

Agencies Issue Joint Proposed Rules To Rein In Credit Card And Deposit Account Providers

In the wake of the subprime lending crisis, government agencies are reining in credit card and deposit account providers by placing new limitations on the rates and terms of their products. With such changes in the works, credit card and deposit account providers must move quickly to ensure that their voices are heard.

Proposed Rulemaking

On May 2, 2008, the Board of Governors of the Federal Reserve System ("Board") issued a proposed rulemaking for notice and comment under the Federal Trade Commission Act, the Truth in Lending Act, and the Truth in Savings Act. The proposed rulemaking would modify Regulation AA, Regulation Z, and Regulation DD. The modifications place substantial limitations on the rates and terms of credit cards and also alter overdraft protection plans for deposit accounts. In an effort to require consistency across the practices of all types of financial institutions, the Office of Thrift Supervision and the National Credit Union Administration published similar proposals for their own versions of Regulation AA, applicable to savings and loan associations and federally-chartered credit unions, respectively.

As stated by Board Chairman Ben S. Bernanke, the "proposed rules are intended to establish a new baseline for fairness in how credit card plans operate." This "new baseline" prohibits unexpected increases of interest rates applicable to pre-existing credit card balances and also prevents maximizing interest charges through the use of certain payment-allocation methods. In addition to altering financial institution credit card practices, the proposed regulations also require that financial institutions provide consumers with a chance to opt out of overdraft payments, eliminating the possibility of overdraft fees.

Regulation AA – Credit Card Regulations

In relation to the practices of credit cards providers, the proposed rules alter Regulation AA in many ways, including:

- **Existing Balance Rate Increases:** The proposed rules prohibit increasing the rate on existing balances unless the rate is tied to an index, a promotional rate expires, or the minimum due is not received within 30 days following the due date.
- **Payment Times:** Under the proposed rules, credit card payments may not be considered "late" unless the provider gives reasonable time to make payments (including a safe harbor provision for providers that send statements at least 21 days before the payment due date).
- **Payment Allocation:** Payments above the minimum due, made when multiple rates apply to multiple balances, would require allocation by one of three methods. Applying the entire payment to the lowest rate will no longer be permitted. Further, all payments above the minimum due must be allocated first to non-discounted-rate balances.
- **Two-Cycle Billing:** The proposed rules prohibit calculating finance charges in relation to days in billing cycles preceding the current billing cycle.
- **Firm Offers of Credit:** Financial institutions advertising offers of credit with multiple rates would be required to disclose the factors assessed to determine if the consumer qualifies for the lowest rate.
- **Credit Card Holds:** The proposed rules prohibit imposing fees when the credit limit is exceeded because of a hold on available credit.
- **Subprime Credit Cards:** The proposed rules prohibit financing security deposits and credit availability fees, if such charges over the first year would exceed 50 percent of the initial credit limit. Also,

financed security deposits and credit availability fees exceeding 25 percent of the initial credit limit must be spread across the first year.

Regulation AA – Overdraft Regulations

Regulation AA also contains new rules regarding overdraft payments on consumer deposit accounts at financial institutions, including:

- Opt Out Rights: The new rules prohibit assessing overdraft fees, unless the consumer was given a chance to opt out of overdraft payment services and declined. Also, the financial institution must offer a partial opt out for ATM and point-of-sale.
- Debit Holds: No fees may be imposed when the account is overdrawn because of a hold on available funds.

Regulations Z and DD

The Board's proposed rules also alter Regulations Z and DD in their attempt to rein in credit card and deposit account providers. As to Regulation Z, the proposed rules require that mailed credit card payments received by 5:00 p.m. be considered timely. Further, in cases when the due date falls on a weekend or holiday, payments received by mail the next business day must be considered timely.

As to Regulation DD, financial institutions must:

- Disclose month-to-date and year-to-date totals for overdraft and returned-item fees on periodic statements; and
- Disclose available funds irrespective of funds to cover overdrafts, when using an automated information system.

Key Dates and Actions

Interested parties may now submit comments on the proposed rules. The comment period for Regulation AA concludes 75 days after publication in the Federal Register. For Regulations Z and DD, the comment period ends just 60 days after publication. Publication is expected soon.

Although still in the notice and comment phase, these regulatory changes are coming. Financial institutions that provide credit cards and deposit accounts should consider participating in the comment period. And, once the rules are finalized, financial institutions should move quickly to develop and implement a plan for compliance with the new rules.

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