



May 2, 2008

**Fed Issues Proposal on Unfair or Deceptive Credit Card and Overdraft Practices
Also Proposes Changes to Regulation Z and DD**

Today, the Federal Reserve Board (FRB) issued proposed rules under Regulation AA (Unfair or Deceptive Acts or Practices, or UDAP), regarding credit cards and overdraft protection programs by banks, identical to the UDAP proposals issued yesterday by the Office of Thrift Supervision (OTS) for thrifts, and National Credit Union Administration (NCUA) for credit unions.

However, the FRB's proposal also included new proposed revisions to Regulation Z (TILA) along with proposed changes to Regulation DD (Truth in Savings), intended to complement the UDAP proposal. The comment period for Regulation DD and Regulation Z will be 60 days. The comment period for the UDAP changes proposed by all three agencies will be 75 days.

As we alerted you yesterday, the UDAP proposal would do the following:

For Credit Cards:

- **Time to Make Payments.** The proposal would prohibit banks from treating a payment as late unless the consumer has been provided a reasonable amount of time to make that payment. There would be a safe harbor for banks that send periodic statements at least 21 days prior to the payment due date.
- **Allocation of Payments.** When different annual percentage rates (APRs) apply to different balances on a credit card account (for example, purchases and cash advances), banks would have to allocate payments exceeding the minimum payment using one of three methods or a method equally beneficial to consumers. They could not allocate the entire amount to the balance with the lowest rate. A bank could, for example, split the amount equally between two balances. In addition, to enable consumers to receive the full benefit of discounted promotional rates (for example, on balance transfers), during the promotional period payments in excess of the minimum would have to be allocated first to balances on which the rate is not discounted.
- **Applying Rate Increases to Existing Balances.** The proposal would prohibit banks from increasing the interest rate on outstanding balances unless the increase

is due to: (i) the operation of an index (in other words, the rate is a variable rate); (ii) the expiration or loss of a promotional rate (provided the rate is not increased to a penalty rate); or (iii) the minimum payment not being received within 30 days of the due date.

- **Credit Card Holds.** The proposal would prohibit banks from imposing a fee when the credit limit is exceeded solely because a hold was placed on available credit. This can occur where the final dollar amount of a transaction was not known in advance (for example, when a consumer checks into a hotel, a hold is placed for the expected cost of the stay).
- **Two-Cycle Billing.** The proposal would prohibit banks from imposing finance charges based on balances on days in billing cycles preceding the most recent billing cycle, a practice that is sometimes referred to as two-cycle billing.
- **Financing of Security Deposits and Fees.** The proposal would address concerns regarding subprime credit cards by prohibiting banks from financing security deposits and fees for credit availability (such as account-opening fees or membership fees) if charges assessed during the first twelve months would exceed 50 percent of the initial credit limit. The proposal would also require financed security deposits and fees exceeding 25 percent of the initial credit limit to be spread over the first year.
- **Firm Offers of Credit.** The proposal would require banks making firm offers of credit advertising multiple APRs or credit limits to disclose the factors that determine whether a consumer will qualify for the lowest APR and highest credit limit advertised (for example, the consumer's credit history, income, and debts). A safe harbor disclosure is provided.

For Overdraft Programs:

- **Right to Opt Out.** The proposal would prohibit banks from imposing a fee for paying an overdraft unless the bank has provided the consumer with an opportunity to opt out of the payment of overdrafts and the consumer has not done so. The opt-out right would apply to all transaction types. Banks also would be required to provide consumers a partial opt-out for overdrafts resulting from ATM and point-of-sale transactions.
- **Debit Holds.** The proposal would prohibit banks from imposing a fee when the account is overdrawn solely because a hold was placed on funds in the consumer's deposit account. This can occur where the final dollar amount of the transaction was not known in advance (for example, when a consumer purchases fuel at the pump, a hold is placed for the estimated amount of fuel that will be purchased).

The proposed amendments to Reg Z to address specific credit card practices are as follows:

- **Due Dates for Mailed Payments.** The proposal would provide that mailed credit card payments received by 5 p.m. on the due date must be considered timely. In addition, if a creditor does not receive or accept mailed payments on the due date (for example, when the due date falls on a Sunday or holiday), a payment received by mail on the next business day would be considered timely.
- **Right to Reject Cards with Substantial Fees.** The proposal would address concerns regarding subprime credit cards by requiring creditors that assess security deposits and fees at account opening that exceed 25% of the minimum credit limit notify consumers that, after receiving the account-opening disclosures, they can reject the credit card and avoid the fees (unless the consumer has made a payment on the card after receiving the billing statement or used the card).
- **Deferred Interest Plans.** The proposal would require written or electronic advertisements for deferred interest plans stating “no interest” or a similar term to disclose prominently the circumstances under which interest may be charged (e.g., if the balance is not paid in full by a certain date).
- **Limiting the Issuance of “Substitute” Cards.** Creditors would be prohibited from substituting a new general purpose credit card for an existing single-merchant card without the consumer’s consent when the existing card has been “inactive” (i.e., the existing card has a zero balance and has not been used by the consumer for 24 months or longer).
- **Grace Periods.** The Board’s exemption authority would be used to eliminate the statutory requirement that creditors describe any interest-free period using the term “grace period.” Based on consumer testing results, the proposal includes new language that is easier for consumers to understand.
- **Minimum Finance Charge.** Creditors would no longer have to disclose in their summary tables a minimum finance charge of \$1.00 or less.

The proposed amendments to Regulation DD to address depository institutions’ overdraft practices are as follows:

- **Disclosure of Right to Opt Out.** The proposal would establish format, content, and timing requirements for disclosing consumers’ right to opt out of overdraft protection services pursuant to the Regulation AA proposal.
- **Disclosure of Aggregate Overdraft Fees.** The proposal would extend to all banks and savings associations the requirement to disclose on periodic statements the aggregate dollar amounts charged for overdraft fees and for returned item fees

(for the month and the year-to-date). Currently, only institutions that promote or advertise the payment of overdrafts must disclose aggregate amounts.

- **Disclosure of Balance Information.** The proposal would require banks and savings associations that provide account balance information through an automated system to disclose the amount of the consumer's funds available for immediate use or withdrawal, without including additional funds the institution may provide to cover overdrafts.

For more information, please go to the FRB website at:

<http://www.federalreserve.gov/newsevents/press/bcreg/20080502a.htm>. CBA will be commenting. Please contact Steve Zeisel at szeisel@cbanet.org or Darlene Rosenkoetter at drosenkoetter@cbanet.org with your questions or comments.