

"Misrepresentations of the cost of credit" by banks "concerned" the Council too. It pointed out the Federal Trade Commission ruled some ads "a deceptive trade practice," but "commercial banks are exempt from FTC jurisdiction, leaving an inconsistency" in Federal law.

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HOW MUCH YOUR MORTGAGE REALLY COSTS—THESE TABLES SHOW WHAT RATE YOU ACTUALLY PAY WHEN YOU'RE CHARGED INTEREST PLUS "POINTS"

In times of scarce or "tight" money, a person who wants to buy or sell a house may find himself required to pay the money lender a commission, commonly known as a "discount" or as "points." A point is a one-time charge equal to 1% of the loan and, in most places, is considered a perfectly legal way for a lending institution to boost its return without violating the legal ceiling on interest rates. Points may be charged to the buyer, the seller or to both.

When a *borrower* pays points, the money is, in effect, deducted from the total amount of the loan he is seeking. Thus, for example, if he is paying four points on a \$20,000 loan, he actually gets only \$19,200 ($\$20,000 \times .04\% = \800) but has to pay interest on the full \$20,000. The result of this is to raise the "effective" interest rate—the real rate the lender is earning on the amount he loaned—well above the rate stated in the loan contract. And if the borrower pays off his loan sooner than expected, the impact of paying points is even more pronounced.

The tables on the next page were prepared for *Changing Times* by Carleton Financial Computations, Inc., of South Bend, Ind. If you are comparison shopping for a mortgage loan, you can use them to help decide which of two lenders to do business with if both are charging points or if one is and the other is not.

Let's say, for example, Bank A agrees to a 20-year loan. For this, it will charge $6\frac{1}{4}\%$ interest—but no points.

Bank B offers a similar deal for only 6% interest. But it requires that you pay four points before it will approve the loan.

Which is the better deal?

Look at the table calculated on the basis of 6% interest rate payable over 20 years. You'll see that Bank B's "nominal" 6% interest rate goes up to an effective rate of 6.51%—slightly more than $6\frac{1}{2}\%$ —if you pay four points. And if you sell the house in five years, the effective rate will have been even higher—7.02%.

All else being equal, in this case you'd obviously do better with Bank A, even though its nominal rate is higher than Bank B's. (The difference in rates has no effect on tax-deductible interest, by the way. You still deduct only the dollars you pay in interest each month—points are not deductible.)

The tables can also be used to satisfy curiosity. Let's assume, again, that you are the buyer and are being charged four points by Bank B. You learn from the person who is selling the house that the bank is also charging him points, let's say five. What is the bank's rate of return all told?

If you add your points to his points, the grand total is nine points, so that Bank B is really earning a yield of more than 7% (7.20%) on the deal.