

Consumer Action

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Jennifer J. Johnson,
Secretary Board of Governors of the Federal Reserve System
20th St., & Constitution Ave., NW
Washington, DC 20551

Sept. 25, 2007

Re: Docket No. R-1286

Via U.S. Mail and E-Mail

Dear Members of the Federal Reserve Board of Governors:

Consumer Action¹ commends the board for its extraordinary efforts to amend Regulation Z. The work you have done has resulted in some sorely needed improvements to the disclosures required for open-end (revolving) credit products, including credit cards. These enhanced disclosures and advertising requirements will provide consumers with greater access to some of the key information they need to make informed credit decisions.

However, we would like to point out that while better credit disclosure may permit better-informed credit decisions, all the disclosure in the world cannot protect consumers from unfair and deceptive practices in the marketplace. Disclosure alone will never replace strong laws to protect consumers.

We urge the board to adopt its suggested improvements providing for:

- Tabular, standardized disclosure notices not only in solicitations but also in initial account opening agreements and in monthly periodic statements.

¹ Consumer Action (www.consumer-action.org) is a national non-profit consumer education and advocacy organization founded in San Francisco in 1971. The organization's hallmark is its free multilingual consumer education materials distributed through a national network of 9,000-plus non-profit and community-based agencies. In addition, Consumer Action serves consumers and its members nationwide by advancing consumer rights, referring consumers to complaint-handling agencies and training community group staff on the effective use of its educational materials. Each year, Consumer Action distributes more than 2 million pieces of its free consumer education materials through these groups. Consumer Action also advocates for consumers in the media and before lawmakers and compares prices on credit cards, bank accounts and long distance services. Its newsletter, *Consumer Action News*, is published several times a year and contains articles of general interest to consumers as well as news of the organization. All Consumer Action publications are available on its free web site (www.consumer-action.org).

- More lead time for notices of changes in terms. We believe the notice clock should start ticking at receipt not from the date the notice is "sent." Because date of receipt may be hard to predict, we urge you to amend the advance notice to 60 days if it is timed from the date the notice is sent.
- Advance notice of *at least* 45 days before any issuer may impose a penalty rate. Again, we urge the Board to amend the advance notice to 60 days if it is timed from the date the notice is sent.
- Adding penalty type fees (late/over limit) to the effective APR, or "fee inclusive APR" on billing statements.
- Protections for subprime credit card customers.
- Improvements in advertising requirements.
- Prohibit imposition of penalty fees and rates if they are based on an approval of a charge or other action by an issuer.

In addition, we urge the board to:

- Ban the use of unilateral change-in-terms within the card's effective contract period. Changes in terms, upon renewal, should apply only to future purchases—not on existing balances.
- Require a meaningful opt-out if cardholders don't accept change of terms. Don't give consumers a Hobson's choice of having to pay the entire balance or pay the entire balance at a higher rate of interest. This encourages default by consumers. Allow consumers the opportunity to pay off the balance—over time—under the original rate and terms.
- Require that a card never be issued until the consumer has been given the opportunity to accept the card's interest rate and credit limit. During the underwriting process for "unknown" customers (online, take-one, etc.) the applicant should have a chance to accept a specific interest rate and credit limit *before* the card is issued.
- Stop late fees for payments mailed on time. Employ postmark dates, time stamps, electronic time stamps or any other method that is easily and independently verifiable by the consumer.
- Prohibit over-limit fees when issuer approves transaction.

Below Consumer Action presents specific comments on the Regulation Z proposal:

Applications and Solicitations

- ***Disclosure for how long penalty rates will be in effect.*** While we support such a disclosure in general, we find that the Board's willingness to allow issuers to state that the penalty rate could apply indefinitely is a poor idea. We believe that in any situation in which a consumer is being "punished" for a perceived transgression, companies must offer a foreseeable forgiveness period in which cardholders can "pull up their socks" and regain the lower rate by making on time payments. Penalty rates that last longer than six months should be prohibited if the consumer has made six on-time monthly payments since the rate was increased.

- **Payment allocation practices disclosure.** The Board is concerned that consumers do not realize that they lose their grace period when they transfer a balance in order to take advantage of a lower interest rate. The Board proposes to alert consumers that they will pay interest on their purchases until the transferred balance is paid in full. This is crucial information, but Consumer Action believes it does not convey an equally important point about payment allocation—that it allows higher-interest portions of the balance to compound more quickly as they are unencumbered by any payments until the lower-rate balance is paid in full. The notice should point out: “You will have to pay off your low-interest balances in full before your payment is used to satisfy your higher-interest balances, such as purchases or cash advances. Meanwhile all payments will be applied to the low-rate portion of your balance, and your higher rate balances will continue to accrue interest, extending the time it will take you to repay your debt.”

- **Subprime cards:** We applaud the Board’s proposal to insure that applicants for subprime cards with high fees and low credit limits be notified if upfront fees reduce the available credit limit. You propose to alert consumers if the fees required to receive the card are 25% or more of the minimum available credit limit. Consumer Action believes the disclosure threshold would better serve cardholders if it was triggered when upfront fees exceed 10% or more of the minimum available credit limit. We also recommend that the fees and available balance should be highlighted in full size, bolded print in solicitations and initial account disclosures—not in fine print footnotes. We highly recommend that new cardholders be given a specific “opt out” period in which they can rescind the agreement, close the card and be relieved from the responsibility of paying the fees. This would allow anyone who did not understand the deal they were getting into, to opt out without liability.

Account Opening Disclosures

- **Oral approach to disclosing fees:** We do not support any allowance for solely disclosing any fees, policies or terms via oral disclosures. Creditors should not at any time have a choice to disclose important account opening information orally, such as, but not limited to, APRs, fees, payment requirements, penalty rate practices or change-in-terms provisions, unless the company provides or points to an independent, easily verifiable written disclosure that the consumer can use to double-check the information. Consumer Action’s credit card surveyors have found that when representatives give the answers to important questions about credit card terms and these answers cannot be independently validated via a written source, it results in a confusing array of inaccurate and misleading information. Oral disclosures should occur only in addition to easily verifiable, written and retainable disclosures.

- **Future fees, practices and account terms.** We urge the board to provide flexibility in its rules so that that new fees or heretofore-unused account terms or practices must also be disclosed in writing and with the same notice requirements for any change in terms.

Periodic Statement Disclosures

- ***Late payments:*** In addition to the Board’s proposal to alert consumers to the consequences of paying late, Consumer Action recommends that consumers are given a prominent disclosure if and when penalty APRs are applied, if the higher rate will be applied retroactively to the entire balance (a practice we adamantly oppose) and will immediately increase the cost of carrying a balance.

- ***Proof of late payments is needed.*** Along with the due date, Consumer Action recommends that consumers be given a firm “mail by” or “postmarked by” date. This is a simple solution to a chronic problem. If the IRS accepts this system to determine late tax filings, then it can be made to work for the credit card industry.

- ***Totals for fees and interest rates, monthly and year-to-date.*** Consumer Action urges the board to require creditors to disclose the (1) total fees and (2) total interest imposed for the cycle—whether or not changes are made to the effective APR concept. Providing year-to-date totals for interest charges and fees in dollars would provide consumers with the overall cost of their credit account on an annualized basis.

- ***Fee-inclusive APR.*** Consumer Action does not support complete elimination of the disclosure of “effective APR.” Instead, we support the Board’s proposal to revise the concept as “fee inclusive APR.” Additionally, we urge the Board to include penalty type fees (late, over-limit, etc.) in its “fee inclusive APR” designation.

Consumer Action strongly urges the Board to categorize over-the-credit limit fees as finance charges, because they are a cost associated with using a credit card. In processing charges that exceed the credit limit instead of rejecting them at the time of verification, banks are capitalizing on a loophole that allows them to reap repeated additional monthly profits from a situation they could easily control.

- ***Cut off times before 5 p.m.*** Disclosure of an early payment deadline on the due date does not protect consumers from this deceptive practice. Consumer Action suggests that the Board prohibit this practice outright. A due date should be a due date. The current proposal to disclose cut-off times before 5 p.m. could lead to confusion unless it specifies 5 p.m. Pacific Time. If creditors interpreted the requirement to be 5 p.m. Eastern Time, consumers to the West would be not be treated equally and would not have until the close of business to submit payments.

- ***Minimum payment warning.*** Under the proposal, credit card issuers must provide (1) a “warning” statement indicating that making only the minimum payment will increase the interest the consumer pays and the time it takes to repay the consumer’s balance; (2) a hypothetical example of how long it would take to pay a specified balance in full if only minimum payments are made; and (3) a toll-free telephone number that consumers may call to obtain an estimate of the time it would take to repay their actual account balance using minimum payments.

Consumer Action strongly urges the Board to require an actual, personalized calculation, not a hypothetical one, on each statement, showing exactly how long it would take to repay the current month's balance if the cardholder made only the minimum payment. Consumer Action believes that most consumers will not call the toll-free number and that a personalized example each month on the periodic statement would encourage them to pay more than the minimum.

- ***Minimum calculation formula.*** Consumer Action urges the board to require a disclosure of how the minimum monthly payment will be arrived at in solicitations and initial disclosures. While some creditors provide this information voluntarily, the Board can standardize the disclosure and allow consumers to understand what portion of principal balance repayment is being included in the minimum payment.

Changes in Consumer's Interest Rate and Other Account Terms

- ***Advance notice of changes in terms and the imposition of penalty or risk-based changes in rates or terms.*** While we maintain that adverse changes should not be allowed during the life of a contract, Consumer Action does agree with the Board that much more time than the current 15-days is needed to warn consumers of changes in terms and we support the Board's intention to warn consumers before they get hit with adverse, risk-based or penalty changes in terms. However, we believe the notice clock should start at receipt, not from the date the notice is sent. Because date of receipt may be hard to predict, we suggest the advance notice be 60 days if timed from when it is sent.

Ban issuer-caused penalty fees and rates. Consumer Action believes that if an issuer's actions result in a penalty, the cardholder should not be obliged to pay the punitive fee or rate. For instance, if an issuer lowers a cardholder's credit line, which results in putting the consumer's balance over the limit, the issuer should be banned from imposing a penalty fee or raising an interest rate based on the issuer's actions.

- ***A real opt-out.*** Consumer Action urges the Board to go further and require meaningful opt-out of risk-based pricing increases. Consumers already have the option to pay off the entire balance and close the card, however many consumers are trapped because they can't afford the pay-off amount. We would like to see every consumer be given the option to convert the revolving account to a closed end account and pay off the balance over time at the old rate. This would actually reduce the risk to the creditor because the consumer can no longer make new charges.

Advertising Provisions

- ***Use of minimum payment in advertising.*** If a minimum monthly payment is advertised on a plan offered to finance the purchase of goods or services, the Board proposes that it must also state with equal prominence the time period required to pay off the balance and the total number of payments. Consumer Action suggests that the Board also require such

prominent disclosure when credit offers are interest free for a certain number of months or years, but retroactive interest charges will be triggered if the debt is not paid in full by the promotion's end.

- **Fixed rates.** If an advertisement refers to a temporary fixed rate, it must also specify how long the fixed rate will remain in effect. We ask the Board not to allow an exception to this rule for "penalty" provisions, such as late payments, over limit or bounced payment checks. We urge the Board to insure that if a time period is not specified, the creditor cannot increase the rate for any reason while the account is open, including "penalty" provisions, such as late payments, over limit or bounced payment checks.

Model Forms and Formats

Consumer Action applauds the board for its vast improvements and new requirements for model formats on applications and solicitations, account opening agreements and periodic statements.

We are especially enthusiastic about the proposed requirement that credit card issuers offering cards on the Internet must include the same tabular summary of key terms that is currently required for applications or solicitations sent by direct mail. We urge the Board to require that these tabular summaries of key terms be given equal prominence to the marketing of so-called card "benefits." We urge the requirement to go further to ensure that electronic disclosures be current and should never be available to consumers if they are out of date. All publicly available electronic disclosures should be accurate. Applicants must be able to rely on the information presented. The disclosures that were available on the date of application should be honored, even if the posted terms have expired and even if the disclosures carry an out-of-date "good thru" date.

Additionally, we urge the Board to ensure that consumers who choose to access their actual credit account online be provided with an online version of the original account opening documents and contractual terms that govern their use of the card. As the Board is no doubt aware, many cardholders throw out these important documents and it would be of great value to have immediate and continuous online access to the cardholder agreement.

Other Disclosures and Protections

- **Convenience checks.** The proposed revisions would require that checks mailed by card issuers be accompanied by interest rate and fee cost disclosures. The Board has proposed that the cost disclosures appear in a table on the front side of the page containing the checks. Consumer Action suggests that a notice be printed directly on the check under the signature line: "The use of this check will trigger immediate interest and additional fees."

- **Credit insurance, debt cancellation, and debt suspension coverage.** Under the proposal, the existing rules for debt cancellation coverage would also be applied to "debt

suspension” coverage (for both open-end credit and closed-end transactions). Under the proposal, to exclude the cost of debt suspension coverage from the finance charge and APR, creditors must inform consumers that the coverage suspends, but does not cancel, the debt. Consumer Action recommends that during any period that interest is accruing under a debt suspension plan, consumers should receive monthly periodic statements that clearly show the current balance and, broken out specifically, the cost of the accrued interest **in dollars**.

Concluding Points

Consumer Action recommends that the Board give consumers stronger protections to deter illegal acts. We call upon the Board to ban the use of pre-dispute binding mandatory arbitration. No consumer should be forced to waive his or her right to a court trial as a condition of using a credit card.

The Board must facilitate stronger penalties for companies that violate the Truth in Lending Act. We recommend that aggrieved consumers be given a private right of action to enforce the Federal Trade Commission Act to challenge unfair or deceptive practices by businesses, including banks.

If the Board does not believe that its powers include the ability to make these must needed changes, Consumer Action recommends it communicate the need for these improvements in consumer protection to Congress.

As noted earlier in these comments, disclosure alone will never replace strong laws to protect consumers. At our consumer assistance hotline, Consumer Action sees first hand how damaging unfair and deceptive credit policies can be to consumers.

Sincerely,

A handwritten signature in cursive script that reads "Linda Sherry".

Linda Sherry
Director, National Priorities
Consumer Action