May 3, 2023

The Hon. Rohit Chopra
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Re: Credit Card Penalty Fees (Regulation Z), CFPB-2023-0010

Dear Director Chopra,

The American Financial Services Association (AFSA)[1] welcomes the opportunity to provide information regarding several aspects of the Consumer Financial Protection Bureau's (CFPB) proposed rule amending Regulation Z by adjusting the fee charges for late payment on a credit card account.[2] The proposal, which radically reduces the safe harbor dollar amount for late fees to $8, (i) mischaracterizes the use of late fees, (ii) would have a negative effect on consumers and the market, (iii) ignores consumer protections already in place, and (iv) violates rulemaking requirements. The CFPB must not proceed with this rulemaking.

I. Mischaracterization of Late Fees

The proposed rule mischaracterizes late fees as a profit maker, referencing "revenue," on average three times every five pages. Contrary to the CFPB's statements, late fees are critical in managing credit risk and maintaining a safe and sound credit system. Late fees are designed to weigh several factors outlined in Section 149(c) of the Credit Card Accountability Responsibility and Disclosure Act of 2009 (CARD Act), specifically to (i) recover the costs incurred by the issuer "from such omission or violation;" (ii) the deterrence of such omission or violation by the cardholder; and (iii) the conduct of the cardholder.

In the proposed rule, the CFPB is arbitrarily seeking to rewrite the CARD Act to narrow the purpose of late fees to simply recouping costs associated with pre-charge off collections. Aside from the fact that such an interpretation is at direct odds with the language of the statute, it ignores the larger purpose and scope of late fees. Focusing on a narrow view of late fees as revenue ignores the full costs to banks associated with late payments, the costs to consumers from late payments,

[1]Founded in 1916, AFSA is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members provide consumers with many kinds of credit, including traditional installment loans, mortgages, direct and indirect vehicle financing, payment cards, and retail sales finance.
[2] Credit Card Penalty Fees (Regulation Z), 12 CFR Part 1026, https://files.consumerfinance.gov/f/documents/cfpb_credit-card-penalty-fees-nprm_2023-01.pdf ("Credit Card Penalty Fees Proposal")

and the larger impact late payments have on the credit ecosystem. Moreover, the Bureau ignores the fact that late fees are used to cover the significant costs of notifying customers of delinquency, processing late payments, and incurring the opportunity cost of the lost use of the delinquent payment.

Issuers must staff a call center and may have to contact the customer more than once to either get the customer back on track or to collect the debt before the account is charged off – both of which benefit the customer. Call center employees must be well-compensated, increasing the overhead that companies pay as they make attempts to reach their customers. Additionally, financial institutions have costs associated with mailings, technologies to send alerts, compliance lawyers, and other professionals to consider. If a debt goes to a collection agency, that agency will charge, at a minimum, 25% of the total amount of the debt collected. That fee may go up as high as 40%. Additionally, delinquent amounts are not always collected. Late fees help defray the cost of extraordinary collection efforts made to help customers avoid the costs and implications of becoming further delinquent, as well as potentially mitigate inevitable losses associated with riskier borrowers.

II. Negative Individual and Market-wide Effects of the Proposed Rule

What the CFPB also fails to adequately address in the proposed rule, or to have adequately researched in advance of the proposed rule, is any quantification of the deterrent effect on consumer behavior. Absent such research and an understanding of the effect that such a severe reduction of late fees could precipitate, the CFPB should not move forward with this rulemaking. Research would likely show there will be a contraction of availability of credit for American consumers on both an individual and a market wide level.

On the individual level, the proposed rule is likely to promote moral hazard. According to the CFPB, "moral hazard" is defined as "the idea that you are less likely to be careful when you are shielded from the consequences of your actions." The proposed rule decreases the incentive for consumers to make timely payments by making the immediate cost of not paying on time negligible in the short term. If a consumer feels that there is minimal penalty for being late, they are more likely to skip a payment due, which may lead to longer term consequences such as an increase in accrued finance charges on existing credit and a decrease in credit score - consequences which are less immediate and likely less to be understood by consumers. A future reduction in a credit score can make future credit much more expensive if future credit can be accessed at all.

On a market-wide level, some issuers could be exposed to increased risk. Some issuers finance receivable balances by issuing debt themselves. When a consumer pays late, the issuer can incur

919 18th Street NW, Washington, DC, 20006 202.296.5544 www.afsaonline.org @AFSA_DC

unanticipated additional interest expense on that balance. During the underwriting process for a new consumer, an issuer cannot determine with complete certainty whether the consumer may become chronically delinquent, occasionally delinquent, or always current. After a consumer uses their card, their subsequent behavior determines if they are riskier than average for the cohort. The late fee is an automatic "stabilizer" that adjusts pricing for riskier consumers based on their actual post-account opening behavior (*i.e.*, a form of implicit risk-based pricing). Without this stabilizer, a credit card company may need to raise the price of credit to all consumers to cover the additional, unacceptable risk. Less risky consumers would unfairly subsidize riskier consumers in a more uniform pricing system. A recent report from the Center for Capital Market Competitiveness (CCMC)[3] shows that customers are better off in the risk-based pricing system than in a uniform pricing system. In fact, customers, over time, will pay less in this pricing system than in a uniform pricing system.

The CFPB expressly acknowledges this adverse effect, noting that "[c]ardholders who never pay late will not benefit from the reduction in late fees and could pay more for their account if maintenance fees in their market segment rise in response– or if interest rates increase in response and these on-time cardholders also carry a balance."[4] This increase in cost would affect how many consumers will be able to access credit. There would likely be less credit extended. The proposed rule also penalizes those who have been responsible and have stretched to make on-time payments every month in favor of those who are not exhibiting prudent behavior.

III. Existing Consumer Protection Practices and Regulations

The proposed rule ignores (i) the actions issuers take to ensure on time payments and (ii) the assistance measures they provide to help consumers avoid fees or take advantage of alternate repayment options. Often when a customer faces hardship, they call their credit card company and frequently have their late fees waived or receive offers to participate in hardship programs to help them manage their payments. Many members also offer features such as payment reminders (via email, text push notification) and autopay that help customers keep their accounts current.

Previous legislation has already enhanced consumer protection. The CARD Act has had a significant impact in limiting credit card fees. This bipartisan legislation was signed into law by former President Obama, and, until recently, has received praise from the CFPB and both sides of the aisle. In fact, the CFPB's own recent report on the credit card market noted that, "CARD Act pricing restrictions have resulted in a substantial decline in overall fee costs to consumers since the pre-CARD Act period."[5] Regulation Z also requires issuers to provide extensive disclosures at

[3] The Economic Benefits of Risk-Based Pricing for Historically Underserved Consumers in the United States. Nam D. Pham, Ph.D and Mary Donovon, Spring 2021.

[4] Credit Card Penalty Fees Proposal, 88 Fed. Reg. at 18,934.

[5] 2021 Consumer Credit Card Market Report, at 52 n. 94, https://files.consumerfinance.gov/f/documents/cfpb_consumer-credit-card-market-report_2021.pdf

the time of account opening and, on each statement, including disclosures specific to late payment fees.[6] The CFPB has not sufficiently demonstrated that additional regulation is needed.

Some aspects of the proposed rule actually contradict the Truth in Lending Act (TILA). The additional, 15-day "courtesy period" under consideration in this proposed rule impermissibly conflicts with TILA's provisions that permit card issuers to treat payments not received by the due date as late immediately if the consumer is sent a periodic statement at least 21 days before the payment is due. Under Section 163 of TILA,[7] a creditor can "treat a payment on a credit card account under an open end consumer credit plan as late for any purpose" so long as "the creditor has adopted reasonable procedures designed to ensure that each periodic statement including the [statement disclosures required pursuant to 15 U.S.C. § 1637(b)] is mailed or delivered to the consumer not later than 21 days before the payment due date." Notably, Section 127(b)(12) of TILA[8] requires "[in] the case of a credit card account…under which a late fee or charge may be imposed due to the failure of the obligor to make payment on or before the due date for such payment" must include "in a conspicuous location on the billing statement, the date on which the payment is due." A final rule cannot contradict TILA.

The proposed rule now seeks to unilaterally and arbitrarily redefine when a payment is late in a way that is inconsistent with the plain and well understood meaning of late payment, Congressional intent, and contract law. In addition to the "courtesy period" violating long-standing law, it would also create customer confusion and poor financial habits. Consumers would likely be confused about when their payment was actually due, why interest is still occurring, and why they are being charged a late fee in a subsequent month's statement. This courtesy period would also alter the credit risk and funding structure by elongating the period of repayment by 15 days, which would have broad credit risk ramifications.

IV. Violation of Rulemaking Requirements

The CFPB has violated or skirted several rulemaking and regulatory requirements during this process, and so the rulemaking should not proceed.

1. **Administrative Procedure Act (APA) and Due Process Clause Violation:** Directives from the White House and CFPB statements made with this proposed rule's release are strong evidence that this proposed rule was not developed by an open-minded decisionmaker, as required by the APA and the due process clause. Less than a week into the comment period, the President placed enormous pressure on the CFPB by essentially directing them to finalize this rule without change and without taking into account the

[6] 12 C.F.R. 1026.6(b)(2)(viii).
[7] 15 U.S.C. § 1666b.
[8] 15 U.S.C. § 1637(b)(12)(A).

919 18th Street NW, Washington, DC, 20006 ▲ 202.296.5544 ▲ www.afsaonline.org ▲ @AFSA_DC

public's input gathered through the comment period. In his State of the Union Address, the President shared with the American people that "[we are] cutting credit card late fees by 75 percent, from $30 to $8." The CFPB's ability to weigh the public's comments on their late fee proposed rule and revise the proposed $8 safe harbor upwards has been compromised. The CFPB cannot decide to revise the rule to reflect the public's input without also deciding to revise a promise the President of the United States made to the American people in his State of the Union Address. Concurrent with the release of this proposed rule, Director Chopra also revealed the lack of an open mind when he described the Federal Reserve Board's existing safe harbor as a "regulatory loophole that has allowed [companies] to escape scrutiny for charging an otherwise illegal junk fee."[9]

2. **Dodd-Frank Violation:** The proposed rule acknowledges that it lacks research and data regarding potential secondary impacts of its proposed rule, including higher costs and reduced access to credit for consumers, effectively violating the CFPB's mandate in Section 1021 of Dodd-Frank to ensure that "all consumers have access to markets for consumer financial products."

3. **CARD Act Violation:** The proposed rule fails to comply with the express language in Section 149(a) of the CARD Act[10] by tying the amount of the late fee solely to costs. The CFPB routinely misstates the CARD Act as requiring the late fee be reasonable and proportional to the costs incurred by issuers. As an example, the CFPB's press release on this proposed rule said the changes would "ensure that late fees meet the [CARD] Act's requirement to be 'reasonable and proportional to the costs' incurred by issuers to handle late payments."[11] The CARD Act *actually* states that the fee be reasonable and proportional to the omission or violation.[12] To read "such omission or violation" as equaling costs alone is inconsistent with a plain reading of the statute, since Congress would have used different language if it wanted to focus on costs alone, which it has done in other statutes. Congress clearly intended late fees to encapsulate more than just the cost associated with the late payment given its express language in the CARD Act

---

[9] Press Release, Consumer Financial Protection Bureau, "CFPB Proposes Rule to Rein in Excessive Credit Card Late Fees" (Feb. 1, 2023) https://www.consumerfinance.gov/about-us/newsroom/cfpb-proposes-rule-to-rein-in-excessive-credit-card-late-fees/

[10] 15 U.S.C. § 1665d(c).

[11] CFPB Proposes Rule to Rein in Excessive Credit Card Late Fees (Feb. 1, 2023). Available at: https://www.consumerfinance.gov/about-us/newsroom/cfpb-proposes-rule-to-rein-in-excessive-credit-card-late-fees/.

[12] 15 U.S.C. § 1665d(a).

The proposed rule fails to comply with the requirements set forth in Section 149(c) of the CARD Act[13] by failing to appropriately consider:

1. The costs incurred by the creditor from such omission or violation - The CFPB seeks to narrow the scope of costs to only those associated with direct collection efforts pre-charge off. There is no basis within the CARD Act for such a narrow view, and such a view fails to appropriately quantify/include the actual costs associated with late payments.

2. The deterrence of such omission or violation by the cardholder - The CFPB acknowledges that its proposed rule may actually result in more consumers paying late and embraces that possibility in order to give consumers more choice about which bills to pay on time, which is a complete abdication of any deterrent effect in the rule. By contrast, the rule establishing the existing safe harbor has been in place for over 12 years and was deliberately set to provide a deterrent effect. The CFPB has failed to study and chosen to ignore the deterrent effects in this proposed rule.

3. The conduct of the cardholder - The CFPB's proposed rule treats consumers that only pay late one time the same as consumers that pay late multiple times. Moreover, the CFPB acknowledges that consumers who pay on time are likely to be harmed by the rule, given costs are likely to increase and access to credit is likely to decrease. Such an imposition on consumers who are complying with their obligations under their agreements is the antithesis of what was intended under the CARD Act. The existing rule, in place for over 12 years, has permitted higher late fees in cases of multiple late payments within a six-month period due to the "conduct of the cardholder" and to hopefully help improve their repayment behavior.

4. The overall requirement that the late fee be reasonable and proportional to the violation or omission - The CFPB's decision to base the late fee solely upon costs ignores longstanding precedent associated with "penalties," namely that they must include both a cost and deterrence component.

4. **Small Business Regulatory Enforcement Fairness Act (SBREFA) Violation:** The CFPB failed to assess this proposed rule's impact on small financial institutions. The CFPB has violated SBREFA's requirement that the CFPB develop rules only after consulting with the small businesses likely to be impacted. The proposed rule makes no effort to quantitatively analyze small bank and credit union impact and relies exclusively on the

[13] 15 U.S.C. § 1665d(a).

Federal Reserve's Capital Assessments and Stress Testing information collected from large banks, despite the availability of avenues to collect small bank data.[14]

5. **Truth in Lending Act (TILA) Violation:** The proposed rule also signals a desire to evade Section 105(d)[15] of the Truth in Lending Act, which sets forth the effective dates of regulations containing new or changed TILA disclosure requirements and legally requires the CFPB to provide sufficient time for regulated institutions to change their product disclosures.

V. Conclusion

For the reasons outlined above, the proposed rule should not go forward. The rule demonstrates a lack of understanding of late fees, would negatively affect consumers, is unnecessary, and violates rulemaking requirements. While limiting credit card late fees to $8 sounds like a consumer-benefit, it would end up eliminating many consumers' ability to get a credit card, raising the cost of low-risk customers to have a credit card, and cause a contraction of available credit on a market level. Please contact cwinslow@afsamail.org or (202) 776-7300.

Sincerely,

Celia Winslow

Celia Winslow
Senior Vice President
American Financial Services Association

[14] See Proposed rule at page 46: The Bureau recognizes that the analysis above is based on data from the largest issuers, and ***may not be representative of smaller issuers***, who do not report to the Y-14 collection. As discussed above, the Bureau did not receive specific cost data in response to its request in the ANPR for data on card issuers' pre-charge-off collection costs, including data on pre-charge-off collection costs incurred by smaller issuers. Although the Bureau does not have data equivalent to the Y-14 data for smaller issuers' pre-charge-off collection costs, it has no reason to expect that smaller issuers exhibit substantially higher pre-charge-off collection costs than larger issuers. (emphasis added).

[15] 15 U.S.C. § 1604(d).