

vehicle loans, these agreements, sometimes referred to as "gap" agreements, offer protection to consumers if the vehicle is stolen or destroyed and the motor vehicle insurance proceeds are insufficient to extinguish the debt. In return for a fee, the consumer will not be held liable for the remaining balance due on the loan. Other types of agreements provide for debt cancellation if the borrower dies or becomes disabled. In some states these agreements are regulated as or otherwise considered insurance under state law.

i. *Insurance.* If the agreement is regulated as or considered insurance under state law, the fee paid by the consumer may be excludable from the finance charge if it meets the requirements in § 226.4(d). Insurance protecting the creditor against credit loss, however, is a finance charge under § 226.4(b)(5).

ii. *Other.* If the agreement is not considered insurance under state law, debt cancellation fees paid to the creditor, whether required or optional, are incident to the extension of credit and must be disclosed as a finance charge. An optional debt cancellation fee paid to a third-party is a finance charge only to the extent that the third-party shares the fee with the creditor. If a creditor cannot determine whether state law considers the agreement insurance, the fees must be treated as if the agreement is not insurance. fi

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*Paragraph 4(d).*

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5. *Required credit life insurance.* Credit life, accident, health, or loss-of-income insurance must be voluntary in order for the premium or charges to be excluded from the finance charge. Whether the insurance is in fact required or optional is a factual question. If the insurance is required, the premiums must be included in the finance charge, whether the insurance is purchased from the creditor or from a third party. If the fi consumer is required to elect one of several options—such as fi [only option the creditor gives the consumer is] to purchase credit life insurance from the creditor fi [or to] assign an existing life insurance policy, fi or pledge security such as a certificate of deposit, fi and the consumer purchases the credit life insurance, the premium must be included in the finance charge. (If the consumer assigns a preexisting policy instead, no premium is included in the finance charge. fi The security interest would be disclosed under § 226.6(c) or § 226.18(m). fi See the commentary to § 226.4(b) (7) and (8).)

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3. In supplement I to part 226, under *section 226.6—Initial Disclosure Statement, under 6(b) Other charges.*, paragraph 1.v. would be revised to read as follows:

\* \* \* \* \*

*Subpart B—Open-End Credit*

\* \* \* \* \*

*Section 226.6—Initial Disclosure Statement*

\* \* \* \* \*

*6(b) Other charges.*

1. \* \* \*

v. A membership or participation fee for a package of services that includes an open-end credit feature, unless the fee is required whether or not the open-end credit feature is included. For example, a membership fee to join a credit union is not an "other charge," even if membership is required to apply for credit. fi For the fee to be excluded from disclosure as an "other charge," however, the package of services must have some substantive purpose other than access to the credit feature. For example, if the primary benefit of membership in an organization is the opportunity to apply for a credit card, and the other benefits offered are incidental to the credit feature, the membership fee is an "other charge." fi

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4. In supplement I to part 226, under *Section 226.12—Special Credit Card Provisions, under 12(c)(2) Adverse credit reports prohibited.*, new paragraph 2. would be added to read as follows:

\* \* \* \* \*

*Section 226.12—Special Credit Card Provisions*

\* \* \* \* \*

*12(c)(2) Adverse credit reports prohibited.*

\* \* \* \* \*

fi 2. *Settlement of dispute.* A card issuer may not consider a dispute settled and report an amount disputed as delinquent or begin collection of the disputed amount until it has completed a reasonable investigation of the cardholder's claim. In conducting an investigation, the card issuer may reasonably request the cardholder's cooperation. The card issuer may not automatically consider a dispute settled due to the cardholder's failure or refusal to comply with a particular request. fi

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5. In supplement I to Part 226, under *Section 226.14—Determination of Annual Percentage Rate, under 14(c) Annual percentage rate for periodic statements.*, a new paragraph 10. would be added to read as follows:

\* \* \* \* \*

*Section 226.14—Determination of Annual Percentage Rate*

\* \* \* \* \*

*14(c) Annual percentage rate for periodic statements.*

\* \* \* \* \*

fi 10. *Transactions at end of billing cycle.* The annual percentage rate reflects transactions and charges imposed during the billing cycle. However, a transaction that occurs at the end of a billing cycle may be impracticable to post until the following cycle, such as a cash advance that occurs on the last day of a billing cycle. The transaction is posted to the account in the following cycle. In this case, the annual percentage rate shall be calculated as follows for the billing cycle in which the transaction and charges are posted:

i. The denominator shall be calculated as if the transaction occurred on the first day of the billing cycle, and

ii. The numerator shall include the amount of the transaction charge plus all finance charges derived from the application of the periodic rate to the amount of the transaction (including all charges from a prior cycle). fi

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6. In Supplement I to Part 226, under *Section 226.17—General Disclosure Requirements, under Paragraph 17(c)(1).*, paragraph 10. would be revised and a new paragraph 18. would be added to read as follows:

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*Subpart C—Closed-End Credit*

*Section 226.17—General Disclosure Requirements*

\* \* \* \* \*

*17(c) Basis of disclosures and use of estimates.*

*Paragraph 17(c)(1).*

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10. *Discounted and premium variable-rate transactions.* In some variable-rate transactions, creditors may set an initial interest rate that is not determined by the index or formula used to make later interest rate adjustments. Typically, this initial rate charged to consumers is lower than the rate would be if it were calculated using the index or formula. However, in some cases the initial rate may be higher. In a discounted transaction, for example, a creditor may calculate interest rates according to a formula using the six-month Treasury bill rate plus a 2 percent margin. If the Treasury bill rate at consummation is 10 percent, the creditor may forgo the 2 percent spread and charge only 10 percent for a limited time, instead of setting an initial rate of 12 percent.

fi i. fi When creditors use an initial interest rate that is not calculated using the index or formula for later rate adjustments, the disclosures should reflect a composite annual percentage rate based on the initial rate for as long as it is charged and, for the remainder of the term, the rate that would have been applied using the index or formula at the time of consummation. The rate at consummation need not be used if a contract provides for a delay in the implementation of changes in an index value. For example, if the contract specifies that rate changes are based on the index value in effect 45 days before the change date, creditors may use fi any fi [the] index value in effect fi during the 45 day period fi [not more than 45 days] before consummation in calculating a composite annual percentage rate.

fi ii. fi The effect of the multiple rates must also be reflected in the calculation and disclosure of the finance charge, total of payments, and payment schedule.

fi iii. fi If a loan contains a rate or payment cap that would prevent the initial rate or payment, at the time of the first adjustment, from changing to the rate determined by the index or formula at consummation, the effect of that rate or payment cap should be reflected in the disclosures.

fi iv. fi Because these transactions involve irregular payment amounts, an annual