

Federal Reserve Board
Proposed Rule, Regulation Z
March 2010

The Federal Reserve Board has issued its proposed regulations governing the final sections of the CARD Act which go into effect August 22, 2010. The Agency will be accepting public comment on the following provisions which relate to the size of penalty fees and the process for reevaluating rate increases. You can submit through our website at www.creditcardreform.org.

Limitations on Penalty Fees

- Prohibitions
 - A penalty fee can not exceed the dollar amount associated with the conduct.
 - Example: A late fee cannot exceed the amount of a minimum payment which was paid late.
 - Multiple penalty fees can not be charged for the same event.
 - No fees for declined transactions, account inactivity, or account closure.
- To determine the amount of a penalty fee, an credit card bank must make one of these determinations every 12 months, or use the “safe harbor” fee method:
 - **Cost:** The amount of the fee is proportional to the total costs incurred by the issuer for that particular violation.
OR
 - **Deterrence:** The issuer can show that the amount of the fee is necessary to deter that type of violation.
OR
 - **Safe Harbor:** The Board proposes to set a permissible penalty fee level that an issuer can use without making either of the above determinations. The Agency is asking for public comment on the standard for “safe harbor” fees.

This is the Board’s current “safe harbor” proposal. X and Y are to be set in the final regulation.

- The issuer can choose a penalty fee that is the *greater* of the following:
 - \$X
 - OR
 - 5% of the dollar amount of the violation (capped at \$Y)

CU recommends:

- The safe harbor should equal the lesser, not the greater of the dollar caps.
- The safe harbor cap amounts should be low, since it will always be permissible to charge the fee even when there is no justification.
- The Fed should include limitations on how high penalty rates can be under its authority to ensure that penalty charges are reasonable and proportional.

Reevaluation of Rate Increases

- When an issuer raises a consumer's interest rate based factors such as credit risk or market conditions, it must review the increase every 6 months and reduce the rate if appropriate.
- Issuers must review all future rate increases as well as rate increases made since January 1, 2009.
- The review is not required for rates that have increased because of a change in the variable rate or an expiration of a promotional rate.
- Issuers are not required to review the same factors which led to the increase.
- The first review is not required until February 2011.

CU Recommends:

- Banks should be required to review rate hikes as soon as the regulations go into effect in August of this year.
- Banks should report to the Fed the number of rate increases that were reduced following the six month review. These results should be public record.

Additional Notice Requirement

- When an issuer raises an interest rate, it must provide 45 days notice to the consumer. That notice must include the reason/s (no more than four) for the increase.
 - Examples: market conditions, decline in creditworthiness or credit score

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