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May 3, 2023

Via Federal eRulemaking Portal

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

RE: CFPB Credit Card Penalty Fees (Regulation Z);
(Docket No. CFPB-2023-0010; RIN 3170-AB15)

Dear Director Chopra:

Auriemma Roundtables, a leading provider of business intelligence solutions to consumer finance companies, together with a group of our clients including First National Bank of Omaha, other regional and national credit card issuers, and other financial institutions, serving a cross-section of super-prime, prime and sub-prime borrowers, respectfully submits this comment in response to the Consumer Financial Protection Bureau's ("CFPB") Proposed Rule with Request for Public Comment regarding Credit Card Penalty Fees under Regulation Z, published in the Federal Register on March 29, 2023 at 88 FR 18907 (the "Proposed Rule").

If enacted, the Proposed Rule will drastically alter the existing, well-reasoned regulatory framework governing credit card late fees. As discussed in detail below, the Proposed Rule, if adopted, would violate the Administrative Procedure Act ("APA"), would fail to satisfy the requirements of the Truth in Lending Act ("TILA"), and would raise significant public policy concerns. We also provide responses to certain issues on which the CFPB requested comment in the Proposed Rule.

I. Adoption of the Proposed Rule Would Violate the Administrative Procedure Act

Congress grants tremendous power to federal agencies when it delegates rulemaking authority. Recognizing this, Congress enacted the APA to ensure agency actions are appropriate and consistent with the delegated authority. The APA requires that an agency rule or other action be set aside if the rule is arbitrary and capricious or otherwise not in accordance with law. 5 U.S.C. § 706(2)(a). A rule's promulgation is not in accordance with law if it is in excess of the agency's statutory jurisdiction or authority, or adopted without observance to any procedures required by applicable law. 5 U.S.C. § 706(2)(d). The Proposed Rule (i) is arbitrary and capricious, (ii) exceeds the CFPB's statutory authority, and (iii) if promulgated, will have been adopted without observance of the procedures required by law. Each of these grounds is distinctly fatal on its own. Combined, these flaws demonstrate the CFPB's disregard for the limited bounds of authority granted by Congress.

A. The Proposed Rule Is Arbitrary and Capricious

The Proposed Rule is arbitrary and capricious and, therefore, in violation of the APA on at least two bases: (i) the data forming the premise of the CFPB's position fails to take into consideration a substantial and important segment of the market; and (ii) the data is not publicly available, leaving the public no meaningful opportunity to review or comment on its accuracy or application in support of rulemaking that could have enormous economic and public policy consequences.

The APA's arbitrary and capricious standard requires that agency action be reasonable and reasonably explained. An agency must act "within a zone of reasonableness", which means it must have "reasonably considered the relevant issues and reasonably explained [its] decision." *FCC v. Prometheus Radio Project*, 141 S. Ct. 1150, 1158 (2021). If an agency departs from an established precedent, it must have a reasoned explanation for doing so. *ANR Pipeline Co. v. FERC*, 71 F.3d 897, 901 (D.C. Cir. 1995) ("[W]here an agency departs from established precedent without a reasoned explanation, its decision will be vacated as arbitrary and capricious."). In determining whether an agency has provided a reasoned explanation for departing from precedent, one must look to the reasons given by the agency. *SEC v. Chenery Corp.*, 318 U.S. 80, 88 (1943). In order to provide a reasoned explanation, an agency must provide findings supported by "substantial evidence on the record considered as a whole." *Id.*, quoting S. Rep. No. 1301, 89th Cong., 2d Sess., 8 (1966); H. R. Rep. No. 1776, 89th Cong., 2d Sess., 21 (1966). The D.C. Circuit has stated that an agency "commits serious procedural error when it fails to reveal portions of the technical basis for a proposed rule in time to allow for meaningful commentary." *Owner-Operator Independent Drivers Ass'n., Inc. v. Fed. Motor Carrier Safety Admin.,* 494 F.3d 188, 199 (D.C. Cir. 2007) (citations omitted). An agency has a duty "to identify and make available technical studies and data that it has employed in reaching the decisions to propose particular rules …" *Id.*; *see also Air Trans. Ass'n. of Am. v. FAA*, 169 F.3d 1, *7 (D.C. Cir. 1999) ("[T]he most critical factual material that is used to support the agency's position on review must have been made public in the proceeding and exposed to refutation.") (citations omitted); *see also International Ladies' Garment Workers' Union v. Donovan*, 722 F.2d 795 (D.C. Circuit 1983) (agency's failure to cogently explain why it exercised its discretion in a given manner, or to provide an adequate statement of basis or purpose, rendered its decision arbitrary and capricious.); *Connecticut Light & Power Co. v. Nuclear Regulatory Com'n*, 673 F.2d 525, 530 (D.C. Cir. 1982) ("To allow an agency to play hunt the peanut with technical information, hiding or disguising the information that it employs, is to condone a practice in which the agency treats what should be a genuine interchange as mere bureaucratic sport.").

To support this proposed drastic reduction in late fees, which is based on the assertion that the current framework is misaligned with reasonable collection costs, the CFPB relies on its own March 2022 report entitled "Credit Card Late Fees" (the "March 2022 Report") which itself is based on confidential data: primarily, data collected on only one largely homogenous segment of the overall market: the very largest financial institutions in the nation with large credit card portfolios. This data, which is based on de-identified account-level data collected by the Federal Reserve Board ("Board") as part of its Y-14M ("Y-14") data collection, is representative of bank

holding companies with total consolidated assets of $100 billion[1] or more that [also] have credit card portfolio balances in excess of $5 billion. Although the CFPB claims that the data represents more than 70% of the overall credit card market, it does not include information about smaller institutions, which are more likely to be market disrupters that increase competition and access to credit, two objectives the CFPB ostensibly promotes. Therefore, the limited data set cannot reasonably support the conclusions inferred by the CFPB about the overall credit card market. Moreover, there is no way for the public to meaningfully point out all of the inadequacies and potential manipulations, since it is not publicly available.[2]

The CFPB even acknowledges the inadequacy of its data. *See* 88 FR at 18917 (Mar. 29, 2023) (stating that the Proposed Rule "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."); the CFPB's admission in the March 2022 Report, that the data it relies on is not representative of the entire market[3]; and the CFPB's concession that the Y-14+ data fails to cover a substantial portion of the market in its September 2021 report entitled "The Consumer Credit Market"[4]. Based on a CFPB report issued earlier this year entitled "Credit Card Late Fees: Revenue and Collection Costs at Large Bank Holding Companies," it appears that the Y-14 data collected comes from 20 to 22 credit card issuers, a fraction of the industry.[5] The CFPB's decision to exclude from reasoned consideration such a wide swath of the industry leaves a shocking gap in the underpinnings of the

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[1] The reporting threshold was raised from $50 billion to $100 billion on December 21, 2019. 84 FR 59032. Despite that fact, the Proposed Rule refers only to the original, lower threshold when describing the Y-14 data ("Since June 2012, the Board has collected these data monthly from bank holding companies with total assets exceeding $50 billion.") This inconsistent characterization of the data used to develop the Proposed Rule is confusing, and is another example of the fact that it is not at all clear to the public what data is being used, as it is unavailable to review it or in any way determine whether or not it supports the CFPB's conclusions.

[2] The March 2022 Report also refers to "data provided in response to a series of data filing orders from a diverse group of specialized issuers," which data the CFPB states are used to supplement the Y-14 data with respect to "certain facets of the market," resulting in what the CFPB calls "Y-14+" data. Again, this data is not available for review and the details of how and when it is used to supplement the Y-14 data is not explained.

[3] See the March 2022 Report, footnote 3: "This study reports only aggregate measures and reveals no information about any specific issuer. These issuers represent a large portion of the market but are not necessarily representative of the portion of the market not covered by the data the Bureau receives. Results reported from Y-14 data throughout this report should be interpreted accordingly."

[4] See the CFPB's September 2021 Report entitled "The Consumer Credit Card Market", footnote 29: "The Y-14+ data cover a larger and more representative portion of the credit card market, but the remaining uncovered portion is still substantial, and the Y-14+ data should similarly not be considered representative of that uncovered portion."

[5] A letter filed by The American Bankers Association (ABA), Credit Union National Association (CUNA), Independent Community Bankers of America (ICBA), National Bankers Association (NBA), and National Association of Federally-Insured Credit Unions (NAFCU) (collectively, the Associations) on January 20, 2023 regarding the Consumer Financial Protection Bureau's (CFPB) planned rulemaking activity concerning credit card penalty fees states there are approximately 3,932 credit card issuers in the United States: 805 credit card issuing banks and 3.127 credit card issuing credit unions. This would indicate that the Y-14M data is representative of only about 0.5% of credit card issuers.

Proposed Rule, a gap that even when viewed in the light most favorable to the CFPB excludes at least 30% of the market. We conclude that basing a decision that will cause a reduction of at least $9 billion in cost recovery on information that is only indicative of a very small fraction of issuers is wholly arbitrary and establishes a frightening precedent for small businesses subject to the oversight of the CFPB – an agency that as of late has made multiple public statements championing competition and expressing concerns about anti-competitive practices.

Beyond a general stated desire to address what it perceives as a reliance on late fees as a revenue generator by some issuers, the CFPB fails to adequately explain the basis for the new late fee framework and is, in essence, serving up a drastic change on the basis of factors concealed in a "Black Box."[6] We are not alone in this contention. Other comments submitted regarding the Proposed Rule have taken issue with either the lack of data supporting the CFPB's late fee proposal and/or its reliance on Y-14 data. *See, e.g.*, Aug. 1, 2022 Comment Letter from the American Bankers Association ("ABA"), Consumer Bankers Association ("CBA"), Credit Union National Association ("CUNA"), and National Association of Federally-Insured Credit Unions ("NAFICU") on the ANPR (providing analysis and data relevant to the late fee structure); Feb. 28, 2023 Request for Extension of Comment Period for NPRM from ABA, Bank Policy Institute ("BPI"), CBA, CUNA, Independent Community Bankers of America, NAFICU, and National Bankers Association (requesting an extension of the public comment period so as to allow for large and small issuers to collect and analyze data to be considered in the rulemaking); and Mar. 16, 2023 Comment Letter on NPR on Credit Card Penalty Fees from the BPI, ABA, CBA, CUNA, and NAFICU (requesting the CFPB to release anonymized and/or aggregated Y-14 data to allow for review and comment or to refrain from relying on the data and related analysis in support of the Proposed Rule). The public cannot reasonably or meaningfully comment on data to which it has no access. It is impossible to foresee all the potential effects of such a drastic change in the economics of the credit card market, but unintended adverse consequences are inevitable. This is especially true here since data forming the basis for the change is demonstrably unrepresentative of the market and impossible to critique because of its confidential nature. If the purpose for public comment is to inform an agency about potential unintended consequences of its actions, then transparency is a critical element of the rulemaking process. Congress recognized this by establishing guardrails under the APA. The CFPB needs to follow the rules or risk untold consequences to an industry already facing economic challenges.

[6] The Board and the CFPB, in the course of issuing rules and adjusting penalty fee safe harbors for over a decade, previously found safe harbor amounts substantially in excess of $8 to be "reasonable and proportional" and to adequately consider the "cost incurred by the creditor" in accordance with TILA. The sudden reversal of the CFPB's position reflecting a conclusion that a substantially lower safe harbor of $8 satisfies the same statutory standard that has been in place since 2010 seems an impermissible stretch, especially in the absence of any publicly available data provided for review to support that change. This failure on the part of the CFPB to make its case is inconsistent with the APA.

B. The Proposed Rule is in Excess of the CFPB's Statutory Jurisdiction, Authority, or Limitations

A rule will also separately violate the APA if an agency acts "in excess of its statutory jurisdiction, authority, or limitations, or short of statutory right." 5 U.S.C. § 706(2)(c).

TILA requires late fee limitations and any safe harbors (if established) to be "reasonable and proportional" to the violation they are designed to address. TILA requires any rule relating to late fees to be implemented only after contemplation of: "(1) the cost incurred by the creditor from such omission or violation; (2) the deterrence of such omission or violation by the cardholder; [and] (3) the conduct of the cardholder; ..." 15 U.S.C. § 1665d(c). The CFPB has failed to address these vital requirements in the Proposed Rule because it has failed to adequately look beyond the Y-14 data.

Cost Incurred by the Creditor

TILA requires the CFPB to consider "the cost" incurred by the creditor from a violation in determining the amount of the penalty fee. 15 USC §1665d(c)(1).[7]

The CFPB's consideration of cost is both conclusory and superficial. The CFPB should have taken other sources of cost into consideration as the Board did in 2010 when it first promulgated late fee limitations. Data considered by the Board that were not considered by the CFPB include average penalty fees assessed across the industry, all costs associated with late payments, dollar amounts of penalty fees on other types of non-credit card consumer accounts, state and local laws regulating penalty fees, and the safe harbor threshold for credit cards established by the United Kingdom's

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[7] The May 4, 2009 Senate Report regarding S 414, which was the precursor Senate bill to the CARD Act, indicated the legislative intent that "the cost" meant that issuers be permitted to recover all their costs associated with late payments:

> The Credit Card Act will help put an end to unreasonable penalty fees. The CARD Act further addresses fees by requiring that the penalty fees charged to cardholders be reasonably related to the issuers' costs . . . . The Committee understands that the Federal Reserve Board, in determining reasonable relation to cost, will take into account a number of factors, including; costs associated with individual transactions; costs of managing the portfolio; credit risk associated with both the portfolio and the individual; the conduct of the cardholder; and circumstances leading to such omission or violation; and such other factors as the Board may deem appropriate. *See* S Rep. No. 111-16 at 7 (2009). *See also* at 10 (stating that Section 103 "requires that penalty fees assessed to cardholders be reasonably related to the cost incurred by the issuer."

On May 11, 2009, Senator Dodd offered a substitute amendment (SA 1058) to HR 627 based on bipartisan negotiations over the text of S 414. That version contained the language that appears in Section 1665d(a) that penalty fees be "reasonable and proportional to the omission or violation" together with the provisions now found in 1665d(b) – (e). During the May 13, 2009 debate, Senator Menendez referred to the fact that the amendment reasonably ties fees to costs:

> This Congress, as I have done for several Congresses, I introduced the Credit Card Reform Act to tackle essentially the same issues this current bill deals with, including banning retroactive rate increases, protecting young consumers from being sucked into the cycle of debt, reasonably tying fees to costs, and prohibiting unilateral changes to agreements. (emphasis added). *See* Congressional Record – Senate (May 13, 2009), S 5409.

Office of Fair Trading. Instead of considering these and other relevant sources, the CFPB based its determinations on data that is neither representative of card issuers nor available for public review. The CFPB's failure to contemplate other data, including data that is publicly available, is indicative of a failure to adequately take into consideration a creditor's costs of collection in establishing the proposed late fee limitations and the safe harbor.

The CFPB presents several tenuous arguments for why a cap on late fees of 25% of the minimum payment due ("MPD") is valid under TILA. The CFPB argues that an $8 safe harbor amount is sufficient to permit most issuers to recover their allowable costs. Its position is that as long as 25% of the MPD is $32 or more, those costs will be recovered, and the instances where the 25% of the MPD would be less than $8 "do not appear to be frequent." This argument misses the point that Congress intended issuers to recover their costs with the late fees they charged. The whole reason for the cost method authorized by TILA is to permit an issuer that has costs that cannot be recovered using the safe harbor amount to recover those costs by setting its late fee at an amount sufficient to permit it to do so. Assuming an issuer has used the cost method to set a late fee at $X, that amount represents its actual recoverable costs, which do not vary depending upon the MPD. Requiring an issuer to accept a late fee of less than $X by applying the 25% limitation would require the issuer not to recover its costs associated with the late payment violation, which is contrary to the language of Section 1665d.

Deterrence
TILA also requires the CFPB to consider the deterrence of a violation as a factor in setting a penalty fee. It is apparent that the nominal nature of the Proposed Rule's $8 late fee safe harbor and late fee cap of 25% of the MPD likely would result in late fees that would not deter late payments. The CFPB states that it analyzed available data to consider the extent to which lower late fees for both the first and subsequent late payments could potentially lessen deterrence, and that available evidence suggests that the proposed $8 safe harbor amount would still have a deterrent effect on late payments. Notwithstanding, the CFPB's conclusion that this new lower late fee structure will still have a deterrent effect is, again, primarily based on Y-14 data and its own March 2022 report, which also drew its conclusions from Y-14 data.

Other than this, there is no support in the Proposed Rule for the premise that the late fees permitted thereunder would have any deterrent effect.[8] While the CFPB's analysis of deterrence factors in the Proposed Rule takes issue with some of the Board's analysis in the prior rulemaking, at no point does the CFPB explain how the proposed $8 safe harbor fee is a deterrent against late payment violations. There is insufficient support in the record to substantiate the CFPB's conclusion that a late fee safe harbor of $8, coupled with a prohibition against any late fee in excess

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[8] By contrast, the Board's consideration of deterrence during the original rulemaking in 2010 resulted in a revision of the safe harbor fee for repeated violations. The two-tier late fee safe harbor amounts that the Board formulated – $25 for a first violation and $35 for any additional violation of the same type during the next six billing cycles when first promulgated and prior to any adjustment for inflation – was designed with deterrence in mind. Specifically, the Board found that "there is some evidence that the experience of incurring a late payment fee makes consumers less likely to pay late for a period of time." 75 FR 37525 (Jun. 29, 2010). Because some "consumers may be deterred by the imposition of the fee itself", the Board set the higher late fee for multiple violations on the grounds that it "will have a significant deterrent effect on future violations." *Id.*

of 25% of the MPD would have a deterrent effect, or adequately considers cardholder conduct in setting the proposed late fee framework.

Discussing deterrence, the CFPB suggests that a late fee of $8 would be effective to deter "a rational consumer faced with the decision of whether to make a [$100] minimum balance payment on time or to put off the payment until later" because the imputed APR if the payment is deferred for a full month would be 96%, or up to 730% if the payment is made within 10 days of its due date. In reality, however, serious economic analysis recognizes that rational consumers make decisions based on alternative choices, not knee-jerk reactions to one alternative in isolation. In the case of a consumer who needs to finance a minimum payment over a short period, the obvious alternative to doing nothing and incurring a late fee would be getting a payday loan, which the Consumer Education Portal on the CFPB's website reports will cost from $10 to $30 for every $100 borrowed. It should be obvious that, when consumers compare the alternative of doing nothing with going through the trouble of seeking out, applying for and obtaining a payday loan, and then using the proceeds in a separate transaction to make a payment, rational consumers will surely prefer the do-nothing approach, especially when the cost of doing nothing is lower, or at worst roughly the same as, the alternative. This is especially true if the consumer carries the balance for an additional month because, unlike a payday loan rollover fee, the late fee may not be charged again. Consumers will recognize a fee of 25% of the MPD as a convenience fee, not a late fee, which is exactly what it will become. It would encourage, not deter, late payment.

Conduct

TILA requires that the CFPB consider the conduct of the cardholder in establishing a penalty fee. The Proposed Rule does not take into consideration the conduct of the cardholder in any meaningful way. The CFPB merely states that it is not clear from its analysis of the Y-14 data that multiple violations during a relatively short period are associated with increased credit risk and reflect a more serious consumer violation. Based on this, the CFPB proposes to remove dual-tiered late fees that have been effective for over a decade and that were implemented based on the Board's reasoned approach. This conclusory assertion, which cannot be tested since the data is unavailable, encompasses the entirety of the CFPB's consideration of a statutorily required factor.

The CFPB's assessment of consumer conduct is deficient in connection with setting the 25% of MPD cap on the late fee. For example, the CFPB inexplicably invokes the timeline for reporting payments as late to credit reporting agencies after 30 or more days as evidence that the credit card industry itself does not consider late payments to be a serious form of consumer conduct until that point. While noting that some consumers may chronically pay late due to cash flow issues and then cure within 30 days, the CFPB ignores the fact that many consumers do not cure within 30 days and that consumer conduct should be taken into account, as required under TILA, in determining the reasonableness of a late fee. The CFPB also states that card issuers have methods other than late fees to address credit risk, like reducing credit lines or applying a penalty rate. These examples also show that the CFPB has decided not to take consumer conduct into account in issuing its late fee rule, contrary to the requirements of TILA.

C. If the CFPB Proceeds as Proposed, the Rule Will Have Been Adopted Without Observance of Procedure Required by Law

Where an agency action is found to be made "without observance of procedure required by law," it is unlawful and should be set aside under the APA. 5 U.S.C. § 706(2)(d). Key procedural requirements set forth in the Small Business Regulatory Enforcement Fairness Act of 1996 ("SBREFA") must be observed before the Proposed Rule can be legally adopted.

The CFPB has failed to comply with an important requirement mandated under the SBREFA. Pursuant to the SBREFA, the CFPB must convene a Small Business Review Panel if it is considering a proposed rule that could have a significant economic impact on a substantial number of small entities. The Proposed Rule will have a significant impact on a substantial number of smaller credit card issuers that are already at a disadvantage based on their size in competing against larger issuers. As such, the CFPB must convene a small business panel. The CFPB has not met this requirement. This is especially important in light of the complete lack of data about smaller issuers and the significant impact the Proposed Rule may have on them.

This clear violation of the SBREFA will certainly lead to challenges in court to the validity of the regulation, which could be easily precluded by compliance with the mandate to convene a small business panel.

II. The Proposed Rule Violates TILA

The CARD Act amended TILA to require that any penalty fee must be "reasonable and proportional" to the violation the fee is designed to address. Simply put, the 25% of the MPD limit on any late fee assessed is an arbitrary cap that is not reasonably related to the actual cost of collections when cardholders fail to make their monthly payment. The Proposed Rule fails to consider all costs actually incurred by creditors; therefore, this proposed limitation would not allow a creditor to charge a fee that bears a reasonable and proportional relationship to the violation. While this part of the Proposed Rule may achieve the CFPB's goal of reducing the late fee, it does not bear a reasonable relationship to actual collection costs. Therefore, for both of these reasons, the Proposed Rule violates TILA.

Post-charge-off collection costs should not be excluded from the penalty fee calculation. Currently, the Regulation Z Official Interpretation, at 52(b)(1)(i)-2.i, provides that "Losses and associated costs (including the cost of holding reserves against potential losses and the cost of funding delinquent accounts)" are not to be taken into consideration in determining the cost incurred due to a violation in calculating a reasonable and proportional penalty fee.[9] The CFPB proposes to summarily expand this interpretation to exclude post-charge-off collection costs from the

[9] We note this interpretation appears to conflict with congressional intent that credit risk is to be taken into account in determining a penalty fee reasonably related to the issuers' costs. *See* the discussion of the May 4, 2009 Senate Report, footnote 7, above.

calculation of costs incurred.[10] Contrary to the CFPB's assertion, all collection costs, including post-charge-off collection costs, are directly related to the cardholder's violation that the late fees are intended to address, and should be included in calculating a reasonable and proportional late fee. The proposed interpretation that would exclude post-charge-off collection costs would further impair a card issuer's ability to charge a late fee proportional to the actual total costs of default, which despite the current official interpretation, actually include the cost of reserving against loan losses: under the current expected credit loss methodology ("CECL") promulgated by the Financial Accounting Standards Board in 2016 (six years after the Board's adoption of its interpretation at 52(b)(1)(i)-2.i), charge-off costs are to be included when estimating allowances for credit losses. The CECL standard applies to all banks, savings associations, credit unions, and financial institution holding companies, regardless of size, that file regulatory reports for which the reporting requirements conform to GAAP.[11] As such, Official Interpretation 52(b)(1)(i)-2.i, that was adopted in 2010, prior to CECL, causes costs that must be included in GAAP-compliant accounting for credit losses by financial institutions to be excluded for purposes of determining if the proposed late fee is reasonable and proportional. The CFPB should not now adopt an interpretation that strays even farther from TILA requirement that penalty fees be "reasonable and proportional" and take into consideration all costs incurred due to the violation.

Further, if the Proposed Rule were adopted, credit card issuing banks would be required to increase loan loss reserves in light of the increased risk of default caused by the greatly decreased deterrent effect of these significantly lowered late fees, thus compounding the issue described above.

Other costs not taken into consideration include the loss of interest income when a consumer fails to pay, and potential reduction in interchange income to issuers when late payers cannot make purchases due to lower available credit.

III. The Proposed Rule Raises Significant Public Policy Concerns and Risk of Negative Consequences.

The Proposed Rule raises significant public policy concerns and presents significant risk of negative consequences to consumers, credit card issuers, and smaller issuers in particular.

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[10] The Proposed Rule includes an addition to the Official Interpretation to "clarify" that exclusion of post-charge-off collection costs should be excluded from the cost analysis provisions for determining penalty fee amounts. This change would apply to all penalty fee calculations, not just late fees:

> "The Bureau also proposes one clarification that would apply to penalty fees generally. Specifically, the Bureau proposes to amend comment 52(b)(1)(i)-2.i to clarify that costs for purposes of the cost analysis provisions in § 1026.52(b)(1)(i) for determining penalty fee amounts do not include any collection costs that are incurred after an account is charged off pursuant to loan loss provisions." *See* 88 FR 18906, at 18907.

[11] *See* FAQ on the New Accounting Standard on Financial Instruments – Credit Losses (Apr. 3, 2019), *available at* https://www.fdic.gov/news/financial-institution-letters/2019/fil19020.html

A. Consumer Considerations

Public policy concerns about the Proposed Rule and its impact on consumers include:

Potential detrimental effects on consumers who pay late
By drastically reducing the penalty for late payment, the Proposed Rule, if adopted, likely will lead to an increase in late payments by removing the deterrent of the current, higher penalty. With such a low late fee, consumers will not have the same incentive to make timely payments. Indeed, the nominal nature of the proposed $8 safe harbor payment may actually serve to encourage consumers to miss payments. The CBA survey cited above found that nearly half of Americans (48%) are unaware of the consequences of paying a credit card bill late.[12] Missed payments may lead to lost grace periods on purchases and increases the risk of higher debt, higher delinquency rates, lower credit scores, and lower lines of credit available to individual consumers unaware of the repercussions of missing a payment deadline because the late fee is no longer sufficient to act as a deterrent to late payment.

Detrimental effect on credit availability
Instead of expanding access to credit, the Proposed Rule will restrict access to credit – especially for lower-income and subprime consumers. The 25% MPD cap is likely to result in an increase in the MPD established by issuers. This, in turn, likely will reduce the number of consumers who qualify for and/or can afford credit under ability-to-pay requirements, constricting credit availability. Further, there will be less credit available for those who need it most, such as those with little or no credit history, since this population poses a higher risk of late payment. This reduction in, or lack of, available credit will make life more difficult for consumers, leaving them without the ability to make daily purchases. Ironically, this may drive consumers to short-term alternative credit such as payday loans. Further, individuals who cannot obtain a credit card may encounter barriers to certain types of common consumer purchases, such as an inability to rent a car, arrange for transportation (such as ride share services), or reserve a hotel room, which could in turn make it more difficult to obtain and keep employment, take care of their family and other personal obligations, and engage in everyday activities.

Detrimental effect on credit card pricing for consumers who pay on time
The drastic reduction of the late fee under the Proposed Rule, and the fact that the safe harbor amount would no longer be adjusted for inflation, means the true cost of the impact of late payments will be incorporated into credit card pricing in the form of higher APRs imposed on all cardholders. As the CFPB admits, the Proposed Rule, if adopted, likely will result in the imposition of higher interest charges on an issuer's entire portfolio to make up for an inability to recover costs through a more narrowly targeted, reasonable and proportional late fee paid by the small percentage of cardholders who pay late (estimated to be as low as 3% of cardholders). The CFPB even encourages this outcome, stating that one option to cover collection costs if the $8 safe harbor fee is insufficient would be to "use interest rates or other charges to recover some of the costs of

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[12] *See* New Poll: Majority of Americans Believe Credit Card Late Fees are Legitimate (Apr. 5, 2023), *available at* https://www.consumerbankers.com/cba-media-center/media-releases/new-poll-majority-americans-believe-credit-card-late-fees-are

collecting late payments." 88 FR 18919 (Mar. 29, 2023). Using a simple formula that does not account for any inevitable change in consumer behavior, the CFPB estimates that the average APR would need to increase approximately 200 basis points to make up for the late fee deficiency. It is patently unfair to increase APRs across the board, as that needlessly increases the cost on consumers who are timely payers, in lieu of the more targeted late fee on late payers. Despite any headline the CFPB might use to suggest the rule benefits consumers, consumers generally will be negatively impacted by this change.[13]

Potential encouragement of irresponsible financial behavior
The Proposed Rule may encourage irresponsible financial behavior by replacing the current deterrent in place with a more nominal late fee that is more likely to be ignored. Accordingly, the Proposed Rule contravenes the CFPB's mission under Dodd-Frank to promote financial literacy by suggesting that paying late is the same as obtaining a further loan, and that late payment can be acceptable or even encouraged behavior.

B. Market Considerations

Public policy concerns about the Proposed Rule and its impact on the credit card industry include:

Effects on financial soundness of credit card issuers
The CFPB entirely ignores the potential impact that this proposal may have upon the U.S. banking system generally. The Proposed Rule must be viewed in the context of a banking system that is already highly strained by 40-year high inflation rates and drastic increases in interest rates over the past 18 months. The CFPB's own data finds that late fee revenue totals approximately $12 billion annually, but it does not estimate or project revenue totals that may be realized if the Proposed Rule goes into effect. The CFPB estimates that late fee revenue would likely decrease by more than 70%, and credit losses would likely increase -- despite the CFPB's assertion that $8 will deter late payment. We do not believe the impact that such a monumental change will have on an already strained banking system has been adequately contemplated.[14]

Detrimental effect on competition and smaller issuer participation
Rather than promoting competition in consumer financial services (a stated goal of the CFPB's leadership), the Proposed Rule would most likely force many smaller issuers out of the market, resulting in less competition. As discussed above, the CFPB did not examine data related to smaller

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[13] Currently, late payers pay a late fee and typically are able to continue using their credit cards unless they are seriously delinquent. There clearly is value assigned by cardholders to this ongoing ability to use their credit cards, and under the current rule, those benefiting from that value are paying for it. Under the Proposed Rule, cardholders who pay on time would be forced to subsidize late-payer conduct through increased finance charges, and card issuers may determine they cannot offer late payers ongoing access to charging privileges.

[14] We also note that the extremely nominal nature of the $8 safe harbor late fee, and the likelihood that it would encourage rather than deter late payment, suggests an approach that would not be a safe and sound banking practice. Banks should not be forced to make another unsecured "loan" to refinance an already delinquent loan, which the CFPB suggests is what would occur when a cardholder fails to make a timely payment and pays an $8 late fee, and further suggests the late fee should be viewed as an additional finance charge for that additional loan. *See* 88 FR at 18920.

issuers, as the Y-14 data is provided by large issuers only. By assuming the costs of the Proposed Rule will not be qualitatively different for smaller issuers, the CFPB ignores the reality that financial institutions with $100 billion or more in total consolidated assets will be better positioned to absorb the impact of the drastic reduction in late fee revenue and the corresponding costs of recovery. Less competition will lead to less innovation, fewer and less valuable credit card rewards, and increasingly fewer choices for consumers.

IV. Additional Comments Relating to the Proposed Rule

The CFPB has requested comment on a number of significant issues within the Proposed Rule with Request for Public Comment. While we believe the entire Proposed Rule should be rescinded, we respond with respect to three of these issues:

Application of Similar Restrictions to Other Penalty Fees
While the Proposed Rule is limited to late fees, the CFPB also seeks comment as to whether the proposed late fee amendments should apply to other penalty fees. We object to extending the amendments to other penalty fees for the reasons discussed in this letter with respect to the late fee proposed rule, namely that the framework proposed is not reasonable and proportional under TILA, and data has not been provided for review to support the application of the proposed late fee amendments to other penalty fees.

Imposition of a "Courtesy Period" Before a Late Fee Can Be Charged
15 U.S.C. §1666b of TILA demonstrates a determination by Congress that mailing or delivery of a billing statement at least 21 days before the payment due date provides a sufficient and appropriate period of time to allow the cardholder to pay on time.

A rule requiring (or tying use of the late fee safe harbor to) a "courtesy period" of 15 days (or another number of days) after the due date before a late fee is imposed would contradict congressional intent and contravene the provisions of TILA. 15 U.S.C.§ 1666b(a) provides:

> a) Time to make payments. A creditor may not treat a payment on a credit card account under an open end consumer credit plan as late for any purpose, unless the creditor has adopted reasonable procedures designed to ensure that each periodic statement including the information required by section 127(b) [15 USCS § 1637(b)] is mailed or delivered to the consumer not later than 21 days before the payment due date.

If Congress had wanted to distinguish between the post-statement timing for imposition of a late fee versus other actions that constitute "treating a payment as late", it could have done so. Under 15 U.S.C.§1666b(a), a creditor that meets the congressionally mandated requirement to adopt reasonable procedures to ensure each periodic statement is mailed or delivered no later than 21 days before the payment due date earns the right to treat a payment made later than the payment due date as late for any purpose.

Further, such a rule would only exacerbate the myriad problems (discussed above) that would be caused by the proposed $8 late fee safe harbor and late fee limit of 25% of the MPD: Such a courtesy period would further encourage late payments, which, as pointed out above, can have

significant negative impacts on consumers. For example, even if the cardholder were to escape a late fee when the MPD is paid within 15 days after the due date, other detrimental consequences of late payment still would apply, such as the loss of a grace period on purchases. Moreover, such a courtesy period would cause customer confusion as to the distinction between the late fee courtesy period versus a grace period on purchases.

Assessment of "Staggered" Late Fees Amounts

The CFPB has requested comment as to whether and why it should set a staggered late amount with a cap on the maximum dollar amount, such that card issuers could impose a fee of a small dollar amount every certain number of days until a cap is hit. We believe such an approach introduces needless complexity at the risk of consumer confusion without any added benefit. Further, this would require extensive, time-consuming and costly re-engineering of credit card platforms.

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We appreciate the opportunity to comment on the Proposed Rule. While we submit that the Proposed Rule, if adopted, would violate the APA, would fail to satisfy the requirements of TILA, and would raise significant public policy concerns, to the extent the CFPB decides to finalize the Proposed Rule, the effective date should be at least a year after publication in the Federal Register. This would be necessary, at a minimum, for card issuers to undertake massive system updates, implement sweeping portfolio management changes, and communicate with and provide notice to customers, to name just a few actions that would be required if the Proposed Rule is adopted.

If you have any questions or we can provide any additional information that may assist you in the rulemaking process, please contact Kathy Castle at kcastle@roundtables.us.

Respectfully submitted,

Auriemma Roundtables