

FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Regulation Z; Docket No. R-1136]

Truth in Lending

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule; official staff commentary.

SUMMARY: This final rule revises the official staff commentary to Regulation Z, which implements the Truth in Lending Act. The commentary interprets the requirements of Regulation Z. The revisions state the rules for disclosing fees to expedite a payment or delivery of a card. The revisions interpret the rules for replacing an accepted credit card to permit an issuer, under certain conditions, to replace an accepted card with more than one card. The revisions also discuss the treatment of private mortgage insurance payments in disclosing the payment schedule and the selection of Treasury security yields for determining whether a mortgage loan is covered by provisions in Regulation Z that implement the Home Ownership and Equity Protection Act.

DATES: This rule is effective April 1, 2003; the date for mandatory compliance is October 1, 2003.

FOR FURTHER INFORMATION CONTACT: Krista P. DeLargy or Dan S. Sokolov, Attorneys, or Jane E. Ahrens, Senior Counsel, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, at (202) 452-3667 or 452-2412; for users of Telecommunications Device for the Deaf (“TDD”) only, contact (202) 263-4869.

SUPPLEMENTARY INFORMATION:

I. Background

The purpose of the Truth in Lending Act (TILA), 15 U.S.C. 1601 *et seq.*, is to promote the informed use of consumer credit by providing for uniform disclosures about its terms and cost. TILA gives consumers the right to rescind certain transactions that involve a lien on their principal dwelling, and it requires additional disclosures and imposes substantive restrictions on certain home-secured loans with rates or fees above a certain amount. The act also addresses the rights and responsibilities of credit card issuers and cardholders.

TILA is implemented by the Board's Regulation Z (12 CFR part 226). The Board has delegated to officials in the Board's Division of Consumer and Community Affairs authority to issue official staff interpretations of Regulation Z. Good faith compliance with the commentary affords creditors protection from liability under section 130(f) of TILA. The commentary is a substitute for individual staff interpretations; it is updated periodically to address significant questions that arise.

In December 2002, the Board published for comment proposed changes to the commentary (67 FR 72,618, December 6, 2002). The revisions discuss the rules for disclosing fees to expedite a payment or delivery of a card; replacing an accepted credit card; including private mortgage insurance premiums in the payment schedule disclosure; and selecting Treasury security yields for determining whether a mortgage loan is covered by the Home Ownership and Equity Protection Act. The Board received approximately 350 comment letters, most on the inquiry about overdraft or "bounced check" services. About 280 of the comments were from financial institutions, other creditors, and their representatives. The remaining comment letters were from consumer groups, individuals, and one state agency.

With one exception, the final rule is being adopted substantially as proposed; the proposed comment concerning expedited payment fees has not been adopted. In addition, some changes have been made for clarity in response to commenters' suggestions.

In addition to the proposed commentary revisions, the Board's staff requested information on overdraft or "bounced check" protection services. Institutions provide the service in lieu of establishing a traditional overdraft line of credit for the customer. Under these programs, even though the institution generally reserves the right not to pay particular items, a dollar limit is typically established for the account holder and then the institution routinely pays overdrafts on the account up to that amount without a case-by-case assessment. The staff solicited comment and information from the public about how these services are designed and operated, to determine the need for additional guidance to financial institutions under Regulation Z or other laws.

About 300 of the comment letters responded to the request to provide information about the various ways that depository institutions offer bounced check protection services. The comment letters describe programs being offered to depository institutions by a number of vendors. The programs vary from vendor to vendor, and also appear to vary in their implementation from institution to institution. The Board's staff is continuing to gather information on these services, which are not addressed in the final rule.

II. Commentary Revisions

Subpart B^{3/4} Open-End Credit

Section 226.6—Initial Disclosure Statement

6(b) Other Charges

Representatives of the credit card industry requested official guidance on the rules for disclosing two fees charged to consumers in connection with open-end credit plans—a fee imposed when a consumer requests that an individual payment be expedited, and a fee imposed when a consumer requests expedited delivery of a credit card. Because the proper characterization of these fees under TILA previously has been unclear, the staff proposed to revise comment 6(b) to provide guidance.

Under Regulation Z, creditors must disclose fees that are “finance charges,” which are defined as “charges payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit.” For open-end credit plans, fees that are not finance charges but that may be imposed as part of the plan must also be disclosed; these are commonly referred to as “other charges.” The commentary interprets this requirement to apply to “significant charges related to the plan.” Regulation Z does not require disclosure of charges that are not considered either finance charges or “other charges.”

Fee to expedite a payment on a credit or charge card account

Card issuers increasingly have been making expedited payment services available to consumers. The expedited payment service provides consumers an alternative to mailing a payment that might not reach the card issuer by the due date. Typically to avoid being assessed a late fee, consumers request expedited payment service for a lesser charge.

Comment 6(b)-1 provides examples of “other charges” that must be disclosed to consumers under Regulation Z; the list of examples is not exhaustive. A revision to comment 6(b)-1 was proposed indicating that a fee imposed for expediting an individual payment at the consumer’s request should be disclosed as an “other charge.” The proposed comment only covered an expedited payment service where that method of payment was not established in advance as the regular payment method for the account. Under the proposal, changes in the amount of the fee would not trigger a change-in-terms notice.

Generally, consumer groups agreed with the proposal to treat the fee for an expedited payment service as an “other charge” subject to the condition that creditors document consumers’ knowing and voluntary assent to the fee. Otherwise, they believed the fee is a finance charge. They also advocated that the change-in-terms notice requirements apply.

Most industry commenters opposed the proposed comment on expedited payment fees. They asserted that the fee should not be disclosed under TILA as an “other charge” because in their view the payment service is not part of the credit plan and is not significant in its occurrence or in amount. Industry commenters disagreed that the fee resembles a late charge or substitutes for it. They noted that the fee is disclosed to consumers at the time they request the payment service and, therefore, they believe consumers will not benefit materially from disclosure of the fee on account-opening disclosures or on periodic statements under TILA. More generally, industry commenters believe that because there is another reasonable payment option available to the consumer without paying a charge, the expedited payment fee should not be disclosed either as a finance charge or as an “other charge” under TILA. They contend that the creditor’s fee should be considered separate from the credit plan as though it were imposed by a third-party courier or wire transfer service. Some commenters expressed concern about the potential effect of treating an expedited payment fee as part of the credit plan for home-equity lines of credit; they believe the fee should not be considered a term of the plan subject to the rules in § 226.5b that limit unilateral changes.

The proposal was intended to address fees charged to consumers who request an expedited payment service as an alternative to mailing a payment that might not reach the card issuer by the due date. This service typically allows consumers to avoid being assessed a late fee, which typically is higher than the fee imposed for the expedited payment service. The expedited payment service covered by the proposal is not a payment method established in advance as the expected method for making regular payments on the account. Where a card issuer offers an expedited payment service, it is usually available to all account holders; the proposal was not directed to situations where the issuer makes an ad hoc accommodation to satisfy the request of a particular customer. The proposal also was not intended to address electronic payment options that are not offered as an alternative to paying a late fee, or bill-payment services offered in connection with a consumer’s deposit account that might be used to pay credit card bills as well as other bills.

For the reasons discussed in the proposal, expedited payment fees, as currently constructed and described above, are not finance charges under TILA and Regulation Z because the consumer has a reasonable means for making payment on the account without paying a fee to the creditor. As noted above, the act and regulation also require disclosure by the creditor of the amount of any charge other than a finance charge “that may be imposed as part of the plan” 15 U.S.C. 1637(a)(5); 12 CFR 226.6(b). The official staff commentary interprets this requirement to apply to “significant charges related to the plan (that are not finance charges)” and provides examples of charges that are “other charges” under this standard as well as charges that are not “other charges” under this standard. See comments 6(b)-1 and -2.

Based on the record established by the comment letters, the fee for expediting a payment that was described in the proposal does not clearly meet the standard for treatment as an “other charge.” Accordingly, the proposed revision to comment 6(b)-1, classifying the fee as an “other charge,” is not being adopted. In order to provide clear compliance guidance,

comment 6(b)-2 is being revised to indicate that, at this time, creditors are not required to disclose the fee under TILA and Regulation Z. Creditors should continue their current practice of informing consumers of the amount of the charge at the time the service is requested. In addition, when the fee is charged to the credit account, creditors must include the cost on the periodic statement for that billing cycle. See § 226.7(b).

In response to the request for comment on the proper classification of this fee and the fee to expedite delivery of a credit card discussed below, commenters suggested that the Board adopt a general rule for classifying fees under TILA. In their view, the adoption of such a rule would aid creditors' compliance, particularly when determining how new fees should be treated under TILA. There is significant merit in reviewing this area to assess whether general principles can be articulated for determining the appropriate treatment of creditors' fees. Accordingly, in connection with a broader review of Regulation Z, the staff plans to recommend that the Board undertake such an assessment to determine if a general rule can be established consistent with the requirements of TILA. This review would include assessing the treatment of existing fees to determine if a different classification for individual fees is appropriate.

Fees for expediting delivery of a credit or charge card

Comment 6(b)-2 provides examples of charges that are neither finance charges nor "other charges." A revision to comment 6(b)-2 was proposed to add, as an example, a card issuer's fee for expediting delivery of a card upon request, provided the issuer does not charge for delivery by standard mail service. The proposed comment is being adopted substantially as proposed. A minor revision has been made to clarify that the comment also applies when the card is delivered without a fee by a means other than standard mail service that is at least as fast as standard mail service.

Industry commenters uniformly agreed that fees for expedited credit card delivery should not have to be disclosed under TILA as long as the consumer can obtain the card without paying a fee; some of these commenters believe it should be sufficient if the card issuer sends the card without a fee by any "reasonable method." Consumer groups contended that the fee should be disclosed as an "other charge" if the creditor documents consumers' knowing and voluntary assent to the fee, the fee charged for expediting delivery is reasonably related to the actual cost of delivery, and the card is available without a fee by first-class mail or faster. If these conditions are not satisfied, consumer advocates believe the fee should be disclosed as a finance charge.

The final comment reflects the view that a fee for expedited delivery of a credit card is not incidental to the extension of credit and thus is not a finance charge where the consumer requests the service and the card is also available by standard mail service (or another means that is at least as fast) without a fee. In those circumstances, the amount of the voluntary charge for expedited delivery in relation to the creditor's cost is not a factor in determining whether the fee is a finance charge.

In addition, the fee does not appear to be an “other charge” under Regulation Z. An expedited card delivery service does not appear to be significant or related to the credit plan because the service is provided only occasionally, such as when a consumer seeks to replace a lost or stolen credit card and requests expedited delivery. Finally, nothing in the record suggests the need for additional documentation to demonstrate that the consumer’s assent to the service is knowing and voluntary.

Section 226.9—Subsequent Disclosure Requirements

9(c) Change in Terms

A revision to comment 9(c)(2)-1 was proposed to address expedited payment fees consistent with the proposed revision to comment 6(b)-1. Because expedited payment fees are not being classified as “other charges” at this time, the proposed revision to comment 9(c)(2)-1 is unnecessary and is not being adopted.

Section 226.12—Special Credit Card Provisions

12(a) Issuance of Credit Cards

Under the proposal, comment 12(a)(2)-6 would be revised to allow card issuers, subject to certain conditions, to replace an accepted credit card with one or more replacement cards. Most commenters supported the proposed commentary provision with some suggested revisions, as discussed below. The proposal is adopted with revisions.

Section 132 of TILA, 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. 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 card (as that term is defined under Regulation Z). The existing staff commentary does not, however, construe Section 132 as requiring one-for-one replacement in all circumstances. See comment 12(a)(2)-6.

Advances in technology used for information transmittal have enabled card issuers to issue credit cards in different sizes and formats. These new cards may enhance consumer convenience. A merchant’s card reading equipment determines, however, whether a consumer can use a particular credit card with that merchant. For example, some merchants’ equipment and some automated teller machines require insertion of a “full-size” credit card. Certain cards that are reduced in size may require different card readers than those presently used for “full-size” cards. Some card issuers have requested guidance on the issuance of cards using new technologies, which are intended to supplement but not necessarily replace a cardholder’s existing card.

To address these developments, under the proposal, comment 12(a)(2)-6 would be revised to provide additional guidance, consistent with the statute and legislative purpose. The proposed comment indicated that a card issuer may replace an accepted credit card with more than one renewal or substitute card on the same account where: (1) the replacement cards access only the account of the accepted card; (2) all cards issued under the account are governed by the same terms and conditions; and (3) the consumer's total liability for unauthorized use with respect to the account does not increase.

Several industry commenters requested that the first condition be revised to require only that any replacement card access the same "credit plan" as the accepted card. This suggested revision is too broad. For example, some open-end credit plans might include multiple accounts, such as a credit card account and a home equity line of credit (HELOC), where the consumer's credit card does not access the HELOC account. The commenters' suggestion to broaden the comment would permit creditors to replace an accepted card with one that accesses the credit card account and another that accesses the HELOC. Because the consumer did not previously have credit card access to the HELOC, adding such access on an unsolicited basis would be inconsistent with the legislative purposes of Section 132. Accordingly, the final comment provides that the replacement cards should access only the accounts previously accessed by the consumer's accepted card. Minor revisions have been made to this part of the final comment for clarity; no change in meaning is intended.

Some industry commenters requested a clarification in the final rule that a supplemental card need not access all of the features of the consumer's existing card account. Neither the proposal nor the final comment requires that all replacement cards issued access all of the account features of the accepted card.

Commenters also requested a clarification that issuers would not be prevented from issuing multiple replacement cards when there is a substitution due to a change in the card issuer's name or account number, or where there is a successor card issuer. The requirement that supplemental cards must access the same account as the accepted card does not preclude issuers from issuing multiple replacement cards as part of a proper substitution. See, e.g., comments 12(a)(2)-2 and -3.

Some industry commenters opposed the second condition—that all cards issued in connection with a renewal or substitution be subject to the same terms and conditions. Some commenters noted that for safety and soundness reasons, an issuer might limit use of a supplemental access device to low-dollar sales transactions (such as purchases at a vending machine or gas pump); limit the availability of credit on a supplemental card (such as a card for the cardholder's dependent child); or limit use of particular access devices to transactions with merchants that employ special security procedures or agree to special risk-sharing arrangements. Other commenters requested clarification that all credit features accessible with a supplemental card need not be subject to the same terms, for example, a different APR might apply to purchase transactions and cash advances.

As proposed, the final comment provides that where a card issuer replaces an accepted card with more than one renewal or substitute card on an unsolicited basis, all replacement cards must be issued subject to the same terms and conditions. The final comment clarifies that this requirement applies only to terms and conditions that are required to be disclosed under § 226.6 of Regulation Z, except that a creditor may vary terms for which no change-in-terms notice is required under § 226.9(c). For example, a card issuer could issue a supplemental card that has a lower APR, has a lower credit limit, can only be used for small dollar transactions or for a subset of merchants, or is subject to different security procedures than the accepted card. Moreover, the comment does not suggest that all the credit features available with the unsolicited supplemental card must be subject to the same terms; for example, the APRs for purchase transactions and cash advances might differ for the supplemental card to the same extent that these terms differ for the accepted card.

Commenters generally supported the third condition, that the consumer's total liability for unauthorized use of the account must not increase as a result of the creditor's issuance of a supplemental card. That condition is adopted without revision in the final comment.

Several consumer groups advocated adding a condition that either the replacement cards all be mailed in the same envelope to deter identity theft or the consumer be given written notice seven days before the mailing of an additional card. They also recommended requiring other security measures, such as consumer-initiated card activation.

Card issuers typically send cards that are not activated and employ security procedures requiring the consumer to verify receipt of the card, to avoid or limit monetary losses from the theft of credit cards sent through the mail. These measures have become increasingly common and are used on a substantial portion of cards now issued. It is expected that industry will continue these practices, which should be as effective when replacing an accepted card with one or more renewal or substitute cards.

Comment was also solicited on whether it would be appropriate to allow the unsolicited issuance of supplemental cards for an existing account on the conditions specified above even when there is no renewal of or substitution for the cardholder's existing card. Industry commenters stated that allowing additional cards to be sent outside of renewal or substitution would reduce card issuers' costs by eliminating the need to produce and distribute unnecessary replacement cards. They also noted that the issuance of supplemental cards alone (as opposed to issuance in connection with a renewal or substitution) would not result in increased risk of liability for unauthorized use of the cards. Consumer advocates opposed the unsolicited issuance of more than one card on an existing account (when there is no renewal or substitution) unless consumers are notified by mail seven days before an additional card is sent and security measures such as consumer-initiated card activation are required, to protect against any added risk of theft and unauthorized use.

Based on the comments received, staff plans to recommend that the Board consider amending § 226.12(a) to allow the unsolicited issuance of additional cards on an existing

account outside of renewal or substitution under certain conditions. Also, consideration may be given to whether changes to Regulation E's restrictions on the unsolicited issuance of additional debit cards on a consumer's existing asset account are warranted.

Subpart C³/₄ Closed-End Credit

Section 226.18³/₄ Content of Disclosures

18(g) Payment Schedule

The disclosures for closed-end loans must include the number, amounts, and timing of payments scheduled to repay the obligation. Premiums paid for insurance that protects the creditor against the consumer's default or other credit loss (sometimes referred to as private mortgage insurance) are finance charges that must be included in the payment schedule. The payment schedule should reflect the fact that, under the Homeowners Protection Act of 1998 (HPA), such insurance generally must terminate before the term of the loan expires.

With some revisions for clarity, changes to comment 18(g)-5 are adopted as proposed to provide additional guidance on how mortgage insurance premiums should be disclosed on the payment schedule when some premiums are collected and escrowed at the time the loan is closed. Creditors are required to disclose a payment schedule based on the borrower's legal obligation. The comment provides an example to facilitate compliance.

Commenters generally supported the proposal. Several commenters noted that the loan documents might be silent on how the termination of insurance premiums will be implemented under the HPA. TILA disclosures must be based on the legal obligation, which is determined by applicable state or other law, and not solely by the parties' written agreement. See comment 17(c)(1)-1. Comment 18(g)-5 has been revised to reflect this guidance.

Two commenters sought clarification that the rules for disclosing mortgage insurance premiums under TILA would not affect the rules for escrow accounts under the Real Estate Settlement Procedures Act (RESPA). The text of the final comment has been modified to allay those concerns; the comment in no way affects creditors' compliance with RESPA's aggregate escrow accounting rules.

Section 226.19³/₄ Certain Residential Mortgage Transactions

19(b) Certain Variable-Rate Transactions

A technical amendment to comment 19(b)(1)-2 is adopted, as proposed, to change the citation to comment 19(b)-5, as amended (65 FR 17129, March 31, 2000). No substantive change is intended.

Subpart E^{3/4} Special Rules for Certain Home Mortgage Transactions

Section 226.32—Requirements for Certain Closed-End Home Mortgages

32(a) Coverage

Section 226.32 implements the Home Ownership and Equity Protection Act of 1994 (HOEPA), which is part of the Truth in Lending Act. HOEPA requires additional disclosures and provides substantive protections for certain home-secured loans carrying rates or fees above specified triggers. HOEPA covers mortgage loans for which the annual percentage rate (APR) exceeds the yield on Treasury securities with a comparable maturity by a specified number of percentage points (8 for first-lien loans, 10 for subordinate-lien loans). The APR is compared with the yield on Treasury securities as of the 15th day of the month immediately preceding the month of application.

Revisions to comment 32(a)(1)(i)-4 were proposed to clarify how creditors should determine the applicable yield on Treasury securities. The proposal provided that creditors should not use results of Treasury auctions. Instead, creditors should use yields on actively traded issues adjusted to constant maturities that are listed on the Board's "Selected Interest Rates" (statistical release H-15). The H-15 is published daily and is posted on the Board's Internet website at www.federalreserve.gov/releases/h15.

The proposed comment also clarified that for purposes of HOEPA's rate-based trigger, creditors should compare the APR on 30-year loans (and other loans of 20 or more years) with the yield reported on the H-15 for a 20-year constant maturity. The Department of the Treasury recently ceased auctioning 30-year securities. Creditors asked for additional guidance since the H-15 lists a 20-year constant maturity and a long-term average of the yields for Treasury securities with terms to maturity of 25 or more years, and refers to a Treasury formula for estimating a 30-year yield.

Commenters generally supported the proposed revisions as enhancing uniformity and easing compliance. However, several credit unions that commented preferred having flexibility to use any figure on the H-15 comparable to a loan's maturity, including the Treasury formula for estimating a 30-year yield. Other commenters, while concurring with the guidance to use 20-year constant maturities to calculate the APR trigger for 30-year loans, encouraged the Board to explore alternatives and make further revisions to the commentary if more suitable alternatives become available. One commenter requested guidance on the effect of an irregular first payment period on the loan's maturity.

The comment has been adopted substantially as proposed, with a minor revision for clarification. Requiring that all creditors use the yields on the H-15 for Treasury constant maturities should ensure uniform application of HOEPA. The final comment clarifies that for purposes of determining a loan's maturity under HOEPA's rate-based trigger, creditors may rely on the rules in § 226.17(c)(4). Under the rule, creditors may ignore the effect of first payment periods that are slightly longer or shorter than other scheduled payment periods.

List of Subjects in 12 CFR Part 226

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

Text of Revisions

Comments are numbered to comply with Federal Register publication rules. For the reasons set forth in the preamble, the Board amends 12 CFR part 226 as follows:

PART 226 -- TRUTH IN LENDING (REGULATION Z)

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

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

2. In Supplement I to Part 226:

- a. Under Section 226.6—Initial Disclosure Statement, under 6(b) Other charges, paragraph 2. is revised.

- b. Under Section 226.12—Special Credit Card Provisions, under Paragraph 12(a)(2), paragraph 6. is revised.

- c. Under Section 226.18—Content of Disclosures, under 18(g) Payment schedule, paragraph 5. is revised.

- d. Under Section 226.19—Certain Residential Mortgage and Variable-Rate Transactions, under Paragraph 19(b)(1), paragraph 2. is amended by removing “comment 19(b)-4” and adding “comment 19(b)-5” in its place.

- e. Under Section 226.32—Requirements for Certain Closed-End Home Mortgages, under Paragraph 32(a)(1)(i), paragraph 4. is revised.

SUPPLEMENT I TO PART 226—OFFICIAL STAFF INTERPRETATIONS

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SUBPART B—OPEN-END CREDIT

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Section 226.6—Initial Disclosure Statement

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6(b) Other charges.

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2. Exclusions. The following are examples of charges that are not “other charges”:
- i. Fees charged for documentary evidence of transactions for income tax purposes.
 - ii. Amounts payable by a consumer for collection activity after default; attorney's fees, whether or not automatically imposed; foreclosure costs; post-judgment interest rates imposed by law; and reinstatement or reissuance fees.
 - iii. Premiums for voluntary credit life or disability insurance, or for property insurance, that are not part of the finance charge.
 - iv. Application fees under § 226.4(c)(1).
 - v. A monthly service charge for a checking account with overdraft protection that is applied to all checking accounts, whether or not a credit feature is attached.
 - vi. Charges for submitting as payment a check that is later returned unpaid (see commentary to § 226.4(c)(2)).
 - vii. Charges imposed on a cardholder by an institution other than the card issuer for the use of the other institution's ATM in a shared or interchange system. (See also comment 7(b)-2.)
 - viii. Taxes and filing or notary fees excluded from the finance charge under § 226.4(e).
 - ix. A fee to expedite delivery of a credit card, either at account opening or during the life of the account, provided delivery of the card is also available by standard mail service (or other means at least as fast) without paying a fee for delivery.
 - x. A fee charged for arranging a single payment on the credit account, upon the consumer's request (regardless of how frequently the consumer requests the service), if the

credit plan provides that the consumer may make payments on the account by another reasonable means, such as by standard mail service, without paying a fee to the creditor.

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Section 226.12—Special Credit Card Provisions

12(a) Issuance of credit cards.

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Paragraph 12(a)(2)

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6. One-for-one rule—exceptions. The regulation does not prohibit the card issuer from:

i. Replacing a debit/credit card with a credit card and another card with only debit functions (or debit functions plus an associated overdraft capability), since the latter card could be issued on an unsolicited basis under Regulation E.

ii. Replacing an accepted card with more than one renewal or substitute card, provided that:

A. No replacement card accesses any account not accessed by the accepted card;

B. For terms and conditions required to be disclosed under § 226.6, all replacement cards are issued subject to the same terms and conditions, except that a creditor may vary terms for which no change in terms notice is required under § 226.9(c); and

C. Under the account's terms the consumer's total liability for unauthorized use with respect to the account does not increase.

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SUBPART C—CLOSED-END CREDIT

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Section 226.18—Content of Disclosures

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18(g) Payment schedule.

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5. Mortgage insurance. The payment schedule should reflect the consumer's mortgage insurance payments until the date on which the creditor must automatically terminate coverage under applicable law, even though the consumer may have a right to request that the insurance be cancelled earlier. The payment schedule must reflect the legal obligation, as determined by applicable state or other law. For example, assume that under applicable law, mortgage

insurance must terminate after the 130th scheduled monthly payment, and the creditor collects at closing and places in escrow two months of premiums. If, under the legal obligation, the creditor will include mortgage insurance premiums in 130 payments and refund the escrowed payments when the insurance is terminated, the payment schedule should reflect 130 premium payments. If, under the legal obligation, the creditor will apply the amount escrowed to the two final insurance payments, the payment schedule should reflect 128 monthly premium payments. (For assumptions in calculating a payment schedule that includes mortgage insurance that must be automatically terminated, see comments 17(c)(1)-8 and 17(c)(1)-10.)

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SUBPART E—SPECIAL RULES FOR CERTAIN HOME MORTGAGE TRANSACTIONS

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Section 226.32—Requirements for Certain Closed-End Home Mortgages

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32(a) Coverage

Paragraph 32(a)(1)(i)

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4. Treasury securities. To determine the yield on comparable Treasury securities for the annual percentage rate test, creditors may use the yield on actively traded issues adjusted to constant maturities published in the Board's "Selected Interest Rates" (statistical release H-15). Creditors must use the yield corresponding to the constant maturity that is closest to the loan's maturity. If the loan's maturity is exactly halfway between security maturities, the annual percentage rate on the loan should be compared with the yield for Treasury securities having the lower yield. In determining the loan's maturity, creditors may rely on the rules in § 226.17(c)(4) regarding irregular first payment periods. For example:

i. If the H-15 contains a yield for Treasury securities with constant maturities of 7 years and 10 years and no maturity in between, the annual percentage rate for an 8-year mortgage loan is compared with the yield of securities having a 7-year maturity, and the annual percentage rate for a 9-year mortgage loan is compared with the yield of securities having a 10-year maturity.

ii. If a mortgage loan has a term of 15 years, and the H-15 contains a yield of 5.21 percent for constant maturities of 10 years, and also contains a yield of 6.33 percent for constant maturities of 20 years, then the creditor compares the annual percentage rate for a 15-year mortgage loan with the yield for constant maturities of 10 years.

iii. If a mortgage loan has a term of 30 years, and the H-15 does not contain a yield for 30-year constant maturities, but contains a yield for 20-year constant maturities, and an average

yield for securities with remaining terms to maturity of 25 years and over, then the annual percentage rate on the loan is compared with the yield for 20-year constant maturities.

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By order of the Board of Governors of the Federal Reserve System, acting through the Director of the Division of Consumer and Community Affairs under delegated authority, March 28, 2003.

Robert deV. Frierson (signed)

Robert deV. Frierson,

Deputy Secretary of the Board.

BILLING CODE 6210-01-P