures, the statement regarding the consumer's option to receive an itemization is deleted.

16. *Samples H–[13]▶19(D)◀ through H–[15]▶19(I)◀.* These samples illustrate various mortgage transactions. They assume that the mortgages are subject to the Real Estate Settlement Procedures Act (RESPA). As a result, no option regarding the itemization of the amount financed has been included in the samples, because providing the good faith estimates of settlement costs required by RESPA satisfies Truth in Lending's amount financed itemization requirement. (See [footnote 39 to § 226.18(c)]▶§ 226.38(j)(1)(iii)◀.)

17. *Sample H–[13]▶16◀.* ▶This sample illustrates the disclosures required under § 226.32(c)(1) through (5). The sample illustrates▶ notices,◀ the amount borrowed▶,◀ and the disclosures about optional insurance that are required for mortgage refinancings under § 226.32(c)(5). The sample also includes disclosures required under § 226.32(c)(3) when the legal obligation includes a balloon payment.◀[This sample illustrates a mortgage with a demand feature. The loan amount is $44,900, payable in 360 monthly installments at a simple interest rate of 14.75%. The 15 days of interim interest ($294.34) is collected as a prepaid finance charge at the time of consummation of the loan (April 15, 1981). In calculating the disclosure amounts, the minor irregularities provision in § 226.17(c)(4) has been used. The property insurance premiums are not included in the payment schedule. This disclosure statement could be used for notes with the 7-year call option required by the Federal National Mortgage Association (FNMA) in states where due-on-sale clauses are prohibited.]

18. *[Sample H–14]▶Models H–19(A) through H–19(C)◀.* ▶i. These model forms illustrate, in the tabular format, the disclosures required generally under § 226.38(a) through 226.38(j) for transactions secured by real property or a dwelling. Creditors can use model H–19(A) for fixed-rate mortgage loans subject to § 226.38; model H–19(B) for adjustable-rate mortgages subject to § 226.38; and model H–19(C) for mortgages that are negatively amortizing and subject to § 226.38.

ii. Except as otherwise permitted, disclosures must be substantially similar in sequence and format to model forms H–19(A) through (C), as applicable.

iii. Although creditors are not required to use a certain paper size in disclosing the §§ 226.19(b), 226.20(c), 226.20(d) or 226.38 disclosures, samples H–4(D) through H–(F), and H–19(D) through H–19(I) are designed to be printed on an 8 × 11½ sheet of paper. In addition, the following formatting techniques were used in presenting the information in the sample forms to ensure that the information is readable:

A. A readable font style and font size (10-point Arial font style, except for the annual percentage rate which is shown in 16-point type);

B. Sufficient spacing between lines of the text;

C. Standard spacing between words and characters. In other words, the text was not compressed to appear smaller than 10-point type, except the headings in the tabular format used to provide the interest rate and payment disclosures required under § 226.38(c), which are shown in 9-point type;

D. Sufficient white space around the text of the information in each row, by providing sufficient margins above, below and to the sides of the text;

E. Sufficient contrast between the text and the background. Generally, black text was used on white paper.

iv. The Board is not requiring creditors to use the above formatting techniques in presenting information in the tabular format or scaled graph (except for the 10-point and 16-point minimum font requirements);

however, the Board encourages creditors to consider these techniques when disclosing information in the table or scaled graph to ensure that the information is presented in a readable format.◄[This sample disclosure form illustrates the disclosures under § 226.19(b) for a variable-rate transaction secured by the consumer's principal dwelling with a term greater than one year. The sample form shows a creditor how to adapt the model clauses in appendix H–4(C) to the creditor's own particular variable-rate program. The sample disclosure form describes the features of a specific variable-rate mortgage program and alerts the consumer to the fact that information on the creditor's other closed-end variable-rate programs is available upon request. It includes information on how the interest rate is determined and how it can change over time. Section 226.19(b)(2)(viii) permits creditors the option to provide either a historical example or an initial and maximum interest rates and payments disclosure; both are illustrated in the sample disclosure. The historical example explains how the monthly payment can change based on a $10,000 loan amount, payable in 360 monthly installments, based on historical changes in the values for the weekly average yield on U.S. Treasury Securities adjusted to a constant maturity of one year. Index values are measured for 15 years, as of the first week ending in July. This reflects the requirement that the index history be based on values for the same date or period each year in the example. The sample disclosure also illustrates the alternative disclosure under § 226.19(b)(2)(viii)(B) that the initial and the maximum interest rates and payments be shown for a $10,000 loan originated at an initial interest rate of 12.41 percent (which was in effect July 1996) and to have 2 percentage point annual (and 5 percentage point overall) interest rate limitations or caps. Thus, the maximum amount that the interest rate could rise under this program is 5 percentage points higher than the 12.41 percent initial rate to 17.41 percent, and the monthly payment could rise from $106.03 to a maximum of $145.34. The loan would not reach the maximum interest rate until its fourth year because of the 2 percentage point annual rate limitations, and the maximum payment disclosed reflects the amortization of the loan during that period. The sample form also illustrates how to provide consumers with a method for calculating their actual monthly payment for a loan amount other than $10,000.]

19. *Sample H–[15]►19(D)◄*. ►This sample illustrates the disclosures under § 226.38 for a fixed rate mortgage with a shared-equity feature. The loan amount is $210,000, payable in 36 monthly installments at a simple interest rate of 5.50%. The date of the transaction is March 26, 2009, and the sample assumes the average prime offer rate for the week of March 23, 2009 is 5.66%. There is a balloon payment of $202,217.84 due in March 2012. The taxes and property insurance premiums are not escrowed, and therefore, are shown as not included in the interest rate and payment summary table required under § 226.38(c).◄[This sample illustrates a graduated payment mortgage with a 5-year graduation period and a 7½ percent yearly increase in payments. The loan amount is $44,900, payable in 360 monthly installments at a simple interest rate of 14.75%. Two points ($898), as well as an initial mortgage guarantee insurance premium of $225.00, are included in the prepaid finance charge. The mortgage guarantee insurance premiums are calculated on the basis of ¼ of 1% of the outstanding principal balance under an annual reduction plan. The abbreviated disclosure permitted under § 226.18(g)(2) is used for the payment schedule for years 6 through 30. The prepayment disclosure refers to both penalties and rebates because information about penalties is required for the simple interest portion of the obligation and information about rebates is required for the mortgage insurance portion of the obligation.]

20. *Sample H–[16]►19(E)◄*. ►This sample illustrates the disclosures under § 226.38 for a fixed rate mortgage with interest-only payments for the first 10 years. The loan amount is $200,000, payable in 360 monthly installments, at a simple interest rate of 6.50%. The date of the transaction is February 26, 2009, and the sample assumes the average prime offer rate for the week of February 23, 2009 is 6.19%. The taxes and property insurance premiums are escrowed, and therefore, are shown as included in the total estimated monthly payment in the interest rate and payment summary table required under § 226.38(c).◄[This sample illustrates the disclosures required under § 226.32(c). The sample illustrates the amount borrowed and the disclosures about optional insurance that are required for mortgage refinancings under § 226.32(c)(5). Creditors may, at their option, include these disclosures for all loans subject to § 226.32. The sample also includes disclosures required under § 226.32(c)(3) when the legal obligation includes a balloon payment].

►21. *Sample H–19(F).* This sample illustrates the disclosures under § 226.38 for a step-payment mortgage with a seven-year step period and a 4 percent annual payment cap. This sample does not offer payment options. The consumer is required to make minimum payments for the first seven years; the minimum payments cover no principal and only some interest for the first two years and therefore, the mortgage has a negative amortization feature. Fully amortizing payments begin in year eight. The loan amount is $200,000, payable in 360 monthly installments at a simple interest rate of 6.50%. The date of the transaction is February 4, 2009, and the sample assumes the average prime offer rate for the week of February 2, 2009 is 5.75%. The taxes and property insurance are escrowed, and therefore, a statement of the amount of estimated taxes and insurance is included in the interest rate and payment summary disclosure required under § 226.38(c)(6)(i).

22. *Sample H–19(G).* This sample illustrates the disclosures under § 226.38 for a hybrid adjustable rate mortgage with a prepayment penalty that is in effect for the first 2 years. The loan amount is $200,000, payable in 360 monthly installments, with an initial discounted rate of 5.625% that is fixed for the first 3 years. The date of the transaction is February 26, 2009, and the sample assumes the average prime offer rate for the week of February 23, 2009 is 6.50%. The taxes and property insurance premiums are escrowed, and therefore, are shown as included in the total estimated monthly payment in interest rate and payment summary table required under § 226.38(c).

23. *Sample H–19(H).* This sample illustrates the disclosures under § 226.38 for a hybrid adjustable rate mortgage. The loan has an interest only payment option for the first 5 years, and a prepayment penalty that is in effect for the first 2 years. The loan amount is $200,000, payable in 360 monthly installments, with an initial discounted rate of 6.875% that is fixed for the first 5 years. The date of the transaction is February 26, 2009, and the sample assumes the average prime offer rate for the week of February 23, 2009 is 4.00%. The taxes, property insurance and private mortgage insurance premiums are escrowed, and therefore, are included in the interest rate and payment summary table required under § 226.38(c).

24. *Sample H–19(I).* This sample illustrates the disclosures under § 226.38 for an adjustable-rate mortgage with payment options. The loan amount is $200,000 and payable in 360 monthly installments. The loan has an initial 1-month introductory rate of 1.5% that adjusts to the maximum of 10.5% in the second month of the loan. The date of the transaction is February 4, 2009, and the sample assumes the average prime offer rate for the week of February 2, 2009 is 4.75%. The minimum payment option has an annual payment cap of 7.5% and can be made until the loan recasts at 115% of the original loan amount. This sample assumes only minimum payments are made until the loan recasts in June 2011, when fully amortizing payments of $2,402.54 would be required. The taxes and property insurance are escrowed, and therefore, a statement of the amount of estimated taxes and insurance is included in the interest rate and payment summary disclosure required under § 226.38(c)(6)(i).

25. *Model H–20.* This contains the balloon payment clause.

26. *Model H–21.* This contains the introductory rate clause.

27. *Model H–22.* These model clauses illustrate, in the tabular format, the disclosures required generally under § 226.38(d)(2) regarding key questions about risk for transactions secured by real property or a dwelling. Except as otherwise permitted, disclosures must be substantially similar in sequence and format to model forms H–19(A)–(C).

28. *Model H–23.* These model clauses illustrate the following disclosures required generally under § 226.38(j)(2)–(6) for transactions secured by real property or a dwelling: rebate; late payment; property insurance; contract reference; and assumption.◄

[21]►29◄. *HRSA–500–1 9–82.* Pursuant to section 113(a) of the Truth in Lending Act, Form HRSA–500–1 9–82 issued by the U.S. Department of Health and Human Services for certain student loans has been approved. The form may be used for all Health Education Assistance Loans (HEAL) with a

variable interest rate that are interim student credit extensions as defined in Regulation Z.

[22]►30◄. *HRSA–500–2 9–82.* Pursuant to section 113(a) of the Truth in Lending Act, Form HRSA–500–2 9–82 issued by the U.S. Department of Health and Human Services for certain student loans has been approved. The form may be used for all HEAL loans with a fixed interest rate that are interim student credit extensions as defined in Regulation Z.

[23]►31◄. *HRSA–502–1 9–82.* Pursuant to section 113(a) of the Truth in Lending Act, Form HRSA–502–1 9–82 issued by the U.S. Department of Health and Human Services for certain student loans has been approved. The form may be used for all HEAL loans with a variable interest rate in which the borrower has reached repayment status and is making payments of both interest and principal.

[24]►32◄. *HRSA–502–2 9–82.* Pursuant to section 113(a) of the Truth in Lending Act, Form HRSA–502–2 9–82 issued by the U.S. Department of Health and Human Services for certain student loans has been approved. The form may be used for all HEAL loans with a fixed interest rate in which the borrower has reached repayment status and is making payments of both interest and principal.

By order of the Board of Governors of the Federal Reserve System, July 24, 2009.

Robert deV. Frierson,

Deputy Secretary of the Board.

Note: The following attachments A and B will not appear in the Code of Federal Regulations.

BILLING CODE 6210–01–P

Attachment A

FEDERAL RESERVE BOARD CONSUMER PROTECTION RESOURCES

Key Questions to Ask About Your Mortgage

When you are shopping for a loan, ask each lender the questions below. Some loans have risky features that could make it difficult for you to make payments in the future. Make sure you understand the terms of your loan. If you are not comfortable with the risks, ask your lender about other loan products. **The only way to make sure you get the best possible loan terms is to talk to several lenders.**

Shop. Compare. Negotiate.

For more information about risky loan features, read *Shop Wisely: Understanding Your Mortgage Choices*, available at: www.federalreserve.gov.

1	**Can my interest rate increase?** If you have an adjustable rate mortgage (ARM), your interest rate can go up or down after a short period. This means that your monthly payments could increase.
2	**Can my monthly payment increase?** With some loans, your monthly payment could increase after a period of time, often by hundreds of dollars. This increase could be because you have a lower introductory interest rate, your property taxes or insurance premiums increase, or because in the beginning your monthly payment only covers the interest on the loan, and not the principal owed.
3	**Will my monthly payments reduce my loan balance?** Some loans let you pay only the interest on your loan each month. These payments do not pay down the amount you borrowed. As a result, if you have this type of loan, you may not build any equity in your home.
4	**Even if I make my monthly payments, can my loan balance increase?** Some loans let you choose to pay even less than the interest owed each month. The unpaid interest is added to your loan balance and increases the total amount that you owe. This could cause you to lose equity in your home over time.
5	**Could I owe a prepayment penalty?** Some loans charge you a large fee if you pay off your loan, refinance it, or sell your home within the first few years of the loan. This penalty fee could be thousands of dollars.
6	**Will I owe a balloon payment?** Some loans require a very large payment at the end of the loan—sometimes tens of thousands of dollars. If interest rates go up or if the value of your property drops, you may not be able to refinance your loan before you have to make this large payment.
7	**Will I have to document my employment, income, and assets to get this loan?** Sometimes a lender will make a loan without requiring you to show that you are employed and have the income or assets to repay the loan. These no-documentation ("no-doc") or low-documentation ("low-doc") loans usually have higher interest rates or higher fees than other loans.

Attachment B

FEDERAL RESERVE BOARD CONSUMER PROTECTION RESOURCES

Fixed vs. Adjustable Rate Mortgages

What Type of Mortgage is Right for You?

A traditional fixed rate mortgage is a safe choice for many borrowers, but in some circumstances an adjustable rate mortgage (ARM) might make sense for you. If you are considering an ARM, be sure you understand the tradeoffs.

Fixed Rate Mortgages	ARMs
With a fixed rate mortgage, the interest rate and monthly payment stay the same for the entire loan term.	With an ARM, the interest rate and monthly payment often start out lower than with a fixed rate mortgage. However, both the rate and payment can increase very quickly.
Consider a Fixed Rate Mortgage if: • You would prefer predictable payments or have difficulty managing monthly payments that increase; or • You plan to stay in your home for a long period of time.	*Consider an ARM if:* • You are confident that you could afford increases in your monthly payment, even at the maximum amount (sometimes as much as double your initial payment amount); or • You plan to sell your home within a short period of time.

If you are considering an ARM, don't count on being able to refinance before your interest rate and monthly payments increase. You might not qualify for refinancing if the market value of your home goes down, or your financial situation changes due to job loss, illness, or other large debts.

Where to Find Help

For more information about how to choose the right loan for you, or for a list of licensed housing counselors in your area that could help you make this decision, visit www.federalreserve.gov.

[FR Doc. E9–18119 Filed 8–25–09; 8:45 am]

BILLING CODE 6210–01–C