

REG Z PROPOSAL ISSUED TO ACCOMPLISH SECOND STAGE IMPLEMENTATION OF CREDIT CARD ACT

The second state of implementation of the *Credit CARD Act* (the Act) is scheduled to take effect February 22, 2010. The time between the signing of the law in May and the first effective date of August 20, 2009, was so short the **Federal Reserve Board** (FRB) issued an interim final rule to implement those provisions. This proposed rule (the Rule) would implement the provisions of the Act that go into effect on February 22, 2010. This proposal also republishes portions of the final rules amending Regulation Z's (*Truth in Lending*) provisions regarding open-end credit that was published in the *Federal Register* on January 29, 2009. Finally, the proposal also republishes several proposed amendments to the January 2009 Reg Z rule that were originally published in the *Federal Register* on May 5, 2009.

This article provides a high level summary of the Rule. Understanding the organization can make studying the Rule easier. For example:

- Subpart A contains general information.
- Subpart B contains the rules for open-end credit. It requires that account-opening disclosures and periodic statements be provided, as well as additional disclosures for credit and charge card applications and solicitations and for home-equity plans subject to the requirements of Section 226.5a and 226.5b, respectively. It also describes special rules that apply to credit card transactions, treatment of payments and credit balances, procedures for resolving credit billing errors, annual percentage rate calculations, rescission requirements, and advertising. (Begins on page 332 at <http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20090929a1.pdf>).
- Subpart C relates to closed-end credit.
- Subpart D contains rules on oral disclosures, disclosures in languages other than English, record retention, effect on state laws, state exemptions, and rate limitations.
- Subpart E contains special rules for certain mortgage transactions.
- Subpart F relates to private education loans.
- Subpart G relates to credit card accounts under an open-end (not home-secured) consumer credit plan except for Section 226.57(c) which applies to all open-end credit plans).

Major Provisions

There are several items of interest among the major provisions. Those include:

- One item of good news -- *the minimum payment warning language will only apply to credit card accounts* under an open-end plan. Originally, this was to apply to all open-end credit based on the wording of the Act.
- The periodic statement requirement to disclose a payment due date and information about late payments -- *will only apply to credit card accounts* rather than all open-end credit as was the case in the January 2009 rule.
- Another item to be aware of -- this Rule *eliminates what appeared to give the consumer the right to cancel* any proposed interest rate hike for credit card accounts. The FRB explains that due to other protections created by the Act, a consumer that rejects an increased APR really does not gain any substantive rights. Consumers may think that rejection blocks the increase while allowing them to use the card with no affect. That, of course, is not the case.

- On a related note -- the **National Credit Union Administration** (NCUA) issued Regulatory Alert 09-RA-10 explaining that when accredit union *changes material terms or increases an APR* it must give 45-days notice. Once the notice has been mailed; however, the credit union can begin charging the higher rate or implement the new significant term 14 days after they mail the change-in-terms disclosure. While the credit union is not required to notify members about the 14-day provision, the NCUA suggests that credit unions disclose this fact by inserting the following language in the notice:

NOTE: Even if you reject this change in terms, the new terms will be applied to any transactions on your account that occur on or after {Insert Date}.

This relates to Section 226.55.

Increases in APRs, Fees, and Charges (226.54)

The rule would prohibit creditors from applying increased annual percentage rates (APRs) and certain fees and charges to *existing credit card balances*, except in the following circumstances:

- When a temporary rate lasting at least six months expires.
- When the rate is increased due to the variable-rate nature of an account.
- When the minimum payment has not been received within 60 days after the due date.
- When the consumer successfully completes or fails to comply with the terms of a workout arrangement.

Also, when an APR has been reduced pursuant to the *Servicemember Civil Relief Act* (SCRA), the creditor can increase the APR when the SCRA provisions no longer apply.

With regard to new transactions, the APR cannot be increased during the first year after an account is opened. After the first year, creditors would be permitted to increase APRs that apply to new transactions as long as the 45-day advance notice requirement is met. (Section 226.52)

Evaluation of Consumer's Ability to Pay (226.51)

The proposal would require a creditor to determine that a consumer has the ability to make the minimum payments required to repay the debt under the terms of the agreement before opening a new account or increasing the credit limit.

Since the creditor will not know the amount of minimum payments at the time the consumer's ability is being evaluated, the proposal would require creditors to use a reasonable method for estimating the ability to pay. The Rule would provide a safe harbor for creditors to satisfy this requirement which would provide that it is reasonable to estimate minimum payments based on the consumer's utilization of the full credit line and using the minimum payment formula used by the creditor based on the credit card product for which the consumer is being considered.

The Rule would clarify that the creditor's review to determine the consumer's ability to pay must include a review of the consumer's income or assets as well as current obligations. The creditor must have policies and procedures in place for this process.

Fees or Charges for Transactions that Exceed the Credit Limit (226.56)

The Rule will require creditors to obtain a consumer's consent before assessing over-the-limit fees. Specifically, the Rule would require creditors to:

- Have the consumer's express consent before charging the over-the limit-fee. Before obtaining consent, the creditor must disclose the amount of any fee and any possible increase in the APR if the member goes over the limit. The consent only has to be obtained once.
- Get separate consent. In other words, the consent to the over-the-limit fee cannot be combined with the applications' signature line.

- Provide notice of the right to revoke the consent on any periodic statement showing an over-the-limit fee.
- Apply this to the entire credit card portfolio. Existing account holders are *not* grandfathered.
- Limit fees to no more than one over-the-limit fee per cycle. If the member goes over the limit, you can only charge a fee for that over-the-limit transaction for three billing cycles, if the consumer remains over the limit.

The rule includes a comment that clarifies that if the credit has a policy and practice not to pay or authorize transactions that are reasonably believed to result in the consumer being over his/her limit, the credit would not be subject to these over-the-limit requirements. A few more exceptions apply, including prohibiting the creditor from:

- Assessing an over-the-limit fee or charge that is caused by the creditor's failure to promptly replenish the consumer's available credit.
- Conditioning the amount of available credit on the consumer's consent to payment of the over-the-limit transactions.
- Imposing any over-the-limit fees to charges if the credit limit is exceeded solely because of the creditor's assessment or charges, including accrued interest charges on the consumer's account.

On-line Disclosure of Credit Card Agreements (226.58)

The Rule would require creditors to post on its web site or otherwise make available its credit card agreements with its current cardholders and submit the agreements to the FRB. There would be two limitations to sending the agreements to the FRB. First, there would be a de minimis exception for creditors with fewer than 10,000 credit card accounts. Second, creditor would not be required to submit agreements that are not currently offered to the public.

Double Cycle Billing

The Rule prohibits creditor from imposing finance charges on balances for days in the previous billing cycles as a result of the loss of a grace period. When a consumer pays some but not all of a balance prior to expiration of a grace period, the creditor is prohibited from imposing finance charges on the portion of the balance that has been repaid.

Limitations on Fees (226.55)

The Rule would prohibit a separate fee to be charged for accepting payment on a credit card account unless the payment was processed in an expedited manner by a customer service representative. This prohibition would cover payments by telephone (including voice response unit), online, or through the mail. The Rule would limit fees, other than late payment, returned payment, and exceeding the limit fees, to 25 percent of the initial credit.

Minimum Payments & Allocation of Payments (226.53)

Minimum payments – for *credit card accounts only*, the Rule would require the following new disclosures on the periodic statement:

- The amount of time and the total cost (interest and principal) involved in paying the balance in full making only the minimum payments; and
- The monthly payment amount required to pay off the balance in 36 months and the total cost (interest and principal) of repaying the balance in 36 months.

Under the Rule, Home Equity Lines of Credit (HELOCs) and overdraft lines of credit are exempt from the minimum payment disclosure even if accessed by credit cards. General purpose lines of credit are exempt as well.

The minimum payment disclosure related to 36 months is not required if the repayment period is three years or less or if there is negative amortization.

Allocation of payments – if the payment includes funds in excess of the minimum requirement, that amount shall be allocated first to the amounts subject to the highest interest rate. The remaining amount shall be allocated to the balance with the next highest interest rate, etc.

Comments Due

Comments are due November 20. The complete proposal can be read at <http://edocket.access.gpo.gov/2009/pdf/E9-23733.pdf>.