May 3, 2023

Comment Intake- 2023 NPRM Credit Card Late Fees
c/o Legal Division Docket Manager
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC, 2052

Re: Proposed rule to "rein in excessive credit card late fees" (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15

Dear Director Chopra,

I appreciate this opportunity to respond to the Consumer Financial Protection Bureau's (the "Bureau") Notice of Proposed Rulemaking seeking information from credit card issuers, consumer groups, and the public regarding its proposed rule changes to credit card late fees and late payments.

Background

At the time of its passage, the Credit Card Accountability Responsibility and Disclosure Act of 2009 ("CARD" Act) CARD Act required the Board of Governors of the Federal Reserve System (the "Board") to issue rules establishing standards for assessing the reasonableness and proportionality of credit card penalty fees.[1] This authority transferred to the CFPB in 2011.[2] In issuing these rules, the Consumer Financial Protection Bureau (the "Bureau") **must consider** the four following statutory factors;

(1) the cost incurred by the creditor from an omission or violation;

(2) the deterrence of omissions or violations by the cardholder;

(3) the conduct of the cardholder; and

(4) such other factors deemed necessary or appropriate by the Board.[3]

The CARD Act also granted the Board discretion to provide an amount for any penalty fee or charge that is presumed to be reasonable and proportional to the omission or violation to which the fee or charge relates.[4] In establishing the current late payment amount rules, the Board gave ample consideration to typical collection costs, deterrence effect, and multiple late

[1] CARD Act section 102, 123 Stat. 1740 (15 U.S.C. 1665d(b)).
[2] Pub. L. 111–203, 124 Stat. 1376 (2010).
[3] CARD Act section 102, 123 Stat. 1740 (15 U.S.C. 1665d(c)).
[4] CARD Act section 102, 123 Stat. 1740 (15 U.S.C. (1665d(e)).

payments. The CFPB adopted both the safe harbor rule and the annual adjustment of the fees to account for inflation.

Pursuant to the CARD Act, the Bureau's Regulation Z (Reg Z) provides a "safe harbor" deemed statutorily compliant for a creditor to impose a fee of up to $30 for an initial late payment and up to $41 for a subsequent late payment within 6 billing cycles.[5] These limits adjust annually to account for inflation. Late fee amounts must not exceed 100 percent. These safe harbor limits increase annually according to the inflation rate. A creditor may impose a fee exceeding the safe harbor provisions only "if the card issuer has determined that the dollar amount of the fee represents a reasonable proportion of the total costs incurred by the card issuer as a result of that type of violation." [6]

The Bureau proposes significant changes to the existing late fee rules:

(1) Lowers the safe harbor dollar amount for late fees to $8 and no longer applies to late fees a higher safe harbor dollar amount for subsequent violations of the same type that occur during the same billing cycle or in one of the next six billing cycles.[7]
(2) The annual inflation adjustments for the safe harbor dollar amounts would not apply to the safe harbor amount for late fees.[8]
(3) Provides that late fee amounts must not exceed 25 percent of the required payment.
(4) "Clarifies" 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.

I. Reducing the safe harbor ceiling arbitrarily and capriciously harms the intended beneficiaries (both issuers and card holders) by incentivizing higher default and delinquency rates.

The CARD Act requires the Bureau to consider both the potential benefits and costs to consumers and covered persons, including the potential reduction of access by consumers to consumer financial products or services resulting from this rule.[9] Reducing the safe harbor ceiling arbitrarily and capriciously harms the intended beneficiaries by incentivizing higher default and delinquency rates. To the extent that late payments are incentivized, some consumers will end up with more credit delinquencies—and lower credit scores. Late fees—when set at a substantially high level—promote healthy financial habits. The lower credit scores stemming from more numerous late payments will diminish credit availability to delinquent consumers, limits on credit card awards, and also result in higher interest rates due to a

[5] 12 C.F.R. 1026.52(b)
[6] 12 C.F.R. 1026.52(b)
[7] 12 C.F.R. 1026.52(b)(1)(ii).
[8] CFPB Regulation Z, § 226.52(b)(1)(ii)(D)
[9] 12 U.S.C. § 5512(b)(2)(A).

negative risk profile. This will also disproportionately impact lower income borrowers who historically have higher delinquency rates. Some issuers may also choose to shrink the grace period for late payments, reduce the number of waived late fees, increase fees elsewhere, reduce rewards programs, and expand the application of penalty APRs. These changes may impact not only the delinquent accounts. All borrowers are forced to cover the costs of the delinquent.

Furthermore, reducing the safe harbor limits will force card issuers to more often choose between (1) conducting the cost analysis required by the Bureau to prove that the late fee imposed does not exceed the collection costs incurred to the issuer or (2). finding another mechanism to reduce the expense incurred when the collection costs on delinquent debt exceed the safe harbor allowance. Issuers may pass these costs along to the consumers or their shareholders.

The Bureau has acted arbitrarily and capriciously by failing to adequately consider the potential costs to issuers . The Bureau audaciously claims the proposed rule will "continue to save costs for most card issuers, by continuing to save them the administrative burden and complexity of using the [Bureau's] cost analysis provisions" while failing to even estimate the current cost of this administrative burden and the possible increase of this burden as more credit card issuers find it necessary to prove their collection costs exceed the safe harbor limits.[10]

The Bureau also acted arbitrarily and capriciously by failing to adequately consider the potential costs to consumers. The Bureau admits that "a lower late fee amount for the first or subsequent late payments might cause more consumers to pay late" and that it "does not have direct evidence on what consumers would do in response to a fee reduction."[11]

The Bureau provided no estimate of the potential costs to consumers incentivized to make poor credit decisions with these diminished late payment penalties. The Bureau speculates that "the more constrained cardholders" may benefit by using the late payment savings on principal repayment—but offers no actual statistical analysis of these predicted savings.[12]Ironically, the very research paper the Bureau relied upon in suggesting subprime borrowers may divert the late payment savings to principal reduction also found that lower late fees may indeed spur more late payments.[13] The Bureau concedes that issuers may make up for all lost revenue and potential cost increase by raising revenue through other price changes—including higher maintenance fees, lower rewards, or higher interest rates.[14]

The Bureau warns that its estimates of potential benefits and costs to consumers and card issuers "do not consider potential responses by consumers to lower late fees—in particular, the

[10] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 55.
[11] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 57.
[12] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 67.
[13] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 67.
[14] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 112.

possibility that consumers are more likely to miss a payment due date if the fee for doing so is reduced."[15] The Bureau admits that if consumers make more untimely payments, the costs uncured from increased penalty interest rates or lower credit scores "would affect the estimates above, as well as the final incidence of the benefits and the burden."[16]

This inability for the Bureau to even say whether consumers would be better or worse off on account of its rule underscores that the proposal is indeed arbitrary and capricious.

II. The Bureau arbitrarily and capriciously caps late fees at 25 percent of the required minimum payment due rather than the current cap of 100 percent.

The costs of mailing late notices and the labor expense of making phone calls to the consumer and documenting outreach attempts remain constant regardless of the minimum payment due. Typically, minimum payments for larger balances over $1000 are set at 2 percent of the balanced owed. For small balances, the minimum will typically be the smaller of the total principal balance or $25. A late fee cap equal to the minimum payment due ensures an issuer can collect the costs incurred either through the safe harbor limit or the cap at 100 percent of the minimum payment. As discussed elsewhere in this letter, a reduction in the allowable level of late fees erodes the deterrence effect of the late fee. The agency also fails to properly consider the impact on borrowers if issuers raise the minimum payment levels substantially on all borrowers (regardless of balance owed) to ensure 25 percent of any minimum payment will cover collection costs. This proposed 25 percent cap is an arbitrary and capricious change.

III. The Bureau arbitrarily and capriciously ceases to adjust the safe-harbor provision by the annual inflation rate.

The Agency fails to consider that failing to adjust the safe-harbor provision annually to account for inflation will force consumers to bear an increasing share of the costs from delinquent borrowers. Holding the safe harbor steady would have resulted in the safe-harbor cap declining by 15 percent in real terms since the beginning of 2020. As highlighted by the National Association of Federally-Insured Credit Unions, "Rising labor costs weigh on credit unions' margins and many have no choice but to pass part of this cost onto consumers, whether through late fees or higher costs for products and services for all members."[17] Freezing the safe harbor provision as costs rise is an arbitrary and capricious change.

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[15] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 110.
[16] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 111.
[17] Comment Intake—Credit Card Late Fees, Letter to the Consumer Financial Protection Bureau, NAFCU, August 1, 2022.
https://www.nafcu.org/system/files/files/8.01.2022%20NAFCU%20Comment%20Letter%20to%20CFPB%20re%20ANPR%20on%20Credit%20Card%20Late%20Fees.pdf

IV. **The Bureau arbitrarily and capriciously eliminates the higher safe harbor amount for subsequent late payment violations.**

The CARD Act requires that in assessing the reasonableness and proportionality of credit card penalty fees, the Bureau **must consider as one of the four statutory factors the conduct of the cardholder***.* A subsequent late payment in a six-month period is a more serious infraction than a solo infraction. Accordingly, the late fee presumed to be reasonable and proportional should be higher for a subsequent violation than an initial, solo violation. At the very least, the agency was required to explain why this difference in consumer conduct was irrelevant to the penalty amount, but it failed entirely to consider one of the factors Congress picked out for consideration. Indeed, the Board implemented the current rule allowing for such a higher safe harbor provision because generally consistent with the statutory factors of cost, deterrence, and consumer conduct."[18]

A higher safe harbor provision for subsequent late payments reflects the heightened importance of deterring multiple late payments and that multiple late payments are more deleterious to both the borrower and the card issuer. As explained by the Board in implementing the current rule, "…imposition of a higher fee when multiple violations occur will have a significant deterrent effect on future violations."[19] The Board also reasoned, "multiple violations during a relatively short period can be associated with increased costs and credit risk and reflect a more serious form of consumer conduct than a single violation."[20] This higher fee for repeat late payments allows card issuers to distinguish between those repeatedly violating terms of their agreement and those who are engaged in such recurrent behavior.

Now, the Bureau "preliminarily determines that a late fee amount of $8 for the first and subsequent late payments is presumed to be reasonable and proportional to the late payment violation to which the fee relates"—finding that an identical $8 amount for first and subsequent violations would "cover most issuers' costs from late payments."

The Bureau's rationale arbitrarily and capriciously deemphasizes the consumer conduct and deterrence considerations relied upon in issuance of the current rule. Eliminating the higher safe harbor amount for subsequent late payment violations arbitrarily and capriciously ignores the deterrent effect of this higher late fee. Elimination of the higher safe harbor amount also arbitrarily and capriciously ignores that consumer conduct in a repeated breach of contract is more egregious than an isolated breach. **The Bureau arbitrarily and capriciously excludes costs related to collecting charge-offs from its estimates in determining whether a credit card late fee is reasonable and proportional.**

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[18] 75 FR 37526, 37527 (June29, 2010).
[19] 75 FR 37533 (June29, 2010).
[20] 75 FR 37527 (June29, 2010).

For issuers seeking to levy late payment fees in excess of the safe harbor, a cost analysis is conducted to ensure the fee levied is proportional to the cost incurred.[21] After an extended delinquency, a card issuer typically "charges off" the account as a loss. However, an issuer does not relinquish its contractual rights to collect payment. Often, a card issuer authorizes a third party to purse payment on charged off accounts on the card issuer's behalf. If the third party collector is successful, the card issuer pays a commission to the third party based on the repayment amount. This commission is a very real cost of doing business for the issuer.

The Bureau arbitrarily and capriciously seeks to exclude collection costs that are incurred after an account is charged off in accordance with a loan loss provision (LLP). The Board claims it is merely "clarifying" the cost analysis rule. Because the issuer has already written the loan off for accounting purposes, the Bureau claims any expense in collecting on past due account AFTER a charge-off is "mitigating a loss as opposed to the cost of violation of the account terms."[22] [23]

Verbal gymnastics aside, the costs incurred by an issuer in furtherance of collecting an account written off for accounting purposes is still a very real costs incurred to collect on a past due account. The Bureau's attempted "clarification" arbitrarily and capriciously excludes these costs from the analysis, for the proposal fails to explain why the fact that an issuer has already written off the cost just for its own accounting purposes eliminates the fact that the issuer has still borne the cost of collecting these payments.[24] The commission paid by issuers to third parties to collect bad debt is an expense incurred to minimize actual loan losses. This exclusion of post charge-off costs from the cost analysis required by the Bureau in determining permissible late fee artificially reduces the estimated collection costs by 25 percent.[25]

V. The Bureau arbitrarily and capriciously disregards that collection costs for smaller issuers are potentially higher than larger issuers.[26]

The Bureau admits it does not have data for smaller issuers' pre-charge-off collection costs equivalent to its data on larger issuers. Regardless, the Bureau proposes to decrease the safe harbor provisions for smaller issuers in an identical manner to larger issuers. The Bureau flippantly dismisses these concerns, saying "has no reason to expect that smaller issuers exhibit substantially higher pre-charge-off collection costs than larger issuers." The Bureau mentions that smaller issuers (on a partial review of credit card issuers) generally impose lower fees than larger issuers as evidence that costs may actually be lower than large issuers. But the Bureau does not even make an attempt to show with substantive evidence that the costs for collection

[21] 12 C.F.R. 52(b)(1)(i)-1.

[22] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 29.

[23] Comment 52(b)(1)(i)-2.i provides that one such amount that cannot be considered as costs incurred for purposes of § 1026.52(b)(1)(i) are losses and associated costs (including the cost of holding reserves against potential losses and the cost of funding delinquent accounts). BUT this is much different than *collection* costs incurred!

[24] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 19.

[25] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 20.

[26] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 46.

are identical or lower to larger issuers. The Bureau even admits that the cost analysis from larger issuer data "may not be representative of smaller issuers."[27] Furthermore, smaller creditors and community banks will be especially impacted with proportionally higher compliance costs in proving collection costs exceed the safe harbor limits.[28] Decreasing the safe harbor provisions identically for both large and small issuers is arbitrary and capricious because the agency lacks adequate evidence to conclude that collection costs for smaller issuer are substantially the same as for larger issuers. The Agency should have considered evidence that the safe harbor changes will disproportionately impact smaller issuers, including warnings from some smaller issuers that these changes may limit their ability to participate in the credit card marketplace.

VI. The Bureau arbitrarily and capriciously deemphasizes the deterrence factor required by law to be considered in determining the reasonableness and proportionality of credit card late fees and arbitrarily dismisses evidence indicating a lower late fee will greatly diminish deterrence.

The CARD Act expressly requires the Bureau to consider the reasonableness and proportionality a credit card late fee as it relates to *the deterrence of omissions or violations by the cardholder* and the conduct of the cardholder (i.e., repeated late payments). Proportionality of the fee to the cost incurred Is just one of the factors to be considered in determining whether a fee is reasonable and proportional. Only if a card issuer seeks to impose a fee in excess of the safe harbor does the determination of the reasonableness or proportionality of the fee hinge solely on proportionality of the fee to the cost incurred. The current safe-harbor reflects the balancing of these considerations. The proposed rule arbitrarily and capriciously focuses on proportionality of the fee imposed to the cost incurred, deemphasizing proportionality in relation to deterrence and conduct of the cardholder.

Lowering the maximum fee by 75 percent, eliminating the annual safe harbor inflation adjustment, and eliminating the higher cap for subsequent late payments will undoubtedly lower the deterrence impact. The Bureau arbitrarily and capriciously fails to estimate or consider the extent of this deterrence diminishment.

The Bureau determined that the proposed $8 late fee safe harbor amount is still a "powerful deterrent" simply because an $8 fee on $40 payment 10 days past due is a 730 percent APR.[29] This is akin to arguing that lowering the daily fine on the late return of a $10 library book from

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[27] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 46.

[28] "…banks with assets of $1 billion to $10 billion reported total compliance costs averaging 2.9 percent of their noninterest expenses, while banks with less than $100 million in assets reported costs averaging 8.7 percent of their noninterest expenses." Drew Dahl , Andrew P Meyer , Michelle Clark Neely, "Scale Matters: Community Banks and Compliance Costs," Federal Reserve Bank of St. Louis, July 14, 2016, https://www.stlouisfed.org/publications/regional-economist/july-2016/scale-matters-community-banks-and-compliance-costs (accessed May 3, 2023).

[29] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 54.

$2 per day to 10 cents per day is still a "powerful deterrent" because annualized this fine exceeds 360 percent. A typical borrower will be far more inclined to return a book on time rather than hold onto it for an extra month is the fine is $60 vs $3 for that period.

The Bureau also counters the concern that deterrence will be diminished by insisting that the $8 fee will have "a" deterrent effect. This is a straw man argument. No one is arguing that a smaller fee will have "no" deterrent effect. The concern is that a significantly smaller fee will have a much *smaller* deterrent effect. Once again, the Bureau implies that so long as its late fee rules have "a" deterrent effect, this satisfies the statutory requirement that determination of the *reasonableness and proportionality of fees must take into consideration "the deterrence of omissions or violations by the cardholder."* The mere existence of "a" deterrent effect is not sufficient.

The Bureau arbitrarily and capriciously focuses primarily on the cost incurred by the creditor from an omission or violation—deemphasizing the deterrence of omissions or violations by the cardholder and the conduct of the cardholder. The Bureau admits that its collection cost analysis does "not take into account the possibility that reduced late fees will lead to more late payments."[30] The Bureau then seeks to allay issuer concerns by claiming that an increase in the frequency of late payments as a result of the decrease in late fees may increase fee income.[31] In other words, the Bureau admits both that lowering the allowed late payment fees might have the dual impact of increasing frequency of delinquency and sparking an increase in fee income. The Bureau further admits that "late fees are a cost to consumers of paying late, and a lower late fee amount for the first or subsequent late payments might cause more consumers to pay late."

The Bureau claims that it "does not have direct evidence on what consumers would do in response to a fee reduction similar to those contained in the proposal."[32] The Bureau dismisses an ANPR survey from 2010 showing fees of $40-$46 are the threshold which late fees must reach to deter majority.[33] The Bureau also rejects a 2022 research paper showing that the limits imposed under current rule (initially implemented in 2010) increased the likelihood a cardholder paying late.[34] The Bureau claims this study does not constitute "robust evidence" that the $8 fee would not have "a" deterrent effect[35] and discounts the study results ostensibly because "the causal attribution of an increase in late payments to a reduction of the late fee amount is hard to prove due to the general economic uncertainty around that time." Specifically, the Bureau claims the U.S. economy was still dealing with the aftermath of the Great Recession. Yet, the paper shows an increase in delinquencies during an economic

[30] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 47.
[31] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 47.
[32] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 52.
[33] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 58.
[34] Grodzicki, D., Alexandrov, A., Bedre-Defolie, Ö. *et al.* Consumer Demand for Credit Card Services. *J Financ Serv Res* (2022). https://doi.org/10.1007/s10693-022-00381-4.
[35] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 55.

recovery, not during a recession.[36] The Bureau discards the data by misconstruing the time frame as a period of economic uncertainty. But the Great Recession ended in the summer of 2009 with more than 1 million jobs added in 2010 and more than 2 million jobs added in 2011. Mortgage delinquencies fell in both years.[37] To be clear, in a period of economic growth after the implementation of the fee caps, the frequency of credit card late payments grew. The Bureau arbitrarily and capriciously disregards the results of both studies that suggest lower the late fee limits will significantly diminish deterrence.

The Bureau's failure to "cogently explain why it has exercised its discretion in a given manner" violates the Administrative Procedure Act and is thus arbitrary and capricious.

Sincerely,

Joel Griffith

[36] Proposed Rule, Credit Card Penalty Fees (Regulation Z); Docket No. CFPB-2023-0010 or RIN 3170-AB15, p. 55.
[37] Board of Governors of the Federal Reserve System (US), Delinquency Rate on Single-Family Residential Mortgages, Booked in Domestic Offices, All Commercial Banks [DRSFRMACBS], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/DRSFRMACBS , March 27, 2023.