July 12, 1991

Dennis Flickinger,
President
First Capital Credit Union
1720 Loucks Road
York, Pennsylvania 17404

Re: Regulation Z (Your June 14, 1991 Letter)

Dear Mr. Flickinger:

You asked whether Regulation Z, 12 C.F.R. Part 226, would prohibit First Capital Credit Union ("First Capital") from extending the initial payment period on its loans from the current 30 days to 45 days. Regulation Z governs only lend- ing disclosure requirements, as opposed to loan terms, and therefore does not preclude the proposed change in the ini- tial payment period. However, Regulation Z would affect First Capital's disclosure options, if First Capital chooses to make the proposed change.

Subpart C of Regulation Z, 12 C.F.R. Section 226.16-226.24, sets forth disclosure requirements for closed-end credit transactions. Section 226.17(c)(4) describes certain circum- stances under which a creditor may disregard irregularities in a loan's initial payment period for purposes of making the calculations and disclosures (such as payment schedules, fi- nance charges and annual percentage rates) required by Regulation Z. You state, "As we interpret Regulation Z, Sec- tion 226.17(c)(4), . . . only those loans with a monthly pay- ment period would be allowed to extend the initial payment out to 45 days (assumes loan of 1 to 10 years.) Ap- proximately 70% of our loans are paid weekly, bi-weekly, or semi-monthly; therefore, the longest we can extend them is 28, 35 and 36 days respectively (regular period plus 21 days)."

Section 226.17(c)(4)(ii) governs transactions with terms of 1 to 10 years. That section provides:

In making calculations and disclosures, the creditor may disregard any irregular- ity in the first period that falls within the limits described below and any payment schedule irregularity that re- sults from the irregular first period: . . . For transactions in which the term is at least one year and less than ten years, a first period not more than 11 days shorter or 21 days longer than a regular period . . . . (emphasis sup- plied)

You correctly reason that, for purposes of Section 226.17(c)(4)(ii), the only loans on which the initial payment period could be extended to 45 days are those on which the loan contract calls for monthly payments. The regular pay- ment periods on the other loans that First Capital currently makes are too short to be extended to 45 days.

However, compliance with Section 226.17(c)(4) is not required in order for a creditor to make a loan. Noncompliance merely affects the creditor's disclosure duties. Whereas a creditor who permissibly shortens or extends the initial payment pe- riod may disregard the resulting irregularities when making its calculations and disclosures, a creditor who alters the initial payment period beyond the allowable limits must take the variation in payment periods into account in its calcula- tions and disclosures. The choice is left to the creditor.

Under Regulation Z, First Capital is free to extend the ini- tial payment period on any of its loans to 45 days, as long as it complies with the relevant disclosure requirements. If First Capital wishes to ignore the irregular initial payment period as permitted in Section 226.17(c)(4), then only those loans with monthly payments may have initial payment periods of 45 days. The initial payment periods on the other loans may be altered as described in your letter.

While First Capital's proposal does not violate Regulation Z. we caution you that state law may have some bearing on this issue. We suggest that you contact local counsel for an opinion based on Pennsylvania law.

Sincerely,

James J. Engel
Deputy General Counsel

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