



CFPB RELEASES CARD ACT REPORT

The Consumer Financial Protection Bureau recently issued its 102-page first CARD Act Report, dated October 2013 ("Report"). The Credit Card Accountability Responsibility and Disclosure Act of 2009 ("CARD Act") requires a review of the consumer credit market every two years. The Report examined the credit card marketplace, including:

- The terms of credit card agreements and practices of credit card issuers;
- The effectiveness of disclosure of terms, fees, and other expenses of credit card plans;
- The adequacy of protections against unfair or deceptive acts or practices relating to credit card plans; and
- Whether or not, and to what extent, the implementation of the CARD Act has affected (i) cost and availability of credit, particularly with respect to non-prime borrowers, (ii) the safety and soundness of credit card issuers, (iii) the use of risk-based pricing, or (iv) credit card product innovation.

Agreements, Disclosures and Issuer Practices

This Report focused on (i) the presentation of terms and the readability of documents, (ii) periodic statement disclosure and the minimum payment warning required by the CARD Act and (iii) risk-based pricing and interest rate reviews. The CFPB found that cardholder agreements became more streamlined and readable between 2008 and 2012, with the average word count dropping 24.4% and the Flesch readability score increasing from 49 to 55.3 during that time. The minimum payment warning on periodic statements demonstrated some effect in reducing the number of consumers making only the minimum payment, but more research is needed, the CFPB said. The CFPB found that risk-based pricing continued between 2008 and 2012. Finally, with respect to interest rate reviews, the CFPB estimates savings to consumers of \$2.1 billion during the period analyzed based on rate reductions resulting from required reviews.

Cost of Credit

Consumers pay for credit in a number of ways, including the payment of penalty fees (e.g., overlimit and late payment fees), annual (or monthly) fees, other fees (e.g., cash advance, balance

transfer and foreign transaction fees) and interest. The Report details the impact of the CARD Act on each of these components of pricing.

The CFPB found that the CARD Act had its most direct and immediate impact with respect to overlimit fees. The Report details the two changes made by the CARD Act with respect to overlimit fees — requirements for consumer opt-in and fees that are reasonable and proportional to the violation. As a result of these changes, the CFPB found that most issuers simply stopped charging overlimit fees. The Report estimates the savings to consumers in overlimit fees in 2012 to be \$2.5 billion. The Report also discusses the changes required by the CARD Act to late payment fees and the subsequent overall decrease in such fees, which the CFPB estimates as saving consumers an estimated \$1.5 billion.

With respect to annual (or monthly) fees, the CFPB found an increase in both the amount and incidence of the fees. These changes resulted in an additional cost to consumers estimated at \$475 million in 2012. Still, the Report notes that because an annual fee is certain (as distinct from back-end overlimit and late fees), its incurrence makes it easier for consumers to anticipate costs. The Report states that the CFPB views the increase in annual fees following implementation of the CARD Act as part of a shift away from complex and often confusing pricing to pricing that is more predictable and transparent for consumers.

With respect to other fees, the CFPB found that the largest dollar amount of "other fees" comes from debt suspension (45% of all other fees), with balance transfer fees and cash advance fees representing 25% and 20%, respectively, of all other fees. On a per-active account basis, other fees rose from \$1.35 in 2008 to \$1.75 in 2012.

With respect to repricing of interest rates, the Report notes that the CARD Act sharply curtailed repricing practices. In particular, the CARD Act placed strict limitations on applying interest rate increases to existing balances, requires certain disclosures before rates can be increased with respect to new and existing transactions and requires account review at specified intervals after rates are increased. Although the CFPB admits some limitations in the data, it estimates that the incidence of repricing has declined to a quarterly rate of 1.5% in 2012 from 6.4% in 2008. Overall, the Report calls the decline in APR repricing as a result of the CARD Act meaningful.

Darrell L. Dreher
ddreher@dtllaw.com

Judith M. Scheiderer
jscheiderer@dtllaw.com

Elizabeth L. Anstaett
eanstaett@dtllaw.com

Charles V. Gall
cgall@dtllaw.com

2750 HUNTINGTON CENTER
41 S. HIGH STREET
COLUMBUS, OHIO 43215
TELEPHONE: (614) 628-8000 FACSIMILE: (614) 628-1600
WWW.DTLTAW.COM

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Michael C. Tomkies
mtomkies@dtllaw.com

Margaret M. Stolar
mstolar@dtllaw.com

Robin R. De Leo
robin@dreher-la.com

Susan L. Ostrander
sostrander@dtllaw.com

Susan M. Manship
smanship@dtllaw.com



Availability of Credit

The Report addressed whether changes in the availability of credit can be attributed to the CARD Act. The CFPB noted that making such a determination was challenging and required looking at a number of metrics, including (i) supply and demand, which considered overall solicitations, new account originations, subprime solicitations and new accounts, new accounts for students and young adults, new account originations across consumer credit markets, approval rates, and new line size, and (ii) total credit line, which considered a time series overview of total extended credit line, drivers of change in total credit line for consumer cards, and drivers of change in total credit line for small business cards. The CFPB found that less credit is available now than in 2007, especially in the subprime market. But, it also found no evidence that the CARD Act caused the reduction in available credit, other than the few areas in which the CARD Act was intended to restrict access (*e.g.*, students and young people and consumers without the ability to pay).

Adequacy of Protections

The Report highlighted the following areas that the CFPB believes may pose risks to cardholders and require further attention:

- Add-on products, including debt protection, identity theft protection, credit score monitoring and other supplementary products;
- Fee harvesting, particularly the use of application fees in connection with account opening;
- Deferred interest products, particularly whether additional action is necessary to promote a more fair and transparent market; and
- Transparency issues, including disclosures on online payment portals, rewards and transparency of grace periods.

These issues were emphasized in Director Cordray's remarks in Chicago and follow several high profile consent orders involving the CFPB and the Office of the Comptroller of the Currency on related topics. *See, e.g.*, our ALERTS of September 24, 2013, July 23, 2012 and July 19, 2012. □

✧ *Mike Tomkies and Margaret Stolar*