transaction. However, these costs may be excluded from the finance charge and APR (for both open-end and closed-end credit transactions), if creditors disclose the cost and the fact that the coverage is not required to obtain credit, and the consumer signs or initials an affirmative written request for the insurance. Since 1996, the same rules have applied to creditors' "debt cancellation" agreements, in which a creditor agrees to cancel the debt, or part of it, on the occurrence of specified events.

Under the proposal, the existing rules for debt cancellation coverage would also be applied to "debt suspension" coverage (for both open-end credit and closed-end transactions). "Debt suspension" products are related to, but different from, debt cancellation. Debt suspension products merely defer consumers' obligation to make the minimum payment for some period after the occurrence of a specified event. During the suspension period, interest may continue to accrue, or it may be suspended as well. Under the proposal, to exclude the cost of debt suspension coverage from the finance charge and APR, creditors must inform consumers that the coverage suspends, but does not cancel, the debt.

Under the current rules, charges for credit insurance and debt cancellation coverage are deemed not to be finance charges if a consumer requests coverage after an open-end credit account is opened or after a closed-end credit transaction is consummated (the coverage is deemed not to be "written in connection" with the credit transaction). Because in such cases the charges are defined as non-finance charges, Regulation Z does not require a disclosure or written evidence of consent to exclude them from the finance charge. The proposed revisions to Regulation Z would implement a broader interpretation of "written in connection" with a credit transaction and require creditors to provide disclosures, and obtain evidence of consent, on sales of credit insurance or debt cancellation or suspension coverage during the life of an open-end account. If a consumer requests the coverage by telephone, creditors may provide the disclosures orally, but in that case they must mail written disclosures within three days of the call.[5]

## VI. Section-by-section Analysis

In reviewing the rules affecting open-end credit, the Board has reorganized some provisions to make the regulation easier to use. Rules affecting home-equity lines of credit (HELOCs) subject to § 226.5b are separately delineated in § 226.6 (account-opening disclosures), § 226.7 (periodic statements), and § 226.9 (subsequent disclosures) Footnotes have been moved to the text of the regulation or commentary, as appropriate. These proposed revisions are identified in a table below. See **IX. Redesignation Table.**

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[5] The proposed revisions to Regulation Z requiring disclosures to be mailed within three days of a telephone request for these products are consistent with the rules of the federal banking agencies governing insured depository institutions' sales of insurance and with guidance published by the Office of the Comptroller of the Currency (OCC) concerning national banks' sales of debt cancellation and debt suspension products.

**Introduction**

The official staff commentary to Regulation Z begins with an Introduction. Comment I-6 discusses reference materials published at the end of each section of the commentary adopted in 1981. 46 FR 50,288; October 9, 1981. The references were intended as a compliance aid during the transition to the 1981 revisions to Regulation Z. The Board would delete these references and comment I-6, as obsolete. Comment I-3, I-4(b), and I-7, which address 1981 rules of transition, also would be deleted as obsolete.

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

Section 226.1(c) generally outlines the persons and transactions covered by Regulation Z. Comment 1(c)-1 provides, in part, that the regulation applies to consumer credit extended to residents (including resident aliens) of a state. Technical revisions are proposed for clarity. Comment is requested if further guidance on the scope of coverage would be helpful.

Section 226.1(d)(2), which summarizes the organization of the regulation's open-end credit rules (Subpart B), would be amended to reinsert text inadvertently deleted in a previous rulemaking. See 54 FR 24,670; June 9, 1989. Section 226.1(d)(4), which summarizes miscellaneous provisions in the regulation (Subpart D), would be updated to describe amendments made in 2001 to Subpart D relating to disclosures made in languages other than English. See 66 FR 17,339; March 30, 2001. The substance of Footnote 1 would be deleted as unnecessary.

**Section 226.2 Definitions and Rules of Construction**

**2(a) Definitions**
**2(a)(2) Advertisement**

For clarity, the Board proposes technical revisions to the commentary to § 226.2(a)(2), with no intended change in substance or meaning. No changes are proposed for the text of § 226.2(a)(2).

**2(a)(4) Billing Cycle**

TILA Section 127(b) provides that, for an open-end credit plan, the creditor shall send the consumer a periodic statement for each billing cycle at the end of which there is an outstanding balance or with respect to which a finance charge is imposed. 15 U.S.C. 1637(b). "Billing cycle" is not defined in the statute, but is defined in § 226.2(a)(4) of Regulation Z as "the interval between the days or dates of regular periodic statements." In addition, § 226.2(a)(4) requires that billing cycles be equal and no longer than a quarter of a year, and allows a variance of up to four days from the regular day or date of the statement. Comment 2(a)(4)-3 provides an exception to the requirement for equal cycles: the "transitional billing cycle that can occur when the creditor occasionally changes its billing cycles so as to establish a new statement day or date." Under the proposal, the Board would clarify that creditors may also vary the length of the first cycle on an open-end account in certain situations.

Questions have sometimes arisen about the first cycle that occurs when a consumer opens an open-end credit account, and specifically, about whether the first cycle may vary by more than four days from the regular cycle interval without violating the equal-cycle requirement. For example, in order to establish the consumer's account on the creditor's billing system, the first cycle may need to be longer or shorter than a monthly period by more than four days, depending upon the date the account is opened. The Board believes that such a variance for a first cycle, within reason, would not harm consumers and would facilitate compliance. Comment 2(a)(4)-3 would be revised to clarify this point.

**2(a)(15) Credit Card**

TILA defines "credit card" as "any card, plate, coupon book or other credit device existing for the purpose of obtaining money, property, labor, or services on credit." TILA Section 103(k); 15 U.S.C. 1602(k). In addition, Regulation Z provides that a credit card is a "single credit device that may be usable from time to time to obtain credit." See § 226.2(a)(15). The definition of "credit card" in the regulation would remain largely unchanged; however, the current reference to a "coupon book" in the definition would be deleted as obsolete.

Checks that access credit card accounts. Credit card issuers sometimes provide cardholders with checks that access a credit card account, which can be used to obtain cash, purchase goods or services, or pay the outstanding balance on another account. These checks are often mailed to consumers unsolicited, sometimes with consumers' monthly statements. When a consumer uses such a check, the amount of the check will be billed to the cardholder's account.

Historically, checks that access credit card accounts have not been treated as "credit cards" under TILA because each check can be used only once and not "from time to time." See comment 2(a)(15)-1. As a result, TILA's protections involving merchant disputes, unauthorized use of the account, and the prohibition against unsolicited issuance, which apply only to "credit cards," do not apply to these checks. See § 226.12. However, other protections do apply to such checks. See § 226.13. In the December 2004 ANPR, the Board solicited comment as to whether it should extend TILA's protections for credit cards to other extensions on credit card accounts, in particular checks that access credit card accounts. Q45. The Board also asked whether the industry is developing open-end credit plans that would allow consumers to conduct transactions using only account numbers and that do not involve the issuance of physical devices traditionally considered to be credit cards. Q44.

In response to the December 2004 ANPR, several consumer commenters urged the Board to expand the definition of "credit card" to include checks that access a credit card account, in particular to address the risk of increased fraud and heightened identity theft stemming from the unrestricted issuance of such checks. Specifically, these commenters cited concerns that these checks could be sent to a consumer at any time without the consumer's request. Alternatively, some consumer commenters suggested that if these checks continued to be issued on an unsolicited basis, consumers should at least be able to opt out from receiving them. In addition, one consumer group commented that the Board could address non-physical credit cards by clarifying that the term "device" as it appears in the definition of "credit card" can include any physical object or a method or process.

Industry commenters opposed expanding the definition of "credit card" to cover checks that access credit card accounts, for various reasons. In general, industry commenters stated that they were aware of few complaints regarding such checks, and that in their experience, most consumers find the checks useful and convenient, as demonstrated by their frequent use. In addressing unsolicited issuance concerns specifically, industry commenters noted that upon a consumer's request, most issuers will discontinue sending checks that access a credit card account.

Industry commenters also stated that it was unnecessary to extend the unauthorized use protections to convenience checks because convenience check transactions are generally subject to the Uniform Commercial Code (UCC) provisions governing checks, and thus a consumer generally would not have any liability for a forged check, provided the consumer complies with certain timing requirements. Industry commenters also opposed applying the merchant dispute provisions (in § 226.12) to checks that access a credit card account, stating that these checks are not processed through the payment card associations' networks. Because card issuers may have no connection to or relationship with merchants that accept these checks, industry commenters stated that issuers do not have the ability to charge back to that merchant transactions conducted with these checks. Accordingly, industry commenters believed that the consumer was in the best position to contact the merchant in the event of a dispute involving a transaction using one of these checks.

In the proposal, the definition of "credit card" would remain unchanged. The Board believes it may be unnecessary to address unauthorized use concerns by treating checks that access credit card accounts as credit cards, to the extent existing law or agreements provide protections to these transactions. Moreover, under Regulation Z, a consumer is currently able to assert billing error claims for transactions involving checks that access a credit card account because the billing error provisions in § 226.13 apply to any extension of credit under an open-end plan, and are not limited to credit cards. The Board also does not believe that it is necessary to require issuers to provide consumers with the ability to opt out of receiving checks that access credit card accounts. The Board understands that in many instances, issuers will honor consumer requests to opt out of receiving such checks, and the Board encourages creditors to continue the practice. In addition, as noted above, consumers would be able to assert a billing error claim with respect to any unauthorized transactions involving such checks and is not liable for unauthorized transactions, as provided for under § 226.13.

Plans in which no physical device is issued. The proposal does not address circumstances where a consumer may conduct a transaction on an open-end plan that does not have a physical device. The Board had solicited comment on such plans because it has received anecdotal information about limited cases in which consumers obtained credit by providing an account number (for example, to obtain food and services at a resort) and where a physical device was not issued to the consumer. Industry commenters stated that, in general, they were unaware of any plans to provide open-end accounts that did not involve the issuance of a card or other physical device. In particular, industry commenters noted that creditors will continue to issue physical devices because transactions where a card or other physical device is present are generally far more secure and less likely to involve fraud compared to those in which only the account number, along with other information, is used to verify the identity of the user. Moreover, industry commenters noted that consumers still need a tangible device bearing account information that they can easily carry with them. As a result, industry commenters generally believed that issuers would be unlikely to abandon the issuance of a physical card or device.

The Board believes that it is not necessary at this time to address this issue, but it will continue to monitor developments in the marketplace. Of course, to the extent a creditor has issued a device that meets the definition of a "credit card" for an account, transactions on that account are subject to the provisions that apply to transactions involving the use of a "credit card," even if the particular transaction itself is not conducted using the device (for example, in the case of phone or Internet transactions).

Coupon books. As noted above, the definition of "credit card" under both TILA and Regulation Z includes a reference to a "coupon book." Neither the statute nor the regulation provides any guidance on the types of devices that would constitute a "coupon book" so as to qualify as a "credit card" under the definition. Comment 2(a)(15)-1, as discussed above, states that checks and similar instruments that can be used only once to obtain a single credit extension are not "credit cards," and, logically such instruments, even if issued in a separate booklet or in conjunction with a periodic statement, also would not be considered to be coupon books. Thus, as the Board is not aware of devices existing today that would qualify as a coupon book under the statute and regulation, the Board is proposing to delete the reference to such devices in the definition of "credit card" as obsolete. Comment is requested as to whether removal of the reference to "coupon book" in § 226.2(a)(15) would help clarify the definition of "credit card" without inadvertently limiting the availability of Regulation Z protections.

Charge cards. Comment 2(a)(15)-3 discusses charge cards and identifies provisions in Regulation Z in which a charge card is distinguished from a credit card. As discussed in detail in the section-by-section analysis to § 226.7(b)(11) and § 226.7(b)(12), the new late payment and minimum payment disclosure requirements contained in the Bankruptcy Act do not apply to charge card issuers. Thus, comment 2(a)(15)-3 is updated to reflect those changes.

**<u>2(a)(17) Creditor</u>**

For reasons explained in the section-by-section analysis to § 226.3, the Board is proposing to exempt from TILA coverage credit extended under employee-sponsored retirement plans. Comment 2(a)(17)(i)-8, which provides guidance on whether such a plan is a creditor for purposes of TILA, would be deleted. The guidance would no longer be necessary because loans granted under such plans would be exempt from TILA and, as such, the definition of "creditor" would not need to be clarified.

In addition, the substance of footnote 3 would be moved to a new § 226.2(a)(17)(v), and references revised, accordingly. The dates used to illustrate numerical tests for determining whether a creditor "regularly" extends consumer credit are updated in comments 2(a)(17)-3 through -6.

**<u>2(a)(20) Open-end Credit</u>**

Under TILA Section 103(i), as implemented by § 226.2(a)(20) of Regulation Z, "open-end credit" is consumer credit extended by a creditor under a plan in which (1) the creditor reasonably contemplates repeated transactions, (2) the creditor may impose a finance charge from time to time on an outstanding unpaid balance, and (3) the amount of credit that may be extended to the consumer during the term of the plan, up to any limit set by the creditor, generally is made available to the extent that any outstanding balance is repaid. Comment 2(a)(20)-1 reiterates that consumer credit must meet all three of these criteria to be open-end credit. Comment 2(a)(20)-5 currently states, with respect to replenishment of the credit line, that a creditor need not establish a specific credit limit for the line of credit and that the line need not always be replenished to its original amount.

<u>"Spurious" open-end credit</u>. The Board has received comments from time to time from state attorneys general and consumer groups voicing concern that the definition of open-end credit permits creditors to treat as open-end plans certain credit transactions that would be more properly characterized as closed-end credit. These commenters note that as a practical matter, such "spurious" open-end credit is unlikely to be used for repeated transactions and the credit line does not replenish to the extent that the consumer pays down his or her balance. Furthermore, these open-end plans may be established primarily to finance an infrequently purchased product or service, the credit limits for many of the creditor's customers may be close to the cost of that product or service, and the creditor may have no reasonable grounds for expecting that there will be repeated transactions by many of its customers. When open-end disclosures are given for such products, the concern voiced by state attorneys general and consumer groups is that those disclosures fail to adequately disclose the period of time that it will take to repay the balance, the total of the payments that a consumer will be required to make (assuming in both cases that the consumer makes only the minimum required payments).

In an effort to address these concerns, in 1997 the Board proposed adding two sets of factors to the commentary, one set that creditors should consider when determining whether they "reasonably contemplate repeated transactions," and another set to provide guidance on whether a credit line is "reusable."[6] The Board received many comments from industry in response to this proposal, most of which criticized the factors on the grounds that they would result in excluding from the definition of "open-end credit" legitimate open-end credit products. In particular, commenters were concerned about the status of private label credit cards that offer an incentive to the consumer to make a large initial purchase. In response to these concerns, the two sets of factors were not adopted in the final commentary revisions.

As discussed further in the section-by-section analysis to § 226.16, the Board proposes to address potential "spurious" open-end credit transactions through improved advertising disclosures. The Board believes this to be a more targeted and effective approach than revising the definition of open-end credit. One of the major problems with "spurious" open-end credit highlighted by commenters is that creditors advertise a low minimum monthly payment which can mislead consumers, who may not be aware of the total amount of payments they would be required to make, or the term over which they would be obligated to make those payments. As discussed below in the section-by-section analysis to § 226.16(b), the proposed rule would require a creditor that states a minimum monthly payment in an advertisement also to state the term that it will take to repay the debt at that minimum payment level, as well as the total amount of the payments. The proposed rule would require that disclosure of the term and total amount of payments be equally prominent to the advertisement of the minimum payment. The Board believes that disclosure of the term and total of payments in advertisements will help to improve consumer understanding about the cost of credit products for which a low monthly payment is advertised, addressing one of the major concerns regarding "spurious" open-end credit.

<u>"Open-end" plans comprised of closed-end features</u>. The Board also is concerned that, under current guidance in the commentary, some credit products are treated as open-end plans, with open-end disclosures given to consumers, when such products would more appropriately be treated as closed-end transactions. Closed-end disclosures are more appropriate than open-end disclosures when the credit being extended is individual loans that are individually approved and underwritten. The Board is particularly concerned about certain credit plans, where each individual credit transaction is separately evaluated.

For example, under certain so-called multifeatured open-end plans, creditors may offer loans to be used for the purchase of an automobile. These automobile loan

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[6] The factors that were proposed regarding the "repeated transactions" portion of the definition were: (1) whether the product is something that consumers would most likely not purchase in multiples, (2) whether the line of credit is established for the purpose of purchasing a designated item, (3) the amount of the initial purchase relative to the credit limit, (4) the extent to which the creditor reasonably solicits customers to make additional purchases, and (5) whether the creditor has information on consumers with the credit line showing that they have made repeat purchases. The proposed revisions also would have provided that a line of credit generally is not self-replenishing if the initial line of credit is less than, or not much more than, the amount of the item purchased to open the credit line (or the minimum monthly payments are so low that the credit line is not reusable for an extended period of time). <u>See</u> 62 FR 64,769, December 9, 1997.

transactions are approved and underwritten separately from other credit made available on the plan. (In addition, the consumer typically has no right to borrow additional amounts on the automobile loan "feature" as the loan is repaid.) If the consumer repays the entire automobile loan, he or she may have no right to take further advances on that "feature," and must separately reapply if he or she wishes to obtain another automobile loan, or use that aspect of the plan for similar purchases. Typically, while the consumer may be able to obtain additional advances under the plan as a whole, the creditor separately evaluates each request.

Currently, some creditors may be treating such plans as open-end credit, in light of several sections in the current commentary. Current comment 2(a)(20)-2 provides that if a program as a whole meets the definition of open-end credit, such a program may be considered a single multifeatured plan, notwithstanding the fact that certain features might be used infrequently. In addition, current comment 2(a)(20)-3 indicates that, for a multifeatured open-end plan, a creditor need not believe a consumer will reuse a particular feature of the plan. Also, current comment 2(a)(20)-5 indicates that a creditor may verify credit information such as a consumer's continued income and employment status or information for security purposes.

The Board believes that in certain circumstances treating such credit as open-end is inappropriate under Regulation Z, and accordingly proposes a number of revisions to § 226.2(a)(20) and the accompanying commentary. Closed-end disclosures are more appropriate than open-end disclosures unless the consumer's credit line generally replenishes to the extent that he or she repays outstanding balances so that the consumer may continue to borrow and take advances under the plan without having to obtain separate approval for each subsequent advance. Replenishment of the amount of credit available to a consumer in good standing without the need for separate underwriting or approval of each advance distinguishes open-end credit from a series of advances made pursuant to separate closed-end loan commitments, such as the automobile loan described above. For example, if a consumer makes two payments of $500 that reduce the outstanding principal balance on the line of credit, the consumer generally should be able to obtain an additional $1,000 of credit under the open-end plan without having a creditor separately underwriting or evaluating whether the consumer can borrow the $1,000.

The Board proposes to revise comment 2(a)(20)-2 to clarify that while a consumer's account may contain different sub-accounts, each with different minimum payment or other payment options, each sub-account must meet the self-replenishing criterion. In particular, proposed comment 2(a)(20)-2 would provide that repayments of an advance for any sub-account must generally replenish a single credit line for that sub-account so that the consumer may continue to borrow and take advances under the plan to the extent that he or she repays outstanding balances without having to obtain separate approval for each subsequent advance.

Due to the concerns noted above regarding closed-end automobile loans being characterized as features of so-called open-end plans, the Board proposes to delete comment 2(a)(20)-3.ii.. While there may be circumstances under which it would be more reasonable for a financial institution to make advances from an open-end line of credit for the purchase of an automobile than for an automobile dealer to sell a car under an open-end plan, the Board believes that the current example places inappropriate emphasis on the identity of the creditor rather than the type of credit being extended by that creditor.

TILA Section 103(i) provides that a plan can be an open-end credit plan even if the creditor verifies credit information from time to time. 15 U.S.C. 1602(i). The Board believes this provision is not intended to permit a creditor to separately underwrite each advance made to a consumer under an open-end plan or account. Such a process could result in closed-end credit being deemed open-end credit. The Board proposes to clarify in comment 2(a)(20)-5 that in general, a credit line is self-replenishing if a consumer can obtain further advances or funds without being required to separately apply for those additional advances, and without undergoing a separate review by the creditor of that consumer's credit information, in order to obtain approval for each such additional advance.

Notwithstanding this proposed change, a creditor could verify credit information to ensure that the consumer's creditworthiness has not deteriorated (and could revise the consumer's credit limit or account terms accordingly). However, to perform such an inquiry for each specific credit request would go beyond verification and would more closely resemble underwriting of closed-end credit. The Board recognizes that a creditor may need to review, and as appropriate, decrease the amount of credit available to a consumer from time to time to address safety and soundness and other concerns. Such a review would not be affected by the proposed changes, as explained in proposed comment 2(a)(20)-5.

These revisions are not intended to impact home-equity lines of credit (HELOCs), which may have a fixed draw period (during which time a consumer may continue to take advances to the extent that he or she repays the outstanding balance) followed by a repayment period where the consumer may no longer draw against the line, as closed-end credit. The Board seeks comment regarding the proposed rule's impact on HELOCs.

Comment 2(a)(20)-5.ii. currently notes that a creditor may reduce a credit limit or refuse to extend new credit due to changes in the economy, the creditor's financial condition, or the consumer's creditworthiness. The Board's proposal would delete the reference to changes in the economy to simplify this provision.

The Board also proposes a technical update to comment 2(a)(20)-4 to delete a reference to "china club plans," which may no longer be very common. No substantive change is intended.

**2(a)(24) Residential Mortgage Transaction**

Comment 2(a)(24)-1, which identifies key provisions affected by the term "residential mortgage transaction," is revised to include a reference to § 226.32, correcting an inadvertent omission.

**Section 226.3 Exempt Transactions**

Section 226.3 implements TILA Section 104 and provides exemptions for certain classes of transactions specified in the statute. 15 U.S.C. 1603.

The Board proposes a number of substantive and technical revisions to § 226.3 as described below. The substance of footnote 4 is moved to the commentary. See comment 3-1.

**3(a) Business, Commercial, Agricultural, or Organizational Credit**

Section 226.3(a) provides, in part, that the regulation does not apply to extensions of credit primarily for business, commercial or agricultural purposes. The Board received no comments regarding this exemption in regard to the December 2004 ANPR. Questions have arisen from time to time, however, regarding whether transactions made for business purposes on a consumer purpose credit card are exempt from TILA. The Board seeks to provide clarification regarding this question. The determination as to whether a credit card account is primarily for consumer purposes or business purposes is best made when the account is opened, rather than on a transaction-by-transaction basis, and thus the Board is proposing to add a new comment 3(a)-2 to clarify that transactions made for business purposes on a consumer-purpose credit card are covered by TILA (and, conversely, that purchases made for consumer purposes on a business-purpose credit card are exempt from TILA). Other sections of the commentary regarding § 226.3(a) would be renumbered accordingly. A new comment 3(a)-7 would provide guidance on card renewals, consistent with proposed comment 3(a)-2.

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

Section 226.3(b) exempts from Regulation Z extensions of credit not secured by real property or a dwelling, in which the amount financed exceeds $25,000 or in which there is an express written commitment to extend credit in excess of $25,000. The $25,000 threshold in § 226.3(b) is the same as the statutory threshold set in TILA Section 104(3). 15 U.S.C. 1603(3).

In the December 2004 ANPR, the Board solicited comment as to whether the rules implementing TILA Section 104 needed to be updated. Q58. The Board received several comments regarding the $25,000 threshold. One consumer group noted that the $25,000 figure is outdated due to inflation and should be increased. One bank noted that the threshold remains appropriate for unsecured credit but suggested that the Board might consider at a later stage of the Regulation Z review whether the $25,000 figure should be raised for secured credit, such as automobile loans. The Board agrees that the § 226.3(b) threshold would be more appropriately considered in connection with its planned review of the closed-end credit provisions of Regulation Z and is not proposing to take any action at the present time. In delaying consideration of the $25,000 threshold to the closed-end Regulation Z review, the Board expresses no view on whether the $25,000 threshold is appropriate for open-end (not home-secured) credit. Rather, the Board proposes to review the threshold for all credit covered by TILA at the same time.

**3(c) Public Utility Credit**

Section 226.3(c) exempts from Regulation Z extensions of credit involving public utility services provided through pipe, wire, other connected facilities, or radio or similar transmission, if the charges for service, delayed payment, or any discounts for prompt payment are filed with or regulated by any government unit. 15 U.S.C. 1603(4).

The Board received no comments on the December 2004 ANPR regarding the applicability and scope of § 226.3(c). However, the Board has received inquiries from time to time regarding the applicability of Regulation Z to service plans for cellular telephones. In addition, in light of the deregulation in recent years by some states of utilities such as gas and electric services, the Board believes that it may be appropriate to reconsider the scope of the public utility credit exemption more generally. The Board also notes that due to technological advances, there may be additional types of services, such as certain Internet services, for which exemption from Regulation Z may be appropriate. The Board is not proposing to take any action at the present time, however, because these issues would be better considered in the context of the Board's upcoming rulemaking regarding the closed-end credit provisions of Regulation Z.

**3(g) Employer-Sponsored Retirement Plans**

The Board has received questions from time to time regarding the applicability of TILA to loans taken against employer-sponsored retirement plans. Pursuant to TILA Section 104(5), the Board has the authority to exempt transactions for which it determines that coverage is not necessary in order to carry out the purposes of TILA. 15 U.S.C. 1603(5). The Board also has the authority pursuant to TILA Section 105(a) to provide adjustments and exceptions for any class of transactions, as in the judgment of the Board are necessary or proper to effectuate the purposes of TILA. 15 U.S.C. 1604(a). The Board proposes to add to the regulation a new § 226.3(g), which would exempt loans taken by employees against their employer-sponsored retirement plans qualified under Section 401(a) of the Internal Revenue Code and tax-sheltered annuities under Section 403(b) of the Internal Revenue Code, provided that the extension of credit is comprised of fully-vested funds from such participant's account and is made in compliance with the Internal Revenue Code. 26 U.S.C. 1 et seq.; 26 U.S.C. 401(a); 26 U.S.C. 403(b).

The Board believes that an exemption for loans taken against funds invested in such types of employer-sponsored retirement plans is appropriate for the following reasons. The consumer's interest and principal payments on such a loan are reinvested in the consumer's own account, and there is no third-party creditor imposing finance charges on the consumer. Also, TILA disclosures would be of very limited, if any, value. The costs of a loan taken against assets invested in a 401(k) plan, for example, are not comparable to the costs of a third party loan product, because a consumer pays the interest on a 401(k) loan to himself or herself rather than to a third party. Moreover, plan administration fees must be disclosed under Department of Labor regulations. See 29 CFR part 2520.1023(1).

**Family Trusts**

The Board also has from time to time received inquiries regarding TILA coverage of family trusts created for estate planning purposes. Because most of these questions pertain to real-estate secured loans, the applicability of the exemptions in § 226.3 to these types of estate planning arrangements would be better considered in the context of the Board's upcoming closed-end Regulation Z review.

**Section 226.4 Finance Charge**

Various provisions of TILA and Regulation Z specify how and when the cost of consumer credit as a dollar amount, the "finance charge," is to be disclosed. The rules for determining which charges make up the finance charge are set forth in TILA Section 106 and Regulation Z § 226.4. 15 U.S.C. 1605. Some rules apply only to open-end credit and others apply only to closed-end credit, while some apply to both. With limited exceptions discussed below, the Board is not proposing to change § 226.4 for either closed-end credit or open-end credit.

The Board is aware of longstanding criticisms that the definition of the "finance charge" in § 226.4, as interpreted in the regulation and the related commentary, is too narrow, too broad, or too vague. In a 1998 report to Congress, the Board discussed these concerns, and proposed solutions, in the context of closed-end mortgage loans.[7] In this proposal, the Board addresses concerns about the definition of the "finance charge" in the context of open-end (not home-secured) plans through changes to § 226.5, § 226.6, and § 226.7 to simplify disclosure of charges on such plans. The Board is not proposing to address these concerns through changes to § 226.4, with limited exceptions. The Board proposes to revise § 226.4 and related commentary to address (1) transaction charges imposed by credit card issuers, such as charges for obtaining cash advances from ATMs and for making purchases in foreign currencies, and (2) charges for credit insurance, debt cancellation coverage, and debt suspension coverage.

**4(a) Definition**

Under the definition of "finance charge" in TILA Section 106 and Regulation Z § 226.4(a), a charge specific to a credit transaction is ordinarily a finance charge. 15 U.S.C. 1605. See also § 226.4(b)(2). However, also under Section 106 and § 226.4(a), the finance charge does not include any charge of a type payable in a "comparable cash transaction." Under the staff commentary to § 226.4(a), in determining whether a charge associated with a credit transaction is a finance charge, the creditor should compare the credit transaction in question with a "similar" cash transaction, if one exists. See comment 4(a)-1. The commentary states a general principle for applying this rule in the case of credit that finances the sale of property or services: the creditor should compare charges with those that would be payable if the services or property were purchased using cash rather than a loan. Thus, for example, if an escrow agent charges

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[7] Board of Governors of the Federal Reserve System and Department of Housing and Urban Development, Joint Report to the Congress Concerning Reform to the Truth in Lending Act and the Real Estate Settlement Procedures Act, July 1998.

the same fee regardless of whether real estate is bought in cash or with a mortgage loan, then the agent's fee is not a finance charge.

In other cases, however, particularly in cases involving credit cards, determining which, if any, transaction is a "similar" or "comparable" cash transaction for purposes of § 226.4(a) can be difficult. For example, when consumers became able to take cash advances on credit card accounts using ATMs, a question arose as to whether a fee charged by a card issuer for the transaction was a finance charge if the issuer charged the same fee for using a debit card to withdraw cash from an asset account. The Board solicited comment on this question in 1983 and adopted staff comment 4(a)-4 in 1984. 48 FR 54,642; December 6, 1983 and 49 FR 40,560; October 17, 1984. That comment indicates that the fee is not a finance charge to the extent that it does not exceed the charge imposed by the card issuer on its cardholders for using the ATM to withdraw cash from a consumer asset account, such as a checking or savings account. Another comment indicates that the fee is an "other charge." See current comment 6(b)-1(vi). Accordingly, the fee must be disclosed at account opening and on the periodic statement, but it is not labeled as a "finance charge" nor included in the effective APR.

Since comment 4(a)-4 was adopted, questions have been raised about its scope and application. For example, the comment does not address whether it applies when an affiliate of the card issuer, but not the card issuer itself, issues a debit card. Even in the seemingly simple case where the credit card issuer itself issues a debit card, a variety of complexities arise. The issuer may assess an ATM fee for one kind of deposit account (for example, an account with a low minimum balance) but not for another. The comment does not indicate which account is the proper basis for comparison.

Questions have also been raised about whether disclosure of the charge pursuant to comments 4(a)-4 and 6(b)-1.iv. is meaningful to consumers. Under the comment, the disclosure a consumer receives after incurring a fee for taking a cash advance through an ATM depends on the structure of the institution that issued the credit card. If the credit card issuer does not provide asset accounts and is not affiliated with an institution that does, then it must disclose the charge as a finance charge. If the credit card issuer provides asset accounts and offers debit cards on those accounts, then, depending on the circumstances, the issuer must not disclose the charge as a finance charge. It is not clear that the distinction is meaningful to consumers.

Recently, a question has arisen about the proper disclosure of another kind of transaction fee imposed on credit cards. The question is whether fees that credit cardholders are assessed for making purchases in a foreign currency or outside the United States – for example, when the cardholder travels abroad – are finance charges. The question has arisen in litigation between consumers and major card issuers.[8] Some card issuers have argued by analogy to comment 4(a)-4 that a foreign transaction fee is not a finance charge if the fee does not exceed the issuer's fee for using a debit card for the

[8] See Third Consolidated Amended Class Action Complaint at 47-48, In re Currency Conversion Fee Antitrust Litigation, MDL Docket No. 1409 (S.D.N.Y.). The court approved a settlement on a preliminary basis on November 8, 2006.

same purchase. Some card issuers disclose the foreign transaction fee as a finance charge and include it in the effective APR, but others do not.

The uncertainty about proper disclosure of charges for foreign transactions and for cash advances from ATMs reflects the inherent complexity of seeking to distinguish transactions that are "comparable cash transactions" to credit card transactions from transactions that are not. The Board believes that clearer guidance may result from a new and simpler approach that treats as a finance charge any fee charged by credit card issuers for transactions on their credit card plans. This guidance may be helpful to creditors in determining which charges must be included in the computation of the effective APR, if the Board retains the effective APR. <u>See</u> section-by-section analysis to § 226.7(b)(7). Such an approach would also provide more meaningful disclosures to consumers by assuring a consistent approach to the disclosure of transaction fees.

The current approach of providing guidance on a case-by-case (fee-by-fee) basis, such as for ATM fees, has not provided sufficient certainty for many creditors about how to disclose transaction charges on credit cards. Moreover, to the extent creditors have adopted different disclosure practices in the face of regulatory uncertainty, consumers may have had difficulty understanding the disclosures, since, for example, one creditor might disclose an ATM fee as a finance charge while another creditor may disclose the fee as an "other" charge. Thus, while the Board could adopt guidance specific to fees as they arise, such as the Board did in 1984 for the ATM fee and could do for the foreign transaction fee, it is not clear that fee-by-fee guidance is sufficient to both facilitate compliance by credit card issuers and promote understanding by consumers.

It is also not clear that an attempt to adopt general rules for distinguishing comparable transactions from non-comparable transactions, in the case of credit cards, would adequately facilitate compliance by credit card issuers and promote understanding by cardholders. One major difficulty in formulating such rules would be deciding whether to adopt the perspective of the card issuer or that of the cardholder. For example, a transaction on an asset account with a card issuer may be comparable to a credit card transaction from the perspective of the card issuer, but not from the perspective of a cardholder who does not have an asset account with the issuer. A rule based on the issuer's perspective may confuse consumers; it may not be reasonable to expect a consumer to understand that one transaction fee is a finance charge and the other is not because one card issuer issues a debit card and the other does not. Yet a rule based on the cardholder's perspective may not be practicable for the issuer to implement; the issuer may not be able to determine whether a particular consumer has an asset account with another institution and, if so, the amount of the fee charged on the account. As explained above in the context of the fee for cash advances from ATMs, even when a rule is based on the card issuer's perspective, the card issuer may have difficulty determining which asset account, precisely, is the relevant basis for comparison. The difficulty of determining which perspective to adopt increases in a case such as a fee for a purchase conducted in a foreign currency. From the perspective of the consumer, the debit card is not the only alternative to the credit card; the consumer may also pay in cash.

Thus, having considered alternative approaches, the Board is proposing to adopt a simple interpretive rule that any transaction fee on a credit card plan is a finance charge, regardless of whether the issuer in its capacity as a depository institution imposes the same or lesser charge on withdrawals of funds from an asset account such as a checking or savings account. This proposal would be implemented by removing staff comment 4(a)-4 and replacing it with a new comment of the same number reflecting this rule. The comment would give as examples of such finance charges a fee imposed by the issuer for foreign transactions and a fee imposed by the issuer for taking a cash advance at an ATM.[9] Such guidance would be consistent with TILA Section 106, 15 U.S.C. 1605, which gives the Board discretion to determine whether a given credit transaction has a comparable cash transaction within the meaning of the statute. This guidance would also facilitate compliance and promote consumer understanding. See TILA Section 105(a), 15 U.S.C. 1604(a).

The Board seeks comment on whether this new approach would facilitate compliance and improve consumer understanding without causing unintended consequences.

Comment 4(a)-1 provides examples of charges in comparable cash transactions that are not finance charges. Among the examples are 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 institution. The Board solicits comment on whether the example is still useful, or should be deleted as unnecessary or obsolete.

**4(b) Examples of Finance Charges**

Charges for credit insurance or debt cancellation or suspension coverage. Premiums or other charges for credit life, accident, health, or loss-of-income insurance are finance charges if the insurance or coverage is "written in connection with" a credit transaction. 15 U.S.C. 1605(b); § 226.4(b)(7). Creditors may exclude from the finance charge premiums for credit insurance if they disclose the cost of the insurance and the fact that the insurance is not required to obtain credit. In addition, the statute requires creditors to obtain an affirmative written indication of the consumer's desire to obtain the insurance, which, as implemented in § 226.4(d)(1)(iii), requires creditors to obtain the consumer's initials or signature. 15 U.S.C. 1605(b). In 1996, the Board expanded the scope of the rule to include plans involving charges or premiums for debt cancellation coverage. See § 226.4(b)(10), § 226.4(d)(3). See also 61 FR 49,237; September 19, 1996. Currently, however, insurance or coverage sold after consummation of a closed-end credit transaction or after the opening of an open-end plan and upon a consumer's request is considered not to be "written in connection with the credit transaction," and, therefore, a charge for such insurance or coverage is not a finance charge. See comment 4(b)(7) and (8)-2.

The Board is proposing a number of revisions to these rules:

[9] The proposed change to comment 4(a)-4 would not affect disclosure of ATM fees assessed by institutions other than the credit card issuer. See proposed § 226.6(b)(1)(ii)(A).

(1) The same rules that apply to debt cancellation coverage would be applied explicitly to debt suspension coverage. However, to exclude the cost of debt suspension coverage from the finance charge, creditors would be required to inform consumers, as applicable, that the obligation to pay loan principal and interest is only suspended, and that interest will continue to accrue during the period of suspension. These proposed revisions would apply to all open-end plans and closed-end credit transactions.

(2) Creditors could exclude from the finance charge the cost of debt cancellation and suspension coverage for events beyond those permitted today, namely, life, accident, health, or loss-of-income. This proposed revision would also apply to all open-end plans and closed-end credit transactions.

(3) The meaning of insurance or coverage "written in connection with" an open-end plan would be expanded to cover sales made throughout the life of an open-end (not home-secured) plans. Under the proposal, for example, consumers solicited for the purchase of optional insurance or debt cancellation or suspension coverage for existing credit card accounts would receive disclosures about the cost and optional nature of the product at the time of the consumer's request to purchase the insurance or coverage. Home-equity lines of credit (HELOCs) subject to § 226.5b and closed-end transactions would not be affected by this proposed revision.

(4) For telephone sales, creditors offering open-end (not home-secured) plans would be provided with flexibility in evidencing consumers' requests for optional insurance or debt cancellation or suspension coverage, consistent with rules published by federal banking agencies to implement Section 305 of the Gramm-Leach-Bliley Act regarding the sale of insurance products by depository institutions and guidance published by the Office of the Comptroller of the Currency (OCC) regarding the sale of debt cancellation and suspension products. See 12 CFR part 208.81 et seq. regarding insurance sales; 12 CFR part 37 regarding debt cancellation and debt suspension products. For telephone sales, creditors could provide disclosures orally, and consumers could request the insurance or coverage orally, if the creditor maintains evidence of compliance with the requirements, and mails written information within 3 days after the sale. HELOCs subject to § 226.5b and closed-end transactions would not be affected by this proposed revision.

All of these products serve similar functions but some are considered insurance under state law and others are not. Taken together, the proposed revisions would provide consistency in how creditors deliver, and consumers receive, information about the cost and optional nature of similar products.

**4(b)(7) and (8) Insurance Written in Connection with Credit Transaction**

Premiums or other charges for insurance for credit life, accident, health, or loss-of-income, loss of or damage to property or against liability arising out of the ownership or use of property are finance charges if the insurance or coverage is written in connection with a credit transaction. 15 U.S.C. 1605(b) and (c); § 226.4(b)(7) and (8). Comment 4(b)(7) and (8)-2 provides that insurance is not written in connection with a credit transaction if the insurance is sold after consummation on a closed-end transaction or after an open-end plan is opened and the consumer requests the insurance. The Board believes this approach remains sound for closed-end transactions, which typically consist of a single transaction with a single advance of funds. Consumers with open-end plans, however, retain the ability to obtain advances of funds long after account opening, so long as they pay down the principal balance. That is, a consumer can engage in credit transactions throughout the life of a plan.

Accordingly, under proposed revisions to comment 4(b)(7) and (8)-2, insurance purchased after an open-end (not home-secured) plan was opened would be considered to be written "in connection with a credit transaction." Proposed new comment 4(b)(10)-2 would give the same treatment to purchases of debt cancellation or suspension coverage. As proposed, therefore, purchases of voluntary insurance or coverage after account opening would trigger disclosure and consent requirements. For purchases by telephone, creditors would be permitted to provide disclosures and obtain consent orally, so long as they meet requirements intended to ensure the purchase is voluntary. See proposed § 226.4(d)(4).

**4(b)(9) Discounts**

Comment 4(b)(9)-2, which addresses cash discounts to induce consumers to use cash or other payment means instead of credit cards or open-end plans is revised for clarity. No substantive change is intended.

**4(b)(10) Debt Cancellation and Debt Suspension Fees**

As discussed above, premiums or other charges for credit life, accident, health, or loss-of-income insurance are finance charges if the insurance or coverage is written in connection with a credit transaction. In 1996, the Board amended § 226.4 to make clear that the term "finance charge" includes charges or premiums paid for debt cancellation coverage. See § 226.4(b)(10). Although debt cancellation fees meet the definition of "finance charge," they may be excluded from the finance charge on the same conditions as credit insurance premiums. See § 226.4(d)(3).

Recent years have seen two developments in the market for coverage of this type. First, creditors have been selling a related, but different, product called debt suspension. Debt suspension is essentially the creditor's agreement to suspend, on the occurrence of a specified event, the consumer's obligation to make the minimum payment(s) that would otherwise be due. During the suspension period, interest may continue to accrue or it may be suspended as well, depending on the plan. The borrower may be prohibited from using the credit plan during the suspension period. In a second development, creditors have been selling debt suspension coverage for events other than loss of life, health, or income, such as a wedding, a divorce, the birth of child, a medical emergency, and military deployment.

The Board is proposing to revise § 226.4(b)(10) to make it explicit that charges for debt suspension coverage are finance charges. In the proposed commentary, debt suspension coverage would be defined as coverage that suspends the consumer's obligation to make one or more payments on the date(s) otherwise required by the credit agreement, when a specified event occurs. The commentary would clarify that the term debt suspension coverage as used in § 226.4(b)(10) does not include "skip payment" arrangements in which the triggering event is the borrower's unilateral election to defer repayment, or the bank's unilateral decision to allow a deferral of payment. (A skip payment fee, although a finance charge, would not be factored into the effective APR under the proposal. See proposed § 226.14(e).) These revisions would apply to closed-end as well as open-end credit transactions. It appears appropriate to consider charges for debt suspension products to be finance charges, because these products operate in a similar manner to debt cancellation, and re-allocate the risk of non-payment between the borrower and the creditor. The conditions under which debt cancellation and debt suspension charges may be excluded from the finance charge are discussed under § 226.4(d)(3), below.

**4(c) Charges Excluded from the Finance Charge**

**4(c)(1)**

Section 226.4(c)(1) excludes from the finance charge application fees charged to all applicants for credit, whether or not credit is actually extended. Application fees are charged for both closed-end and open-end credit transactions, and represent an additional cost to consumers who obtain credit. Because application fees are more prevalent for home-secured credit, the Board will consider whether to revise § 226.4(c)(1) in its upcoming review of rules for home-secured credit.

As discussed below in the section-by-section analysis to § 226.6, the Board proposes to require for open-end (not home-secured) plans, the disclosure of charges imposed as part of the plan, which include fees that must be paid to receive access to the plan, without regard to whether the fees are or are not finance charges. Application fees charged to all applicants for credit, whether or not credit is actually extended, would be considered charges imposed as part of the plan, and would be included in the account-summary table given at account opening. See proposed § 226.6(b)(1)(i). This would provide useful information to consumers about the total cost of obtaining credit. The fee, if financed, would also be included among the fees required to be grouped on periodic statements. See proposed § 226.7(b)(6).

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

**4(d)(3) Voluntary Debt Cancellation or Debt Suspension Fees**

As explained under § 226.4(b)(10), debt cancellation fees and, as clarified in this proposal, debt suspension fees meet the definition of "finance charge." Under current § 226.4(d)(3), debt cancellation fees may be excluded from the finance charge on the same conditions as credit insurance premiums. These conditions are: the coverage is not required and this fact is disclosed in writing, and the consumer affirmatively indicates in writing a desire to obtain the coverage after written disclosure to the consumer of the cost. Debt cancellation coverage that may be excluded from the finance charge is limited to coverage that provides for cancellation of all or part of a debtor's liability (1) in case of accident or loss of life, health, or income; or (2) for amounts exceeding the value of collateral securing the debt (commonly referred to as "gap" coverage, frequently sold in connection with motor vehicle loans). See current § 226.4(d)(3)(ii).

To address the development of debt cancellation and debt suspension coverage discussed earlier, the OCC adopted, for national banks, substantive limitations and procedures for disclosure and affirmative election on the sale of such coverage. See 12 CFR part 37. Some states have also adopted regulations that address these products, or incorporate the OCC regulations under parity laws.

The Board solicited comment in 2003 on whether and how to address disclosure of these kinds of coverage under TILA. 68 FR 68,793; December 10, 2003. About 30 commenters responded, the vast majority of them creditors or vendors. Several creditors and vendors urged the Board to expressly permit creditors to exclude from the finance charge fees for products that cover any event to which a creditor and borrower agree, not just the events listed in the regulation, and fees for agreements that suspend, rather than cancel, debt repayment. Some commenters disagreed. A major consumer group urged the Board to include even voluntary credit insurance premiums and debt cancellation fees in the finance charge. The Board deferred a decision on these issues until this review.

The December 2004 ANPR did not specifically seek comment again on these issues. Nonetheless, a coalition of companies that issue or administer debt cancellation and debt suspension agreements submitted two comments in response to the December 2004 ANPR reiterating the 2003 request by industry commenters that the Board modify § 226.4(d)(3) to cover any triggering event and explicitly recognize that debt suspension agreements are also covered by that provision. These companies also requested that the Board revise § 226.4(d)(3) to provide that the disclosures and consumer affirmative request required as conditions to excluding the fee from the finance charge may be provided orally.

Debt 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. The two types of coverage are, however, different in a key respect. One cancels debt, at least up to a certain agreed limit, while the other merely suspends the payment obligation while the debt remains constant or increases, depending on coverage terms.

The Board proposes 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 a product. The Board also proposes to add a disclosure, to be provided as applicable, that the obligation to pay loan principal and interest is only suspended, and that interest will continue to accrue during the period of suspension. These revisions would apply to closed-end as well as open-end credit transactions. Model Clauses and Samples are proposed at Appendix G-16(A) and G-16(B) and H-17(A) and H-17(B).

The same industry coalition has also requested that charges for debt cancellation or debt suspension coverage be excludable from the finance charge when the coverage applies to events other than the events covered by the product lines identified in current § 226.4(d)(3)(ii), namely, accident or loss of life, health, or income. The identification of those events in § 226.4(d)(3)(ii) is based on TILA Section 106(b), which addresses credit insurance for accident or loss of life or health. 15 U.S.C. 1605(b). That statutory provision reflects the regulation of credit insurance by the states, which may limit the types of insurance that insurers may sell. Many states, however, do not restrict debt cancellation or debt suspension coverage to a select few events, and regulations of the OCC expressly permit national banks to sell debt cancellation and debt suspension coverage for any event.

The Board proposes to continue to limit the exclusion permitted by § 226.4(d)(3) to charges for coverage for accident or loss of life, health, or income. The Board also proposes, however, to add comment 4(d)(3)-3 to clarify that, if debt cancellation or debt suspension coverage for two or more events is sold 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. This approach would recognize that debt cancellation and suspension coverage often are not limited by applicable law to the events allowed for insurance and it also would be consistent with the purpose of Section 106(b). 15 U.S.C. 1605(b).

The regulation provides guidance on how to disclose the cost of debt cancellation coverage. See proposed § 226.4(d)(3)(ii). The Board seeks comment on whether additional guidance is needed for debt suspension coverage, particularly for closed-end loans.

For the reasons discussed below, § 226.4(d)(4) would be added to provide flexibility in telephone sales to obtain consumers' requests for voluntary debt cancellation and debt suspension coverage on open-end (not home-secured) plans.

In a technical revision, the substance of footnotes 5 and 6 would be moved to the text.

**4(d)(4) Telephone Purchases**

As discussed above, TILA Section 106(b), 15 U.S.C. 1605(b), permits creditors to exclude from the finance charge premiums for credit insurance if, among other conditions, the creditor obtains a specific written indication of the consumer's desire to obtain the insurance. This requirement is implemented in § 226.4(d)(1) by requiring written initials or a signature. The Board expanded in 1996 the types of products covered by the exclusion to include debt cancellation agreements, and now proposes to extend the exclusion to debt suspension products. As mentioned, an industry coalition has requested that the Board permit the disclosures and affirmative consumer request, which are conditions to this exclusion, to be provided orally.

Congress has recognized the practice of telephone sales for the purchase of insurance products. 12 U.S.C. 1831x(c)(1)(E). Similarly, the OCC has issued telephone sales guidelines for national banks that sell debt cancellation and debt suspension coverage. 12 CFR part 37.6(c)(3), 37.7(b). Accordingly, the Board is proposing an exception to the requirement to obtain a written signature or initials for telephone purchases of credit insurance or debt cancellation and debt suspension coverage on an open-end (not home-secured) plan. Under new § 226.4(d)(4), for telephone purchases the creditor may make the disclosures orally and the consumer may affirmatively request the insurance or coverage orally, provided that the creditor (1) maintains reasonable procedures to provide the consumer with the oral disclosures and maintains evidence that demonstrates the consumer then affirmatively elected to purchase the insurance or coverage; and (2) mails the disclosures under § 226.4(d)(1) or § 226.4(d)(3) within three business days after the telephone purchase. Comment 4(d)(4)-1 would provide that a creditor does not satisfy the requirement to obtain an affirmative request if the creditor uses a script with leading questions or negative consent.

Requiring a consumer's written signature or initials is intended to evidence that the consumer is purchasing the product voluntarily; the proposal contains safeguards intended to insure that oral purchases are voluntary. Under the proposal, creditors must maintain tapes or other evidence that the consumer received required disclosures orally and affirmatively requested the product. Comment 4(d)(4)-1 indicates that a creditor does not satisfy the requirement to obtain an affirmative request if the creditor uses a script with leading questions or negative consent. In addition to oral disclosures, under the proposal consumers will receive written disclosures shortly after the transaction. The fee will also appear on the first monthly periodic statement after the purchase, and, as applicable, thereafter. Consumer testing conducted for the Board suggests that consumers review the transactions on their statements carefully. Moreover, the Board proposes to better highlight fees, including insurance and coverage fees, on statements. Consumers who are billed for insurance or coverage they did not purchase may dispute the charge as a billing error. These safeguards are expected to ensure that purchases of credit insurance or debt cancellation or suspension coverage by telephone are voluntary.

The Board proposes this approach 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 uniformed use of credit. 15 U.S.C. 1601(a), 1604(a). Section 105(f) authorizes the Board to exempt any class of transactions (with an exception not relevant here) 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). 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 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 it is appropriate to exempt, for open-end (not home-secured) plans, telephone sales of credit insurance or debt cancellation or debt suspension plans from the requirement to obtain a written signature or initials from the consumer. As noted above, the consumer would continue to be protected by a variety of safeguards to assure that the purchase is voluntary, including a requirement that the creditor maintain tapes or other evidence of the transaction, the receipt of written disclosures shortly after the transaction, and inclusion of fees on periodic statements, for which consumers may dispute billing errors. At the same time, the proposal should facilitate the convenience to both consumers and creditors of conducting transactions by telephone. The proposal, therefore, has the potential to better inform consumers and further the goals of consumer protection and the informed use of credit for open-end (not home-secured) credit. The Board welcomes comment on this matter.

**Section 226.5 General Disclosure Requirements**

Section 226.5 contains format and timing requirements for open-end credit disclosures. Under the current rules, a creditor must disclose a charge that is a "finance charge" or "other charge" before the account is opened, before the charge is added to the plan after account opening and before the charge is increased. These disclosures must be in writing. As discussed below, the proposal seeks to reform the rules governing disclosure of charges before they are imposed. Under the proposal: (1) all charges imposed as part of the plan would be disclosed before they are imposed; (2) specified charges would continue to be disclosed in writing at account opening, and before being increased or newly introduced; and (3) other charges imposed as part of the plan could be disclosed orally at any relevant time before the consumer becomes obligated to pay the charge. The proposed reform is intended to assure that all charges imposed as part of the plan are disclosed before they are imposed, simplify the rules for identifying such charges, and better match the timing and method of disclosure with reasonable industry practices and consumer expectations. The proposal responds to comments received on the December 2004 ANPR that criticize current rules (1) as unduly vague and inconsistent in identifying charges covered by TILA, and (2) as failing to recognize that some transactions on the plan between the consumer and the creditor are appropriately, or even necessarily, conducted by telephone.

**5(a) Form of Disclosures**

The Board is proposing substantive changes to § 226.5(a) and the associated commentary regarding the standard to provide "clear and conspicuous" disclosures. In addition, creditors would be required to use consistent terminology in all open-end TILA-required disclosures. In technical revisions, the Board proposes to rearrange certain provisions in § 226.5(a) for clarity.

**<u>5(a)(1) General</u>**

<u>Clear and conspicuous standard</u>. TILA Section 122(a) mandates that all TILA-required disclosures be made clearly and conspicuously. 15 U.S.C. 1632(a). The Board has implemented this requirement for open-end credit plans in § 226.5(a)(1). Under current comment 5(a)(1)-1, the Board has interpreted clear and conspicuous to mean that the disclosure must be in a reasonably understandable form. In most cases, this standard does not require that disclosures be segregated from other material or located in any particular place on the disclosure statement, nor that numerical amounts or percentages be in any particular type size.

However, the Board has previously determined that certain disclosures in Subpart B of Regulation Z are subject to a higher standard in meeting the clear and conspicuous requirement due to the importance of the disclosures and the context in which they are given. Specifically, disclosures in credit and charge card applications and solicitations subject to § 226.5a must be both in a reasonably understandable form and readily noticeable to the consumer. <u>See</u> current comment 5a(a)(2)-1, which the Board is proposing to amend as discussed below.

1. <u>Readily noticeable standard</u>. The Board is proposing to highlight certain information in a tabular format in the account-opening disclosures pursuant to § 226.6(b)(4); on checks that access a credit card account pursuant to § 226.9(b)(3); in change-in-terms notices pursuant to § 226.9(c)(2)(iii)(B); and in disclosures when a rate is increased due to delinquency, default or as a penalty pursuant to § 226.9(g)(3)(ii). As discussed in further detail in the section-by-section analysis to §§ 226.6(b), 226.9(b), 226.9(c), and 226.9(g), consumer testing conducted for the Board suggests that highlighting important information in a tabular format helps consumers locate the information disclosed in these tables much more easily. Because these disclosures would be highlighted in a tabular format similar to the table required with respect to credit card applications and solicitations under § 226.5a, the Board is proposing that these disclosures also be in a reasonably understandable form and readily noticeable to the consumer. The Board is proposing to amend comment 5(a)(1)-1 accordingly. The Board also is proposing to move the guidance on the meaning of "reasonably understandable form" to comment 5(a)(1)-2. Current comment 5(a)(1)-2, which provides guidance on what constitutes an "integrated document," is moved to comment 5(a)(1)-4.

The Board also proposes to add comment 5(a)(1)-3 to provide guidance on the meaning of the readily noticeable standard. Specifically, new comment 5(a)(1)-3 provides that to meet the readily noticeable standard, disclosures for credit card applications and solicitations under § 226.5a, highlighted account-opening disclosures under § 226.6(b)(4), highlighted disclosures on checks that access a credit card account under § 226.9(b)(3); highlighted change-in-terms disclosures under § 226.9(c)(2)(iii)(B), and highlighted disclosures when a rate is increased due to delinquency, default or as a penalty under § 226.9(g)(3)(ii) must be given in a minimum of 10-point font. The Board believes that with respect to these disclosures, special formatting requirements, such as a tabular format and font size requirements, are needed to highlight for consumers the importance and significance of the disclosures. The Board notes that this approach of requiring a minimum of 10-point font for certain disclosures is consistent with the approach taken recently by eight federal agencies (including the Board) in issuing a proposed model form that financial institutions may use to comply with the privacy notice requirements under Section 503 of the Gramm-Leach-Bliley Act. 15 U.S.C. 6803(e); 72 FR 14,940; Mar. 29, 2007. In the privacy proposal, the eight federal agencies indicate that financial institutions that use the privacy model form must use an easily readable type font; easily readable type font includes a minimum of 10-point font and sufficient spacing between the lines of type.

2. Disclosures subject to the clear and conspicuous standard. The Board has received questions on the types of communications that are subject to the clear and conspicuous standard. Thus, the Board proposes comment 5(a)(1)-5 to make clear that all required disclosures and other communications under Subpart B of Regulation Z are considered disclosures required to be clear and conspicuous. This would include, for example, the disclosure by a person other than the creditor of a finance charge imposed at the time of honoring a consumer's credit card under § 226.9(d) and the correction notice required to be sent to the consumer under § 226.13(e).

Oral disclosure. In order to give guidance about the meaning of clear and conspicuous for oral disclosures, the Board proposes to amend the guidance on what constitutes a "reasonably understandable form," in proposed comment 5(a)(1)-2. This amendment is based in part on the Federal Trade Commission's (FTC) guidance on oral disclosure in its publication Complying with the Telemarketing Sales Rule (available at the FTC's web site). Oral disclosures would be considered to be in a reasonably understandable form when they are given at a volume and speed sufficient for a consumer to hear and comprehend the disclosures.

**5(a)(1)(ii)**

Section 226.5(a)(1)(ii) provides that in general, disclosures for open-end plans must be provided in writing and in a retainable form.

Oral disclosures. The Board is proposing that certain charges may be disclosed after account opening. See proposed § 226.5(b)(1)(ii). The goal of this proposal is to better ensure that consumers receive disclosures at relevant times; some charges may not be relevant to a consumer at account opening but may become relevant later. The Board is also proposing to permit creditors to make the form of disclosure more relevant to consumers. A written form of disclosure has obvious merit at account opening, when a consumer must assimilate a lot of information that may influence major decisions by the consumer about how, or even whether, to use the account. During the life of the account, in contrast, a consumer will sometimes need to decide whether to purchase a single service from the creditor, a service that may not be central to the consumer's use of the account (for example, the service of providing documentary evidence of transactions). Moreover, during the life of the account, the consumer may become accustomed to purchasing such services by telephone. The consumer and the creditor may find it convenient to conduct the transaction by telephone, and will, accordingly, expect to receive a disclosure of the charge for the service during the same telephone call. For these reasons, the Board is proposing to permit creditors to disclose orally charges not specifically identified by the proposed regulation in § 226.6(b)(4) as critical to disclose in writing at account opening. Further, the Board proposes that creditors be provided with the same flexibility when the cost of such a charge changes or is newly introduced, as discussed in the section-by-section analysis to § 226.9(c). The proposal, set forth in§ 226.5(a)(1)(ii)(A), is intended to be consistent with consumers' expectations and with the business practices of card issuers.

Under the proposal, creditors may continue to comply with TILA by providing written disclosures at account-opening for all fees. In proposing to permit creditors to disclose certain costs orally for purposes of TILA, the Board anticipates that creditors will continue to identify fees in the account agreement for contract and other reasons, although the proposal would not require creditors to do so. For example, some creditors identify the types of fees that could be assessed on the account in the account agreement. The Board anticipates that such practices will continue.

Creditors are permitted to provide in electronic form any TILA disclosure 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 requests comment on whether there are circumstances in which creditors should be permitted to provide cost disclosures in electronic form to consumers who have not affirmatively consented to receive electronic disclosures for the account, such as when a consumer seeks to make a payment online, and the creditor imposes a fee for the service.

In technical revisions, the Board proposes to move to proposed § 226.5(a)(1)(ii)(A) the current exemption that disclosures required by § 226.9(d) need not be in writing. (This exemption currently is in footnote 7 under § 226.5(a)(1).) Section 226.9(d) requires disclosure when a finance charge is imposed by a person other than the card issuer at the time of a transaction.

In another technical revision, the substance of footnote 8, regarding disclosures that do not need to be in a retainable form the consumer may keep, is moved to proposed § 226.5(a)(1)(ii)(B).

Electronic communication. In April 2007, the Board issued for public comment a proposal on electronic communication which would withdraw portions of the interim final rules issued in 2001 and to implement certain provisions of the Bankruptcy Act ("2007 Electronic Disclosure Proposal"). See 72 FR 21,141; April 30, 2007. Proposed § 226.5(a)(1)(iii) and the proposal to delete current § 226.5(a)(5) is also proposed in the 2007 Electronic Disclosure Proposal. The language in proposed § 226.5(a)(1)(iii) clarifies that creditors may provide open-end disclosures to consumers in electronic form, subject to compliance with the consumer consent and other applicable provisions of the E-Sign Act. 15 U.S.C. 1001, et seq. The language also provides that the open-end disclosures required by §§ 226.5a, 226.5b, and 226.16 may be provided to the consumer in electronic form, under the circumstances set forth in those sections, without regard to the consumer consent or other provisions in the E-Sign Act.

**5(a)(2) Terminology**

Consistent terminology. Currently, disclosures given pursuant to §§ 226.5a(b), 226.6, and 226.7 must use consistent terminology. See current § 226.5a(a)(2)(iv), comment 5a(a)(2)-6, and comment 6-1. The Board proposes to expand this requirement more generally in new § 226.5(a)(2)(i) to include other disclosures required by the open-end provisions of the regulation (Subpart B), such as subsequent disclosures under § 226.9. A new comment 5(a)(2)-4 would clarify that terms do not need to be identical but must be close enough in meaning to enable the consumer to relate the disclosures to one another, which is consistent with current guidance in current comment 5a(a)(2)-6 and current comment 6-1. The Board believes that the use of consistent terminology should be applied to all open-end TILA-required disclosures to allow consumers to better identify the terms across all disclosures.

As discussed above, the Board is proposing to highlight certain information in a tabular format in the account-opening disclosures pursuant to § 226.6(b)(4); on checks that access a credit card account pursuant to § 226.9(b)(3); in change-in-terms notices pursuant to § 226.9(c)(2)(iii)(B); and in disclosures when a rate is increased due to delinquency, default or as a penalty pursuant to § 226.9(g)(3)(ii). These disclosures are meant to be highlighted in a tabular format similar to the table currently required with respect to credit card applications and solicitations under § 226.5a.

Currently, disclosures required for credit card applications and solicitation under § 226.5a must use the term "grace period" to describe the date by which or the period within which any credit extended for purchases may be repaid without incurring a finance charge. The Board proposes in new § 226.5(a)(2)(iii) to extend this requirement to use the term "grace period" to all references to such a term for the disclosures required to be in the form of a table as discussed above. In addition, proposed § 226.5(a)(2)(iii) provides that if disclosures are required to be presented in a tabular format, the term "penalty APR" shall be used to describe an increased rate that may result because of the occurrence of one or more specific events specified in the account agreement, such as a late payment or an extension of credit that exceeds the credit limit. For example, creditors would be required to provide information about penalty rates in the table given with credit card applications and solicitations under § 226.5a; in the summary table given at account opening under § 226.6(b)(4); if the penalty rate is changing, in the summary table given on or with the change-in-terms notice under § 226.9(c)(2)(iii)(B), or if a penalty rate is triggered, in the table given under § 226.9(g)(3)(ii).

Requiring card issuers to use a uniform term to describe the grace period and disallowing variants like "free-ride period" may improve consumers' understanding of the concept. Similarly, requiring card issuers to use a uniform term to describe the increased rate may improve consumers' understanding of the rate and when it applies. In the consumer testing conducted for the Board, many participants believed the term "Penalty APR" as opposed to "Default APR" or "Highest Possible APR" more clearly conveyed the increased rate. In testing the term “Default APR,” some participants said that the word “default” indicated to them that it would only apply when the account was closed due to delinquent payments. Some other participants said that the word “default” seemed like the “normal” rate, not something that occurs because a cardholder does something wrong. Some participants also were confused by the term “Highest Possible APR;” one participant, for example, assumed that this was the highest point to which variable rates could increase.

Moreover, if credit insurance or debt cancellation or debt suspension coverage is required as part of the plan and information about that coverage is required to be disclosed in a tabular format, proposed § 226.5(a)(2)(iii) requires that in describing the coverage, the term “required” shall be used and the program shall be identified by its name. For example, creditors would be required to provide information about the required coverage in the table given with credit card applications and solicitations under § 226.5a, in the summary table given at account opening under § 226.6(b)(4), and if certain information about the coverage is changing, in the summary table given in change-in-terms notice under § 226.9(c)(2)(iii)(B). In consumer testing conducted for the Board, the Board tested disclosing information about the required debt suspension coverage in the disclosure table given with a mock credit card solicitation. The Board found that describing the coverage by its name allowed participants to link disclosures that were provided in the table to other information about the coverage that was provided elsewhere in the solicitation materials given to the participants.

Furthermore, the Board proposes in § 226.5(a)(2)(iii) that if required to be disclosed in a tabular format, APRs may be described as “fixed” or any similar term only if that rate will remain in effect unconditionally until the expiration of a specified time period. If no time period is specified, then the term “fixed” or any similar term may not be used unless the rate remains in effect unconditionally until the plan is closed. As further discussed in the section-by-section analysis to proposed § 226.16(g) below, the Board is proposing these rules in order to avoid consumer confusion and the uninformed use of credit.

<u>Terms required to be more conspicuous than others</u>. TILA Section 122(a) requires that the terms “annual percentage rate” and “finance charge” be disclosed more conspicuously than other terms, data, or information. 15 U.S.C. 1632(a). The Board has implemented this provision in current § 226.5(a)(2)(iii) by requiring that the terms “finance charge” and “annual percentage rate,” when disclosed with a corresponding amount or percentage rate, be disclosed more conspicuously than any other required disclosure. Under current footnote 9, however, the terms do not need to be more conspicuous when used under §§ 226.5a, 226.7(d), 226.9(e), and 226.16.

In September 2006, the United States Government Accountability Office (GAO) issued a report that analyzed current credit card disclosures and recommended improvements to these disclosures (GAO Report on Credit Card Rates and Fees).[10] The

[10] United States Government Accountability Office, <u>Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers</u>, 06-929 (September 2006).

GAO criticized credit card disclosure documents that "unnecessarily emphasized specific terms." GAO Report on Credit Card Rates and Fees, p. 43. As an illustration of this point, the GAO reprinted a paragraph of text from a creditor's credit card disclosure documents where the phrase "periodic finance charge" was singled out for emphasis each time the phrase was used, even when such term was not disclosed with a corresponding amount or percentage rate. The usability consultant used by the GAO commented that this type of emphasis potentially required readers to work harder to understand the passage's message.

The Board agrees that overemphasis of these terms may make disclosures more difficult for consumers to read. In order to address this problem, the Board considered a proposal to prohibit the terms "finance charge" and "annual percentage rate" from being disclosed more conspicuously than other required disclosures except when the regulation so requires. However, this proposal could produce unintended consequences. For example, in a change-in-terms notice, the term "annual percentage rate" may appear as a heading, and thus be disclosed more conspicuously than other disclosures in the notice even though the term is not disclosed with a rate figure. It appears, therefore, that a rule prohibiting more conspicuous terms in certain cases would need to include detailed safe harbors or exceptions, which might make it unworkable. Therefore, the Board seeks comment on how to address this issue.

Furthermore, the Board is proposing to amend the regulation to expand the list of disclosures where the terms "finance charge" and "annual percentage rate" need not be more conspicuous to include the account-opening disclosures that would be highlighted under proposed § 226.6(b)(4), the disclosure of the effective APR under proposed § 226.7(b)(7), disclosures on checks that access a credit card account under proposed § 226.9(b)(3), the information on change-in-terms notices that would be highlighted under proposed § 226.9(c)(2)(iii)(B), the disclosures given when a rate is increased due to delinquency, default or as a penalty under proposed § 226.9(g)(3)(ii). Currently, the requirement that the terms "finance charge" and "annual percentage rate" be more conspicuous than other disclosures does not apply to disclosures highlighted in the tabular format used for credit card application and solicitations under § 226.5a. All of the disclosures discussed above must be highlighted in a tabular format similar to the table required for credit card applications and solicitations under § 226.5a. The Board believes the rule should be consistent across these disclosures. Moreover, the Board believes that the tabular format sufficiently highlights the disclosures, so that the "more conspicuous" rule is not needed. Finally, for organizational purposes, the Board proposes to consolidate current § 226.5(a)(2) and current footnote 9 into § 226.5(a)(2)(ii).

**5(a)(3) Specific Formats**

There are special rules regarding the specific format for disclosures under § 226.5a for credit and charge card applications and solicitations and § 226.5b for home-equity plans, as noted in current § 226.5(a)(3) and current § 226.5(a)(4), respectively. These rules would be consolidated in proposed § 226.5(a)(3), for clarity. In addition, as discussed below, the Board is proposing that certain account-opening disclosures, periodic statement disclosures and subsequent disclosures, such as change-in-terms disclosures, must be provided in specific formats under proposed § 226.6(b)(4); §§ 226.7(b)(6), (b)(7) and (b)(13); and §§ 226.9(b), (c) and (g) and these special format rules are noted in proposed § 226.5(a)(3).

**5(b) Time of Disclosures**

**5(b)(1) Account-opening Disclosures**

TILA Section 127(a) requires creditors to provide disclosures "before opening any account." 15 U.S.C. 1637(a). Section 226.5(b)(1) requires these disclosures (identified in § 226.6) to be furnished "before the first transaction is made under the plan," which is interpreted as "before the consumer becomes obligated on the plan." Comment 5(b)(1)-1. Also under the existing commentary, creditors may provide the disclosures required by § 226.6 after the first transaction only in limited circumstances. This guidance would be moved from the commentary to the regulation. See proposed § 226.5(b)(1)(iii)-(v). In addition, the Board is proposing revisions to the timing rules for disclosing certain costs imposed on an open-end (not home-secured) plan, and in connection with certain transactions conducted by telephone, as discussed below. Additional guidance is proposed on providing timely disclosures when the first transaction is a balance transfer. Technical revisions would change references from "initial" disclosures required by § 226.6 to "account-opening" disclosures, without any intended substantive change. In today's marketplace, there are few open-end products for which consumers receive the disclosures required under § 226.6 as their "initial" Truth in Lending disclosure. See §§ 226.5a, 226.5b, which require creditors to provide disclosures before consumers apply for a credit or charge card, or for a HELOC.

**5(b)(1)(i) General Rule**

Section 226.5(b)(1)(i), as renumbered, would state the general timing rule for furnishing account-opening disclosures. Specifically, creditors generally must provide the account-opening disclosures before the first transaction is made under the plan.

Balance transfers. Creditors commonly extend credit to consumers for the purpose of paying off consumers' existing credit balances with other creditors. Requests for these "balance transfers" are often part of an offer to open a credit card account, and consumers may request transfers as part of the application for the new account. Comment 5(b)(1)(i)-5, as renumbered, provides that creditors must provide account-opening disclosures before the balance transfer occurs.

The Board proposes to update this comment to reflect current business practices. Some creditors provide account-opening disclosures, including APRs, along with the balance transfer offer and account application, and these creditors would not be affected by the proposal. Other creditors offer balance transfers for which the APRs rate that may apply are disclosed as a range, depending on the consumer's creditworthiness. Consumers who respond to such an offer and apply for the transfer later receive account-opening disclosures, including the APR that will apply to the transferred balance. The proposed change would clarify that the creditor must provide disclosures sufficiently in advance of the transfer to allow the consumer to respond to the terms that will apply to the transfer, including to contact the creditor before the balance is transferred and decline the transfer.

Guidance in current comment 5(b)(1)-1 regarding account-opening disclosures provided with cash advance checks would be deleted as unnecessary.

Assessing fees on an account as acceptance of the account. Comment 5(b)(1)(i)-1(i), as renumbered, currently provides that if after receiving the account-opening disclosures, the consumer uses the account, pays a fee or negotiates a cash advance check, the creditor may consider the account not rejected. The comment would be amended to clarify that if the only activity on account is the creditors' assessment of fees (such as start-up fees), the consumer is not considered to have accepted the account until the consumer is provided with a billing statement and makes a payment. The clarification addresses concerns about some subprime card accounts that assess a large number of fees at account opening. Consumers who have not made purchases or otherwise obtained credit on the account would have an opportunity to review their account-opening disclosures and decide whether to reject the account and decline to pay the fees.

**5(b)(1)(ii) Charges Imposed as Part of an Open-end (not Home-secured) Plan**

Currently, charges imposed on an open-end plan that are a "finance charge" or an "other charge" must be disclosed before the first transaction. 15 U.S.C. 1637(a); current § 226.5(b)(1) and § 226.6(a) and (b). When a new service (and associated charge) is introduced or an existing charge is increased, creditors must provide a change-in-terms notice to update account-opening disclosures for all accountholders if the new charge is a finance charge or an other charge. See current § 226.9(c).

For the reasons discussed in the section-by-section analysis to § 226.6, the Board is proposing revisions to the rules identifying charges required to be disclosed under open-end (not home-secured) plans. The current rule requiring the disclosure of costs before the first transaction (in writing and in a retainable form) would continue to apply to specified costs. See proposed § 226.6(b)(4)(iii) for the charges, and § 226.9(c)(2) where such charges are changing or newly introduced. These costs are fees of which consumers should be aware before using the account such as annual or late payment fees, or fees that the creditor would not otherwise have an opportunity to disclose before the fee is triggered, such as a fee for using a cash advance check during the first billing cycle. The Board proposes to except charges imposed as part of an open-end (not home-secured) plan, other than those specified in proposed § 226.6(b)(4)(iii), from the requirement to disclose charges before the first transaction. Creditors would be permitted, at their option, to disclose those charges either before the first transaction or later, though before the cost is imposed. Examples of these charges would be fees to obtain documentary evidence or to expedite payments or delivery of a credit card. Creditors may, of course, continue to disclose any charge imposed as part of an open-end (not home-secured) plan at account opening (or when increased or newly introduced under § 226.9(c)(2)).

The charges covered by the proposed exception are triggered by events or transactions that may take place months, or even years, into the life of the account, when the consumer may not reasonably be expected to recall the amount of the charge from the account-opening disclosure, nor readily to find or obtain a copy of the account-opening disclosure or most recent change-in-term notice. Requiring such charges to be disclosed before account opening may not provide a meaningful benefit to consumers in the form of useful information or protection. Consumers would benefit, however, from a rule that permits creditors to disclose charges when consumers reasonably expect to receive the disclosures, and, thus, are most likely to notice and use the disclosures. The proposal assures that consumers continue to receive disclosure of charges imposed as part of the plan before they become obligated to pay them.

Examples of the charges to which the proposed exception would apply are fees to expedite payments or delivery of a card. Fees to expedite payments or card delivery are now excluded from TILA coverage. In a 2003 rulemaking concerning those two charges, the Board determined that neither was required to be disclosed under TILA. 68 FR 16,185; April 3, 2003. In the supplementary information accompanying the final rule, the Board noted some commenters' views that requiring a written disclosure of a charge for a service long before the consumer might consider purchasing the service did not provide the consumer material benefit. The Board also noted creditors' practice of disclosing the charge when the service is requested, and encouraged them to continue that practice. The Board believes that flexible disclosure of such charges may better serve TILA's purposes than the present exclusion of the charges from TILA's coverage altogether.

The Board also believes the proposed exception may facilitate compliance by creditors. As stated earlier, it can be challenging under the current rule to determine whether charges are a finance charge or an other charge or not covered by TILA, and thus whether advance notice is required if a charge is increased or newly introduced. The proposal reduces these uncertainties and risks. Under the proposal, the creditor could disclose a new or increased charge only to those consumers for whom it is relevant because they are considering at the time of disclosure whether to take the action that would trigger the charge. Moreover, the creditor would not have to determine whether a charge was a finance charge or other charge or not covered by TILA so long as the creditor disclosed the charge, orally or in writing, before the consumer became obligated to pay it, which creditors, in general, already do for business and other legal reasons.

The proposal would allow flexibility in the timing of certain cost disclosures. In proposing to permit creditors to disclose certain charges—orally or in writing—before the fee is imposed, the Board would require creditors to disclose a charge at a time consumers would likely notice the charge when the consumer decides whether to take the action that would trigger the charge, such as purchasing a service. Proposed comment 5(b)(1)(ii)-1 would provide an example that illustrates the standard.

The limited exception to TILA's requirement to disclose charges imposed as part of the plan before the first transaction is proposed pursuant to TILA Section 105(a).

Specifically, 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 the title, to prevent circumvention or evasion thereof, or to facilitate compliance therewith." 15 U.S.C. 1604(a). The class of transactions that would be affected is transactions on open-end plans not secured by a dwelling, though only with respect to certain charges. On the basis of the information currently available to the Board, a narrow adjustment and exception appears necessary and proper to effectuate TILA's purpose to assure meaningful disclosure and informed credit use, and to facilitate compliance.

**5(b)(1)(iii) Telephone Purchases**

Consumers who call a retailer to order goods by telephone commonly use an existing credit card account to finance the purchase. Some retailers, however, offer discounted purchase prices or promotional payment plans to consumer who finance the purchase by establishing a new open-end credit plan with the retailer. Under the current timing rule, retailers must provide TILA account-opening disclosures before the first transaction. This means retailers must delay the shipment of goods until a consumer has received the disclosures. Consumers who want goods shipped immediately may use another credit card to finance the purchase but they lose any discount or promotion that may be associated with opening a new plan. The Board proposes to provide additional flexibility to retailers and consumers for such transactions.

Under proposed § 226.5(b)(1)(iii), retailers that establish an open-end plan in connection with a telephone purchase of goods or services initiated by the consumer may provide account-opening disclosures as soon as reasonably practicable after the first transaction if the retailer (1) permits consumers to return any goods financed under the plan at the time the plan is opened and provides the consumer sufficient time to reject the plan and return the items free of cost after receiving the written disclosures required by § 226.6, and (2) informs the consumer about the return policy as a part of the offer to finance the purchase. Alternatively, the retailer may delay shipping the goods until after the account disclosures have been provided.

Proposed commentary provisions would clarify that creditors may provide disclosures with the goods, or for creditors that have separate distribution systems for credit documents and for goods, by establishing procedures reasonably designed to have the disclosures sent within the same time period after the purchase as when the goods will be sent. A return policy would be of sufficient duration if the consumer is likely to receive the disclosures and have sufficient time to decide about the financing plan. A return policy would include returns via the United States Postal Service for goods delivered by private couriers. The commentary would also clarify that retailers' policies regarding the return of merchandise need not provide a right to return goods if the consumer consumes or damages the goods. The proposal does not affect merchandise purchased after the plan was initially established, or purchased by other means such as a credit card issued by another creditor. See proposed comments 5(b)(1)(iii)-1.

**5(b)(2) Periodic Statements**

TILA Sections 127(b) and 163 provide the timing requirements for providing periodic statements for open-end credit accounts. 15 U.S.C. 1637(b) and 15 U.S.C. 1666b. The Board proposes to retain the existing regulation and commentary, with a few changes discussed below.

**5(b)(2)(i)**

TILA Section 127(b) establishes that creditors generally must send periodic statements at the end of billing cycles in which there is an outstanding balance or a finance charge is imposed. Section 226.5(b)(2)(i) provides for a number of exceptions to a creditor's duty to send periodic statements.

De minimis amounts. Creditors need not send periodic statements if an account balance (debit or credit) is $1 or less (and no finance charge is imposed). In the December 2004 ANPR, the Board requested comment on whether the de minimis amount should be adjusted. Q53. Few commented on this issue; there was little support for an adjustment. One major credit card issuer stated that the cost to reprogram systems would exceed the benefit. Thus, the Board proposes to retain the $1 threshold.

Uncollectible accounts. Creditors are not required to send periodic statements on accounts the creditor has deemed "uncollectible." That term is not defined. The Board understands that creditors typically send statements on past-due accounts until the account is charged-off for purposes of loan-loss provisions, which is typically after 180 days of nonpayment. The Board is not proposing regulatory or commentary provisions on when an account is deemed "uncollectible" but seeks comment on whether additional guidance would be helpful.

Instituting collection proceedings. Creditors need not send statements if "delinquency collection proceedings have been instituted." Over the years, the Board's staff has been asked for guidance on what actions a creditor must take to be covered by the exception. The Board proposes to add comment 5(b)(2)(i)-3 to clarify that a collection proceeding entails a filing of a court action or other adjudicatory process with a third party, and not merely assigning the debt to a debt collector.

Workout arrangements. Comment 5(b)(2)(i)-2 provides that creditors must continue to comply with all the rules for open-end credit, including sending a periodic statement, when credit privileges end, such as when a consumer stops taking draws and pays off the outstanding balance over time. Another comment provides that "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 comment 17(b)-2.

Over the years, the Board's staff has received requests for guidance on the effect of certain work-out arrangements for past-due open-end accounts. For example, a borrower with a delinquent credit card account may agree by telephone to a workout plan to reduce or extinguish the debt and the conversation is later memorialized in a writing.

The Board proposes to clarify that creditors entering into workout agreements for delinquent open-end plans without converting the debt to a closed-end transaction comply with the regulation if creditors continue to follow the regulations and procedures under Subpart B during the work-out period. The Board's proposal is intended to provide flexibility and reduce burden and uncertainty. The Board seeks comment on whether further guidance would be helpful, such as by establishing a safe harbor for when an open-end plan is deemed to be satisfied and replaced by a new closed-end obligation.

**5(b)(2)(ii)**

Credit card issuers commonly offer consumers a "grace period" or "free-ride period" during which consumers can avoid finance charges on purchases by paying the balance in full. TILA does not require creditors to provide a grace period, but if creditors provide one, TILA Section 163(a) requires them to send statements at least 14 days before the grace period ends. 15 U.S.C. 1666c(a). The rule is a "mailbox" rule; that is, the 14-day period runs from the date creditors mail their statements, not from the end of the statement period nor from the date consumers receive their statements.

The Board is aware of anecdotal evidence of consumers receiving statements relatively close to the payment due date, with little time remaining before the payment must be mailed to meet the due date. This may be due to the fact that at the end of a billing cycle, it may take several days for a consumer to receive a statement. In addition, for consumers who mail their payments, they may need to mail their payments several days before the due date to ensure that the payment is receive by the creditor by the due date. Although the Board notes that using the Internet to make payments is increasingly common, the Board requests comment on (1) whether it should recommend to Congress that the 14-day period be increased to a longer time period, so that consumer will have additional time to receive their statements and mail their payments to ensure that payments will be received by the due date, and (2) if so, what time period the Board should recommend to Congress.

**5(b)(2)(iii)**

In a technical revision, the substance of footnote 10 is moved to the regulatory text.

**5(c) through 5(e)**

Sections 226.5(c), (d), and (e) address, respectively: the basis of disclosures and the use of estimates; multiple creditors and multiple consumers; and the effect of subsequent events. The Board does not propose any changes to these provisions, except that the Board proposes to add new comment 5(d)-3, referencing the statutory provisions pertaining to charge cards with plans that allow access to an open-end credit plan maintained by a person other than the charge card issuer. TILA 127(c)(4)(D); 15 U.S.C. 1637(c)(4)(D. (See the section-by-section analysis to § 226.5a(f).)

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

TILA Section 127(c), implemented by § 226.5a, requires card issuers to provide certain cost disclosures on or with an application or solicitation to open a credit or charge card account.[11] 15 U.S.C. 1637(c). The format and content requirements differ for cost disclosures in card applications or solicitations, depending on whether the applications or solicitations are given through direct mail, provided electronically, provided orally, or made available to the general public such as in "take-one" applications and in catalogs or magazines. Disclosures in applications and solicitations provided by direct mail or electronically must be presented in a table. For oral applications and solicitations, certain cost disclosures must be provided orally, except that issuers in some cases are allowed to provide the disclosures later in a written form. Applications and solicitations made available to the general public, such as in a take-one application, must contain one of the following: (1) the same disclosures as for direct mail presented in a table; (2) a narrative description of how finance charges and other charges are assessed, or (3) a statement that costs are involved, along with a toll-free telephone number to call for further information.

The Board proposes a number of substantive and technical revisions to § 226.5a and the accompanying commentary, as described in more detail below. For example, the proposal contains a number of revisions to the format and content of application and solicitation disclosures, to make the disclosures more meaningful and easier to understand. Format changes would affect type size, placement of information within the table, use of cross-references to related information, and use of boldface type for certain key terms. Information concerning penalty APRs and the reasons they may be triggered would be more noticeable, and information would be added about how long penalty APRs may apply. The existing disclosures about how variable rates are determined would be shortened and simplified. Creditors that allocate payments to transferred balances that carry low rates would be required to disclose to consumers that they will pay interest on their (higher rate) purchases until (lower rate) transferred balances are paid in full. Creditors also would be required to include a reference to the Board's web site where additional information about shopping for credit cards is available.

To address concerns about subprime credit cards programs that have high fees with low credit limits, additional disclosures would be required if the fees or security deposits required to receive the card are 25 percent or more of the minimum credit limit that the consumer may receive. For example, the initial fees on an account with a $250 credit limit may reduce the available credit to less than $100.

Under the proposal, the disclosure of the balance computation method, which now appears in the table, would be required to be outside the table so that the table emphasizes information that is more useful to consumers when they are shopping for a card.

With respect to take-one applications and solicitations, under the proposal, card issuers that provide cost disclosures in take-one applications and solicitations would be

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[11] Charge cards are a type of credit card for which full payment is typically expected upon receipt of the billing statement. To ease discussion, this memorandum will refer simply to "credit cards."

required to provide the disclosures in the form of a table, and would no longer be allowed to meet the requirements of § 226.5a by providing a narrative description of account-opening disclosures. This proposed revision is consistent with other revisions contained in the proposal that would require certain account-opening information (such as information about key rates and fees) to be given in the form of a table. See section-by-section analysis to § 226.6(b)(4).

**5a(a) General Rules**

Combining disclosures. Currently, comment 5a-2 states that account-opening disclosures required by § 226.6 do not substitute for the disclosures required by § 226.5a; however, a card issuer may establish procedures so that a single disclosure document meets the requirements of both sections. The Board proposes to retain this comment, but to revise it to account for proposed revisions to § 226.6. Specifically, the Board is proposing to require that certain information given at account opening must be disclosed in the form of a table. See proposed § 226.6(b)(4). The account-opening table would be substantially similar to the table required by § 226.5a, but the content required would not be identical. The account-opening table would require information that would not be required in the § 226.5a table, such as a reference to billing error rights. The Board proposes to revise comment 5a-2 to provide that a card issuer may satisfy § 226.5a by providing the account-opening summary table on or with a card application or solicitation, in lieu of the § 226.5a table. For various reasons, card issuers may want to provide the account-opening disclosures with the card application or solicitation. When issuers do so, this comment allows them to provide the account-opening summary table in lieu of the table containing the § 226.5a disclosures.

Clear and conspicuous standard. Section 226.5(a) requires that disclosures made under subpart B (including disclosures required by § 226.5a) must be clear and conspicuous. Currently, comment 5a(a)(2)-1 provides guidance on the clear and conspicuous standard as applied to the § 226.5a disclosures. The Board proposes to provide guidance on applying the clear and conspicuous standard to the § 226.5a disclosures in comment 5(a)(1)-1. Thus, guidance currently in comment 5a(a)(2)-1 would be deleted as unnecessary. The Board proposed to add comment 5a-3 to cross reference the clear and conspicuous guidance in comment 5a(a)(1)-1.

**5a(a)(1) Definition of Solicitation**

Firm offers of credit. The term "solicitation" is defined in § 226.5a(a)(1) of Regulation Z to mean "an offer by the card issuer to open a credit card account that does not require the consumer to complete an application." 15 U.S.C. 1637(c). Board staff has received questions about whether card issuers making "firm offers of credit" as defined in the Fair Credit Reporting Act (FCRA) are considered to be making solicitations for purposes of § 226.5a. 15 U.S.C. 1681 et seq. The Board proposes to amend the definition of "solicitation" to clarify that such "firm offers of credit" for credit cards are solicitations for purposes of § 226.5a, as discussed below.

The definition "solicitation" was adopted in 1989 to implement part of the Fair Credit and Charge Card Disclosure Act of 1988. It captures situations where an issuer has preapproved a consumer to receive a card, and thus, no application is required. In 1996, the FCRA was amended to allow creditors to use consumer report information in connection with pre-selecting consumers to receive "firm offers of credit." 15 U.S.C. 1681a(l), 1681b(c). A "firm offer of credit" is an offer that must be honored by a creditor if a consumer continues to meet the specific criteria used to select the consumer for the offer. 15 U.S.C. 1681a(l). Creditors may obtain additional credit information from consumers, such as income information, when the consumer responds to the offer. However, creditors may decline to extend credit to the consumer based on this additional information only where the consumer does not meet specific criteria established by the creditor before selecting the consumer for the offer. Thus, because consumers who receive "firm offers of credit" have been preapproved to receive a credit card and may be turned down for credit only under limited circumstances, the Board believes that these preapproved offers are of the type intended to be captured as a "solicitation," even though consumers are asked to provide some additional information in connection with accepting the offer.

Invitations to apply. The Board also proposes to add comment 5a(a)(1)-1 to distinguish solicitations from "invitations to apply," which are not covered by § 226.5a. An "invitation to apply" occurs when a card issuer contacts a consumer who has not been preapproved for a card account about opening an account (whether by direct mail, telephone, or other means) and invites the consumer to complete an application, but the contact itself does not include an application. The Board believes that these "invitations to apply" do not meet the definition of "solicitation" because the consumer must still submit an application in order to obtain the offered card. Thus, proposed comment 5a(a)(1)-1 would clarify that this "invitation to apply" is not covered by § 226.5a unless the contact itself includes an application form in a direct mailing, electronic communication or "take one," an oral application in a telephone contact initiated by the card issuer, or an application in an in-person contact initiated by the card issuer.

**5a(a)(2) Form of Disclosures and Tabular Format**

Fees for late payment, over-the-credit-limit, balance transfers and cash advances. Currently, § 226.5a(a)(2)(ii) and comment 5a(a)(2)-5, which implement TILA Section 127(c)(1)(B), provide that card issuers may disclose late payment fees, over-the-credit-limit fees, balance transfer fees, and cash advance fees in the table or outside the table. 15 U.S.C. 1637(c)(1)(B). In the December 2004 ANPR, the Board requested comment on whether these fees should be required to be in the table. Q8. Many commenters indicated that the Board should require these fees to be in the table, because these are core fees, and uniformity in the placement of the fees would make the disclosures more familiar and predictable for consumers. Some commenters, however, urged the Board to retain the flexibility for card issuers to place the fee disclosures either in the table or immediately outside the table.

The Board proposes to require that these fees be disclosed in the table. In the consumer testing conducted for the Board, participants consistently identified these fees as among the most important pieces of information they consider as part of the credit card offer. With respect to the disclosure of these fees, the Board tested placement of these fees in the table and immediately below the table. Participants who were shown forms where the fees were disclosed below the table tended not to notice these fees compared to participants who were shown forms where the fees were presented in the table. The Board proposes to amend § 226.5a(a)(2)(i) to require these fees to be disclosed in the table, so that consumers can easily identify them. Current § 226.5a(a)(2)(ii) and comment 5a(a)(2)-5, which currently allow issuers to place the fees outside the table, would be deleted. These proposed revisions are based in part on TILA Section 127(c)(5), which authorizes the Board to add or modify § 226.5a disclosures. 15 U.S.C. 1637(c)(5).

Highlighting APRs and fee amounts in the table. Section 226.5a generally requires that certain information about rates and fees applicable to the card offer be disclosed to the consumer in card applications and solicitations. This information includes not only the annual percentage rates and fee amounts that will apply, but also explanatory information that gives context to these figures. The Board seeks to enable consumers to identify easily the rates and fees disclosed in the table. Thus, the Board proposes to add § 226.5a(a)(2)(iv) to require that when a tabular format is required, issuers must disclose in bold text any APRs required to be disclosed, any discounted initial rate permitted to be disclosed, and any fee amounts or percentages required to be disclosed, except for any maximum limits on fee amounts disclosed in the table. Proposed Samples G-10(B) and G-10(C) provide guidance on how to show the rates and fees described in bold text. Proposed Samples G-10(B) and G-10(C) also provide guidance to issuers on how to disclose the percentages and fees described above in a clear and conspicuous manner, by including these percentages and fees generally as the first text in the applicable rows of the table so that the highlighted rates and fees generally are aligned vertically. In consumer testing conducted for the Board, participants who saw a table with the APRs and fees in bold and generally before any text in the table were more likely to identify the APRs and fees quickly and accurately than participants who saw other forms in which the APRs and fees were not highlighted in such a fashion.

Electronic applications and solicitations. Section 1304 of the Bankruptcy Act amends TILA Section 127(c) to require solicitations to open a card account using the Internet or other interactive computer service to contain the same disclosures as those made for applications or solicitations sent by direct mail. Regarding format, the Bankruptcy Act specifies that disclosures provided using the Internet or other interactive computer service must be "readily accessible to consumers in close proximity" to the solicitation. 15 U.S.C. 1637(c)(7).

In September 2000, the Board revised § 226.5a, and as part of these revisions, provided guidance on how card issuers using electronic disclosures may comply with the § 226.5a requirement that certain disclosures be "prominently located" on or with the application or solicitation. 65 FR 58,903; October 3, 2000. In March 2001, the Board issued interim final rules, which are not mandatory, containing additional guidance for the electronic delivery of disclosures under Regulation Z, consistent with the requirements of the E-Sign Act. 66 FR 17,329; March 30, 2001. As discussed above, in April 2007, the Board issued for public comment the 2007 Electronic Disclosure Proposal. See section-by-section analysis to § 226.5(a)(1).

The Bankruptcy Act provision applies to solicitations to open a card account "using the Internet or other interactive computer service." The term "Internet" is defined as the international computer network of both Federal and non-Federal interoperable packet-switched data networks. The term "interactive computer service" is defined as any information service, system or access software provider that provides or enables computer access by multiple users to a computer server, including specifically a service or system that provides access to the Internet and such systems operated or services offered by libraries or educational institutions. 15 U.S.C. 1637(c)(7). Based on the definitions of "Internet" and "interactive computer service," the Board believes that Congress intended to cover card offers that are provided to consumers in electronic form, such as via e-mail or an Internet web site.

In addition, although this Bankruptcy Act provision refers to credit card solicitations (where no application is required), the Board requested comment in the October 2005 ANPR on whether the provision should be interpreted also to include applications. Q93. Almost all commenters on this issue stated that there is no reason to treat electronic applications differently from electronic solicitations. With respect to both electronic applications and solicitations, it is important for consumers who are shopping for credit to receive accurate cost information before submitting an electronic application or responding to an electronic solicitation. The Board proposes to apply the Bankruptcy Act provision relating to electronic offers to both electronic solicitations and applications to promote the informed use of credit and avoid circumvention of TILA. 15 U.S.C. 1601(a), 1604(a). Thus, in implementing the Bankruptcy Act provision, the Board proposes to amend § 226.5a(c) to require that applications and solicitations that are provided in electronic form contain the same disclosures as applications and solicitations sent by direct mail. The same proposal is included in the Board's 2007 Electronic Disclosure Proposal.

With respect to the form of disclosures required under § 226.5a, the Board proposes to amend § 226.5a(a)(2) by adding a new paragraph (v) to provide that if a consumer accesses an application or solicitation for a credit card in electronic form, the disclosures required on or with an application or solicitation for a credit card must be provided to the consumer in electronic form on or with the application or solicitation. A consumer accesses an application or solicitation in electronic form when, for example, the consumer views the application or solicitation on his or her personal computer. On the other hand, if a consumer receives an application or solicitation in the mail, the creditor would not satisfy its obligation to provide § 226.5a disclosures at that time by including a reference in the application or solicitation to the web site where the disclosures are located. See proposed comment 5a(a)(2)-6. The same proposal is included in the Board's 2007 Electronic Disclosure Proposal. See § 226.5a(a)(2)(v) and comment 5a(a)(2)-9 in the 2007 Electronic Disclosure Proposal.

The Board also proposes to revise existing comment 5a(a)(2)-8 added by the 2001 interim final rule, which states that a consumer must be able to access the electronic disclosures at the time the application form or solicitation reply form is made available by electronic communication. The Board proposes to revise this comment to describe alternative methods for presenting electronic disclosures. This comment is intended to provide examples of the methods rather than an exhaustive list. The same proposal was included in the Board's 2007 Electronic Disclosure Proposal.

The Board also proposes to provide guidance on a Bankruptcy Act provision requiring that the § 226.5a disclosures must be "readily accessible to consumers in close proximity" to an application or solicitation that is made electronically. In the October 2005 ANPR, the Board asked whether additional or different guidance is needed from the guidance previously issued by the Board in 2000 regarding how card issuers using electronic disclosures may comply with the § 226.5a requirement that certain disclosures be "prominently located" on or with the application or solicitation. Q95.

In particular, the 2000 guidance states that the disclosures required by § 226.5a must be prominently located on or with electronic applications and solicitations. 65 FR 58,903; October 3, 2000. The guidance provides flexibility for satisfying this requirement. For example, a card issuer could provide on the application or reply form a link to disclosures provided elsewhere, as long as consumers cannot bypass the disclosures before submitting the application or reply form. Alternatively, if a link to the disclosures is not used, the electronic application or reply form could clearly and conspicuously indicate where the fact that rate, fee or other cost information could be found. Or the disclosures could automatically appear on the screen when the application or reply form appears. (See current comment 5a(a)(2)-2, which would be renumbered as 5a(a)(2)-1 under the proposal.)

Most commenters stated that the Board should retain this existing guidance to interpret the "close proximity" standard. A few industry commenters stated that the existing guidance should not apply, and that, for example, it should suffice to provide a link to the disclosures that the consumer could choose to access or not. Some commenters urged the Board generally to allow maximum flexibility to creditors regarding the display of electronic disclosures, and stated that no guidance or specific rules were necessary.

The Board proposes to revise the existing guidance to interpret the "close proximity" standard. The existing guidance would be revised to be consistent with proposed changes to comment 5a(a)(2)-8, that provides guidance to issuers on providing access to electronic disclosures at the time the application form or solicitation reply form is made available by electronic communication. Specifically, the Board proposes to provide that electronic disclosures are deemed to be closely proximate to an application or solicitation if, for example, (1) they automatically appear on the screen when the application or reply form appears, (2) they are located on the same web "page" as the application or reply form without necessarily appearing on the initial screen, if the application or reply form 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, or (3) they are posted on a web site and the application or solicitation reply form is linked to the disclosures in a manner that prevents the consumer from by-passing the disclosures before submitting the application or reply form. See proposed comment 5a(a)(2)-1.ii.

The Board proposes to retain the requirement that if an electronic link to the disclosures is used, the consumer must not be able to bypass the link before submitting an application or a reply form. The Board believes that the "close proximity" standard is designed to ensure that the disclosures are easily noticeable to consumers, and this standard is not met when consumers are only given a link to the disclosures, but not to the disclosures themselves. The Board proposes to incorporate the "close proximity" standard for electronic applications and solicitations in § 226.5a(a)(2)(vi)(B), and the guidance regarding the location of the § 226.5a disclosures in electronic applications and solicitations in comment 5a(a)(2)-1.ii.

Terminology. Section 226.5a currently requires terminology in describing the disclosures required by § 226.5a must be consistent with terminology describing the account-opening disclosures (§ 226.6) and for the periodic statement disclosures (§ 226.7). TILA and § 226.5a also require that the term "grace period" be used to describe the date by which or the period within which any credit extended for purchases may be repaid without incurring a finance charge. 15 U.S.C. 1632(c)(2)(C). The Board proposes that all guidance for terminology requirements with respect to § 226.5a disclosures be placed in proposed § 226.5(a)(2)(iii). The Board proposes to add comment 5a(a)(2)-7 to cross-reference the guidance in § 226.5(a)(2).

**5a(a)(4) Certain Fees That Vary By State**

Currently, under § 226.5a, if the amount of a late-payment fee, over-the-credit-limit fee, cash advance fee or balance transfer fee varies from state to state, a card issuer may disclose the range of the fees instead of the amount for each state, if the disclosure includes a statement that the amount of the fee varies from state to state. See existing § 226.5a(a)(5), renumbered as new § 226.5a(a)(4). As discussed below, the Board proposes to require card issuers to disclose in the table any fee imposed when a payment is returned. See proposed § 226.5a(b)(12). The Board proposes to amend new § 226.5a(a)(4) to add returned payment fees to the list of fees for which an issuer may disclose a range of fees. The Board requests comment on whether other fees required to be disclosed under § 226.5a should be added to the list of fees for which the issuer may disclose a range of fees, such as fees for required insurance or debt cancellation or suspension coverage under proposed § 226.5a(b)(14).

**5a(a)(5) Exceptions**

Section 226.5a currently contains several exceptions to the disclosure requirements. Some of these exceptions are in the regulation itself, while others are contained in the commentary. For clarity, all exceptions would be placed together in new § 226.5a(a)(5), as indicated in the redesignation table below.

**5a(b) Required Disclosures**

Section 226.5a(b) specifies the disclosures that are required to be included on or with certain applications and solicitations.

**5a(b)(1) Annual Percentage Rate**

Section 226.5a requires card issuers to disclose the rates applicable to the account, such as rates applicable to purchases, cash advances, and balance transfers. 15 U.S.C. 1637(c)(1)(A)(i)(I).

16-point font for disclosure of purchase APRs. Currently, under § 226.5a(b)(1), the purchase rate must be disclosed in the table in at least 18-point font. This font requirement does not apply to (1) a temporary initial rate for purchases that is lower than the rate that will apply after the temporary rate expires; or (2) a penalty rate that will apply upon the occurrence of one or more specified events. In response to the December 2004 ANPR, several industry commenters suggested that the Board delete this 18-point font requirement. These commenters indicated that disclosing the purchase rate in 18-point font size might distract consumers from other important terms being disclosed, and that disclosing the purchase rate in the table in large font size is not necessary because simply disclosing the purchase rate in the table provides consumers meaningful and comparable disclosure of that term.

The Board is proposing to reduce the 18-point font requirement to a 16-point font. The purchase rate is one of the most important terms disclosed in the table, and it is essential that consumers be able to identify that rate easily. A 16-point font size requirement for the purchase APR appears to be sufficient to highlight the purchase APR. (The Board is proposing that other disclosures in the table are required to be in 10-point type. See proposed comment 5(a)(1)-3.) In consumer testing conducted for the Board, versions of the table in which the purchase rate was the same font as other rates included in the table were reviewed. In other versions, the purchase rate was in 16-point type while other disclosures were in 10-point type. Participants tended to notice the purchase rate more often when it was in a font bigger than the font used for other rates. Nonetheless, there was no evidence from consumer testing that it was necessary to use a font size of 18-point in order for the purchase APR to be noticeable to participants. Given that the proposal is requiring a minimum of 10-point type for the disclosure of other terms in the table, based on document design principles, the Board believes that a 16-point font size for the purchase APR would be effective in highlighting the purchase APR in the table.

Periodic rate. Currently, comment 5a(b)(1)-1 allows card issuers to disclose the periodic rate in the table in addition to the required disclosure of the corresponding APR. The Board proposes to delete comment 5a(b)(1)-1, and thus, prohibit disclosure of the periodic rate in the table. Based on consumer testing conducted for the Board, consumers do not appear to shop using the periodic rate, nor is it clear that this information is important to understanding a credit card offer. Allowing the periodic rate to be disclosed in the table may distract from more important information in the table, and contribute to "information overload." Thus, in an effort to streamline the information that appears in the table, the Board proposes to prohibit disclosure of the periodic rate in the table. Nonetheless, card issuers may disclose this information outside of the table.

Variable rate information. Section 226.5a(b)(1)(i), which implements TILA Section 127(c)(1)(A)(i)(II), currently requires for variable-rate accounts, that the card issuer must disclose the fact that the rate may vary and how the rate is determined. 15 U.S.C. 1637(c)(1)(A)(i)(II). In disclosing how the applicable rate will be determined, the card issuer is required to provide the index or formula used and disclose any margin or spread added to the index or formula in setting the rate. The card issuer may disclose the margin or spread as a range of the highest and lowest margins that may be applicable to the account. A disclosure of any applicable limitations on rate increases or decreases may also be included in the table. See current comment 5a(b)(1)-3.

1. Index and margins. Currently, the variable rate information is required to be disclosed separately from the applicable APR, in a row of the table with the heading "Variable Rate Information." Some card issuers will include the phrase "variable rate" with the disclosure of the applicable APR and include the details about the index and margin under the "Variable Rate Information" heading. In the consumer testing conducted for the Board, many participants who saw the variable rate information presented as described above understood that the label "variable" meant that a rate could change, but could not locate information on the tested form regarding how or why these rates could change. This was true even if the index and margin information was taken out of the row of the table with the heading "Variable Rate Information" and placed in a footnote to the phrase "variable rate." Many participants who did find the variable rate information were confused by the variable-rate margins, often interpreting them erroneously as the actual rate being charged. In addition, very few participants indicated that they would use the margins in shopping for a credit card account.

Accordingly, the Board proposes to amend § 226.5a(b)(1)(i) to specify that issuers may not disclose the amount of the index or margins in the table. Specifically, card issuers would not be allowed to disclose in the table the current value of the index (for example, that the prime rate currently is 7.5 percent) or the amount of the margin that is used to calculate the variable rate. Card issuers would be allowed to indicate only that the rate varies and the type of index used to determine the rate (such as the "prime rate," for example.) In describing the type of index, the issuer may not include details about the index in the table. For example, if the issuer uses a prime rate, the issuer must just describe the rate as tied to a "prime rate" and may not disclose in the table that the prime rate used is the highest prime rate published in the Wall Street Journal two business days before the closing date of the statement for each billing period. See proposed comment 5a(b)(1)-2. Also, the Board would require that the disclosure about a variable rate (the fact that the rate varies and the type of index used to determine the rate) must be disclosed with the applicable APRs, so that consumers can more easily locate this information. See proposed Model Form G-10(A), Samples G-10(B) and G-10(C). Proposed Samples G-10(B) and G-10(C) provide guidance to issuers on how to disclose the fact that the applicable rate varies and how it is determined.

2. Rate floors and ceilings. Currently, card issuers may disclose in the table, at their option, any limitations on how high (i.e., a rate ceiling) or low (i.e., a rate floor) a particular rate may go. For example, assume that the purchase rate on an account could

not go below 12 percent or above 24 percent. An issuer would be required to disclose in the table the current rate offered on the credit card (for example, 18 percent), and would be permitted to disclose in the table that the rate would not go below 12 percent and above 24 percent. See current comment 5a(b)(1)-4. The Board proposes to revise the commentary to prohibit the disclosure of the rate floors and ceilings in the table. Based on consumer testing conducted for the Board, consumers do not appear to shop based on these rate floors and ceilings, and allowing them to be disclosed in the table may distract from more important information in the table, and contribute to "information overload." Thus, in an effort to streamline the information that may appear in the table, the Board proposes to prohibit disclosure of the rate floors and ceilings in the table. Nonetheless, card issuers may disclose this information outside of the table.

Discounted initial rates. Currently, comment 5a(b)(1)-5 specifies that if the initial rate is temporary and is lower than the rate that will apply after the temporary rate expires, a card issuer must disclose the rate that will otherwise apply to the account. A discounted initial rate may be provided in the table along with the rate required to be disclosed if the card issuer also discloses the time period during which the introductory rate will remain in effect. The Board proposes to move comment 5a(b)(1)-5 to new § 226.5a(b)(1)(ii). The Board also proposes to add new comment 5a(b)(1)-3 to specify that if a card issuer discloses the discounted initial rate and expiration date in the table, the issuer is deemed to comply with the standard to provide this information clearly and conspicuously if the issuer uses the format specified in proposed Samples G-10(B) and G-10(C) to present this information.

In addition, under TILA Section 127(c)(6)(A), as added by Section 1303(a) of the Bankruptcy Act, the term "introductory" must be used in immediate proximity to each listing of a discounted initial rate in the application, solicitation, or promotional materials accompanying such application or solicitation. Thus, the Board proposes to revise new § 226.5a(b)(1)(ii) to specify that if an issuer provides a discounted initial rate in the table along with the rate required to be disclosed, the card issuer must use the term "introductory" in immediate proximity to the listing of the initial discounted rate.

In the October 2005 ANPR, commenters asked the Board to consider permitting creditors to use the term "intro" as an alternative to the word "introductory." Because "intro" is a commonly understood abbreviation of the term "introductory," and consumer testing indicates that consumers understand this term, the Board proposes to allow creditors to use "intro" as an alternative to the requirement to use the term "introductory" and is proposing to clarify this approach in new § 226.5a(b)(1)(ii). Also, to give card issuers guidance on the meaning of "immediate proximity," the Board is proposing to provide guidance for creditors that place the word "introductory" or "intro" within the same phrase as each listing of the discounted initial rate. This guidance is set forth in proposed comment 5a(b)(1)-3. The Board believes that interpreting "immediate proximity" to mean adjacent to the rate may be too restrictive. Moreover, the Board has proposed the "within the same phrase" standard as a safe harbor instead of requiring this placement, recognizing that even if the term "introductory" is not "within the same phrase" as the rate it may still meet the "immediate proximity" standard.

Penalty rates. Currently, comment 5a(b)(1)-7 requires that if a rate may increase upon the occurrence of one or more specific events, such as a late payment or an extension of credit that exceeds the credit limit, the card issuer must disclose the increased penalty rate that may apply and the specific event or events that may result in the increased rate. If a tabular format is required, the issuer must disclose the penalty rate in the table under the heading "Other APRs," along with any balance transfer or cash advance rates.

The specific event or events must be described outside the table with an asterisk or other means to direct the consumer to the additional information. At its option, the issuer may include outside the table with the explanation of the penalty rate the period for which the increased rate will remain in effect, such as "until you make three timely payments." The issuer need not disclose an increased rate that is imposed if credit privileges are permanently terminated.

In the December 2004 ANPR, the Board solicited comment on whether the table was effective as currently designed. Q7. In response to this question, many commenters suggested that the specific event or events that may result in the penalty rate should be disclosed in the table along with the penalty rate, because this would enhance comparison shopping and consumer understanding by highlighting penalty pricing and its effect on the other rates for the account.

In the consumer testing conducted for the Board, when reviewing forms in which the specific events that trigger the penalty rate were disclosed outside the table, many participants did not readily notice the penalty rate triggers when they initially read through the document or when asked follow-up questions. In addition, many participants did not readily notice the penalty rate when it was included in the row "Other APRs" along with other rates. The GAO also found that consumers had difficulty identifying the default rate and circumstances that would trigger rate increases. See GAO Report on Credit Card Rates and Fees, at page 49. In the testing conducted for the Board, when the penalty rate was placed in a separate row in the table, participants tended to notice the rate more often. Moreover, participants tended to notice the specific events that result in the penalty rate more often when these events were included with the penalty rate in a single row in the table. For example, two types of forms related to placement of the events that could trigger the penalty rate were tested – several versions showed the penalty rate in one row of the table and the description of the events that could trigger the penalty rate in another row of the table. Several other versions showed the penalty rate and the triggering events in the same row. Participants who saw the versions of the table with the penalty rate in a separate row from the description of the triggering events tended to skip over the row that specified the triggering events when reading the table. Nonetheless, participants who saw the versions of the table in which the penalty rate and the triggering events were in the same row tended to notice the triggering events when they reviewed the table.

As a result, the Board proposes to add § 226.5a(b)(1)(iv) and amend new comment 5a(b)(1)-4 (previously comment 5a(b)(1)-7) to require card issuers to briefly disclose in the table the specific event or events that may result in the penalty rate. In addition, the Board is proposing that the penalty rate and the specific events that cause the penalty rate to be imposed must be disclosed in the same row of the table. See proposed Model Form G-10(A). In describing the specific event or events that may result in an increased rate, new comment 5a(b)(1)-4 provides that the descriptions of the triggering events in the table should be brief. For example, if an issuer may increase a rate to the penalty rate if the consumer does not make the minimum payment by 5 p.m., Eastern time, on its payment due date, the issuer should describe this circumstance in the table as "make a late payment." Proposed Samples G-10(B) and G-10(C) provide additional guidance on the level of detail that issuers should use in describing the specific events that result in the penalty rate.

The Board also proposes to specify in new § 226.5a(b)(1)(iv) that in disclosing a penalty rate, a card issuer also must specify the balances to which the increased rate will apply. Typically, card issuers apply the increased rate to all balances on the account. The Board believes that this information helps consumers better understand the consequences of triggering the penalty rate.

In addition, the Board proposes to specify in new § 226.5a(b)(1)(iv) that in disclosing the penalty rate, a card issuer must describe how long the increased rate will apply. Proposed comment 5a(b)(1)-4 provides that in describing how long the increased rate will remain in effect, the description should be brief, and refers issuers to Samples G-10(B) and G-10(C) for guidance on the level of detail that issuer should use to describe how long the increased rate will remain in effect. Also, proposed comment 5a(b)(1)-4 provides that if a card issuer reserves the right to apply the increased rate indefinitely, that fact should be stated. The Board believes that this information may help consumers better understand the consequences of triggering the penalty rate.

Also, the Board proposes to add language to new § 226.5a(b)(1)(iv) to specify that in disclosing a penalty rate, card issuers must include a brief description of the circumstances under which any discounted initial rates may be revoked and the rate that will apply after the discounted initial rate is revoked. Section 1303(a) of the Bankruptcy Act requires that a credit card application or solicitation must contain in a prominent location on or with the application or solicitation a clear and conspicuous disclosure of a general description of the circumstances that may result in revocation of a discounted initial rate offered with the card, and the rate that will apply after the discounted initial rate is revoked. 15 U.S.C. 1637(c)(6)(C). The Board is proposing that this information be disclosed in the table along with other penalty rate information. Often, the same events that trigger a loss of a discounted initial rate and an increase to the penalty rate also trigger an increase in other rates on the account.

Rates that depend on consumers' creditworthiness. Credit card issuers often engage in risk-based pricing such that the rates offered on a credit card will depend on later determinations of a consumer's creditworthiness. For example, an issuer may use information collected in a consumer's application or solicitation reply form (e.g., income information) or obtained through a credit report from a consumer reporting agency to determine the rate for which a consumer qualifies. For preapproved solicitations, issuers that engage in risk-based pricing typically will disclose the specific rates offered to the consumer, because for these offers, issuers typically will have some indication of a consumer's creditworthiness based on the prescreening process done through a consumer reporting agency. For applications not involving prescreens, however, issuers that use risk-based pricing may not be able to disclose the specific rate that would apply to a consumer, because issuers may not have sufficient information about a consumer's creditworthiness at the time the application is given.

In response to the December 2004 ANPR, industry commenters asked for guidance on how rates should be disclosed under § 226.5a when an issuer does not know the specific rate for which the consumer will qualify at the time the disclosures are made because the specific rate depends on a later determination of the consumer's creditworthiness. Some industry commenters asked the Board to clarify that issuers may disclose the range of possible rates, with an explanation that the rate obtained by the consumer is based on the consumer's creditworthiness. Another industry commenter suggested that the Board should allow issuers to disclose a recent APR or the median rate within the range of possible rates, with an explanation that the rate could be higher or lower depending on the consumer's creditworthiness. Several consumer group commenters suggested that the Board should not allow issuers to disclose a range of possible rates. Instead, issuers should be required to disclose the actual APR that the creditor is offering, because otherwise, consumers do not know the rate for which they are applying.

The Board proposes to add § 226.5(b)(1)(v) and comment 5a(b)(1)-5 to clarify that in circumstances in which an issuer cannot state a single specific rate being offered at the time disclosures are given because the rate will depend on a later determination of the consumer's creditworthiness, issuers must disclose the possible rates that might apply, and a statement that the rate for which the consumer may qualify at account opening depends on the consumer's creditworthiness. A card issuer may disclose the possible rates as either specific rates or a range of rates. For example, if there are three possible rates that may apply (e.g., 9.99, 12.99 or 17.99 percent), an issuer may disclose specific rates (9.99, 12.99 or 17.99 percent) or a range of rates (9.99 to 17.99 percent). Proposed Samples G-10(B) and G-10(C) provide guidance for issuers on how to meet these requirements. In addition, the Board solicits comment on whether card issuer should alternatively be permitted to list only the highest possible rate that may apply instead of a range of rates (e.g., up to 17.99 percent).

As discussed above, one industry commenter suggested that the Board should allow issuers to disclose a recent APR or the median rate within the range of possible rates, with an explanation that the APR could be higher or lower depending on the consumer's creditworthiness. The Board believes that requiring card issuers to disclose all the possible rates (as either specific rates, or as a range of rates) provides more useful information to consumers than allowing issuers to disclose a median APR within the range. If only one rate is disclosed in the table, consumers may mistake the rate disclosed as the specific rate offered on the account, and not understand that it is a median rate within a certain range, even if there is an explanation that the rate could be higher or lower. If a consumer sees a range or several specific rates, the consumer may be better able to determine that more than one rate is being disclosed.

Transactions with both rate and fee. When a consumer initiates a balance transfer or cash advance, card issuers typically charge consumers both interest on the outstanding balance of the transaction, and a fee to complete the transaction. It is important that consumers understand when both a rate and a fee apply to specific transactions. In the consumer testing conducted for the Board, several ways of presenting rate and fee information were reviewed. In some tests, the cash advance and balance transfer rates were included in a section with other rates, and cash advance and balance transfer fees were included in a section with other fees. In other tests, cash advance and balance transfer fees were not included with other fees, but instead were included with the cash advance and balance transfer rates. Participants in the first test (the one where balance transfer and cash advance fees were grouped with other fees) were more likely to notice the balance transfer and cash advance fees than participants in the other tests. Participants tended to notice rates more easily when they were grouped together, and fees more easily when they are grouped together. Thus, the Board is proposing to group APRs together in the table and fees together in the table, rather than grouping APRs and fees related to cash advances together and APRs and fees related to balance transfers together.

Nonetheless, because the rates and the fees related to cash advances and balance transfers are not grouped together, a cross reference from the cash advance and balance transfer rates to the applicable fees may help consumers notice both the rate and the fee. In consumer testing conducted for the Board, some participants were more aware that an interest rate applies to cash advances and balance transfers than they were aware of the fee component, so a cross reference between the rate and the fee may help those consumers notice both the rate and the fee components. Therefore, the Board proposes to add new § 226.5a(b)(1)(vi) to require that if a rate and fee both apply to a balance transfer or cash advance transaction, a card issuer must disclose that a fee also applies when disclosing the rate, and a cross-reference to the fee. 15 U.S.C. 1637(c)(5).

Typical APR. In response to the December 2004 ANPR, several consumer groups indicated that the current disclosure requirements in § 226.5a allow card issuers to promote low APRs, that include interest but not fees, while charging high penalty fees and penalty rates when consumers, for example, pay late or exceed the credit limit. As a result, these consumer groups suggested that the Board require credit card issuers to disclose in the table a "typical rate" that would include fees and charges that consumers pay for a particular open-end credit products. This rate would be calculated as the average effective rate disclosed on periodic statements over the last three years for customers with the same or similar credit card product. These consumer groups believe that this "typical rate" would reflect the real rate that consumers pay for the credit card product.

The Board is not proposing that card issuers disclose the “typical rate” as part of the § 226.5a disclosures. Although a single cost figure (like the APR on closed-end credit) is a laudable objective, the Board does not believe that the proposed typical APR would be helpful to consumers that seek credit cards. There are many different ways consumers may use their credit cards, such as the features they use, what fees they incur, and whether a balance is carried from month to month. For example, some consumers use their cards only for purchases, always pay off the bill in full, and never pay fees. Other consumers may use their cards for purchases, balance transfers or cash advances, but never pay late-payment fees, over-the-credit-limit fees or other penalty fees. Still others may pay penalty fees and incur penalty rates. A “typical rate,” however, would be based on average fees and average balances that may not be typical for many consumers. Moreover, such a rate may confuse consumers about the actual rate that may apply to their account.

Nonetheless, the Board believes it is important that consumers understand the penalty rates and penalty fees that apply to a credit card account. Thus, the Board is proposing to make penalty rates more prominent in the table and require card issuers to describe in the table the reasons why a penalty rate may apply and how long the penalty rate will apply. See proposed § 226.5a(b)(1)(iv). Likewise, the Board is proposing to highlight penalty fees by requiring that late payment fees, over-the-credit-limit fees, and returned-payment fees be disclosed in the table. See proposed § 226.5a(a)(2)(i).

**5a(b)(2) Fees for Issuance or Availability**

Section 226.5a(b)(2), which implements TILA Section 127(c)(1)(A)(ii)(I), requires card issuers to disclose any annual or other periodic fee, expressed as an annualized amount, that is imposed for the issuance or availability of a credit card, including any fee based on account activity or inactivity. 15 U.S.C. 1637(c)(1)(A)(ii)(I). In 1989, the Board used its authority under TILA Section 127(c)(5) to require that issuers also disclose non-periodic fees related to opening the account, such as one-time membership or participation fees. 15 U.S.C. 1637(c)(5); 54 FR 13,855, April 6, 1989.

Fees for issuance or availability of credit card products targeted to subprime borrowers. Often, subprime credit cards will have substantial fees related to the issuance and availability of credit. For example, these cards may impose an annual fee, and a monthly maintenance fee for the card. In addition, these cards may impose multiple one-time fees when the consumer opens the card account, such as an application fee and a program fee. The Board believes that these fees should be clearly explained to consumers at the time of the offer so that consumers better understand when these fees will be imposed.

The Board proposes to amend § 226.5a(b)(2) to require additional information about periodic fees. 15 U.S.C. 1637(c)(5). Currently, issuers are required to disclose only the annualized amount of the fee. The Board proposes to amend § 226.5a(b)(2) to require issuers also to disclose the amount of the periodic fee, and how frequently it will be imposed. For example, if an issuer imposes a $10 monthly maintenance fee for a card, the issuer must disclose in the table that there is a $10 monthly maintenance fee, and that the fee is $120 on an annual basis.

In addition, the Board proposes to amend § 226.5a(b)(2) to require additional information about non-periodic fees related to opening the account. Currently, issuers are required to disclose the amount of the non-periodic fee, but not that it is a one-time fee. The Board proposes to amend § 226.5a(b)(2) to require card issuers to disclose the amount of the fee and that it is a one-time fee. This additional information will allow consumers to better understand set-up and maintenance fees that are often imposed in connection with subprime credit cards. For example, the proposed changes would provide consumers with additional information about when the fees will be imposed by identifying which fees are one-time fees, which fees are periodic fees (such as monthly fees), and which fees are annual fees.

In addition, application fees that are charged regardless of whether the consumer receives credit currently are not considered fees as imposed for the issuance or availability of a credit card, and thus are not disclosed in the table. See current comment 5a(b)(2)-3 and § 226.4(c)(1). The Board proposes to delete the exception for these application fees and require that they be disclosed in the table as fees imposed for the issuance or availability of a credit card. The Board believes that consumers should be aware of these fees when they are shopping for a credit card.

**5a(b)(3) Minimum Finance Charge**

Currently, § 226.5a(b)(3), which implements TILA Section 127(c)(1)(A)(ii)(II), requires that card issuers must disclose any minimum or fixed finance charge that could be imposed during a billing cycle. Card issuers typically impose a minimum charge (e.g., $.50) in lieu of interest in those months where a consumer would otherwise incur an interest charge that is less than the minimum charge (a so-called "minimum interest charge"). In response to the December 2004 ANPR, one industry commenter suggested that the Board no longer require that the minimum finance charge be disclosed in the table because these fees are typically small (e.g., $.50) and consumers do not shop on them. Another industry commenter suggested that the Board only require that the minimum finance charge be included in the table if the charge is a significant amount. On the other hand, several consumer groups urged the Board to continue to include the minimum finance charge in the table because this charge can have a significant effect on the cost of credit.

The Board proposes to retain the minimum finance charge disclosure in the table. Although minimum charges currently may be small, card issuers may increase these charges in the future. Also, Board is aware of at least one credit card product for which no APR is charged, but each month a fixed charge is imposed based on the outstanding balance (for example, $6 charge per $1,000 balance). If the minimum finance charge disclosure was eliminated from the table, card issuers that offer this type of pricing would no longer be required to disclose the fixed charge in the table. The Board is not proposing to require the minimum finance charge only if it is a significant amount. This approach could undercut the uniformity of the table, and could be misleading to consumers. If consumers do not see a minimum finance charge disclosed in the table, the Board is concerned that most consumers might assume that there is not a minimum finance charge on the card, when the charge was below a certain threshold.

Under § 226.5a(b)(3), card issuers are only required to disclose the amount of any minimum or fixed finance charge that could be imposed during a billing cycle. Card issuers currently are not required to provide a description of when this charge may be imposed. In consumer testing conducted for the Board, model forms were tested that only included the amount of the minimum interest charge in the table. In viewing these forms, some participants misunderstood that they would pay the minimum interest charge every month, not just those months where they otherwise would incur interest that was less than the minimum charge. Thus, the Board proposes to amend § 226.5a(b)(3) to require card issuers to disclose in the table a brief description of the minimum finance charge, to give consumers context for when this charge will be imposed.
15 U.S.C. 1637(c)(5). Proposed Samples G-10(B) and G-10(C) provide guidance regarding how to disclose a minimum interest charge.

**5a(b)(4) Transaction Charges**

Section 226.5a(b)(4), which implements TILA Section 127(c)(1)(A)(ii)(III), requires that card issuers disclose any transaction charge imposed on purchases. The current commentary to this provision clarifies that only transaction fees on purchases imposed by the issuer must be disclosed. (See comment 5a(b)(4)-1.) For clarity, the Board would amend § 226.5a(b)(4) to incorporate this commentary provision.

In addition, the Board proposes to amend § 226.5a(b)(4) to specify that fees charged for transactions in a foreign currency or that take place in a foreign country may not be disclosed in the table. In an effort to streamline the contents of the table, the Board proposes to highlight only those fees that may be important for a significant number of consumers. In consumer testing for the Board, participants did not tend to mention foreign transaction fees as important fees they use to shop. There are few consumers who may pay these fees with any frequency. Thus, the Board proposes to except foreign transaction fees from disclosure of transaction fees. The Board proposes to include foreign transaction fees in the account-opening summary table that is required under § 226.6(b)(4), so that interested consumers can learn of the fees before using the card.

**5a(b)(5) Grace Period**

Section 226.5a(b)(5), which implements TILA Section 127(c)(A)(iii)(I), requires that card issuers disclose in the table the date by which or the period within which any credit extended for purchases may be repaid without incurring a finance charge. If no grace period is provided, that fact must be disclosed. Comment 5a(b)(5)-1 provides that a card issuer may, but need not, refer to the beginning or ending point of any grace period and briefly state any conditions on the applicability of the grace period. For example, the grace period disclosure might read “30 days” or “30 days from the date of the periodic statement (provided you have paid your previous balance in full by the due date).”

The consumer testing conducted for the Board indicated that some participants misunderstood the word "grace period" to mean the time after the payment due date that an issuer may give the consumer to pay the bill without charging a late-payment fee. The GAO found similar misunderstandings by consumers in its consumer testing. Furthermore, many participants in the GAO testing incorrectly indicated that the grace period was the period of time promotional interest rates applied. See GAO Report On Credit Card Rates and Fees, at page 50.

In consumer testing conducted for the Board, participants tended to understand the grace period more clearly when additional context was added, such as describing that if the consumer paid the bill in full each month, the consumer would have some period of time (e.g., 25 days) to pay the new purchase balance in full to avoid interest. Thus, the Board proposes to amend § 226.5a(b)(5) to require card issuers to disclose briefly any conditions on the applicability of the grace period. 15 U.S.C. 1637(c)(5). The Board also proposes to amend comment 5a(b)(5)-1 to provide guidance for how issuers may meet the requirements in proposed § 226.5a(b)(5).

**5a(b)(6) Balance Computation Method**

TILA Section 127(c)(1)(A)(iv) calls for the Board to name not more than five of the most common balance computation methods used by credit card issuers to calculate the balance on which finance charges are computed. 15 U.S.C. 1637(c)(1)(A)(iv). If issuers use one of the balance computation methods named by the Board, § 226.5a(b)(6) requires that issuers must disclose the name of that balance computation method in the table as part of the disclosures required by § 226.5a, and issuers are not required to provide a description of the balance computation method. If the issuer uses a balance computation method that is not named by the Board, the issuer must disclose a detailed explanation of the balance computation method. See current § 226.5a(b)(6); § 226.5a(a)(2)(i).

In response to the December 2004 ANPR, several commenters suggested that the Board delete the description of the balance computation method from the table. These commenters believed that the implications of the balance computation method on the actual cost of credit are simply too complex and too contingent on future purchasing patterns to be of any use to consumers in shopping for credit.

The Board agrees that balance computation methods are too complex to explain in a simple fashion in the table. Most card issuers use one of two methods – either the "average daily balance method (including new purchases)" or the "two-cycle average daily balance method (including new purchases)." For consumers that carry a balance on their credit card every month or for consumers that pay off their balance in full every month, there essentially is no difference between these two methods. There is a difference between the two methods only in those months where a consumer paid off their previous balance in full, but did not pay off their current balance in full. In those months, the consumer will pay more interest under the "two-cycle average daily balance method" than under the "average daily balance method." How much more interest the consumer pays depends on the amount of the purchases in the previous billing cycle, when those purchases were made, the amount of any payments made in that billing cycle, and when those payments were made.

In consumer testing conducted for the Board, virtually no participants understood the two balance computation methods most used by card issuers – the average daily balance method and the two-cycle average daily balance method – when those methods were just described by name. The GAO found similar results in its consumer testing. See GAO Report On Credit Card Rates and Fees, at pages 50-51. In the consumer testing conducted for the Board, a version of the table was used which attempted to explain briefly that the "two-cycle average daily balance method" would be more expensive than the "average daily balance method" for those consumers that sometimes pay their bill in full and sometimes do not. Participants' answers suggested they did not understand this disclosure. They appeared to need more information about how balances are calculated. Nonetheless, the addition of more information would likely add too much detail to the disclosures and result in "information overload." In addition, it is unclear whether most consumers would consider the balance computation method when shopping for a credit card.

As a result, the Board proposes to retain a brief reference to the balance computation method, but move the disclosure from the table to directly below the table. See § 226.5a(a)(2)(iii). TILA Section 122(c)(2) states that for certain disclosures set forth in Section TILA 127(c)(1)(A), including the balance computation method, the Board shall require that the disclosure of such information shall, to the extent the Board determines to be practicable and appropriate, be in the form of a table. 15 U.S.C. 1632(c)(2). The Board believes that it is no longer appropriate to continue to disclose the balance computation method in the table, because the name of the balance computation method used by issuers does not appear to be meaningful to consumers without additional context and may distract from more important information contained in the table. The Board proposes to continue to require that issuers disclose the name of the balance computation method beneath the table, so that consumers and others will have access to this information if they find it useful.

**5a(b)(8) Cash Advance Fee**

Currently, comment 5a(b)(8)-1 provides that a card issuer must disclose only those fees it imposes for a cash advance that are finance charges under § 226.4. For example, a charge for a cash advance at an automated teller machine (ATM) would be disclosed under § 226.5a(b)(8) if no similar charge is imposed for ATM transactions not involving an extension of credit. As discussed in the section-by-section analysis to § 226.4, the Board proposes to provide that all transaction fees on credit cards would be considered finance charges. Thus, the Board proposes to delete the current guidance discussed in comment 5a(b)(8)-1 as obsolete.

**5a(b)(12) Returned Payment Fee**

Currently, § 226.5a does not require a card issuer to disclose a fee imposed when a payment is returned. The Board proposes to add § 226.5a(b)(12) to require issuers to disclose this fee in the table. Typically, card issuers will impose a fee and a penalty rate if a cardholder's payment is returned. As discussed above, the Board proposes to require card issuers to disclose in the table the reasons that a penalty rate may be imposed. See proposed § 226.5a(b)(1)(iv). The Board proposes that the returned payment fee be disclosed too, so that consumers are told both consequences of returned payments.

**5a(b)(13) Cross References from Fees to Penalty Rate**

Card issuers often impose both a fee and penalty rate for the same behavior – such as a consumer paying late, exceeding the credit limit, or having a payment returned. In consumer testing conducted for the Board, participants tended to associate paying penalty fees with certain behaviors (such as paying late or going over the credit limit), but they did not tend to associate rate increases with these same behaviors. By linking the penalty fees with the penalty rate, participants more easily understood that if they engage in certain behaviors, such as paying late, their rates may increase in addition to incurring a fee. Thus, the Board proposes to add § 226.5a(b)(13) to provide that if a card issuer may impose a penalty rate for any of the reasons that a penalty fee would be disclosed in the table (such as late payments, going over the credit limit, or returned payments), the issuer in disclosing the fee also must disclose that the penalty rate may apply, and a cross-reference to the penalty rate. Proposed Samples G-10(B) and G-10(C) provide guidance on how to provide these disclosures.

**5a(b)(14) Required Insurance, Debt Cancellation Or Debt Suspension Coverage**

Credit card issuers often offer optional insurance or debt cancellation or suspension coverage with the credit card. Under the current rules, costs associated with the insurance or debt cancellation or suspension coverage are not considered "finance charges" if the coverage is optional, the issuer provides certain disclosures to the consumer about the coverage, and the issuer obtain an affirmative written request for coverage after the consumer has received the required disclosures. Card issuers frequently provide the disclosures discussed above on the application form and a space to sign or initial an affirmative written request for the coverage. Currently, issuers are not required to provide any information about the insurance or debt cancellation or suspension coverage in the table that contains the § 226.5a disclosures.

In the event that a card issuer requires the insurance or debt cancellation or debt suspension coverage (to the extent permitted by state or other applicable law), the Board proposes new § 226.5a(b)(14) to require that the issuer disclose any fee for this coverage in the table. In addition, new § 226.5a(b)(14) would require that the card issuer also disclose a cross-reference to where the consumer may find more information about the insurance or debt cancellation or debt suspension coverage, if additional information is included on or with the application or solicitation. Proposed Sample G-10(B) provides guidance on how to provide the fee information and the cross-reference in the table. If insurance or debt cancellation or suspension coverage is required in order to obtain a credit card, the Board believes that fees required for this coverage should be highlighted in the table so that consumers are aware of these fees when considering an offer, because they will be required to pay the fee for this coverage every month in order to have the credit card.

**5a(b)(15) Payment Allocation**

Some credit card issuers will allocate payments first to balances that are subject to the lowest APR. For example, if a cardholder made purchases using a credit card account and then initiated a balance transfer, the card issuer might allocate a payment (less than the amount of the balances) to the transferred balance portion of the account if that balance was subject to a lower APR than the purchases. Card issuers often will offer a discounted initial rate on balance transfers (such as 0 percent for an introductory period) with a credit card solicitation, but not offer the same discounted rate for purchases. In addition, the Board is aware of at least one issuer that offers the same discounted initial rate for balance transfers and purchases for a specified period of time, where the discounted rate for balance transfers (but not the discounted rate for purchases) may be extended until the balance transfer is paid off if the consumer makes a certain number of purchases each billing cycle. At the same time, issuers typically offer a grace period for purchases if a consumer pays his or her bill in full each month. Card issuers, however, do not typically offer a grace period on balance transfers or cash advances. Thus, on the offers described above, a consumer cannot take advantage of both the grace period on purchases and the discounted rate on balance transfers. Because the payments will be allocated to the balance transfers first, the only way for a consumer to avoid paying interest on purchases - and thus have the benefit of the grace period - is to pay off the entire balance, including the balance transfer subject to the discounted rate.

The Board believes that it is important that consumers understand payment allocation in these circumstances, so that they can better understand the offer and decide whether to use this particular card for purchases. For example, if consumers knew that they would pay interest on all purchases made while paying off the balance transfer at the discounted rate, they might not use that particular card for purchases. They might use another card for purchases and pay that card in full every month to take advantage of the grace period on purchases. Or they might use another card with a lower purchase rate, if they did not plan to pay off the purchases in full each month.

In the consumer testing conducted for the Board, many participants did not understand that they could not take advantage of the grace period on purchases and the discounted rate on balance transfers at the same time. Model forms were tested that included a disclosure notice attempting to explain this to consumers. Nonetheless, testing showed that a significant percentage of participants still did not fully understand how payment allocation can affect their interest charges, even after reading the disclosure tested. The Board plans to conduct further testing of the disclosure to determine whether the disclosure can be improved to be more effectively communicate to consumers how payment allocation can affect their interest charges. Nonetheless, because some participants did benefit from the disclosure, and in light of further testing, the Board, under its authority pursuant to TILA Section 127(c)(5), proposes to add § 226.5a(b)(15) to require a card issuer to explain payment allocation to consumers.
15 U.S.C. 1637(c)(5). Proposed § 226.5a(b)(15) states that if (1) a card issuer offers a discounted initial rate on a balance transfers or cash advance that is lower than the rate on purchases, (2) the issuer offers a grace period on purchases, and (3)the issuer may allocate payments to the lower rate balance first, then the issuer must make certain

disclosures in the table. Specifically, issuers would be required to disclose: (1) that the discounted initial rate applies only to balance transfers or cash advances, as applicable, and not to purchases; (2) that payments will be allocated to the balance transfer or cash advance balance, as applicable, before being allocated to any purchase balance during the time the discounted initial rate is in effect; and (3) that the consumer will incur interest on the purchase balance until the entire balance is paid, including the transferred balance or cash advance balance, as applicable. The Board would require these disclosures in the table only if the discounted initial rate applies to balance transfers or cash advances that consumers can request as part of accepting the offer. If the discounted initial rate only applies to subsequent balance transfers or checks that access a credit card account, the issuer would not need to provide this disclosure with the offer. The Board proposes to add comment 5a(b)(15)-1 to provide examples of when these disclosures must be given. The Board also proposes to add comment 5a(b)(15)-2 to specify that a card issuer may comply with the requirements in new § 226.5a(b)(15) by providing the applicable disclosures contained in proposed Samples G-10(B) and G-10(C).

**5a(b)(16) Available Credit**

Subprime credit cards often have substantial fees assessed when the account is opened. Those fees will be billed to the consumer as part of the first statement, and will substantially reduce the amount of credit that the consumer initially has available with which to make purchases or other transactions on the account. For example, for cards for which a consumer is given a minimum credit line of $250, after the start-up fees have been billed to the account, the consumer may have less than $100 of available credit with which to make purchases or other transactions in the first month. In addition, consumers will pay interest on these fees until they are paid in full.

The federal banking agencies have received a number of complaints from consumers with respect to cards of this type. Complainants often claim that they were not aware of how little available credit they would have after all the fees were assessed. Thus, the Board is proposing to add § 226.5a(b)(16) to inform consumers about the impact of these fees on their initial available credit. Specifically, § 226.5a(b)(16) would provide that if (1) a card issuer imposes required fees for the issuance or availability of credit, or a security deposit, that will be charged against the card when the account is opened, and (2) the total of those fees and/or security deposit equal 25 percent or more of the minimum credit limit applicable to the card, a card issuer must disclose in the table an example of the amount of the available credit that a consumer would have remaining after these fees or security deposit are debited to the account, assuming that the consumer receives the minimum credit limit offered on the relevant account. In determining whether the 25 percent threshold test is met, the issuer must only consider fees for issuance or availability of credit, or a security deposit, that are required. If certain fees for issuance or availability are optional, these fees should not be considered in determining whether the disclosure must be given. Nonetheless, if the 25 percent threshold test is met in connection with the required fees or security deposit, the issuer must disclose the available credit after excluding any optional fees from the amounts debited to the account, and the available credit after including any optional fees in the amounts debited to the account. The Board believes that 25 percent is an appropriate threshold because it represents a significant reduction in the initial available credit as a result of the imposition of fees or security deposit. The Board solicits comment on this threshold amount.

In addition, the Board proposes comment 5a(b)(16)-1 to clarify that in calculating the amount of available credit that must be disclosed in the table, an issuer must consider all fees for the issuance or availability of credit described in § 226.5a(b)(2), and any security deposit, that will be imposed when the account is opened and charged to the account, such as one-time issuance and set-up fees that will be imposed when the card is opened. For example, in calculating the available credit, issuers must consider the first year's annual fee and the first month's maintenance fee (if applicable) if they are charged to the account immediately at account opening. Proposed Sample G-10(C) provides guidance to issuers on how to provide this disclosure. (See proposed comment 5a(b)(16)-2).

As described above, a card issuer would consider only required fees for issuance or availability of credit, or a security deposit, that will be charged against the card when the account is opened in determining whether the 25 percent threshold test is met. The Board requests comment on whether there are other fees (other than fees required for issuance or availability of credit) that are typically imposed on these types of accounts when the account is opened, and should be included in determining whether the 25 percent threshold test is met.

**5a(b)(17) Reference to Board Web Site for Additional Information**

In the December 2004 ANPR, the Board requested comment on suggestions for non-regulatory approaches that may further the Board's goal of improving the effectiveness of TILA's disclosures and substantive protections. Q57. In response to the ANPR, several commenters encouraged the Board to develop educational materials, such as pamphlets, targeted media, and interactive web sites, that could educate consumers on a variety of topics related to shopping for and using credit cards. These commenters believe that certain topics that are difficult to explain to consumers, such as balance computation methods, are better provided in educational materials than in the TILA disclosures.

The Board proposes to revise § 226.5a to require that credit card issuers must disclose in the table a reference to a Board web site and a statement that consumers can find on this web site educational materials on shopping for and using credit card accounts. See proposed § 226.5a(b)(17). Such materials would expand those already available on choosing a credit card at the Board's web site.[12] The Board recognizes that some consumers may need general education about how credit cards work and an explanation of typical account terms that apply to credit cards. In the consumer testing conducted for the Board, participants showed a wide range of knowledge about how credit cards work generally, with some participants showing a firm understanding of terms that relate to credit card accounts, while others had difficulty expressing basic financial concepts, such how the interest rate differs from a one-time fee. The Board's

[12] The materials can be found at http://www.federalreserve.gov/pubs/shop/default.htm.

current web site explains some basic financial concepts – such as what an annual percentage rate is – as well as terms that typically apply to credit card accounts. Through the web site, the Board could expand the explanation of other credit card terms, such as balance computation methods, that may be difficult to explain concisely in the disclosures given with applications and solicitations.

As part of consumer testing, participants were asked whether they would use a Board web site to obtain additional information about credit cards generally. Some participants indicated they might use the web site, while others indicated that it was unlikely they would use such a web site. Although it is hard to predict from the results of the 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 credit card and manage their account once they obtain a credit card. Thus, the Board is proposing that a reference to a Board web site be included in the table because this is a cost-effective way to provide consumers with supplemental information on credit cards. The Board seeks comments on the content for the web site.

Additional disclosures. In response to the December 2004 ANPR, several consumer groups suggested that the Board require information about the minimum payment formula, credit limit, any security interest, and all fees imposed on the account be disclosed in the table. The Board has decided not to propose this additional information in the table for the reasons detailed below.

1. Minimum payment formula. In the consumer testing conducted for the Board, participants did not tend to mention the minimum payment formula as one of the terms on which they shop for a card. In addition, minimum payment formulas used by card issuers can be complicated formulas that would be hard to describe concisely in the table. For example, while some issuers still use a percentage to calculate the payment, such as 2 percent of the outstanding balance or $10, whichever is less, other issuers use much more complicated formulas, such as "the greater of (1) $15 or (2) 2 percent of the balance or (3) the applicable finance charges, and if the finance charges are largest, add $15 to that amount." Even if the Board were to require issuers to provide an example showing the amount of the minimum payment for a certain balance (for example, $1000), this example be of doubtful usefulness for the many consumers who have balances different from the example. In addition, the example might mislead consumers, because one card might yield a lower minimum payment amount than another card for one balance (for example, $1000), but the second card might yield a lower minimum payment than the first card if the minimum payment was calculated on a different balance.

2. Credit limit. Card issuers often indicate a credit limit in a cover letter sent with an application or solicitation. Frequently, this credit limit is not stated as a specific amount but, instead, is stated as an "up to" amount, indicating the maximum credit limit for which a consumer may qualify. The actual credit limit for which a consumer qualifies depends on the consumer's creditworthiness, which is evaluated after the application or solicitation is submitted. Several consumer groups suggested that the Board include the

credit limit in the table because it is a key factor for many consumers in shopping for a credit card. These groups also suggested that the Board require issuers to state a specific credit limit, and not an "up to" amount.

The Board is not proposing to include the credit limit in the table. As explained above, in most cases, the credit limit for which a consumer qualifies depends on the consumer's creditworthiness, which is fully evaluated after the application or solicitation has been submitted. In addition, in consumer testing conducted for the Board, participants were not generally confused by the "up to" credit limit. Most participants understood that the "up to" amount on the solicitation letter was a maximum amount, rather than the amount the issuer was promising them. Almost all participants tested understood that the credit limit for which they would qualify depended on their creditworthiness, such as credit history.

3. Security interest. Several consumer groups suggested that any required security interest should be disclosed in the table. These commenters suggest that if a security interest is required, the disclosure in the table should describe it briefly, such as "in items purchased with card" or "required $200 deposit." These commenters indicated that a security deposit is a very important consideration in credit shopping, especially for low-income consumers. In addition, they stated that many credit cards issued by merchants are secured by the goods that the consumer purchases, but consumers are often unaware of the security interest.

The Board is not proposing to include a disclosure of any required security interest in the table at this time. Credit card-issuing merchants may include in their account agreements a security interest in the goods that are purchased with the card. It is not apparent that consumers would shop on whether a retail card has this type of security interest. Requiring or allowing this type of security interest to be disclosed in the table may distract from important information in the table, and contribute to "information overload." Thus, in an effort to streamline the information that may appear in the table, the Board is not proposing to include this disclosure in the table.With respect to security deposits, if a consumer is required to pay a security deposit prior to obtaining a credit card and that security deposit is not charged to the account but is paid by the consumer from separate funds, a card issuer must necessarily disclose to the consumer that a security deposit is required, so that the consumer knows to submit the deposit in order to obtain the card. A security deposit in these instances may already be sufficiently highlighted in the materials accompanying the application or solicitation, and may not need to appear in the table. Nonetheless, the Board recognizes that a security deposit may need to be highlighted when the deposit is not paid from separate funds but is charged to the account when the account is opened. In those cases, consumers may not realize that the security deposit may significantly decrease their available credit when the account is opened. Thus, as described above, the Board proposes to provide that if (1) a card agreement requires payment of a fee for issuance or availability of credit, or a security deposit, (2) the fee or security deposit will be charged to the account when it is opened, and (3) the total of those fees and security deposit equal 25 percent or more of the minimum credit limit offered with the card, the card issuer must disclose in the table an example of the amount of the available credit that a consumer would have remaining after these fees or security deposit are debited to the account, assuming that the consumer receives the minimum credit limit offered on the card.

4. Fees. In response to the December 2004 ANPR, several consumer groups suggested that all fees imposed on an account should be included in the table. They believed that by requiring only certain fees in the table, card issuers have an incentive to devise new fees that do not have to be disclosed so prominently. They indicate that if the Board excludes any fees, the list of such fees should be an exclusive list. They also suggested that the Board should require card issuers to report periodically on the volume of the excluded fees collected. If a certain type of fee increases in volume, these commenters suggested that the Board should delete this fee from the list of excluded fees on the grounds that that fee has become a more significant component of the cost of credit.

As described above, the Board is proposing to include certain transaction fees and penalty fees, such as cash advance fees, balance transfer fees, late-payment fees, and over-the-credit limit fees, in the table because these fees are frequently paid by consumers, and consumers have indicated these fees are important for shopping purposes. The Board is not proposing to include other fees in the table, such as copying fees and stop-payment fees, in the table because these fees tend to be imposed less frequently and are not fees on which consumers tend to shop. In consumer testing conducted for the Board, participants tended to mention cash advance fees, balance transfer fees, late-payment fees, and over-the-credit-limit fees as the most important fees they would want to know when shopping for a credit card. In addition, most participants understood that issuers were allowed to impose additional fees, beyond those disclosed in the table. Thus, the Board believes it is important to highlight in the table the fees that consumers want to know when shopping for a card, rather than including infrequently-paid fees, to avoid creating "information overload" such that consumers could not easily identify the fees that are most important to them. Nonetheless, the Board recognizes that fees can change over time, and the Board plans to monitor the market and update the fees required to be disclosed in the table as necessary.

**5a(c) Direct-Mail and Electronic Applications**

**5a(c)(1) General**

Electronic applications and solicitations. As discussed above, the Bankruptcy Act amends TILA Section 127(c) to require that solicitations to open a card account using the Internet or other interactive computer service must contain the same disclosures as those made for applications or solicitations sent by direct mail. 15 U.S.C. 1637(c)(7). The interim final rules adopted by the Board in 2001 revised § 226.5a(c) to apply the direct mail rules to electronic applications and solicitations. The Board proposes to retain these provisions in § 226.5a(c)(1). (Current § 226.5a(c) would be revised and renumbered as new §226.5a(c)(1).) The same proposal was included in the Board's 2007 Electronic Disclosure Proposal.

The Bankruptcy Act also requires that the disclosures for electronic offers must be "updated regularly to reflect the current policies, terms, and fee amounts." In the October 2005 ANPR, the Board also solicited comment on what guidance the Board should provide on how to apply that standard for credit card accounts. The Board's 2001 interim final rules provided guidance that disclosures for a variable-rate credit card plan provided electronically must be based on an APR in effect within the last 30 days. The 2001 guidance did not contain specific guidance on accuracy requirements for other disclosures provided electronically, such as disclosure of fees. The majority of commenters on the October 2005 ANPR which addressed the accuracy of variable rates agreed that a 30-day standard would be appropriate to implement the "updated regularly" standard in the Bankruptcy Act. Some commenters advocated longer periods such as 60 days or shorter periods such as daily or weekly updating, or suggested that the Board should not provide specific guidance or rules, instead allowing maximum flexibility in this area.

The Board proposes to revise § 226.5a(c) to implement the "updated regularly" standard in the Bankruptcy Act with regard to the accuracy of variable rates. A new § 226.5a(c)(2) would be added to address the accuracy of variable rates in direct mail and electronic applications and solicitations. This new section would require issuers to update variable rates disclosed on mailed applications and solicitations every 60 days and variable rates disclosed on applications and solicitations provided in electronic form every 30 days, and to update other terms when they change. The Board believes the 30-day and 60-day accuracy requirements for variable rates strike an appropriate balance between seeking to ensure consumers receive updated information and avoiding imposing undue burdens on creditors. The Board believes it is unnecessary for creditors to disclose to consumers the exact variable APR in effect on the date the application or solicitation is accessed by the consumer, so long as consumers understand that variable rates are subject to change. Moreover, it would be costly and operationally burdensome for creditors to comply with a requirement to disclose the exact variable APR in effect at the time the application or solicitation is accessed. The obligation to update the other terms when they change ensures that consumers receive information that is accurate and current, and should not impose significant burdens on issuers. These terms generally do not fluctuate with the market like variable rates. In addition, based on discussions with industry representatives concerning operational issues, the Board staff understands that issuers typically change other terms infrequently, perhaps once or twice a year.

Section 226.5a(c)(2) consists of two subsections. Section 226.5a(c)(2)(i) would provide that § 226.5a disclosures mailed to a consumer must be accurate as of the time the disclosures are mailed. This section would also provide that an accurate variable APR is one that is in effect within 60 days before mailing. Section 226.5a(c)(2)(ii) would provide that § 226.5a disclosures provided in electronic form (except for a variable APR) must be accurate as of the time they are sent to a consumer's e-mail address, or as of the time they are viewed by the public on a web site. For the reasons discussed above, this section would provide that a variable APR is accurate if it is in effect within 30 days before it is sent, or viewed by the public. Presently, variable APRs on most credit cards may change on a monthly basis, so a 30-day accuracy requirement for variable APRs appears appropriate.

Many of the provisions included in proposed § 226.5a(c)(2) have been incorporated from current § 226.5a(b)(1). To eliminate redundancy, the Board proposes to revise § 226.5a(b)(1) by deleting § 226.5a(b)(1)(ii), § 226.5a(b)(1)(iii), and comment 5a(c)-1. The same revisions were included in the Board's 2007 Electronic Disclosure Proposal.

**5a(d) Telephone Applications and Solicitations**

**5a(d)(2) Alternative Disclosure**

Section 226.5a(d) specifies rules for providing cost disclosures in oral applications and solicitations initiated by a card issuer. Card issuers generally must provide certain cost disclosures during the oral conversation in which the application or solicitation is given. Alternatively, an issuer is not required to give the oral disclosures if the card issuer either does not impose a fee for the issuance or availability of a credit card (as described in § 226.5a(b)(2)) or does not impose such a fee unless the consumer uses the card, provided that the card issuer provides the disclosures later in a written form. Specifically, the issuer must provide the disclosures required by § 226.5a(b) in a tabular format in writing within 30 days after the consumer requests the card (but in no event later than the delivery of the card), and disclose the fact that the consumer need not accept the card or pay any fee disclosed unless the consumer uses the card. The Board proposes to add comment 5a(d)-2 to indicate that an issuer may disclose in the table that the consumer is not required to accept the card or pay any fee unless the consumer uses the card.

**5a(d)(3) Accuracy**

Proposed § 226.5a(d)(3) would provide guidance on the accuracy of telephone disclosures. Current comment 5a(b)(1)-3 specifies that for variable-rate disclosures in telephone applications and solicitations, the card issuer must provide the rates currently applicable when oral disclosures are provided. For the alternative disclosures under § 226.5a(d)(2), an accurate variable APR is one that is (1) in effect at the time the disclosures are mailed or delivered; (2) in effect as of a specified date (which rate is then updated from time to time, for example, each calendar month); or (3) an estimate in accordance with § 226.5(c). Current comment 5a(b)(1)-3 would be moved to § 226.5a(d)(3), except that the option of estimating a variable APR would be eliminated as the least meaningful of the three options. Proposed § 226.5a(d)(3) also would specify that if an issuer discloses a variable APR as of a specified date, the issuer must update the rate on at least a monthly basis, the frequency with which variable rates on most credit card products are adjusted. The Board also would amend proposed § 226.5a(d)(3) to specify that oral disclosures under § 226.5a(d)(i) must be accurate when given, consistent with the requirement in § 226.5(c) that disclosures must reflect the terms of the legal obligation between the parties. For the alternative disclosures, terms other than variable APRs must be accurate as of the time they are mailed or delivered. See proposed § 226.5a(d)(3).

**5a(e) Applications and Solicitations Made Available to General Public**

TILA Section 127(c)(3) and § 226.5a(e) specify rules for providing disclosures in applications and solicitations made available to the general public such as "take-one" applications and catalogs or magazines. 15 U.S.C. 1637(c)(3). These applications and solicitations must either contain: (1) the disclosures required for direct mail applications and solicitations, presented in a table; (2) a narrative that describes how finance charges and other charges are assessed; or (3) a statement that costs are involved, along with a toll-free telephone number to call for further information.

Narrative that Describes How Finance Charges and Other Charges Are Assessed. TILA Section 127(c)(3)(D) and § 226.5a(e)(2) allow issuers to meet the requirements of § 226.5a for take-one applications and solicitations by giving a narrative description of certain account-opening disclosures (such as information about how finance charges and other charges are assessed), a statement that the consumer should contact the card issuer for any change in the required information, and a toll-free telephone number or a mailing address for that purpose. 15 U.S.C. 1637(c)(3)(D). Currently, this information does not need to be in the form of a table, but may be a narrative description, as is also currently allowed for account-opening disclosures. The Board is proposing, however, to require that certain account-opening information (such as information about key rates and fees) must be given in the form of a table. See the section-by-section analysis to § 226.6(b)(4). Therefore, the Board also is proposing that card issuers give this same information in a tabular form in take-one applications and solicitations. Thus, the Board proposes to delete § 226.5a(e)(2) and comments 5a(e)(2)-1 and -2 as obsolete. Card issuers that provide cost disclosures in take-one applications and solicitations would be required to provide the disclosures in the form of a table, for which they could use the account-opening summary table. See § 226.5a(e)(1) and comment 5a-2.

**5a(e)(4) Accuracy**

For applications or solicitations that are made available to the general public, if a creditor chooses to provide the cost disclosures, § 226.5a(b)(1)(ii) currently requires that any variable APR disclosed must be accurate within 30 days before printing. The proposal would move this provision to § 226.5a(e)(4). Proposed § 226.5a(e)(4) also would specify that other disclosures must be accurate as of the date of printing.

**5a(f) In-Person Applications and Solicitations**

Card issuer and person extending credit are not the same. Existing § 226.5a(f) and its accompanying commentary contain special charge card rules that address circumstances in which the card issuer and the person extending credit are not the same person. (These provisions implement TILA Section 127(c)(4)(D), 15 U.S.C. 1637(c)(4)(D).) The Board understands that these types of cards are no longer being offered. Thus, the Board proposes to delete these provisions and the Model Clause G-12 from Regulation Z as obsolete, recognizing that the statutory provision in TILA Section 127(c)(4)(D) will remain in effect if these products are offered in the future. The Board requests comment on whether these provisions should be retained in the regulation. A commentary provision referencing the statutory provision would be added to § 226.5(d), which addresses disclosure requirements for multiple creditors. See proposed comment 5(d)-3.

In-person applications and solicitations. The Board is proposing a new § 226.5a(f) and accompanying commentary to address in-person applications and solicitations initiated by the card issuer. In in-person applications, a card issuer initiates a conversation with a consumer inviting the consumer to apply for a card account, and if the consumer responds affirmatively, the issuer takes application information from the consumer. For example, in-person applications include instances in which a retail employee, in the course of processing a sales transaction using the customer's bank credit card, invites the customer to apply for the retailer's credit card and the customer submits an application.

In in-person solicitations, a card issuer offers a consumer in-person to open an account that does not require an application. For example, in-person solicitations include instances where a bank employee offers a preapproved credit card to a consumer who came into the bank to open a checking account.

Currently, in-person applications in response to an invitation to apply are exempted from § 226.5a because they are considered applications initiated by consumers. (See current comments 5a(a)(3)-2 and 5a(e)-2.) On the other hand, in-person solicitations are not specifically addressed in § 226.5a. Neither in-person applications nor solicitations are specifically addressed in TILA.

The Board proposes to cover in-person applications and solicitations under § 226.5a, pursuant to the Board's authority under TILA Section 105(a). Requiring in-person applications and solicitations to include credit terms under § 226.5a could help serve TILA's purpose to provide meaningful disclosure of credit terms so that consumers will be able to compare more readily the various credit terms available to him or her, and avoid the uninformed use of credit. 15 U.S.C. 1601(a). Also, the Board understands that card issuers routinely provide § 226.5a disclosures in these circumstances; therefore, any additional compliance burden would be minimal.

Card issuers must provide the disclosures required by § 226.5a in the form of a table, and those disclosures must be accurate when given (consistent with the direct mail rules) or when printed (consistent with one option for the take-one rules). See § 226.5a(c), (e)(1). These two alternatives appear to provide issuers flexibility, while also providing consumers with the information they need to make informed credit decisions. Existing comment 5a(a)(3)-2 (which would be moved to comment 5a(a)(5)-1) and comment 5a(e)-2 would be revised to be consistent with § 226.5a(f).

**5a(g) Balance Computation Methods Defined**

TILA Section 127(c)(1)(A)(iv) calls for the Board to name not more than five of the most common balance computation methods used by credit card issuers to calculate the balance on which finance charges are computed. 15 U.S.C. 1637(c)(1)(A)(iv). If issuers use one of the balance computation methods named by the Board, the issuer must disclose that name of the balance computation method as part of the disclosures required by § 226.5a, and is not required to provide a description of the balance computation method. If the issuer uses a balance computation method that is not named by the Board, the issuer must disclose a detailed explanation of the balance computation method. See current § 226.5a(b)(6). Currently, the Board has named four balance computation methods: (1) average daily balance (including new purchases) or (excluding new purchases); (2) two-cycle average daily balance (including new purchases) or (excluding new purchases); (3) adjusted balance; and (4) previous balance. The Board proposes to retain these four balance computation methods. The Board requests comment on whether the list should be revised, along with data indicating why.

**Section 226.6 Account-opening Disclosures**

TILA Section 127(a), implemented in § 226.6, requires creditors to provide information about key credit terms before an open-end plan is opened, such as rates and fees that may be assessed on the account. Consumers' rights and responsibilities in the case of unauthorized use or billing disputes are also explained. 15 U.S.C. 1637(a). See also Model Forms G-2 and G-3 in Appendix G.

Home-equity lines of credit. Account-opening disclosure and format requirements for home-equity lines of credit (HELOCs) subject to § 226.5b would be unaffected by the proposal, consistent with the Board's plan to review Regulation Z's disclosure rules for home-secured credit in a separate rulemaking. To facilitate compliance, the substantively unrevised rules applicable only to HELOCs are grouped together in proposed § 226.6(a), including rules relating to the disclosure of finance charges, other charges, and specific HELOC-related disclosures. (See redesignation table below.) For the reasons set forth in the section-by-section analysis to § 226.6(b)(1), the Board would update references to "free-ride period" as "grace period" in the regulation and commentary, without any intended substantive change.

Open-end (not home-secured) plans. The Board proposes two significant revisions to account-opening disclosures for open-end (not home-secured) plans, which are set forth in proposed § 226.6(b). The rule would (1) require a tabular summary of key terms to be provided before an account is opened (see proposed § 226.6(b)(4)), and (2) reform how and when cost disclosures must be made (see proposed § 226.6(b)(1) for content, § 226.5(b) and § 226.9(c) for timing). The Board proposes to apply the tabular summary requirement to all open-end loan products, except HELOCs. Such products include credit card accounts, traditional overdraft credit plans, personal lines of credit, and revolving plans offered by retailers without a credit card. The benefit to consumers from receiving a concise summary of rates and important fees appears to outweigh the costs, such as developing the new disclosures and revising them as needed.

Disclosure requirements in § 226.6 that potentially affect all open-end creditors, namely rules relating to security interests and billing error disclosure requirements, are grouped together in proposed § 226.6(c). The section also would be retitled "Account-opening disclosures" to more accurately reflect the timing of the disclosures. In today's marketplace, there are few open-end products for which consumers receive the disclosures required under § 226.6 as their "initial" Truth in Lending disclosure. See § 226.5a, § 226.5b. The substance of footnotes 11 and 12 is moved to the regulation; the substance of footnote 13 is moved to the commentary. (See redesignation table below.)

In technical revisions, comments 6-1 and 6-2 would be deleted. The substance of comment 6-1, which requires consistent terminology, is discussed more generally in proposed § 226.5(a)(2). Comment 6-2 addresses certain open-end plans involving more than one creditor, and is proposed to be deleted as obsolete. See section-by-section analysis to § 226.5a(f).

Tabular summary. As provided by Regulation Z, creditors may, and typically do, include account-opening disclosures as a part of an account agreement document that also contains other contract terms and state-law disclosures. The agreement is typically lengthy and in small print. In the December 2004 ANPR, the Board sought comment on possible approaches to ease consumers' ability to navigate account-opening disclosures, such as a summary paragraph, a table similar to the one required on or with credit and charge card applications, or a table of contents to highlight key features and terms of the account. Q2 – Q3.

Commenters generally encouraged the Board to consider format rules that focus on providing essential terms in a simplified way. In general, commenters suggested that a summary of key terms would improve the effectiveness of the now-lengthy and complex account agreement documents. Some industry commenters, however, opposed a summary. These commenters noted that the current format rules integrating account terms and TILA disclosures allow creditors to explain features coherently, and noted that summarizing information and repeating it in detail in the contract document may result in information overload. As a part of consumer research conducted for the Board regarding consumer understanding of current TILA disclosures, tests simulated consumers' review of packets of information typically received when new accounts are opened. Most of the consumers in the Board's sample group set aside the lengthy multi-fold account agreement pamphlets without reading them, saying they were too long, the type was too small, and the language too legalistic. Consumers who reviewed packets that included a summary of account terms generally noticed and reviewed the summary, even if they set aside the contract document.

Based on public comment, consumer testing, and its own analysis, the Board is proposing to introduce format requirements for account-opening disclosures for open-end (not home-secured) plans. The Board proposes to summarize key information most important to informed decision-making in a table similar to that required on or with credit and charge card applications and solicitations. The proposal would permit TILA disclosures that are typically lengthy or complex and less-often used in determining how to use an account, such as how variable rates are determined, to be integrated with the account agreement terms. The content requirements for the proposed summary are set forth in new § 226.6(b)(4) and are discussed below; proposed Model Form G-17(A) and Samples G-17(B) and G-17(C) in Appendix G illustrate the table.

Charges imposed as part of the plan. The Board proposes to reform its rules regarding cost disclosures provided at account opening for open-end (not home-secured) plans. Under TILA and current Regulation Z, account-opening disclosures must include charges that are either a "finance charge" or an "other charge" (TILA charges). According to TILA, a charge is a finance charge if it is payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor "as an incident to the extension of credit." The Board implemented the definition by including as a finance charge under Regulation Z, any charge imposed "as an incident to or a condition of the extension of credit." TILA also requires a creditor to disclose, before opening an account, "other charges which may be imposed as part of the plan . . . in accordance with regulations of the Board." The Board implemented the provision virtually verbatim, and the staff commentary interprets the provision to cover "significant charges related to the plan." 15 U.S.C. 1605(a), § 226.4; 15 U.S.C. 1637(a)(5), § 226.6(b), current comment 6(b)-1.

The terms "finance charge" and "other charge" are given broad and flexible meanings in the regulation and commentary. This ensures that TILA adapts to changing conditions, but it also creates uncertainty. The distinctions among finance charges, other charges, and charges that do not fall into either category are not always clear. As creditors develop new kinds of services, some find it difficult to determine if associated charges for the new services meet the standard for a "finance charge" or "other charge" or are not covered by TILA at all. This uncertainty can pose legal risks for creditors that act in good faith to classify fees. Examples of charges that are included or excluded charges are in the regulation and commentary, but they cannot provide definitive guidance in all cases.

A 2003 rulemaking concerning charges for two services—expediting payments and expediting card delivery—illustrates the challenges in applying current rules. 68 FR 16,185; April 3, 2003. Public comments on the proposal reflected a lack of consensus about the proposed interpretations of expedited payment fee as an "other charge" and expedited card delivery fee as not covered by TILA. More broadly, the comments reflected a lack of consensus over the basic principles that should determine whether a charge is a finance charge or an "other charge."

In the final rule, staff adopted official interpretations indicating that neither charge was a charge covered by TILA. In the supplementary information accompanying the final rule, Board staff recognized that requiring a written disclosure of a charge for a service long before the consumer might consider purchasing the service did not provide the consumer with any material benefit. The staff also noted creditors' current practice of disclosing the charge when the service is requested, and encouraged the continuation of that practice.

Board staff also indicated that a more comprehensive review of existing rules was needed. Accordingly, the December 2004 ANPR solicited comment on the effectiveness of the rules governing disclosure of charges covered by TILA, and on potential alternatives. The comments indicated a consensus that the current approach should be replaced with a new one. Commenters split, however, on the proper approach. Most focused on the definition of "finance charge" or "other charge." Approaches ranged from industry's suggestions to restrict finance charges to interest or to charges required as a condition to the extension of credit, to consumer groups' suggestion to include virtually all charges the consumer would pay. While commenters disagreed over which approach would best serve TILA's purposes, they shared a common objective: provide a clear test.

In light of the comments received, consumer testing, and the Board's experience and analysis, the Board is proposing to reform the rules governing disclosure of charges before they are imposed, as discussed below. The proposed rule is intended to respond collectively to these concerns by (1) giving full effect to TILA's requirement that all charges imposed as part of an open-end (not home-secured) plan be disclosed before they are imposed, (2) specifying precisely important costs that must be disclosed in writing at account opening (e.g., interest rates, annual fees, and late-payment or over-the-credit-limit fees), and (3) permitting the creditor to disclose all other charges imposed as part of the plan (e.g., fees to expedite payments or to provide an additional card) at account opening <u>or</u> orally at any time before the consumer agrees to or becomes obligated to pay the charge. Charges added or increased during the life of the plan would be subject to similar rules. <u>See</u> § 226.9(c)(2).

Under the proposal, some charges would be covered by TILA that the current regulation, as interpreted by the staff commentary, excludes from TILA coverage, such as fees for expedited payment and expedited delivery. It may not have been useful to consumers to cover such charges under TILA when such coverage would have meant only that the charges were disclosed long before they became relevant to the consumer. It may, however, be useful to cover such charges under TILA as part of a rule that permits their disclosure at a (later) more relevant time. Further, as new services (and associated charges) are developed, the proposal is intended to reduce uncertainty of how to disclose such fees and risks of civil liability. The list of charges creditors must disclose in the account-opening table would be specific and exclusive, not open-ended as is the case today. Creditors could otherwise comply with the rule by disclosing other costs at any other relevant time.

**<u>6(a) Rules Affecting Home-equity Plans</u>**

For the reasons discussed above and as illustrated in the redesignation table below, the proposal would set forth in § 226.6(a) all requirements applying exclusively to home-equity plans subject to § 226.5b (HELOCs). Rules relating to the disclosure of finance charges currently in § 226.6(a)(1) through (4) would be moved to proposed § 226.6(a)(1)(i) through (iv); those rules and accompanying official staff interpretations are substantively unchanged. Rules relating to the disclosure of other charges would be moved from current § 226.6(b) to proposed § 226.6(a)(2), and specific HELOC-related disclosure requirements would be moved from current § 226.6(e) to proposed § 226.6(a)(3). Several technical revisions to commentary provisions are proposed for clarity and in some cases for consistency with corresponding comments to proposed § 226.6(b)(2), which addresses rate disclosures for open-end (not home-secured) plans, but these revisions are not intended to be substantive. <u>See</u>, for example, proposed comments 6(a)(1)(ii)-1 and 6(b)(2)(i)(B)-1, which address disclosing ranges of balances. Also, commentary provisions that currently apply to open-end plans generally but are inapplicable to HELOCs would not moved. For example, guidance in current 6(a)(2)-2 regarding a creditor's general reservation of the right to change terms would not be moved to proposed comment 6(a)(1)(ii)-2, because § 226.5b(f)(1) prohibits "rate-reservation" clauses for HELOCS. Comment 6-1, which addresses the need for consistent terminology with periodic statement disclosures, would be deleted as duplicative. See proposed § 226.5(a)(2)(i).

**6(b) Rules Affecting Open-end (not Home-secured) Plans**

**6(b)(1) Charges Imposed as Part of Open-end (not Home-secured) Plans**

Proposed § 226.6(b)(1) would apply to all open-end plans except HELOCs subject to § 226.5b. It retains TILA's general requirements for disclosing costs for open-end plans: Creditors would be required to continue to disclose the circumstances under which charges are imposed as part of the plan, including the amount of the charge (e.g., $3.00) or an explanation of how the charge is determined (e.g., 3 percent of the transaction amount). For finance charges, creditors must include a statement of when the finance charge begins to accrue and an explanation of whether or not a "grace period" or "free-ride period" exists (a period within which any credit that has been extended may be repaid without incurring the charge). Regulation Z generally refers to this period as a "free-ride period." Since 1989, creditors have been required to use the term "grace period" in complying with disclosure requirements for credit and charge card applications and solicitations in § 226.5a. 15 U.S.C. 1632(c)(2)(C); current § 226.5a(a)(2)(iii); 54 FR 13,856; April 6, 1989. For consistency and the reasons set forth in the section-by-section analysis to § 226.6(b)(1), the Board would update references to "free-ride period" as "grace period" in the regulation and commentary, without any intended substantive change.

Currently, the rules for disclosing costs related to open-end plans create two categories of charges covered by TILA: finance charges (§ 226.6(a)) and "other charges" (§ 226.6(b)). Under the proposal, the rules would create a single category of "charges imposed as part of an open-end (not home-secured) plan" as identified in proposed § 226.6(b)(1)(i). This new section would identify a complete description of the types of charges that would be considered to be imposed as part of a plan. These charges include finance charges under § 226.4(a) and (b), penalty charges, taxes, and charges for voluntary credit insurance, debt cancellation or debt suspension coverage.

Charges to be disclosed would also include any charge the payment, or nonpayment of which affects the consumer's access to the plan, duration of the plan, the amount of credit extended, the period for which credit is extended, and the timing or method of billing or payment. This proposed provision is intended to be broad but provide greater clarity than current rules and capture charges that relate to the key attributes of a credit plan. The proposed commentary would provide examples of charges covered by the provision, such as application fees and participation fees (which affect access to the plan), fees to expedite card delivery (which also affect access to the plan), and fees to expedite payment (which affect the timing and method of payment). See proposed comment 6(b)(1)(i)-2.

Three examples of types of charges that are not imposed as part of the plan are listed in proposed § 226.6(b)(1)(ii). These examples include charges imposed on a cardholder by an institution other than the card issuer for the use of the other institution's ATM; and charges for a package of services that includes an open-end credit feature, if the fee is required whether or not the open-end credit feature is included and the non-credit services are not merely incidental to the credit feature. Comment 6(b)(1)(ii)-1 provides examples of fees for packages of services that are considered to be imposed as part of the plan and fees for packages of services that are not. This comment is substantively identical to current comment 6(b)-1.v.

The proposal would not completely eliminate ambiguity about what are TILA charges. To mitigate ambiguity, however, the proposal provides a complete list in new § 226.6(b)(4) of which charges identified under § 226.6(b)(1) must be disclosed in writing at account opening (or before they are increased or newly introduced). See proposed § 226.5(b)(1) and § 226.9(c)(2) for timing rules. Any fees aside from those identified in proposed § 226.6(b)(4) would not be required to be disclosed in writing at account opening. However, other charges imposed as part of an open-end (not home-secured) plan may be disclosed at account opening, or orally at any relevant time before the consumer agrees to or becomes obligated to pay the charge. This approach is intended in part to reduce creditor burden. Creditors presumably disclose fees at relevant times, such as when a consumer orders a service by telephone, for business reasons and to comply with other state and federal laws. Moreover, compared to the approach reflected in the current regulation, the proposed broad application of the statutory standard of fees "imposed as part of the plan" should make it easier for a creditor to determine whether a fee is a charge covered by TILA, and reduce litigation and liability risks. In addition, this approach will help ensure that consumers receive the information they need when it would be most helpful to them.

**6(b)(2) Rules Relating to Rates for Open-end (not Home-secured) Plans**

Rules for disclosing rates that affect the amount of interest that will be imposed would be reorganized and consolidated in proposed § 226.6(b)(2). (See redesignation table below.)

**6(b)(2)(i)**

Finance charges attributable to periodic rates. Currently, creditors must disclose finance charges attributable to periodic rates. These costs are typically interest but may include other costs such as premiums for required credit insurance. As discussed earlier, in consumer testing for the Board, participants understood credit costs in terms of interest and fees. The text of proposed § 226.6(b)(2)(i) reflects the Board's intention to make the distinction between interest and fees clear.

Balance computation methods. Proposed § 226.6(b)(2)(i) sets forth rules relating to the disclosure of rates. Proposed § 226.6(b)(2)(i)(D) (currently § 226.6(a)(3)) requires creditors to explain the method used to determine the balance to which rates apply. 15 U.S.C. 1637(a)(2). Model Clauses that explain commonly used methods, such as the average daily balance method, are at Appendix G-1. The Board requests comment on whether model clauses for methods such as "adjusted balance" and previous balance" should be deleted as obsolete, and more broadly, whether G-1 should be eliminated entirely because creditors no longer use the model clauses.

In the December 2004 ANPR, the Board sought comment on how significantly the choice of a balance computation method might affect consumers' cost of credit, and on possible ways to enhance the effectiveness of any required disclosure. Q28 – Q30. Commenters acknowledged that balance computation methods can affect consumers' cost of credit but in general would favor an approach that emphasizes other key cost terms instead of the details of balance computation methods. The Board concurs with these views.

Calculating balances on open-end plans can be complex, and requires an understanding of how creditors allocate payments, assess fees, and record transactions as they occur during a billing cycle. Currently, neither TILA nor Regulation Z requires creditors to disclose all the information necessary to compute balances to which periodic rates are applied, and requiring that level of detail would not appear to benefit consumers because consumers are unlikely to review such detailed information. Although the Board's model clauses are intended to assist creditors in explaining common methods, consumers continue to find explanations in account agreements to be lengthy and complex, and are not understood. The proposal would require creditors to continue to explain the balance computation methods in the account-opening agreement, but the explanation would not be permitted in the account-opening summary. As discussed below, along with the account-opening summary proposed in § 226.6(b)(4), creditors would name the balance computation method and refer consumers to the account-opening disclosures for an explanation of the balance computation method.

**6(b)(2)(ii)**

New § 226.6(b)(2)(ii) would set forth the rules for variable-rate disclosures now contained in footnote 12. In addition, guidance on the accuracy of variable rates provided at account opening would be moved from the commentary to the regulation, and revised. Currently, comment 6(a)(2)-3 provides that creditors may provide the current rate, a rate as of a specified date if the rate is updated from time to time, or an estimated rate under § 226.5(c). The Board proposes an accuracy standard that is consistent with the Board's 2007 Electronic Disclosure Proposal; that is, the rate disclosed is accurate if it was in effect as of a specified date within 30 days before the disclosures are provided. See 72 FR 21,1141; April, 30, 2007. The proposal would eliminate creditors' option to provide an estimate as the rate in effect for a variable-rate account. The Board believes creditors are provided with sufficient flexibility under the proposal to provide a rate as of a specified date, so the use of an estimate would not be appropriate. New proposed comment 6(b)(2)(ii)-5, which addresses discounted variable-rate plans and is substantively unchanged from current comment 6(a)(2)-10, contains technical revisions.

The Board also proposes to require that, in describing how a variable rate is determined, creditors must disclose the applicable margin, if any. See proposed § 226.6(b)(2)(ii)(B). Creditors state the margin for purposes of contract or other law and are currently required to disclose margins related to penalty rates, if applicable. No particular format requirements would apply. Thus, the Board does not expect the revision would add burden.

**6(b)(2)(iii)**

New § 226.6(b)(2)(iii) would consolidate existing rules for rate changes that are specifically set forth in the account agreement but are not due to changes in an index or formula, such as rules for disclosing introductory and penalty rates. In addition to identifying the circumstances under which a rate may change (such as the end of an introductory period or a late payment), creditors would be required to disclose how existing balances would be affected by the new rate. The proposed change is intended to improve consumer understanding as to whether a penalty rate triggered by, for example, a late payment would apply not only to outstanding balances for purchases but to existing balances that were transferred at a low promotional rate. If the increase in rate is due to an increased margin, creditors must disclose the increase; the highest margin can be stated if more than one might apply. See proposed comment 6(b)(2)(iii)-2.

**6(b)(3) Voluntary Credit Insurance; Debt Cancellation or Suspension**

As discussed in the section-by-section analysis to § 226.4, the Board is proposing revisions to the requirements to exclude charges for voluntary credit insurance or debt cancellation or debt suspension coverage from the finance charge. See proposed § 226.4(d). Creditors must provide information about the voluntary nature and cost of the credit insurance or debt cancellation or suspension product, and about the nature of coverage for debt suspension products. Because creditors must obtain the consumer's affirmative request for the product as a part of the disclosure requirements, the Board expects the disclosures proposed under § 226.4(d) will be provided at the time the product is offered to the consumer. Thus, consumers may receive the disclosures at the time they open an open-end account, or earlier in time, such as at application.

**6(b)(4) Tabular Format Requirements for Open-end (not Home-secured) Plans**

Proposed § 226.6(b)(4) would introduce format requirements for account-opening disclosures for open-end (not home-secured) plans. The proposed summary of account-opening disclosures is based on the format and content requirements for the tabular disclosures provided with direct mail applications for credit and charge cards under § 226.5a, as it would be revised under the proposal. Proposed forms under G-17 in Appendix G illustrate the account-opening tables. As proposed, comment 6(b)(4)-1 would refer generally to guidance in § 226.5a regarding format and disclosure requirements for the application and solicitation table. For clarity, rules under § 226.5a that do not apply to account-opening disclosures are specifically noted. Comment is requested on this approach, or whether importing essentially identical guidance from § 226.5a to § 226.6 would ease compliance.

Rates. Proposed § 226.6(b)(4)(ii) sets forth disclosure requirements for rates that would apply to accounts. Periodic rates and index and margin values would not be permitted to be disclosed in the table, for the same reasons underlying, and consistent with, the proposed requirements for the table provided with credit card applications and solicitations. See comment 6(b)(4)(ii)-1. Creditors would continue to disclose periodic rates, and index and margin values as part of the account opening disclosures, and these could be provided in the credit agreement, as is likely currently the case.

The rate disclosures required for the account-opening table differ from those required for the table provided with credit card applications and solicitations. For applications and solicitations, creditors may provide a range of APRs or specific APRs that may apply, where the APR is based on a later determination of the consumer's creditworthiness. At account opening, creditors must disclose the specific APRs that will apply to the account.

Fees. Fees that would be highlighted in the account-opening summary are identified in § 226.6(b)(4)(iii). The Board believes that these fees, among the charges that TILA covers, are the most important fees, at least in the current marketplace, for consumers to know about before they start to use an account. They include charges that the consumer could incur without creditors otherwise being able to disclose the cost in advance of the consumers' act that triggers the cost, such as fees triggered by a consumer's use of a cash advance check or by a consumers' late payment. Transaction fees imposed for transactions in a feign currency or that take place in a foreign country would be among the fees disclosed at account opening, though the Board is not proposing to require that foreign transaction fees be disclosed in the table provided with credit card applications and solicitations. See section-by-section analysis to § 226.5a(b)(4). Although consumer testing for the Board indicated that consumers do not choose to apply for a card based on foreign transaction fees, the Board believes highlighting the fee may be useful for some consumers before they obtain credit on the account.

The Board intends this list of fees to be exclusive, for two reasons. An exclusive list eases compliance and reduces the risk of litigation; creditors have the certainty of knowing that as new services (and associated fees) develop, the new fees need not be highlighted in the account-opening summary unless and until the Board requires their disclosure after notice and public comment. And as discussed in the section-by-section analysis to § 226.5(a)(1) and § 226.5(b)(1), charges required to be highlighted under new § 226.6(b)(4) would have to be provided in a written and retainable form before the first transaction and before being increased or newly introduced. Creditors would have more flexibility regarding disclosure of other charges imposed as part of an open-end (not home-secured) plan.

The exclusive list of fees also benefits consumers. The list focuses on fees consumer testing conducted for the Board showed to be most important to consumers. The list is manageable and focuses on key information rather than attempting to be comprehensive. Since all fees imposed as part of the plan must be disclosed before the cost is incurred, not all fees need to be included in the table.

The Board notes that if the amount of a fee such as a late-payment fee or balance transfer fee varies from state to state, for disclosures required to be provided with credit card applications and solicitations, card issuers may disclose a range of fees and a statement that the amount of the fee varies from state to state. See existing § 226.5a(a)(5), renumbered as new § 226.5a(a)(4). A goal of the proposed account-opening summary table is to provide to a consumer with key information about the terms of the account. Permitting creditors to disclose a range of fees seems not to meet that standard. Nonetheless, the Board solicits comment on whether there are any operational issues presented by the proposed rule to disclose fees applicable to the consumer's account in the account-opening summary table, and if so, suggested solutions.

Grace period. Under TILA, creditors providing disclosures with applications and solicitations must discuss grace periods on purchases; at account opening, creditor must explain grace periods more generally. 15 U.S.C. 1637(c)(1)(A)(iii); 15 U.S.C. 1637(a)(1). Under proposed § 226.6(b)(4)(iv), creditors would state for all balances on the account, whether or not a period exists in which consumers may avoid the imposition of finance charges, and if so, the length of the period.

Required insurance, debt cancellation or debt suspension. For the reasons discussed in the section-by-section analysis to § 226.5a(b)(14), as permitted by applicable law, creditors that require credit insurance, or debt cancellation or debt suspension coverage, as part of the plan would be required to disclose the cost of the product and a reference to the location where more information about the product can be found with the account-opening materials, as applicable. See proposed § 226.6(b)(4)(v).

Payment allocation. In the December 2004 ANPR, the Board asked about creditors' payment allocation methods, how the methods are typically disclosed, and whether additional disclosures about payment allocation should be required. Q34 – Q36. Responses suggest that in general, creditors tend to apply consumers' payments to satisfy low-rate balances first, but that payment allocation methods vary. The timing and detail of disclosures also vary. Some card issuers disclose their payment allocation policies in materials accompanying credit card applications, while others provide information as part of the account agreement. Descriptions of payment allocation are typically general.

The Board proposes in § 226.6(b)(4)(vi) to require creditors to disclose, if applicable, the information proposed to be required with credit card applications and solicitations regarding how payments will be allocated if the consumer transfers balances at a low rate and then makes purchases on the account. The Board believes the information is useful to the consumer, although perhaps more so at the time of application when consumers may establish an account to take advantage of a promotional balance transfer rate. Because the Board is proposing to allow the account-opening table to substitute for the table given with an application or solicitation, the Board proposes also to include the payment allocation disclosure in the account-opening summary, to ensure that consumers receive this information, if applicable, at the time of application or solicitation.

Available credit. For the reasons discussed under § 226.5a(b)(16), the Board proposes a disclosure targeted at subprime card accounts that assess substantial fees at account opening and leave consumers with a limited amount of available credit. Proposed § 226.6(b)(4)(vii) would require creditors to disclose in the account-opening table the disclosures required under § 226.5a(b)(16). The proposed requirements would apply to creditors that require fees for the availability or issuance of credit, or a security deposit, that equals 25 percent or more of the minimum credit limit offered on the account. If that threshold is met, card issuers must disclose in the table an example of the amount of available credit the consumer would have after the fees or security deposit are debited to the account, assuming the consumer receives the minimum credit limit.

Web site reference. For the reasons stated under § 226.5a(b)(17), credit card issuers would be required under proposed § 226.6(b)(4)(viii) to provide a reference to the Board's web site for additional information about shopping for and using credit card accounts.

Balance computation methods. TILA requires creditors to explain as part of the account-opening disclosures the method used to determine the balance to which rates are applied. 15 U.S.C. 1637(a)(2). Explaining balance computation methods in the account-opening table may not benefit consumers, because the explanations can be lengthy and complex, and consumer testing indicates the explanations are not understood. Including an explanation in the table also may undermine the goal of presenting essential information in a simplified way. Nonetheless, some balance computation methods are more favorable to consumers than others, and the Board believes it is appropriate to highlight the method used, if not the technical computation details. For those reasons, the Board proposes that the name of balance computation methods used be disclosed beneath the table, along with a statement that an explanation of the method is provided in the account agreement or disclosure statement. See proposed § 226.6(b)(4)(ix). To determine the name of the balance computation method to be disclosed, creditors would refer to § 226.5a(g) for a list of commonly-used methods; if the method used is not among those identified, creditors would provide a brief explanation in place of the name.

Billing error rights reference. All creditors offering open-end plans must provide notices of billing rights at account opening. See current § 226.6(d); proposed § 226.6(c)(2). This information is important, but lengthy. The Board proposes to draw consumers' attention to the notices by requiring a statement that information about billing rights and how to exercise them is provided in the account-opening disclosures. See proposed § 226.6(b)(4)(x). The statement, along with the name of the balance computation method, would be located directly below the table.

## 6(c) Rules of General Applicability

### 6(c)(1) Security Interests

Comments to proposed § 226.6(c)(1) (current § 226.6(c)) are revised for clarity, without any substantive change.

**<u>6(c)(2) Statement of Billing Rights</u>**

Creditors offering open-end plans must provide information to consumers at account opening about consumers' billing rights under TILA, in the form prescribed by the Board. 15 U.S.C. 1637(a)(7). This requirement is implemented in the Board's Model Form G-3. The Board is proposing revisions to Model Form G-3, proposed as G-3(A). The proposed revisions are not based on consumer testing, although design techniques and changes in terminology are proposed to improve consumer understanding of TILA's billing rights. Creditors offering HELOCs subject to § 226.5b could continue to use current Model Form G-3, or proposed G-3(A), at the creditor's option.

**<u>Section 226.7 Periodic Statement</u>**

TILA Section 127(b), implemented in § 226.7, identifies information about an open-end account that must be disclosed when a creditor is required to provide periodic statements. 15 U.S.C. 1637(b).

<u>Home-equity lines of credit</u>. Periodic statement disclosure and format requirements for home-equity lines of credit (HELOCs) subject to § 226.5b would be unaffected by the proposal, consistent with the Board's plan to review Regulation Z's disclosure rules for home-secured credit in a separate rulemaking. To facilitate compliance, the substantively unrevised rules applicable only to HELOCs are grouped together in proposed § 226.7(a). (<u>See</u> redesignation table below.)

<u>Open-end (not home-secured) plans</u>. The Board proposes a number of significant revisions to periodic statement disclosures for open-end (not home-secured) plans. These rules are grouped together in proposed § 226.7(b). First, interest and fees imposed as part of the plan during the statement period would be disclosed in a simpler manner and in a consistent location. Second, the Board is proposing for comment two alternative approaches to disclose the effective APR: The first approach would try to improve consumer understanding of this rate and reduce creditor uncertainty about its computation. The second approach would eliminate the requirement to disclose the effective APR. Third, if an advance notice of changed rates or terms is provided on or with a periodic statement, a summary of the change would be required on the front of the periodic statement. Model clauses would illustrate the proposed revisions, to facilitate compliance. In addition, the Board proposes to add new paragraphs § 226.7(b)(11) and (12) to implement disclosures regarding late-payment fees and the effects of making minimum payments in Section 1305(a) and 1301(a) of the Bankruptcy Act (further discussed below). TILA Section 127(b)(11) and (12); 15 U.S.C. 1637(b)(11) and (12).

A number of technical revisions are made for clarity. For the reasons set forth in the section-by-section analysis to § 226.6(b)(1), the Board would update references to "free-ride period" as "grace period" in the regulation and commentary, without any intended substantive change. Current comment 7-2, which addresses open-end plans involving more than one creditor, would be deleted as obsolete and unnecessary.

Format requirements for periodic statements. TILA and Regulation Z contain few formatting requirements for periodic statement disclosures. In the December 2004 ANPR, the Board noted that some information about past account activity also may be useful to consumers in making future decisions concerning the plan. The Board sought comment on possible ways to format information to improve the effectiveness of periodic statement disclosures, including proximity requirements or grouping of terms or fees. Q4 – Q6.

Commenters' views were mixed. Industry commenters generally opposed mandating specific format requirements. They suggested that consumers are not confused by basic information conveyed on periodic statements, and that mandated format requirements would be expensive to implement and could stifle creditors' ability to tailor statements to specific products. Some of these commenters suggested that grouping of terms or fees might be helpful, but cautioned against a total of fees that would not differentiate interest from other charges such as penalty fees (late or over-the-credit-limit, for example). Some consumer group commenters suggested importing format requirements similar to the tabular disclosures for credit card applications and solicitations.

Consumer testing conducted for the Board has shown that targeted proximity requirements on periodic statements tend to improve the effectiveness of cost disclosures for consumers. For the reasons discussed below, the Board proposes several proximity requirements. For example, the proposal would link by proximity the payment due date with the late payment fee and penalty rate that could be triggered by an untimely payment. The minimum payment amount also would be linked by proximity with the new warning required by the Bankruptcy Act about the effects of making such payments on the account. The Board believes grouping these disclosures together would enhance consumers' informed use of credit.

To ensure consumers are alerted to rate increases and other changes that increase the cost of using their account, a summary of key rate and term changes would precede the transactions when an advance notice of a change in term or rate accompanies a periodic statement. Transactions would be grouped by type, and fee and interest charge totals would be located with the transactions. Participants in the consumer testing conducted for the Board tended to review their transactions and to notice fees and interest charges when placed there. The Board notes that some financial institutions presently group transactions by type. Form G-18(A) would illustrate these requirements.

The Board is publishing for the first time forms illustrating front sides of a periodic statement. The Board is publishing forms G-18(G) and G-18(H) to illustrate how a periodic statement might be designed to comply with the requirements of § 226.7. Forms G-18(G) and G-18(H) contain some additional disclosures that are not required by Regulation Z. The forms also present information in some additional formats that are not required by Regulation Z. The Board is publishing the front side of a statement form as a compliance aid.

Consumer testing for the Board indicates that the effectiveness of periodic statement disclosures is improved when certain information is grouped together. The Board seeks comment on any alternative approaches that would provide creditors more flexibility in grouping related information together on the periodic statement.

**7(a) Rules Affecting Home-equity Plans**

For HELOCs, creditors are required to comply with the disclosure requirements under proposed § 226.7(a)(1) through (10), including existing rules and guidance regarding the disclosure of finance charges and other charges, which would be combined in a new § 226.7(a)(6). These rules and accompanying commentary are substantively unchanged from current § 226.7(a) through (k). Proposed § 226.7(a) also provides that at their option, creditors offering HELOCs may comply with the requirements of § 226.7(b). The Board understands that some creditors may use a single processing system to generate periodic statements for all open-end products they offer, including HELOCs. These creditors would have the option to generate statements according to a single set of rules.

In technical revisions, the substance of footnotes referenced in § 226.7(d) is moved to proposed § 226.7(a)(4) and comment 7(a)(4)-6.

**7(a)(7) Annual Percentage Rate**

The Board is proposing two alternative approaches to address concerns about the effective APR. These approaches are discussed in detail in the section-by-section analysis to proposed § 226.7(b)(7). The first approach seeks to improve the effective APR. For HELOCs subject to § 226.5b, creditors would have an option to comply with the new rules or continue to comply with the current rules applicable to the effective APR. This is intended as a temporary measure until the Board reviews comprehensively the rules for HELOCs subject to § 226.5b. The second approach would eliminate the requirement to disclose the effective APR; thus, under this approach, the effective APR would be optional for HELOC creditors pending the Board's review of home-secured disclosure rules.

**7(b) Rules Affecting Open-end (not Home-secured) Plans**

Current comment 7-3 provides guidance on various periodic statement disclosures for deferred-payment transactions, such as when a consumer may avoid interest charges if a purchase balance is paid in full by a certain date. Under the proposal, the substance of comment 7-3, revised to conform to other proposed revisions in § 226.7(b), is proposed as comment 7(b)-1. The Board believes the guidance is unnecessary for HELOCs.

**7(b)(2) Identification of Transactions**

Proposed § 226.7(b)(2) requires creditors to identify transactions in accordance with rules set forth in § 226.8. The Board proposes to revise and significantly simplify those rules, as discussed in the section-by-section analysis relating to § 226.8 below.

The Board would introduce a format requirement to group transactions by type, such as purchases and cash advances. In consumer testing conducted for the Board, participants found such groupings helpful. Moreover, consumers noticed fees and interest charges more readily when transactions were grouped together, the fees imposed for the statement period were not interspersed among the transactions, and the interest and fees were disclosed in proximity to the transactions. Comment 7(b)(2)-1 would reflect the new requirement. Sample G-18(A) would illustrate the proposal.

**7(b)(3) Credits**

Creditors are required to disclose any credits to the account during the billing cycle. Creditors typically disclose credits among other transactions. The Board proposes no substantive changes to the disclosure requirements for credits. However, consistent with the format requirements proposed in § 226.7(b)(2), the proposal would require credits and payments to be grouped together. Consumers who participated in testing conducted for the Board consistently identified credits as statement information they review each month, and favored a separation of credits and payments among the transactions.

Current comment 7(c)-2, which permits creditors to commingle credits related to extensions of credit and credits related to non-credit accounts, such as a deposit account, is not proposed under new § 226.7(b)(3). The Board solicits comment on the need for alternatives to the proposed format requirements to segregate transactions and credit, such as when a depository institution provides on a single periodic statement account activity for a consumer's checking account and an overdraft line of credit.
Sample G-18(A) would illustrate the proposal. Comment 7(b)(3)-3, as renumbered, is revised for clarity.

**7(b)(4) Periodic Rates**

Periodic rates. TILA Section 127(b)(5) and current § 226.7(d) require creditors to disclose all periodic rates that may be used to compute the finance charge, and an APR that corresponds to the periodic rate multiplied by the number of periods in the years. 15 U.S.C. 1637(b)(5); § 226.14(b). The Board is proposing to eliminate, for open-end (not home-secured) plans, the requirement to disclose periodic rates on periodic statements.

The Board proposes this approach 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 uniformed use of credit. 15 U.S.C. 1601(a), 1604(a). Section 105(f) authorizes the Board to exempt any class of transactions (with an exception not relevant here) 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). 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 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 proposing the exemption is appropriate. In consumer testing conducted for the Board, consumers indicated they do not use periodic rates to verify interest charges. Consistent with the Board's proposal to not allow periodic rates to be disclosed in the tabular summary on or with credit card applications and disclosures, the Board believes that requiring periodic rates to be disclosed on periodic statements may distract from more important information on the statement, and contribute to information overload. The proposal to eliminate periodic rates from the periodic statement therefore has the potential to better inform consumers and further the goals of consumer protection and the informed use of credit for open-end (not home-secured) credit. The Board welcomes comment on this matter.

Labeling APRs. Currently creditors are provided with considerable flexibility in identifying the APR that corresponds to the periodic rate. Current comment 7(d)-4 permits labels such as "corresponding annual percentage rate," "nominal annual percentage rate," or "corresponding nominal annual percentage rate." To promote uniformity, creditors offering open-end (not home-secured) plans would be required to label the annual percentage rate disclosed under proposed § 226.7(b)(4) as "annual percentage rate." In combination with the Board's proposed approach to improve consumers' understanding of the effective APR discussed in the section-by-section analysis to proposed § 226.7(b)(7), it is important that the "interest only" APR be uniformly distinguishable from the effective APR that includes interest and fees. Forms G-18(G) and G-18(H) illustrate periodic statements that disclose an APR but no periodic rates.

Rates that "may be used." Currently, comment 7(d)-1 interprets the requirement to disclose all periodic rates that "may be used" to mean "whether or not [the rate] is applied during the cycle." For example, rates on cash advances must be disclosed on all periodic statements, even for billing periods with no cash advance activity or balances. The regulation and commentary do not clearly state whether promotional rates, such as those offered for using checks accessing credit card accounts, that "may be used" should be disclosed under current § 226.7(d) regardless of whether they are imposed during the period. See current comment 7(d)-2. The Board is proposing a limited exception to TILA Section 127(b)(5) to effectuate the purposes of TILA to require disclosures that are meaningful and to facilitate compliance.

Under the proposal, creditors would be required to disclose promotional rates only if the rate actually applied during the billing period. See proposed § 226.7(b)(4)(ii). For example, a card issuer may impose a 22 percent APR for cash advances but offer for a limited time a 1.99 percent promotional APR for advances obtained through the use of a check accessing a credit card account. Creditors are currently required to disclose, in this example, the 22 percent cash advance APR on periodic statements whether or not the consumer obtains a cash advance during the previous statement period. The proposal would make clear that creditors are not required to disclose the 1.99 percent promotional APR unless the consumer used the check during the statement period. The Board believes that interpreting TILA to require the disclosure of all promotional rates would be operationally burdensome for creditors and result in information overload for consumers. The proposed exception would not apply to HELOCs covered by § 226.5b. The Board requests comment on whether the class of transactions under the proposed exceptions should be tailored more broadly to include HELOCs subject to § 226.5b, and if so, why.

Combining interest and other charges. Currently, creditors must disclose finance charges attributable to periodic rates. These costs are typically interest but may include other costs such as premiums for required credit insurance. If applied to the same balance, creditors may disclose each rate, or a combined rate. See current comment 7(d)-3. As discussed earlier, consumer testing for the Board indicates that participants appeared to understand credit costs in terms of "interest" and "fees," and the proposal would require disclosures to distinguish between interest and fees. To the extent consumers associate periodic rates with "interest," it seems unhelpful to consumers' understanding to permit creditors to include periodic rate charges other than interest into the dollar cost disclosed. Thus, guidance about combining periodic rates attributable to interest and other finance charges would be retained for HELOCs in proposed comment 7(a)(4)-3, but would be eliminated for open-end (not home-secured) plans.

A new comment 7(b)(4)-7 would be added to provide guidance to creditors when a fee is imposed, remains unpaid, and accrues interest on the unpaid balance. The comment provides that creditors disclosing fees in accordance with the format requirements of § 226.7(b)(6) need not separately disclose which periodic rate applies to the unpaid fee balance.

In technical revisions, the substance of footnotes referenced in § 226.7(d) is moved to the regulation and comment 7(b)(4)-5.

**7(b)(5) Balance on which Finance Charge is Computed**

Creditors must disclose the amount of the balance to which a periodic rate was applied and an explanation of how the balance was determined. The Board provides model clauses creditors may use to explain common balance computation methods. 15 U.S.C. 1637(b)(7); current § 226.7(e); Model Clauses G-1, Appendix G. The staff commentary to current § 226.7(e) interprets how creditors may comply with TILA in disclosing the "balance," which typically changes in amount throughout the cycle, on periodic statements.

Amount of balance. The proposal does not change how creditors are required to disclose the amount of the balance on which finance charges are computed. It would, however, permit creditors, at their option, not to include an explanation of how the finance charge may be verified for creditors that use a daily balance method. Currently, creditors that use a daily balance method are permitted to disclose an average daily balance for the period, provided they explain that the amount of the finance charge can be verified by multiplying the average daily balance by the number of days in the statement period, and then applying the periodic rate. The Board would retain the rule permitting creditors to disclose an average daily balance but would eliminate the requirement to provide the explanation. Consumer testing conducted for the Board suggests that the explanation may not be used by consumers as an aid to calculate their interest charges. Participants suggested that if they attempted without satisfaction to calculate balances and verify interest charges based on information on the periodic statement, they would call the creditor for assistance.

The section-by-section analysis to § 226.7(b)(6) discusses proposed revisions intended to further consumers' understanding of interest charges, as distinguished from fees. To complement those proposed revisions, the Board would require creditors to refer to the balance as "balances subject to interest rate," for consistency. Forms G-18(G) and 18(H) illustrate this format requirement. For the reasons discussed regarding guidance on disclosing periodic rates, guidance about disclosing balances to which periodic rates attributable to interest and other finance charges are applied would be retained for HELOCs in proposed comment 7(a)(5)-1, but would be eliminated for open-end (not home-secured) plans.

<u>Explanation of balance computation method</u>. The Board is proposing an alternative to providing an explanation of how the balance was determined. Under the proposal, a creditor that uses a balance computation method identified in § 226.5a(g) has two options. The creditor may: (1) provide an explanation, as the rule currently requires, or (2) identify the name of the balance computation method and provide a toll-free telephone number where consumers may obtain more information from the creditor about how the balance is computed and resulting finance charges are determined. If the creditor uses a balance computation method that is not identified in § 226.5a(g), the creditor would provide a brief explanation of the method. The Board's proposal is guided by the following factors.

Calculating balances on open-end plans can be complex, and requires an understanding of how creditors allocate payments, assess fees, and record transactions as they occur during the cycle. Currently, neither TILA nor Regulation Z requires creditors to disclose on periodic statements all the information necessary to compute a balance, and requiring that level of detail appears not to be warranted. Although the Board's model clauses are intended to assist creditors in explaining common methods, consumers continue to find these explanations lengthy and complex. As stated earlier, consumer testing indicates that consumers call the creditor for assistance when they attempt without satisfaction to calculate balances and verify interest charges.

The Board believes that providing the name of the balance computation method (or a brief explanation, if the name is not identified in § 226.5a(g)), along with a reference to where additional information may be obtained provides essential information in a simplified way, and in a manner consistent with how consumers obtain further balance computation information. The proposal is consistent with the views of some commenters who responded to the December 2004 ANPR and suggested that the Board simplify some of the more complex disclosures not used by most consumers. Current comment 7(e)-6, which refers creditors to guidance in § 226.6 about disclosing balance computation methods would be deleted as unnecessary.

**7(b)(6) Charges Imposed**

As discussed in the section-by-section analysis to § 226.6, the Board proposes to reform cost disclosure rules for open-end (not home-secured) plans, in part, to ensure that all charges assessed as part of an open-end (not home-secured) plan are disclosed before they are imposed and to simplify the rules for creditors to identify such charges. Consistent with the proposed revisions at account opening, the proposed revisions to cost disclosures on periodic statements are intended to simplify how creditors identify the dollar amount of charges imposed during the statement period.

Consumer testing conducted for the Board indicates that most participants reviewing mock periodic statements could not correctly explain the term "finance charge." The proposed revisions are intended to conform labels of charges more closely to common understanding, "interest" and "fees." Format requirements would also help ensure that consumers notice charges imposed during the statement period.

Two alternatives are proposed: One addresses interest and fees in the context of an effective APR disclosure, the second assumes no effective APR is disclosed.

Charges imposed as part of the plan. Proposed § 226.7(b)(6) would require creditors to disclose the amount of any charge imposed as part of an open-end (not home-secured) plan, as stated in § 226.6(b)(1). Guidance on which charges are deemed to be imposed as part of the plan is in proposed § 226.6(b)(1) and accompanying commentary. Although coverage of charges would be broader under the proposed standard of "charges imposed as part of the plan" than under current standards for finance charges and other charges, the Board understands that creditors have been disclosing on the statement all charges debited to the account regardless of whether they are now defined as "finance charges," "other charges," or charges that do not fall into either category. Accordingly, the Board understands that creditors already disclose all charges that would be considered "imposed as part of the plan," and it does not expect this proposed change to affect significantly the disclosure of charges on the periodic statement.

Interest charges and fees. For creditors complying with the new proposed cost disclosure requirements, the current requirement in § 226.7(f) to label finance charges as such would be eliminated. See current § 226.7(f). Testing of this term with consumers found that it did not help them to understand charges. Instead, charges imposed as part of an open-end (not home-secured) plan would be disclosed under the labels of "interest charges" and "fees." Consumer testing supplies evidence that consumers may generally understand interest as the cost of borrowing money over time and characterize other costs—regardless of their characterization under TILA and Regulation Z—as fees (other than interest). The Board's proposal is consistent with this evidence.

TILA Section 127(b)(4) requires creditors to disclose on periodic statements the amount of any finance charge added to the account during the period, itemized to show amounts due to the application of periodic rates and the amount imposed as a fixed or minimum charge. 15 U.S.C. 1637(b)(4). This requirement is currently implemented in § 226.7(f), and creditors are given considerable flexibility regarding totaling or subtotaling finance charges attributable to periodic rates and other fees. See current § 226.7(f) and comments 7(f)-1, -2, and -3. To improve uniformity and promote the informed use of credit, creditors would be required under proposed § 226.7(b)(6)(ii) to itemize finance charges attributable to interest, by type of transaction labeled as such, and would be required to disclose, for the statement period, a total interest charge, labeled as such. Although creditors are not currently required to itemize interest charges by transaction type, creditors often do so. For example, creditors may disclose the dollar interest costs associated with cash advance and purchase balances. Based on consumer testing, the Board believes consumers' ability to make informed decisions about the future use of their open-end plans—primarily credit card accounts—may be promoted by a simply-labeled breakdown of the current interest cost of carrying a purchase or cash advance balance. The breakdown would enable consumers to better understand the cost for using each type of transaction, and uniformity among periodic statements would allow consumers to compare one account with other open-end plans the consumer may have. Under the proposal, finance charges attributable to periodic rates other than interest charges, such as required credit insurance premiums, would be identified as fees and would no longer be permitted to be combined with interest costs. See proposed comment 7(b)(4)-3.

Current § 226.7(h) requires the disclosure of "other charges" parallel to the requirement in TILA Section 127(a)(5) and current § 226.6(b) to disclose such charges at account opening. 15 U.S.C. 1637(a)(5). Consistent with current rules to disclose "other charges," revised § 226.7(b)(6)(iii) would require that other costs be identified consistent with the feature or type, and itemized. The proposal differs from current requirements in the following respect: fees would be required to be grouped together and a total of all fees for the statement period would be required. Currently, creditors typically include fees among other transactions identified under § 226.7(b). In consumer testing, consumers were able to more accurately and easily determine the total cost of non-interest charges when fees were grouped together and a total of fees was given than when fees were scattered among the transactions without a total. (Section 226.7(b)(6)(iii) also would require that certain fees that are included in the computation of the effective APR pursuant to § 226.14 must be labeled either as "transaction fees" or "fixed fees." This proposed requirement is discussed in further detail in the section-by-section analysis to § 226.7(b)(7).)

To highlight the overall cost of the credit account to consumers, creditors would disclose the total amount of interest charges and fees for the statement period and calendar year to date. Participants in consumer testing conducted for the Board noticed the year-to-date cost figures and indicated they would find the numbers helpful in making future financial decisions. The Board believes that disclosure of year-to-date totals would better inform consumers about the cumulative cost of their credit plans over a significant period of time. Comment 7(b)(6)-3 would provide guidance on how creditors may disclose the year to date totals at the end of a calendar year.

Proposed § 226.7(b)(6)(iv) in Alternative 1 contains requirements for calculating and disclosing totals for interest and certain fees in connection with the disclosure of the effective APR pursuant to § 226.7(b)(7). These requirements are in addition to the total interest and fee disclosures disclosed in proximity to transactions, and are discussed in further detail in the section-by-section analysis to § 226.7(b)(7).

Format requirements. In consumer testing, consumers consistently reviewed transactions identified on their periodic statements and noticed fees and interest charges, itemized and totaled, when they were grouped together with transactions. Some creditors also disclose these costs in account summaries or in a progression of figures associated with disclosing finance charges attributable to periodic rates. The proposal would not affect creditors' flexibility to provide this information in such summaries. See Forms G-18(G) and G-18(H), which illustrate, but do not require, such summaries. However, the Board believes TILA's purpose to promote the informed use of credit would be furthered significantly if consumers are uniformly provided, in a location they routinely review, basic cost information—interest and fees—that enables consumers to compare costs among their open-end plans. The Board proposes that charges required to be disclosed under § 226.7(b)(6)(i) would be grouped together with the transactions identified under § 226.7(b)(2), substantially similar to Sample G-18(A) in Appendix G. Proposed § 226.7(b)(6)(iii) would require non-interest fees to be itemized and grouped together, and a total of fees would be disclosed for the statement period and calendar year to date. Interest charges would be itemized by type of transaction, grouped together, and a total of interest charges would be disclosed for the statement period and year to date. Sample G-18(A) in Appendix G illustrates the proposal.

**7(b)(7) Effective Annual Percentage Rate**

TILA Section 127(b)(6) requires disclosure of an APR calculated as the quotient of the total finance charge for the period to which the charge relates divided by the amount on which the finance charge is based, multiplied by the number of periods in the year. 15 U.S.C. 1637(b)(6). This rate has come to be known as the "historical APR" or "effective APR." (This APR will be referred to as the "effective APR" in this section-by-section analysis, and in the regulation and accompanying commentary.) Section 127(b)(6) exempts a creditor from disclosing an effective APR when the total finance charge does not exceed 50 cents for a monthly or longer billing cycle, or the pro rata share of 50 cents for a shorter cycle. In such a case, TILA Section 127(b)(5) requires the creditor to disclose only the periodic rate and the annualized rate that corresponds to the periodic rate. 15 U.S.C. 1637(b)(5). When the finance charge exceeds 50 cents, the act requires creditors to disclose the periodic rate but not the corresponding APR. Since 1970, however, Regulation Z has required disclosure of the corresponding APR in all cases. See current § 226.7(d). Current § 226.7(g) implements TILA Section 127(b)(6)'s requirement to disclose an effective APR.

The effective APR and corresponding APR for any given plan feature are the same when the finance charge in a period arises only from application of the periodic rate to the applicable balance (the balance calculated according to the creditor's chosen method, such as average daily balance method). When the two APRs are the same, Regulation Z requires that the APR be stated just once. The effective and corresponding APRs diverge when the finance charge in a period arises (at least in part) from a charge not determined by application of a periodic rate and the total finance charge exceeds 50 cents. When they diverge, Regulation Z requires that both be stated.

The following example illustrates the relationship between the effective APR and the corresponding APR in a simple case. A credit cardholder with no balance in the previous cycle takes a cash advance of $100 on the first day of the cycle. A cash advance fee of 3 percent applies (a finance charge of $3), as does a periodic rate of 1½ percent per month on the average daily balance of $100 (a finance charge of $1.50). No other transactions, and no payments, occur during the cycle, which is 30 days. The corresponding APR is 18 percent (1½ percent times 12). To determine the effective APR, first the total finance charge of $4.50 is divided by the balance of $100. This quotient, 4½ percent, is the rate of the total finance charge on a monthly basis. The monthly rate is annualized, or multiplied by 12, to yield an effective APR of 54 percent. Under Regulation Z, the creditor would disclose on the periodic statement both the corresponding APR of 18 percent and the effective APR of 54 percent.

The controversy over the effective APR. The statutory requirement of an effective APR is intended to provide the consumer with an annual rate that reflects the total finance charge, including both the finance charge due to application of a periodic rate (interest) and finance charges that take the form of fees. This rate, like other APRs required by TILA, presumably was intended to provide consumers information about the cost of credit that would help consumers compare credit costs and make informed credit decisions and, more broadly, strengthen competition in the market for consumer credit. 15 U.S.C. 1601(a). There is, however, a longstanding controversy about the extent to which the requirement to disclose an effective APR advances TILA's purposes or, as some argue, undermines them. This controversy has been reflected in such forums as discussions by the Board's Consumer Advisory Council and comments on the ANPR. Q23 – Q25. The following discussion seeks to place the controversy over the effective APR in the context of certain objective characteristics of the disclosure.

The effective APR is essentially retrospective, or "historical." An effective APR on a particular periodic statement represents the cost of transactions in which the consumer engaged during the cycle to which that statement pertains. It is not likely, however, that the effective APR for a transaction in a given cycle will predict accurately the cost of a transaction in a future cycle. If any one of several factors is different in the future cycle than it was in the past cycle, such as the balance at the beginning of the cycle or the amount and timing of each transaction and payment during the cycle, then the effective APRs in the two cycles will be different, too.[13] In short, the effective APR is by nature retrospective and idiosyncratic and, therefore, provides limited information about the cost of future transactions.

Consumer groups argue that the information the rate provides about the cost of future transactions, even if limited, is meaningful. The effective APR for a specific transaction or set of transactions in a given cycle may provide the consumer a rough indication that the cost of repeating such transactions is high in some sense or, at least, higher than the corresponding APR alone conveys. Industry commenters respond that the cost of a transaction is not usually as high as the effective APR makes it appear, and that this tendency of the rate to exaggerate the cost makes this APR misleading. Commenters generally agree that the effective APR can be "shocking," but they disagree as to whether it conveys meaningful information.

One reason that effective APRs appear high is the assumption built into the disclosure that the borrower paid the balance at the end of the cycle. This assumption tends to make the APR higher, and more volatile, than if a longer repayment period were used. In the example given above, the effective APR on cash advances, 54 percent, is three times the corresponding APR, 18 percent. Moreover, the effective APR would have been 18 percent (the same as the corresponding APR) in the previous cycle if no cash advances had been taken then, and it will fall back to 18 percent in the next cycle if no cash advance is taken then (assuming the rate is fixed). Use of a longer repayment period would, other things being equal, yield a lower, and less volatile, effective APR. A lower APR based on available information about the consumer's expected time to repay might seem more realistic. But its disclosure would require making assumptions about activity in future cycles, such as the timing and amount of future transactions and payments – or it would require assuming that there is to be no activity on the account until the balance is repaid. Such assumptions would often appear arbitrary and unrealistic. Accordingly, Regulation Z has always required that the effective APR be calculated on the premise that payment was made at the end of the cycle. The likelihood that the premise is often wrong accounts, at least in part, for the controversy as to whether the effective APR can supply meaningful information about credit costs.

Consumer advocates and industry representatives also disagree as to whether the effective APR promotes credit shopping. The dependence of the effective APR on the particular activity in a given cycle means that any given effective APR in any given cycle is not typically a practical shopping tool. Comparing two particular effective APRs for any two cycles on two different accounts is not usually a reliable basis to determine

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[13] An example demonstrates how the effective APR depends critically on the timing of transactions during two different cycles. Assume for the sake of simplicity that the transaction amount and beginning balance remain the same in both cycles. In the example discussed above, a cash advance of $100 on the first day of a 30-day cycle yielded an effective APR of 54 percent, three times the corresponding APR of 18 percent. If in a later cycle the consumer were to take the cash advance on the last day of the 30-day cycle, the effective APR would be 36.6 percent, about twice the corresponding APR. (The finance charge produced by the periodic rate would be $.05 (1½ percent times the average daily balance of $3.33). The total finance charge of $3.05 divided by the transaction amount of $100 yields a quotient of 3.05 percent, which is multiplied by 12 to yield an effective APR of 36.6 percent.)

which account costs the consumer more. Moreover, an effective APR for a given month on an existing account cannot be compared reliably to the corresponding APR advertised on a different account, which by definition does not reflect any finance charges imposed in the form of fees. There may be cases in which repeated disclosure of effective APRs in consecutive cycles, as opposed to one effective APR for one cycle, would facilitate shopping. For example, if an account had a periodic rate and a corresponding APR of zero, the effective APRs disclosed on the account might provide the most practical basis for assessing the cost of the account in relationship to other advertised accounts. This example, though, does not appear to be common in today's market.

Although the effective APR is not commonly usable as a shopping tool in itself, consumer group commenters argue that the effective APR promotes credit shopping by encouraging consumers to seek out other sources of credit, especially when the rate reaches levels that "shock" consumers. Industry commenters respond, however, that the tendency of the effective APR to exaggerate the cost of credit may lead consumers to make invalid comparisons. They say that disclosure of a high effective APR in a cycle may cause a consumer to discontinue using the account in favor of another account that appears less expensive based on its corresponding APR but is in fact more expensive, because of fixed or minimum charges or other factors.

Supporters of the effective APR also argue that high effective APRs typical for cash advances and balance transfers benefit consumers by discouraging them from engaging in these transactions. Industry commenters respond that consumers do not necessarily benefit if they refrain categorically from a particular kind of credit transaction; depending on the alternatives consumers choose, they may be worse-off rather than better-off. Some of these commenters also argue that discouraging particular kinds of credit transactions is not a valid objective of Regulation Z.

Industry and community group commenters find some common ground in their observations that consumers do not understand the effective APR well. Industry commenters argue from their experience with their customers that consumers do not understand how this APR differs from the corresponding APR, why it is "so high," or which fees it reflects. Creditor commenters say that when their customers call them and express alarm or confusion over the effective APR, the creditors find it difficult, if not impossible, to make the caller understand the disclosure. Nor, they argue, does a consumer find the disclosure any more useful than disclosure of interest and fees in dollars and cents, even if the consumer understands the disclosure. Consumer groups concede that, as implemented today, the effective APR is difficult for consumers to understand, and they support efforts to make it more understandable, such as improved presentation on the periodic statement. Industry commenters expressed doubt that such efforts would be worthwhile.

Industry commenters also claim the effective APR imposes direct costs on creditors that consumers pay indirectly. They represent that the effective APR raises compliance costs when they introduce new services, including legal analysis of Regulation Z to determine whether the fee for the new service must be included in the effective APR and software programming if it is included; they are also concerned about litigation risks. Also, responding to telephone inquiries from confused customers and accommodating them (e.g., with fee waivers or rebates) increases operational costs. Costs associated with adverse consumer reactions to the effective APR may influence creditors to take steps to minimize the frequency with which they must disclose it. One such step would be to price credit mostly through a periodic rate rather than fees. Although this effect is difficult to measure, a trade association commenter concedes a policy argument for retaining the effective APR as a hedge against creditors shifting their pricing from periodic rates to transaction-triggered fees and charges.

Like most other industry commenters, however, this same commenter concludes that the effective APR should be eliminated because, for the reasons discussed above, its costs outweigh its benefits. Some industry commenters support replacing the effective APR with enhanced fee disclosures (for example, grouping fees on the statement or summing them for each period or for the year), but many do not. Consumer groups urge the Board not only to retain the effective APR, but to expand it in two respects: (1) include in the rate all charges, including charges not currently defined as finance charges in Regulation Z; and (2) require creditors to disclose a "typical effective APR" (an average of effective APRs) on solicitations and account-opening disclosures.[14]

Consumer research conducted for the Board. It is difficult to measure directly how the effective APR ultimately affects consumers, creditors, and the credit market generally. It is feasible, however, at a minimum, to assess to some degree consumers' awareness and understanding of the disclosure. Such assessments may support inferences about the disclosure's effectiveness.

Accordingly, the Board undertook research, through a consultant, to shed light on consumer awareness and understanding of the effective APR; and on whether changes to the presentation of the disclosure could increase awareness and understanding. A Board consultant used a qualitative testing method, one-on-one cognitive interviews with consumers. Consumers were provided mock disclosures of periodic statements that included effective APRs and asked questions about the disclosure designed to elicit their understanding of the rate. In the first round the statements were copied from examples in the market. For subsequent testing rounds, however, statements were modified in language and design to better convey how the effective APR differs from the corresponding APR. Several different approaches and many variations on those approaches were tested.

In most of the rounds, a minority of participants correctly explained that the effective APR for cash advances in the last cycle was higher than the corresponding APR for cash advances because a cash advance fee had been imposed. A smaller minority correctly explained that the effective APR for purchases was the same as the corresponding APR for purchases because no transaction fee had been imposed on purchases. A majority offered incorrect explanations or did not offer any explanation.

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[14] Consumer group comments about a "typical APR" disclosure are summarized in the section-by-section analysis to § 226.5a.

Results changed at the final testing site, however, when a majority of participants evidenced an understanding that the effective APR for cash advances would be elevated for the statement period when a cash advance fee was imposed during that period, that the effective APR would not be as elevated for periods where a cash advance balance remained outstanding but no fee had been imposed, and that the effective APR for purchases was the same as the corresponding APR for purchases because no transaction fee had been imposed on purchases.

The form in the final round labeled the rate "Fee-Inclusive APR" and placed it in a table separate from the corresponding APR. The "Fee-Inclusive APR" table included the amount of interest and the amount of transaction fees. An adjacent sentence stated that the "Fee-Inclusive APR" represented the cost of transaction fees as well as interest. Similar approaches had been tried in some of the earlier rounds, except that the effective APR had been labeled "Effective APR."

The Board's two alternative proposals. The considerations and data discussed above lead the Board to propose two alternative approaches for disclosing the effective APR: The first approach would try to improve consumer understanding of this rate and reduce creditor uncertainty about its computation. The second approach would eliminate the requirement to disclose the effective APR. The evidence of consumer understanding of the effective APR supplied by the qualitative research conducted for the Board is mixed, but it suggests that it may be possible to increase current levels of understanding by modifying the presentation of the rate on the periodic statement. The Board's experience with Regulation Z also suggests that it may be possible to reduce burdens by simplifying computation of the effective APR.

The Board plans to conduct further research into consumer understanding of the effective APR after the comment period has ended. The Board will evaluate this additional research with the research conducted to date, and with other information, including comments received on this proposal, and determine whether the effective APR should be retained with modifications as proposed, eliminated, or addressed in some other way.

1. First alternative proposal. Under the first alternative, the Board proposes to impose uniform terminology and formatting on disclosure of the effective APR and the fees included in its computation. See proposed §§ 226.7(b)(7)(i), 226.7(b)(6)(iv). This proposal is based largely on a form developed through several rounds of one-on-one interviews with consumers. The Board also proposes under this alternative to revise § 226.14, which governs computation of the effective APR, in an effort to increase certainty about which fees the rate must include. See proposed § 226.14(d). See section-by-section analysis to § 226.7(a)(7) regarding how the proposal affects HELOCs subject to § 226.5b.

Under proposed § 226.7(b)(7)(i) and Sample Form G-18(B), creditors would label the effective APR "Fee-Inclusive APR" and indicate that the Fee-inclusive APRs are the "APRs that you paid this period when transactions or fixed fees are taken into account as well as interest." Creditors would disclose an effective APR for each feature, such as purchases and cash advances, in a tabular format. A composite effective APR for two or more features would no longer be permitted, as it is more difficult to explain to consumers. The effective APR(s) would appear in a table, by feature, with the total of interest, labeled as "interest charges," and the total of the fees included in the effective APR, labeled as "transaction and fixed charges." To facilitate understanding, proposed § 226.7(b)(6)(iii) would require creditors to label the specific fees used to calculate the effective APR either as "transaction" or "fixed" fees, depending whether the fee relates to a specific transaction; such fees would be disclosed in the list of transactions. If the only finance charges in a billing cycle are interest charges, the corresponding and effective APRs are identical. In those cases, creditors would disclose only the corresponding APRs and would not be required to label fees as "transaction" or "fixed" fees. These requirements would be illustrated in forms under G-18 in Appendix G, and creditors would be required to use the model or a substantially similar presentation.

To facilitate compliance, the proposed regulation would give specific guidance about how to attribute fees to account features. For convenience and uniformity, two kinds of charges, when used to calculate the effective APR, would be grouped under the purchase feature of the account: (1) charges that relate to specific purchase transactions; and (2) minimum, fixed and other non-interest charges not related to a specific transaction. See proposed § 226.7(b)(6)(iv)(B). If there are purchase features other than the standard purchase feature – such as a promotional purchase feature – then the minimum, fixed or other non-interest charges would be grouped with other charges relating to the balance on the standard purchase feature. See proposed comment 7(b)(6)-5. In addition, a minimum charge would be disclosed as a fee, rather than as interest, and it would be grouped together with other fees related to standard purchases and used to calculate the effective APR with respect to the standard purchase feature. See proposed comment 7(b)(6)-4.

The proposal also seeks to simplify computation of the effective APR, both to increase consumer understanding of the disclosure and facilitate creditor compliance. New § 226.14(e) would provide a specific and exclusive list of finance charges that would be included in calculating the effective APR.[15] This proposed change is discussed further in the section-by-section analysis to § 226.14.

The Board seeks comment on the potential benefits and costs of the first alternative proposal.

2. Second alternative proposal. Under the second alternative proposal, for the reasons discussed in the introduction to the discussion of the effective APR, the effective APR would no longer be disclosed. The Board proposes this approach pursuant to its

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[15] Under the statute, the numerator of the quotient used to determine the historical APR is the total finance charge. See Section 107(a)(2), 15 U.S.C. 1606(a)(2). The Board has authority to make exceptions and adjustments to this calculation method to serve TILA's purposes and facilitate compliance. See Section 105(a), 15 U.S.C. 1604(a). The Board has used this authority before to exclude certain kinds of finance charges from the historical APR. See current § 226.14(c)(2), fn. 33.

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 uniformed use of credit. 15 U.S.C. 1601(a), 1604(a). Section 105(f) authorizes the Board to exempt any class of transactions (with an exception not relevant here) 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). 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 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 proposing the exemption is appropriate. Consumer testing suggests that consumers find the current requirement of disclosing an APR that combines rates and fees to be confusing. The proposal would require disclosure of the nominal interest rate and fees in a manner that is more readily understandable and comparable across institutions. It therefore has the potential to better inform consumers and further the goals of consumer protection and the informed use of credit for all types of open-end credit. A potentially competing consideration is the extent to which "sticker shock" from the effective APR benefits consumers, even if the disclosure is somewhat arbitrary. A second consideration is whether the effective APR is a hedge against fee-intensive pricing by creditors, and if so, the extent to which it promotes transparency. On balance, however, the Board believes that the benefits of the proposal would outweigh these considerations. The Board welcomes comment on this matter.

**7(b)(9) Address for Notice of Billing Errors**

Consumers who allege billing errors must do so in writing. 15 U.S.C. 1666; § 226.13(b). Creditors must provide on or with periodic statements an address for this purpose. See current § 226.7(k). Currently, comment 7(k)-2 provides that creditors may also provide a telephone number along with the mailing address as long as the creditor makes clear a telephone call to the creditor will not preserve consumers' billing error rights. The Board would update comment 7(k)-2, renumbered as comment 7(b)(9)-2, to address notification by e-mail or via a web site. The comment would provide that the address is deemed to be clear and conspicuous if a precautionary instruction is included that telephoning or notifying the creditor by e-mail or web site will not preserve the consumer's billing rights, unless the creditor has agreed to treat billing error notices provided by electronic means as written notices, in which case the precautionary instruction is required only for telephoning.

**<u>7(b)(10) Closing Date of Billing Cycle; New Balance</u>**

Creditors must disclose the closing date of the billing cycle and the account balance outstanding on that date. As a part of its proposal to implement TILA amendments in the Bankruptcy Act regarding late payment and the effect of making minimum payments, the Board is proposing to require creditors to group together, as applicable, disclosures of related information about due dates and payment amounts, including the new balance. This is discussed in the section-by-section analysis to §§ 226.7(b)(11) and (b)(13) below, and illustrated in Forms G-18(G) and G-18(H) in Appendix G.

**<u>7(b)(11) Due Date; Late Payment Costs</u>**

TILA Section 127(b)(12), added by Section 1305(a) of the Bankruptcy Act, requires creditors that charge a late-payment fee to disclose on the periodic statement (1) the payment due date or, if different, the earliest date on which the late-payment fee may be charged, and (2) the amount of the late-payment fee. 15 U.S.C. 1637(b)(12). The October 2005 ANPR solicited comment on the need for additional guidance on the date to be disclosed under the new rule, and whether the Board should consider any format requirements, such as proximity rules, or the publication of model disclosures. Q97 – Q99.

<u>Home-equity plans</u>. The Board intends to implement the late payment disclosure for HELOCs as a part of its review of rules affecting home-secured credit. Creditors offering HELOCs may comply with proposed § 226.7(b)(11), at their option.

<u>Charge card issuers</u>. TILA Section 127(b)(12) applies to "creditors." TILA's definition of "creditor" includes card issuers and other persons that offer consumer open-end credit. Issuers of "charge cards" (which are typically products where outstanding balances cannot be carried over from one billing period to the next and are payable when a periodic statement is received) are "creditors" for purposes of specifically enumerated TILA disclosure requirements. 15 U.S.C. 1602(f); § 226.2(a)(17). The new disclosure requirement in TILA Section 127(b)(12) is not among those specifically enumerated.

The Board proposes that charge card issuers are not subject to the late payment disclosure requirements contained in the Bankruptcy Act and to be implemented in new § 226.7(b)(11); the new requirement is not specifically enumerated to apply to charge card issuers. In addition, the Board understands that for some charge card issuers, payments are not considered "late" for purposes of imposing a fee until a second statement is received without a payment. The Board believes it would be undesirable to encourage consumers who in January receive a statement with the balance due upon receipt, for example, to avoid paying the balance when due because a late-payment fee may not be assessed until mid-February; such a disclosure could cause issuers to change such a practice.

<u>Payment due date</u>. Under the proposal, creditors must disclose the due date for a payment if a late-payment fee could be imposed under the credit agreement. The Board interprets this to be a date that is required by the legal obligation and not to encompass

informal "courtesy periods" that are not part of the legal obligation and that creditors may observe for a short period after the stated due date before a late-payment fee is imposed, to account for minor delays in payments such as mail delays. Several commenters asked the Board to clarify that in complying with the new late-payment fee disclosure, creditors need not disclose informal "courtesy periods" not part of the legal obligation. The Board proposes a comment to this effect. See proposed comment 7(b)(11)-1.

Under the statute, creditors must disclose on periodic statements the payment due date or, if different, the earliest date on which the late-payment fee may be charged. Some state laws require that a certain number of days must elapse following a due date before a late-payment fee may be imposed. Under such a state law, the later date arguably would be required to be disclosed on periodic statements. The Board is concerned, however, that such a disclosure would not provide a meaningful benefit to consumers in the form of useful information or protection and would result in consumer confusion. For example, assume a payment is due on March 10 and state law provides that a late payment fee cannot be assessed before March 21. The Board is concerned that highlighting March 20 as the last date to avoid a late payment fee may mislead consumers into thinking that a payment made any time on or before March 20 would have no adverse financial consequences. However, failure to make a payment when due is considered an act of default under most credit contracts, and can trigger higher costs due to interest accrual and perhaps penalty APRs. Particularly in the case of an increased rate that applies to all account balances, the cost of paying late may be significant.

The Board considered additional disclosures on the periodic statement that would more fully explain the consequences of paying after the due date and before the date triggering the late-payment fee, but such an approach appears cumbersome and overly complicated. For those reasons, the Board proposes that creditors must disclose the due date under the terms of the legal obligation, and not a date different than the due date, such as when creditors are required by state or other law to delay for a specified period imposing a late-payment fee when a payment is received after the due date. Consumers' rights under state laws to avoid the imposition of late-payment fees during a specified period following a due date are unaffected by the proposal; that is, in the above example, the creditor would disclose March 10 as the due date for purposes of § 226.7(b)(11), but could not, under state law, assess a late-payment fee before March 21. However, the proposal would provide additional protections to consumers by not requiring a disclosure that a late-payment fee will be imposed only after a specified period after the due date, which, if followed, may result in even more costly consequence of an increased penalty rate.

Cut-off time for making payments. As discussed in the section-by-section analysis to § 226.10(b), the Board proposes to require that creditors disclose any cut-off time for receiving payments closely proximate to each reference of the due date, if the cut-off time is before 5 p.m. on the due date. If cut-off times prior to 5 p.m. differ depending on the method of payment (such as by check or via the Internet), the creditor must state the earliest time without specifying the method to which it applies. This avoids information overload by potentially identifying several cut-off times. Cut-off hours of 5 p.m. or later may continue to be disclosed under the existing rule (including on the reverse side of periodic statements).

Amount of late payment fee; penalty APR. Creditors must disclose the amount of the late-payment fee and the payment due date on periodic statements, under TILA amendments contained in the Bankruptcy Act. The purpose of the new late payment disclosure requirement is to ensure consumers know the consequences of paying late. To fulfill that purpose, the Board proposes that the amount of the late-payment fee must be disclosed in close proximity to the due date. If the amount of the late-payment fee is based on outstanding balances, the proposal would permit the creditor to disclose either the fee that would apply to that specific balance, or the highest fee in the range (e.g., "up to" a stated dollar amount).

In addition, the Board believes that an equally (or more) important consequence of paying late is the potential increase in APRs. The extent of rate increases may be substantial, particularly where the increased APR applies to all existing balances, including balances at low promotional rates. Further, the increased APR may apply for a lengthy period of time (although if the creditor imposes a penalty rate, the increase would not become effective for at least 45 days, under the Board's proposal). See proposed § 226.9(g). The Board is concerned that if the disclosure refers to only the late payment fee, consumers may overlook the more costly consequence of penalty rates. Therefore, the Board proposes to require creditors to disclose any increased rate that may apply if consumers' payments are received after the due date. If, under the terms of the account agreement, a late payment could result in the loss of a promotional rate, the imposition of a penalty rate, or both, the creditor must disclose the highest rate that could apply, to avoid information overload. Under the proposal, the increased APR would be disclosed closely proximate to the fee and due date, as set forth in proposed § 226.7(b)(13). The Board believes this fulfills Congress's intent to warn consumers about the effects of paying late.

**7(b)(12) Minimum Payment**

The Bankruptcy Act amends TILA Section 127(b) to require creditors that extend open-end credit to provide a disclosure on the front of each periodic statement in a prominent location about the effects of making only minimum payments. 15 U.S.C. § 1637(b)(11). This disclosure must include: (1) a "warning" statement indicating that making only the minimum payment will increase the interest the consumer pays and the time it takes to repay the consumer's balance; (2) a hypothetical example of how long it would take to pay off a specified balance if only minimum payments are made; and (3) a toll-free telephone number that the consumer may call to obtain an estimate of the time it would take to repay their actual account balance.

Under the Bankruptcy Act, depository institutions may establish and maintain their own toll-free telephone numbers or use a third party. In order to standardize the information provided to consumers through the toll-free telephone numbers, the Bankruptcy Act directs the Board to prepare a "table" illustrating the approximate number of months it would take to repay an outstanding balance if the consumer pays only the required minimum monthly payments and if no other advances are made. The Board is directed to create the table by assuming a significant number of different APRs, account balances, and minimum payment amounts; instructional guidance must be provided on how the information contained in the table should be used to respond to consumers' requests. The Board is also required to establish and maintain, for two years, a toll-free telephone number for use by customers of creditors that are depository institutions having assets of $250 million or less. The Federal Trade Commission (FTC) must maintain a toll-free telephone number for creditors that are not depository institutions. 15 U.S.C. 1637(b)(11)(A)-(C).

The Bankruptcy Act provides that consumers who call the toll-free telephone number may be connected to an automated device through which they can obtain repayment information by providing information using a touch-tone telephone or similar device, but consumers who are unable to use the automated device must have the opportunity to be connected to an individual from whom the repayment information may be obtained. Creditors, the Board and the FTC may not use the toll-free telephone number to provide consumers with repayment information other than the repayment information set forth in the "table" issued by the Board. 15 U.S.C. 1637(b)(11)(F)-(H).

Alternatively, a creditor may use a toll-free telephone number to provide the actual number of months that it will take consumers to repay their outstanding balance instead of providing an estimate based on the Board-created table. A creditor that does so also need not include a hypothetical example on its periodic statements, but must disclose the warning statement and the toll-free telephone number on its periodic statements. 15 U.S.C. 1637(b)(11)(J)-(K).

For ease of reference, the Board will refer to the above disclosures about the effects of making only the minimum payment as "the minimum payment disclosures."

<u>Proposal to limit the minimum payment disclosure requirements to credit card accounts</u>. Under the Bankruptcy Act, the minimum payment disclosures apply to all open-end accounts (such as credit card accounts, HELOCs, and general-purpose credit lines). The Act expressly states that these disclosure requirements do not apply, however, to any "charge card" account, the primary aspect of which is to require payment of charges in full each month.

In the October 2005 ANPR, the Board requested comment on whether certain open-end accounts should be exempted from some or all of the minimum payment disclosure requirements. Q59. Many industry commenters urged the Board to limit the minimum payment disclosure requirements to credit card accounts because they believed that Congress intended the minimum payment disclosures only for such accounts. On the other hand, several consumer groups urged the Board to apply the minimum payment disclosures to all open-end plans because they believed that these disclosures could be useful to consumers for all open-end products, including HELOCs.

The Board is proposing to exempt open-end credit plans other than credit card accounts from the minimum payment disclosure requirements. This exemption would cover, for example, HELOCs (including open-end reverse mortgages), overdraft lines of credit and other general-purpose personal lines of credit.

The debate in Congress about the minimum payment disclosures focused on credit card accounts. For example, Senator Grassley, a primary sponsor of the Bankruptcy Act, in discussing the minimum payment disclosures, stated:

> [The Bankruptcy Act] contains significant new disclosures for consumers, mandating that credit card companies provide key information about how much [consumers] owe and how long it will take to pay off their credit card debts by only making the minimum payment. That is very important consumer education for every one of us.
>
> Consumers will also be given a toll-free number to call where they can get information about how long it will take to pay off their own credit card balances if they only pay the minimum payment. This will educate consumers and improve consumers' understanding of what their financial situation is.

Remarks of Senator Grassley (2005), Congressional Record (daily edition), vol. 151, March 1, p. S 1856.

Thus, it appears the principal concern of Congress was that consumers may not be fully aware of the length of time it takes to pay off their credit card accounts if only minimum monthly payments are made. The concern expressed by Congress for credit card accounts does not necessarily apply to other types of open-end credit accounts. These other types of open-end accounts are discussed below.

1. HELOCs. Many industry commenters requested that HELOCs be exempted from the minimum payment disclosure requirements. These commenters indicated that most HELOCs have a fixed repayment period specified in the account agreement, so that consumers know from the account agreement the length of the draw period and the length of the repayment period. Nonetheless, several consumer groups urged that HELOCs should not be exempted entirely. They advocated a warning to HELOC consumers that they can pay down the balance faster and save on finance charges if they pay more than the minimum monthly payment required.

Based on the comments received in response to the October 2005 ANPR as well as other information, the Board understands that most HELOCs have a fixed repayment period. Thus, for those HELOCs, consumers could learn from the current disclosures the length of the draw period and the repayment period. See current § 226.6(e)(2). The minimum payment disclosures would not appear to provide useful information to consumers that is not already disclosed to them. The cost of providing this information a second time, including the costs to reprogram periodic statement systems and to establish and maintain a toll-free telephone number, may not be justified by the limited benefit to consumers. Thus, the Board proposes to exempt HELOCs from the minimum payment disclosures requirements at this time, but will consider changes to HELOC disclosures as part of the HELOC review.

2. Open-end reverse mortgages. An open-end reverse mortgage is a HELOC that is designed to allow consumers to convert the equity in their homes into cash. During an extended "draw" period consumers continue living in their homes, can draw on the line of credit to the extent they repay any outstanding balance. The principal and interest become due when the homeowner moves, sells the home, or dies. Consumers with open-end reverse mortgages would not likely benefit from the minimum payment disclosures, because these disclosures would be based on assumptions about events difficult to predict, such as when the homeowner will move, sell the house or die.

3. Overdraft lines of credit and other general-purpose personal lines of credit. In response to the October 2005 ANPR, several industry commenters suggested that the Board exempt overdraft lines of credit from the minimum payment disclosure requirements. For example, one industry trade group indicated that overdraft lines of credit have relatively low credit limits and are not intended as a long term credit option. The commenter also indicated that features and terms of overdraft lines of credit vary widely from institution to institution. Some banks require that an overdraft line of credit be paid in full within a short period after the consumer receives notice that the overdraft line has been used. Other banks permit longer periods of time to repay, but those periods and the size of any minimum payment vary significantly from bank to bank. This commenter indicated that the cost to small institutions of providing the minimum payment disclosures might cause them to stop providing overdraft products.

The Board is proposing to exempt overdraft lines of credit and other general-purpose credit lines from the minimum payment disclosure requirements for several reasons. First, these lines of credit are not in wide use. The 2004 Survey of Consumer Finances data indicates that few families – 1.6 percent – had a balance on lines of credit other than a home-equity line or credit card at the time of the interview. (In terms of comparison, 74.9 percent of families had a credit card, and 58 percent of these families had a credit card balance at the time of the interview.)[16] Second, these lines of credit typically are neither promoted, nor used, as long-term credit options of the kind for which the minimum payment disclosures are intended. Third, the Board is concerned that the operational costs of requiring creditors to comply with the minimum payment disclosure requirements with respect to overdraft lines of credit and other general-purpose lines of credit may cause some institutions to no longer provide these products as accommodations to consumers, to the detriment of consumers who currently use these products. For these reasons, the Board is proposing to exempt overdraft lines of credit and other general-purpose credit lines from the minimum payment disclosure requirements.

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[16] Brian Bucks, et al., Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances, FEDERAL RESERVE BULLETIN (March 2006).

**7(b)(12)(i) General Disclosure Requirements**

Under the Bankruptcy Act, the hypothetical example that creditors must disclose on periodic statements varies depending on the creditor's minimum payment requirement. Generally, creditors that require minimum payments equal to 4 percent or less of the account balance must disclose on each statement that it takes 88 months to pay off a $1000 balance at an interest rate of 17 percent if the consumer makes a "typical" 2 percent minimum monthly payment. Creditors that require minimum payments exceeding 4 percent of the account balance must disclose that it takes 24 months to pay off a balance of $300 at an interest rate of 17 percent if the consumer makes a "typical" 5 percent minimum monthly payment (but a creditor may opt instead to disclose the statutory example for 2 percent minimum payments). The 5 percent minimum payment example must be disclosed by creditors for which the FTC has the authority under the Truth in Lending Act to enforce the act and this regulation. Creditors also have the option to substitute an example based on an APR that is greater than 17 percent. The Bankruptcy Act authorizes the Board to periodically adjust the APR used in the hypothetical example and to recalculate the repayment period accordingly. 15 U.S.C. § 1637(b)(11)(A)-(E).

Wording of the examples. The Bankruptcy Act sets forth specific language for issuers to use in disclosing the applicable hypothetical example on the periodic statement. The Board proposes to amend the statutory language to facilitate consumers' use and understanding of the disclosures, 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). First, the Board proposes to require that issuers disclose the payoff periods in the hypothetical examples in years, rounding fractional years to the nearest whole year, rather than in months as provided in the statute. Thus, issuers would disclose that it would take over 7 years to pay off the $1,000 hypothetical balance, and about 2 years for the $300 hypothetical balance. The Board believes that disclosing the payoff period in years allows consumers to better comprehend the repayment period without having to convert it themselves from months to years. Participants in the consumer testing conducted for the Board reviewed disclosures with the estimated payoff period in years, and they indicated they understood the length of time it would take to repay the balance if only minimum payments were made. Consumers may also appreciate more that the repayment periods are merely estimates.

Second, the statute requires that issuers disclose in the examples the minimum payment formula used to calculate the payoff period. In the $1,000 example above, the statute would require issuers to indicate that a "typical" 2 percent minimum monthly payment was used to calculate the repayment period. In the $300 example above, the statute would require issuers to indicate that a 5 percent minimum monthly payment was used to calculate the repayment period. The Board proposes to eliminate the specific minimum payment formulas from the examples. The references to the 2 percent minimum payment in the $1,000 example, and a 5 percent minimum payment in the $300 example, are incomplete descriptions of the minimum payment requirement. In the $1,000 example, the minimum payment formula used to the calculate repayment period is the greater of 2 percent of the outstanding balance or $20. In the $300 example, the minimum payment formula used to calculate the repayment period is the greater of 5 percent of the outstanding balance or $15. In fact, in each example, the hypothetical consumer always pays the absolute minimum ($20 or $15, depending on the example).

The Board believes that including the entire minimum payment formula, including the floor amount, in the disclosure could make the example too complicated and have the unintended consequence of misleading a consumer who reads the language set out in the statute into concluding that the payment is smaller than it actually is. While the disclosures could be revised to indicate that the repayment period in the $1,000 balance was calculated based on a $20 payment, and repayment period in the $300 balance was calculated based on a $15 payment, the Board believes that revising the statutory language in this way changes the disclosure to focus consumers on the effects of making a fixed payment each month as opposed to the effects of making minimum payments. Moreover, disclosing the minimum payment formula is not necessary for consumers to understand the essential point of the examples – that it can take a significant amount of time to pay off a balance if only minimum payments are made. In testing conducted for the Board, the $1,000 balance example was tested without including the 2 percent minimum payment disclosure required by the statute. Consumers appeared to understand the purpose of the disclosure—that it would take a significant amount of time to repay a $1,000 balance if only minimum payments were made. For these reasons, the Board is proposing to require the hypothetical examples without a minimum payment formula.

The proposed regulatory language for the examples is set forth in new § 226.7(b)(12)(i). In addition to the revisions mentioned above, the Board also proposes several stylistic revisions to the statutory language, based on plain language principles, in an attempt to make the language of the examples more understandable to consumers.

Adjustments to the APR used in the examples. The Bankruptcy Act specifically authorizes the Board to periodically adjust the APR used in the hypothetical example and to recalculate the repayment period accordingly. In the October 2005 ANPR, the Board requested comment on whether the Board should adjust the APR used in the hypothetical examples, because current APRs on credit cards may be less than the 17 percent APR in the examples. Q62. Commenters were split on whether the Board should adjust the APR in the examples.

The Board is not proposing to adjust the APR used in the hypothetical examples. The Board recognizes that the examples are intended to provide consumers with an indication that it can take a long time to pay off a balance if only minimum payments are made. Revising the APR used in the example to reflect the average APR paid by consumers would not significantly improve the disclosure, because for many consumers an average APR would not be the APR that applies to the consumer's account. Moreover, consumers will be able to obtain a more tailored disclosure of a repayment period based on the APR applicable to their accounts by calling the toll-free telephone number provided as part of the minimum payment disclosure.

**<u>7(b)(12)(ii) Estimate of Actual Repayment Period</u>**

Under the Bankruptcy Act, a creditor may use a toll-free telephone number to provide consumers with the actual number of months that it will take consumers to repay their outstanding balance instead of providing an estimate based on the Board-created table. Creditors that choose to give the actual number via the telephone number need not include a hypothetical example on their periodic statements. Instead, they must disclose on periodic statements a warning statement that making the minimum payment will increase the interest the consumer pays and the time it takes to repay the consumer's balance and a toll-free telephone number that consumers may use to obtain the actual repayment disclosure. 15 U.S.C. 1637(b)(11)(I) and (K). The Board proposes to implement this statutory provision in new § 226.7(b)(12)(ii)(A).

In addition, the Board proposes to provide that if card issuers provide the actual repayment disclosure on the periodic statement, they need not disclose the warning, the hypothetical example and a toll-free telephone number on the periodic statement, nor need they maintain a toll-free telephone number to provide the actual repayment disclosure. <u>See</u> proposed § 226.7(b)(12)(ii)(B).

The Board strongly encourages card issuers to provide the actual repayment disclosure on periodic statements, and solicits comments on whether the Board can take other steps to provide incentives to card issuers to use this approach. A recent study conducted by the GAO on minimum payments suggests that certain cardholders would find the actual repayment disclosure more helpful than the generic disclosures required by the Bankruptcy Act. For this study, the GAO interviewed 112 consumers and collected data on whether these consumers preferred to receive on the periodic statement (1) customized minimum payment disclosures that are based on the consumers' actual account terms (such as the actual repayment disclosure), (2) generic disclosures such as the warning statement and the hypothetical example required by the Bankruptcy Act; or (3) no disclosure.[17] According to the GAO's report, in the interviews with the 112 consumers, most consumers who typically carry credit card balances (revolvers) found customized disclosures very useful and would prefer to receive them in their billing statements. Specifically, 57 percent of the revolvers preferred the customized disclosures, 30 percent preferred the generic disclosures, and 14 percent preferred no disclosure. In addition, 68 percent of the revolvers found the customized disclosure extremely useful or very useful, 9 percent found the disclosure moderately useful, and 23 percent found the disclosure slightly useful or not useful. According to the GAO, the consumers that preferred the customized disclosures liked that such disclosures would be specific to their accounts, would change based on their transactions, and would provide more information than generic disclosures. <u>GAO Report on Minimum Payments</u>, pages 25, 27.

[17] United States Government Accountability Office, <u>Customized Minimum Payment Disclosures Would Provide More Information to Consumers, but Impact Could Vary</u>, 06-434 (April 2006). (The GAO indicated that the sample of 112 consumers was not designed to be statistically representative of all cardholders, and thus the results cannot be generalized to the population of all U.S. cardholders.)

In addition, the Board believes that disclosing the actual repayment disclosure on the periodic statement would simplify the process for consumers and creditors. Consumers would not need to take the extra step to call the toll-free telephone number to receive the actual repayment disclosure, but instead would have that disclosure each month on their periodic statements. Card issuers (other than issuers that may use the Board or the FTC toll-free telephone number) would not have the operational burden of establishing a toll-free telephone number to receive requests for the actual repayment disclosure and the operational burden of linking the toll-free telephone number to consumer account data in order to calculate the actual repayment disclosure.

The Board proposes this approach 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 uniformed use of credit. 15 U.S.C. 1601(a), 1604(a). Section 105(f) authorizes the Board to exempt any class of transactions (with an exception not relevant here) 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). 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 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 it is appropriate to provide an exemption from the requirement to provide on periodic statements a warning about the effects of making minimum payments, a hypothetical example, and a toll-free telephone number consumers may call to obtain repayment periods, and to maintain a toll-free telephone number for responding to consumers' requests, if the creditor instead provides the actual repayment period on the periodic statement. As noted above, consumer testing indicated that actual repayment period information is more useful to consumers than estimated information. Providing that disclosure on a statement rather than over the telephone provides consumers with easier access to the information. Thus, the proposal has the potential to better inform consumers and further the goals of consumer protection and the informed use of credit for credit card accounts. The Board welcomes comment on this matter.

**7(b)(12)(iii) Exemptions**

As explained above, the Board proposes to require the minimum payment disclosures only for credit card accounts. See proposed § 226.7(b)(12)(i). Thus, creditors would not need to provide the minimum payment disclosures for HELOCs (including open-end reverse mortgages), overdraft lines of credit or other general-purpose personal lines of credit. For the same reasons, the Board proposes to exempt these products regardless of whether they can be accessed by a credit card device. Specifically, proposed § 226.7(b)(12)(iii) would exempt the following types of credit card accounts: (1) HELOCs accessible by credit cards that are subject to § 226.5b; (2) overdraft lines of credit tied to asset accounts accessed by check-guarantee cards or by debit cards; and (3) lines of credit accessed by check-guarantee cards or by debit cards that can be used only at automated teller machines. See proposed § 226.7(b)(12)(iii)(A)-(C). The Board also proposes to exempt charge cards from the minimum payment disclosure requirements, to implement TILA Section 127(b)(11)(I). 15 U.S.C. § 1637(b)(11)(I); See proposed § 226.7(b)(12)(iii)(D).

Exemption for credit card accounts with a specific repayment period. In the October 2005 ANPR, the Board requested comment on whether certain open-end accounts should be exempted from some or all of the minimum payment disclosure requirements, such as open-end plans that have a fixed repayment period. Q59. Industry commenters generally supported an exemption for open-end plans that have a fixed repayment period. These commenters indicated that the minimum payment disclosures are not necessary in this context, because the consumer will already know from the account agreement how long it will take to repay the balance.

The Board proposes to exempt credit card accounts where a fixed repayment period for the account is specified in the account agreement and the required minimum payments will amortize the outstanding balance within the fixed repayment period. See proposed § 226.7(b)(12)(iii)(E). The minimum payment disclosures would not appear to provide useful information to consumers that they do not already have in their account agreements. The cost of providing this information a second time, including the costs to reprogram periodic statement systems and to establish and maintain a toll-free telephone number, may not be justified by the limited benefit to consumers.

In order for this proposed exemption to apply, a fixed repayment period must be specified in the account agreement. As proposed, this exemption would include, for example, accounts where the account has been closed due to delinquency and the required monthly payment has been reduced or the balance decreased to accommodate a fixed payment for a fixed period of time designed to pay off the outstanding balance. See proposed comment 7(b)(12)(iii)-1. This exemption would not apply where the credit card may have a fixed repayment period for one credit feature, but an indefinite repayment period on another feature. For example, some retail credit cards have several credit features associated with the account. One of the features may be a general revolving feature, where the minimum payment for this feature does not pay off the balance in a specific period of time. The card also may have another feature that allows consumers to make specific types of purchases (such as furniture purchases, or other large purchases), and the minimum payments for that feature will pay off the purchase within a fixed period of time, such as one year. New comment 7(b)(12)(iii)-1 makes clear that the exemption relating to a fixed repayment period does not apply to the above situation, because the retail card account as a whole does not have a fixed repayment period.

Exemption where cardholders have paid their accounts in full for two consecutive months. In the October 2005 ANPR, the Board requested comment on whether the Board should exempt credit card accounts of consumers who typically do not revolve balances or make monthly payments that regularly exceed the minimum. Q60. In response to the October 2005 ANPR, several industry commenters urged the Board to exempt card issuers from providing minimum payment disclosures to consumers who do not regularly make minimum payments. These commenters indicated that excluding non-minimum payers is appropriate because the minimum payment disclosures are less meaningful to those consumers. On the other hand, several consumer groups indicated that the Board should not provide an exemption based on the characteristics or habits of the accountholder, such as whether they typically pay in full. These commenters indicated that the typical behavior of a particular consumer can change quickly, due either to a temporary change in circumstances (a move, a layoff, or a major medical expense) or a permanent change (the death of a spouse or a disability). The consumer groups believed that in these circumstances, it is important that consumers have disclosure about the effects of paying the minimum payments in a timely fashion, before an outstanding balance grows unmanageable.

The Board proposes to provide that card issuers are not required to comply with minimum payment disclosure requirements for a particular billing cycle if a consumer has paid the entire balance in full for the previous two billing cycles. See proposed § 226.7(b)(12)(iii)(F). The GAO found in its study on minimum payment disclosures that cardholders who pay their balances in full each month (non-revolvers) were generally satisfied with receiving generic disclosures or none at all, and did not prefer customized disclosures such as actual repayment disclosures. Thirty-seven percent of non-revolvers found the customized disclosure extremely or very useful. Eight percent of non-revolvers found the customized disclosure moderately useful and 55 percent found it slightly or not useful. The GAO indicated that many of the non-revolvers it interviewed who preferred not to receive a customized disclosure explained that they paid their balance in full each month, already understood the consequences of making only minimum payments, and did not need the additional reminder. See GAO Report on Minimum Payments, pages 26, 30-31.

Thus, because non-revolvers may not find the minimum payment disclosures very useful or meaningful, the Board proposes to exempt card issuers from the requirement to provide the minimum payment disclosures in a particular billing cycle if a consumer has paid the entire balance in full for the two previous billing cycles. For example, if a consumer paid the entire balance in full for account activity in March and April, the creditor would not be required to provide the minimum payment disclosure for the statement representing account activity in May. The Board believes this approach strikes an appropriate balance between benefits to consumers from the disclosures, and compliance burdens on issuers in providing the disclosures. Consumers who might benefit from the disclosures will receive them. Consumers who carry a balance each month will always receive the disclosure, and consumers who pay in full each month will not. Consumers who sometimes pay their bill in full and sometimes do not will receive the minimum payment disclosures if they do not pay in full the prior two consecutive months (cycles). Also, if a consumer's typical payment behavior changes from paying in full to revolving, the consumer will begin receiving the minimum payment disclosures after not paying in full one billing cycle, when the disclosures would appear to be timely. In addition, creditors already typically track whether a consumer has paid their balance in full for two consecutive months. Typically, creditors provide a grace period on new purchases to consumers (that is, creditors do not charge interest to consumers on new purchases) if consumers paid both the current balance and the previous balance in full. Thus, creditors currently capture payment history for consumers for two billing cycles.

In response to the October 2005 ANPR, one industry commenter indicated that many creditors do not have the processing systems that are capable of selectively pricing the disclosures from month-to-month based on customers' prior payment patterns. Card issuers are not required to take advantage of this exemption from providing the minimum payment disclosures for a particular billing cycle if a consumer has paid the entire balance in full for the previous two billing cycles. Card issuers may provide the minimum payment disclosures to all of its cardholders, even to those cardholders that fall within this exemption. If issuers choose to provide voluntarily the minimum payment disclosures to those cardholders that fall within this exemption, issuers should follow the disclosures rules set forth in § 226.7(b)(12), the accompanying commentary, and Appendices M1-M3 (as appropriate) for those cardholders.

Exemption where balance has fixed repayment period. In response to the October 2005 ANPR, several industry commenters urged the Board to exempt credit cards with fixed payment features from the minimum payment disclosures. As described above, some retail credit cards may have several features on the card. One of those features may allow consumers to make certain types of purchases with the feature (such as furniture purchases, or other large purchases), and the minimum payments for that feature will pay off the purchase within a specific period of time, such as one year. Some commenters indicated that these types of accounts should be exempted from the minimum payment disclosure requirements because consumers would know the repayment period from the account agreement.

The Board proposes to exempt credit card issuers from providing the minimum payment disclosures on periodic statements in a billing cycle where the entire outstanding balance held by consumers in that billing cycle is subject to a fixed repayment period specified in the account agreement and the required minimum payments applicable to this feature will amortize the outstanding balance within the fixed repayment period. This exemption is meant to cover the retail cards described above in those cases where the entire outstanding balance held by a consumer in a particular billing cycle is subject to a fixed repayment period specified in the account agreement. The minimum payment disclosures would not appear to provide useful information to consumers in this context because consumers would be able to learn from their account agreements how long it would take to repay the balance. The cost of providing this information a second time, including the costs to reprogram periodic statement systems and to establish and maintain a toll-free telephone number, may not be justified by the limited benefit to consumers. See proposed comment 7(b)(12)(iii)-2.

Other exemptions. In response to the October 2005 ANPR, several commenters suggested other exemptions to the minimum payment requirements, as discussed below. For the reasons discussed below, the Board is not proposing to include these exemptions.

1. Exemption for discontinued credit card products In response to the October 2005 ANPR, one commenter urged the Board to provide a partial exemption for credit card products for which no new accounts are being opened and for which existing accounts are closed to new transactions. With respect to these products, the commenter urged the Board to exempt issuers of these products from having to place the minimum payment disclosures on the periodic statement, but instead allow issuers to provide these notices in freestanding inserts to the periodic statements. The commenter indicates that the number of accounts that are discontinued are usually very small and the computer systems used to produce the statements for the closed accounts are being phased out.

The Board solicits further comment on why this exemption is needed. What are the costs of redesigning the old computer systems to provide the minimum payment disclosures (that is, the warning statement, the hypothetical example, and the toll-free telephone number) on the periodic statements?

2. Exemption for credit card accounts purchased within the last 18 months. In response to the October 2005 ANPR, one commenter urged the Board to provide an exemption for accounts purchased by a credit card issuer. With respect to these purchased accounts, the commenter urged the Board to exempt issuers from placing the minimum payment disclosures on the periodic statement during a transitional period (up to 18 months) while the purchasing issuer converts the new accounts to its statement system. In this situation, the commenter indicated that issuers should be allowed to provide these notices in freestanding inserts to the periodic statements.

The Board solicits further comment on why this exemption is needed. Why could the purchasing issuer not continue to use the periodic statement system and toll-free telephone numbers used by the selling issuer to meet the requirements of the minimum payment disclosures, until the purchased accounts are converted to the purchaser's systems?

3. Credit card products that do not use declining balance amortization. One commenter suggested that the Board exempt from the minimum payment disclosure requirements credit card products that do not use declining balance amortization to calculate the minimum payment. For example, some retail credit cards base their minimum payment formula on the original purchase price or similar amount, rather than on the declining balance. The commenter indicates that these products should be exempt because amortization schedules for these products result in far shorter repayment periods. The Board is proposing not to adopt this exemption because even though the amortization

schedules for these products may be shorter than for cards where the minimum payment is calculated on the declining balance, the payoff time may not be so short as to justify an exemption. For example, assume the minimum payment formula is 3.33 percent of the highest balance or $10, whichever is greater. It could still take around 4 years to pay off a $500 balance at a 21.9 percent APR if a consumer only made minimum payments. (For contrast, the repayment period would be around 7 years if the minimum payment was calculated based on the outstanding balance, instead of the highest balance.)

4. <u>Credit cards with balances of less than $500</u>. One commenter suggested that the Board exempt credit card accounts from the minimum payment disclosure requirements in cases where the balance on the card is less than $500. This commenter indicated in cases of low balances, the repayment period is fairly short and so the minimum payment disclosure is less needed. The Board is not proposing to exempt these credit card accounts. Depending on how the minimum payment is calculated, it can still take a significant amount of time to pay off a $500 balance if only minimum payments are made. For example, assume the minimum payment is calculated based on the following formula: the greater of (1) 1 percent of the outstanding balance plus interest charges that accrued in the past month; or (2) $10. It could still take around 5 years to repay a $500 balance at a 7.99 percent APR if only minimum payments are made.

**<u>7(b)(12)(iv) Toll-free Telephone Numbers</u>**

Under Section 1301(a) of the Bankruptcy Act, depository institutions generally must establish and maintain their own toll-free telephone numbers or use a third party to disclose the repayment estimates based on the "table" issued by the Board. 15 U.S.C. 1637(b)(11)(F)(i). At the issuer's option, the issuer may disclose the actual repayment disclosure through the toll-free telephone number. The Board also is required to establish and maintain, for two years, a toll-free telephone number for use by customers of depository institutions having assets of $250 million or less. 15 U.S.C. 1637(b)(11)(F)(ii). The FTC must maintain a toll-free telephone number for creditors other than depository institutions. 15 U.S.C. 1637(b)(11)(F).

The Bankruptcy Act also provides that consumers who call the toll-free telephone number may be connected to an automated device through which they can obtain repayment information by providing information using a touch-tone telephone or similar device, but consumers who are unable to use the automated device must have the opportunity to be connected to an individual from whom the repayment information may be obtained. Unless the issuer is providing an actual repayment disclosure, the issuer may not provide through the toll-free telephone number a repayment estimate other than estimates based on the "table" issued by the Board. 15 U.S.C. 1637(b)(11)(F). These same provisions apply to the FTC's and the Board's toll-free telephone numbers as well.

The Board proposes to add new § 226.7(b)(12)(iv) and accompanying commentary to implement the above statutory provisions related to the toll-free telephone numbers. In addition, new comment 7(b)(12)(iv)-3 would provide that once a consumer has indicated that he or she is requesting the generic repayment estimate or the actual repayment disclosure, as applicable, card issuers may not provide advertisements or marketing information to the consumer prior to providing the repayment information required or permitted by Appendix M1 or M2, as applicable.

**7(b)(12)(v) Definitions**

As discussed above, Section 1301(a) of the Bankruptcy Act requires the Board to establish and maintain, for two years, a toll-free telephone number for use by customers of depository institutions having assets of $250 million or less. 15 U.S.C. 1637(b)(11)(F)(ii). For ease of reference in the regulation, the Board proposes to define the above depository institutions as "small depository institution issuers." See proposed § 226.7(b)(12)(v).

**7(b)(13) Format Requirements**

As discussed throughout this section-by-section analysis to § 226.7, consumer testing conducted for the Board indicates improved understanding when related information is grouped together. Under the proposal, creditors would group together when a payment is due (due date and cut-off time if before 5 p.m.), how much is owed (minimum payment and ending balance), and what the potential costs are for paying late (late-payment fee, and penalty APR if triggered by a late payment). See proposed Samples G-18(E) and G-18(F) in Appendix G. The proposed format requirements are intended to fulfill Congress's intent to have the new late payment and minimum payment disclosures ensure consumers' ability to understand the consequences of paying late or making only minimum payments.

**7(b)(14) Change-in-terms and Increased Penalty Rate Summary for Open-end (not Home-secured) Plans**

A major goal of its review of Regulation Z's open-end credit rules is to address consumers' surprise at increased rates (and/or fees). In part, the Board is addressing the issue in § 226.9(c) and § 226.9(g) to give more time before new rates and changes to significant costs become effective. See proposed § 226.9(c)(2) and § 226.9(g). The proposed new § 226.7(b)(14) is intended to enable consumers to notice more easily changes in their account terms. Increasing the time period to act is ineffective if consumers do not see the change-in-term notice. Consumers who participated in testing conducted for the Board consistently set aside change of term notices that accompanied periodic statements. Research conducted for the Board indicates that consumers do look at the front side of periodic statements and do look at transactions. Therefore, when a change-in-terms notice is provided on or with a periodic statement the proposal would require a summary of key changes to precede transactions. In addition, when a notice of a rate increase due to delinquency or default or as a penalty is provided on or with a periodic statement, the proposal would require this notice to precede transactions. Samples G-20 and G-21 in Appendix G illustrate the proposed format requirement under § 226.7(b)(14) and the level of detail required for the notice under § 226.9(c)(2)(iii) and § 226.9(g)(3). Forms G-18(G) and G-18(H) illustrate the placement of these notices on a periodic statement.

**<u>Section 226.8 Identifying Transactions on Periodic Statements</u>**

TILA Section 127(b)(2) requires creditors to identify on periodic statements credit extensions that occurred during a billing cycle. 15 U.S.C. 1637(b)(2). The statute calls for the Board to implement requirements that are sufficient to identify the transaction or to relate the credit extension to sales vouchers or similar instruments previously furnished. The rules for identifying transactions are implemented in § 226.8, and vary depending on whether: (1) the sales receipt or similar credit document is included with the periodic statement, (2) the transaction is sale credit (purchases) or nonsale credit (cash advances, for example), and (3) the creditor and seller are the "same or related." TILA's billing error protections include consumers' requests for additional clarification about transactions listed on a periodic statement. 15 U.S.C. 1666(b)(2); § 226.13(a)(6).

The Board proposes to update and simplify the rules for identifying sales transactions when the sales receipt or similar document is not provided with the periodic statement (so called "descriptive billing"), which is typical today. The rules for identifying transactions where such receipts accompany the periodic statement are not affected by the proposal. The proposed changes reflect current business practices and consumer experience, and are intended to ease compliance. Currently, creditors that use descriptive billing are required to include on periodic statements an amount and date as a means to identify transactions, and the proposal would not affect those requirements. As an additional means to identify transactions, current rules contain description requirements that differ depending on whether the seller and creditor are "same or related." For example, a retail department store with its own credit plan (seller and creditor are same or related) sufficiently identifies purchases on periodic statements by providing the department such as "jewelry" or "sporting goods;" item-by-item descriptions are not required. Periodic statements provided by issuers of general purpose credit cards, where the seller and creditor are not the same or related, identify transactions by the seller's name and location.

The Board proposes to provide additional flexibility to creditors that do not provide sales slips or similar documents with the periodic statement. Under the proposal, all creditors would be permitted to identify sales transactions (in addition to the amount and date) by the seller's name and location. Thus, creditors and sellers that are the same or related could, at their option, identify transactions by a brief identification of goods or services, which they are currently required to do in all cases, or they could provide the seller's name and location for each transaction. Guidance on the level of detail required to describe amounts, dates, the identification of goods, or the seller's name and location remains unchanged.

The Board's proposal is guided by several factors. The standard set forth by TILA for identifying transactions on periodic statements is quite broad. 15 U.S.C. 1637(b)(2). Whether a general description such as "sporting goods" or the store name and location would be more helpful to a consumer can depend on the situation. Many retailers permit consumers to purchase in a single transaction items from a number of departments; in that case, the seller's name and location may be as helpful as the description of a single department from which several dissimilar items were purchased. Also, the seller's name and location has become the more common means of identifying transactions, as the use of general purpose cards increases and the number of store-only cards decreases. Under the proposed rule, retailers that commonly accept general purpose credit cards but also offer a credit card account or other open-end plan for use only at their store would not be required to maintain separate systems that enable different descriptions to be provided, depending on the type of card used. Finally, it appears that any consumer benefits would be minimally affected by the proposed change because many retailers permit purchases from different departments to be charged in a single transaction. Moreover, consumers are likely to carefully review transactions on periodic statements and inquire about transactions they do not recognize, such as when a retailer is identified by its parent company on sales slips which the consumer may not have noticed at the time of the transaction. Moreover, consumers are protected under TILA with the ability to assert a billing error to seek clarification about transactions listed on periodic statements, and are not required to pay the disputed amount while the creditor obtains the necessary clarification. Maintaining rules that require more standardization and detail would be costly, and likely without significant corresponding consumer benefit. Thus, the proposal is intended to provide flexibility for creditors without reducing consumer protection.

The Board notes, however, that some retailers offering their own open-end credit plans tie their inventory control systems to their systems for generating sales receipts and periodic statements. In these cases, purchases listed on periodic statements may be described item by item, for example, to indicate brand name such as "XYZ Sweater." This item-by-item description, while not required under current or proposed rules, would remain permissible under the proposal; thus, no operational changes would be required for these retailers.

To implement the approach described above, § 226.8 would be revised as follows. Section 226.8(a)(1) would set forth the proposed rule providing flexibility in identifying sales transactions, as discussed above. Section 226.8(a)(2) would contain the existing rules for identifying transactions when sales receipts or similar documents accompany the periodic statement. Section 226.8(b) is revised for clarity. A new § 226.8(c) would be added to set forth rules now contained in footnotes 16 and 19; and, without references to "same or related" parties, footnotes 17 and 20. The substance of footnote 18, based on a statutory exception where the creditor and seller are the same person, would be deleted as unnecessary. The title of the section would be revised for clarity.

The commentary to § 226.8 would be reorganized and consolidated but would not be substantively changed. Comments 8-1, 8(a)-1, and 8(a)(2)-4 would be deleted as duplicative. Similarly, comments 8-6 through 8-8, which provide creditors with flexibility in describing certain specific classes of transactions regardless of whether they are "related" or "nonrelated" sellers or creditors, would be deleted as unnecessary. Existing comments 8-4 and 8(a)(2)-3, which provide guidance when copies of credit or sales slips accompany the statement, also would be deleted. The Board believes this practice is no longer common, and to the extent sales or similar credit documents accompany billing statements, additional guidance seems unnecessary. Proposed § 226.8(a)(1)(ii) and comments 8(a)-3 and 8(a)-7, which provide guidance for identifying mail or telephone transactions, also would refer to Internet transactions. Proposed comment 8(a)-1 would provide an example of new services that are now commonly purchased from creditors as well as third party service providers (sale credit).

**Section 226.9 Subsequent Disclosure Requirements**

Section 226.9 sets forth a number of disclosure requirements that apply after an account is opened, including a requirement to provide billing rights statements annually, a requirement to provide at least 15 days advance notice whenever a term required to be disclosed in the account-opening disclosures is changed, and a requirement to provide finance charge disclosures whenever credit devices or features are added on terms different from those previously disclosed.

With respect to open-end (not home-secured) plans, the Board proposes a number of substantive and technical revisions to § 226.9 and the accompanying commentary, as further described below. The proposal would require certain disclosures to accompany checks that access a credit card account. In addition, the proposal would require creditors to provide a summary table of a limited number of key terms if those terms are changed. The summary table would appear on the first page of the notice or a separate piece of paper. Moreover, if the change-in-terms notice is included with a periodic statement, that summary table would be required to be provided on the front of the first page of the periodic statement, before the list of transactions for the statement period. Also, the Board would require creditors to provide advance notice when a rate is increased due to a consumer's delinquency or default or as a penalty. The Board's proposal also would require creditors to provide 45 days advance notice for changes in terms or increases in rates due to delinquency or default or penalty pricing. Home-equity lines of credit (HELOCs) subject to § 226.5b would not be affected by these proposed revisions. For the reasons set forth in the section-by-section analysis to § 226.6(b)(1), the Board would update references to "free-ride period" as "grace period" in the regulation and commentary, without any intended substantive change.

**9(a) Furnishing Statement of Billing Rights**

TILA Section 127(a)(7) and § 226.9(a) require creditors to mail or deliver a billing error rights statement annually, either to all consumers or to each consumer entitled to receive a periodic statement. 15 U.S.C. 1637(a)(7). (See Model Form G-3.) Alternatively, creditors may provide a billing rights statement on each periodic statement. (See Model Form G-4.) Both the regulation and commentary would be unchanged under the proposal. However, the Board proposes to revise both Model Forms G-3 and G-4 to improve the readability of these notices. The revised forms are in G-3(A) and G-4(A) of Appendix G. For open-end (not home-secured) plans, creditors may use Model Forms G-3(A) and G-4(A). For HELOCs subject to the requirements of § 226.5b, creditors may use the current Model Forms G-3 and G-4, or the revised forms.

**9(b) Disclosures for Supplemental Credit Access Devices and Additional Features**

Section 226.9(b) requires certain disclosures when a creditor adds a credit device or feature to an existing open-end plan. When a creditor adds a credit feature or delivers a credit device to the consumer within 30 days of mailing or delivering the account-opening disclosures under current § 226.6(a), and the device or feature is subject to the same finance charge terms previously disclosed, the creditor is not required to provide additional disclosures. If the credit feature or credit device is added more than 30 days after mailing or delivering the account-opening disclosures, and is subject to the same finance charge terms previously disclosed in the account-opening agreement, the creditor must disclose that the feature or device is for use in obtaining credit under the terms previously disclosed. However, if the added credit device or feature has finance charge terms that differ from the disclosures previously given under § 226.6(a), then the disclosures required by § 226.6(a) that are applicable to the added feature or device must be given before the consumer uses the new feature or device.

In the December 2004 ANPR, the Board solicited comment as to whether there are formatting tools or navigational aids that could more effectively link information in account-opening disclosures with information provided in subsequent disclosures under § 226.9(b), such as checks that access a credit card account. Q45. Many creditors commented that there would be no benefit to linking subsequent disclosures and account-opening disclosures because many consumers fail to retain the information they receive at account opening. Several creditors commented that improved formatting could improve consumer understanding; however, they were concerned about overly prescriptive requirements that might hinder creditors' ability to tailor their disclosure formats to their products and product terms. Some creditors and consumer groups suggested importing the tabular format used to disclose information in credit card or charge card applications and solicitations to the subsequent disclosure context.

The Board is proposing to retain the current rules set forth in §§ 226.9(b)(1) and 226.9(b)(2) for all credit devices and credit features except checks that access a credit card account. With respect to such checks, the Board is concerned that the current rule in § 226.9(b)(1) may not communicate effectively to the consumer the material terms of checks that access a credit card account, when those checks are mailed or sent to a consumer 30 days or more after the § 226.6 disclosures for the underlying account are provided. The Board agrees with commenters that, after a significant time has passed, it becomes less likely that consumers will still have a copy of the account-opening disclosures, and all relevant change-in-terms notices.

With respect to open-end (not home-secured) plans, the Board is proposing to create a new § 226.9(b)(3) that would require that certain information be disclosed each time that checks that access a credit card account are mailed to a consumer, for checks mailed more than 30 days following the delivery of the account-opening disclosures. This provision would apply regardless of whether that information was previously included in the account-opening disclosures. As under the current regulation, no additional disclosures would be required when a creditor provides, within 30 days of the account-opening disclosures, checks that access a credit card account, if the finance charge terms are the same as those that were previously disclosed. HELOCs would not be affected by this proposed revision.

Creditors would be required to provide the new § 226.9(b)(3) disclosures on the front of the page containing the checks that access a credit card account. Specifically, the proposed amendments would require the following key terms be disclosed on the front of the page containing the checks: (1) any discounted initial rate, and when that rate will expire, if applicable; (2) the type of rate that will apply to the checks after expiration of any discounted initial rate (such as whether the purchase or cash advance rate applies) and the applicable annual percentage rate; (3) any transaction fees applicable to the checks; and (4) whether a grace period applies to the checks, and if one does not apply, that interest will be charged immediately. If a discounted initial rate applies, a creditor must disclose the type of rate that will apply after the discounted initial rate expires, and the rate that will apply after the discounted initial rate expires. The disclosures must be accurate as of the time the disclosures are given. A variable annual percentage rate is accurate if it was in effect within 30 days of when the disclosures are given. Proposed § 226.9(b)(3) would require that these key terms be disclosed in a tabular format substantially similar to Sample G-19 in Appendix G.

It is the Board's understanding that checks that access a credit card account often are mailed with the periodic statement, so consumers will frequently receive an updated disclosure of the periodic rate in the same envelope as the checks. The Board considered permitting creditors to disclose the rate that applies to a check by means of a reference to the type of applicable periodic rate (e.g., balance transfer or cash advance) accompanied by a reference to the consumer's periodic statement. However, consumer testing conducted for the Board showed that while participants looked at actual numbers on the front of the page of checks, they generally did not notice or pay attention to a cross reference to the periodic statement.

Thus, the Board proposes that the actual APRs and fees applicable to the checks must be disclosed pursuant to § 226.9(b)(3). The Board understands, however, that creditors may engage in risk-based pricing with regard to checks used by consumers , and seeks with this proposal to strike an appropriate balance between meaningful disclosure for consumers and the operational burden on creditors. The proposed rule would require that creditors customize each set of checks sent to reflect a particular consumer's rate. The Board seeks comment on the operational burden associated with customizing the checks, and on alternatives, such as whether providing a reference to the type of rate that will apply, accompanied by a toll-free telephone number that a consumer could call to receive additional information, would provide sufficient benefit to consumers while limiting burden on creditors.

The Board also seeks comment as to whether there are other credit devices or additional features that creditors add to consumers' accounts to which this proposed rule should apply.

The Board has proposed several technical revisions to improve the clarity of § 226.9(b) and the associated commentary.

**9(c) Change in Terms**

Under § 226.9(c) of Regulation Z, certain changes to the terms of an open-end plan require specific notice of the change. (TILA does not address changes in terms to open-end plans.) The general rule is that creditors must provide 15 days' advance notice of changes in terms required to be included in the account-opening disclosures, with some exceptions, or to increase the minimum payment. See current § 226.9(c)(1).

Advance notice currently is not required in all cases. For example, if an interest rate or other finance charge increases due to a consumer's default or delinquency, notice is required, but need not be given in advance. See current § 226.9(c)(1); comment 9(c)(1)-3. Furthermore, no change-in-terms notice is required if the specific change is set forth initially by the creditor in the account-opening disclosures. See current comment 9(c)-1. For example, some credit card account agreements permit the card issuer to increase the periodic rate if the consumer makes a late payment. Because the circumstances of the increase are specified in advance in the account agreement, the creditor currently need not provide a change-in-terms notice; under current § 226.7(d) the new rate will appear on the periodic statement for the cycle in which the increase occurs.

In the December 2004 ANPR, the Board sought comment as to whether mailing a notice 15 days prior to the effective date of a change in an interest rate provided timely notice to consumers. Q26. The Board also asked whether existing disclosure rules for increases to interest rates and other finance charges were adequate to enable consumers to make timely decisions about how to manage their accounts. Q27. Some commenters noted that consumers are surprised by changes to the terms of their accounts and are not aware that such changes are possible before they take effect, because they do not receive advance notice of those changes and do not remember the information regarding those changes that was contained in the account-opening disclosures. Consumer advocates expressed concern that consumers are not aware when they have triggered rate increases, for example by paying late, and thus are unaware that it might be in their best interest to shop for alternative financing before the rate increase takes effect. Some consumer commenters requested that the Board ban certain practices, such as "universal default clauses," which permit a creditor to raise a consumer's interest rate to the penalty rate if the consumer, for example, makes a late payment on any account, not just on accounts with that creditor.

The Board proposes three revisions to the regulation and commentary to improve consumers' awareness about changes in their account terms or increased rates due to delinquency or default or as a penalty. These revisions also are intended to enhance consumers' ability to shop for alternative financing before such account terms become effective. The proposed revisions generally apply when a creditor is changing terms that must be disclosed in the account-opening summary table under § 226.6(b)(4). See section-by-section analysis to § 226.6(b)(4). First, the Board proposes to expand the circumstances under which consumers receive advance notice of changed terms, or increased rates due to delinquency, or for default or as a penalty. Second, the Board proposes to give consumers earlier notice of a change in terms, or for increased rates due to delinquency or default or as a penalty. Third, the Board proposes to introduce format requirements to make the disclosures about changes in terms or for increased rates due to delinquency, default or as a penalty more effective. HELOCs would not be affected by these proposed revisions. The provisions dealing with notices about increased rates due to delinquency, or default or as a penalty are discussed in the section-by-section analysis to § 226.9(g).

Changes in late-payment fees and over-the-credit limit fees. Creditors currently do not have to provide notice of changes to late-payment fees and over-the-credit-limit charges, pursuant to current § 226.9(c)(2). For open-end (not home-secured) plans, the Board's proposal would require 45 days advance notice for changes involving late-payment charges or over-the-credit-limit charges, other than a reduction in the amount of the charges. See proposed § 226.9(c)(2)(i). The Board believes that it would be beneficial for consumers to have advance notice of changes to these charges, which can be substantial depending on how a consumer uses his or her account. Late-payment charges and over-the-credit-limit charges can have a large aggregate effect, particularly since they need not be one-time charges, and can be charged month after month if a consumer repeatedly makes late payments or exceeds his or her credit limit. Advance notice regarding changes in the amount of these charges may assist consumers to make better decisions regarding their account usage and regarding when and in what amount they should make payments in order to avoid these potentially recurring charges. This amendment would require that 45 days' advance notice be given only when the amount of a late-payment fee or over-the-credit-limit fee changes, not when such a fee is applied to a consumer's account.

Timing. As discussed above, § 226.9(c)(1) currently provides that whenever any term required to be disclosed under § 226.6 is changed or the required minimum payment is increased, a written notice must be mailed or delivered to the consumer at least 15 days before that change becomes effective. Commenters responding to the December 2004 ANPR expressed a number of opinions about this requirement. One consumer group and a number of individual consumers stated that 15 days is not enough time for a consumer to seek alternative financing, and recommended that consumers be given more time. Some creditors stated that 15 days' advance notice was adequate. Other industry commenters stated that they did not oppose increasing the notice period from 15 days to 30 days, and added that many consumers already receive notice approximately one month before a change in terms becomes effective, because the notices often are sent with periodic statements. A few consumer group commenters recommended 90 days' advance notice for all changes to terms.

In light of the comments received and upon further consideration of this issue, for open-end (not home-secured) plans, the Board proposes to add § 226.9(c)(2)(i) to extend the notice period from 15 days to 45 days. For changes that require advance notice, the Board believes that consumers should have sufficient time, following the notice and before the change becomes effective, to change the usage of their plan or to pursue alternative means of financing their purchases, such as using another credit card, utilizing a home-equity line or installment loan, or shopping for a new credit card.

The Board considered requiring that advance notice of changes in terms be sent 30 days in advance, but concluded that 30 days could be inadequate in some circumstances. The rule governs when notices must be sent, not received by the consumer, so in practice the notice will be received by the consumer with less days remaining to act than the full advance notice period specified in the rule. In light of delays in mail delivery, for example, a notice sent to a consumer 30 days in advance may give a consumer only 25 days to seek alternative financing before the change in terms takes effect. For example, if a consumer wants to shop for another credit card, apply for, open, and transfer a balance from an existing card to a new card, 30 days may be too short a time in some cases. The Board's proposal that notice be sent 45 days in advance should ensure, in most cases, that a consumer will have at least one calendar month following receipt of the notice and before the change in terms takes effect, to seek alternative financing or otherwise mitigate the effect of the new terms.

The proposed 45 day notice period would not apply when the changes affect charges that are not required to be disclosed under § 226.6(b)(4). See proposed § 226.9(c)(2)(ii). Specifically, if a creditor increases any component of a charge, or introduces a new charge, that is imposed as part of the plan under § 226.6(b)(1) but is not required to be disclosed as part of the account-opening summary table under § 226.6(b)(4), the creditor may either, at its option (1) provide at least 45 days written advance notice before the change becomes effective, or (2) provide notice orally or in writing of the amount of the charge to an affected consumer at a relevant time before the consumer agrees to or becomes obligated to pay the charge. For example, a fee for expedited delivery of a credit card is a charge imposed as part of the plan under § 226.6(b)(1) but is not required to be disclosed in the account-opening summary table under § 226.6(b)(4). If a creditor changes the amount of that expedited delivery fee, the creditor may provide written advance notice of the change to affected consumers at least 45 days before the change becomes effective. Alternatively, the creditor may provide notice orally or in writing of the amount of the charge to an affected consumer at a relevant time before the consumer agrees to or becomes obligated to pay the charge. See comment 9(c)(2)(ii)-1. Creditors meet the standard to provide the notice at a relevant time if the oral or written notice of a charge is given when a consumer would likely notice it, such as when deciding whether to purchase the service that would trigger the charge. For example, if a consumer telephones a card issuer to discuss a particular service, a creditor would meet the standard if the creditor clearly and conspicuously discloses the fee associated with the service that is the topic of the telephone call. See comment 9(c)(2)(ii)-2. The Board believes that for these charges, consumers do not need advance notice of the current amount of the charge.

As discussed in the section-by-section analysis to § 226.5(a)(1)(ii), creditors are permitted under the E-Sign Act to provide in electronic form any TILA disclosure 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.

15 U.S.C. 7001 et seq. The Board requests comment on whether there are circumstances in which creditors should be permitted to provide cost disclosures in electronic form to consumers who have not affirmatively consented to receive electronic disclosures for the account, such as when a consumer seeks to make a payment online, and the creditor imposes a fee for the service.

Format. Section 226.9 currently contains no restrictions or requirements with regard to how change-in-terms notices are presented or formatted. The consumer testing conducted for the Board explored the usability of current change-in-terms notices. The results of this consumer testing suggest that typical change-in-terms notices are not formatted in a manner that is noticeable and easy for consumers to understand. Consumer testing also suggests that improvements can be made to these notices. A typical change-in-terms notice contains dense blocks of contractual language in a small font, and may be on an accordion-style pamphlet included with the consumer's periodic statement. Consumer testing indicated that consumers may not look at these pamphlets when they are included with periodic statements, and that some consumers have trouble navigating these notices even when their attention is explicitly drawn to the disclosures. These pamphlets generally are not designed to draw attention to the changes because they provide a disclosure of contractual provisions.

For open-end (not home-secured) plans, the Board proposes that creditors be required to provide a summary table of a limited specified number of key terms on the front of the first page of the change-in-terms notice, or segregated on a separate sheet of paper. See proposed § 226.9(c)(2)(iii), Sample G-20 in Appendix G. Creditors would be required to utilize the same headings as in the account-opening tables in Model Form G-17(A) and Samples G-17(B) and G-17(C) in Appendix G. If the change-in-terms notice were included with a periodic statement, a summary table would be required to appear on the front of the periodic statement, preceding the list of transactions for the period. See §§ 226.7(b)(14), 226.9(c)(2)(iii).

The Board believes that requiring a tabular summary of the key terms of the consumer's account would make change-in-terms notices more useful to consumers by highlighting those terms that may be of most interest to them. Based on consumer testing conducted for the Board, when a summary of key terms was included on change-in-terms notices tested, consumers tended to read the notice and appeared to understand better what key terms were being changed than when a summary was not included.

The proposal also would require that creditors provide other information in the change-in-terms notice, specifically (1) a statement that changes are being made to the account; (2) a statement indicating the consumer has the right to opt out of these changes, if applicable, and a reference to additional information describing the opt out right provided in the notice, if applicable; (3) the date the changes to terms described in the summary table will become effective; (4) if applicable, an indication that the consumer may find additional information about the summarized changes, and other changes to the account, in the notice; and (5) if the creditor is changing a rate on the account, other than a penalty rate, a statement that if a penalty rate applies to the consumer's account, the new rate described in the notice does not apply to the consumer's account until the consumer's account balances are no longer subject to the penalty rate. This information must be placed directly above the summary of key changes described above. This information is intended to give context to the summary of key changes.

With respect to the reference to a right to opt out of the changes, the Board is not requiring that creditors provide such an opt out right. State law or other applicable laws may provide consumers with a right to opt out of certain changes. If a consumer has the right to opt out of the changes in the notice, a creditor must include a statement indicating the consumer has the right to opt out of these changes, if applicable, and a reference to additional information describing the opt out right provided in the notice, if applicable.

Reduction in credit limit. Under Regulation Z, a creditor generally may decrease a consumer's credit limit without providing any notice, except with regard to HELOCs. As a result, there could be situations where a consumer may exceed his or her credit limit without realizing it, potentially triggering late-payment fees and penalty pricing. Under new § 226.9(c)(2)(v), for open-end (not home-secured) plans, if a creditor decreases the credit limit on an account, advance notice of the decrease must be provided before an over-the-limit fee or a penalty rate can be imposed solely as a result of the consumer exceeding the newly decreased credit limit. Under the proposal, notice must be provided in writing or orally at least 45 days prior to imposing the over-the-limit fee or penalty rate and shall state that the credit limit on the account has been or will be decreased. The Board and other federal banking agencies in the past have received a number of complaints from consumers who were not notified when their credit limits were decreased, and were surprised at the subsequent imposition of an over-the-credit-limit fee. The Board is not proposing that creditors may not reduce a consumer's credit limit. The Board recognizes that creditors have a legitimate interest in mitigating the risk of loss when a consumer's creditworthiness deteriorates, and that a consumer's creditworthiness can deteriorate quickly. Therefore, the Board's proposal would simply require that a creditor provide a notice that it has reduced or will be reducing a consumer's credit limit 45 days before imposing any fee or penalty rate for exceeding that new limit. This proposed amendment would apply only when the over-the-credit-limit fee is imposed solely as a result of a reduction in the credit limit; if the over-the-credit-limit fee would have been charged notwithstanding the reduction in a credit limit, no advance notice would be required. This provision is not intended to permit creditors to provide a general notice at account opening that a consumer's credit limit may change from time to time; rather, the notice should be sent with regard to a specific credit limit reduction that has occurred or will be occurring.

Rules affecting home-equity plans. The Board proposes at the present time to retain in proposed § 226.9(c)(1), without intended substantive change, the current rules regarding the circumstances, timing, and content of change-in-terms notices for HELOCs. These rules will be reviewed in the Board's upcoming review of the provisions of Regulation Z addressing closed-end and open-end (home-secured) credit.

The Board is aware that the current change-in-terms rules, which have applicability both to HELOCs and open-end (not home-secured) credit, address several types of changes in terms that are impermissible for HELOCs subject to § 226.5b. Section 226.5b imposes substantive restrictions on which terms of HELOCs may be changed, and in retaining the current change-in-terms rules for HELOCs, the Board does not intend to amend or in any way change the substantive restrictions imposed by § 226.5b. Accordingly, the Board proposes to make several deletions in proposed § 226.9(c)(1) and the related commentary with respect to HELOCs. For example, the Board proposes deleting in new comment 9(c)(1)-1 the requirement that notice "be given if the contract allows the creditor to increase the rate at its discretion but does not include specific terms for an increase," because such a contractual term would be prohibited under § 226.5b.

The Board welcomes comment on whether there are any remaining references in § 226.9(c)(1) and the related commentary to changes in terms that would be impermissible for open-end (home-secured) credit pursuant to § 226.5b.

**9(e) Disclosures upon Renewal of Credit or Charge Card**

TILA Section 127(d), which is implemented in § 226.9(e), requires card issuers that assess an annual or other periodic fee, including a fee based on activity or inactivity, on a credit card account of the type subject to § 226.5a to provide a renewal notice before the fee is imposed. 15 U.S.C. 1637(d). The creditor must provide disclosures required for credit card applications (although not in a tabular format) and must inform the consumer that the renewal fee can be avoided by terminating the account by a certain date. The notice must generally be provided at least 30 days or one billing cycle, whichever is less, before the renewal fee is assessed to the account. However, there is an alternative delayed notice procedure where the fee can be assessed; the fee must be reversed if the consumer terminates the account provided the consumer is given notice.

Creditors are given considerable flexibility in the placement of the disclosures required under § 226.9(e). For example, the notice can be preprinted on the periodic statement, such as on the back of the statement. See § 226.9(e)(3) and comment 9(e)(3)-2. However, creditors that place any of the disclosures on the back of the periodic statement must include a reference to those disclosures under § 226.9(e)(3). To aid in compliance, a model clause that may, but is not required to, be used is proposed for creditors that use the delayed notice method. See proposed comment 9(e)(3)-1.

Comment 9(e)-4, which addresses accuracy standards for disclosing rates on variable rate plans, would be revised, for the same reasons and consistent with the proposed accuracy standard for account-opening disclosures. See section-by-section analysis to § 226.6(b)(2)(ii)(G).

Other proposed changes to § 226.9(e) are minor with no intended substantive change. For example, footnote 20a, dealing with format, is deleted as unnecessary. The proposed reorganization of § 226.5a is intended, in part, to separate more clearly content and format requirements in that section. Nonetheless, to avoid any possible confusion, comment 9(e)-2, which generally repeats footnote 20a, would be retained.

**9(g) Increase in Rates Due to Delinquency or Default or Penalty Pricing**

As discussed above with respect to § 226.9(c), in the December 2004 ANPR, the Board asked whether existing disclosure rules for increases to interest rates and other finance charges were adequate to enable consumers to make timely decisions about how to manage their accounts. Q27. Consumer advocates expressed concern that consumers are not aware when they have triggered rate increases, for example by paying late, and thus are unaware that it might be in their interest to shop for alternative financing before the rate increase takes effect. Some consumer commenters requested that the Board ban certain practices, such as "universal default clauses," which permit a creditor to raise a consumer's interest rate to the penalty rate if the consumer defaults on any accounts, not just on accounts with that creditor.

The Board is not proposing at the present time to prohibit universal default clauses or similar practices. Instead, as discussed in the section-by-section analysis to § 226.5a, the Board's proposal seeks to improve the effectiveness of the disclosures given to consumers regarding the conditions in which penalty pricing will apply. In addition, the Board seeks to improve the ability of consumers to use the disclosures given to them by proposing that disclosures be provided prior to the application of penalty pricing to their accounts. To this end, with respect to open-end (not home-secured) plans, the Board's proposed rule would add § 226.9(g)(1) to require creditors to provide 45 days advance notice when a rate is increased due to a consumer's delinquency or default, or if a rate is increased as a penalty for one or more events specified in the account agreement, such as a late payment or an extension of credit that exceeds the credit limit. This notice would be required even if, as is currently the case, the creditor specifies the penalty rate and the specific events that may trigger the penalty rate in the account-opening disclosures.

Neither Regulation Z nor TILA defines what a "default" is, and the Board is aware that credit agreements of some creditors permit penalty pricing based on a single late payment by the consumer to that creditor. The Board is concerned that the imposition of penalty pricing can come as a costly surprise to consumers who are not aware of, or do not understand, what behavior is considered a "default" under their agreement. As discussed in the section-by-section analysis to § 226.5a, consumer testing conducted for the Board indicated that some consumers do not understand what factors can give rise to penalty pricing, such as the fact that one late payment may constitute a "default." Moreover, when penalty pricing is imposed, it may apply to all of the balances on a consumer's account and often applies to balances for several months or longer. Penalty rates can be more than twice as much as the consumer's normal rate on purchases; for example, default rates in excess of 30 percent are not uncommon.

The Board believes that the way to address penalty pricing is through improved disclosures regarding the conditions under which penalty pricing may be imposed. In part, the Board is proposing, in connection with the disclosures given with credit card applications and solicitations and at account opening, to enhance disclosures about penalty pricing and revise terminology to address consumer confusion regarding the meaning of "default." However, in light of the relatively low contractual threshold for rate increases based on consumer delinquency, default or as a penalty, the Board believes that consumers also would benefit from advance notice of these rate increases, which they otherwise may not expect. Advance notice would give consumers an opportunity to shop for alternate sources of credit, pay down account balances before the rate increase takes effect, or contact the card issuer to rectify any errors before penalty rates are imposed. To make this opportunity viable, the Board is proposing that the notice be provided at least 45 days before the increase takes effect. The Board requests comment on whether a shorter time period, such as 30 days' advance notice, would be adequate notice for consumers whose interest rates are being increased due to default or delinquency, or as a penalty.

The proposed rule would impose a de facto limitation on the implementation of contractual terms between a consumer and creditor, in that creditors would no longer be permitted to provide for the immediate application of penalty pricing upon the occurrence of certain events specified in the contract. The Board believes that this delay in implementing contract terms is appropriate in light of the potential benefit to consumers. Many consumers are likely unaware of the events that will trigger such pricing. The account-opening disclosures may be provided to the consumer too far in advance for the consumer to recall the circumstances that may cause his or her rates to increase. In addition, the consumer may not have retained a copy of the account-opening disclosures and may not be able to effectively link the information disclosed at account opening to the current repricing of his or her account.

The Board notes that this advance notice provision does not, in any manner, limit the contractual ability of creditors to establish the events that trigger penalty pricing, or to establish the rates that apply for such events. The Board also notes that use of this sort of de facto delay in implementing contract terms has precedent in Regulation Z. For example, since 1988, § 226.20(c) has provided that 25 days' advance notice must be given for certain increases in the payment for an adjustable rate mortgage, even if the circumstances of the increase are specified in advance in the contract.

Under the proposed rule, creditors would retain the ability to mitigate risk by freezing credit accounts or lowering the credit limit without providing advance notice (subject to proposed § 226.9(c)(2)(v) discussed above, which addresses over-the-credit-limit fees or penalty rates). Thus, creditors would be able to effectively mitigate risk on accounts that are delinquent or in default notwithstanding the fact that they would be required to provide a notice 45 days before increasing the rate.

The rule also would not require that 45 days' advance notice be given for certain changes made in accordance with the contract, provided that such adjustment is not due to delinquency, default or as a penalty. For example, if an employee offers an open-end plan with discounted rates to its employees, the employer would not be required to give a former employee 45 days' advance notice before increasing the rate on that individual's account from the preferential employees' rate to the standard rate, provided that the rate increase was set forth in the account agreement.

Disclosure content and format. With respect to open-end (not home-secured) plans, under the Board proposal, if a creditor is increasing the rate due to delinquency or default or as a penalty, the creditor must provide a notice with the following information: (1) a statement that the delinquency or default rate or penalty rate has been triggered, as applicable; (2) the date as of which the delinquency or default rate or penalty rate will be applied to the account, as applicable; (3) the circumstances under which the delinquency or default rate or penalty rate, as applicable, will cease to apply to the consumer's account, or that the delinquency or default rate or penalty rate will remain in effect for a potentially indefinite time period; and (4) a statement indicating to which balances on the account the delinquency or default rate or penalty rate will be applied, as applicable. See proposed § 226.9(g)(3)(i). In consumer testing conducted for the Board, some participants did not appear to understand that penalty rates can apply to all of their balances, including existing balances. Some participants also did not appear to understand how long a penalty rate could be in effect. Without information about the balances to which the penalty rate applies and how long it applies, consumers might have difficultly determining whether they should shop for another card or pursue alternate sources of financing. Consumers also may consider the duration of penalty pricing when shopping for alternative sources of credit which would enhance their ability to make prudent decisions.

If the notice regarding increases in rates due to delinquency, default or penalty pricing were included on or with a periodic statement, this notice must be in a tabular format. Under the proposal, the notice also would be required to appear on the front of the periodic statement, preceding the list of transactions for the period. See proposed §§ 226.7(b)(14), 226.9(g)(3)(ii)(A). If the notice is not included on or with a periodic statement, the information described above must be disclosed on the front of the first page of the notice. See § 226.9(g)(3)(ii)(B).

## Section 226.10 Prompt Crediting of Payments

Section 226.10, which implements TILA Section 164, generally requires a creditor to credit to a consumer's account a payment that conforms to the creditor's instructions (also known as a conforming payment) as of the date of receipt, except when a delay in crediting the account will not result in a finance or other charge. 15 U.S.C. 1666c; § 226.10(a). Section 226.10 also requires a creditor that accepts a non-conforming payment to credit the payment within five days of receipt. See § 226.10(b). The Board has interpreted § 226.10 to permit creditors to specify cut-off times indicating the time when a payment is due, provided that the requirements for making payments are reasonable, to allow most consumers to make conforming payments without difficulty. See comments 10(b)-1 and -2. Pursuant to § 226.10(b) and comment 10(b)-1, if a creditor imposes a cut-off time, it must be disclosed on the periodic statement; many creditors put the cut-off time on the back of statements.

The December 2004 ANPR solicited comment regarding the cut-off times used currently by most issuers for receiving payments, whether cut-off times differ based on the type of payment (e.g., check, EFT, telephone, or Internet), and whether the operating times of third party processors differ from those of creditors. Q47 – Q48, Q50. The December 2004 ANPR also requested comment regarding the adequacy and clarity of current disclosures of payment due dates and cut-off times, and asked whether the Board should issue a rule requiring creditors to credit payments as of the date they are received, regardless of the time. Q49, Q51.

Disclosure of cut-off times. In response to the December 2004 ANPR, the Board received a number of comments describing issuers' current practices regarding cut-off times. The majority of industry commenters noted that they do set cut-off times that are in the early or mid-afternoon, but that cut-off times may differ based on the means by which a consumer makes his or her payment, with telephone and Internet payments often having later cut-off times than payments made by mail. These industry commenters argued that current disclosure of these cut-off times is clear. Consumer groups and consumers commented that the majority of banks now set a cut-off time on payment due dates and that these cut-off times are a problem because they could result in a due date that is one day earlier in practice than the date disclosed. Consumer groups expressed particular concern about cut-off times because they believe that issuers simultaneously may be decreasing the time period between the end of the statement period and the time when the payment is due.

Almost all industry comments opposed the Board's suggestion to require creditors to credit payments as of the date they are received, regardless of the time, noting that issuers need flexibility to work with external vendors and that creditors' internal processes and systems will to some extent dictate the timing of payment crediting. Consumer and consumer group comments proposed a rule that would require banks to consider the postmark to be the day the payment is received.

The Board is not proposing to require a minimum cut-off time. Instead, as discussed above, the Board is proposing, in what would be new § 226.7(b)(11), to require that for open-end (not home-secured) plans, creditors must disclose the earliest of their cut-off times for payments near the due date on the front page of the periodic statement, if that earliest cut-off time is before 5 p.m. on the due date. The Board believes that the disclosure-based approach may benefit consumers without imposing an unreasonable operational burden on creditors. Consumers would be able to make better decisions about when to make payments in order to avoid late-payment fees and default rates if earlier cut-off times such as 12:00 p.m. were more prominently disclosed on the periodic statement. In recognition of the fact that creditors may have different cut-off times depending on the type of payment (e.g., mail, Internet, or telephone), the Board's proposal would require that creditors disclose only the earliest cut-off time, if earlier than 5 p.m. on the due date. See proposed § 226.7(b)(11). HELOCs would not be affected by the disclosure rule in § 226.7(b)(11).

Receipt of electronic payments made through a creditor's web site. The Board also proposes to add an example to comment 10(a)-2 that states that for payments made through a creditor's web site, the date of receipt is the date as of which the consumer authorizes the creditor to debit that consumer's account electronically. Industry comments to the December 2004 ANPR stated that most credit card payments are still received by mail. Nevertheless, the Internet is an increasingly utilized resource for making credit card payments and for receiving information about accounts. Unlike payments delivered by mail, payments made via a creditor's web site may be received almost immediately by that creditor.

The proposed comment would refer to the date on which the consumer authorizes the creditor to effect the electronic payment, not the date on which the consumer gives the instruction. The consumer may give an advance instruction to make a payment and some days may elapse before the payment is actually made; accordingly, comment 10(a)-2 would refer to the date on which the creditor is authorized to debit the consumer's account. If the consumer authorized an immediate payment, but provided the instruction after a creditor's cut-off time, the relevant date would be the following business day. For example, a consumer may go online on a Sunday evening and instruct that a payment be made; however, the creditor could not transmit the request for the debit to the consumer's account until the next day, Monday. Under proposed comment 10(a)-2 the date on which the creditor was authorized to effect the electronic payment would be deemed to be Monday, not Sunday. Proposed comment 10(b)-1.i.B would clarify that the creditor may, as with other means of payment, specify a cut-off time for an electronic payment to be received on the due date in order to be credited on that date. The Board solicits comment regarding the incidence of, and types of, any delays that may prevent creditors or their third party processors from receiving electronic payments on the date on which the creditor is authorized to effect the payment.

The Board considered expanding this comment to cover electronic payments received by other means (e.g., if the consumer authorizes a payment to his deposit account-holding bank's web site), because it is likely that such electronic payments made through such parties also may be received by the creditor on the same day that they are authorized. However, it could be difficult for a creditor to monitor when a consumer gives a third party an instruction to send a payment, and, in addition, the creditor has no direct control over how long it takes the third party to process that instruction. As a result, the Board's proposed clarification of comment 10(a)-2 is limited to electronic payments effected through the creditor's own web site, over which the creditor has control.

Promotion of payment via the creditor's web site. The Board also proposes to update the commentary to clarify that if a creditor discloses that payments can be made on that creditor's web site, then payments made through the creditor's web site will be considered conforming payments for purposes of § 226.10(b). Many creditors now permit consumers to make payments via their web site. Payment on the creditor's web site may not be specified on or with the periodic statement as conforming payments, but it may be promoted in other ways, such as in the account-opening agreement, via e-mail, in promotional material, or on the web site itself. It would be reasonable for a consumer who receives materials from the creditor promoting payment on the creditor's web site to believe that it would be a conforming payment and credited on the date of receipt. Therefore, the Board proposes to amend comment 10(b)-2 to clarify that if a creditor promotes that it accepts payments via its web site (such as disclosing on the web site itself or on the periodic statement that payments can be made via the web site), then it is considered a conforming payment for purposes of § 226.10(b).

Third party processors. With regard to third party processors, industry commenters noted that current practice is that payments received by a third party processor are treated as if they were received directly by the creditor, and that no further clarification is necessary. Accordingly, the Board is not currently proposing any amendments to specifically address third party processors.

**Section 226.11 Treatment of Credit Balances; Account Termination**

**11(a) Credit Balances**

TILA Section 165, implemented in § 226.11, sets forth specific steps that a creditor must take to return any credit balance in excess of $1 on a credit account, including making a good faith effort to refund any credit balance remaining in the consumer's account for more than six months. 15 U.S.C. 1666d. The substance of § 226.11 would remain unchanged; however, the commentary would be revised to provide that a creditor may comply with this section by refunding any credit balance upon receipt of a consumer's oral or electronic request. See proposed comment 11(a)-1. In addition, the Board proposes to move the current rules in § 226.11 to a new paragraph (a), with the commentary renumbered accordingly, and to add a new paragraph (b) which implements the account termination prohibition for certain open-end accounts in Section 1306 of the Bankruptcy Act (further discussed below). See TILA Section 127(h); 15 U.S.C. 1637(h). The section title would be amended to reflect the new subject matter.

**11(b) Account Termination**

TILA Section 127(h), added by the Bankruptcy Act, prohibits an open-end creditor from terminating open-end accounts for certain reasons. Creditors cannot terminate an open-end plan before its expiration date solely because the consumer has not incurred finance charges on the account. The prohibition does not prevent a creditor from terminating an account for inactivity in three or more consecutive months. The October 2005 ANPR solicited comment on the need for additional guidance, such as when an account "expires" and when an account is "inactive." Q106 – Q108.

The Board proposes to implement TILA Section 127(h) in new § 226.11(b). The general rule is stated in § 226.11(b)(1) and mirrors the statute; the prohibition would apply to all open-end plans.

Commenters expressed differing views on how the Board might interpret "expiration date." Some suggested using the expiration date on credit cards as the date the account is deemed to expire. Others noted that while cards may expire from time to time, the underlying open-end plans commonly do not have maturity or expiration dates. These commenters were concerned that if an account were deemed to "expire" when a credit card's expiration date occurs, new account-opening disclosures would be required for the account to continue. The Board believes that Congress did not intend such a result. Therefore, comment 11(b)(1)-1 would clarify that the underlying credit agreement, not the credit card, determines if there is a stated expiration (maturity) date. Creditors offering accounts without a stated expiration date could not terminate those accounts solely because the consumer does not incur finance charges on the account.

Under the proposal, a new § 226.11(b)(2) would be added to provide that the new rule in § 226.11(b)(1) does not prevent creditors from terminating an account under an open-end plan (with or without an expiration date) that is inactive for three consecutive months. Commenters were split on the need for guidance on an "inactive" account. Of those that suggested guidance, commenters generally concurred that "activity" includes purchases or cash advances, for example. But commenters disagreed whether an account with an outstanding balance was "active." Because finance charges are likely to accrue on balances remaining after the end of a grace period if any, the Board believes the Congress was addressing situations where no finance charges were accruing due to inactivity. Therefore, proposed § 226.11(b)(2) would provide that an account is inactive if there has been no extension of credit (such as by purchase, cash advance, or balance transfer) and the account has no outstanding balance.

**Section 226.12 Special Credit Card Provisions**

Section 226.12 contains special rules applicable to credit cards and credit card accounts, including conditions under which a credit card may be issued, liability of cardholders for unauthorized use, and cardholder rights to assert merchant claims and defenses against the card issuer. The proposal would, among other things, provide additional guidance on the rules on unauthorized use and the rights of cardholders to assert claims or defenses involving a merchant against the card issuer (consumer claims with merchants) and update the section to address Internet transactions.

**12(a) Issuance of Credit Card**

TILA Section 132, which is implemented by § 226.12(a) of Regulation Z, generally prohibits creditors from issuing credit cards except in response to a request or application. Section 132 explicitly exempts from this prohibition credit cards issued as renewals of or substitutes for previously accepted credit cards. 15 U.S.C. 1642. Existing comment 12(a)(2)-5, the "one-for-one rule," interprets these statutory and regulatory provisions by providing that, in general, a creditor may not issue more than one credit card as a renewal of or substitute for an accepted credit card. The proposal would leave § 226.12(a) and the accompanying commentary generally unchanged, except that the text of footnote 21 defining the term "accepted credit card" would be moved to new comment 12(a)-2.

In 2003, Board staff revised the commentary to § 226.12(a) to allow card issuers to replace an accepted credit card with more than one card, subject to certain conditions, including the limitation that the consumer's total liability for unauthorized use with respect to the account could not increase with the issuance of the additional renewal or substitute card(s). See comment 12(a)(2)-6; 68 FR 16,185; April 3, 2003. Card issuers could thus, for example, issue credit cards using a new format or technology to existing accountholders, even though the new card is intended to supplement rather than replace the traditional card. In the December 2004 ANPR, the Board solicited comment as to whether it should consider revising § 226.12(a) to allow the unsolicited issuance of additional cards on an existing account outside of renewal or substitution under certain conditions, including that the additional cards be sent unactivated. Q46.

Consumer groups stated that additional credit cards should only be sent if the consumer specifically requests such cards, citing identity theft concerns if issuers were permitted to send out credit cards without any advance warning or notice. One consumer group suggested that the Board require that consumers be notified in writing or by phone before additional cards are sent. Industry commenters strongly encouraged the Board to amend the regulation to permit the unsolicited issuance of additional cards on existing accounts even when a previously accepted card is not being replaced. These industry commenters observed that the current constraints on distributing new types of credit cards potentially impeded industry innovation in providing more convenient methods for consumers to access their accounts. Industry commenters also contested the notion that sending additional cards on an unsolicited basis would increase the risk of identity theft because, in their view, providing an additional card presents no greater risk than sending the first card, which the consumer has requested, or a renewal card, which consumers often would not know when to expect. Industry commenters also noted that allowing the unsolicited issuance of credit cards outside the context of a renewal or substitution would not expose consumers to greater liability for unauthorized transactions given the contemplated condition that liability for unauthorized use on the card account may not increase with the issuance of the additional card.

At this time, the Board does not propose to amend § 226.12(a) and the one-for-one rule to allow the unsolicited issuance of credit cards outside the context of a renewal or substitution of an accepted access device. Based on current card issuer practices, the Board understands that some issuers may be unable to require separate activation procedures for access devices on the same credit card account. As a result, additional cards sent on an unsolicited basis outside the context of a renewal or substitution might be sent in activated form, which could cause considerable harm to consumers. Even if the card issuer were not permitted to impose any additional liability on the consumer for unauthorized use, consumers would nevertheless still suffer the inconvenience of refuting unwarranted claims of liability.

**12(b) Liability of Cardholder for Unauthorized Use**

TILA Section 133(a) limits a cardholder's liability for an unauthorized use of a credit card to no more than $50 for transactions that occur prior to notification of the card issuer that an unauthorized use has occurred or may occur as the result of loss, theft or otherwise. 15 U.S.C. 1643. Before a card issuer may impose liability for an unauthorized use of a credit card, it must satisfy certain conditions: (1) the card must be an accepted credit card; (2) the issuer must have provided adequate notice of the cardholder's maximum liability and of the means by which the issuer may be notified in the event of loss or theft of the card; and (3) the issuer must have provided a means to identify the cardholder on the account or the authorized user of the card. The statutory provisions on unauthorized use are implemented in § 226.12(b) of the regulation. The Board is proposing a number of revisions that would clarify the scope of the provision and update the regulation to reflect current business practices. The proposed revisions also would provide guidance on the relationship between the unauthorized use provision and the billing error provisions in § 226.13.

Scope. The definition of "unauthorized use" currently found in footnote 22 would be moved into the regulation in new § 226.12(b)(1)(i). The definition provides that unauthorized use is use of a credit card by a person who lacks "actual, implied, or apparent authority" to use the credit card. Comment 12(b)(1)-1 further clarifies that whether such authority exists must be determined under state or other law. Commenters were asked in the December 2004 ANPR about whether there was a need to revise any of the substantive protections for open-end credit accounts. Q43. Some commenters urged the Board to consider adopting a provision similar to the existing staff commentary under Regulation E (Electronic Fund Transfer Act) to address circumstances where a consumer has furnished an access device to a person who has exceeded the authority given. The proposal would add a new comment 12(b)(1)-3 to clarify that if a cardholder furnishes a credit card to another person and that person exceeds the authority given, the cardholder is liable for that credit transaction unless the cardholder has notified (in writing, orally, or otherwise) the creditor that use of the credit card by that person is no longer authorized. See also comment 205.2(m)-2 of the Official Staff Commentary to Regulation E, 12 CFR part 205. New comment 12(b)(1)-4 would provide, however, that an unauthorized use would include circumstances where a person has obtained a credit card, or otherwise has initiated a credit card transaction through robbery or fraud (e.g., if the person holds the consumer at gunpoint). See also comment 205.2(m)-3 of the Official Staff Commentary to Regulation E, § 205.5. In both cases, the Board believes it is appropriate for the same standard to apply to credit cards that applies to debit cards under Regulation E. Thus, the Board is proposing to adopt the two standards under Regulation Z for consistency.

The Board does not anticipate that the proposed comments would significantly expand the circumstances under which liability could be imposed on a cardholder for a particular transaction, in light of the existing reference in the definition of "unauthorized use" to "implied or apparent authority." Nevertheless, the addition of this comment could help provide greater clarity for issuers when investigating unauthorized use claims. Comment is requested, however, as to whether this clarification is necessary in light of the existing definition of "unauthorized use." Current § 226.12(b)(1) would be re-designated as § 226.12(b)(1)(ii).

Section 226.12(b)'s liability provisions apply only to unauthorized uses of a cardholder's credit card. Thus, the liability limits established in § 226.12(b) do not apply to unauthorized transactions involving the use of a check that accesses a credit card account. (See prior discussion of "credit card" under § 226.2(a)(15).) The consumer would nevertheless be able to assert the billing error protections in § 226.13 which are independent of the protections under § 226.12(b). New comment 12(b)-4 would contain this clarification.

Some commenters on the December 2004 ANPR urged the Board to adopt a time period within which consumers must make claims for unauthorized transactions made through the use of a credit card. These commenters asserted that over time, evidence becomes more difficult to obtain, making a creditor's investigation more difficult and that a consumer's early detection and notification would prevent additional fraud on the account. In contrast to TILA Section 161 which requires consumers to assert a billing error claim within 60 days after a periodic statement reflecting the error has been sent, TILA Section 133 does not prescribe a time frame for asserting an unauthorized use claim. 15 U.S.C. 1643. The Board believes that had Congress intended that a consumer's rights to assert an unauthorized use claim to be time-limited, it would have established a time frame for asserting the claim. Accordingly, the proposal does not contain the suggested change.

Conditions for imposing liability. Section 226.12(b)(2) requires the card issuer to satisfy three conditions before the issuer may impose any liability for an unauthorized use of a credit card. First, the credit card must be an accepted credit card. See footnote 21; proposed comment 12-2. Second, the card issuer must have provided "adequate notice" to the cardholder of his or her maximum potential liability and the means by which to notify the issuer of the loss or theft of the card. Third, the card issuer also must have provided a means to identify the cardholder on the account or the authorized user of the card. See § 226.12(b)(2).

Under the proposal, the guidance regarding what constitutes adequate notice currently in footnote 23 would be moved to the staff commentary. See new comment 12(b)(2)(ii)-2. In addition, the examples in comment 12(b)(2)(iii)-1 describing means of identifying a cardholder or user would be updated to contemplate additional biometric means of identification other than a fingerprint on a card.

Comment 12(b)(2)(iii)-3 currently states that a cardholder may not be held liable under § 226.12(b) when the card itself or some other sufficient means of identification of the cardholder is not presented. In these circumstances, the card issuer has not satisfied one of the conditions precedent necessary to impose liability; that is, it has not provided a means to identify the cardholder of the account or the user of the card. For example, no liability may be imposed on the cardholder if a person without authority to do so orders merchandise by telephone, using a credit card number or another number that appears only on the card. The example would be updated to also apply to Internet transactions.

In many instances, a credit card will bear a separate 3- or 4-digit number, which is typically printed on the back of the card on the signature block or in some cases on the front of the card above the card number. Although the provision of the 3- or 4- digit number may suggest that the person providing the number is in possession of the card, it does not meet the requirement to provide a means to identify the cardholder or the authorized user of the card, as required by the regulation. Thus, comment 12(b)(2)(iii)-3 would clarify that a card issuer may not impose liability on the cardholder when merchandise is ordered by telephone or Internet if the person using the card without the cardholder's authority provides the credit card number by itself or with other information that appears on the card because it has not met the requirement that a means to identify the cardholder or authorized user of the card in the transaction.

The Board is also proposing revisions to Model Clause G-2, which can be used to explain the consumer's liability for unauthorized use, to improve its readability. For HELOCs subject to § 226.5b, at the creditor's option, the creditor may use Model Clause G-2 or G-2(A). For open-end (not home-secured) plans, the creditor may use G-2(A).

**12(c) Right of Cardholder to Assert Claims or Defenses Against Card Issuer**

Under TILA Section 170, as implemented in § 226.12(c) of the regulation, a cardholder may assert against the card issuer a claim or defense for defective goods or services purchased with a credit card. The claim or defense applies only as to unpaid balances for the goods or services, and if the merchant honoring the card fails to resolve the dispute. See 15 U.S.C. 1666i. The cardholder may withhold payment up to the unpaid balance of the purchase that gave rise to the dispute and any finance or other charges imposed on that amount. The right is limited to disputes exceeding $50 for purchases made in the consumer's home state or within 100 miles. See § 226.12(c).[18] The proposal would update the regulation to address current business practices and move guidance currently in the footnotes to the rule or the staff commentary as appropriate.

In order to assert a claim under § 226.12(c), a cardholder must have used a credit card to purchase the goods or services associated with the dispute. Comment 12(c)(1)-1 lists examples of circumstances that are excluded or included by § 226.12(c). The proposal would add Internet transactions charged to the credit card account to the list of circumstances included within the scope of § 226.12(c) (provided that certain conditions are met, including that the disputed transaction take place in the same state as the cardholder's current designated address, or within 100 miles from that address).

In technical revisions, guidance stating § 226.12(c)'s inapplicability to the transactions listed in footnote 24 has been moved to comment 12(c)-3 with corresponding changes in comment 12(c)(1)-1. The reference to "paper-based debit cards" in existing comment 12(c)(1)-1 would be deleted as obsolete. The Board is aware of at least one product, however, whereby a consumer can pay cash and is instantly issued an account number (along with a 3-digit card identification number and expiration date) that allows the consumer to conduct transactions with an online merchant. No physical card device is issued to the consumer. Comment is requested whether the reference to paper-based debit cards should be retained or expanded to include these "virtual" cards. Comment is also requested as to whether the references to "check-guarantee cards" under comments

[18] Certain merchandise disputes, such as the nondelivery of goods, may also be separately asserted as a "billing error" under § 226.13(a)(3). See comment 12(c)-1.

12(c)-3 (see existing footnote 24) and 12(c)(1)-1 should continue to be retained as guidance in the commentary or whether they should also be deleted as obsolete.

Section 226.12 also requires that the disputed transaction must have occurred in the same state as the cardholder's current designated address or, if different, within 100 miles from that address. See § 226.12(c)(3). Thus, if applicable state law provides that a mail, telephone, or Internet transaction occurs at the cardholder's address, such transactions would be covered under § 226.12(c), even if the merchant is located more than 100 miles from the cardholder's address. The conditions for asserting merchant claims would be re-designated under § 226.12(c)(3)(i)(A) and (B) in the proposal. In addition, the Board proposes to move the guidance currently found in footnote 26 regarding the applicability of some of the limitations in § 226.12(c) to § 226.12(c)(3)(ii). Corresponding revisions to reflect the proposed changes would also be made to the staff commentary, with additional clarifying changes.

Guidance regarding how to calculate the amount of the claim or defense that may be asserted by the cardholder under § 226.12(c), currently found in footnote 25, would be moved to the commentary in proposed comment 12(c)-4.

**12(d) Offsets by Card Issuer Prohibited**

TILA Section 169 prohibits card issuers from taking any action to offset a cardholder's credit card indebtedness against funds of the cardholder held on deposit with the card issuer. 15 U.S.C. 1666h. The statutory provision is implemented by § 226.12(d) of the regulation. Section 226.12(d)(2) currently provides that card issuers are permitted to "obtain or enforce a consensual security interest in the funds" held on deposit. Comment 12(d)(2)-1 provides guidance on the security interest provision. For example, the security interest must be affirmatively agreed to by the consumer, and must be disclosed as part of the account-opening disclosures under § 226.6. In addition, the comment provides that the security interest must not be "the functional equivalent of a right of offset." The comment states that the consumer "must be aware that granting a security interest is a condition for the credit card account (or for more favorable account terms) and must specifically intend to grant a security interest in a deposit account." The comment gives some examples of how this requirement can be met, such as use of separate signature or initials to authorize the security interest, placement of the security agreement on a separate page, or reference to a specific amount or account number for the deposit account. The comment also states that the security interest must be "obtainable and enforceable by creditors generally. If other creditors could not obtain a security interest in the consumer's deposit accounts to the same extent as the card issuer, the security interest is prohibited by § 226.12(d)(2)."

From time to time, questions have been raised about comment 12(d)(2)-1. For example, some card issuers have asked whether using only one of the methods to ensure the consumer's awareness and intent is sufficient, versus using more than one. Card issuers have also asked about the requirement that the security interest be obtainable and enforceable by creditors generally. The Board requests comment on whether additional guidance is needed and, if so, the specific issues that the guidance should address.

**12(e) through 12(g)**

Sections § 226.12(e), (f), and (g) address, respectively: the prompt notification of returns and crediting of refunds; discounts and tie-in arrangements; and guidance on the applicable regulation (Regulation Z or Regulation E) in instances involving both credit and electronic fund transfer aspects. The Board does not propose any changes to these provisions.

**Section 226.13 Billing Error Resolution**

TILA Section 161, as implemented in § 226.13 of the regulation, addresses error resolution procedures for billing errors, and requires a consumer to provide written notice of the error within 60 days after the first periodic statement reflecting the alleged error is sent. 15 U.S.C. 1666. The written notice triggers a creditor's duty to investigate the claim within prescribed time limits. In contrast to the consumer protections in § 226.12 of the regulation, which are limited to transactions involving the use of a credit card, the billing error procedures apply to any extensions of credit that are made in connection with an open-end account. Commenters on the December 2004 ANPR provided few comments addressing the billing error provisions, except to urge the Board to increase the time period for investigating errors. Q43.

The proposed revisions would clarify, among other things, that (1) the billing error provisions apply to purchases made using a third-party payment intermediary, where the purchase is funded through an extension of credit using the consumer's credit card or other open-end plan; (2) a creditor must complete its investigation within the time frames established under the regulation and may not reverse any credits made once the time frames have expired; and (3) a creditor may not deduct any portion of a disputed amount or related charges when a cardholder uses an automatic payment service offered directly by or through the creditor.

In technical revisions, the substance of footnotes 27-30 would be moved to the regulation or the commentary, as appropriate, and footnote 31 would be deleted. (See redesignation table below.) For the reasons set forth in the section-by-section analysis to § 226.6(b)(1), the Board would update references to "free-ride period" as "grace period" in the regulation and commentary, without any intended substantive change.

**13(a) Definition of Billing Error**

The definition of a billing error in § 226.13(a) would be substantively unchanged in the proposal. Under § 226.13(a)(3), the term "billing error" includes disputes about property or services that are not accepted by the consumer or not delivered to the consumer as agreed. See § 226.13(a)(3). The proposal would add a new comment 13(a)(3)-2 to clarify that § 226.13(a)(3) also applies when a consumer uses his or her credit card or other open-end account to purchase a good or service through a third-party payment intermediary, such as a person-to-person Internet payment service.

In some cases, a consumer might pay for merchandise purchased through an Internet auction site using an Internet payment service, which is in turn funded through an extension of credit from the consumer's credit card or other open-end account. As in the case of purchases made using a check that accesses a consumer's credit card account, there may not be a direct relationship between the merchant selling the merchandise and the card issuer when an Internet payment service is used. Because a consumer has billing error rights with respect to purchases made with checks that access a credit card account, the Board believes the same result should apply when the consumer makes a purchase using a third-party intermediary funded using the same credit card account. In particular, the Board believes that there is little difference between a consumer using his or her credit card to make a payment directly to the merchant on the merchant's Internet web site or to make a payment to the merchant through a third-party intermediary. Accordingly, comment 13(a)(3)-2 would clarify that when an extension of credit from the consumer's credit card or other open-end account is used to fund a purchase through a third-party payment intermediary, the good or service purchased is not the payment medium, but rather the good or service that is obtained using the payment service.

Proposed new comment 13(a)(3)-3 would clarify that prior notice to the merchant is not required before the consumer can assert a billing error that the good or service was not accepted or delivered as agreed. Thus, in contrast to claims or defenses asserted under TILA Section 170 and § 226.12(c) of the regulation which require that the cardholder first make a good faith attempt to obtain satisfactory resolution of a disagreement or problem with the person honoring the credit card, the consumer need not provide prior notice of the dispute to the person from whom the consumer purchased the good or service of the dispute before asserting a billing error claim directly with the creditor. 15 U.S.C. 1666i.

The text of footnote 27 prohibiting a creditor from accelerating a consumer's debt or restricting or closing the account because the consumer has exercised billing error rights, and alerting creditors to the statutory forfeiture penalty under TILA Section 161(e) (15 U.S.C. 1666) for failing to comply with any of the requirements in § 226.13 would be moved to the list of error resolution rules under § 226.13(d)(3). Current comment 13-1 referring to this general prohibition would be deleted as redundant.

**13(b) Billing-Error Notice**

To assert a billing error under § 226.13(b), a consumer must provide a written notice of the error to the creditor no later than 60 days after the creditor transmitted the first periodic statement that reflects the alleged error. The notice must provide sufficient information to enable the creditor to investigate the claim, including the consumer's name and account number, the type, date and amount of the error, and, to the extent possible, the consumer's reasons for his or her belief that a billing error exists.

Comment 13(b)-1 would be revised to incorporate the guidance currently in footnote 28 stating that the creditor need not comply with the requirements of § 226.13(c) through (g) if the consumer voluntarily withdraws the billing error notice. Comment 13(b)-2 would be added to incorporate the guidance currently in footnote 29 stating that the creditor may require that the written billing error notice not be made on the payment coupon or other material accompanying the periodic statement if the creditor so states in the billing rights statement on the account-opening disclosure and annual billing rights statement. In addition, comment 13(b)-2 would provide that billing error notices submitted electronically would be deemed to satisfy the requirement that billing error notices be provided in writing, provided that the creditor has stated in the billing rights statement required by §§ 226.6(c)(2) and 226.9(a) that it will accept notices submitted electronically, including how the consumer can submit billing error notices in this manner.

**13(c) Time for Resolution; General Procedures**

Section 226.13(c) generally requires a creditor to mail or deliver written acknowledgment to the consumer within 30 days of receiving a billing-error notice, and to complete the billing error investigation procedures within two billing cycles (but no later than 90 days) after receiving a billing-error notice. Comment 13(c)(2)-2 would be added to clarify that a creditor must complete its investigation and conclusively determine whether an error occurred within the error resolution time frames. Thus, once the error resolution time frame has expired, the creditor may not reverse any corrections it has made related to the asserted billing error, including any previously credited amounts, even if the creditor subsequently obtains evidence indicating that the billing error did not occur as asserted. The statute is clear that a creditor must complete its investigation and make appropriate corrections to the consumer's account within two complete billing cycles after the receipt of the consumer's notice of error, and does not permit the creditor to continue its investigation beyond the error resolution period. 15 U.S.C. 1666. This rule is intended to ensure finality in the error resolution process, and to ensure creditors complete their investigations in a timely manner. Of course, a creditor may reverse a prior determination, based on an investigation, that no error occurred and subsequently credit the consumer's account for the amount of the error even after the error resolution period has elapsed.

Some commenters on the December 2004 ANPR urged the Board to increase the time period for investigating errors from 90 days to 120 days to allow issuers to investigate billing error claims effectively. Q43. The 90-day time frame is statutory, and the Board does not propose to extend the maximum error resolution period. The Board further notes that the 90-day maximum time frame would apply only in cases where a creditor's billing cycle is 45 days or more. Otherwise, the creditor must complete its investigation within the time period represented by two billing cycles. Thus, for example, if a creditor's billing cycle is 30 days, it would only have 60 days to conclude its investigation of alleged billing errors.

Of course, any determination that an error has not occurred must be based upon a reasonable investigation. See § 226.13(f).

**13(d) Rules Pending Resolution**

Once a billing error is asserted by a consumer, the creditor is prohibited under § 226.13(d) from taking certain actions with respect to the dispute in order to ensure that the consumer is not otherwise discouraged from exercising his or her billing error rights. For example, the creditor may not take action to collect any disputed amounts, including related finance or other charges, or make or threaten to make an adverse report, including reporting that the amount or account is delinquent, to any person about the consumer's credit standing arising from the consumer's failure to pay the disputed amount or related finance or other charges.

Under the current rule, the card issuer is specifically prohibited from deducting any part of the disputed amount or related charges from a cardholder's deposit account that is also held by the card issuer. To reflect new payment practices, the proposal would extend the prohibition to automatic deductions from the consumer's deposit account where the consumer has enrolled in the card issuer's automatic payment plan. The Board believes that whenever an automatic payment service is offered by the card issuer, thereby giving the card issuer control over the amount to be debited, a cardholder should not treated any differently solely because the consumer's deposit account is maintained at a different account-holding institution. Thus, for example, if the cardholder has agreed to pay a predetermined amount each month and subsequently disputes one or more transactions that appear on a statement, the card issuer must ensure that it does not debit the consumer's asset account for any part of the amount in dispute. The proposed revision would apply whether the card issuer operates the automatic payment service itself or outsources the service to a third-party service provider, but would not apply where the consumer has enrolled in a third-party bill payment service that is not offered by the card issuer. Thus, for example, the proposed revision would not apply where the consumer uses a bill-payment service offered by his or her deposit account-holding institution to pay his debt (unless the account-holding institution is also the card issuer). Section 226.13(d)(1) and comment 13(d)(1)-4, which describes the coverage of the automatic payment plan exclusion, would be revised to reflect the proposed change. Comment is requested regarding any operational issues card issuers may encounter in implementing the systems changes necessary to comply with the proposed revision.

**13(e) Procedures if Error Occurred As Asserted and 13(f) Procedures if Different Billing Error or No Billing Error Occurred**

Paragraphs (e) and (f) of § 226.13 set forth procedures that a creditor must follow to resolve a billing error claim, depending on whether the billing error occurred as asserted, or if a different billing error or no billing error occurred. In particular, § 226.13(f) requires that a creditor first conduct a reasonable investigation before the creditor may deny the consumer's claim or conclude that the billing error occurred differently than as asserted by the consumer. See TILA Section 161(a)(3)(B)(ii); 15 U.S.C. 1666(a)(3)(B)(ii). These provisions in the regulation would be substantively unchanged in the proposal. The text of footnote 31 is deleted as unnecessary in light of the general obligation under § 226.13(f) to conduct a reasonable investigation before a creditor may deny a billing error claim.

**13(g) Creditor's Rights and Duties After Resolution**

Section 226.13(g) specifies the creditor's rights and duties once it has determined, after a reasonable investigation under § 226.13(f), that a consumer owes all or a portion of the disputed amount and related finance or other charges. The proposal would provide guidance to clarify the length of the time the consumer would have to repay the amount determined still to be owed without incurring additional finance charges (i.e., the grace period) that would apply under these circumstances.

Before a creditor may collect any amounts owed related to a disputed charge that is determined to be proper, the creditor must promptly notify the consumer in writing when the payment is due and the portion of the disputed amount and related finance or other charges that is still owed (including any charges that may be retroactively imposed on the amount found not to be in error). See 15 U.S.C. 1666(a); § 226.13(g)(1). The consumer must then be given any grace period disclosed under proposed §§ 226.6(a)(1), 226.6(b)(1), 226.7((a)(8), or 226.7(b)(8), as applicable, to pay the amount due as specified in the written notice without incurring any additional finance or other charges. See § 226.13(g)(2). Comment 13(g)(2)-1 would be revised to clarify that if the consumer was entitled to a grace period at the time the consumer asserted the alleged billing error, then the consumer must be given a period of time equivalent to the disclosed grace period to pay the disputed amount as well as related finance or other charges. The Board believes that this interpretation is necessary to ensure that consumers are not discouraged from asserting their statutory billing rights by putting the consumer in the same position (that is, with the same grace period) if the consumer had not disputed the transaction in the first place.

**13(i) Relation to Electronic Fund Transfer Act and Regulation E**

Section 226.13(i) is designed to facilitate compliance when financial institutions extend credit incident to electronic fund transfers that are subject to the Board's Regulation E, for example, when the credit card account is used to advance funds to prevent a consumer's deposit account from becoming overdrawn or to maintain a specified minimum balance in the consumer's account. See 12 CFR part 205. The provision states that under these circumstances, the creditor should comply with the error resolution procedures of Regulation E, rather than those in Regulation Z (except that the creditor must still comply with §§ 226.13(d) and (g)). The Board is not proposing any changes to this provision as it appears in the regulation; however, a minor clarification is proposed for an existing comment.

Comment 13(i)-2 states that incidental credit that is not extended under an agreement between the consumer and the financial institution is governed solely by the error resolution procedures in Regulation E. The example in the current comment would be revised to include a specific reference to overdraft protection services that are not subject to the Board's Regulation Z when there is no agreement between the creditor and the consumer to extend credit when the consumer's account is overdrawn. See § 226.4(c)(3); 70 FR 29,582; May 24, 2005.

Comment is requested as to whether the Board should expand the guidance provided under § 226.13(i) to apply more generally to other circumstances when an extension of credit is incident to an electronic fund transfer, rather than limited to transactions pursuant to an agreement between a consumer and a financial institution to extend credit when the consumer's account is overdrawn or to maintain a specified balance. For example, in situations where a consumer transfers funds from an open-end credit plan, such as a home-equity line of credit, to the consumer's checking or savings account, the wrong amount may be transferred from the credit plan to the deposit account. Both Regulation E and Z could potentially apply under this circumstance leaving a potential issue as to which set of error resolution provisions the creditor/ financial institution should follow. In particular, if Regulation E is deemed to apply, the institution would have a shorter period of time in which to complete its investigation.

**Section 226.14 Determination of Annual Percentage Rate**

As discussed in the section-by-section analysis to § 226.7(b)(7), Regulation Z requires disclosure on periodic statements of both the effective APR and the corresponding APR. The regulation also requires disclosure of the corresponding APR in account-opening disclosures, change-in-terms notices, advertisements, and other documents. The computation methods for both the corresponding APR and the effective APR are implemented in § 226.14 of Regulation Z. Section 226.14 also provides tolerances for accuracy in APR disclosures.

As also discussed in the section-by-section analysis to § 226.7(b)(7), the Board is proposing for comment two alternative approaches regarding the computation and disclosure of the effective APR. Under the first alternative, the Board proposes to retain the requirement that the effective APR be disclosed on the periodic statement, with modifications to the rules for computing and disclosing the effective APR to reflect an approach tested with consumers. See proposed § 226.7(b)(7) and § 226.14(d). For HELOCs subject to § 226.5b, the Board proposes to allow a creditor to comply with the current rules applicable to the effective APR; creditors would not be required to make changes in their periodic statement systems for such plans at this time. See proposed §§ 226.7(a)(7), 226.14(c). If the creditor chooses, however, the creditor may disclose an effective APR for its HELOCs according to any revised rules adopted for the effective APR.

The second alternative would be to eliminate the requirement to provide the effective APR on the periodic statement. Under the second alternative, for a HELOC subject to § 226.5b, a creditor would have the option of providing the effective APR according to current rules. The two proposed alternatives are reflected in two proposed alternative versions of § 226.14.

Under either alternative, the current provisions in § 226.14(a) and (b) dealing with tolerances for the APR and guidance on calculating the APR for certain disclosures other than the periodic statement would not be substantively revised, but minor changes would be made. Section 226.14(b) identifies the regulatory sections where a corresponding APR (the periodic rate multiplied by the number of periods in a year) must be disclosed. A reference to proposed §§ 226.7(a)(4) and 226.7(b)(4) (currently § 226.7(d)), which requires creditors to disclose corresponding APRs on periodic statements, would be added to § 226.14(b). (A reference to § 226.7(d) would be deleted from § 226.14(c) as obsolete.) With respect to technical revisions, under both alternatives, the § 226.14 regulatory and commentary text would be revised where necessary to reflect changes in terminology and to eliminate footnotes, moving their substance into the text of the regulation.

First alternative proposal. Under the first alternative, the proposed new rules for calculating the effective APR are contained in §§ 226.14(d) and 14(e), and accompanying commentary. As discussed above under § 226.7(b)(7), for multifeatured plans, the Board proposes to require that the creditor must compute and disclose an effective APR separately for each feature. For example, purchases and cash advances would be separate features; there might be two separate cash advance features, if there was a promotional APR on certain cash advances and a different APR on others. Proposed § 226.14(d) and accompanying commentary provide rules on how the effective APR should be computed for each feature. (Current § 226.14(d) would be redesignated as § 226.14(c)(5).

In proposed § 226.14(e), the Board proposes to limit the finance charges that are included in calculating the effective APR. These charges would be: (1) charges attributable to a periodic rate used to calculate interest; (2) charges that relate to a specific transaction; (3) charges related to required credit insurance or debt cancellation or suspension coverage; (4) minimum charges imposed if, and only if, a charge would otherwise have been determined by applying a periodic rate to a balance except for the fact that such charge is smaller than the minimum (such as a $1.00 minimum finance charge); and (5) charges based on the account balances, account activity or inactivity, or the amount of credit available. This exclusive list is intended to limit disclosure of an effective APR to situations in which it is more likely to be understood by consumers and be useful to consumers, as well as provide creditors with certainty as to the fees that must be included in the computation of the effective APR.

For finance charges that relate to a specific transaction, such as cash advance and balance transfers, expressing the interest and transactions fees in the effective APR may help consumers better understand the costs of these transactions. For finance charges that relate to required credit insurance or debt cancellation or suspension coverage (coverage for which the regulation's conditions for excluding the charge from the finance charge have not been satisfied), consumers may benefit from seeing an effective APR that combines two costs that will be imposed every month if a consumer carries a balance – interest on the balance and the required fee for insurance or debt cancellation or suspension coverage. For finance charges that are minimum charges in lieu of interest described above, a consumer that typically carries a small balance may benefit from seeing an effective APR that includes this minimum charge, so that the consumer understands that he or she is paying a higher rate for carrying that small balance than the corresponding APR suggests. For finance charges based on the account balances, account activity or inactivity, or the amount of credit available, consumers may benefit from seeing an effective APR that includes these charges, because these charges could be imposed as often as every month as a substitute for interest or in addition to interest. For example, the Board is aware of at least one credit card product where there is no interest rate applicable to the card, but each month a fixed charge is charged based on the outstanding balance on the card (for example, $6 charge per $1,000 balance). For such a price structure, which has a corresponding APR of zero, consumers may find the effective APR helpful.

Also, in proposed § 226.14(e), the Board would make clear that a finance charge related to opening the account, and a finance charge imposed not more often than annually as a condition to continuing or renewing the account, is not included in calculating the effective APR. Because these fees would be imposed infrequently (either at account opening or annually, or less frequently, to continue or renew the account), including these finance charges in the effective APR may not be helpful to consumers.

With respect to open-end (not home-secured) plans, the Board would also revise the current rule that exempts a creditor from disclosing an effective APR when the total finance charge does not exceed 50 cents for a monthly or longer billing cycle, or the pro rata share of 50 cents for a shorter cycle. See 15 U.S.C. 127(b)(6); current § 226.14(c)(4). The Board would exercise its exceptions authority to adjust the 50-cent threshold to $1.00 to reflect adjusted prices since the rule was implemented. Section 226.14(d)(4) would also be revised to limit the finance charges included in determining whether the threshold is exceeded to those specified in proposed § 226.14(e). See proposed § 226.14(d)(4).

Also under the first alternative, the Board proposes to place in § 226.14(c) the rules for calculating the effective APR for periodic statements for HELOCs subject to § 226.5b. As proposed, § 226.14(c) provides that, for HELOCs subject to § 226.5b, a creditor may comply either with (1) the current rules applicable to the effective APR, (which are contained in proposed § 226.14(c)), or (2) with the revised rules applicable to open-end (not home-secured) plans (which are contained in proposed § 226.14(d)).

Second alternative proposal. Under the second alternative, for the reasons discussed in the section-by-section analysis to § 226.7(b)(7), the Board proposes to eliminate the requirement to provide the effective APR on the periodic statement. Under this alternative, however, for a HELOC subject to § 226.5b, a creditor would have the option of disclosing an effective APR according to the current rules in Regulation Z for computing and disclosing the effective APR. No guidance would be given for disclosing the effective APR on open-end (not home-secured) plans, since the requirement to provide the effective APR on such plans would be eliminated.

## Section 226.16 Advertising

TILA Section 143, implemented by the Board in § 226.16, governs advertisements of open-end credit plans. 15 U.S.C. 1663. The statute applies to the advertisement itself, and therefore, the statutory and regulatory requirements apply to any person advertising an open-end credit plan, whether or not such person meets the definition of creditor. See comment 2(a)(2)-2. Under the statute, if an advertisement sets forth any of the specific terms of the plan, then the advertisement must also state: (1) any minimum or fixed amount which could be imposed; (2) the periodic rates expressed as

APRs, if periodic rates may be used to compute the finance charge; and (3) any other term the Board requires by regulation. The specific terms of an open-end plan that "trigger" additional disclosures, which are commonly known as "triggering terms," are finance charges and other charges required to be disclosed under current §§ 226.6(a) and 226.6(b). If an advertisement states a triggering term, the regulation requires that the advertisement also state (1) any minimum, fixed, transaction, activity or similar charge that could be imposed; (2) any periodic rate that may be applied expressed as an APR; and (3) any membership or participation fee that could be imposed. See current § 226.16(b) and comment 16(b)-7 (as redesignated to proposed comment 16(b)-1.)

The Board is proposing several changes to the advertising rules in § 226.16 in order to ensure meaningful disclosure of advertised credit terms, alleviate compliance burden for certain advertisements, and implement provisions of the Bankruptcy Act. Specifically, under § 226.16(b), the Board is proposing to make the triggering terms consistent for all open-end credit advertisements by including terms stated negatively (for example, no interest), as is currently required under TILA for advertisements of HELOCs. Presently, for advertisements for open-end (not home-secured) plans, only positive terms trigger the additional disclosure.

If an advertisement states a minimum month payment to finance a purchase under a plan established by a creditor or retailer, the proposal would amend § 226.16(b) to require a disclosure of the total number of payments and time period to repay. In addition, the Board is proposing in new § 226.16(g) to provide guidelines concerning use of the word "fixed" in connection with an APR. To ease compliance burden on advertisers, the Board is proposing in new § 226.16(f), alternative disclosures for television and radio advertisements in recognition of the time and space constraints on such media. Finally, the Board is implementing Section 1303 of the Bankruptcy Act, in part, in new § 226.16(e) and Section 1309 of the Bankruptcy Act in the commentary on clear and conspicuous in new comment 16-2. The Board's proposed revisions to § 226.16 and the accompanying commentary are described in more detail below.

Clear and conspicuous standard. Comment 16-1 provides that disclosures made under § 226.16 are subject to the clear and conspicuous standard required for all disclosures for open-end credit plans. See § 226.5(a)(1). To be clear and conspicuous, disclosures must be in a reasonably understandable form. See comment 5(a)(1)-1. Generally, there are no specific rules regarding the format of disclosures in advertisements. See comment 16-1.

Section 1309 of the Bankruptcy Act requires the Board to implement the "clear and conspicuous" term as it applies to certain disclosures required by Section 1303(a) of the Bankruptcy Act. Section 1303(a) applies to direct-mail applications and solicitations for credit cards and accompanying promotional materials. The Bankruptcy Act requires, in part, that when an introductory rate is stated, the time period in which the introductory period will end and the rate that will apply after the end of the introductory period must be stated "in a clear and conspicuous manner" in a prominent location closely proximate to the first listing of the introductory rate. The statute requires these disclosures to be "reasonably understandable and designed to call attention to the nature and significance of the information in the notice."

The Board solicited comment in the October 2005 ANPR on interpreting the standard for clear and conspicuous set forth in Section 1309 of the Bankruptcy Act. Q85. Most industry commenters stated that additional guidance on clear and conspicuous was unnecessary. Consumer group commenters suggested that the Board impose minimum font size requirements, while industry commenters universally opposed such requirements.

After considering comments, the Board is proposing in comment 16-2 that creditors clearly and conspicuously disclose when the introductory period will end and the rate that will apply after the end of the introductory period if the information is equally prominent to the first listing of the introductory rate to which it relates. Guidance on what is considered the first listing of the introductory rate is given in proposed comment 16(e)-4, as discussed below. The Board is also proposing that if these disclosures are the same type size as the first listing of the introductory rate, they will be deemed to be equally prominent. See proposed comment 16-2. Requiring equal prominence for this information calls attention to the nature and significance of such information by ensuring that the information is at least as significant as the introductory rate to which it relates. Furthermore, an equally prominent standard for similar information currently applies to advertisements for HELOCs. See current § 226.16(d)(2).

**16(b) Advertisement of Terms that Require Additional Disclosures**

Negative terms as triggering terms. If an advertisement states certain terms, additional information must be disclosed. See § 226.16(b). The goal of this triggering term approach is to provide consumers with a more complete picture of costs that may apply to the plan when certain specified charges for the plan are given. TILA Section 143 provides that stating any specific term of the plan triggers additional disclosures. 15 U.S.C. 1663. The Board, however, limited triggering terms for advertisements of open-end (not home-secured) plans to those terms that are stated as a positive number. For home-equity advertisements, under TILA Section 147(a) (15 U.S.C. 1665b(a)), triggering terms include both positive as well as negative terms. See also current § 226.16(d)(1) and comments 16(b)-2 and 16(d)-1. Pursuant to TILA Section 143(3), the Board proposes to apply this approach to advertisements for all open-end plans. The Board believes that negative terms such as "no interest" and "no annual fee" alone may not provide consumers with a sufficiently accurate portrayal of possible costs associated with the plan if the additional disclosures are not provided. This approach would also ensure similar treatment for all open-end plans. Current comment 16(b)-2 would be amended accordingly and moved to a revised comment 16(b)-1, which includes guidance on triggering terms in general. See redesignation table below.

Advertisement of minimum monthly payment. The Board has the authority under TILA Section 143(3) to require the disclosure in advertisements for open-end credit of any terms in addition to those explicitly required by the statute. 15 U.S.C. 1663(3). The Board proposes to require additional disclosures for advertisements that provide a minimum monthly payment for an open-end credit plan that would be established to finance the purchase of goods or services. If a minimum monthly payment is advertised, the advertisement would be required to state, in equal prominence to the minimum payment, the time period required to pay the balance and the total dollar amount of payments if only minimum payments are made. Proposed § 226.16(b)(2) would clarify that this disclosure should assume that the consumer makes only the minimum payment required during each payment period.

The Board believes that advertisements that state a minimum monthly payment will provide a clearer picture of credit costs if such advertisements also state the total dollar amount of payments the consumer would make, and the amount of time needed to pay the balance if only the minimum payments are made. The Board has received comments from time to time from state attorneys general regarding creditors that sell large-ticket items and simultaneously arrange financing for the purchase of those items. See discussion regarding the definition of open-end credit in the section-by-section analysis to § 226.2(a)(20). The comments the Board has received indicate that some consumers agree to the financing on the basis of a certain advertised minimum payment but are later surprised to learn how long the debt will take to pay, and how much the credit will cost them over that time period. The Board believes that disclosure of the time period and total dollar amount of payments will help to improve consumer understanding about the cost of credit products for which a minimum monthly payment is advertised.

Other changes to 226.16(b). Currently, terms that are required to be disclosed under § 226.6 trigger the disclosure of additional terms. See § 226.16(b). Under current comment 16(b)-1, this would include terms required to be disclosed under §§ 226.6(a) and 226.6(b). As discussed in the section-by-section analysis to § 226.6, the Board is proposing new cost disclosure rules for open-end (not home-secured) plans, but is preserving existing cost disclosure rules for HELOCs pending a review of all home-secured rules. Section 226.16(b) would be conformed to reflect these revisions.

In technical revisions, § 226.16(b) has been renumbered: triggering term requirements would be set forth in a revised § 226.16(b)(1); and the new proposed minimum monthly payment disclosures would be set forth in a revised § 226.16(b)(2). Footnote 36d (stating that disclosures given in accordance with § 226.5a do not constitute advertising terms) would be deleted as unnecessary since "advertisements" do not include notices required under federal law, including disclosures required under § 226.5a. See comment 2(a)(2)-1(ii). The Board is proposing to move the guidance in current comments 16(b)-1 and 16(b)-8 to new § 226.16(b)(1), with some revisions. Proposed comment 16(b)-1 would provide guidance on triggering terms by consolidating current comment 16(b)-2, amended as discussed above, with current comment 16(b)-7. Current comment 16(b)-6 would be eliminated as duplicative of the requirements under proposed § 226.16(e), as discussed below.

**16(c) Catalogs or Other Multiple-Page Advertisements; Electronic Advertisements**

Amendments to § 226.16(c) and comments 16(c)(1)-1, 16(c)(1)-2, and 16(c)(3)-1 reflect provisions contained in the 2007 Electronic Disclosure Proposal. See 72 FR 21,1141; April 30, 2007. The amendments provide that for an advertisement that is accessed by the consumer in electronic form, the disclosures required under § 226.16 must be provided to the consumer in electronic form on or with the advertisement.

**16(d) Additional Requirements for Home-equity Plans**

No revisions are proposed for the advertising rules under § 226.16(d), consistent with the Board's plan to review rules affecting HELOCs in a separate rulemaking.

High loan-to-value disclosures. Section 1302 of the Bankruptcy Act amends TILA Section 127(a)(13) to require that credit applications for, and advertisements related to, an extension of credit secured by a dwelling that may exceed the fair market value of the dwelling include a statement that the interest on the portion of the credit extension that is greater than the fair market value of the dwelling is not tax deductible for Federal income tax purposes. 15 U.S.C. 1637(a)(13). For these applications and advertisements, the statute also requires inclusion of a statement that the consumer should consult a tax adviser for further information on the deductibility of the interest. The new disclosures would apply to advertisements for home-secured credit, whether open-end or closed-end; thus, the Board plans to address issues related to this requirement during its review of the rules relating to home-secured credit.

**16(e) Introductory Rates**

TILA Section 127(c)(6), as added by Section 1303(a) of the Bankruptcy Act, requires that if a credit card issuer states an introductory rate in applications, solicitations, and all accompanying promotional materials, the issuer must use the term "introductory" clearly and conspicuously in immediate proximity to each mention of the introductory rate. 15 U.S.C. 1637(c)(6). Credit card issuers also must disclose, in a prominent location closely proximate to the first mention of the introductory rate, other than the listing of the rate in the table required for credit card applications and solicitations, the time period when the introductory rate expires and the rate that will apply after the introductory rate expires.

TILA Section 127(c)(7), as added by Section 1304(a) of the Bankruptcy Act, applies these requirements to "any solicitation to open a credit card account for any person under an open end consumer credit plan using the Internet or other interactive computer service." 15 U.S.C. 1637(c)(7). The Board proposes to implement these requirements for promotional materials accompanying such applications or solicitations in a new § 226.16(e). In addition, the Board proposes to apply these requirements more broadly, pursuant to the Board's authority under TILA Section 105(a), to issue regulations with classification, differentiations or other provisions as in the judgment of the Board are necessary to effectuate the purposes of TILA, as discussed below. 15 U.S.C. 1604(a). Sections 1303 and 1304 of the Bankruptcy Act would be implemented in § 226.5a, and are discussed in the section-by-section analysis to § 226.5a.

**16(e)(1) Scope**

The Bankruptcy Act amendments regarding "introductory" rates, the time period these rates may be in effect, and the post-introductory rate apply to direct-mail applications and solicitations, and accompanying promotional materials.

15 U.S.C. 1637(c)(1)(A). To provide meaningful disclosure of credit terms in order to avoid the uninformed use of credit, the Board is proposing to extend these requirements to applications or solicitations to open a credit card account, and all accompanying promotional materials, that are available publicly ("take-ones"). 15 U.S.C. 1601(a); 15 U.S.C. 1604(a); 15 U.S.C. 1637(c)(3)(A). Consumers who obtain publicly available applications and solicitations are in essentially the same position in terms of the shopping process as consumers who receive direct mail applications and solicitations or applications or solicitations offered through the Internet. Therefore, the Board believes the information provided about introductory rates in these materials should be the same.

Moreover, as discussed in the section-by-section analysis to § 226.5a(a)(2), the Board is proposing to apply the Bankruptcy Act provisions relating to Internet offers to both electronic solicitations <u>and</u> applications, although the statute refers only to solicitations, in order to promote the informed use of credit. Therefore, proposed § 226.16(e)(1) would state that the introductory rate requirements in § 226.16(e) apply to all promotional materials accompanying credit card applications and solicitations offered through direct mail and electronically as well as those available publicly.

Furthermore, the Board proposes to extend some of the requirements in Section 1303 of the Bankruptcy Act regarding the presentation of introductory rates to other written advertisements for open-end credit plans that may not accompany an application or solicitation, other than advertisements of HELOCs subject to § 226.5b, in order to promote the informed use of credit. Advertisements for open-end credit plans are already required to comply with similar, though not identical, requirements to those set forth in Section 1303 of the Bankruptcy Act for "discounted variable-rate plans." <u>See</u> current comment 16(b)-6. Specifically, "discounted variable-rate plans" are required to provide both the initial rate (with the statement of how long it will remain in effect) and the current indexed rate (with the statement that this second rate may vary). The Board's proposal would ensure that the presentation of introductory rates in all written advertisements for open-end credit is consistent with the presentation requirements for promotional materials accompanying applications and solicitations, as discussed below. The Board believes consumers will benefit from these enhancements and advertisers will benefit from the consistent application of requirements related to introductory rates for all written open-end advertisements. Since the Board plans to address issues related to HELOCs during the next phase of its review of Regulation Z, proposed § 226.16(e) would not apply to advertisements of HELOCs subject to § 226.5b. The requirements of § 226.16(e) would apply to communications that are considered advertisements, and would not include disclosures required under § 226.5a and under § 226.6.

**<u>16(e)(2) Definitions</u>**

TILA Section 127(c)(6)(D)(i), as added by Section 1303(a) of the Bankruptcy Act, defines a temporary APR as a rate of interest applicable to a credit card account for an introductory period of less than 1 year, if that rate is less than an APR that was in effect within 60 days before the date of mailing the application or solicitation. 15 U.S.C. 1637(c)(6)(D)(i). TILA Section 127(c)(6)(D)(ii) defines an "introductory period" as "the maximum time period for which the temporary APR may be applicable."

15 U.S.C. 1637(c)(6)(D)(ii). The Board proposes to implement the definition of "introductory period" in § 226.16(e)(2) without change. With respect to the definition of "temporary APR," the Board proposes to implement the term more broadly, as discussed below.

Since the term "introductory rate" is a commonly understood term that is currently used in Regulation Z, the Board proposes to use the term "introductory rate" in place of "temporary APR" for consistency and to facilitate compliance. Furthermore, for the reasons set forth below, the Board would implement the term more broadly to apply to any rate of interest applicable to an open-end plan for an introductory period if that rate is less than the advertised APR that will apply at the end of the introductory period.

The statutory definition compares the temporary APR to an APR that was in effect within 60 days before the date of mailing of the application or solicitation. Since the advertised variable rate that will apply at the end of the introductory period in direct-mail credit card applications and solicitations (and accompanying promotional materials) must have been in effect within 60 days before the date of mailing, as required under proposed § 226.5a(c)(2)(i) (and currently under § 226.5a(b)(1)(ii)), the Board's proposed definition captures the same concept in more simple language. Furthermore, because the Board is proposing to extend these requirements to publicly available applications and solicitations as well as applications and solicitations offered through the Internet, the Board's proposed definition of "introductory rate" would also incorporate the timing requirements for variable rates under proposed §§ 226.5a(c)(2) and 226.5a(e)(4).

The statutory definition currently applies to offers where the introductory period is less than 1 year. The Board is proposing to extend the definition of "introductory rate" to include offers where the introductory period is a year or more, in order to promote the informed use of credit. Creditors, however, often offer an introductory rate for a year or more, and the Board believes that consumers would benefit from the application of the requirements imposed by the Bankruptcy Act on introductory rates to these types of offers as well. In addition, the requirements for the advertisement of "discounted variable-rate plans" under current comment 16(b)-6 are not limited to offers where the introductory period is less than 1 year, and the Board believes that these requirements should continue to apply to such advertised offers.

The requirements for "discounted variable-rate plans" under current comment 16(b)-6 apply solely to variable-rate plans. In adopting the proposed definition of "introductory rate" at § 226.16(e)(2), the Board would cover both variable- and nonvariable-rate plans under the requirements regarding the presentation of introductory rates. Current comment 16(b)-6 would be deleted as obsolete.

**16(e)(3) Stating the Term "Introductory"**

Under TILA Section 127(c)(6)(A), as added by section 1303(a) of the Bankruptcy Act, the term "introductory" must be used in immediate proximity to each listing of the temporary APR in the application, solicitation, or promotional materials accompanying such application or solicitation. 15 U.S.C. 1637(c)(6)(A). The Board solicited comment in the October 2005 ANPR on what type of guidance was appropriate with respect to this requirement. Q86.

Abbreviation. In the October 2005 ANPR, many commenters asked the Board to consider permitting creditors to use the term "intro" as an alternative to the word "introductory." One commenter also asked the Board to consider permitting creditors to use terms that convey the same meaning (such as "temporary"). Because "intro" is a commonly-understood abbreviation of the term "introductory," the Board proposes to allow creditors to use "intro" as an alternative to the requirement to use the term "introductory" in new § 226.16(e)(3). Because the Bankruptcy Act requires the use of the term "introductory," the Board does not propose to allow use of a different term.

Immediate proximity. Responses to the October 2005 ANPR suggested three general approaches to interpreting the meaning of "immediate proximity": (1) immediately preceding or following the APR; (2) within the same sentence as the APR (or within a certain number of words); or (3) in the sentence immediately preceding or following the sentence with the APR. After considering comments, the Board is proposing to provide a safe harbor for creditors that place the word "introductory" or "intro" within the same phrase as each listing of the temporary APR. This guidance is in proposed comment 16(e)-2. The Board believes that interpreting "immediate proximity" to mean adjacent to the rate may be too restrictive and would effectively ban phrases such as "introductory balance transfer rate X percent." Moreover, the Board has proposed a safe harbor, recognizing that there may be instances where the term "introductory" may arguably appear in "immediate proximity" of the rate, yet not necessarily be in the same phrase as the rate, such as in a graphic.

**16(e)(4) Stating the Introductory Period and Post-Introductory Rate**

TILA Section 127(c)(6)(A), as added by Section 1303(a) of the Bankruptcy Act, also requires that the time period in which the introductory period will end and the APR that will apply after the end of the introductory period be listed in a clear and conspicuous manner in a "prominent location closely proximate to the first listing" of the introductory APR (disclosures in the application and solicitation table are not covered). 15 U.S.C. 1637(c)(6)(A). The Board specifically solicited comments on this provision in the October 2005 ANPR. Q87 – Q90.

Prominent location closely proximate. Industry comments received during the October 2005 ANPR generally advocated flexibility in interpreting the phrases "prominent location" and "closely proximate." Consumer group commenters suggested very specific formatting requirements in interpreting these phrases, including minimum font size and placement requirements.

The Board believes flexible guidance is appropriate in interpreting "prominent location closely proximate" given the numerous ways this information may be presented. Accordingly, the Board is proposing a safe harbor in order to provide guidance on this issue. Specifically, the Board would provide a safe harbor for advertisers that place the time period in which the introductory period will end and the APR that will apply after the end of the introductory period in the same paragraph as the first listing of the introductory rate. This proposal is in proposed comment 16(e)-3. Congress's use of the term "closely proximate" may be distinguished from its use of the term "immediate proximity", and thus, the Board believes that guidance on the meaning of "prominent location closely proximate" should be more flexible than the guidance given for the meaning of "immediate proximity" in comment 16(e)-2.

Recognizing that there may be instances where the information may not appear in the same "paragraph" as the first listing and yet may still be considered in a prominent location closely proximate to the first listing (for example, in a graphic), the Board's guidance has been provided as a safe harbor. Consumer testing conducted for the Board suggests that placing this type of information in a footnote makes it much less likely the consumer will notice it. In light of the statutory provision providing that this information appear in a prominent location closely proximate to the listing, the Board believes that placing this information in footnotes would not be a prominent location closely proximate to the listing.

First listing. In the October 2005 ANPR, the Board solicited comments on which listing of the temporary APR should be considered the "first listing" other than the rate listed in the table required on or with credit card applications or solicitations. In particular, the Board requested comment on (1) which document within a multi-page mailing should be considered the one with the first listing, and (2) which listing of the introductory APR within a particular document should be considered the first listing. With respect to the first question, commenters suggested either (1) that the first listing should apply to the "principal promotional document" in the package, or (2) that the Board treat each separate document within a mailing as a separate solicitation such that the information would need to appear in a prominent location closely proximate to the first listing on each separate document. The "principal promotional document" is a concept used in connection with the placement of a prescreening opt-out notice under the Fair Credit Reporting Act (FCRA). 15 U.S.C. 1681 et seq. The FTC, in its regulations related to the FCRA, defines the "principal promotional document" as "the document designed to be seen first by the consumer such as the cover letter." 16 CFR part 642.2(b).

After considering comments received during the ANPR, the Board is proposing in comment 16(e)-4 to provide that for a multi-page mailing or application or solicitation package, the first listing should apply solely to the "principal promotional document" in the package, unless the introductory rate is not listed in the principal promotional document and appears in another document in the package. If the introductory rate does not appear in the principal promotional document but appears in another document in the package, then the requirements apply to each separate document that lists the introductory rate. Proposed comment 16(e)-4 clarifies that the term "principal promotional document" includes solicitation letters. The Board's consumer testing efforts suggest that consumers are likely to read the principal promotional document. Applying the requirement to each document in a mailing/package would be unnecessary if the consumer will already have seen the introductory rate in the principal promotional document. If the introductory rate does not appear in the principal promotional document, however, the Board proposes that the requirements apply to the first listing of the introductory rate in each document in the package containing the introductory rate as it is not clear which document the consumer will read first in such circumstances.

With respect to the question of which listing of the introductory rate within a particular document should be considered the first listing, many industry commenters suggested that creditors be given flexibility in determining which listing is the first listing. Some commenters suggested that the first listing be the highest listing on the page while other commenters advocated the most prominent listing. After considering comments, the Board is proposing that the first listing be the most prominent listing of the introductory rate on the front of the first page of the document. Consumer testing conducted for the Board suggests that consumers may not necessarily read documents in an application/solicitation package from top to bottom. Instead, they may tend to look first to the pieces of information that are set forth most prominently on the document. As a result, the Board believes that the first listing (i.e., the one the consumer sees first) would not necessarily be the highest one on the page, especially if such listing is in an inconspicuous format, and instead, it would be the one that is most prominent to the consumer. In terms of judging which listing is the "most prominent," the Board is proposing a safe harbor for the listing with the largest type size. While type size is one measure for judging the most prominent listing, the Board recognizes that there may be other ways to assess the most prominent listing independent of type size.

Post-introductory rate. The Board requested comment in the October 2005 ANPR regarding whether the Board should issue guidance with respect to listing the rate that will apply after the end of the introductory period. Q90. Most commenters agreed that advertisers should be permitted to list a range of rates. Consistent with the guidance given above for listing the APR in the table required for credit card applications and solicitations under § 226.5a(b)(1)(v), the Board is proposing that a range of rates may be listed as the rate that will apply after the introductory period if the specific rate for which the consumer will qualify will depend on later determinations of a consumer's creditworthiness. See section-by-section analysis to § 226.5a(b)(1). The Board proposes comment 16(e)-5 to be consistent with comment 5a(b)(1)-5. In addition, the Board solicits comment on whether advertisers may alternatively list only the highest rate that may apply instead of a range of rates. For example, if there are three rates that may apply (9.99 percent, 12.99 percent or 17.99 percent), instead of disclosing three rates (9.99 percent, 12.99 percent or 17.99 percent) or a range of rates (9.99 percent to 17.99 percent), card issuers should be permiteed toprovide only the highest rate (up to 17.99 percent).

**16(e)(5) Envelope Excluded**

TILA Section 127(c)(6)(B), as added by Section 1303(a) of the Bankruptcy Act, specifically excludes envelopes or other enclosures in which an application or solicitation to open a credit card account is mailed from the requirements of TILA Section 127(c)(6)(A)(ii) and (iii). 15 U.S.C. 1637(c)(6)(B). This guidance is set forth in proposed § 226.16(e)(5).

In the October 2005 ANPR, the Board solicited comment on whether there should be any difference in guidance provided to applications and solicitations provided electronically with those that are provided in paper form. Q92. In response to comments received, the Board is proposing in § 226.16(e)(5) to exclude banner advertisements and pop-up advertisements that are linked to an electronic application or solicitation. In the Board's view, these devices are similar to envelopes or other enclosures in the direct mail context.

**16(f) Alternative Disclosures—Television or Radio Advertisements**

For radio and television advertisements, the Board is proposing to allow alternative disclosures to the ones required by § 226.16(b) if a triggering term is stated in the advertisement. Radio and television advertisements would still be required to disclose any APR applicable to the plan, consistent with the requirements in proposed § 226.16(b)(1)(ii); however, instead of the detailed information in proposed§§ 226.16(b)(1)(i) and (iii) (minimum or fixed payments, and annual or membership fees, respectively) an advertisement would be able to provide a toll-free telephone number that the consumer may call to receive more information.

This approach is consistent with the approach taken in the advertising rules for Regulation M (See § 213.7(f)). Given the space and time constraints on radio and television advertisements, the additional disclosures required by proposed §§ 226.16(b)(1)(i) and (iii) may go unnoticed by consumers or be difficult for them to retain and would therefore not provide a meaningful benefit to consumers. An alternative means of disclosure may be more effective in many cases given the nature of television and radio media.

While proposed § 226.16(f) is similar to § 213.7(f) in Regulation M, it is not identical. For example, § 213.7(f)(1)(ii) permits a leasing advertisement made through television or radio to direct the consumer to a written advertisement in a publication of general circulation in a community served by the media station. The Board believes that advertisers of open-end credit plans would be unlikely to use this option and has thus not proposed it for § 226.16(f).

**16(g) Misleading Terms**

Creditors often refer to an APR as "fixed" to denote an APR that is not tied to an index. However, the Board has found through consumer testing efforts that most participants did not appear to understand the term "fixed" in this manner. Participants also did not appear to understand that creditors often reserve the right to increase a "fixed" rate upon the occurrence of certain events (such as when a consumer pays late or goes over the credit limit) or for other reasons. Thus, consumer testing suggests many consumers believe a "fixed" rate does not change, such as with fixed-rate mortgage loans.

Therefore, to avoid consumer confusion and the uninformed use of credit, the Board proposes to restrict the term "fixed" to instances where the rate will not change for any reason. 15 U.S.C. 1601(a), 1604(a). Proposed § 226.16(g) prohibits the use of the term "fixed" or any similar term in describing an APR unless that rate will remain in effect unconditionally until the expiration of an advertised time period. If no time period is advertised, then the term "fixed" or any similar term may not be used unless the rate will remain in effect unconditionally until the plan is closed. For example, a creditor could describe a rate that is subject to change as non-indexed, to indicate that the rate will not change due to changes in the market. A creditor could not, however, describe a rate as "unchanging" or "permanent" unless the standard in proposed § 226.16(g) is met. Restricting the use of the term "fixed" is intended to help consumers distinguish rates that do not change for any reason from rates that can change for one reason or another.

**APPENDIX E – Rules for Card Issuers That Bill on a Transaction-by-Transaction Basis**

Appendix E applies to card programs in which the card issuer and the seller are the same or related persons; no finance charge is imposed; cardholders are billed in full for each use of the card on a transaction-by-transaction basis; and no cumulative account is maintained reflecting transactions during a period of time such as a month. At the time the provisions now constituting Appendix E (originally adopted as an official Board interpretation to Regulation Z) were added to the regulation, they were intended to address card programs offered by automobile rental companies.

Appendix E specifies the provisions of Regulation Z that apply to credit card programs covered by the Appendix. For example, for the account-opening disclosures under § 226.6, the required disclosures are limited to penalty charges such as late charges, and to a disclosure of billing error rights and of any security interest. For the periodic statement disclosures under § 226.7, the required disclosures are limited to identification of transactions and an address for notifying the card issuer of billing errors. Further, since Appendix E card issuers do not issue periodic statements of account activity, Appendix E provides that these disclosures may be made on the invoice or statement sent to the consumer for each transaction. In general, the disclosures that this category of card issuers need not provide are those that are clearly inapplicable, either because the disclosures relate to finance charges, are based on a system in which periodic statements are generated, or apply to three-party credit cards (such as bank-issued credit cards).

The Board proposes to revise Appendix E by inserting material explaining what is meant by "related persons." In addition, technical changes would be made, including numbering the paragraphs within the appendix and changing cross-references to conform to the renumbering of other provisions of Regulation Z.

The Board solicits comment on whether Appendix E should be revised to specify that the disclosures required under § 226.5a apply to card programs covered by the appendix. For the most part, the credit card application and solicitation disclosures required by § 226.5a appear to be inapplicable to this category of card programs because most of those disclosures relate to finance charges or APRs. However, a few of the § 226.5a disclosures could potentially apply, such as annual or membership fees and late charges. (Appendix E does not currently require a disclosure of annual or membership fees; comment is requested, however, on whether the appendix should be revised to require such a disclosure, if a transaction-by-transaction card issuer were to impose such a fee.) If few or no such card issuers impose fees covered by § 226.5a, there may be no need to revise Appendix E to apply these requirements. In addition, the value of such a revision may depend on whether transaction-by-transaction card issuers typically make credit card applications or solicitations available to consumers in the ways specified by § 226.5a, such as by direct mail, telephone solicitation, or as take-ones. On the other hand, if Appendix E were revised to apply § 226.5a to these card issuers, they would have to comply only to the extent the requirements are applicable. Thus, no burden would be imposed on card issuers that, for example, do not impose late-payment fees or annual fees, or do not conduct direct-mail credit card solicitations or other activities that come within § 226.5a.

The Board also requests comment on whether any other provisions of Regulation Z not currently specified in Appendix E as applicable to transaction-by-transaction card issuers (such as §§ 226.5b and 226.16) should be specified as being applicable, and on whether any provisions currently specified as being applicable should be deleted.

**APPENDIX F – Annual Percentage Rate Computations for Certain Open-end Credit Plans**

Appendix F provides guidance regarding the computation of the effective APR under § 226.14(c)(3), which applies to situations where the finance charge imposed during a billing cycle includes a transaction charge, such as a balance transfer fee or a cash advance fee. As discussed in the section-by-section analysis to §§ 226.7(a)(7) and (b)(7), and § 226.14, the Board is proposing two alternative approaches for computation and disclosure of the effective APR. Depending upon the alternative and upon whether or not the plan is home-secured, the creditor (1) may use proposed § 226.14(c)(3) or § 226.14(d)(3) if the finance charge for the billing cycle includes a transaction charge, or (2) would not be required to calculate and disclose an effective APR at all. The guidance in existing Appendix F would continue to apply to either proposed § 226.14(c)(3) or proposed § 226.14(d)(3). Therefore, the Board is not proposing changes to Appendix F except to add applicable cross references and to move the substance of footnote 1 to Appendix F to the text of the appendix. A cross-reference to proposed comment 14(d)(3)-3 is added to the staff commentary to Appendix F.

**APPENDIX G – Open-end Model Forms and Clauses; APPENDIX H – Closed-end Model Forms and Clauses**

Appendices G and H set forth models 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 add or revise several model and sample forms to Appendix G. The new or revised model and samples forms are discussed above in the section-by-section analysis applicable to the regulatory provisions to which the forms relate. See section-by-section analysis to §§ 226.4(d)(3), 226.5a(b), 226.6(b)(4), 226.6(c)(2), 226.7(b), 226.9(a), 226.9(b), 226.9(c), 226.9(g) and 226.12(b). In addition, the Board proposes to add a new model clause and sample form relating to debt suspension coverage in Appendix H. These forms are discussed above in the section-by-section analysis of § 226.4(d)(3). In Appendix G, all the existing forms applicable to home-equity lines of credit (HELOCs) have been retained without revision. The Board anticipates considering changes to these forms when it reviews the home-equity disclosure requirements in Regulation Z.

The Board also proposes to revise or add commentary to the model and sample forms in Appendix G, as discussed below. The Board solicits comment on the proposed revisions below, as well as whether any additional commentary should be added to explain the model and sample forms contained in Appendix G.

Permissible changes to the model and sample forms. 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. See comment app. G and H-1. As discussed above, the Board is proposing format requirements with respect to certain disclosures applicable to open-end (not home-secured) plans, such as a tabular requirement for certain account-opening disclosures and certain change-in-terms disclosures. See § 226.5(a)(3). In addition, the Board is proposing revisions to certain model forms to improve their readability. See proposed G-2(A), G-3(A) and G-4(A). Thus, the Board would amend comment app. G and H-1 to indicate that with respect to certain model and sample forms in Appendix G, formatting changes may not be made to the model and sample forms.

In a technical revision, the Board proposes to delete comment app. G and H-1(vii) as obsolete. This comment allows a creditor to substitute appropriate references, such as "bank," "we" or a specific name, for "creditor" in the account-opening disclosures, but none of the model or sample forms applicable to the account-opening disclosures uses the term "creditor."

Model clauses for notice of liability for unauthorized use and billing-error rights. Currently, Appendix G contains Model Clause G-2 which provides a model clause for the notice of liability for unauthorized use of a credit card. The Board is proposing revisions to Model Clause G-2 to improve its readability. This revised model clause is designated G-2(A). In addition, Appendix G currently contains Model Forms G-3 and G-4, which contain models for the long-form billing-error rights statement (for use with the account-opening disclosures and as an annual disclosure or, at the creditor's option, with each periodic statement) and the alternative billing-error rights statement (for use with each periodic statement), respectively. Like with Model Clause G-2, the Board is proposing revisions to Model Forms G-3 and G-4 to improve readability. The revised model forms are designated Model Form G-3(A) and G-4(A). The Board is proposing to revise comments app. G and H-2 and 3 to provide that for HELOCs subject to § 226.5b, at the creditor's option, a creditor either may use the current forms (G-2, G-3, and G-4) or the revised forms (G-2(A), 3(A) and 4(A)). For open-end (not home-secured) plans, creditors may use the revised forms.

Model and sample forms applicable to disclosures for credit card applications and solicitations and account-opening disclosures. Currently, Appendix G contains several model forms related to the credit card application and solicitation disclosures required by § 226.5a. Current Model Form G-10(A) illustrates, in the tabular format, the disclosures required under § 226.5a for applications and solicitations for credit cards other than charge cards. Current Sample G-10(B) is a sample disclosure illustrating an account with a lower introductory rate and a penalty rate. Model Form G-10(A) and Sample G-10(B) would be substantially revised to reflect the proposed changes to § 226.5a, as discussed in the section-by-section analysis to § 226.5a. In addition, the Board proposes to add Sample G-10(C) to provide another example of how certain disclosures required by § 226.5a may be given. Under the proposal, current Model Form G-10(C) illustrating the tabular format disclosures for charge card applications and solicitations would be moved to G-10(D) and revised. The Board proposes to add Sample G-10(E) to provide an example of how certain disclosures in § 226.5a applicable to charge card applications and solicitations may be given. In addition, the Board proposes to add a model form and two sample forms to illustrate, in the tabular format, the disclosures required under § 226.6(b)(4) for account-opening disclosures. See proposed Model G-17(A) and Samples G-17(B) and G-17(C).

The Board also proposes to revise the existing commentary that provides guidance to creditors on how to use Model Forms and Samples G-10(A)-(E) and G-17(A)-(C). Currently, the commentary indicates that the disclosures required by § 226.5a may be arranged horizontally (where headings are at the top of the page) or vertically (where headings run down the page, as is shown in the Model Forms G-10(A), G-10(D) and G-17(A), and need not be highlighted aside from being included in the table. The Board proposes to delete this guidance and instead require that the table for credit card application and solicitation disclosures and account-opening disclosures be presented in the format shown in proposed Model Forms G-10(A), G-10(D) and G-17(A), where a vertical format is used. The Board would no longer allow a horizontal format because such formats would be difficult for consumers to read, given the information that is required to be disclosed in the table. In addition, the Board proposes to delete the provision that disclosures in the tables need not be highlighted aside form being included in the table, as inconsistent with the proposed requirement that creditors must include certain rates and fees in the tables in bold text. See §§ 226.5a(a)(2)(iv) and 226.6(b)(4)(i)(C).

In addition, Model Form G-10(A) applicable to credit card applications and solicitations currently uses the heading "Minimum Finance Charge" for disclosing a minimum finance charge under § 226.5a(b)(3). The Board proposes to amend Model Form G-10(A) to provide two alternative headings ("Minimum Interest Charge" and "Minimum Charge") for disclosing a minimum finance charge under § 226.5a(b)(3). The same two heading are proposed for Model Form G-17(A), the model form for the account-opening table required under § 226.6(b)(4). In the consumer testing conducted for the Board, many participants did not understand the term “finance charge” in this context. The term “interest” was more familiar to many participants. Under the proposal, if a creditor imposes a minimum finance charge in lieu of interest in those months where a consumer would otherwise incur an interest charge but that interest charge is less than the minimum charge, the creditor should disclose this charge under the heading “Minimum Interest Charge.” Other minimum finance charges should be disclosed under the heading “Minimum Charge.”

Also, under the proposal, Model Forms G-10(A), G-10(D) and G-17(A) contain two alternative headings (“Annual Fees” and “Set-up and Maintenance Fees”) for disclosing fees for issuance or availability of credit under § 226.5a(b)(2) or § 226.6(b)(4)(iii)(A). The Board proposes to provide guidance on when creditor should use each heading. Under the proposal, if the only fee for issuance or availability of credit disclosed under § 226.5a(b)(2) or § 226.6(b)(4)(iii)(A) is an annual fee, a creditor should use the heading “Annual Fee” to disclose this fee. If a creditor imposes fees for issuance or availability of credit disclosed under § 226.5a(b)(2) or § 226.6(b)(4)(iii)(A) other than, or in addition to, an annual fee, the creditor should use the heading “Set-up and Maintenance Fees” to disclose fees for issuance or availability of credit, including the annual fee.

The Board also would revise the commentary to provide details about proposed sample forms G-10(B), G-10(C), G-17(B) and G-17(C) for credit card application and solicitation disclosures and account-opening disclosures. For example, the commentary indicates that samples G-10(B), G-10(C), G-17(B) and G-17(C) are designed to be printed on an 8x14 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 purchase 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.

3. Adequate spacing between paragraphs when several pieces of information were included in the same row of the table, as appropriate. For example, in the samples, in the row of the tables with the heading “APR for Balance Transfers,” the forms disclose three components: (a) the applicable balance transfer rate, (b) a cross-reference to the balance transfer fee, and (c) a notice about payment allocation. The samples show these three components on separate lines with adequate space between each component. On the other hand, in the samples, in the disclosure of the late payment fee, the form discloses two components: (a) the late-payment fee, and (b) the cross-reference to the penalty rate. Because the disclosure of both these components is short, these components are disclosed on the same line in the table.

4. Standard spacing between words and characters.

5. 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.

6. Sufficient contrast between the text and the background. Black text was used on white paper.

While the Board is not requiring issuers 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 issuers to consider these techniques when disclosing information in the table, to ensure that the information is presented in a readable format.

<u>Model and sample forms for periodic statements</u>. The Board is proposing to add several model forms for periodic statements disclosures that creditors may use to comply with the requirements in proposed § 226.7(b) applicable to open-end (not home-secured) plans. As discussed above in the section-by-section analysis of § 226.7(a), for HELOCs subject to § 226.5b, at the creditor's option, a creditor either may comply with the current rules applicable to periodic statement disclosures in § 226.7(a) or comply with the new rules applicable to periodic statement disclosures in § 226.7(b). The Board proposes to added comment app. G and H-8 to provide that for HELOCs subject to § 226.5b, if a creditor chooses to comply with the new periodic statement requirements in § 226.7(b), the creditor may use Samples G-18(A)-(F) to comply with the requirements in § 226.7(b).

## <u>APPENDIX M1 – Generic Repayment Estimates</u>

As discussed in the section-by-section analysis to § 226.7(b)(12), Section 1301(a) of the Bankruptcy Act requires creditors, the FTC and the Board to establish and maintain toll-free telephone numbers in certain instances in order to provide consumers with an estimate of the time it will take to repay the consumer's outstanding balance, assuming the consumer makes only minimum payments on the account and the consumer does not make any more draws on the account. 15 U.S.C. § 1637(b)(11)(F). The Act requires creditors, the FTC and the Board to provide estimates that are based on tables created by the Board that estimate repayment periods for different minimum monthly payment amounts, interest rates, and outstanding balances. Instead of issuing a table, the Board proposes to issue guidance in Appendix M1 to card issuers and the FTC for how to calculate this generic repayment estimate. The Board would use the same guidance to calculate the generic repayment estimates given through its toll-free telephone number. The Board expects that this guidance would be more useful than a table, because the guidance will facilitate the use of automated systems to provide the required disclosures, although the guidance also can be used to generate a table.

Under Section 1301(a) of the Bankruptcy Act, a creditor may use a toll-free telephone number to provide the actual number of months that it will take consumers to repay their outstanding balance instead of providing an estimate based on the Board-created table. 15 U.S.C. 1637(b)(11)(I)-(K). The Board proposes new Appendix M2 to provide guidance to issuers on how to calculate the actual repayment disclosure.

Calculating generic repayment estimates. Proposed Appendix M1 provides guidance on how to calculate the generic repayment estimates. In the October 2005 ANPR, the Board noted that the Bankruptcy Act directs the Board in estimating repayment periods to allow for a significant number of different minimum payment amounts, interest rates, and outstanding balances. With respect to the toll-free telephone numbers set up by the Board and the FTC, information about the consumers' account terms must come from consumers because the information is not available to the Board or the FTC. Consumers would need convenient access to this information to request an estimated repayment period. Because consumers' outstanding account balances appear on their monthly statements, consumers are able to provide that amount when requesting an estimate of the repayment period. Issues arise, however, with respect to the minimum payment requirement and interest rate information.

Periodic statements do not disclose the fixed percentage or formula used to determine the minimum dollar amount that must be paid each month. The statements only disclose the minimum dollar amount that must be paid for the current statement period, which would vary each month as the account balance changes. Furthermore, while periodic statements must disclose all APRs applicable to the account, the statements may, but do not necessarily, indicate the portion of the account balance subject to each APR. This information is also needed to estimate the actual repayment period.

The Board sought commenters' views regarding three basic approaches for developing a system to calculate estimated repayment periods for consumers who call the toll-free telephone number. The three approaches were:

(1) Prompting consumers to provide an account balance, a minimum payment formula, and all applicable APRs in order to obtain an estimated repayment period. For information about minimum payments and APRs that is not currently disclosed on periodic statements, the Board could require additional disclosures on those statements. But the Board also could develop guidance that makes assumptions about these variables for a "typical" account.

(2) Prompting consumers to input information, or using assumptions based on a "typical" account to calculate an estimated repayment period—but also giving creditors the option to input information from their own systems regarding consumers' account terms, to provide more accurate estimates. Estimates provided by creditors that elect this option would differ somewhat from the estimates provided by other creditors, the Board, and the FTC.

(3) Prompting consumers to provide their account balance, but requiring creditors to input information from their own systems regarding the account's minimum payment requirement, APRs, and the portion of the balance subject to each APR. These estimates

would be more accurate, but would impose additional compliance burdens, and would not necessarily reflect consumers' actual repayment periods because of the use of several other assumptions.

In response to the October 2005 ANPR, industry commenters urged the Board not to require issuers to program their systems to obtain consumers' account information from their account management systems to calculate the generic repayment estimate. These commenters indicated that such a requirement was not contemplated by the statute. Several consumer group commenters indicated that issuers should be required to use inputs from their own systems about minimum monthly payment formulas, APRs, and account balances applicable to an account in calculating the generic repayment estimate.

The Board is proposing to allow credit card issuers and the FTC to use a "consumer input" system to collect information from the consumer to calculate the generic repayment estimate. The Board would also use a "consumer input" system for its toll-free telephone number. For example, certain information is needed to calculate the generic repayment estimate, such as the outstanding balance on the account and the APR applicable to the account. The Board's proposed rule would allow issuers and the FTC to prompt the consumer to input this information so that the generic repayment estimate can be calculated. Although issuers have the ability to program their systems to obtain consumers' account information from their account management systems, the Board is not proposing that issuers be required to do so. Allowing issuers to use a "consumer input" system in calculating the generic repayment estimate preserves the distinction between estimates based on the Board table and actual repayment disclosures contemplated in the statute.

In proposed Appendix M1, the Board sets forth guidance for credit card issuers and the FTC in determining the minimum payment formula, the APR, and the outstanding balance to use in calculating the generic repayment estimates. With respect to other terms that could impact the calculation of the generic repayment estimate, the Board proposes to set forth assumptions about these terms that issuers and the FTC must use.

1. Minimum payment formula. In the October 2005 ANPR, the Board sought comment on whether the Board should select a "typical" minimum payment formula that issuers and the FTC must use in calculating the generic repayment estimates. Q66. In response to the ANPR, many industry commenters acknowledged that there is no "typical" minimum payment formula for credit cards. Nonetheless, some industry commenters indicated that the Board should use a minimum formula of 1 percent of the outstanding balance plus the accrued finance charges for the billing period, with a minimum payment of $20. Another industry commenter indicated that the Board should require that issuers, the FTC and the Board use the minimum payment formula in the statutory examples to calculate the generic repayment estimate. As indicated above, several consumer groups indicated that issuers should be required to use the minimum payment formula(s) that is applicable to the consumer's account. These commenters indicated that the FTC and the Board should be required to use a minimum payment

formula that is identified by the Board as producing the "worst-case scenario" repayment estimate.

As indicated in Appendix M1, the Board proposes to require credit card issuers to use the minimum payment formula that applies to most of the issuer's accounts. The Board proposes different rules for general-purpose credit cards and retail credit cards in selecting the "most common" minimum payment formula. The Board proposes to define retail credit cards as credit cards that are issued by a retailer for use only in transactions with the retailer or a group of retailers that are related by common ownership or control, or a credit card where a retailer arranges for a creditor to offer open-end credit under a plan that allows the consumer to use the credit only in transactions with the retailer or a group of retailers that are related by common ownership or control. General-purpose credit cards are defined as credit cards that are not retail credit cards.

When calculating the generic repayment estimate for general-purpose credit cards, card issuers must use the minimum payment formula that applies to most of its general-purpose credit card accounts. The issuer must use this "most common" formula to calculate the generic repayment estimate for all of its general-purpose credit card accounts, regardless of whether this formula applies to a particular account. Proposed Appendix M1 contains additional guidance to issuers of general-purpose credit cards in complying with the "most common" formula approach. The Board solicits comment on the need for guidance if two or more formulas could apply equally to the same number of accounts.

When calculating the generic repayment estimate for retail credit cards, credit card issuers must use the minimum payment formula that most commonly applies to its retail credit card accounts. If an issuer offers credit card accounts on behalf of more than one retailer, credit card issuers must group credit card accounts relating to each retailer separately, and determine the minimum formula that is most common to each retailer. For example, if Issuer A, the owner of Retailer A and Retailer B, issues separate cards for Retailer A and Retailer B, the proposal would require Issuer A to determine the most common formula separately for each retailer (A and B). Under the proposal, the issuer must use the "most common" formula for each retailer to calculate the generic repayment estimate for the retail credit card accounts related to each retailer, regardless of whether this formula applies to a particular account. Proposed Appendix M1 provides additional guidance to issuers of retail credit cards on how to comply with the "most common" formula approach. The Board solicits comment on whether Issuer A in the example above should be permitted to determine a single "most common" formula for all retailers under its common ownership or control, and if so, what the standard of affiliation should be. The Board also solicits comment on the need for guidance if two or more formulas could apply equally to the same number of accounts.

The Board believes that the "most common" approach described above is preferable to using a "typical" minimum payment formula identified by the Board for several reasons. First, as acknowledged by the industry commenters, there is no "typical" minimum payment formula that generally applies to credit card accounts. Informally, the

Board gathered data on the minimum payment formulas used by the top 10 issuers of general-purpose credit cards. With respect to those 10 issuers, there was no minimum payment formula that most of the issuers used. Second, the minimum payment formula can have a significant impact on the calculation of the generic repayment estimate. For example, based on the minimum payment formulas used by the top 10 issuers, the repayment period for paying a $1000 balance at a 13.99 percent APR if only minimum payments are made can range from 6 years to 12 years depending on the issuer.

In addition, it appears that at least for general-purpose credit cards, issuers typically use the same or similar minimum payment formula for their entire credit card portfolio. Thus, for those types of credit cards, the "most common" minimum payment formula identified by an issuer often will match the actual formula used on a consumer's account. The Board recognizes that in some cases the "most common" minimum payment formula will not match the actual formula used on a consumer's account, for example, where a consumer has opted out of a change in the minimum payment formula, and the consumer is paying off the balance under the old minimum payment formula. The Board also recognizes that allowing retail card issuers to use one minimum payment formula under the "most common" formula approach to calculate the generic repayment estimate even when multiple minimum payment formulas apply to the account yields a less accurate estimate than if the issuer were required to use all the minimum payment formulas applicable to a consumer's account. Nonetheless, short of requiring issuers to obtain the actual minimum payment formula(s) applicable to a consumer's account from the issuer's account management systems to calculate the generic repayment estimate, which does not appear to be contemplated by the statute, the Board believes that the approach of requiring issuers to identify their "most common" minimum payment formulas to calculate the generic repayment estimates is a preferable approach than allowing issuers to use a "typical" formula identified by the Board.

As discussed in the section-by-section analysis to § 226.7(b)12), the Board is required to establish and maintain, for two years, a toll-free telephone number for use by customers of depository institutions having assets of $250 million or less to obtain generic repayment estimates. The Board proposes to use the following minimum payment formula to calculate the generic repayment estimates: either 2 percent of the outstanding balance, or $20, whichever is greater. This is the same minimum payment formula used to calculate the repayment estimate for the statutory example related to the $1,000 balance. The Board proposes to use the same formula as in the statutory example because the Board is not aware of any "typical" minimum payment formula that applies to general-purpose credit cards issued by smaller depository institutions. For the same reasons, the Board proposes that the FTC use the 5 percent minimum payment formula used in the $300 example in the statute to calculate the generic repayment estimates given through the FTC's toll-free telephone number.

2. Annual percentage rates. In the October 2005 ANPR, the Board noted that the statute's hypothetical repayment examples assume that a single APR applies to a single account balance. But credit card accounts can have multiple APRs. The APR may differ for purchases, cash advances, and balance transfers. A card issuer may have a

promotional APR that applies to the initial balance transfer and a separate APR for other balance transfers. Although all the APRs for accounts are disclosed on periodic statements, calculating the repayment period requires information about what percentage or amount of the total ending balance is subject to each APR, and what payment allocation method is used. 15 U.S.C. 1637(b)(5); current § 226.7(d). Currently, the total ending balance is required to be disclosed, but not the portion of the cycle's ending balance that is subject to each APR. 15 U.S.C. 1637(b)(8); current § 226.7(i). (Some creditors may voluntarily disclose such information on periodic statements.) For example, assuming a $1,000 outstanding balance on an account with a 12 percent APR for purchases and a 19.5 percent APR on cash advances, the consumer will know from his or her periodic statement the amount of the total outstanding balance ($1,000), but may not know the percentage or amount of the ending balance is subject to the 12 percent rate and what amount of the ending balance is subject to the 19.5 percent rate. Creditors know the portion of the cycle's ending balance that is subject to each APR, and could develop automated systems that incorporate this information as part of their calculation. But again, the toll-free telephone systems developed by the Board and FTC would have to depend solely on data provided by the consumer.

If multiple APRs apply to the outstanding balance, using the lowest APR to calculate the repayment period would estimate repayment periods that are shorter for some consumers, depending on the components of the balance, while using the highest APR would estimate repayment periods that are longer for some consumers. How much the repayment periods are underestimated or overestimated in each of these cases would depend on which rate applies to the outstanding balance. Using an average of the multiple rates may either overestimate or underestimate the repayment period depending on which rate applies to the outstanding balance. It is unclear whether detailed transaction data about how consumers use their credit card accounts would support a finding that there is a "typical" approach that would provide the best estimate of the repayment periods in most cases.

In the October 2005 ANPR, the Board solicited comment on whether it would be appropriate for accounts that have multiple APRs to calculate an estimated repayment period using a single APR, and if so, which APR for the account should be used. Q71. Most industry commenters suggested that the Board use a single APR. They pointed out that it would be impractical to use multiple APRs for the generic repayment estimate. Consumers would need to understand and input multiple APRs and balances that apply to the accounts (as well as any expiration dates and APRs that apply after any promotional APRs expire). The complexity and effort required to accommodate multiple APRs would be unduly burdensome for consumers, which could discourage consumers from using such an approach, and for creditors. In terms of which APR on the account to use to calculate the generic repayment estimate, some industry commenters indicated that the purchase APR should be used because this is the rate that most typically applies to the majority of the balances on consumers' accounts. Other industry commenters indicated that the highest APR on the account should be used to calculate the generic repayment estimates because this would provide consumers with the "worst-case scenario." Several consumer groups indicated that the Board should require issuers to use all the APRs applicable to a consumer's account in calculating the generic repayment estimates.

The Board proposes to require that the generic repayment estimate be calculated using a single APR, even for accounts that have multiple APRs. As indicated above, the Board does not believe that the statute contemplates that issuers be required to use their account management systems to disclose an estimate based on all of the APRs applicable to a consumer's account and the actual balances to which those rates apply. The Board also agrees with several industry commenters that the complexity and effort required to accommodate multiple APRs using a "consumer-input" system would be unduly burdensome. In selecting the single APR to be used in calculating the generic repayment estimates, the Board proposes to require that credit card issuers, and the FTC use the highest APR on which the consumer has outstanding balances. As proposed, an issuer and the FTC may use an automated system to prompt the consumer to enter in the highest APR on which the consumer has an outstanding balance, and calculate the generic repayment estimate based on the consumer's response. The Board would follow the same approach in calculating the generic repayment estimates for its toll-free telephone number. The Board recognizes that using the highest APR on which a consumer has an outstanding balance will overestimate the repayment period when the consumer has outstanding balances at lower APRs as well. Nonetheless, allowing issuers to use the purchase APR on the account to calculate the repayment period would underestimate the repayment period, if a consumer also has balances subject to higher APRs, such as cash advance balances. The Board believes that an overestimate of the repayment period is a better approach for purposes of this disclosure than an underestimate of the repayment period because it gives consumers the worst-case estimate of how long it may take to pay of their balance.

3. Outstanding balance. As discussed above, because consumers' outstanding account balances appear on their monthly statements, consumers can provide that amount when requesting an estimate of the repayment period. The Board proposes that when calculating the generic repayment estimate, credit card issuers and the FTC must use the outstanding balance on a consumer's account as of the closing date of the last billing cycle to calculate the generic repayment estimates. As proposed, an issuer and the FTC may use an automated system to prompt the consumer to enter in the outstanding balance included on the last periodic statement received, and calculate the generic repayment estimate based on the consumer's response. The Board would follow the same approach in calculating the generic repayment estimates for its toll-free telephone number.

Other terms. In the October 2005 ANPR, the Board noted that Section 1301(a) of the Bankruptcy Act appears to contemplate that the generic repayment estimate should be calculated based on three variables: the minimum payment formula, the APR, and the outstanding balance. Nonetheless, a number of other assumptions can also affect the calculation of a repayment period. For example, the hypothetical examples that must be disclosed on periodic statements incorporate the following assumptions, in addition to the statutory assumptions that only minimum monthly payments are made each month, and no additional extensions of credit are obtained: (1) the balance computation method used is the previous-balance method and finance charges are based on the beginning balance for the cycle; (2) no grace period applies to any portion of the balance; and (3) when the account balance becomes less than the required minimum payment, the receipt of the final amount in full completely pays off the account. In other words, there is no residual finance charge that accrues in the month when the final bill is paid in full.

In the October 2005 ANPR, the Board requested comment on whether the Board should incorporate the above three assumptions into the calculation of the generic repayment estimates. Q67. Most industry commenters generally favored using the above three assumptions in the calculation of the generic repayment estimates. One consumer group commenter indicated that the Board should use "worst-case scenario" assumptions in calculating the generic repayment estimates.

1. Balance computation method. Instead of using the previous-balance method used in the statutory example, the Board proposes to use the average daily balance method for purposes of calculating the generic repayment estimate. The average daily balance method is more commonly used by issuers to compute the balance on credit card accounts. Nonetheless, requiring use of the average daily balance method makes other assumptions necessary, including the length of the billing cycle, and when payments are made. The Board proposes to assume that all months are the same length. In addition, in the absence of data on when consumers typically make their payments each month, the Board proposes to assume that payments are credited on the last day of the month.

2. Grace period. The Board proposes to assume that no grace period exists. The required disclosures about the effect of making minimum payments are based on the assumption that the consumer will be "revolving" or carrying a balance. Thus, it seems reasonable to assume that the account is already in a revolving condition at the time the consumer calls to obtain the estimate, and that no grace period applies. This assumption about the grace period is also consistent with the Board's proposal to exempt issuers from providing the minimum payment disclosures to consumers that have paid their balances in full for two consecutive months.

3. Residual interest. When the consumer's account balance at the end of a billing cycle is less than the required minimum payment, the statutory examples assume that no additional transactions occurred after the end of the billing cycle, that the account balance will be paid in full, and that no additional finance charges will be applied to the account between the date the statement was issued and the date of the final payment. The Board proposes to make these same assumptions with respect to the calculation of the generic repayment estimates. These assumptions are necessary to have a finite solution to the repayment period calculation. Without these assumptions, the repayment period could be infinite.

Disclosing the generic repayment estimates to consumers. The Board proposes in Appendix M1 to provide guidance regarding how the generic repayment estimate must be disclosed to consumers. As discussed in more detail below, credit card issuers and the FTC would be required to provide certain required disclosures to consumers in responding to a request through a toll-free telephone number for generic repayment estimates. In addition, issuers and the FTC would be permitted to provide certain other information to consumers, so long as that permitted information is disclosed after the required information. The Board would follow the same approach in disclosing the generic repayment estimates through its toll-free telephone number.

1. Required disclosures. In the October 2005 ANPR, the Board requested comment on what key assumptions, if any, should be disclosed to consumers in connection with the estimated repayment period. Q76. Some commenters indicated that a number of assumptions should be disclosed to consumers, such as that the estimated repayment period is based on the assumption there will be no new transactions, no late payments, no changes in the APRs and the minimum payment formula, and that only minimum payments are made. Other commenters indicated that the Board should only require a more general statement that the repayment period provided is only an estimate and the actual repayment period would differ based on a number of factors related to the consumers' behavior and the particular terms of their account.

As the rule is proposed, credit card issuers and the FTC would be required to provide the following information when responding to a request for generic repayment estimates through a toll-free telephone number: (1) the generic repayment estimate; (2) the beginning balance on which the generic repayment estimate is calculated; (3) the APR on which the generic repayment estimate is calculated; (4) the assumptions that only minimum payments are made and no other amounts are added to the balance; and (5) the fact that the repayment period is an estimate, and the actual time it make take to pay off the balance if only making minimum payment will differ based on the consumer's account terms and future account activity. The Board proposes to include a model form in Appendix M1 that credit card issuers and the FTC may use to comply with the above disclosure requirements. The Board is proposing to require a brief statement that the repayment period is an estimate rather than include a list of assumptions used to calculate the estimate, because the Board believes the brief statement is more helpful to consumers. The many assumptions that are necessary to calculate a repayment period are complex and unlikely to be meaningful or useful to most consumers. Nonetheless, the Board proposes to allow issuers and the FTC to disclose through the toll-free telephone number the assumptions used to calculate the generic repayment estimates, so long as this information is disclosed after the required information described above. The Board would follow the same approach in disclosing the generic repayment estimates through its toll-free telephone number.

2. Negative amortization. Negative amortization can occur if the required minimum payment is less than the total finance charges and other fees imposed during the billing cycle. Several major credit card issuers have established minimum payment requirements that prevent prolonged negative amortization. But some creditors may use a minimum payment formula that allows negative amortization (such as by requiring a payment of 2 percent of the outstanding balance, regardless of the finance charges or fees incurred). If negative amortization occurs when calculating the repayment estimate, issuers and the FTC would be required to disclose to the consumer that based on the

assumptions used to calculate the repayment estimate, the consumer will not pay off the balance by making only the minimum payment. As proposed, Appendix M1 contains a model form that issuers and the FTC may use to disclose the consumer that negative amortization is occurring. The Board would follow the same approach in disclosing through its toll-free telephone number that negative amortization is occurring.

If creditors use a minimum payment formula that allows for negative amortization, the Board believes that consumers should be told that negative amortization is occurring. The Board recognizes that in some cases because of the assumptions used to calculate the generic repayment estimate, the estimate may indicate that negative amortization is occurring, when in fact, if the estimate was based on the consumer's actual account terms, negative amortization would not occur. The Board strongly encourages issuers to use the actual repayment disclosure provided in proposed Appendix M2 in these instances to avoid giving inaccurate information to consumers.

3. Permitted disclosures. As the rule is proposed, credit card issuers and the FTC may provide the following information when responding to a request for the generic repayment estimate through a toll-free telephone number, so long as this permitted information is given after the required disclosures: (1) a description of the assumptions used to calculate the generic repayment estimate; (2) an estimate of the length of time it would take to repay the outstanding balance if an additional amount was paid each month in addition to the minimum payment amount, allowing the consumer to select the additional amount; (3) an estimate of the length of time it would take to repay the outstanding balance if the consumer made a fixed payment amount each month, allowing the consumer to select the amount of the fixed payment; (4) the monthly payment amount that would be required to pay off the outstanding balance within a specific number of months, allowing the consumer to select the payoff period, (5) a reference to web sites that contains minimum payment calculators; and (6) the total interest that a consumer may pay if he or she makes minimum payments for the length of time disclosed in the generic repayment estimate. The Board would follow the same approach in disclosing permitted information through its toll-free telephone number.

In consumer testing conducted for the Board, several participants reviewed a disclosure that provided an estimate of the time it would take to pay off a $1,000 balance at a 17 percent APR, if the consumer paid $10 more than the minimum payment each month. Most participants that reviewed this disclosure found it to be useful. Thus, the Board is proposing to allow credit card issuers and the FTC, via the toll-free telephone number, to provide this type of disclosure to consumers, as well as other relevant repayment information. The Board believes that consumers may find this information helpful in making decisions about how much to pay each month.

In addition, in the October 2005 ANPR, the Board solicited comment on whether any creditors currently offer web-based calculation tools that permit consumers to obtain estimates of repayment periods. Several industry commenters indicated that they do offer such web-based calculation tools. In addition, other industry commenters indicated that such tools are available on the Internet from a variety of sources. For example, these web sites may provide calculators that provide the monthly payment amount that would be required to pay off a particular balance within a specific number of months indicated by the consumer, and the total interest that would be paid during that period. Because these types of web sites might be useful to consumers to obtain additional information about repayment periods, the Board proposes to allow issuers, and the FTC to provide Internet addresses for these web sites as part of responding to a request for the generic repayment estimate through a toll-free telephone number.

## APPENDIX M2 – Actual Repayment Disclosures

As indicated above, Section 1301(a) of the Bankruptcy Act allows creditors to forego using the toll-free telephone number to provide a generic repayment estimate if the creditor instead provides through the toll-free telephone number the "actual number of months" to repay the consumer's account. In the October 2005 ANPR, the Board requested comment on whether the Board should provide guidance on the how to calculate the actual repayment disclosures. Q77. Commenters generally favored the Board providing such guidance because without this guidance, issuers would be less likely to provide the actual repayment disclosures. The Board proposes to provide in Appendix M2 guidance to credit card issuers on how to calculate the actual repayment disclosure to encourage issuers to provide these estimates.

Calculating the actual repayment disclosures. As a general matter, the Board is proposing that credit card issuers calculate the actual repayment disclosure for a consumer based on the minimum payment formula(s), the APRs and the outstanding balance currently applicable to a consumer's account. For other terms that may impact the calculation of the actual repayment disclosure, the Board proposes to allow issuers to make certain assumption about these terms.

1. Minimum payment formulas. Generally, when calculating actual repayment disclosures, the Board proposes that credit card issuers generally must use the minimum payment formula(s) that apply to a cardholder's account. The Board proposes to allow issuers to disregard promotional terms that may be currently applicable to a consumer account when calculating the actual repayment disclosure. Specifically, if any promotional terms related to payments currently apply to a cardholder's account, such as a "deferred payment plan" where a consumer is not required to make payments on the account for a certain period of time, credit card issuers may assume the promotional terms do not apply, and use the minimum payment formula(s) that would currently apply without regard to the promotional terms. Allowing issuers to disregard promotional terms on accounts eases compliance burden on issuers, without a significant impact on the accuracy of the repayment estimates for consumers.

In addition, in response to the October 2005 ANPR, one commenter indicated that the issuers should not be required in calculating the actual repayment disclosure to develop different estimating methodologies for minimum payment formulas that apply to atypical customers. The commenter indicated that this might occur, for example, where customers have opted out of a newer version of a creditor's minimum payment formula, customers have received test versions of newer minimum payment formulas, or customers have received a relatively unique product with relatively unique versions of the creditor's basic minimum payment formula. The commenter indicated that requiring creditors to develop special estimating methodologies for such small groups of customers would impose significant systems development costs, operational complexities, and similar burdens on creditors in excess of benefits to those customers.

The Board solicits additional comment on why an exception from the general requirement that the actual repayment estimate should be based on the minimum payment formula(s) applicable to a consumer's account is needed for atypical customers. Are the accounts for these atypical customers contained on separate periodic statements systems from other customers? If not, would not the issuer need to make changes only to one periodic statement system to obtain the minimum payment formula(s) applicable to a consumer's account, even if the minimum payment formulas applicable to the consumer's account were atypical?

2. Annual percentage rates. Generally, when calculating actual repayment disclosures, the Board proposes that credit card issuers must use each of the APRs that currently apply to a consumer's account, based on the portion of the balance to which that rate applies. For the reason discussed above, the Board proposes to allow issuers to disregard promotional APRs that may currently apply to a consumer's account. Specifically, if any promotional terms related to APRs currently apply to a cardholder's account, such as introductory rates or deferred interest plans, credit card issuers may assume the promotional terms do not apply, and use the APRs that currently would apply without regard to the promotional terms.

3. Outstanding balance. When calculating the actual repayment disclosures, the Board proposes that credit card issuers must use the outstanding balance on a consumer's account as of the closing date of the last billing cycle. Issuers would not be required to take into account any transactions consumers may have made since the last billing cycle. This rule makes it easier for issuers to place the estimate on the periodic statement, because the outstanding balance used to calculate the actual repayment disclosure would be the same as the outstanding balance shown on the periodic statement.

4. Other terms. As discussed above, as a general matter, the Board is proposing that issuers calculate the actual repayment disclosures for a consumer based on the minimum payment formulas(s), the APRs and the outstanding balance currently applicable to a consumer's account. For other terms that may impact the calculation of the actual repayment disclosures, the Board proposes to allow issuers to make certain assumptions about these terms. For example, the Board would allow issuers to make the same assumptions about balance computation method, grace period, and residual interest as are allowed for the generic repayment estimates. In addition, the Board proposes to allow issuers to assume that payments are allocated to lower APR balances before higher APR balances when multiple APRs apply to an account. This assumption is consistent with typical industry practice regarding how issuers allocate payments. Allowing issuers

to make these assumptions eases compliance burden for issuers, without a significant impact on the accuracy of the actual repayment disclosures.

Disclosing the actual repayment disclosures to consumers through the toll-free telephone number or on the periodic statement. The Board proposes in Appendix M2 to provide guidance regarding how the actual repayment disclosure must be disclosed to consumers if a toll-free telephone number is used or if the actual repayment disclosure is placed on the periodic statement. The Board proposes similar rules with respect to disclosing the actual repayment disclosures as are being proposed with respect to the generic repayment estimate. Specifically, the Board proposes to require credit card issuers to disclose certain information when providing the actual repayment disclosure, and permits the issuers to disclose other related information, so long as that permitted information is disclosed after the required information. See proposed Appendix M2.

**Appendix M3 – Sample Calculations of Generic Repayment Estimates and Actual Repayment Disclosures**

Proposed Appendix M3 provides samples calculations for the generic repayment estimate and the actual repayment disclosures discussed in appendices M1 and M2. Specifically, proposed Appendix M3 contains an example of how to calculate the generic repayment estimate using the guidance in Appendix M1 where the APR is 17 percent, the outstanding balance is $1,000, and the minimum payment formula is 2 percent of the outstanding balance or $20, whichever is greater. In addition, proposed Appendix M3 also provides an example of how to calculate the actual repayment disclosure using the guidance in Appendix M2 where three APRs apply, the total outstanding balance is $1000, and the minimum payment formula is 2 percent of the outstanding balance or $20, whichever is greater. The sample calculations in Appendix M3 are written in SAS code.

## VII. Initial Regulatory Flexibility Act Analysis

In accordance with Section 3(a) of the Regulatory Flexibility Act (5 U.S.C. §§ 601-612) (RFA), the Board is publishing an initial regulatory flexibility analysis for the proposed amendment to Regulation Z.

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.

1. Reasons, statement of objectives and legal basis for the proposed rule. The purpose of the Truth in Lending Act is to promote the informed use of consumer credit by providing for disclosures about its terms and cost. 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 at application and throughout the life of an open-end account. Accordingly, the Board is proposing changes to format, timing, and content

requirements for the five main types of disclosures governed by Regulation Z: (1) credit and charge card application and solicitation disclosures; (2) account-opening disclosures; (3) periodic statement disclosures; (4) change-in-terms notices; and (5) advertising provisions.

The following sections of the Supplementary Information above describe in detail the reasons, objectives, and legal basis for each component of the proposed rule:

- A high-level summary of the major changes being proposed is in **II. Summary of Major Proposed Changes**, and a more detailed discussion is in **V. Discussion of Major Proposed Revisions** and **VI. Section-by-section Analysis**.

- The Board's major sources of rulemaking authority pursuant to TILA are summarized in **IV. The Board's Rulemaking Authority**. More detailed information regarding the source of rulemaking authority for each individual proposed change, as well as the rulemaking authority for certain changes mandated by the Bankruptcy Act, are discussed in **VI. Section-by-section Analysis**.

2. Description of small entities to which the proposed rule would apply. The total number of small entities likely to be affected by the proposal is unknown, because the open-end credit provisions of TILA and Regulation Z have broad applicability to individuals and businesses that extend even small amounts of consumer credit. See § 226.1(c)(1).[19] Based on December 2006 call report data, there are approximately 13,000 depository institutions in the United States that have assets of $165 million or less and thus are considered small entities for purposes of the Regulatory Flexibility Act. Of them, there were 2,293 banks, 3,603 insured credit unions, and 33 other thrift institutions with credit card assets (or securitizations), and total assets less than $165 million. The number of small non-depository institutions that are subject to Regulation Z's open-end credit provisions cannot be determined from information in call reports, but recent congressional testimony by an industry trade group indicated that 200 retailers, 40 oil companies, and 40 third-party private label credit card issuers of various sizes also issue credit cards.[20] There is no comprehensive listing of small consumer finance companies that may be affected by the proposed rules or of small merchants that offer their own credit plans for the purchase of goods or services. Furthermore, it is unknown how many of these small entities offer open-end credit plans as opposed to closed-end credit products, which would not be affected by the proposed rule.

The effect of the proposed revisions to Regulation Z on small entities also is unknown. Small entities would be required to, among other things, conform their open-

[19] 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).

[20] Testimony of Edward L. Yingling for the American Bankers' Association before the Subcommittee on Financial Institutions and Consumer Credit, Financial Services Committee, United States House of Representatives, April 26, 2007, fn. 1, p 3.

end credit disclosures, including those in solicitations, account opening materials, periodic statements, and change-in-terms notices, and advertisements to the revised rules. The precise costs to small entities of updating their systems are difficult to predict. These costs will depend on a number of factors that are unknown to the Board, including, among other things, the specifications of the current systems used by such entities to prepare and provide disclosures and administer open-end accounts, the complexity of the terms of the open-end credit products that they offer, and the range of such product offerings. Nevertheless, the Board believes that these costs will have a significant economic effect on small entities. The Board seeks information and comment on the effects of the proposed rules on small entities.

3. Projected reporting, recordkeeping and other compliance requirements of the proposed rule. The compliance requirements of the proposed rules are described in **VI. Section-by-section Analysis**. 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 institutions.

4. Other federal rules. As noted in the section-by-section analysis for § 226.13(i), there is a potential conflict between Regulation Z and Regulation E with respect to error resolution procedures when a transaction involves both an extension of credit and an electronic fund transfer. The Board has not identified any other federal rules that duplicate, overlap, or conflict with the proposed revisions to Regulation Z. The Board seeks comment regarding any statutes or regulations, including state or local statutes or regulations, that would duplicate, overlap, or conflict with the proposed rule.

5. Significant alternatives to the proposed revisions. As previously noted, the proposed rule implements the Board's mandate to prescribe regulations that carry out the purposes of TILA. In addition, the Board is directed to implement certain provisions of the Bankruptcy Act that require new disclosures on periodic statements, on credit card applications and solicitations, and in advertisements. The Board seeks with this proposed rule to balance the benefits to consumers arising out of more effective TILA disclosures against the additional burdens on creditors and other entities subject to TILA. To that end, and as discussed in **VI. Section-by-section Analysis**, consumer testing was conducted for the Board in order to assess the effectiveness of the proposed revisions to Regulation Z. In this manner, the Board has sought to avoid imposing additional regulatory requirements without evidence that these proposed revisions may be beneficial to consumer understanding regarding open-end credit products.

The Board welcomes comments on any significant alternatives, consistent with TILA and the Bankruptcy Act, that would minimize the impact of the proposed rule on small entities.

## VIII. 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 Federal Reserve 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.). The respondents/recordkeepers are creditors and other entities subject to Regulation Z, including for-profit financial institutions and small businesses.

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, notices 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 twenty-four months (§ 226.25), but Regulation Z does not specify the types of records that must be retained.

Under the PRA, the Federal Reserve 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 lending 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 on other creditors. The current total annual burden to comply with the provisions of Regulation Z is estimated to be 552,398 hours for the 1,172 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 Federal Reserve provides model forms, which are appended to the regulation.

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 73,240 hours, from 552,398 to 625,638 hours. The total one-time burden increase, as well as the estimates of the one-time burden increase associated with each major section of the proposed rule as set forth below, represent averages for all respondents regulated by the Federal Reserve. The Federal Reserve 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, this one-time burden estimate does not include the burden addressing electronic disclosures as announced in a separate proposed rulemaking (Docket No. R-1284)). In addition, the Federal Reserve estimates that, on a continuing basis, the proposed revisions to the rules governing change-in-terms notices would increase the frequency with which such notices are required, and that this change would increase the total annual burden on a continuing basis from 552,398 to 607,759 hours.

As discussed in the preamble, the Federal Reserve proposes changes to format, timing, and content requirements for the five main types of open-end credit disclosures governed by Regulation Z: (1) application and solicitation disclosures; (2) account-opening disclosures; (3) periodic statement disclosures; (4) change-in-terms notices; and (5) advertising provisions.

The proposed revisions to the application and solicitation disclosures are intended to make the content of those disclosures more meaningful and easier for consumers to use. The Federal Reserve estimates that 279 respondents regulated by the Federal Reserve would take, on average, 8 hours (one business day) to reprogram and update their systems to comply with the proposed disclosure requirements in § 226.5a and estimates the annual one-time burden to be 2,232 hours.

The proposed revisions to the account-opening disclosures are intended to make the information in those disclosures more conspicuous and easier for consumers to read. The Federal Reserve estimates that 1,172 respondents regulated by the Federal Reserve would take, on average, 8 hours (one business day) to reprogram and update their systems to comply with the proposed disclosure requirements in § 226.6 and estimates the annual one-time burden to be 9,376 hours.

The proposed revisions to the periodic statement disclosures are intended to make the information in those disclosures more understandable, primarily through changes to the format requirements, such as by grouping fees, interest charges, and transactions together. The Federal Reserve estimates that 1,172 respondents regulated by the Federal Reserve would take, on average, 40 hours (one week) to reprogram and update their systems to comply with the proposed disclosure requirements in § 226.7 and estimates the annual one-time burden to be 42,880 hours.

The proposed revisions to the change-in-terms notices would expand the circumstances under which consumers receive written notice of changes in the terms (e.g., an increase in the interest rate) applicable to their accounts, and increase the amount of time these notices must be sent before the change becomes effective. The Federal Reserve estimates that 1,172 respondents regulated by the Federal Reserve will take, on average, 8 hours (one business day) to reprogram and update their systems to comply with the proposed disclosure requirements in § 226.9(c) and estimates the annual one-time burden to be 9,376 hours; In addition, the Federal Reserve estimates that, on a continuing basis, the proposed revisions to the change-in-terms notices would increase the estimated annual frequency for from 2,500 to 3,750. The estimated annual burden for change-in-terms notices would increase from 36,907 to 55,361 hours.

The proposed changes to the advertising provisions would revise the rules governing advertising of open-end credit to help improve consumer understanding of the credit terms offered. The Federal Reserve estimates that 1,172 respondents regulated by the Federal Reserve would take, on average, 8 hours (one business day) to reprogram and update their systems to comply with the proposed disclosure requirements in § 226.16 and estimates the annual one-time burden to be 9,376 hours.

Additionally, the Federal Reserve proposes to revise the definition of open-end credit in § 226.2(a)(20) to ensure that the appropriate (i.e., open-end or closed-end) disclosures are provided in connection with multifeatured plans. The Federal Reserve also proposes to extend the applicability of the rules in § 226.4 for debt cancellation products to debt suspension products. The Federal Reserve estimates the burden to comply with the § 226.2(a)(20) provisions for open-end credit would be minimal. The burden associated with reprogramming and updating a respondent's systems to comply with the proposed debt suspension disclosure requirements in § 226.4, is included in the one-time burden estimates for application and solicitation and periodic statement disclosures mentioned above.

The other federal financial agencies are responsible for estimating and reporting to OMB the total paperwork burden for the institutions for which they have administrative enforcement authority. They may, but are not required to, use the Federal Reserve's burden estimates. Using the Federal Reserve's method, the total current estimated annual burden for all financial institutions subject to Regulation Z, including Federal Reserve-supervised institutions, would be approximately 12,324,037 hours. The proposed rule would impose a one-time increase in the estimated annual burden for all institutions subject to Regulation Z by 1,389,600 hours to 13,713,637 hours. On a continuing basis, the proposed revisions to the change-in-terms notices would increase the estimated annual frequency, thus increasing the total annual burden on a continuing basis from 12,324,037 to 13,516,584 hours. The above estimates represent an average across all respondents and reflect variations between institutions based on their size, complexity, and practices. All covered institutions, including card issuers, retailers, and depository institutions (of which there are approximately 19,300) potentially are affected by this collection of information, and thus are respondents for purposes of the PRA.

Comments are invited on: (1) whether the proposed collection of information is necessary for the proper performance of the Federal Reserve's functions; including whether the information has practical utility; (2) the accuracy of the Federal Reserve'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 Michelle Shore, Federal Reserve Board Clearance Officer, Division of Research and Statistics, Mail Stop 151-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 (7100-0200), Washington, DC 20503.

## IX. Redesignation Table

In reviewing the rules affecting open-end credit, The Board has proposed organizational revisions that are designed to make the regulation easier to use. The following table indicates the proposed redesignations.

| **Current** | **Redesignation** |
|---|---|
| Footnote 3 | § 226.2(a)(17)(v) |
| Footnote 4 | Comment 3-1 |
| Comment 3(a)-2 | Comment 3(a)-3 |
| Comment 3(a)-3 | Comment 3(a)-4 |
| Comment 3(a)-4 | Comment 3(a)-5 |
| Comment 3(a)-5 | Comment 3(a)-6 |
| Comment 3(a)-6 | Comment 3(a)-8 |
| Comment 3(a)-7 | Comment 3(a)-9 |
| Comment 3(a)-8 | Comment 3(a)-10 |
| Footnote 5 | § 226.4(d)(2) |
| Footnote 6 | § 226.4(d)(2)(i) |
| Footnote 7 | § 226.5(a)(1)(ii)(A) |
| Footnote 8 | § 226.5(a)(1)(ii)(B) |
| § 226.5(a)(2) | § 226.5(a)(2)(ii) |
| Footnote 9 | § 226.5(a)(2)(ii) |
| § 226.5(a)(3) | § 226.5(a)(3)(i) |
| § 226.5(a)(4) | § 226.5(a)(3)(ii) |
| § 226.5(a)(5) | § 226.5(a)(1)(iii) |
| Comment 5(a)(1)-1 | Comments 5(a)(1)-1 and 5(a)(1)-2 |
| Comment 5(a)(1)-2 | Comment 5(a)(1)-4 |
| Footnote 10 | § 226.5(b)(2)(iii) |
| Comment 5(b)(1)-1 | § 226.5(b)(1)(iv) - (v);<br>Comment 5(b)(1)(i)-1 |
| § 226.5a(a)(2)(i) (prominent location) | § 226.5a(a)(2)(vi) |
| § 226.5a(a)(2)(iii) | § 226.5(a)(2)(iii) |
| § 226.5a(a)(2)(iv) | § 226.5(a)(2)(i) |
| § 226.5a(a)(3) | § 226.5a(a)(5) |
| § 226.5a(a)(4) | § 226.5a(a)(3) |
| § 226.5a(a)(5) | § 226.5a(a)(4) |
| § 226.5a(b)(1)(ii); Comment 5a(c)-1 | § 226.5a(c)(2)(i); § 226.5a(e)(4) |
| § 226.5a(b)(1)(iii) | § 226.5a(c)(2)(ii) |
| § 226.5a(e)(3) | § 226.5a(e)(2) |
| § 226.5a(e)(4) | § 226.5a(e)(3) |
| Comment 5a(a)(2)-2 | Comment 5a(a)(2)-1 |