

FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Regulation Z; Docket No. R-1005]

Truth in Lending

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: The Board is publishing for comment a proposed rule amending Regulation Z, which implements the Truth in Lending Act. The proposal would permit creditors to use electronic communication (for example, communication via personal computer and modem) to provide disclosures required by the act and regulation, if the consumer agrees to such delivery.

DATES: Comments must be received by May 15, 1998.

ADDRESSES: Comments should refer to Docket No. R-1005, and may be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, DC 20551. Comments also may be delivered to Room B-2222 of the Eccles Building between 8:45 a.m. and 5:15 p.m. weekdays, or to the guard station in the Eccles Building courtyard on 20th Street, N.W. (between Constitution Avenue and C Street) at any time. Comments may be inspected in Room MP-500 of the Martin Building between 9:00 a.m. and 5:00 p.m. weekdays, except as provided in 12 CFR 261.12 of the Board's Rules Regarding Availability of Information.

FOR FURTHER INFORMATION CONTACT: Michael Hentrel, Obrea Poindexter, or Pamela Morris Blumenthal, Staff Attorneys, Division of Consumer and Community Affairs, at (202) 452-3667 or (202) 452-2412. For the hearing impaired only, Telecommunications Device for the Deaf (TDD), contact Diane Jenkins, at (202) 452-3544.

SUPPLEMENTARY INFORMATION:

I. Background

The purpose of the Truth in Lending Act (TILA), 15 U.S.C. 1601 et seq., is to promote the informed use of consumer credit by requiring disclosures about its terms and cost. The act

requires creditors to disclose the cost of credit as a dollar amount (the finance charge) and as an annual percentage rate (the APR). Uniformity in creditors' disclosures is intended to assist consumers in comparison shopping. The TILA requires additional disclosures for loans secured by consumers' homes and permits consumers to rescind certain transactions that involve their principal dwellings. The act is implemented by the Board's Regulation Z (12 CFR Part 226).

As part of the Regulatory Planning and Review Program and its review of regulations under section 303 of the Riegle Community Development and Regulatory Improvement Act of 1994 (12 U.S.C. 4803), the Board determined that the use of electronic communication for delivery of information to consumers that is required by federal consumer financial services and fair lending laws could effectively reduce regulatory compliance burden without adversely affecting consumer protections. Thus, the Board has been considering the issue and closely following the development of electronic communication. For example in May 1996, the Board proposed to amend Regulation E (Electronic Fund Transfers) to permit disclosures to be provided electronically. In March 1997, the Board issued an amendment to the staff commentary to Regulation CC (Availability of Funds and Collection of Checks) that allowed financial institutions to send notices electronically. (62 FR 13801, March 18, 1997.)

Having considered the comments received on the Regulation E proposal and other rulemakings, the Board now proposes to amend Regulation Z to allow creditors to provide Regulation Z disclosures electronically; such disclosures would remain subject to any applicable timing, format, and other requirements of the act and the regulation. Concurrently, the Board is issuing similar proposed revisions to address electronic communication under Regulations DD (Truth in Savings), B (Equal Credit Opportunity), and M (Consumer Leasing), published elsewhere in today's Federal Register. In addition, the Board has issued an interim rule under Regulation E so that financial institutions can implement systems to provide Electronic Fund Transfer Act disclosures electronically.

II. Proposed Regulatory Revisions

The TILA and Regulation Z require several disclosures to be provided to consumers in writing. The requirement that disclosures be in writing has been presumed to require that creditors provide paper documents. However, under many laws that call for information to be in writing, information in electronic form is considered to be "written." Information produced, stored, or communicated by computer is also generally considered to be a writing at least where visual text is involved.

Therefore, pursuant to its authority under section 105 of the TILA, the Board proposes to amend Regulation Z to permit creditors to use electronic communication where the regulation calls for information to be provided in writing. The term "electronic communication" is limited to a communication that can be displayed as visual text. An example is an electronic visual text message that is displayed on a screen (such as the consumer's computer monitor). Communications by telephone voicemail systems do not meet the definition of "electronic

communication” for purposes of this regulation because they do not have the feature generally associated with a writing -- visual text.

Section 226.2(a)(27) would be revised to include the definition of electronic communication for purposes of Regulation Z. Under the definition, electronic communication is a visual text message electronically transmitted between a creditor and a consumer's home computer or other electronic device used by a consumer. Sections 226.5, 226.17 and 226.31 would be revised to address electronic communication. These sections contain general disclosure requirements for open-end credit, closed-end credit, and certain home secured loans referred to as “HOEPA loans.”

Agreements Between Creditors and Consumers

Sections 226.5(a)(5), 226.17(a)(3), and 226.31(b)(2) would permit creditors to send electronic disclosures if the consumer agrees. There may be various ways that a creditor and a consumer could agree to the electronic delivery of disclosures and other information. Whether such an agreement exists between the parties would be determined by applicable state law. The regulation would not preclude a creditor and a consumer from entering into an agreement electronically, nor does it prescribe a formal mechanism for doing so. The Board does believe, however, that consumers should be clearly informed when they are consenting to the delivery of TILA disclosures and other information electronically.

Delivery Requirements for Electronic Communication

Regulation Z provides that an institution "furnish," "provide," "send," "deliver," or "mail" information to a consumer. Generally, the delivery requirement anticipates that a creditor will deliver the information--typically by mail--to an address designated by the consumer. For a paper communication, a creditor would not satisfy that requirement by making disclosures "available" to consumers, for example, at a creditor's office or other location. The Board believes that consumers receiving disclosures by electronic communication should have protections regarding delivery similar to those afforded consumers receiving disclosures in paper form. Simply posting information on an Internet site without some appropriate notice and instructions about how the consumer may obtain the required information would not satisfy the requirement.

The requirement to send disclosures to a consumer would be satisfied when the institution ensures that the disclosures will be displayed in a timely manner. For example, under Regulation Z, open-end credit initial disclosures generally must be provided before the first transaction under the plan. Assume that a consumer uses a personal computer to apply for a plan and consents to the electronic delivery of the initial disclosures. If the disclosures automatically appear on the computer screen before the consumer commits to the plan (in accordance with the format, timing rules and any other requirements of the act and regulation), the creditor would satisfy the requirement to provide (deliver or transmit) disclosures to the consumer.

As a practical matter, there may be little distinction between sending or delivering electronic disclosures and making them “available.” Creditors have flexibility in how they may deliver electronic disclosures to consumers, including, but not limited to, the following examples. They may send disclosures to a consumer-designated electronic mail address or they may designate a location on a website where the consumer enters a personal identification number or other identifier to access required information. In the scenario described above, assume that the consumer applies for a credit plan, receives the initial disclosures at that time, and agrees to receive all Regulation Z disclosures electronically. Subsequent disclosures sent to the designated address or placed at a designated location (for example, periodic statements or change-in-terms notices) would satisfy the delivery requirements of the regulation.

Electronic communication would remain subject to any timing or other applicable requirements under Regulation Z. For example, an electronic change in terms notice required by § 226.9(c) of Regulation Z must still be provided at least fifteen days in advance of the change. The Board solicits comment on whether further guidance is needed on how to comply with the timing requirements when a notice is posted on an Internet website.

Section 226.5a -- Credit and Charge Card Applications and Solicitations

The act and regulation require credit and charge card issuers to provide credit disclosures in certain applications and solicitations to open credit and charge card accounts. Format and content requirements differ for applications or solicitations sent in direct mail campaigns and for those made available to the general public such as in “take-ones” and catalogs or magazines. Disclosures accompanying direct mail applications and solicitations must be presented in a tabular format. Disclosures in a take-one also may be presented in a table with the same content as for direct mail, but the act and regulation permit alternatives as to format and content. The APR disclosed in a direct mail solicitation must be accurate within 60 days of mailing; in a take-one, within 30 days of printing.

Consumers could obtain an electronically sent credit or charge card application in much the same way as either opening a direct-mail piece or browsing through a magazine. Under the proposal, if a card issuer sends an application or solicitation to a consumer by electronic means that alert the consumer that the application or solicitation has arrived, such as electronic mail, the card issuer would follow the direct-mail rules under § 226.5a. If an issuer merely makes an application or solicitation publicly available, such as by posting it on an Internet site, the issuer would follow the “take-one” rules. The Board believes that in the context of electronic communications, “printing” is the equivalent of updating a site on the Internet, for example. Thus, where the “take-one” rules apply, consumers would view APRs that are accurate within 30 days of the card issuer’s most recent update of the Internet site. Where the direct-mail rules apply, the APRs disclosed would be accurate within 60 days of the sending of the electronic application or solicitation. The Board requests comment on any compliance difficulties this approach may pose, and possible suggestions for their resolution.

Section 226.17(g) -- Mail or Telephone Orders -- Delay in Disclosures

Section 226.17(g) allows credit to be offered via mail, telephone, or other electronic means and full TILA disclosures to be deferred as long as a certain number of disclosures are "made available in written form." The rationale underlying the deferral is that, in some instances, the creditor cannot provide disclosures in the form required by the regulation because of the lack of face to face or direct interaction with the consumer. Because loan products offered by electronic communication (for example, those offered on the Internet) do not appear to pose the same difficulty, the Board believes that this deferral should not apply to electronic disclosures. The Board believes that permitting a deferral would not effectuate the purpose of the TILA to provide consumers with information about credit terms prior to being obligated. Thus, the proposed rule provides that specific disclosures must be provided before consummation of the transaction.

Requirement That Information Be "Clear and Conspicuous"

The act and Regulation Z require creditors to present required information "clearly and conspicuously." Under the proposed rule, the "clear and conspicuous" requirement applies to electronic communication. The Board does not intend to discourage or encourage specific types of technologies. Regardless of technology, however, the disclosures provided by electronic communication must meet the "clear and conspicuous" standard. While a creditor is generally not required to ensure that the consumer has the equipment to read the disclosures, in some circumstances a creditor would have the responsibility of making sure the proper equipment is in place. For example, to use electronic disclosures for credit offered through terminals in a creditor's lobby, or through kiosks located in public or other places, the creditor must ensure that the equipment meets the clear and conspicuous standard for TILA disclosures that are being provided electronically.

Consumer Ability to Retain Disclosures

Regulation Z requires that many of its written disclosures be in a form that the consumer may keep. This requirement would apply to disclosures provided by electronic communication. Creditors would satisfy the retention requirement if, for example, disclosures can be printed or downloaded by the consumer. The requirements for electronic delivery should be similar to the current paper requirements, where creditors generally must mail or deliver the information to the consumer but need not ensure that the consumer reads or retains it. Thus, creditors would not be required to monitor an individual consumer's ability to retain the information, nor to take steps to find out whether the consumer has in fact retained it. The Board anticipates that, where appropriate, a creditor would provide special technical specifications for receiving or retaining information before or at the time a consumer agrees to receive information electronically.

As in the case of the "clear and conspicuous" standard discussed above, in circumstances where the creditor (or a network of which the creditor is a member) controls the equipment to be used for the service -- such as terminals in institution lobbies or kiosks in shopping centers -- the

creditor would have the responsibility of ensuring retainability. Provided that the delivery requirements (discussed above) are satisfied, methods for fulfilling this requirement could include, for example, printers incorporated into terminals or a screen message offering to transmit the disclosure to the consumer's electronic mail or post office address.

Signature Requirements Under Regulation Z

There are two signature requirements under Regulation Z. Under § 226.4(d) consumers may elect to accept credit life insurance by signing or initialing an affirmative written request after receiving disclosure about the insurance. Under § 226.23 (and the corresponding model forms and official staff commentary) consumers may cancel certain home-secured loans or waive this right by providing a written signed notice to the creditor. The Board indicated in the May 1996 Regulation E proposal that any electronic authentication method should provide the same assurance as a signature in a paper-based system, and cited security codes and digital signatures as examples of authentication devices that might meet the requirements. The Board is interested in learning about other ways in which authentication in an electronic environment might take the place of the consumer's signature.

Current Need for Safeguards Concerning the Electronic Delivery of Disclosures

Today, most consumers receive federal disclosures in paper form. As electronic commerce and electronic banking increase and technological advances take place, obtaining disclosures by electronic communication will likely become more commonplace. Currently, however, the use of electronic communication in the delivery of financial services is still evolving. Thus, it is difficult to fully predict the extent to which additional safeguards, if any, may be needed to ensure that consumers receive the same protections that exist for disclosures in paper form. The Board expects that creditors subject to the TILA and Regulation Z will provide sufficient details about the delivery of disclosures. The Board plans to closely monitor the development of electronic delivery of TILA disclosures and other information, and will address compliance or other issues that may arise as appropriate.

III. Form of Comment Letters

Comment letters should refer to Docket No. R-1005 and, when possible, should use a standard typeface with a type size of 10 or 12 characters per inch. This will enable the Board to convert the text to machine-readable form through electronic scanning, and will facilitate automated retrieval of comments for review. Also, if accompanied by an original document in paper form, comments may be submitted on 3 ½ inch or 5 1/4 inch computer diskettes in any IBM-compatible DOS-based format.

IV. Regulatory Flexibility Analysis

In accordance with section 3(a) of the Regulatory Flexibility Act, the Board's Office of the Secretary has reviewed the proposed amendments to Regulation Z. Overall, the proposed amendments are not expected to have any significant impact on small entities. The proposed rule would relieve compliance burden by giving creditors flexibility in providing disclosures. A final regulatory flexibility analysis will be conducted after consideration of comments received during the public comment period.

V. Paperwork Reduction Act

In accordance with section 3506 of the Paperwork Reduction Act of 1995 (44 U.S.C. Ch. 35; 5 CFR 1320 Appendix A.1), the Board reviewed the proposed revisions under the authority delegated to the Board by the Office of Management and Budget.

The Federal Reserve has no data with which to estimate the burden the proposed revised requirements would impose on state member banks. Creditors would be able to use electronic communication to provide disclosures and other information required by this regulation rather than having to print and mail the information in paper form. The use of electronic communication in home banking and financial services may reduce the paperwork burden on creditors and financial institutions or merely may reduce the dollar cost.

The Federal Reserve requests comments from creditors, especially state member banks, that will help to estimate the number and burden of the various disclosures that would be made in the first year this rule is effective. Comments are invited on: (a) whether the proposed revised collection of information is necessary for the proper performance of the Federal Reserve's functions, including whether the information has practical utility; (b) the accuracy of the Federal Reserve's estimate of the burden of the proposed revised information collection, including the cost of compliance; (c) ways to enhance the quality, utility, and clarity of the information to be collected; and (d) 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 the Office of Management and Budget, Paperwork Reduction Project (7100-0199), Washington, DC 20503, with copies of such comments to be sent to Mary M. McLaughlin, Chief, Financial Reports Section, Division of Research and Statistics, Mail Stop 97, Board of Governors of the Federal Reserve System, Washington, DC 20551.

The collection of information requirements in this proposed revised regulation are found throughout 12 CFR Part 226 and in Appendices F, G, H, J, K, and L. This information is mandatory (15 U.S.C. 1604(a)) to ensure the disclosure of certain credit costs and terms to consumers, at or before the time consumers enter into a consumer credit transaction and when the availability of consumer credit on particular terms is advertised. The purpose of the disclosures is to encourage competition among various credit sources through informed comparison-shopping by consumers. The respondents/recordkeepers are for-profit financial institutions, including small

businesses. Creditors are also required to retain records as evidence of compliance for twenty-four months.

The Board also proposes to extend the Recordkeeping and Disclosure Requirements in Connection with Regulation Z (OMB No. 7100-0199) for three years. The current estimated total annual burden for this information collection is 1,878,846 hours, as shown in the table below. These amounts reflect the burden estimate of the Federal Reserve System for the 996 state member banks under its supervision. This regulation applies to all types of creditors, not just state member banks. However, under Paperwork Reduction Act regulations, the Federal Reserve accounts for the burden of the paperwork associated with the regulation only for state member banks. Other agencies account for the paperwork burden for the institutions they supervise.

	<i>number of respondents</i>	<i>estimated annual frequency</i>	<i>estimated response time</i>	<i>estimated annual burden hours</i>
Open-end credit				
Initial terms	996	1,150	2.5 minutes	47,725
Change in terms	996	2,500	1.0 minute	41,500
Periodic Statements	996	86,250	45.0 seconds	1,073,813
Error resolution	996	8	15.0 minutes	1,992
Credit and charge card accounts				
Advance disclosures	996	29,750	10.0 seconds	82,308
Renewal notice	996	10,700	5.0 seconds	14,802
Insurance notice	996	60	15.0 seconds	249
Home equity plans				
Advance disclosure	996	120	2.0 minutes	3,984
Change in terms	996	3	2.0 minutes	100
Closed-end credit disclosures	996	5,750	6.4 minutes	610,880
Advertising	996	3	30.0 minutes	<u>1,493</u>
<i>Total</i>				<u>1,878,846</u>

General disclosures of credit terms that appear in advertisements or take-one applications are available to the public. Since the Federal Reserve does not collect any information, no issue of confidentiality normally arises. However, the information may be protected from disclosure under the exemptions (b)(4), (6), and (8) of the Freedom of Information Act (5 U.S.C. 522 (b)). Transaction- or account-specific disclosures and billing error allegations are not publicly available and are confidential between the creditor and the consumer. An agency may not conduct or

sponsor, and an organization is not required to respond to, an information collection unless it displays a currently valid OMB control number. The OMB control number for the Recordkeeping and Disclosure Requirements in Connection with Regulation Z is 7100-0199.

List of Subjects in 12 CFR Part 226

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

Text of Proposed Revisions

Certain conventions have been used to highlight the proposed changes to Regulation Z. New language is shown inside bold-faced arrows, while language that would be removed is set off with brackets.

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

PART 226 -- TRUTH IN LENDING (REGULATION Z)

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

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

2. Section 226.2 would be amended by adding a new paragraph (a)(27) to read as follows:

§ 226.2 Definitions and rules of construction.

- (a) Definitions. ***

<(27) Electronic communication means a message transmitted electronically between a consumer and a creditor in a format that allows visual text to be displayed on equipment such as a personal computer monitor.=

3. Section 226.5 would be amended by adding a new paragraph (a)(5) as follows:

§ 226.5 General disclosure requirements.

- (a) Form of disclosures. ***

<(5) Electronic communication. A creditor and a consumer may agree to send by electronic communication, as that term is defined in § 226.2(a)(27), any information required by this subpart

to be provided in writing. Information sent by electronic communication to a consumer must comply with § 226.5(a)(1) and any applicable timing requirements contained in this subpart.=

4. Section 226.17 would be amended as follows:

- a. By adding a new paragraph (a)(3); and
- b. By revising paragraph 17(g).

The revision and addition would read as follows:

§ 226.17 General disclosure requirements.

(a) Form of disclosures. ***

<(3) Electronic communication. A creditor and a consumer may agree to send by electronic communication, as that term is defined in § 226.2(a)(27), any information required by this subpart to be provided in writing. Information sent by electronic communication to a consumer must comply with § 226.17(a)(1) and any applicable timing requirements contained in this subpart.=
* * * * *

(g) Mail or telephone orders--delay in disclosures. If a creditor receives a purchase order or a request for an extension of credit by mail, telephone, or any other written [or electronic] communication <, excluding electronic communication as discussed in § 226.17(a)(3),= without face-to-face or direct telephone solicitation, the creditor may delay the disclosures until the due date of the first payment***:
* * * * *

5. Section 226.31 would be amended by redesignating paragraph (b) as paragraph (b)(1) and adding a new paragraph (b)(2) as follows:

§ 226.31 General rules.

* * * * *

(b)<(1)= Form of disclosures. ***

<(2) Electronic communication. A creditor and a consumer may agree to send by electronic communication, as that term is defined in § 226.2(a)(27), any information required by this subpart

to be provided in writing. Information sent by electronic communication to a consumer must comply with § 226.31(b) and any applicable timing requirements contained in this subpart.=

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By order of the Board of Governors of the Federal Reserve System, March 12, 1998.

 (Signed)
William W. Wiles,
Secretary of the Board.