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May 3, 2023

Via Electronic Mail

2023 NPRM Credit Card Late Fees
c/o Legal Division Docket Manager
Consumer Financial Protection Bureau
1700 G Street, N.W.
Washington, DC 20552

Re: **Notice of Proposed Rulemaking**
Credit Card Penalty Fees (Regulation Z)
Docket No. CFPB-2023-0010

Dear Sir or Madam:

We are writing with respect to the Consumer Financial Protection Bureau's Notice of Proposed Rulemaking regarding Credit Card Penalty Fees (Regulation Z) (the "Proposed Rule").[1] Paul, Weiss, Rifkind, Wharton & Garrison LLP[2] submits these comments on behalf of several clients that are major credit card issuers.

The Proposed Rule contemplates two dramatic changes to the provisions of Regulation Z that regulate credit card late fees: (1) a reduction of the credit card late fee safe harbors, from $30 for a first violation and $41 for subsequent violations within six billing cycles, to $8 for any and all violations and (2) a cap on the amount of the late fee, at 25% of the minimum payment. In addition, the Proposed Rule seeks comment on whether to require a 15-day courtesy period before a late fee can be imposed.

The Proposed Rule would have significant and severe consequences for both the industry and the consumers the Bureau seeks to protect. The Proposed Rule would undermine the deterrent value of late fees and remove an important incentive for consumers to pay their bills on time, necessarily resulting in increased delinquencies. Credit card

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1 Credit Card Penalty Fees (Regulation Z), 88 Fed. Reg. 18906 (proposed Mar. 29, 2023).
2 Paul, Weiss, Rifkind, Wharton & Garrison LLP is an international law firm of over 1,000 lawyers that represents a wide variety of clients, including many financial institutions. Brad S. Karp is the chairman of the firm. Roberto J. Gonzalez leads the firm's CFPB practice and previously served as Principal Deputy General Counsel and Deputy Associate Director of the CFPB.

issuers, which incur substantial risk in lending to consumers on an unsecured basis, use late fees as an important risk-mitigation tool for customers who may not be attentive to making timely payments or may prioritize other spending. Restricting the use of this tool would force credit card issuers to identify alternative means to manage the overall risks of their credit card portfolios and recoup the costs associated with late payments from the riskiest borrowers, likely resulting in increased borrowing costs—in addition to reduced access to credit—for a wide range of consumers, including both those who pay on time and those who pay late.

These changes—in addition to other negative consequences customers would experience from increased late payments, such as reductions in their credit scores—mean that the Proposed Rule would, on balance, have a harmful impact on consumers. Below, we describe several substantive and procedural concerns with the Bureau's proposal to hastily revisit the existing regulations that have successfully implemented the CARD Act for over a decade.

A. The CARD Act Defines a Late Fee as a "Penalty," Which Encompasses More than Costs Alone.

In passing the CARD Act, Congress chose language that makes clear that credit card late fees do, and should, encompass more than an issuer's recovery of costs incurred as a result of a late payment. Credit card agreements are contracts; late payments are breaches of those contracts. And while damages for breach of contract ordinarily do not include penalties,[3] Congress understood the unique role of credit cards in expanding consumer access to credit—exposing credit card issuers to a degree of risk that justifies a unique damages regime. Moreover, the CARD Act purposefully removed other rights and remedies that existed at common law, seeking to balance consumer interests with safe and sound banking interests in order to ensure fair and transparent products and responsible consumer use. The CARD Act provides in Section 1664d(a) that "any *penalty* fee . . . in connection with any omission with respect to, or violation of, the cardholder agreement, including any late payment fee . . . shall be reasonable and proportional to such omission or violation."[4] The term "penalty" was no accident; Congress could have omitted this term if it conceived of late fees as revolving around cost.[5] And in fact, in Section 1665d(c), Congress made clear that cost is only one of among several grounds justifying late fees.[6]

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[3] Indeed, penalties are unusual where a party has breached an agreement. *See, e.g.*, *C.I.R.* v. *Schleier*, 515 U.S. 323, 343 (1995) (O'Connor, J., dissenting) ("Punitive damages are traditionally available only in tort." (citing 3 D. Dobbs, Law of Remedies 118 (2d ed. 1993) ("The rule against punitive damages prevails even if the breach [of contract] is wilful or malicious, as long as the breach does not amount to an independent tort"))).

[4] 15 U.S.C. § 1665d(a) (emphasis added).

[5] *See BedRoc Ltd., LLC* v. *United States*, 541 U.S. 176, 183 (2004) ("The preeminent canon of statutory interpretation requires us to 'presume that [the] legislature says in a statute what it means and means in a statute what it says there.'") (quoting *Connecticut Nat. Bank* v. *Germain*, 503 U.S. 249, 253–254 (1992) (alteration in original)).

[6] 15 U.S.C. § 1665d(c).

Specifically, Congress instructed that agency rulemakings contemplate four factors in evaluating whether a late fee is reasonable and proportional to the omission or violation at issue: (1) "the cost incurred by the creditor from such omission or violation; (2) the deterrence of such omission or violation by the cardholder; (3) the conduct of the cardholder; and (4) such other factors as the Bureau may deem necessary or appropriate."[7] The second and third factors invoke the traditional understanding of special damages, further driving home the point that Congress envisioned a fee beyond the strictures of ordinary contract remedies that would properly incentivize customers based upon the nature of their violation.[8]

The surrounding statutory text reinforces that Congress realized its conception of late fees drew on both contract and tort damages. Contract-law terms like "agreement" and "violation" appear in the same sentence as "penalty" and the phrase "reasonable and proportional to the omission or violation," which Congress borrowed from the standard for special damages in tort law.[9] And further demonstrating the absence of any mistake, Congress repeated all of these choices in the next section, requiring agency rulemakings to "establish standards for assessing whether the amount of any penalty fee or charge described under subsection (a) is reasonable and proportional to the omission or violation to which the fee or charge relates."[10]

Beyond that, the legislative record demonstrates that Congress specifically debated and negotiated the departure from contract norms. For instance, Representative Earl Blumenauer opposed the language for exactly that reason: "The legislation also requires that fees be reasonable and proportional to the consumer's late or over-limit violation. Penalty clauses are generally unenforceable in the realm of contracts. Why should consumers be unfairly burdened?"[11] In the end, however, Congress enacted in Section 1665d language that merges contract and tort principles, meaning that any rulemaking that does not adequately account for both the compensatory and deterrence aspect of the omission or violation is contrary to law. Giving meaning to the word "penalty" in Section 1665d thus requires more than mere compensatory damages—that is, costs—incurred as a result of a breach.[12]

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7 *Id.*

8 *See State Farm Mut. Auto. Ins. Co.* v. *Campbell*, 538 U.S. 408, 416 (2003) (noting that special damages are aimed at deterrence).

9 *Id.* at 426 ("[C]ourts must ensure that the measure of punishment is both reasonable and proportionate to the amount of harm to the plaintiff and to the general damages recovered.").

10 15 U.S.C. § 1665d(b).

11 155 Cong. Rec. 13067 (2009).

12 *See, e.g.*, *Old Stone Corp.* v. *United States*, 450 F.3d 1360, 1368 (Fed. Cir. 2006) ("A non-breaching party may generally recover its mitigation costs incurred in a reasonable effort to avoid loss caused by a breach, even if its efforts prove unsuccessful.") (citing Restatement (Second) of Contracts § 350 cmt. h; *id*. at § 347 cmt. c (1981) ("[T]he injured party is [generally] entitled to recover for all loss actually suffered.") (alteration in original))).

Another contemporaneously enacted statute further demonstrates that, when the 111th Congress wanted to limit a fee to the recovery of costs alone, it did so expressly and unambiguously. In the Durbin Amendment,[13] Congress specifically instructed the Federal Reserve—the same agency Congress had tasked with promulgating rules under the CARD Act just one year earlier—to "prescribe regulations in final form . . . to establish standards for assessing whether the amount of any interchange transaction fee . . . is reasonable and proportional to the ***cost*** incurred by the issuer with respect to the transaction."[14] Likewise, when Congress articulated factors that the Federal Reserve was required to consider in rulemaking, each was grounded solely in costs.[15]

Despite the clear statutory mandate to prescribe late fees that do not myopically focus on cost alone, the Proposed Rule does just that. In determining what amount of a late fee is reasonable and proportional to late payments, the Bureau proposes an amount corresponding only to cost and minimizing to the point of irrelevance the remaining three statutory factors. Specifically as to cost, in support of the proposed $8 safe harbor, the Proposed Rule "preliminarily concludes that a late fee of $8 for the first and subsequent violations is appropriate to cover pre-charge-off costs for card issuers on average while providing issuers compliance certainty and administrative simplicity."[16] That leaves zero margin available for purposes of addressing any of the three remaining statutory factors.

Director Chopra's remarks and the Bureau's own statements double down on this approach:

> Importantly, when the Fed came up with its safe harbor provision, it had no *cost-basis* analysis of its own on which to base the $25 number. Instead, it looked at things like state laws, research from large issuers, overdraft fees, and laws in the United Kingdom. There was little evidence to support how much it actually *costs* a financial institution to process a late fee. It also looked at late fees set by small banks and credit unions, but, again, the final rule had no empirical evidence to suggest the fees were correlated with *costs*.[17]
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> * * * *
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> Many Americans have also encountered junk fees in the consumer finance sector the CFPB regulates, and it's easy to grow accustomed to fees as part

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[13] 15 U.S.C. § 1693o-2.

[14] *Id.* § 1693o-2(a)(3)(a) (emphasis added).

[15] *Id.* § 1693o-2(a)(4)–(5).

[16] 88 Fed. Reg. at 18919.

[17] Press Release, CFPB, Prepared Remarks of Director Chopra on Credit Card Late Fees ANPR Press Call (Jun. 22, 2022), https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-director-chopra-on-credit-card-late-fees-anpr-press-call/ (hereinafter "2022 Press Release") (emphases added).

> of our everyday experience with financial products and services. They take many different forms, including fees for late penalties . . . .[18]
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> * * * *
>
> In markets across the economy, junk fees have unfortunately become the norm. These junk fees aren't subject to the normal forces of competition. They're often charged for so-called services that a consumer never wanted and are set at levels far beyond the true *cost*.[19]
>
> * * * *
>
> Well, I think we've seen it, how junk fees are really creeping across the economy. I think we've all experienced them, where we're charged for a service that we never even wanted. Or it's charged at a level that is way beyond the *cost* to provide.[20]

As discussed above, the Bureau is statutorily prohibited from prescribing a late fee safe harbor that reflects only costs. The Proposed Rule does exactly that, and accordingly violates Congress's instruction in the CARD Act. While federal agencies may receive deference in interpreting ambiguous statutes, the law affords no such deference where the statutory mandate is clear and unambiguous on its face, as it is here.

B. **<u>The Bureau Incorrectly Considers Only Costs of Collection (and Even Then, Only a Subset of Those Costs) and Improperly Relies on Y-14 Data</u>.**

Even if the Bureau's exclusive focus on costs complied with the statute, the Proposed Rule fundamentally misunderstands the nature of costs associated with late payments. For example, it improperly excludes an entire category of costs deemed relevant by the statute—namely, post-charge-off collection costs. The Bureau seeks to justify this exclusion with Y-14 data and, in so doing, impermissibly excludes inputs reflecting other costs associated with late payments.

The Bureau is correct that justification is necessary; the Bureau bears the "initial burden of promulgating and explaining a non-arbitrary, non-capricious rule."[21] In the

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[18] *The Hidden Cost of Junk Fees*, CFPB Blog (Feb. 2, 2022), https://www.consumerfinance.gov/about-us/blog/hidden-cost-junk-fees/.

[19] Press Release, Director Chopra's Remarks on Press Call for Credit Card Late Fees NPRM, CFPB (Feb. 1, 2023), https://www.consumerfinance.gov/about-us/newsroom/director-chopras-remarks-on-press-call-for-credit-card-late-fees-nprm/ (hereinafter "2023 Press Release") (emphasis added).

[20] NPR Morning Edition, *Biden Administration Is Asking State Leaders to Help Fight Junk Fees*, NPR (Mar. 9, 2023), https://www.npr.org/2023/03/09/1162120322/biden-administration-is-asking-state-leaders-to-help-fight-junk-fees/ (emphasis added).

[21] *National Lime Ass'n* v. *EPA*, 627 F.2d 416, 432 (D.C. Cir. 1980).

analogous context of formal rulemaking, the Administrative Procedure Act (the "APA") provides that "the proponent of a rule or order has the burden of proof."[22] Moreover, "the House Report accompanying the APA explains, 'section [556(d)] means that every proponent of a rule or order or the denial thereof has the burden of coming forward with sufficient evidence therefor.'"[23] And as discussed *infra* p. 38, the agency's burden is especially important where an agency seeks to change a longstanding rule or policy, as the Bureau is here.[24]

The CARD Act reiterates that the Bureau bears the burden of proof in demonstrating that any implementing rule is not arbitrary and capricious. Specifically, the CARD Act requires that the Bureau, in consultation with other regulators, "issue final rules . . . to establish standards for assessing whether the amount of any penalty fee or charge . . . is reasonable and proportional to the omission or violation to which the fee relates."[25] In doing so, and as discussed above, the Bureau "shall consider: (1) the cost incurred by the creditor from such omission or violation; (2) the deterrence of such omission or violation by the cardholder; (3) the conduct of the cardholder; and (4) such other factors as the Bureau may deem necessary or appropriate."[26] Thus, in promulgating any rule related to late fees, the Bureau bears the burden of proving that its proposal adequately considers each factor and results in a fee that is "reasonable and proportional" to the omission or violation to which it relates.

For the following reasons, the Proposed Rule fails to comply with the statutory language of the CARD Act and improperly relies on non-public Y-14 data that does not even come close to satisfying the Bureau's burden to justify excluding post-charge-off collection and other costs associated with late payments from the ambit of relevant costs.

1. The Proposed Rule Ignores the Plain Language of the CARD Act.

The Proposed Rule is part of the Bureau's initiative on so-called "junk fees"—fees that the Bureau claims "obscure the true price of their services by luring customers with enticing offers and then charging excessive junk fees."[27] As part of that initiative, the Bureau maintains that it is seeking to address "fees purportedly charged to cover individual

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22 5 U.S.C. § 556(d).

23 *Hazardous Waste Treatment Council* v. *EPA*, 886 F.2d 355, 349 (D.C. Cir. 1989) (citation omitted).

24 *Encino Motorcars, LLC* v. *Navarro*, 579 U.S. 211, 221–222 (2016) (stating that, in changing position, "an agency must also be cognizant that longstanding policies may have engendered serious reliance interests that must be taken into account" and provide a "reasoned explanation" for "disregarding facts and circumstances that underlay or were engendered by the prior policy") (internal quotation marks and citations omitted).

25 15 U.S.C. § 1665d(b).

26 *Id.* § 1665d(c).

27 Press Release, Consumer Financial Protection Bureau Launches Initiative to Save Americans Billions in Junk Fees, CFPB (Jan 26, 2022), https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-launches-initiative-to-save-americans-billions-in-junk-fees/ (hereinafter "Junk Fees Press Release").

expenses, like paperwork processing, [that] can often greatly exceed the actual cost of that service."[28] The Proposed Rule goes further, however, and notes that "the Bureau carefully considered several sources of data and other information to determine the amount that would cover a reasonable and proportional amount of card issuers' pre-charge-off collection costs."[29] Thus, the Proposed Rule not only mischaracterizes the late fee—the statutorily permitted and regulatorily prescribed fee disclosed expressly in the way articulated by the Bureau—as an impermissible "junk fee," it also ignores the express language of the CARD Act regarding what constitutes a permissible late fee. Moreover, even assuming that the Bureau could somehow ignore the express language of the CARD Act and focus solely on costs alone, there is no basis for limiting those costs to pre-charge-off collection costs.

The CARD Act's express language makes clear that "[t]he amount of any penalty fee or charge that a card issuer may impose with respect to a credit card account under an open end consumer credit plan in connection with any omission with respect to, or violation of, the cardholder agreement, including any late payment fee . . . shall be reasonable and proportional to such omission or violation."[30] Moreover, in setting forth cost as one of several considerations for any rulemaking under the statute, the CARD Act provides that the "Bureau shall consider . . . the cost incurred by the creditor from such omission or violation."[31] Finally, as it relates to any safe harbor, the CARD Act again makes clear what the late fee must be reasonable and proportional to—"[t]he Bureau, in consultation with the Comptroller of the Currency, the Board of Directors of the Federal Deposit Insurance Corporation, the Director of the Office of Thrift Supervision, and the National Credit Union Administration Board, may issue rules to provide an amount for any penalty fee or charge described under subsection (a) that is presumed to be reasonable and proportional to the *omission or violation to which the fee or charge relates*."[32]

The Proposed Rule improperly conflates two distinct concepts within the CARD Act—the requirement that late fees be reasonable and proportional to the omission or violation to which the fee relates (i.e., late payments) with one of the considerations to be assessed (i.e., the cost incurred by the creditor from such omission or violation). The Proposed Rule's efforts to combine the two concepts ignores the express statutory language with the purpose of creating a new and much narrower standard to facilitate its prejudged goal of reducing late fees. The Proposed Rule's approach of focusing on whether late fees are reasonable and proportional to pre-charge-off collection costs alone directly contravenes the express language of the CARD Act and is therefore improper.

Moreover, the proposal even runs afoul of the Bureau's own narrowed standard. Although the Proposed Rule notes that it is assessing whether late fees are reasonable and

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[28] *Id*.
[29] 88 Fed. Reg. at 18916.
[30] 15 U.S.C. § 1665d(a).
[31] *Id*. § 1665d(b).
[32] *Id*. § 1665d(e) (emphasis added).

proportional to pre-charge-off collection costs, it actually seeks to impose a standard that makes the late fee equal to those costs, noting that "the Bureau has preliminarily determined that a late fee safe harbor amount of $8 for the first and subsequent violations would cover most issuers' costs from late payments . . . ."[33] The standard "reasonable and proportional to," however, does not mean "equal to," but instead requires a thorough analysis of the required factors in order to make a well-grounded determination. For example, the Federal Reserve conducted an extensive analysis of the competing factors and arguments in determining whether its proposal under the Durbin Amendment was reasonable and proportional to the costs of acceptance—even where cost was the only factor to be considered.[34] In contrast, the Bureau's Proposed Rule seeks unilaterally to rewrite the CARD Act to create a new standard—reasonable and proportional to only a subset of the costs associated with late payments—and then in an improper and conclusory fashion, declares that a fee equal to that narrow subset of costs is reasonable and proportional.

In an effort to bolster its upending of the statutory language to conclude that a late fee based on only one of the statutorily mandated factors is reasonable and proportional, the Bureau cites changes in the United Kingdom, which imposed a presumed reasonableness limit for late fees of £12, "($21 on the day of the rule, $13.40 in November 2022)," as further evidence of its proposal.[35] The Proposed Rule notes that the Bureau "is not aware of evidence suggesting that the £12 . . . limit . . . in 2006 meaningfully increased late payments in the United Kingdom."[36] What the Proposed Rule fails to note, however, is how out of step the current rule is with the existing late fee levels in the United Kingdom. As of today, for example, the proposed $8 safe harbor would be a mere £6.65—or roughly *half* of the amount presumed reasonable in the United Kingdom. Moreover, the policy established in the United Kingdom was based on contractual damages alone, and specifically excluded any consideration of deterrence in setting the £12—a policy choice not available under the CARD Act.[37]

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[33] 88 Fed. Reg. at 18916.

[34] 76 Fed. Reg. 43394, 43423 (July 10, 2011) ("The statute's use of the term 'reasonable' implies that, above some amount, an interchange fee is not reasonable. . . . The use of the term 'proportional' requires a relationship between the interchange fee and costs incurred; however, it does not require equality of fees and costs or demand that the relationship be constant across all quantities . . . including 'forming a relationship with other parts or quantities' or 'corresponding in degree, size, or intensity.'") (citing *Reasonable*, Black's Law Dictionary (7th ed. 1999); *Reasonable*, Webster's New World Dictionary & Thesaurus (2nd ed. 2002); *Proportional*, American Heritage Dictionary (1976); *Proportional*, Merriam Webster's Collegiate Dictionary (10th ed. 1995)).

[35] *Id*. at 18921.

[36] *Id*.

[37] *Calculating Fair Default Charges in Credit Card Contracts*, Office of Fair Trading (Apr. 2006), https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/284445/oft842.pdf ("It has been put to us that to require charges not to exceed recoverable costs might encourage a tendency for banks to 'gold plate' their operations for handling defaults, in order to increase

In sum, the Proposed Rule ignores the express language of the CARD Act to create a much narrower standard that keys the safe harbor to costs alone, and only then to a subset of relevant costs—pre-charge-off collection costs. A comparison of the proposed $8 safe harbor to the late fees permitted in the United Kingdom drives home the unreasonableness of the Proposed Rule's approach, particularly given that the CARD Act requires that the additional considerations of deterrence and cardholder conduct be considered in determining what amount is reasonable and proportional to the violation.

2. Excluding Post-Charge-Off Collection Costs Lacks Any Basis in Law or Fact.

The Bureau provides no valid basis for excluding post-charge-off collection costs from the cost calculation under Section 1026.52(b)(1)(i). Whether collection costs correspond to accounts that have been charged off is irrelevant to whether the costs themselves count as collection costs under Section 1026.52(b)(1)(i). Issuers charge off account balances, recording a loss for accounting and financial-reporting purposes, based on the time a balance has been outstanding, bankruptcy risk, and other factors that reflect the corresponding risk that the customer will not ultimately repay their balance.[38] That provides no basis to differentiate between pre- and post-charge-off collection costs *for purposes of measuring costs associated with late payments*. Post-charge-off collection costs, like pre-charge-off costs, are operating expenses, not losses. Charge-off says nothing about the factual collection of payment. It does not render an account uncollectible, change a borrower's obligation, or even relieve a financial institution of its obligation to try to recover the amounts owed. The Office of the Comptroller of the Currency, for example, has made clear that "[a]n effective collection process is a key component of controlling and minimizing credit losses," including collecting on post-charge-off debt.[39]

The Proposed Rule's exclusion of all post-charge-off collection costs from the cost calculation under Section 1026.52(b)(1)(i) is therefore arbitrary and capricious. The Proposed Rule reasons that post-charge-off collection costs should be excluded because the issuer writes off as a loss the unpaid balance that gives rise to those collection costs. The Proposed Rule makes the assumption that this relationship transforms those costs into

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costs and thus justify higher charges in order to deter defaults. We believe that charges set to match recoverable costs that are higher than necessary would be open to challenge for unfairness, and we would expect to take action accordingly. Taking what a court would order under the common law as a comparable yardstick, it is normal in the assessment of damages for the injured party to be expected to mitigate his loss, and thus to be awarded compensation only for such costs as he could not reasonably avoid incurring.").

[38] Comptroller's Handbook: Credit Card Lending, OCC 46 (version 2 Apr. 2021) https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-handbook/files/credit-card-lending/index-credit-card-lending.html ("Past-due, charge-off, and profitability reports provide bank management with important information *for assessing the quality of the credit card portfolio*. Effective reporting identifies trends in the portfolio with sufficient time for bank management to react appropriately.") (emphasis added).

[39] *See id.* at 38–39.

loss-mitigation efforts—serving only to generally encourage customers to pay on time such that the issuer can write off less going forward—rather than present efforts to collect the unpaid balance.[40] As already explained, that is incorrect as a factual matter.

The CARD Act provides that the Bureau shall consider "the cost incurred by the creditor from such omission or violation."[41] Even if the Bureau can maintain that losses are excluded from "costs" outlined in the statute, the rationale underlying that argument does not extend to excluding post-charge-off collection costs. The CARD Act provides no basis to draw a distinction between pre-charge-off and post-charge-off collection costs. In fact, Director Chopra's own public comments indicate that the inclusion of post-charge-off collection costs is appropriate, given that he has emphasized that the purpose of the Proposed Rule is to ensure that late "fees are in line with [a bank's] collection costs."[42] Even if Director Chopra were correct that the purpose of implementing the regulations is to focus solely on collection costs, nothing in the CARD Act supports the Proposed Rule's inappropriately narrow view of those costs.

Yet the Proposed Rule declines to consider this subset of actual collection costs simply because a customer has not paid the bank for a longer period—and based entirely on an unrelated accounting concept designed to ensure appropriate financial reporting of credit losses.[43] Moreover, banks cannot seek the costs associated with post-charge-off collection activity from customers, making those costs more like pre-charge-off collection costs as opposed to losses. Put simply, the Bureau has no basis for the exclusion.

3. The Bureau Relies on Y-14 Data Not Suitable for the Rulemaking and Fails to Disclose the Data or Methodology, in Violation of the APA.

The notice-and-comment rulemaking process requires an agency to "make available technical studies and data that it has employed in reaching the decisions to propose particular rules," lest the agency commit "serious procedural error" by failing "to reveal portions of the technical basis for a proposed rule in time to allow for meaningful

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[40] 88 Fed. Reg. at 18910–18911.

[41] 15 U.S.C. § 1665d(c)(1).

[42] 2023 Press Release, *supra* note 19.

[43] It is black-letter contract law that a party may not only recover the loss associated with a breach by the non-performance of the other party, but also any other costs—including mitigation costs—associated with attempting to avoid the loss itself. *See, e.g.*, Restatement (Second) of Contracts § 347 (1981) ("[T]he injured party has a right to damages based on his expectation interest as measured by (a) the loss in the value to him of the other party's performance caused by its failure or deficiency, plus (b) any other loss, including incidental or consequential loss, caused by the breach, less (c) any cost or other loss that he has avoided by not having to perform."); *id.* cmt. c (noting that "the injured party is entitled to recover for all losses actually suffered," including "costs incurred in a reasonable effort, whether successful or not, to avoid loss"). Notably, the costs incurred in seeking to mitigate the loss are separate and distinct from the costs associated with the underlying loss for the breach itself.

commentary."[44] This requirement enhances the integrity of not only the notice-and-comment process, but also the judicial review process. "By requiring the 'most critical factual material' used by the agency be subjected to informed comment, the APA provides a procedural device to ensure that agency regulations are tested through exposure to public comment, to afford affected parties an opportunity to present comment and evidence to support their positions, and thereby to enhance the quality of judicial review."[45]

The Bureau "considered data in developing [the Proposed Rule] that the [Federal Reserve] Board collects as part of its Y-14M (Y-14) data."[46] As background, through the Y-14 report, the Federal Reserve "collects monthly detailed data on bank holding companies' (BHCs), savings and loan holding companies' (SLHCs), and intermediate holding companies' (IHCs) loan portfolios."[47] The collection of the data is unrelated to the Bureau's regulatory obligations, and is instead "used to assess the capital adequacy of large firms using forward-looking projections of revenue and losses, to support supervisory stress test models and continuous monitoring efforts, and to inform the Federal Reserve's operational decision-making as it continues to implement the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010."[48]

The Proposed Rule uses four metrics from the Y-14 data: late fee income; collection costs; late fee amount; and total required payments.[49] For late fee income, the Proposed Rule leveraged "net fee income assessed for late or nonpayment accounts . . . [which was] late fee income for the Bureau's purposes."[50] As it relates to collection costs, the Proposed Rule leveraged the "[r]eported costs incurred to collect problem credits that include the total collection cost of delinquent, recovery, and bankrupt accounts."[51] These amounts report "*aggregate costs monthly*," but—as discussed above—do not "include losses and associated costs."[52] Moreover, the definitions for these aggregated amounts are not specific and many costs associated with late payments or even the subset of those associated with collections—e.g., technology costs—may be included in other categories. For late fee amounts, the Proposed Rule leveraged the "[r]eported amount of the late fee

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[44] *Owner-Operator Indep. Drivers Ass'n, Inc.* v. *Fed. Motor Carrier Safety Admin.*, 494 F.3d 188, 199 (D.C. Cir. 2007) (citing *Solite Corp.* v. *EPA*, 952 F.2d 473, 484 (D.C. Cir. 1991)); *see also Air Transp. 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." (citing *Association of Data Processing Serv. Orgs.* v. *Bd. of Governors of the Fed. Reserve Sys.*, 745 F.2d 677, 684 (D.C. Cir. 1984))).

[45] *Am. Radio Relay League, Inc.* v. *F.C.C.*, 524 F.3d 227, 236 (D.C. Cir. 2008) (quoting *Chamber of Com. of U.S.* v. *S.E.C.*, 443 F.3d 890, 900 (D.C. Cir. 2006)).

[46] 88 Fed. Reg. at 18910.

[47] *Reporting Forms: FR Y-14M – Capital Assessments and Stress Testing*, Board of Governors of the Federal Reserve System, https://www.federalreserve.gov/apps/reportingforms/Report/Index/FR_Y-14M (last visited May 3, 2023).

[48] *Id*.

[49] 88 Fed. Reg. at 18910.

[50] *Id.*

[51] *Id*.

[52] *Id.* (emphasis added).

charged on a particular account in a particular month."[53] Finally, as it relates to total required payments, the Proposed Rule leveraged the "[r]eported total payment amount on a particular account in a particular month, including any missed payments or fees that were required to be paid in a particular billing cycle."[54]

The Bureau compiled a set of aggregated and anonymized values for these items in a document published at the same time as the Proposed Rule.[55] Noticeably absent from that document and the Proposed Rule, however, is any explanation of which Y-14 data fields the Bureau used to populate the document, how and why the Bureau designated the data for inclusion in the categories the document sets forth, or how the Bureau ensured that the data categorizations were consistent from bank to bank—all of which prevents commenters from assessing the validity and accuracy of the document or the conclusions it ostensibly supports.

Take, for example, the Bureau's determination regarding costs. The Proposed Rule makes a series of high-level observations that provide no detail or insight into the methodology or accuracy of the Bureau's conclusions—rendering those conclusions insusceptible to challenge or scrutiny:

> The Bureau has analyzed the Y-14 data and other information in considering the factor of the costs of a late payment violation to the card issuer. Based on that analysis, the Bureau has preliminarily determined that a late fee safe harbor amount of $8 for the first and subsequent violations would cover most issuers' costs from late payments while providing card issuers with compliance certainty and administrative simplicity and, therefore, reduce their compliance costs and burden.[56]
>
> * * * *
>
> The Bureau concludes that the collection costs data in the Y-14 are consistent with the costs included for the cost analysis provisions in § 1026.52(b)(1)(i), except that the collection costs in the Y-14 data include post-charge-off collection costs.[57]

Although those commentating on the Proposed Rule are ultimately left to guess given the Bureau's failure to make available the data it is relying upon, there appears to be no support for the Bureau's apparent conclusion that it has identified the full range of costs

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[53] *Id*.

[54] *Id*.

[55] *Credit Card Late Fees: Revenue & Collection Costs at Large Bank Holding Companies*, CFPB (Feb. 1, 2023, https://files.consumerfinance.gov/f/documents/cfpb_credit-card-late-fees-revenue-collection-costs-large-bank_2023-01.pdf.

[56] 88 Fed. Reg. at 18916. Notably, the Bureau offers no support whatsoever for its conclusion that the new rulemaking would decrease compliance costs.

[57] *Id.*

associated with late payments in the Y-14 data that qualify under the cost analysis provisions in Section 1026.52(b)(1)(i).

Although the Proposed Rule and data table document do not specifically indicate the exact field numbers the Proposed Rule used from the Y-14 data—a shortcoming in itself—it appears that the Proposed Rule was leveraging Line Item 32 – Total Non-Interest Expense – Collections Expense.[58] The Y-14 Form and Instructions define that field to include "costs incurred to collect problem credits . . . [i]nclud[ing] the total collection cost for delinquent, recovery, and bankrupt accounts."[59] As the Proposed Rule acknowledges, this field represents "aggregate costs monthly," and thus does not include any line level or expense-specific detail.[60] Moreover, there are a number of other expense line items in the Y-14M-related fields that could also include indirect expenses related to collection activity, such as Total Non-Interest Expenses (Line Item 29) and Total Non-Interest Expense – All Other Expenses (Line Item 30).[61] For example, different banks might place the relevant portion of costs associated with running tech platforms that are leveraged for collection into different categories of expenses.

There are a number of expenses caused by late payments that are not included in the line item chosen by the Bureau in the Y-14 data, and that would be included as costs even under the Bureau's narrowed definition of permissible costs in the Proposed Rule. By way of example, these expenses include technology expenses associated with delinquent customer servicing and processing platforms,[62] certain types of customer communications for customers in a delinquent status, payment-processing expenses associated with specific programs for late payers, and support-function costs for collections activities (risk management, human resources, legal, etc.). This is not an exhaustive list but demonstrates why reliance on the Y-14 data is not proper in this rulemaking—and that is prior to addressing issues with variability between banks regarding how they measure, categorize, and report the relevant cost data.

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58 Board of Governors of the Federal Reserve System, OMB Bull. No. 7100-0341, *Instructions for the Capital Assessments and Stress Testing Information Collection* 185 (Sept. 2022), https://www.federalreserve.gov/apps/reportingforms/Report/Index/FR_Y-14M (hereinafter "Y-14M Form & Instructions").

59 *Id.* at 186.

60 88 Fed. Reg. at 18910.

61 Y-14M Form & Instructions, *supra* note 58, at 185–187.

62 With respect to technology costs specifically, Director Chopra has pointed to technological advancements for collection activity as a basis for arguing that collections costs should be going down. While that may be true over time for any particular piece of technology, these technological advancements are not cost-free; they are only achieved through significant issuer investments. *See* 2022 Press Release, *supra* note 17 ("We are also examining whether it is appropriate for credit card companies to receive immunity from enforcement if they hike the cost of credit card late fees each year by the rate of inflation. Do the costs to process late payments really increase with inflation? Or is it more reasonable to expect that costs are going down with further advancements in technology every year?").

In fairness, the Bureau would not know what costs are excluded and what variability exists because the only information contained in the Y-14 data is a dollar amount for each line item without any itemization for those amounts—which is why the Y-14 data is not the right dataset for the instant purpose.

The Proposed Rule and data tables appear to demonstrate that the Bureau has done no work to understand what categories and types of expenses are included by each bank within each of the various fields. Therefore, the Bureau lacks support for concluding that the collection costs it has identified in the Y-14 data "are consistent with the costs included for the cost analysis provisions in § 1026.52(b)(1)(i)."[63] In any event, the way in which the Bureau has gone about its analysis here violates the mandate in the APA that any such analysis be made available for public review and comment, so that the Bureau's approach and conclusions can be reviewed and scrutinized.

Given that, as discussed above, the Proposed Rule relies heavily upon Y-14 data, these oversights and the lack of detail around the data set and the relevant methodology are critical failures that not only show a lack of necessary support for the Proposed Rule, but also make public scrutiny of the Bureau's interpretation of the data impossible. Even with the information and conclusory statements that the Bureau has shared in its Proposed Rulemaking, the deficiencies are already apparent. A more fulsome understanding of the Bureau's analysis, underlying assumptions, and data (consistent with what could be shared publicly) would almost certainly reveal even greater infirmities. Although the discussion above pertains to cost data, the same flaw applies to the Proposed Rule's use of the Y-14 data and methodology for the other fields and data as well. In short, the Bureau has failed to provide "the most critical factual material used by the agency"[64] in the Proposed Rule by failing to reconcile and provide its data and methodology. As such, the Bureau's failure hinders the ability of "affected parties . . . to present comment and evidence to support their positions" and undercuts the "quality of judicial review."[65]

The APA problems discussed above reveal a more fundamental issue. The simplest explanation for why the Proposed Rule does not include more detail about the Y-14 data, its methodology, or its use by the Bureau is that the Y-14 data is not appropriately used in this late fee rulemaking. As an initial matter, the Y-14 data is collected by an entirely different regulator[66] for an entirely different purpose. The data is "used to assess the capital adequacy of large firms using forward-looking projections of revenue and losses, to support

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[63] 88 Fed. Reg. at 18916.

[64] *Am. Radio Relay League*, 524 F.3d at 236 (internal quotation marks and citations omitted).

[65] *Id.* (internal quotation marks and citations omitted); *see generally* Y-14M Form & Instructions, *supra* note 58.

[66] *See* Y-14M Form & Instructions, *supra* note 58, at 6 ("As these data will be collected as part of the supervisory process, they are subject to confidential treatment under exemption 8 of the Freedom of Information Act. 5 U.S.C. 552(b)(8). In addition, commercial and financial information contained in these information collections may be exempt from disclosure under Exemption 4.5 U.S.C. 552(b)(4). Disclosure determinations would be made on a case-by-case basis.").

supervisory stress test models and continuous monitoring efforts, and to inform the Federal Reserve's operational decision-making . . . ."[67] Moreover, the issuers included in the data "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***."[68]

In the almost 10 years since the Y-14 data has been available, the Bureau has only used the Y-14 data as part of only two prior proposed rules, neither of which leveraged the data for any substantive changes.[69] No final rule has relied on Y-14 data. The lack of prior rulemaking involving Y-14 data is unsurprising, given that the Bureau has an authority that is specifically designed for data collection for purposes of rulemaking—namely, Section 1022(c)(4)(B) of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"). Section 1022(c)(4)(B) provides that the Bureau may "require covered persons and service providers participating in consumer financial services markets to file with the Bureau, under oath or otherwise, in such form and within such reasonable period of time as the Bureau may prescribe by rule or order, annual or special reports, or answers in writing to specific questions, furnishing information described in paragraph (4), as necessary for the Bureau to fulfill the monitoring, assessment, and reporting responsibilities imposed by Congress."[70] That mechanism was specifically created to allow the Bureau to gather information to monitor risks "to support its rulemaking"[71] and also allows the Bureau's methodology to be openly shared with those seeking to comment.

In fact, the Bureau has leveraged Section 1022(c)(4)(B) to engage in factfinding efforts for rulemakings in the past.[72] Notably, those rulemakings have allowed the Bureau

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[67] *Reporting Forms: FR Y-14M – Capital Assessments and Stress Testing*, *supra* note 47.

[68] *Credit Card Late Fees*, CFPB 3 n.3 (Mar. 2022), https://files.consumerfinance.gov/f/documents/cfpb_credit-card-late-fees_report_2022-03.pdf (emphasis added).

[69] Small Business Lending Data Collection Under the Equal Credit Opportunity Act (Regulation B), 86 Fed. Reg. 56356, 56367–56368 (proposed Oct. 8, 2021) ("Mostly extended by depository institutions, the Bureau estimates that the market for small business credit cards totaled over $60 billion in outstanding balances for 2020. Using data from Y-14 Form submissions to the Federal Reserve Board, the Bureau estimates the value of outstanding balances for small business credit card accounts where the loan is underwritten with the sole proprietor or primary business owner as an applicant."); Request for Information Regarding the Integrated Mortgage Disclosures Under the Real Estate Settlement Procedures Act (Regulation X) and the Truth In Lending Act (Regulation Z) Rule Assessment, 84 Fed. Reg. 64436, 64440 (request for comment Nov. 22, 2019) ("To assess market effects, the assessment will rely first on data the Bureau already possess, such as Home Mortgage Disclosure Act (HMDA) data and the National Mortgage Database (NMDB) and stress testing data from the Federal Reserve (Y-14 data). These datasets may be used to identify changes in overall loan volumes, mortgage prices, price dispersions, and the availability of mortgage products.").

[70] 12 U.S.C. § 5512(c)(4)(B)(ii).

[71] *Id.* § 5512(c)(1).

[72] E.g., *Required Rulemaking on Personal Financial Data Rights*, CFPB, https://www.consumerfinance.gov/personal-financial-data-rights/ (last visited May 3, 2023) (noting that the "CFPB issued two sets of market monitoring orders to collect information related to personal

to provide its methodology and sufficient detailed data elements to commenters to permit adequate opportunity to effectively challenge the Bureau's conclusions.[73] To the extent that the Bureau justifies its decision to rely on the Y-14 data because it possesses no other data, the Bureau has nobody to blame but itself. Had the Bureau leveraged Section 1022(c)(4)(B), it could have provided appropriate definitions to ensure consistency between the responding banks and address the very shortcomings the Bureau acknowledges with the Y-14 data. By not exercising its Section 1022(c)(4)(B) information collection authority in support of this rulemaking, the Bureau made the purposeful decision not to gather relevant and necessary data. An agency action should be set aside under the APA for "failure to adduce empirical data that can readily be obtained."[74] The Bureau's failure to use its Section 1022(c)(4)(B) authority and its reliance on Y-14 data that it has not disclosed in any meaningful manner is improper and fatal as a factual basis for the Proposed Rule.[75]

Importantly, the Bureau actually did leverage its Section 1022(c)(4)(B) authority to, for the first time ever, seek information about collection-related costs as part of its biennial CARD Act survey—but it did so *after* it issued the Proposed Rule.[76] Although that Section 1022(c)(4)(B) request does not address the narrowness of the Bureau's

financial data rights" as part of the rulemaking process to implement section 1033 of the Dodd-Frank Act); *see also CFPB Orders Tech Giants to Turn Over Information on Their Payment System Plans*, CFPB (Oct. 21, 2021), https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-tech-giants-to-turn-over-information-on-their-payment-system-plans/ ("The orders [were] issued pursuant to Section 1022(c)(4) of the Consumer Financial Protection Act. The CFPB has the statutory authority to order participants in the payments market to turn over information to help the Bureau monitor for risks to consumers and to publish aggregated findings that are in the public interest."); *CFPB Seeks Public Input on Consumer Credit Card Market*, CFPB (Jan. 24, 2023), https://www.consumerfinance.gov/about-us/newsroom/cfpb-seeks-public-input-on-consumer-credit-card-market/.

[73] *See, e.g.*, Prepaid Accounts Under the Electronic Fund Transfer Act (Regulation E) and the Truth In Lending Act (Regulation Z), 81 Fed. Reg. 83934, 84312–84315 (Nov. 22, 2016); Arbitration Agreements, 82 Fed. Reg. 33210, 33220–33224 (Jul. 19, 2017).

[74] *F.C.C.* v. *Fox Television Stations, Inc.*, 556 U.S. 502, 519 (2009).

[75] To the extent the Bureau contends that issuing banks are the providers of said information and therefore can share submissions in order to understand what fields are included in the aggregated data, such detailed discussions would risk violating confidential supervisory information restrictions underlying the Y-14 submissions and would also run the risk of inflaming the existing unsubstantiated rhetoric around collusion between banks. *See* John McNamara, *Why the Largest Credit Card Companies Are Suppressing Actual Payment Data on Your Credit Report*, CFPB (Feb. 16, 2023), https://www.consumerfinance.gov/about-us/blog/why-the-largest-credit-card-companies-are-suppressing-actual-payment-data-on-your-credit-report/ ("While our analysis didn't seek to investigate whether entities explicitly colluded, the responses indicated that one large credit card company moved first, and other players suppressed data shortly thereafter. After the change made by these players, the share of furnished credit card accounts with actual payment information fell by more than half from 88 percent in late 2013 to only 40 percent by 2015.").

[76] Press Release, *CFPB Enhances Tool to Promote Competition and Comparison Shopping in Credit Card Market*, CFPB (Mar. 21, 2023), https://www.consumerfinance.gov/about-us/newsroom/cfpb-enhances-tool-to-promote-competition-comparison-shopping-credit-card-market/.

proposal or the lack of consistent definitions for any of the terminology and categories requested to ensure grounded responses across all participants, it nevertheless demonstrates that the Bureau could have leveraged its authority to gather the very information it now claims it lacks. The Bureau is unable to rely on that data in its final rule, however, unless it gives the public an adequate opportunity—while safeguarding the proprietary nature of the data—to comment on the data.

The Proposed Rule notes in several places that it "did not receive specific cost data in response to its request in the [Advanced Notice of Proposed Rulemaking ("ANPRM")] for data on card issuers' pre-charge-off collection costs, including data on pre-charge-off collection costs incurred by small issuers."[77] As noted above, this is not a valid excuse for the Bureau's failure to use its Section 1022(c)(4)(B) authority, which provides the agency with the authority to collect data in a consistent manner, where data fields can be defined and therefore reliably compared across banks, and the submission of information is mandatory. This cannot be replicated through an open-ended, voluntary request for data in an ANPRM, as the Bureau did here. In any event, an ANPRM does not create any legal obligations on the part of regulated entities. Moreover, the Bureau was significantly delayed in sharing information regarding how confidential data could be submitted,[78] which deterred industry commentators from submitting their data in light of the ANPRM's broad-sweeping statement that "[a]ll submissions in response to this notice, including attachments and other supporting materials, will become part of the public record and subject to public disclosure."[79] Finally, the nature of the response to the Bureau's invitation to provide information does not lessen the burden on the Bureau to ensure that its rulemaking is well-grounded and appropriately supported.[80]

C. The Proposed Rule's Consideration of Deterrence and Cardholder Conduct Does Not Support the Proposed Safe Harbor.

1. The Deterrence of Such Omission or Violation by the Cardholder.

The Bureau fails to adequately consider the factor of deterrence as mandated by Congress. Credit card issuers incur substantial risk in lending to consumers on an unsecured basis. Given the unsecured nature of credit card debt, it is crucial for lenders to encourage timely repayment. The Proposed Rule acknowledges—consistent with existing academic literature—that late fees have proven to be effective at deterring late payments. For example, the Proposed Rule notes that economist Sumit Agarwal found that, after incurring a late fee, a cardholder is 40% less likely to be delinquent on his or her next

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[77] 88 Fed. Reg. at 18917.

[78] *See* Bank Policy Institute, Comment Letter on Advanced Notice of Proposed Rulemaking Re: Credit Card Late Fees and Late Payments (Aug. 1, 2022), https://bpi.com/wp-content/uploads/2022/08/BPI-Comment-Letter-re-CFPB-CreditCardFee-ANPR-2022.08.01.pdf.

[79] Credit Card Late Fees and Late Payment, 87 Fed. Reg. 38679 (advanced notice June 29, 2022).

[80] *See Motor Vehicle Mfrs. Ass'n of U.S., Inc.* v. *State Farm Mut. Auto, Ins. Co.*, 463 U.S. 29, 43 (1983).

payment.[81] Not mentioned in the Proposed Rule, economist John Gathergood finds that the share of credit card accounts incurring late payment fees in their sample falls from 6% in the first month to 2.5% by the 23rd month, mainly because the payment of an initial late fee prompted consumers to set up automatic payments.[82] Both papers study the impact of late fees that were substantially larger than the $8 late fee proposed by the Bureau, which casts significant doubt on the ability of an $8 late fee to have a sufficient deterrent effect.[83]

Indeed, evidence from a variety of contexts shows that there is a positive association between penalty size and its deterrent effect. For example, economist Michael P. Haselhuhn, as the Proposed Rule notes, shows that fees are efficient compliance tools in the context of video rentals, where consumers are shown to learn to make returns on time when they have to pay a late fee.[84] Late fees per video per day ranged from $1 to $3.[85] Late fees for a single video held for an extended period could be as high as $40 (which would be even higher in 2023 dollars).[86] The article finds that the deterrent effect of personal experience with a fine increases with the size of the fine.[87] Additionally, studies of traffic violations also show that the size of monetary deterrents and fines matters for the change in behavior. Several prominent studies show that higher fines reduce drunk driving, speeding, and parking violations.[88]

The $8 fee proposed by the Bureau, however, is too small to act as a sufficient deterrent considered as an absolute amount and in comparison to other expenses and fees. For example, an $8 fee is less than the cost of various recreational expenses (including the average cost of one movie ticket) and household purchases (such as two pounds of ground beef or a mere three gallons of gasoline).[89] Further, on a percentage basis, the proposed

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[81] Sumit Agarwal et al., *Learning in the Credit Card Market*, at 11, 13 (2013), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1091623; *see also* 88 Fed. Reg. at 18921.

[82] John Gathergood et al., *How do Consumers Avoid Penalty Fees? Evidence from Credit Cards*, at 11 (2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2960004.

[83] Agarwal et al. uses 2002–2004 U.S. data, which pre-dates the CARD Act, and reports late fees ranging from $30 to $35. Gathergood et al. uses 2013–2014 UK data and reports a late fee of £12, approximately $19 given an average $1.60 to the pound during 2013–2014. These would be even higher if inflated to 2023 dollars.

[84] Michael P. Haselhuhn et al., *The Impact of Personal Experience on Behavior: Evidence from Video-Rental Fines*, 58 J. Manag. Sci. 52 (2012); *see also* 88 Fed. Reg. at 18921.

[85] Haselhuhn et al., *supra* note 84, at 54.

[86] *Id.* at 52.

[87] *Id.* at. 55; *see also* 88 Fed. Reg. at 18921.

[88] E.g., Martin Killias et al., *Higher Fines—Fewer Traffic Offences? A Multi-Site Observational Study*, 22 Eur. J. Crim. Policy Res. 619 (2016).

[89] *Theme Report 2021*, Motion Picture Association, https://www.motionpictures.org/wp-content/uploads/2022/03/MPA-2021-THEME-Report-FINAL.pdf, at 45; *Average Price Data (in U.S. dollars), Selected Items*, BLS (Mar. 2023), www.bls.gov/charts/consumer-price-index/consumer-price-index-average-price-data.htm.

$8 fee represents only 0.5% of the $1,729 average credit card balance.[90] This is small in comparison to the late fees charged on other financial products.[91]

Despite this, the Proposed Rule states, without support, that the $8 safe harbor "would still have a deterrent effect on late payments," and tellingly fails to inquire into the pertinent question, which is whether the $8 safe harbor would have a *sufficient* deterrent effect. Indeed, the Proposed Rule expressly concedes 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," and then cites as an excuse that "market participants did not provide data on deterrence" in response to the ANPRM.[92] The notion that an $8 safe harbor creates sufficient deterrence is belied by the Proposed Rule's express acknowledgement that it cuts against deterrence: "[L]ate 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."[93] The Proposed Rule concedes that the deterrent effect of late fees "may be lessened by the proposed change to some extent, and other factors may be more relevant (or may become more relevant) towards creating deterrence."[94]

The Proposed Rule resorts to indirect evidence, again derived from the nonpublic Y-14 data, and brushes aside the data and studies on the deterrent effect of late fees considered by the Federal Reserve in 2010. For example, the Proposed Rule selectively accepts the findings in a 2022 paper by economist Daniel Grodzicki containing "an empirical analysis that concluded that a decrease in the late fee amount stemming from the Board's 2010 Final Rule raised the likelihood of a cardholder paying late."[95] The Proposed Rule summarily dismisses well-supported conclusions that undermine its proposal,[96] noting that while the "paper suggests that consumers may engage in more late payments when they are less costly to consumers . . . , the Bureau does not consider this robust evidence that the proposed $8 safe harbor late fee amount would not have a deterrent effect."[97] The Proposed Rule's rationale is based solely on "the general economic

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[90] Allie Johnson, *The Average Credit Card Balance is $5,910. Here's What You Need to Know*, Credit Cards (Apr. 24, 2023), https://www.creditcards.com/statistics/credit-card-debt-statistics-1276/.

[91] *See Buy Now, Pay Later: Market Trends and Consumer Impacts*, CFPB, at 22–23 (September 2022), https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf. Additionally, at least one of the BNPL lenders surveyed by the Bureau in 2021 does not limit late fee amounts on either a per-installment or per-loan basis. *Id*. The $8 late fee also pales in comparison to the overdraft fees on checking accounts in the United States, which can exceed $30 per charge and a customer may incur several charges in a month on an account. *See Overdraft and Account Fees*, FDIC (Aug. 17, 2022), https://www.fdic.gov/resources/consumers/consumer-news/2021-12.html.

[92] 88 Fed. Reg. at 18919.

[93] *Id.*

[94] *Id.* at 18921.

[95] *Id.* at 18920 (citing Daniel Grodzicki et al., *Consumer Demand for Credit Card Services*, J. Fin. Res. (Apr. 25, 2022), https://link.springer.com/article/10.1007/s10693-022-00381-4).

[96] *Id*.

[97] *Id*.

uncertainty around th[e] time" of the data, August 2010,[98] and without any empirical peer-reviewed evidence whatsoever. And general economic uncertainty was not an obstacle to relying on data from this era for purposes of the Bureau's 2016 Prepaid Accounts Under the Electronic Fund Transfer Act (Regulation E) and the Truth In Lending Act (Regulation Z) rulemaking.[99]

Likewise, the Proposed Rule disregards a 2008 study relied upon in the Federal Reserve's 2010 rulemaking, which found that "a consumer who incurs a late payment fee is 40 percent less likely to incur a late payment fee during the next month, although this effect depreciates approximately 10 percent each month."[100] Without meaningful elaboration, the Proposed Rule concludes that the study is of "limited relevance."[101]

Finally, the Proposed Rule wrongly disregards a number of other studies that were provided in response to the ANPRM showing that cardholders and other consumers learn from late fees. The Proposed Rule acknowledges that these studies' results are "in line with the broader literature . . . indicating that consumers learn from trial and error of personal experience," but then "finds that these studies are less useful to extrapolate how many more cardholders would make a late payment on U.S. credit cards if the late fee safe harbor amount were lowered."[102] In other words, the Proposed Rule sees nothing to be gleaned from studies that examine the concept of deterrence, unless those studies also examine fluctuations in deterrence in response to specific fee amounts or changes.

The Proposed Rule attempts to rely upon Y-14 data to provide support for the deterrence value of an $8 late fee. Specifically, "[t]he Bureau conducted statistical analysis to investigate whether the lower late fee amount in month seven leads to a distinct rise in late payments (Y-14 seventh-month analysis)."[103] That is, the Bureau sought to prove that deterrence survives a late-fee reduction by looking at whether consumers who paid late once, and avoided paying late again during the subsequent six-month period in which they were subject to an increased late fee, paid late again after that period—expecting to

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[98] *Id*.

[99] Prepaid Accounts Under the Electronic Fund Transfer Act (Regulation E) and the Truth In Lending Act (Regulation Z), 81 Fed. Reg. 83934 (Nov. 22, 2016). Specifically, in considering the appropriate threshold for fee disclosure requirements, that rule relied on a study of "aggregate fees paid by cardholders to the prepaid issuer," which "used transactions covering a six-year cycle, but most occurred during the last two years of the data set (2009 and 2010)." 81 Fed. Reg. at 84045 & n.414.

[100] 88 Fed. Reg. at 18921 (citing Agarwal et al., *supra* note 81).

[101] *Id.* ("First, the study considers the months following any late fee and compares them to months with no recent late payment. That comparison is not the same as comparing to months in which a payment was late, but a lower late fee (or even a $0 late fee) was charged. Second, even if the study had compared to months where a payment was missed but no late fee was charged, that comparison still would not be relevant to the proposal in that the proposal would reduce the safe harbor amount to $8, not completely eliminate the late fee.").

[102] *Id.* n.118 (discussing Haselhuhn et al., *supra* note 84; Peter Fishman & Devin G. Pope, *Punishment-Induced Deterrence: Evidence from the Video-Rental Market*, Univ. of Cal., Berkeley, Dept. of Econ. (2006)).

[103] *Id*. at 18920.

attribute "jumps" in late payments to reduced deterrence.[104] The Proposed Rule's statistical analysis concluded that for "consumers that incurred a higher fee for a late payment during the six months after the initial late payment, the payment of that higher late fee did not lead to a discernibly lower chance of late payment for a third time in the future than for those consumers whose second late fee was lower because they paid late seven or more months after their first late payment."[105]

This analysis relies on the maximum permissible late fee being higher if a late payment occurred in the prior six months. In particular, the Proposed Rule investigates whether in the seventh month following an initial late fee, cardholders are more likely to incur a new late fee than in the intervening six months following the first late fee because the maximum late fee has not reverted to the lower regulatory amount.[106] The Proposed Rule's seventh-month analysis suffers from at least five flaws:

- *First*, the Bureau's analysis is unpublished. Details of the analysis and findings are not reported in the Proposed Rule or elsewhere and thus are not available for meaningful review.

- *Second*, the analysis relies on the unreasonable assumption that cardholders are actively tracking the six-month interval fee rule and the number of months between late fees, and then, based upon that tracking, choose to incur a late fee as soon as the late fee drops back to the lower level. This analysis falls far short of demonstrating that late payment in general is insensitive to late fee level. The Bureau's findings are more consistent with cardholders who accidently incur late fees not obsessively tracking when to incur another late fee, and cardholders who choose to incur a late fee either not knowing the details of when the size of the late fee will drop or not needing to incur a late fee six months later. In brief, the Bureau's analysis provides no basis for concluding that "the prevalence of late payments is not highly sensitive to the level of late fees."[107] Instead, the agency conducted an analysis that relies on unreasonable assumptions about cardholders who incur late fees.

- *Third*, the analysis is based on a sample of consumers that had at least one late payment, meaning that the Proposed Rule's results might not be generalizable to the broader population of credit card users and do not speak to the deterrence effect of late fees on the first late payment. The Proposed Rule also does not provide any information to assess these potential biases. For example, the Proposed Rule does not report how relevant characteristics (income, default

[104] *Id.*
[105] *Id.*
[106] *Id.*
[107] *Id.*

probability, credit scores, etc.) of the consumers in their study compared to the characteristics of overall credit card users.

- *Fourth*, the Bureau's use of the Y-14 data looked at a late-fee delta of only $11 (e.g., $29 for first and $40 for subsequent, or $30 for first, and $41 for subsequent), versus the difference between existing late fees (which could range from $21 to $33 depending on the lender and number of late payments) and the $8 proposal. In other words, the lack of a causal impact of payment behavior from the delta observed by the Bureau could actually establish the opposite conclusion from that reached by the Bureau—if an $11 delta does not impact consumer behavior, the $8 level would have no deterrent impact whatsoever. Such a reading of the Bureau's own statistical conclusions is actually more consistent with the empirical studies dismissed in the Proposed Rule.

- *Fifth*, the Proposed Rule's change in the late fee safe harbor is not small. The Proposed Rule proposes a reduction from $30 to $8—a $22, or more than 70%, reduction. Even if the propensity to pay late were only slightly sensitive to the level of fees, a 70% reduction in late fees can be expected to cause a meaningful increase in late payments.

In any event, even the Proposed Rule acknowledges that "the variation in late payments in the Y-14 seventh-month analysis discussed above is not the same as the changes that would result from the Proposed Rule."[108] The Proposed Rule points to no empirical studies that provide a basis for refuting the many empirical studies that show a correlation between penalty fees and deterrence that were relied upon by the Federal Reserve to reach its well-reasoned conclusions in its 2010 study.[109] Nevertheless, the Proposed Rule concludes that its "evidence suggests the prevalence of late payments is not highly sensitive to the level of late fees at the current order of magnitude."[110]

Finally, the Proposed Rule's reliance on other factors which could have a deterrent effect is similarly misplaced. The Proposed Rule notes that "[c]ard issuers also have other tools to deter late payment behavior, and therefore, minimize the potential frequency and cost to card issuers of late payments, such as reporting the late payment to a credit bureau which could affect the consumer's credit score, decreasing the consumer's credit line, limiting the cardholder's earning or redemption of rewards, and imposing penalty rates."[111] But these tools likely have a much lower deterrent effect as compared to late fees, because these tools are not nearly as direct or clear from the consumer's perspective.[112] Consumers may not as easily understand or be able to calculate the impact of an increase in their APR

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[108] *Id*.
[109] *See, e.g.*, Agarwal et al., *supra* note 81.
[110] 88 Fed. Reg. at 18920.
[111] *Id.* at 18922.
[112] *See id*. at 18935.

or a decrease in their credit score, credit line, or ability to redeem credit card rewards. Moreover, such tools impose longer-term implications for borrowers in terms of the cost of credit and ability to access credit. The late fee—a one-time monetary cost—serves as a mechanism to help prevent consumers from experiencing those more lasting and costly consequences.[113]

2. The Conduct of the Cardholder.

Likewise, the Bureau has failed to carry its burden to consider the factor of cardholder conduct.

The Proposed Rule acknowledges that the Federal Reserve's 2010 rulemaking "took consumer conduct into account in adopting the higher $35 fee for repeat late fees within six billing cycles . . . [finding] that '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.'"[114] In contrast, the Bureau has not only eliminated the Federal Reserve's two-tiered approach but also failed to adequately consider cardholder conduct in its proposal.

Based on an "analysis of the Y-14 data" and unspecified "other relevant information," the Proposed Rule rejects the Federal Reserve's observation and corresponding tiered structure premised on the analysis of cardholder conduct.[115] The Proposed Rule appears to focus exclusively on the fact that some accounts pay late less than 30 days past the due date and before the time that they would be reported as late for credit reporting purposes.[116] In addition, the Proposed Rule notes that "some consumers may pay late chronically but otherwise make a payment within 30 days for a number of reasons, including cash flow issues, that do not necessarily indicate that they are at significant risk of defaulting on the credit."[117] Once again, the Proposed Rule points to other factors creditors have to address credit risk—including lowering credit lines and imposing penalty repricing.[118]

As an initial matter, the Proposed Rule's discussion of when customers make late payments is inapposite to the specific issue of cardholder conduct. If the problem is, as the Bureau hypothesizes, with consumer cash flow timing, most major credit card issuers have mechanisms in place to allow customers to change the due date on their account in order

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113 *Credit Card Line Decreases*, CFPB 3 (June 2022), https://files.consumerfinance.gov/f/documents/cfpb_credit-card-line-decreases_report_2022-06.pdf (hereinafter "Credit Card Line Decreases Report") (noting that "[w]hile CLDs might prevent consumers from taking on more credit than they can afford, *CLDs can also have significant negative repercussions on consumers*.") (emphasis added).

114 88 Fed. Reg. at 18923 (citing 75 Fed. Reg. at 37526, 37527 (June 29, 2010)).

115 *Id*. at 18923.

116 *See id*.

117 *Id*.

118 *Id*.

to account for their own paycheck or earning schedules.[119] Regardless, the Proposed Rule does nothing to address the reality that multiple late payments demonstrate an increased credit risk and reflect a more serious violation of the account terms—even if those payments occur before the account would be reported as late under credit reporting guidelines. Moreover, the existence of an adequate late fee creates an incentive for customers who may experience financial difficulties to call in and discuss the availability of hardship and other programs with their lender.

Once again, the Proposed Rule's reference to other mechanisms to address repeated instances of late payments ignores that part of the purpose of penalty fees is to encourage customers to use credit responsibly, deter them from making poor decisions, and avoid them from being impacted by those longer-term and higher-cost alternatives. Cardholder agreements require that customers pay by the due date. That serves the purpose of honoring the contract, helping the customer use credit responsibly and avoid longer-term negative consequences, and aiding the issuer in credit-risk management and the assessment of the customer's likelihood of default in the future.

In reversing the Federal Reserve's approach, the Proposed Rule does not cite research, studies, or any evidence whatsoever—save the Y-14 data (which cannot and should not be relied upon for the reasons discussed earlier) that the Proposed Rule used to estimate that "three out of five accounts paid the amount due within 30 days of the payment due date."[120] In fact, the Proposed Rule devotes a mere *six* paragraphs to its determinations and conclusions related to the customer conduct factor, one of which relates to other factors that can address credit risk and another relates to charge cards. Even if the Proposed Rule were not reversing course from the Federal Reserve's 2010 findings and conclusions, it would lack enough depth or detail to adequately comply with the Bureau's requirements in Section 1665d(c)(3).

D. The Proposed Rule's 25% Cap on Minimum Payments Is Inadequately Supported.

Currently, Regulation Z provides that "[a] card issuer must not impose a fee for violating the terms or other requirements of a credit card account under an open-end . . . consumer credit plan that exceeds the dollar amount associated with the violation."[121] The Proposed Rule asserts simply that "permitting a late fee that is 100 percent of the minimum

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[119] *See, e.g.*, *Frequently Asked Questions: Can I Change My Payment Due Date*, Chase, https://www.chase.com/personal/credit-cards/card-resource-center/cc-payments#:~:text=Choose%20%22Update%20settings%20%26%20preferences%22,we%20officially%20change%20the%20date (last visited May 3, 2023); *Your Payment Due Date*, Capital One, https://www.capitalone.com/help-center/credit-cards/your-payment-due-date/ (last visited May 3, 2023); *Account Management: Payment Options*, Discover, https://www.discover.com/account-management-tips/ (last visited May 3, 2023).

[120] 88 Fed. Reg. at 18923.

[121] 12 C.F.R. § 1026.52(b)(2)(i)(A).

payment does not appear to be reasonable and proportional to the consumer's conduct of paying late when the minimum payment is small."[122] Elaborating no further, the Proposed Rule seeks to "limit the dollar amount associated with a late payment to 25 percent of the required minimum periodic payment due immediately prior to assessment of the late payment."[123]

In justifying the cap, the Proposed Rule repeats many of the mistakes discussed above—focusing on the issuer's cost to the exclusion of the other statutory factors, and inappropriately narrowing the eligible costs. Specifically, the Proposed Rule claims that "lowering the limitation on late fees to 25 percent of the minimum payment due would still likely allow card issuers to cover contingency fees paid to third-party agencies for collecting the amount of the minimum payment prior to account charge-off."[124] The Proposed Rule acknowledges, however, "that the proposal could have the potential to limit the late fee to an amount that is insufficient to cover a card issuer's costs in collecting the late payment."[125] Confusing its reasoning even further, the Proposed Rule suggests that the inability to cover costs might cause card issuers to "build those costs into upfront rates, which has the additional benefit of resulting in greater transparency for consumers regarding the cost of using credit card accounts."[126] But according to the Bureau, the Proposed Rule seeks to minimize fees that customers cannot reasonably avoid. It seems incongruent then to advocate for an approach that shifts a late fee—which customers can avoid by paying on time—to something like an APR, which is not avoidable except by paying the balance in full every month.

Noticeably absent from the Proposed Rule is *any* discussion of the cap with respect to deterrence or the conduct of the cardholder. That is a problem because the cap, not the safe harbor, is the effective late fee limitation with meaningful frequency. The Proposed Rule tries to make the change sound small as a practical matter by saying that "based on the distribution of minimum payments due in the Y-14 on a monthly basis from October 2021 to September 2022, if card issuers could only charge up to 25 percent of the minimum payment, only 7.7 percent of accounts would have been charged a late fee of less than $8."[127] Taking that data at face value, however, the late fee on more than 7% of accounts that had a late payment in 2021 to 2022 would be at a level *less than* the $8 safe harbor. In short, the Proposed Rule fails to acknowledge any of the four statutory factors in imposing a late fee cap that applies to more than 7% of accounts. And without access to the data, there is no way to rule out the possibility that the 7.7% figure undercounts the true incidence. If, as the Proposed Rule acknowledges, an $8 late fee may cause more

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[122] 88 Fed. Reg. at 18929.
[123] *Id*. at 18928.
[124] *Id*.
[125] *Id*. at 18929.
[126] *Id.*
[127] *Id.*

consumers to pay late, a late fee that is less than that would multiply that effect.[128] The late fee would not adequately deter consumers from paying late and incurring the more severe impacts of late payments—delinquent credit reporting, credit line decreases, penalty repricing, etc. These consequences are likely to be borne more heavily by new-to-credit and rebuilding-credit customers for whom paying on time is critical to increasing their credit score and using credit responsibly.

E. The Bureau's Decision to Remove the Consumer Price Index Adjustments Ignores the Deterrence Factor Set Forth in the CARD Act.

The Proposed Rule notes that following the passage of the CARD Act and promulgation of the penalty fee rulemaking by the Federal Reserve, "the average late fee . . . declined by over $10 to $23 in the fourth quarter of 2010."[129] Thereafter, the Proposed Rules claims that "from 2010 through the onset of the COVID-19 pandemic, issuers had steadily been charging consumers more in credit card late fees each year"—largely driven by adjustments due to increases in the Consumer Price Index.[130] If the current proposal were reflected in 2010 dollars, it would reflect a late fee of approximately $5.74[131]—or substantially less than even consumer advocacy groups were proposing to the Federal Reserve for its 2010 rulemaking.[132] Although Director Chopra has claimed that the inflationary adjustment has "allowed credit card companies to hike the fees annually for inflation,"[133] adjusting the current safe harbor amounts to 2010 dollars reveals that they are actually *less* in real dollars than the amounts approved in 2010:

- 2010 Amounts—$25/$35
- 2023 Amounts—$30/41
- 2023 Amounts adjusted to 2010 dollars—$21.54/29.43[134]

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[128] *Id.* at 18919 ("The Bureau recognizes 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.").

[129] *Id.* at 18908.

[130] *Id.*

[131] CPI Inflation Calculator, U.S. Bureau of Labor Statistics, https://www.minneapolisfed.org/about-us/monetary-policy/inflation-calculator (last visited May 3, 2023). We calculated the buying power of $8 today in January 2010.

[132] Truth In Lending, 75 Fed. Reg. 37526, 37541 (June 29, 2010) (codified at 12 C.F.R. pt. 226) ("Consumer groups, a state consumer protection agency, and a municipal consumer protection agency suggested amounts ranging from $10 to $20 based on state laws (which are discussed in detail below) and the fees charged by credit unions and community banks.").

[133] 2023 Press Release, *supra* note 19.

[134] CPI Inflation Calculator, *supra* note 131.

The CARD Act requires that any reasonable and proportional standard consider cost, deterrence, and cardholder conduct,[135] all of which are meaningfully affected by inflation, as measured by the Consumer Price Index ("CPI"). As a matter of common sense, adjustment for inflation is necessary for late fees to continue to have an equivalent deterrent effect. As the value of the dollar decreases due to inflation, so does the deterrent effect of a penalty that stays the same. Accordingly, any deterrence impact of a fee of only $8 would be significantly eroded as time passed if the Bureau refused to allow for inflation adjustments, as suggested in the Proposed Rule. It has been 13 years since the credit card late fee safe harbor was last set. If the Bureau were to wait another 13 years to revisit the $8 fee safe harbor, the "real" value of the safe harbor would likely decrease significantly. In real terms, an $8 late payment fee 13 years from now is equivalent to an inflation-adjusted late payment fee of $4.24 today, based on recent inflation rates.[136]

Congress understood the necessity of a CPI adjustment when it enacted the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015.[137] Other agencies understand it too. Regulations governing penalty fees imposed by agencies consistently provide for increases based on CPI. In fact, the Bureau itself has acknowledged the importance of inflation adjustments to maintain the deterrent effect of monetary penalties and regularly adjusts its monetary penalties to "maintain the deterrent effect of civil penalties and to promote compliance with the law."[138] The Bureau adjusted its own penalty fee provisions based upon the CPI in December 2022.[139] The Government Accountability Office noted that the Bureau complied with the applicable provisions of the interagency agreements and reported civil monetary penalty information, including the annual inflation adjustment, in both the Federal Register and their agency financial report ("AFR") in 2019,[140] 2020,[141] 2021,[142] and 2022.[143]

In its Proposed Rule, as in its 2022 decision to withhold from issuers Regulation Z's CPI adjustment, the Bureau tells issuers to do as it says, not as it—and the rest of the federal government—does. The Bureau provides no explanation for this double standard

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135 15 U.S.C. § 1665d(c).

136 This figure was calculated based on the current inflation rate of 5%. *See Consumer Price Index*, U.S. Bureau of Labor Statistics, https://www.bls.gov/cpi/ (last visited May 3, 2023).

137 *See* Section 701 of the Bipartisan Budget Act of 2015, Pub. L. 114-74, 129 Stat. 584 (2015) (codified at 28 U.S.C. § 2461 note).

138 *Civil Penalty Inflation Adjustments*, CFPB, https://www.consumerfinance.gov/rules-policy/final-rules/civil-penalty-inflation-annual-adjustments/ (last visited May 3, 2023).

139 Civil Penalty Inflation Adjustments, 88 Fed. Reg. 1 (Jan. 3, 2023).

140 GAO, *Civil Monetary Penalties: Review of Federal Agencies' Compliance with the 2019 Annual Inflation Adjustment Requirements* 5 (June 10, 2020), https://www.gao.gov/assets/gao-20-538r.pdf.

141 GAO, *Civil Monetary Penalties: Review of Federal Agencies' Compliance with the 2020 Annual Inflation Adjustment Requirements* 5 (May 27, 2021), https://www.gao.gov/assets/gao-21-488r.pdf.

142 GAO, *Civil Monetary Penalties: Review of Federal Agencies' Compliance with the 2021 Annual Inflation Adjustment Requirements* 6 (Apr. 28, 2022), https://www.gao.gov/assets/730/720259.pdf.

143 GAO, *Civil Monetary Penalties: Review of Federal Agencies' Compliance with the 2022 Annual Inflation Adjustment Requirements* 5 (Apr. 27, 2023), https://www.gao.gov/assets/gao-23-106485.pdf.

or why the amount of a fee impacts deterrence for itself and other government agencies but not for credit card issuers. The Proposed Rule speculates that "automatic adjustments based on the CPI are not necessarily reflective of how the cost of late payment to issuers changes over time and, therefore, may not reflect the 'reasonable and proportional' standard in the statute."[144] And the Proposed Rule concludes that "[t]he deterrence of the proposed safe harbor amount is sufficiently high so that the Bureau is not concerned by the lesser deterrence of a potentially eroded real value under realistic trajectories for medium-term inflation before any potential readjustment could be put in effect," and "that the deterrent effect does not move in lockstep with the CPI."[145] These statements do not explain how the Proposed Rule could conclude that CPI adjustment is not necessary to deter consumers from late payments on credit card bills but is necessary to deter the same consumers from late payments on amounts owed to the government. Tellingly, the Proposed Rule does not address the inevitable effect of locking in, in the face of inflationary pressures, late fee limits that the Proposed Rule already acknowledges might result in more consumers paying late.[146] If the current proposal has a decreased deterrent effect, that eventuality is all but certain with inflationary pressures over time.

F. **The Proposed Rule's Suggestion of a 15-Day Grace Period for Late Fees Exceeds the Bureau's Authority and Is Arbitrary and Capricious.**

The Proposed Rule's suggestion of a 15-day grace period exceeds the Bureau's rulemaking authority delegated by the CARD Act and the Truth in Lending Act ("TILA"). The CARD Act delegates authority to the Bureau to establish a late fee that is "reasonable and proportional" to the omission/violation of paying late, but it says nothing about granting the Bureau authority to redefine when a credit card payment can be considered late by the issuer. Section 163 of TILA authorizes a creditor to "treat a payment on a credit card account under an open end consumer credit plan as late for any purpose" so long as the creditor has created reasonable procedures to ensure delivery of the periodic statement.[147] Requiring a 15-day courtesy period would redefine when an issuer can consider a payment to be late, contrary to congressional intent, the plain meaning of "late" payment, and background principles of contract law. Any general rulemaking authority granted to the Bureau cannot be read to eliminate the limitations created by other statutory provisions.

In addition, as the Bureau has noted, the CARD Act "was enacted to 'establish fair and transparent practices related to the extension of credit' in this market, regulating both the underwriting and pricing of credit card accounts."[148] Congress specifically contemplated ways in which credit card agreements could better serve this goal, requiring

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[144] 88 Fed. Reg. at 18926.

[145] *Id.*

[146] *See id.* at 18919, 18926.

[147] 15 U.S.C. § 1666b(a).

[148] *CARD Act Report*, CFPB 4 (2013), https://files.consumerfinance.gov/f/201309_cfpb_card-act-report.pdf.

upfront disclosures (Schumer Box Disclosures) and streamlined, clearer terms.[149] Congress even more specifically contemplated ways in which the agreements' disclosures concerning late payment deadlines could better serve the goal of transparency: the legislation mandated that "the periodic statement . . . shall include, in a conspicuous location on the billing statement, the date on which the payment is due or, if different, the date on which a late payment fee will be charged, together with the amount of the fee or charge to be imposed if payment is made after that date."[150]

The 15-day grace period for late fees suggested in the Proposed Rule would lead to decreased clarity and generate customer confusion. As the Proposed Rule acknowledges, there would be a significant possibility of customer confusion from separating the due date from the late payment date.[151] Simply put, if the Bureau believes that late fees that are clearly disclosed on its own mandated template "obscure the true cost" of the account,[152] then trying to create disclosures that seek to explain the negative impacts of late payments when the penalty fee is separated from the due date is totally unworkable. Things like credit line increases,[153] grace-period losses, incurring additional interest charges, and other impacts would likely impact consumers who pay after the due date but before the grace period has lapsed. Separating the two concepts would almost certainly cause customer confusion and lead to less transparency—one of the primary things the CARD Act was seeking to avoid.

G. **The Proposed Rule Would Have an Overall Negative Consumer Impact.**

As discussed above, late fees are an important risk-mitigation tool in the credit card pricing model, and limiting them would likely decrease average consumer welfare via increases in interest rates, membership fees, or other costs.

For example, studies suggest that imposing a cap on late fees as a result of the CARD Act may have resulted in increased interest rates.[154] Likewise, a study of the impact

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149 *Id.* at 63–64.

150 15 U.S.C. § 1637(b)(12)(A).

151 88 Fed. Reg. at 18930 ("[T]he Bureau also solicits comment on effective ways to help ensure that consumers understand that a 15-day courtesy period only relates to the late fee, and not to other possible consequences of paying late, such as the loss of a grace period or the application of a penalty rate.").

152 Press Release, CFPB Finds Credit Card Companies Charged $12 Billion in Late Fee Penalties in 2020, CFPB (Mar. 29, 2022), https://www.consumerfinance.gov/about-us/newsroom/cfpb-finds-credit-card-companies-charged-12-billion-in-late-fee-penalties-in-2020/.

153 Comptroller's Handbook: Credit Card Lending, *supra* note 38, at 34 ("Generally, lines are increased for account holders who have demonstrated the financial capacity to perform on a new, higher credit limit.").

154 Massoud et al., *The Cost of Being Late? The Case of Credit Card Penalty Fees*, 7 J. Fin. Stability 49 (2011).

of the Durbin Amendment found that imposing a cap on the fees paid to some banks on debit transactions resulted in "increased . . . deposit fees in response to the regulation."[155]

The fundamental purpose of the Bureau is to "to implement . . . Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive."[156] The legislation that created the Bureau established these foundational principles to ensure that any rule provided overall benefits—rather than harm—to consumers.[157]

The current proposal, however, misses the mark and falls short of that standard, thereby leaving—by the Bureau's own acknowledgment—an overwhelming majority of consumers with higher costs and more negative impacts with the rule, than without. As set forth more fully below, the Bureau has proposed a rule that would likely result in higher costs for at least 85% of cardholders.[158]

1. <u>The Proposed Rule Acknowledges More Harm Than Benefit to Consumers</u>.

The Proposed Rule itself recognizes the potential negative impact on consumers. In addition to acknowledging that cardholders who pay no late fees receive no benefits and might be harmed by the Proposed Rule, the Proposed Rule notes several additional ways in which customers might be harmed by its proposal:

- "The Bureau acknowledges the possibility that consumers who were more likely to pay attention to late fees than to other consequences of paying late, like interest charges, penalty rates, credit reporting, and the loss of a grace period, might be harmed in the short run if a reduction in late fees makes it more likely that they mistakenly miss payments."[159]

- "Other results in psychology and economics might suggest that the proposal might pose some harm to consumers for whom high late fees

[155] Benjamin S. Kay et al., *Bank Profitability and Debit Card Interchange Regulation: Bank Responses to the Durbin Amendment* 5 (Fed. Reserve Bd., Finance & Economics Discussion Series, Working Paper, Paper No. 2014-77), https://www.federalreserve.gov/econresdata/feds/2014/files/201477pap.pdf.

[156] 12 U.S.C. § 5511(a).

[157] *Id.* §§ 5512(b)(2)(A)(i)–(ii).

[158] As demonstrated by the examples below, *see infra* pp. 36–37, if the Proposed Rule causes an increase in interest rates and/or other costs, then at least the never-late and the one-time-late populations, which consist of 74% and 11% of cardholders, respectively, are likely to be net harmed by the Proposed Rule. *See* CFPB *Credit Card Late Fees*, *supra* note 68, at 13 (determined using the share of accounts and share of late fee incidence by credit score data).

[159] 88 Fed. Reg. at 18935.

serve as a valuable commitment device without which they would have a harder time responsibly managing their credit card debt."[160]

- "Cardholders who never pay late will not benefit from the reduction in late fees and could pay more for their account if maintenance fees in their market segment rise in response—or if interest rates increase in response and these on-time cardholders also carry a balance."[161]

- "Besides any impact on collection costs, additional missed payments could result in additional delinquencies and ultimately increase credit losses."[162]

Although the list could go on, these excerpts show that the Proposed Rule would impose higher costs on customers who pay on time and carry a balance, and likely directly benefits only a small minority of "[f]requent late payers."[163] And as discussed above, the Bureau has failed to demonstrate that even those frequent late payers would receive net benefits from the Proposed Rule given that they would likely suffer more serious consequences such as decreased credit scores, lower credit lines, and penalty repricing.

2. <u>The Stated Purpose of the "Junk Fees" Initiative Is Inconsistent with the Acknowledged and Likely Impact of the Proposed Rule</u>.

The Proposed Rule is a foundational pillar of, and grows out of, the Administration's "junk fees" initiative.[164] The stated purpose of the "junk fees" initiative is to create "fair and transparent pricing" and avoid "impos[ing] fees on captive consumers—that is, consumers who are already locked into a product or service and have little choice but to pay the fee."[165] According to the White House, "[j]unk fees make it

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[160] *Id.*

[161] *Id.* at 18934.

[162] *Id.* at 18935.

[163] *Id.* at 18934.

[164] Junk Fees Press Release, *supra* note 27. That Director Chopra refers to late fees based on existing safe harbors as "junk fees" and "regulatory loophole[s]" shows that he lacks the necessary open-mindedness required in rulemaking. *See Ass'n of Nat'l Advertisers* v. *FTC*, 627 F.2d 1151 (D.C. Cir. 1980) (an agency decisionmaker must not act with an "unalterably closed mind"). This is compounded by the fact that President Biden described the safe harbor reduction in the State of the Union, not as a proposal, but as a *fait accompli*. *See Remarks of President Joe Biden – State of the Union as Prepared for Delivery*, The White House (Feb. 7, 2023), https://www.whitehouse.gov/briefing-room/speeches-remarks/2023/02/07/remarks-of-president-joe-biden-state-of-the-union-address-as-prepared-for-delivery/.

[165] *Guide for States: Cracking Down on Junk Fees to Lower Costs for Consumers*, The White House, https://www.whitehouse.gov/wp-content/uploads/2023/03/WH-Junk-Fees-Guide-for-States.pdf (last visited May 3, 2023).

difficult, if not impossible, for consumers to comparison-shop. Junk fees also take advantage of circumstances in which consumers do not have the power to shop around."[166]

That purpose is reflected in the Proposed Rule, which observes that "many consumers may not shop for credit cards based on the amount of late fees . . . [and] that other factors, such as rewards, annual fees, and annual percentage rate(s) (APR), drive credit card usage."[167] Thus, one of the principal goals animating the Bureau's rulemaking is to shift the "cost" of late payments into up-front pricing in areas like APRs and annual membership fees.[168] As with many aspects of the Proposed Rule, however, "[t]he Bureau is not aware of data that could help quantify such effects."[169]

To the contrary, as the Bureau acknowledges, the Proposed Rule would likely result in increased APRs and membership fees. The net result of the Proposed Rule would likely be negative for the following reasons.

- *First*, although consumers may be able to comparison-shop for APRs at account inception and before they are carrying a balance, the imposition of a higher APR is more costly over the longer term—and is not something they can easily avoid except through payment of the balance in full.

- *Second*, the acknowledged potential for increased delinquencies may result in lower credit scores and make it more difficult to transfer balances or move to new cards. More broadly, it may result in higher costs on other sources of credit.

- *Finally*, the CARD Act envisions that the burden of late payments should be borne by those who pay late, and it would be incongruous with the stated purpose of the statute to impose higher costs on *all customers*, including those using credit responsibly.

In short, the Proposed Rule acknowledges that the Bureau has no data to quantify the impacts of its proposal and the purported benefits that would benefit consumers from shifting late fee costs to up-front pricing—when all existing evidence would indicate the opposite.

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166 *Id*.

167 88 Fed. Reg. at 18908, 18934.

168 Importantly, the Proposed Rule does not appear to have any evidence that the terms will achieve those results. *See id.* at 18935 ("Whether or not changes to other prices offset a reduction in late fee revenue, consumers *may benefit* if, when choosing a credit card, they have a more accurate view of the expected total costs of using the card. To the extent that some consumers become better informed about the terms of credit cards, issuers *may respond* by offering improved terms, which could benefit even consumers who do not shop around. In addition, consumers *might benefit* or incur costs from further repricing and restructuring other financial products cross-marketed by credit card issuers and their holding companies." (emphases added)).

169 *Id*.

3. <u>The Other Deterrent Effects Identified by the Bureau in Support of Its Proposed Rule All Cause Larger and Longer-Term Impacts to Customers Than Late Fees</u>.

The Proposed Rule also cites a number of considerations that it maintains provide a deterrence effect notwithstanding its proposed low late fee amount. The Bureau, however, once again fails to point to any evidence that substantiates those conclusions. For example, the Proposed Rule points to a number of potential options for card issuers, including increasing minimum payments, adjusting credit limits, increasing other prices, reporting as late to the credit bureaus sooner, decreasing a consumer's credit line, limiting redemption of rewards, or imposing penalty rates.[170] One of our clients has undertaken a preliminary analysis of the changes that would be required if the Proposed Rule were adopted, and anticipates that, as the Bureau suggests, the Proposed Rule would require several changes to their credit card products.

As an initial matter, despite the Proposed Rule's alternative suggestions, the CARD Act leaves credit issuers with few ways to increase the price of credit only to borrowers showing recent signs of becoming less creditworthy. Under the CARD Act, credit card issuers generally cannot raise interest rates, or any fees, during the first year an account is open, and can change rates after that only on new charges (not existing balances) except "when a variable rate changes, a promotional rate ends or a required minimum payment is more than 60 days late."[171] When combined with an $8 safe harbor on late fees, the effect is that banks would likely offer higher rates and lower credit access than they otherwise would have to a broad range of consumers, including many who pay on time. In any event, the Proposed Rule suggests that consumers would be better off if banks set higher upfront interest rates rather than charge late fees[172] but fails to consider academic literature that

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[170] *Id.* at 18936. Studies have shown similar responses by issuers to the CARD Act. *See, e.g.*, Massoud et al., *supra* note 154. Specifically, a study considering the impact of the Durbin Amendment capping the fees paid to some banks on debit transactions found that "covered banks increased their deposit fees [charged to consumers] in response to the regulation. While these increases are generally insufficient to mitigate all the lost interchange income [due to the regulatory cap], changes in deposit fees offset roughly 30 percent of the lost interchange income." *See* Kay et al., *supra* note 155.

[171] *Fact Sheet: Provisions in the 2009 Credit CARD Act*, Consumer Action (July 18, 2010), https://www.consumer-action.org/downloads/alerts/CC_law.pdf.

[172] 88 Fed. Reg. at 18919 ("Card issuers also may undertake efforts to reduce collection costs or use interest rates or other charges to recover some of the costs of collecting late payments. Building those costs into upfront rates would provide consumers greater transparency regarding the cost of using their credit card accounts.").

indicates that interest rates may have a weaker deterrent effect as compared to late fees[173] due to consumers' relative understanding of both mechanisms.[174]

In addition to likely causing banks to raise interest rates, an $8 safe harbor would likely cause banks to reduce the credit they offer. Evidence from other fee and interest rate regulations suggests that limiting fees and rates can lead to credit rationing, leaving riskier borrowers with less access to credit.[175] The Proposed Rule therefore risks exacerbating an existing credit-access problem in the United States: the Bureau's own study finds that over 40% of consumers who applied for credit (of any kind, not just credit cards) either did not obtain it or did not obtain as much as they wanted.[176]

The Bureau has also reported on credit line decreases, when a credit card issuer reduces a cardholder's credit limit amount on an existing open account.[177] The Bureau has specifically identified a number of negative consequences of credit line decreases—a sudden decline in access to credit, higher utilization rate, credit score impacts, and perceived unfairness to the customer.[178] While credit line decreases play an important and

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173 *See, e.g.*, John T. Warner & Saul Pleeter, *The Personal Discount Rate: Evidence from Military Downsizing Programs*, 91 AM. ECON. REV. 33–53 (Mar. 2001); Jonathan Cohen et al., *Measuring Time Preferences*, 58 J. Econ. Lit. 299–347 (Jun. 2020).

174 A survey on debt literacy found that fewer than 36% of respondents had a basic understanding of interest compounding. Annamaria Lusardi & Peter Tufano, *Debt Literacy, Financial Experiences, and Overindebtedness* 7 (NBER Working Paper, Paper No. 14808), https://www.nber.org/papers/w14808. Additionally, financial literature shows that individuals underestimate interest payments and, furthermore, that this bias is strongly correlated with more borrowing and less saving. *See, e.g.*, Matthew R. Levy & Joshua Tasoff, *Exponential-growth Bias and Overconfidence*, 58 J. Econ. Psychol. 1–41 (Nov. 3, 2016); Victor Stango & Jonathan Zinman, *Exponential Growth Bias and Household Finance*, 64 J. Fin. 2807–2849 (Dec. 2009).

175 An academic study found that reducing the cap on interest rates for consumer loans in Chile by 20 percentage points led to a 19% decrease in the number of loans. *See* José I. Cuesta & Alberto Sepúlveda, *Price Regulation in Credit Markets: A Trade-off Between Consumer Protection and Credit Access* 1, 2 (Stanford Inst. Econ. Policy, Working Paper No. 21-047), https://drive.google.com/file/d/1VJcQ7-Kao6erTo7_fU1wTFzS3SR3OV5R/view. Conversely, a study published by the New York Federal Reserve found that there is a positive relation between overdraft fees and banks' willingness to cover overdrafts. *See* Jennifer Dlugosz, et al., *Hold the Check: Overdrafts, Fee Caps, and Financial Inclusion*, FEDERAL RESERVE BANK OF NEW YORK (June 30, 2021), https://libertystreeteconomics.newyorkfed.org/2021/06/hold-the-check-overdrafts-fee-caps-and-financial-inclusion/.

176 *Making Ends Meet in 2022: Insights from the CFPB Making Ends Meet Survey*, CFPB (Dec. 2022), https://files.consumerfinance.gov/f/documents/cfpb_making-ends-meet-in-2022_report_2022-12.pdf.

177 Credit Card Line Decreases Report, *supra* note 112, at 2.

178 *Id*. at 3–4 (finding that "[w]hile CLDs might prevent consumers from taking on more credit than they can afford, CLDs can also have significant negative repercussions on consumers. First, consumers can experience a sudden decline in their access to credit, which may compound existing financial pressures and reduce resilience. For example, Visa noted that past across-the-board CLDs during the Great Recession led to accelerated spending by at-risk customers as they saw their life line quickly disappearing. CFPB market monitoring indicates that one reason issuers might choose not to notify consumers in advance about a CLD is to prevent them from taking countervailing action, such as running

necessary role in credit risk management, overutilization of the mechanism as a substitute for late fees would only exacerbate the aspects of credit line decreases that the Bureau is already criticizing.

Moreover, absent late fees that have a meaningful deterrent effect, a credit card issuer may choose to stop extending additional credit to a cardholder following a failure to pay the minimum balance due—or not extend credit to those borrowers in the first instance.[179] The Bureau reports that cardholders with a recent delinquency are four times more likely than other cardholders to have a credit line decrease.[180] Accordingly, if a cardholder chose to not pay their minimum balance in exercising the Bureau's goal of flexibility for payment of their amounts due each month, the reduction in credit line may be at a time when the value of that credit line to the cardholder is particularly high and the cardholder would have preferred paying a higher late fee than to have lost access to additional credit or make accessing credit more difficult.

Further, the likely responses to the Proposed Rule might disproportionately affect low-income communities by decreasing access to credit for that segment of the population. In the alternative, these communities could be forced to turn to inferior credit alternatives, bouncing checks,[181] bank overdrafts,[182] or missed payments.[183]

For all of the reasons outlined above, the alternatives and mitigation factors suggested by the Proposed Rule actually would cause more consumer harm than the status quo. By way of example, consider the following hypothetical situations of an increased APR that the Bureau posits is a possible outcome of its proposal. Note that Examples 2, 3, and 4 assume that the customer stops using the card and incurs no additional charges. If the customer continues to use the card, the impacts of the increased APR would be more sizeable and cost the customer more than the examples set forth below.

- **Example 1—Customer Making Continued Purchases and Paying on Time**
    - *Current Rule*—Assume Customer A has a 30% APR, can afford $100 as a monthly payment that is consistently made on time, and balances spending and payments in order to maintain a $1,000 average balance over the course of a year. Customer A will make $1,200 in total

up their credit line. Business practices related to providing transparency and reasons for the CLD to consumers also appear to vary by issuer.") (citations omitted).

[179] *Id*. at 3 ("A line decrease can also be used to limit exposure on accounts perceived as a higher credit risk compared to other accounts.").

[180] *Id*. at 6.

[181] *See, e.g.*, Donald P. Morgan et al., *How Payday Credit Access Affects Overdrafts and Other Outcomes*, 44 JMCB 519–531 (Mar. 2012), https://doi.org/10.1111/j.1538-4616.2011.00499.x.

[182] *See, e.g.*, Neil Bhutta et al., *Consumer Borrowing After Payday Loan Bans*, 59 J. L & Econ. 225 (Feb. 2016), https://www.journals.uchicago.edu/doi/10.1086/686033.

[183] *See, e.g.*, Chintal A. Desai & Gregory Elliehausen, *The Effect of State Bans of Payday Lending on Consumer Credit Delinquencies*, 64 QREF 94 (May 2017).

payments, incur $300 in total finance charges, and have $900 in ability to spend over the course of the year.

- *Proposed Rule*—Assume the same scenario, but that Customer A's APR is now 33% because of the Proposed Rule. The customer will make the same $1,200 in total payments; however, the customer now incurs $330 in total finance charges (an increase of $30 for the year) and will have reduced their spending ability in turn by $30 to $870 for the year.

- **Example 2—Customer Paying Balance Down on Time**

  - *Current Rule*—Assume Customer B carries a $1,000 balance with an APR of 30% and chooses to pay $40 a month without using the credit card for any new purchase. Over the course of the account, Customer B will pay off the account in three years and four months, incurring $587.18 in interest.

  - *Proposed Rule*—Assume all the same terms above, but that Customer B's APR increases to 33% because of the Proposed Rule. Over the course of the account, Customer B will pay off the account in three years and seven months, incurring $712.69 in interest, or over ~ $120 more in interest.[184]

- **Example 3—Customer Paying Balance Down and Making One Late Payment**

  - *Current Rule*—Assume Customer C carries a $1,000 balance with an APR of 30% and chooses to pay $40 a month without using the credit card for any new purchase. The customer is late one month, and pays the regular payment plus the late fee that month. Over the course of the account, Customer C will pay off the account in three years and four months, incurring $588.16 in interest and a $30 late fee.

  - *Proposed Rule*—Assume all the same terms above, but that Customer C's APR increases to 33% because of the Proposed Rule, and the customer pays $8 for the late fee. Over the course of the account, Customer C will pay off the account in three years and seven months, incurring $713.01 in interest and an $8 late fee, or ~ $103 more over the course of the account.

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[184] If the customer continues to use the card, the impacts of the increased APR will be far more sizeable and cost the customer far more than the example provided.

- **Example 4—Customer Paying Balance Down and Making Two Late Payments**
    - *Current Rule*—Assume Customer D carries a $1,000 balance, an APR of 30%, and chooses to pay $40 a month without using the credit card for any new purchase. The customer is late two months (within six months of each other), and pays the regular payment plus the late fees for each of those months. Over the course of the account, Customer D will pay off the account in three years and four months, incurring $596.10 in interest and $71 in late fees ($30 for the first occurrence, and $41 for the second).
    - *Proposed Rule*—Assume all the same terms above, but that Customer D's APR increases to 33% because of the Proposed Rule, and the customer pays $8 for each late fee. Over the course of the account, Customer D will pay off the account in three years and seven months, incurring $715.24 in interest and $16 in late fees, or ~ $64 more over the course of the account. Under this scenario, the customer only pays less under the proposed rule once he or she pays four or five late fees, depending on the individual timing of those late payments.

In summary, the vast majority of customers—including those who pay on time—would be negatively affected by the secondary impacts of the Proposed Rule.[185]

H. <u>The Bureau Failed Adequately to Consider the Benefits and Costs of Its Proposal as Required by Section 1022(b)(2)(A) of the Dodd-Frank Act</u>.

Section 1022(b)(2)(A) makes clear that the Bureau, as part of any rulemaking, is required to consider "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 such rule; and . . . the impact of proposed rules on covered persons, as described in section 1026, and the impact on consumers in rural areas."[186]

While the Bureau acknowledged various costs imposed by the Proposed Rule, it has failed to provide reasoned, evidence-based support for its assessment that the Proposed Rule would result in a net benefit for consumers. As discussed above, the proposal would benefit only the very small subset of the consumer population that regularly pays late fees. And the Proposed Rule acknowledges that cardholders who never make late payments would not benefit and would be worse off due to potential increases in maintenance fees and APRs. Even within the subset of subprime consumers, benefits are limited given the

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[185] Credit Card Late Fees: Figure Data, *supra* note 155.

[186] Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. Law 111-203, §§ 1022(b)(a)(A)(i)–(ii), 12 U.S.C. §§ 5512(c)(4)(b)(i)–(ii).

Bureau's own research that concludes nearly half of subprime credit card accounts paid no late fees in 2019.[187]

With respect to the population of subprime consumers that regularly pay late fees, the proposal fails adequately to consider that any benefits received would ultimately be offset by any of the possible outcomes articulated by the Bureau in the Proposed Rule: increases in the APR; reduced access to credit; increased delinquencies and negative credit reporting; or increases in other credit card fees.[188] These changes would have serious negative implications for subprime customers with lower FICO scores. The current regime permits those with thin or poor credit history to access credit, but the Bureau acknowledges that the Proposed Rule would require card issuers to revise their credit models to satisfy statutory requirements and account for the decrease in liquidity and heightened portfolio risk. And as discussed above, the population of subprime borrowers who make their payments each month on time would bear even greater costs. The rule would thus disproportionately harm the subprime customer market—the very segment that the Bureau is trying to help by pursuing this rule.

The Proposed Rule's consideration of costs and burdens is also flawed because it fails adequately to consider the cost of compliance for card issuers.[189] As previewed, the Proposed Rule would impose disproportionately high costs on credit card issuers that service subprime borrowers, many of whom may need to exceed the $8 safe harbor. Such issuers would need to spend significant resources to build internal processes and procedures for calculating and documenting the costs of late fees. The proposal would also require such issuers to spend significant resources building out an evidentiary record before departing from the safe harbor, particularly in light of the Bureau's ungrounded and repeated assertions that credit card late fees are "junk fees."

Finally, one important consideration for the Proposed Rule is reliance, which dovetails with the heightened importance of the Bureau's burden in proposing to change longstanding policy. The Bureau must accordingly demonstrate that it has adequately considered the various reliance interests at stake.[190] Both issuers and cardholders have significant reliance interests, because they have made financial decisions and entered credit card agreements within the existing penalty regime. The Proposed Rule directly undermines the provisions of those agreements concerning late fees and due dates, and the potential fallout from the Proposed Rule threatens many others.

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[187] *Id*.

[188] The Comprehensive Capital Analysis and Review (CCAR) and Dodd-Frank Act Stress Tests (DFAST) establish certain stress-testing obligations that require certain large banks to maintain certain liquidity levels to meet statutory capital requirements. *See* 12 C.F.R. § 225.8.

[189] *See Michigan* v. *EPA*, 576 U.S. 743, 759–760 (2015).

[190] *Department of Homeland Security* v. *Regents of the University of California*, 140 S. Ct. 1891, 1913–1915 (2020).

Since the CARD Act, many banks voluntarily ceased disclosing or applying penalty repricing to new transactions (due to late payment) and/or existing balances (when the account is past due 60 days) because the late fee penalty made it unnecessary and better allowed consumers to avoid longer-term consequences of paying late. If the Proposed Rule is adopted, those decisions will certainly be revisited across the industry, and with it, the attendant costs associated with administering those programs and the reevaluation of that repricing (which will increase the cost associated with late payments). Moreover, the availability of no-fee cards may very well become less prevalent, membership and/or account maintenance fees could increase or become more prevalent, and a material constriction of credit would occur. Card issuers also have reliance interests in the existing safe harbor, which provides a meaningful alternative to developing the procedural and methodological infrastructure that would be necessary to independently calculate the cost of penalty fees with the degree of precision the Bureau proposes to require. The Bureau neglected to weigh the Proposed Rule's impact on the various reliance interests of either cardholders or issuers who have structured myriad financial decisions according to the existing regime.

I. The Bureau's Decision to Ignore the Delayed Implementation Timelines under Section 105(d) of TILA Is Improper.

Section 105(d) of TILA states that "[a]ny regulation of the Bureau, or any amendment or interpretation thereof, requiring any disclosure which differs from the disclosures previously required by this part, part D, or part E or by any regulation of the Bureau promulgated thereunder shall have an effective date of that October 1 which follows by at least six months the date of promulgation."[191] The Proposed Rule includes a number of suggested changes to the Bureau's form disclosures and tabular disclosures as a result of the proposed maximum late fee safe harbor of $8, reduction of the permissible costs under a cost-based approach, or 25% cap.[192]

Nevertheless, the Proposed Rule concludes that "this proposal, if finalized, would not differ from the current requirement to disclose late fee amounts; instead, it would solely result in a change to the amount of the late fee disclosed for issuers using the safe harbor."[193] In addition, the Proposed Rule states that "this change in amount applies to the safe harbor, which is an amount that card issuers may elect but are not required to use."[194]

These conclusions are woefully incorrect given the scope of the Proposed Rule. *First*, the Proposed Rule does not simply change the amount of the safe harbor—it also changes how costs are calculated and what may be included in those costs under Section 1026.52(b)(1)(i) for those issuers not using the safe harbor, and it places a cap on the late fee of 25% of the minimum payment. *Second*, and equally important, the Proposed

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[191] 15 U.S.C. § 1604(d).
[192] 88 Fed. Reg. at 18930–18931.
[193] *Id.* at 18931.
[194] *Id*.

Rule points to a number of different levers that it relies on as providing the necessary deterrent effect (penalty pricing, trigger repricing, etc.) if the late fee is significantly reduced as proposed—many of which have become less important in light of the CARD Act and prior rulemaking around penalty fees. These changes would require cardholder disclosures changes, likely for all credit card issuers.

Although our clients believe the Bureau's conclusions relating to the Proposed Rule need to be revisited in light of the comments above, the Proposed Rule's determination that Section 105(d) does not apply cannot be maintained in light of its own conclusions. The Proposed Rule acknowledges that some portion of issuers would rely upon cost calculations under Section 1026.52(b)(1)(i) to determine the late fee amounts they can charge consumers, rather than the $8 safe harbor.[195] If the Proposed Rule is correct in assuming that pre-charge-off collection costs fall below the late fee amounts currently charged by issuers, then it means that issuers do not currently have in place the proper processes to calculate these collection costs in a manner designed to ensure compliance. This means that the proposal requires a change to the required cardholder disclosures. The delayed effective date requirements of Section 105(d) of TILA are necessary not only to accommodate the changes in disclosures, but also to provide issuers sufficient time to put in place systems to calculate the late fee amounts they can charge customers, which then become the subject of the disclosures.

Indeed, the Bureau has just recently published a Paperwork Reduction Act notice in the Federal Register on April 18, 2023, for an information collection related to its "Junk Fees Timing Study."[196] The results of this information collection will likely be relevant to its late fee rulemaking as it discusses the impact of disclosure on fees on consumer behavior.

Finally, the need for a delayed effective date is further heightened by *Community Financial Services Association of America* v. *CFPB*,[197] which is pending before the Supreme Court. Last October, the U.S. Court of Appeals for the Fifth Circuit held that the Bureau's funding mechanism violates the Appropriations Clause of the U.S. Constitution.[198] The Bureau should delay the effective date of this rulemaking until the Supreme Court has decided that case in its next term. Requiring compliance with a new rule before that decision is issued could result in a waste of resources for issuers and significant confusion for consumers if the Supreme Court's decision causes the rule to be void. At a minimum, the Proposed Rule fails to evaluate the costs and benefits under

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[195] *Id.* 18913.

[196] Agency Information Collection Activities: Comment Request, 88 Fed. Reg. 23646 (proposed Apr. 18, 2023).

[197] *CFPB* v. *Consumer Fin. Servs. Ass'n*, No. 22-448, 143 S. Ct. 978 (petition for cert. granted Feb. 27, 2023).

[198] *Id.*

Section 1022(b)(2)(A) of adopting an effective date for the Proposed Rule that occurs prior to the Supreme Court's resolution of this key issue.

Conclusion

Despite statutory requirements, the Proposed Rule fails adequately to consider deterrence or consumer behavior, considers only a subset of relevant costs, and relies on data that is not publicly disclosed and thus does not satisfy the APA. And despite the alleged benefits it cites, the Proposed Rule acknowledges that changes would likely occur—higher APRs, higher fees, and less access to credit—with the result that consumers would be worse off than in the status quo.

The CARD Act requires a holistic evaluation that accounts for the numerous purposes late fees serve, and the interests of both consumers and issuers. Discharging that duty, the Federal Reserve in 2010 struck a balance between the competing statutory factors required by the CARD Act. The Bureau is likewise obliged to discharge that statutory duty and satisfy the burden of establishing an adequate factual basis for changing the rules. The Proposed Rule falls short at every step, culminating in an acknowledgment that a significant portion of consumers would either receive no benefit or even be harmed under the proposal.

Put simply, this rulemaking is being rushed. Existing studies that cut against the proposal have been summarily cast aside, without any peer-reviewed and empirical studies to support the proposal. Moreover, in an increasing inflationary environment and against a backdrop of failed and downgraded banks, it would be careless to rush to implement a final rule before the full extent of its impacts on consumers and the banking sector have been evaluated. Pressing forward with the rulemaking in light of the problems outlined here, and the impact on consumers and the industry, is dangerous. We respectfully request that the Bureau pause the rulemaking and revise its proposal to satisfy its statutory, evidentiary, and consumer protection obligations.

Respectfully submitted,
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