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By Electronic Delivery

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

RE: Regulation Z; Docket No. R–1364 (Interim Final Rule)

Dear Ms. Johnson:

In the following comments, we respond to the Board's Interim Final Rule under Regulation Z, published at 74 FR 139 (July 22, 2009) at p. 36077 et. seq., according to new requirements found in the Credit CARD Act of 2009. Our comments include the following key points:

1. Exceptions to § 226.9 notice requirements for fluctuations in variable interest rates should not apply to any account for which the issuer requires a fixed minimum interest rate to apply.

2. There is no basis in the Act for the proposed exception to the right to reject changes in terms for increases in minimum required payments, and it should be deleted.

3. The proposed exception to the requirement to notify cardholders of their right to cancel and avoid interest rate increases or other significant changes in cases where accounts are 60 days past due is unwarranted, and overbroad.

4. Issuers should be required to provide notice to cardholders within 45 days of the expiration of deferred interest periods.

Pew's Safe Credit Cards Project began in 2007 as a research-based effort to protect consumers from unfair credit card practices and promote responsible management of debt. We have published a set of Safe Credit Card Standards as well as various results from our research and analysis. Recently, we completed a new analysis of all credit cards offered by the largest 12 bank issuers and the largest 12 credit union issuers. We have included in our comments selected findings from this research, which will be published soon. Additional results will be available in our future comment letters to the Board. As always, we are available to discuss these comments or any other aspect of our work at any time.

Sincerely,

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1. Exceptions to § 226.9 notice requirements for fluctuations in variable interest rates should not apply on any account for which the issuer requires a fixed minimum interest rate to apply.

Pew's latest analysis of all consumer credit cards offered by the largest bank and credit union issuers found that bank issuers moved away from "fixed" interest rates and toward "variable" rates during the first half of this year.[1] We found that there is a related and possibly troubling trend emerging. A growing number of credit cards include terms designed to ensure that even variable rates will not fall lower than a fixed minimum set by the issuer. For these cards, issuers will benefit as interest rates rise according to operation of a third-party index rate, but many cardholders will be prevented from enjoying the benefits of falling index rates due to the fixed minimums set by issuers. For these cards, the issuer's chosen fixed minimum rate will apply regardless of the disclosed variable interest rate formula. We call this mechanism a *minimum rate requirement*.

The following example, taken from the application disclosures for the Wells Fargo Visa Platinum Card, demonstrates how the minimum rate requirement works.

Example: Wells Fargo Visa Platinum Card – Minimum Rate Requirement

Annual percentage rate (APR) for purchases	Introductory APRs range from 0.00% to 5.90% for the first 6 or 9 billing periods the account is open.[1] After that, APRs range from 8.65% to 22.65% depending on applicant's credit qualifications.

Variable rate information	Your APRs for purchase, cash advance and overdraft protection balances may vary. The purchase APR is determined by adding a margin ranging from 2.90 to 16.90 percentage points to the Index Rate. The cash advances and overdraft protection advances APR is determined monthly by adding 17.74 percentage points to the Index Rate. The Default Rate varies and is determined monthly by adding up to 23.99 percentage points to the Index Rate.[3]

[3]This Index Rate is equal to the highest prime rate published in the Money Rates column of *The Wall Street Journal* three business days prior to your billing statement closing date, subject to the applicable minimum APRs. The standard APRs for purchases are subject to minimum rates ranging from 8.65% to 22.65% and will not decrease below the applicable minimum rate regardless of changes to the Index Rate. The standard APRs on cash advances and overdraft protection advances are subject to a minimum rate of 23.49% and will not decrease below 23.49% regardless of changes to the Index Rate.

Source: Wells Fargo website, July 9, 2009

Since December of last year, use of this minimum rate requirement has increased among credit cards issued by the largest banks, from one percent to nine percent of cards (for purchase rates) and from ten percent to 38 percent of cards (for cash advance rates). In the

[1] Pew will soon release the second in our series of reports on credit card practices. In July of this year, we analyzed application disclosures for all consumer credit cards offered online by the largest 12 bank issuers and the largest 12 credit union issuers (a total of nearly 400 cards). Research of this analysis showed that, while nearly one-third of advertised purchase rates on bank cards were "fixed" in December, fewer than one percent were "fixed" in July. Additional results of this survey may appear in our future comment letters to the Board.

example above, this mechanism added a premium of 2.5 percentage points to the rate that would otherwise have applied based on the disclosed variable rate formula (assuming a current 3.25 percent index rate). The largest minimum rate requirement premium observed in our study was five percentage points.

Section 101(a) of the Credit CARD Act adds new Truth in Lending Act (TILA) Section 127, which requires 45-day advance notice of increases in interest rates, except under three conditions. These exceptions are referenced directly from new Section 171 of TILA, an excerpt of which follows [emphasis added]:

> SEC. 171. LIMITS ON INTEREST RATE, FEE, AND FINANCE CHARGE INCREASES APPLICABLE TO OUTSTANDING BALANCES.
>
> (a) In General- In the case of any credit card account under an open end consumer credit plan, no creditor may increase any annual percentage rate, fee, or finance charge applicable to any outstanding balance, except as permitted under subsection (b).
>
> (b) Exceptions- The prohibition under subsection (a) shall not apply to--
>
> > * * *
> >
> > (2) an increase in a variable annual percentage rate in accordance with a credit card agreement that provides for changes in the rate **according to operation of an index** that is **not under the control of the creditor** and is available to the general public;
> >
> > * * *

This exception, reflected in the Board's proposed paragraph (c)(2)(v)(C) of § 226.9, should not apply to cards including a minimum rate requirement because these cards do not provide for changes "according to operation of an index." Furthermore, by placing a minimum fixed floor against which the index cannot operate, the issuer has exercised control over the index in a way that violates the law's requirement.

The Board noted that changes based on operation of an index generally would not require notice because none of the terms required to be included in application disclosures have changed. 74 FR 139 at p. 36085. However, new Section 127(i) specifically requires 45 day advance notice before any "increase in interest rate" unless one of the three provided exceptions apply. The Board should clearly state that accounts including a minimum rate requirement are subject to the 45 day notice requirement because they do not meet the requirements set in new TILA Section 171(b)(2) for changes in rates according to operation of an index not under the control of the creditor. Since no other exception would apply, issuers should be required to send notice before rates increase.

Similarly, in its upcoming rulemaking efforts, the Board should make clear that accounts with minimum rate requirements will not qualify for the variable rate exception to the prohibition against interest rate increases on outstanding balances (new TILA Section 171(a)). As with the notice requirements, accounts with minimum fixed rates fall short of the law's exception for cards that operate in accordance with an index that is not under the control of the issuer. Furthermore, accounts with minimum rate requirements do not justify an exception allowing interest rates on outstanding balances to increase because they allow issuers to expose cardholders to risk of higher rates if the index rises while limiting cardholders' ability to benefit if the index falls.

2. There is no basis in the Act for the proposed exception to the right to reject changes in terms for increases in minimum required payments, and it should be deleted.

The interim rule concludes that an increase in the required minimum payment is not a change that the cardholder has a right to reject. 74 FR 139 at p. 36084. The effect of the Board's rule, taken to its conclusion, is that issuers can on 45 days notice require payment of all outstanding balances in full. This effect is not consistent with the clear intent of the legislation to eliminate practices under which issuers can unilaterally dictate repayment terms different from those to which cardholders agreed when they borrowed the credit.

For changes in terms that a cardholder has a right to reject, the Credit CARD Act provides protection from undue acceleration of the outstanding balance. Specifically, new TILA Sections 127(i)(4) and 171(c)(2) provide that when a cardholder rejects a change in terms, the issuer can close the account for future purchases but cannot require repayment of the outstanding balance on new terms less favorable than a five year repayment, or a minimum payment that no more than doubles the percentage of the balance due.

Increases in minimum payment are by the Board's proposed rule effectively exempted from this protection. The proposed rule would mean that while cardholders must get 45 days notice of an increase in the minimum payment, they have no remedy. The debtor must accept the increased payment requirement or be prepared to pay off the balance in full and close the account – not a solution that will help cardholders for whom an increase is a problem.

Thus, the Board's treatment of minimum payment increases creates a significant loophole in the protections Congress envisioned limiting acceleration of repayment of outstanding balances when cardholders choose to close an account. An issuer seeking to avoid the carefully crafted repayment protections of the law has only to increase the minimum payment to take away those protections from the cardholder and force repayment of the balance on a schedule far more accelerated than the Act otherwise provides.

The Board justifies forcing cardholders to accept unilateral minimum payment increases by pointing to Congress's concern that cardholders understand the result of paying only the minimum amount. 74 FR 139 at p.36085. Indeed, amended TILA Section 127(b)(11) requires that issuers disclose to cardholders that making only minimum payments will maximize the amount of interest they pay and the amortization period. Clearly Congress wanted cardholders to have this information to foster informed judgments about whether to pay more than the minimum required payment.

But the mandate that consumers have better information about the effects of minimum payments does not lead to the Board's conclusion that cardholders should not be able to reject an increase in the required minimum payment imposed by the issuer. If anything, that mandate points in the opposite direction. If cardholders do not have the right to continue making the minimum payment amounts they originally agreed to, even if doing so would lead to longer and more expensive payouts, the disclosures required by the Act about the adverse effect of such a choice would be meaningless.

3. The proposed exception to the requirement to notify cardholders of their right to cancel and avoid interest rate increases or other significant changes in cases where accounts are 60 days past due is unwarranted, and overbroad.

As explained below, we strongly encourage the Board to require issuers to provide cardholders with notice of the right to cancel any significant change in the account terms, even if the account is 60 days past due. Even if the Board finds that it can and should create an exception such that cardholders may not reject penalty rate increases after accounts become 60 days past due, the exception should be narrowly tailored so that only penalty interest rate increases triggered by the 60 day delinquency are exempted from the right to cancel requirement.

Section 101 of the Credit CARD Act of 2009 ("*Protection of Credit Cardholders*") requires issuers to provide advance notice of interest rate increases and other significant changes, and gives consumers the right to reject these changes by canceling the account. New Section 127 of TILA, as amended by the Credit CARD Act, includes the following language [emphasis added]:

> (i) Advance Notice of Rate Increase and Other Changes Required-
>
> > (1) ADVANCE NOTICE OF INCREASE IN INTEREST RATE REQUIRED- In the case of any credit card account under an open end consumer credit plan, a creditor shall provide a written notice of an increase in an annual percentage rate (except in the case of an increase described in paragraph (1), (2), or (3) of section 171(b)) not later than 45 days prior to the effective date of the increase.
> >
> > (2) ADVANCE NOTICE OF OTHER SIGNIFICANT CHANGES REQUIRED- In the case of any credit card account under an open end consumer credit plan, a creditor shall provide a written notice of **any significant change**, as determined by rule of the Board, in the terms (including an increase in any fee or finance charge, other than as provided in paragraph (1)) of the cardholder agreement between the creditor and the obligor, not later than 45 days prior to the effective date of the change.
> >
> > (3) NOTICE OF RIGHT TO CANCEL- **Each notice** required by paragraph (1) or (2) shall be made in a clear and conspicuous manner, and **shall contain a brief statement of the right of the obligor to cancel** the account pursuant to rules established by the Board before the effective date of the subject rate increase or other change.

This right to cancel found in paragraph 127(i)(3) attaches to "each notice" required by either 127(i)(1) or (i)(2). The law specifically allows only three exceptions when notice and right to cancel requirements do not attach, based on incorporating three of the four exceptions outlined in paragraph 171(b) of the law: for accounts that experience increased interest rates due to (1) expiration of a promotional rate, (2) changes in the rate according to operation of an index not under the control of the issuer, or (3) a cardholder's failure to complete a workout plan. The fourth paragraph and final 171(b) exception, for penalty rates triggered by delinquencies of 60 days or more, is pointedly not incorporated. Consequently, even in cases where accounts are 60 days past due, the new TILA Section 127(i) notice and right to cancel requirements should apply.

The Board's rules correctly reflect that issuers who reprice outstanding balances on accounts that are 60 days past due will be required to give 45 days advance notice of the increase. But the proposed rules create a new exception, excusing issuers from providing notice of the right to cancel and avoid the rate increase. Part of the Board's justification for creating this exception is based on "new TILA Section 127(i)(3)'s express grant of authority to establish rules implementing the right to cancel." 74 FR 139 at p. 36089. But while the relevant sections of the new law quoted above give the Board responsibility for determining what constitutes a "significant change" that triggers a right to notice (Section 127(i)(2)), and for establishing rules governing the manner in which an obligor can cancel the account (Section 127(i)(2)), they do not give the Board authority to create exceptions to the substantive right to receive these notices. The legislative text clearly incorporated a list of allowable exceptions, and this list pointedly did not include reference to the exception that the Board would create. In interpreting the new law, the Board should avoid allowing exceptions to a statutorily prescribed list in the absence of a specific mandate to do so.

The Board also based its authority for creating the exception to the notice of right to cancel requirement on its general authority under 15 U.S.C. 1604(a) to "make adjustments and exceptions to carry out the purposes of TILA. 74 FR 139 at p. 36089. The Board noted that, absent the creation of this exception:

> [A] consumer who is more than 60 days delinquent could use the right to reject a rate increase to override the exception specifically created by the Credit Card Act for such circumstances. The Board does not believe that this was Congress's intent because the Credit Card Act's exception for delinquencies of more than 60 days contains its own remedy for consumers. Specifically, the exception provides that, if an increased rate, fee, or finance charge is applied to an outstanding balance based on a delinquency of more than 60 days, the creditor must 'terminate such increase not later than 6 months after the date on which it is imposed, if the creditor receives the required minimum payments on time during that period…. Thus, based on its review of the Credit Card Act as a whole, the Board believes it would be inconsistent to extend the right to reject to circumstances where a consumer is more than 60 days delinquent. 74 FR 139 at p. 36090.

We disagree. The proposed exception would run contrary to the both the plain language and the purposes of the new law. The "exception specifically created by the Credit Card Act" referenced by the Board is an exception to a rule designed to protect cardholders from interest rate increases on outstanding balances, something the Board itself has determined to cause "substantial consumer injury," particularly in cases where issuers impose penalty rates using “hair trigger” repricing that can cause “unfair surprise.” 74 FR 18 (29 January 2009) at pp. 5522 and 5527. Congress created the 60-day exception as a bright-line rule indicating where outstanding balances could *possibly* be subject to an interest rate increase, but Congress did not intend for issuers to have unfettered power to raise rates in these cases. The cardholder’s rights continue to apply. Congress specifically established that consumers have a “right to cancel” that includes the right to avoid disclosed changes that are the subject of the notices required in new TILA Section 121(i)(1) and (2), including notices of penalty interest rates triggered by 60-day delinquencies.

Even if the Board holds that this exception to the right to cancel is necessary and appropriate, the proposed rules are overbroad, and go too far in exempting all accounts that are past due by 60 days from the right to reject *any* significant change. The Board’s true concern in creating the exception appears to be preventing cardholders from rejecting penalty charges triggered according to the provisions of new TILA Section 171(b)(4). However, proposed Section 226.9(c)(2)(iv)(D)(1) of the rules would prevent cardholders from rejecting *any* of the changes covered by paragraph (c)(2)(ii) of that section, including changes in annual percentage rates but also changes to fees for issuance or availability of the account, transaction charges, grace periods or a variety of fees and methods of calculating charges. While the Board is correct to note that a specific remedy for penalty increases is available, the Board’s proposed rule would create a loophole for non-penalty-related changes that would leave cardholders with no remedy at all.

This blanket exemption is overbroad and would not meet the law’s goal of giving consumers the option to reject substantive amendments to their account agreements. The Board should amend the proposed rule, either to remove the exemption completely or, at a minimum, to exempt issuers from the notice of right to cancel requirement *only* for penalty-related charges triggered by 60-day delinquencies (to which the law’s six-month cure period would apply). For all other significant changes identified by the Board, the notice of right to cancel should be provided for all accounts regardless of delinquency status.

4. Issuers should be required to provide notice to cardholders within 45 days of the expiration of deferred interest periods.

The Board stated that it intends to apply the exception to notice requirements found in Section 226.9(c)(2)(v)(B), regarding expiration of promotional interest rate periods, to deferred interest arrangements as well. 74 FR 139 at p. 36085. Because deferred interest promotions contain a unique danger to consumers (i.e., significant lump-sum interest charges that have accrued for 12 months or more *before* the promotion expires), we request that the Board refine its position so that issuers will be required to notify cardholders before the expiration of the deferred interest period even if cardholders will not have the right to reject imposition of deferred interest at the end of the period.

Our Safe Credit Card Standards call for the prohibition of deferred interest rates because they can be confusing and dangerous to consumers.[2] Deferred interest arrangements allow

[2] Pew’s Safe Credit Cards Project began in 2007 as an effort to protect customers from unfair credit card practices and promote responsible management of debt. Since then, we have published a set of Safe Credit Card Standards as

borrowers to avoid all interest if a promotional balance is paid in full by the end of the deferment period, or else pay the entire sum of accrued interest. Creditors providing deferred interest offers must count on a certain portion of debtors finding themselves unable to pay off a balance within the allotted time, or forgetting when the balance is due. Though none of the general purpose consumer cards we studied from the largest bank and credit union issuers currently include deferred interest arrangements, we are concerned about the dangers these arrangements pose on the margins.[3]

Without arguing for the prohibition of deferred interest arrangements at this time, we urge the Board to change its proposed rules to help improve price transparency and reduce the risk of large debt shocks to cardholders. Specifically, issuers should be required to send notice to cardholders at least 45 days prior to the expiration of a deferred interest period. The general exception for promotional rates should not apply. Unlike the expiration of promotional rates, which merely marks the beginning of higher interest charges on outstanding balances going forward, expiration of deferment periods results in instant and potentially significant increases in a cardholder's debt burden. This change in debt burden is more akin to a significant change in the account agreement than it is to expiration of a temporary promotional rate.

Requiring issuers to notify cardholders prior to expiration of a deferred interest period is consistent with the overall goals of the Credit CARD Act, including the establishment of "fair and transparent practices" relating to credit card plans. It would also complement Congress's intent to give cardholders a chance to repay deferred interest amounts fully before the end of the deferment period. In amended TILA Section 164, Congress required issuers to apply payments (beyond the minimum payment due) first to high-rate balances before low-rate balances, but created an exception that allows cardholders to pay off deferred interest arrangements during the last two months of the deferment period. Requiring issuers to send notice at this time would further that goal by helping cardholders make informed decisions about paying off the deferred balance.

The Board may address its concerns about unintended adverse consequences (74 FR 139 at p. 36085) by requiring notice that the deferred interest period is about to expire without requiring notice of a cardholder's right to cancel and reject the imposition of accrued interest. Cardholders would thus be required to pay off the deferred interest balance prior to the end date or accept the lump sum accrued interest charge as provided in the original deferred interest agreement.

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well as various results from our research and analysis. The Safe Credit Card Standards and related information are available at www.pewtrusts.org/creditcards.

[3] Recently, we completed a new analysis of all credit cards offered by the largest 12 bank issuer and the largest 12 credit union issuers. See footnote 1, supra.