May 18, 2015

Submitted via www.regulations.gov

Ms. Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

Re: Request for Information Regarding Credit Card Market
Docket No. CFPB-2015-0007
Document Citation 80 FR 14365

Dear Monica:

Auriemma Consulting Group (ACG)[1] appreciates the opportunity to submit responsive information to the Bureau of Consumer Financial Protection (Bureau or CFPB) on how the Credit Card Accountability Responsibility and Disclosure Act of 2009 (CARD Act or Act) and associated protections continue to affect consumers and credit card issuers. Section 502 of the CARD Act requires the Bureau to conduct biennial reviews of the consumer credit card market and to seek public comment in connection with such reviews.

This letter is submitted on behalf of a group of regional and mid-tier credit card issuers and retailers with $500 million to $30 billion in receivables. The following comments represent the interests of a diverse set of institutions, including full-service banks, mono-line and subprime issuers, retailers, and finance companies covering general purpose and private label credit cards. To inform our commentary, we held conversations with executive management and legal counsel for these firms.

This latest request for information (RFI) surpasses the statutory requirements of the CARD Act to highlight a number of additional areas of interest, such as online disclosures, rewards products, add-on products, and ability to pay. In addition to commentary on the continuing impacts of the CARD Act, we include observations in a number of these supplementary areas.

Opening Comments

The CARD Act has produced clear consumer benefits, including the reduction or elimination of fees and the curbing of repricing activity. In these regards, the Bureau has achieved its objective of increased transparency for consumers. Credit card costs are now more accurately reflected in the fees and interest rates presented to applicants upfront.

[1] Auriemma Consulting Group is a management consultancy focused on the consumer payments and lending arena that has been advising financial institutions, retailers, capital markets participants, and other interested parties since 1984. We interact regularly with credit card issuers of all sizes.

The Act's repricing restrictions, which took effect in February 2010, help accomplish this goal by severely limiting the circumstances under which interest rates may be raised over the life of a loan. These restrictions are inflexible and leave issuers few opportunities to effectively manage credit exposure and risk, which can materially change over time. Even in instances where rate increases are permitted, the Act's ongoing rate review requirement places an extreme administrative burden on issuers and makes such increases largely unworkable.

As a result, issuers have had to adjust their treatment of all accounts and applicants – particularly those with non-prime credit profiles. Changes in market characteristics, including reduced access to credit and increases in the interest rate component of pricing, reflect this. We believe these tradeoffs negate at least some of the advances in consumer welfare generated by the CARD Act.

Our comments do not call for regulators to discard repricing restrictions. Rather, they seek to highlight ways these restrictions can be adjusted to reduce adverse market impacts while maintaining or strengthening protections for consumers.

In doing so, we recognize that there is a difference between legislative directives and regulatory judgment of appropriate practices. Our comments intend to highlight instances where those legislative actions fall out of step with a sound management approach. Where possible, we seek to encourage balanced interpretations that ensure strong protections for consumers while allowing issuers to operate in a safe and sound manner. Many of our comments relate to the effectiveness of regulatory changes, the tradeoffs that necessarily come with such changes, and unintended consequences that have implications for consumer welfare and the credit card market at large.

As discussed, this letter responds to a range of issues raised in the RFI. Below is a summary of the commentary that follows:

- While issuers share in the goal of increased clarity and transparency in cardholder agreements, ongoing industry efforts to simplify contractual language are impeded by statutory and regulatory requirements and exposure to litigation risk. Certain changes required under Regulation Z, such as tabular disclosure of key terms, are inherently logical and beneficial.
- Disclosure requirements impose significant costs on issuers and – absent proof of their effectiveness – can distract from key content without producing any commensurate benefit for consumers. The extent to which the minimum payment warning has induced a change in consumer comprehension or behavior remains unclear.
- Financial institutions have become hyper-sensitive to unfair, deceptive, and abusive acts and practices (UDAAP) in the course of their day-to-day business operations, and strong protections have been put in place. The predominant issue with respect to UDAAP is the lack of clear regulatory expectations regarding conduct that is either forbidden or required. The CFPB's reliance on enforcement, rather than regulation, is a contributing factor.
- The CARD Act has contributed to a number of changes in market characteristics, including reduced availability of credit for higher-risk consumers and increases in the interest rate component of pricing for new and existing accounts. Repricing restrictions and changes in market characteristics are interconnected.
- Periodic billing statements, including enhanced consumer disclosures, are readily available and easily accessible to cardholders online. There are fundamental differences in how consumers interact with information online versus on paper, and effective print disclosures do not necessarily work well in electronic form.
- The market for rewards products is functioning well overall, evidenced by robust demand, heavy utilization, and low incidence of cardholder dissatisfaction. We are not aware of evidence indicating that consumer awareness or understanding of rewards terms is declining.
- Uncertain regulatory expectations have driven many issuers to withdraw from the market for add-on products, including services such as debt protection and credit score monitoring that provided inherent value to cardholders.

- While issuers are complying with ability to pay requirements, such requirements assume that income and risk are closely related. Efforts by several issuers to substantiate this relationship have either failed to produce a correlation or revealed an inverse relationship between income and likelihood of default.

(a) The Terms of Credit Card Agreements and the Practices of Credit Card Issuers

In opening our commentary, we first seek to convey support for the spirit of the CARD Act and its expressed goal of fostering a more transparent credit card market. Improved cardholder agreements are a major component of this objective, and one the industry champions. In fact, the CFPB's 2013 CARD Act Report found that "many issuers streamlined the presentation and content of their cardholder agreements between 2008 and 2012," citing consolidation of terms and conditions into fewer documents and reductions in the length of agreements. The report also noted improved readability and accessibility. Issuers have undertaken these changes despite the Act not specifically regulating contract length and form.

One change that was required under Regulation Z, the inclusion of a "Schumer Box" in account opening agreements, is endorsed by issuers as a beneficial tool that works well in practice.

Consumers have come to rely on the Schumer Box for important information, particularly when choosing a credit card, and the industry has grown comfortable complying with this requirement.

Broad support for requirements such as the Schumer Box is not surprising. For the purposes of consumer protection, the industry favors reliance on meaningful disclosures over substantive changes to or restrictions on specific credit card practices. The objective should be to encourage maximum consumer understanding, rather than to homogenize credit card products or set the content of agreements in an attempt to simplify them.

While improvements in length and complexity are apparent when comparing pre- and post-CARD Act agreements, and while industry efforts to simplify agreements are ongoing, opportunities for enhancement remain:

- Agreements remain protracted despite incremental reductions in length.
- Marginal improvements in readability are offset by residual use of "legalese" that is compulsory and unavoidable.
- Consumers may use the Schumer Box as their primary source of information, while overlooking the remainder of contracts.
- The likelihood of consumers carefully reviewing and understanding entire card agreements is still low.

Industry efforts to simplify contractual language are impeded by statutory and regulatory requirements, as well as exposure to litigation risk.

It is important to note that the above observations are not the result of lack of effort or incentive on behalf of the industry. In fact, issuers share in the goal of clearer, more concise agreements for their customers, have a vested interest in improving comprehension, and, as stated, continue to make progress. Rather, they reflect limitations on issuers' ability to eradicate legally-required contractual language without significantly increasing their exposure to legal and financial liability and hindering contract enforceability.

Such language is the culmination of decades of industry legislation and regulation. Federal and state statutes, regulatory disclosures, arbitration agreements, and provisions about billing errors, changes in terms, and telephone communication are just a few examples of components issuers are required to include – either directly by law or indirectly as a means to mitigate litigation risk in the form of class action and individual lawsuits. As a result, there is a sense that certain confines have been reached relative to the readability and accessibility of agreements.

The improvements highlighted by the CFPB have not necessarily increased the likelihood of consumers carefully reviewing and understanding entire credit card agreements. Even for consumers that diligently review agreements, many still opt to speak with an agent or access information made available online to resolve questions.

This raises a larger issue of a growing gap between two necessary components of agreements: (1) contractual terms, as detailed above; and (2) non-contractual content, such as educational and explanatory information designed to increase practical understanding of how credit cards work. Grace periods, due dates, late fees, and minimum-due payments are examples of credit card features that require such practical explanation.

Reconciling these disparate yet necessary elements is key. The two-page prototype credit card agreement the CFPB released in 2011 attempted to accomplish this goal. However, in doing so, the prototype illustrates the challenges of attempting to marry contractual terms and non-contractual content in a short-form agreement. The outcome is a document that omits certain provisions, including some required by law, lacks legal protections for issuers, and spreads content across different media to achieve a shorter printed form. For these reasons, adoption of the prototype agreement is unfeasible despite industry support for a short-form agreement in spirit.

Privacy notices stand out as an area in which regulators have achieved meaningful change. In 2009, the Federal Trade Commission (FTC) and seven other federal agencies published amendments to the rules implementing certain privacy provisions of the Gramm-Leach-Bliley Act (GLBA) and adopted a model privacy form.[2] The amendments significantly cut down on the length and complexity of privacy notices, which previously were criticized by consumer advocates as being too complicated. The agencies conducted qualitative consumer research and quantitative data collection to prompt changes. While voluntary, use of the model form established safe harbor from liability – protection the CFPB's prototype falls short of providing. To the extent that changes to privacy notices under the GLBA are applicable to agreements, elements of the FTC's approach may be relevant.

We recommend that the CFPB engage with the industry to develop generic educational content explaining how credit cards work. Such a system, made available to borrowers online, could use examples and other contextual information to further illustrate key features (e.g., grace periods) and prices (e.g., late fees). Rather than covering every potential scenario, such content could highlight select situations based on the most common sources of cardholder confusion.

(b) The Effectiveness of Disclosure of Terms, Fees, and Other Expenses of Credit Card Plans

Title II of the CARD Act introduced enhanced consumer disclosure requirements for periodic billing statements, including a minimum payment warning showing the amount that will be paid and the repayment period length if the consumer makes only the minimum payment.

ACG understands and supports the intent behind the minimum payment warning, i.e., to induce faster pay-down of debt, and, as stated above, supports meaningful information disclosure for the purposes of consumer financial protection. That said, any disclosure requirements should be based on evidence demonstrating a positive impact on consumer understanding or behavior.

Disclosure requirements impose significant costs on issuers and – absent proof of their effectiveness – can distract from key content without producing any commensurate benefit for consumers.

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[2] *See* https://www.ftc.gov/sites/default/files/documents/rules/privacy-consumer-financial-information-financial-privacy-rule/model_form_rule_a_small_entity_compliance_guide.pdf

The extent to which minimum payment warnings on periodic billing statements have induced a change in comprehension or behavior remains unclear. Testing has concluded that consumers understand the negative consequences of paying only the minimum payment,[3] and empirical evidence on the effectiveness of the new disclosures is limited. The CARD Act did not mandate effectiveness testing prior to implementation, and the CFPB's 2013 CARD Act Report designates this as an area for future research.

To the extent that findings are relevant and applicable to the US, and in the absence of data for this market, research and testing from outside the US may be helpful to explore. Mexico is one such market in which rigorous testing has been carried out. With support from financial regulators, which were considering mandating personalized warnings similar to those required under the CARD Act, researchers partnered with a large bank to test several disclosures including minimum payment warnings.[4]

Contrary to expectations, such warnings were shown to have insignificant effects and actually caused delinquency to increase for cardholders that often paid interest or had high levels of debt.[5] Additionally, the amount of payments declined by about 10 percent.[6] Researchers posit that the delinquency induced may be strategic in nature; drawing attention to the length of the repayment period might make pay-down seem unfeasible, discouraging cardholders and leading them to pay less or stop paying altogether.[7]

Anecdotal evidence from our conversations with issuers suggests the effects of the minimum payment warning are insignificant. At least one issuer compared payment behavior on accounts before and after the CARD Act disclosure changes. While the issuer observed a temporary reduction in the percentage of customers making only the minimum payment, perhaps because the change spurred more people to pay attention to the disclosure, payment behavior returned to normal shortly following the initial implementation.

The intent of new disclosure requirements – to raise customer awareness and comprehension – is immaterial or even harmful if the net effect is distraction from key content or degradation in payment behavior, as the above research suggests is possible. Additional disclosures and greater detail in billing statements can overwhelm customers and result in them reading and retaining less information. As a result, we believe regulators should be selective in proposing new disclosure requirements and determining whether to retain existing requirements.

The Bureau should assess whether the repayment disclosure requirement is necessary to retain based on effectiveness testing that either proves or disproves the consumer benefit of such disclosures.

<u>Late Fee Disclosure</u>

In response to the CFPB's question on the effectiveness of current rate and fee disclosures, it is worth noting that, in some instances, abbreviated explanations such as those in the Schumer Box may lead to customer confusion. Due to limited space, late fee amounts are often characterized as "up to $35." This is not an accurate reflection of the penalty fee for a first violation, which, in accordance with the safe harbor of the implementing rule, is $25. Rather, it reflects the highest amount the late fee can be.

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[3] *See* Design and Testing of Effective Truth in Lending Disclosures, Calverton, Md., Macro International Inc., May 16, 2007. *Available at* http://federalreserve.gov/newsevents/press/bcreg/bcreg20081218a7.pdf.
[4] To examine the impact of such disclosures, researchers randomly sent 12,900 messages containing a personalized repayment period and language explicitly advising cardholders to pay more than the minimum-due amount. *See* Seira, Enrique and Elizondo, Alan, Are Information Disclosure Mandates Effective? Evidence from the Credit Card Market (January 1, 2014). *Available at* http://ssrn.com/abstract=2431910.
[5] *Ibid.* The effect was an increase in delinquency equivalent to 8.6 percent of its mean value.
[6] *Ibid.*
[7] *Ibid.*

(c) The Adequacy of Protections Against Unfair or Deceptive Acts or Practices or Unlawful Discrimination Relating to Credit Card Plans

Financial institutions have become hyper-sensitive to UDAAP and the potential for disparate treatment in the course of their day-to-day business operations. UDAAP is a consideration in virtually all decisions issuers make today, and fair customer treatment is engrained in the culture of many organizations.

Strong consumer protections have been put in place in the form of more proactive compliance and risk management systems, rigorous compliance testing and internal audit schemes, comprehensive training procedures, and robust complaint management programs. These protections are intended to prevent, detect, and correct instances of unfair customer treatment. Additionally, issuers have created dedicated compliance roles to assist with risk management and amended policies and procedures to incorporate UDAAP principles.

Complaint management, in particular, has seen major changes. In line with the framework set out by the CFPB's complaint portal, issuers have drastically lowered the bar on what constitutes a complaint. Institutional definitions have been broadened to account for any expression of dissatisfaction voiced by customers either verbally or in writing. This has required major operational changes to intake and monitoring procedures. Issuers have also invested heavily in complaint reporting, analysis, and resolution. Many have established direct executive reporting for greater management insight into sources of cardholder dissatisfaction.

Financial institutions share in the goal of developing strong protections against UDAAP. The vast majority of issuers are focused on building and maintaining healthy, long-term business relationships and extending credit to eligible borrowers – objectives that are fundamentally out of step with unfair, deceptive, or abusive practices and disparate treatment.

The predominant issue with respect to UDAAP is the major lack of clarity regarding regulatory expectations and conduct that is either forbidden or required.

This lack of clarity is driven by (1) the CFPB's decision to define UDAAP through enforcement, rather than regulation; (2) the level of subjectivity inherent to this approach; and (3) continued uncertainty surrounding the newly-created category of "abusive" practices.

First, the CFPB has indicated that it does not anticipate "writing a rule around UDAAP."[8] In fact, the Bureau has taken the stance that an act may constitute UDAAP absent any technical violation of consumer financial protection law.

"Unfair" and "deceptive," which predate the CFPB by decades, are concepts that have been well-defined over the years. In the 1980s, the FTC released policy statements on unfairness and deception that contained clear language on what falls into these categories. The agency stated the purpose of unfairness and deception and outlined how it would enforce them, and its definition of "unfairness" was subsequently codified into law.

The CFPB's reliance on enforcement to define UDAAP is problematic for a number of reasons. Enforcement actions, consent orders, and informal guidance are not legally binding against external parties, and recent consent orders contain less detail on findings and conclusions in connection with UDAAP violations.[9] While regulated parties are closely observing the CFPB's actions to align practices, comply with guidance, and limit UDAAP risk, regulatory expectations remain largely uncertain. As a result, actions taken by issuers are necessarily reactive rather than proactive in nature.

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[8] *See* http://www.americanbanker.com/issues/177_58/cordray-cfpb-supervision-enforcement-consumers-UDAAP-UDAP-1047798-1.html
[9] *See* http://media.mofo.com/docs/PDF/150120-cfpb-udaap.pdf

Second, there is not only a major lack of clarity regarding conduct that is forbidden or required, but also a high level of subjectivity. Judgment of appropriate practices by nature involves a degree of personal bias. One party may deem a practice to be unfair and deceptive, while another may view the same practice as within the bounds of fair treatment. This is true down to the examination level and may lead to inconsistent outcomes among different exam teams.

This level of subjectivity is fundamentally out of sync with the CFPB's expressed goal of creating a more level playing field in the market. In contrast, bright-line standards provide clear boundaries that ultimately promote a level playing field. Clarity on rules of engagement (i.e., what is/is not permissible) would make regulated parties more confident in their decision-making and allow them to more proactively comply with regulatory expectations.

Third, while the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) defined "abusive," it did so in a manner that makes its application uncertain and inherently subjective.

Without clear guidance, issuers are unable to confidently keep practices within the boundaries of regulatory expectations. In some areas this uncertainty has made the landscape too murky for issuers to operate, resulting in reduced choice for consumers. Rather than discouraging UDAAP, the CFPB's approach has caused issuers to eliminate certain products to limit exposure to regulatory risk – without necessarily producing any benefit for consumers. Later in this letter, we discuss the elimination of add-on products that were inherently valuable to cardholders.

(d) Whether implementation of the CARD Act has affected (i) the cost and availability of credit, particularly with respect to non-prime borrowers; (ii) the use of risk-based pricing; or (iii) credit card product innovation

Cost and Availability of Credit

Implementation of the CARD Act has contributed to a number of changes in market characteristics, including (1) reduced availability of credit, particularly for higher-risk consumers; and (2) increases in the interest rate component of pricing, particularly for lower-risk consumers.

Availability of credit, as measured by initial credit limits, the frequency of credit limit increases, and increase amounts, has been significantly reduced, particularly for non-prime borrowers.[10]

A vintage analysis of credit card accounts opened before and after the recession and February 2010 effective date for CARD Act repricing restrictions demonstrates this.[11] The results show that "significantly less credit was extended to approved credit card applicants in 2011, with lower initial credit limits, fewer limit increases, and smaller increase amounts in dollar terms."[12] Credit was most restricted to the riskiest quartile of accounts opened after the CARD Act: for these borrowers, "the median initial credit limit fell 66.7 percent to $500, and the median limit increase amount fell by at least 25 percent at each observation point."[13]

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[10] *See* Santucci, Larry, A Tale of Two Vintages: Credit Limit Management Before and After the CARD Act and Great Recession (February 2015). FRB of Philadelphia - Payment Cards Center Discussion Paper No. 15-01. *Available at* http://ssrn.com/abstract=2566746.
[11] *Ibid.* The analysis, which uses tradeline-level data for 1 million revolving credit card accounts, examines accounts opened in 2005 and 2011 for more than two years (30 months) following acquisition to understand changes in initial limits and credit limit increases over time.
[12] *Ibid.*
[13] *Ibid.*

Average credit lines shrank in the fourth quarter of 2014, with the most significant reduction occurring in non-prime tiers.[14]

Additionally, annual bankcard balances demonstrate that subprime growth is muted despite significant growth in all other consumer credit categories.[15] Overall, average balances per account remain well below pre-recession levels despite significant growth in total balances.[16]

Consumer credit statistics corroborate these findings. According to the Federal Reserve Board of Governors' (Federal Reserve) G.19 release, total consumer revolving credit has remained suppressed since implementation of the CARD Act and continues to be far outpaced by growth in nonrevolving debt.[17]

The CFPB may view some degree of reduced access to credit as desirable, particularly in the case of younger borrowers or those who may be unable to manage debt. However, to the extent that credit is restricted to consumers with a short-term borrowing need or those who wish to establish or repair their credit, less availability can have significant adverse impacts on consumer welfare. In order to satisfy their need for credit, consumers may open additional cards or use higher-cost alternative products offered by unregulated providers.

The interest rate component of pricing, an important element for cardholders who often carry a balance, is higher than it would be absent certain provisions of the CARD Act.

The CARD Act's impact on interest rates has attracted a great deal of industry attention, including within comments received by the CFPB in response to its prior public inquiry. That review found that interest rates increased in 2009 and early 2010, with the account-weighted average retail APR rising by 230 basis points to 18.5 percent.[18] Increases were most pronounced among prime and superprime accounts.[19]

The report acknowledged that "by affecting other components of pricing, the Act likely indirectly impacted the interest rate component of pricing," and linked rising interest rates to a number of factors including the migration of accounts from one risk tier to another and rising loan losses and charge-offs. While changes to pricing in preparation for regulatory changes were mentioned, the report made clear that the CFPB makes "no judgment on the extent to which the CARD Act, as distinguished from other factors such as the impact of the Great Recession, contributed to these increases."

While the recessionary cycle impacted prices and credit availability, it is worth noting that economic conditions and credit card portfolio performance have changed dramatically since passage of the CARD Act in 2009 and publication of the CFPB's prior report two years ago. The number of unemployed individuals has fallen by more than 44 percent since the height of the economic crisis in 2009, when the CARD Act was passed.[20] Additionally, since the CFPB's prior study in 2013, the rate of unemployment has declined to its lowest level in nearly seven years.[21] During the same period, loan losses and charge-off rates have reached near-record lows.[22] As a result, many of the contributing factors linked to rising rates in the prior review – unemployment and related loan losses and charge-offs – should be exerting far less influence today. For example, if the increase in loan losses in 2009 and 2010 did in fact lead to

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[14] Average credit lines for new and existing accounts declined 3.9 percent and 2 percent, respectively, year-over-year. TransUnion Credit Database.
[15] *Ibid.*
[16] *Ibid.*
[17] During the first quarter of 2015, revolving credit decreased at an annual rate of 0.25 percent, while nonrevolving credit increased at a corresponding rate of 7.5 percent. *See* Federal Reserve Board of Governors G.19 Consumer Credit Statistical Release (March 2015). *Available at* http://www.federalreserve.gov/releases/g19/current/.
[18] CARD Act Report (October 1, 2013) Section 2.2.6 Retail APR and Effective Interest Rates (p. 29)
[19] *Ibid.*
[20] *See* St. Louis Federal Reserve Bank, Monthly Unemployment Series. *Available at* http://research.stlouisfed.org/fred2/graph/?s[1][id]=UNEMPLOY
[21] *See* http://data.bls.gov/timeseries/LNS14000000
[22] ACG Credit Card Collections Quarterly Benchmark Study

increases in pricing, as the CFPB suggests, then those increases should have subsided or reversed along with loss rates. This does not appear to be the case.

Interest rates have remained elevated since the period immediately prior to implementation of the CARD Act.[23]

We understand that determining cause-and-effect relationships is difficult due to the confluence of events that coincided with implementation of regulatory changes. However, given the above observations, there should be a greater burden on the Bureau to investigate the extent to which CARD Act provisions, separate from other factors, have contributed to changes in market characteristics. We suggest that the CFPB designate such changes as an area for further research.

CARD Act repricing restrictions and the aforementioned changes in market characteristics are interconnected.[24]

We suspect that many submissions will highlight the relationship between these restrictions and the cost and availability of credit.

Prior to the February 2010 effective date for CARD Act repricing restrictions, issuers controlled for risk by adjusting pricing based on observations of borrower behavior over the life of a loan. Today, this strategy is far less viable. Restrictions on repricing are inflexible and leave few opportunities for rates to be increased, such as a borrower becoming at least 60 days past due (below, we discuss how the 60-day delinquency trigger is excessive and penalizes the wrong people). When there are early indicators that an account is shifting risk profiles, issuers are unduly constrained in terms of how they treat pricing and manage risk for that account.

As a result, issuers must use other methods to limit their exposure to risk and manage expected losses, including reducing available credit to riskier borrowers upfront. As discussed above, the median credit line at acquisition declined by two-thirds for this market segment in the wake of regulatory changes and more than 60 percent for all accounts.[25]

CARD Act restrictions have also necessitated changes to pricing strategies, particularly at origination, as a means to offset risk. All consumers, regardless of creditworthiness, are compensating for the inability to reprice risk. In fact, as stated earlier, interest rate increases have been more severe for prime and superprime accounts. Additionally, as predicted, prohibitions on back-end pricing have given way to greater use of upfront risk-based pricing, a possibility the CFPB's prior report acknowledges.

More broadly, limitations on the repricing of accounts have introduced systemic risk into credit card portfolios and raised safety and soundness concerns for revolving credit. Rigidity of existing balances is particularly problematic in the event of an adverse situation, such as increasing loan losses, financial crisis, and other events that cause credit risk to fluctuate. Upon the incidence of deteriorating economic conditions over the life of a loan, for instance, issuers are likely to experience different credit performance than they may have predicted at account opening. CARD Act restrictions handicap issuers in their ability to respond to and mitigate the impacts of such fluctuations, requiring higher pricing at origination.

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[23] CFPB Credit Card Database (CCDB)
[24] The CARD Act limits the circumstances under which credit card issuers can increase interest rates on existing balances and the circumstances under which issuers can change the interest rate applicable to future transactions. For interest rate increases applicable to existing balances, the card issuer generally cannot increase the rate unless the consumer has missed two consecutive monthly payments (i.e., 60 days past due) and the consumer has been provided 45 days written notice.
[25] Santucci, *Op cit.*

In some ways, repricing restrictions make credit cards characteristically similar to fixed-rate mortgage products with embedded risk. In a fixed-rate environment, issuers must charge a sufficiently high interest rate upfront to offset the losses that are ultimately incurred. They also must restrict credit to people who are more vulnerable and tend to have a greater need for credit. Conversely, we believe providing more flexibility creates greater credit availability and reduces systemic risk.

Of particular concern is the requirement that an account be 60 days delinquent before interest rate increases are applied to existing balances. It is important to convey observations about credit risk at this stage of delinquency.

The likelihood of default increases nearly fourfold from 30 to 60 days past due, when rate increases on existing balances are permitted.[26]

Between cycles one and two, the percentage of accounts that “flow” unobstructed to charge-off nearly quadruples, from 9.3 percent to 35.6 percent.[27] These figures are likely conservative, considering that charge-off flow rates in the current environment are well below historical norms and those experienced in the 2009-2010 timeframe.

Additionally, in order to satisfy the 45-day notice requirement, accounts may not be repriced until 105 days past due. At this point, more than 80% of accounts will roll deeper into delinquency.[28]

Due to the narrow exceptions under which interest rate increases may be applied to existing balances, such increases are ultimately executed on a population of accounts that is significantly less likely to pay. This means that, in effect, rates are only raised on the small share of accounts that do in fact make payments. As a result, those cardholders who make an attempt to meet their financial obligations are the ones being penalized. This is a phenomenon at any level of delinquency, but at 60 days past due the adverse impact is much more pronounced than it would be at 30 days past due, as evidenced by the much lower likelihood of default at that point.

Recommendations

The industry is not advocating for the ability to reprice existing balances at any time or for any reason. Issuers generally agree that repricing as a practice was more widespread than it should have been prior to the CARD Act, particularly in the case of sudden or unexpected rate hikes. However, we believe there are more reasonable provisions that could be put in place while preserving, and in some cases strengthening, consumer welfare. ACG recommends that the CFPB do the following:

- Select a shorter period, such as 30 days past due, after which issuers are permitted to raise interest rates on existing balances.
- Expand disclosure requirements, if necessary, increasing the notice period prior to rate increases being applied.

These recommendations draw inspiration from amendments to Regulation AA (Unfair or Deceptive Acts or Practices) adopted by the Federal Reserve in 2008, including a prohibition on “increasing the rate on a pre-existing credit card balance.”[29] While similar in spirit to the rules implemented under the CARD Act,

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[26] ACG Credit Card Collections Quarterly Benchmark Study - Quarter 4, 2014. *Newly delinquent to chargeoff flow rate definition*: Average monthly contractual charge-off balances for the benchmark quarter divided by cycle 1 delinquent balances lagged two quarters. *Cycle 2 to chargeoff flow rate definition*: Average monthly contractual charge-off balances for the benchmark quarter divided by cycle 2 delinquent balances lagged two quarters.
[27] *Ibid*.
[28] *Ibid.*
[29] *See* http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20081218a1.pdf

which superseded them, the Federal Reserve's final rules permitted interest rate increases on existing balances one cycle sooner, at 30 days past due.

In a 2008 comment letter responding to the Federal Reserve's proposed rules amending Regulation AA, Comptroller John C. Dugan called the 30-day late payment trigger "excessive" and urged regulators to consider an even shorter period.[30] Additionally, Comptroller Dugan noted that the "risk of loss is highly correlated with the extent of the delay in receiving a customer's payment after the due date…"[31]

Given the far greater risk of default at 60 days past due outlined above, and in accordance with the Federal Reserve's 2008 guidelines, we believe 30 days is a more reasonable timeframe.

As a point of compromise, any decision by the CFPB to reduce the 60-day delinquency requirement could be accompanied by a corresponding increase in the 45-day notice period given to customers prior to rate increases taking effect. Consumers should be given ample time to opt out of an impending rate increase by closing the account and paying off the outstanding balance.

Credit Card Product Innovation

Reduced access to credit and muted balance growth among non-prime borrowers are symptomatic of larger changes in the market, including a general shift in focus toward higher credit quality cardholders. As discussed earlier, regulatory changes appear to be restricting industry efforts to serve a broader market.

Product innovation is increasingly directed toward prime and superprime borrowers.

In addition to overall access to credit, this trend is visible in the behavior of existing cardholders. Specifically, there has been a shift away from revolvers in the consumer market and a corresponding rise in transactors – cardholders who use credit cards for the purposes of spending rather than borrowing. We believe this trend is directly related to regulatory changes that have restricted issuers' ability to manage risk.

Interest Rate Reviews

Even in instances where rate increases are permitted, the Act's ongoing rate review requirement places an extreme administrative burden on issuers and makes such increases far less viable.

In the rare case that the interest rate is increased on an account, the CARD Act requires issuers to review that account at least once every six months to determine whether the factors prompting the increase have changed. This requirement applies to interest rate increases that occurred any time after January 1, 2009.

As there is virtually no statute of limitations for rate reviews, today issuers are reviewing accounts that had their interest rates increased more than six years ago. These accounts have failed to qualify for a rate reduction after 12 reviews. This process requires substantial analytics, creates an extreme administrative burden, and has the effect of discouraging rate reviews even under permissible circumstances.

[30] *See* http://blogs.creditcards.com/OCCLettertoFed.pdf
[31] *Ibid.*

We recommend replacing the fixed date established by the CARD Act (i.e., January 1, 2009) with a rolling look-back period for reevaluating rate increases. This period should be a maximum of two years, or four rate reviews.

(e) Online Disclosures

Some disclosures, including those required under Title II of the CARD Act, are delivered through periodic billing statements. The CFPB's prior report raises concern over the provision of such disclosures online, where consumers may choose not to access their monthly statement and opt instead to make payments via online account portals. The minimum payment warning and other disclosures are not currently required in these portals.

Periodic billing statements – Including enhanced consumer disclosures – are at cardholder disposal online.

It is important to note that issuers do make these documents readily available and easily accessible electronically. Cardholders know how to locate and access their billing statements and cardholder agreements as needed online. Issuers have taken steps in recent years to make online banking sites, where these document are located, more user-friendly and easier to navigate. These improvements are part of larger efforts to expand online and mobile functionality to meet customer preferences. Additionally, there is no effective method to induce a customer to review a billing statement, either online or in print.

The online channel represents just one delivery channel for information. In fact, issuers make information available through a range of options including online and mobile. For the purposes of support, cardholders have access to numerous contact methods including traditional telephone contact, interactive voice response (IVR), and live-agent chat. Many cardholders, regardless of their preferred delivery method for billing statements (i.e., print or online), still choose to resolve questions by speaking with an agent via telephone.

While the CFPB's plans relative to online disclosures are unknown, there is concern that future requirements will seek to retrofit certain disclosures to digital channels. For example, the questions in this RFI suggest that the Bureau may consider requiring customers to view the minimum payment warning in online account portals. This approach is unlikely to be successful. Online account portals are designed for convenience and serve a specific purpose, and we believe it is unnecessary to duplicate disclosures that are already accessible elsewhere online.

Additionally, as discussed earlier, the extent to which repayment disclosures have induced a change in consumer comprehension or behavior is uncertain. Empirical evidence on the effectiveness of these disclosures is limited and the CARD Act did not mandate effectiveness testing prior to implementation. The Bureau should assess the effectiveness of such disclosures, including whether they are necessary to retain in print, before issuing any requirement that expands their prevalence online. Alternative methods, such as linking to preexisting disclosures, may be beneficial in the interim.

As the Bureau's prior report suggests, there are larger questions when translating disclosures to digital channels. In proposing any requirements, the Bureau should consider (1) the purpose of digital channels in the minds of consumers and how web users interact with information; (2) alternative methods for presenting information online; and (3) whether certain requirements in print disclosures are necessary online.

Digital channels should not seek to replicate print disclosures.

There are fundamental differences in how consumers interact with information online versus on paper, and effective print disclosures do not necessarily work well online. Web users tend to scan content rather than read it in full, and the general expectation is that online channels will provide abbreviated information. Mobile, in particular, has a distinctly different purpose in the mind of the consumer and is meant to be a more concise and limited access point compared to full-feature desktop sites. Additionally, there are variations in how issuers deliver information online. As such, a one-size-fits-all approach to online disclosures is unlikely to be successful.

The objective should be to present information in a clear and understandable form without interfering with comprehension. As with print disclosures, excess information can be overwhelming and distract consumers from important content.

To illustrate this point, the Bureau need look no further than the digital disclosures that routinely confront consumers. These disclosures come in the form of software license agreements, website terms of service, and countless other user agreements. Consumers ignore such disclosures en masse, opting instead to scroll or click through text or "agree" to terms to complete the task at hand. What this routine behavior demonstrates is that the likelihood of consumers carefully reviewing excessive information online is extremely low. The same is true for online disclosures in the realm of credit cards.

Online disclosures should seek to draw attention to the most critical information for consumers to process, such as payment due date, minimum-due payment, and late payment information. Enabling consumers to link to more detailed information and educational resources is viewed as beneficial.

We encourage the Bureau to conduct consumer testing and research to determine the key information consumers need online.

(f) Rewards Products

Rewards products are resonating with consumers more than ever, comprising more than half of new accounts opened since 2012.[32] Spending on rewards cards has nearly doubled in recent years, while non-rewards spending has declined by nearly a third.[33] It is clear that rewards play a major role when consumers are comparing and shopping for a credit card. Cash-back, points, and airline miles have displaced factors that commanded applicants' purchasing decisions in the past, such as fees, interest rates, and promotional offers. This trend is not exclusive to credit cards; compelling rewards are an expectation in many industries including travel, retail, and hospitality.

Issuers are serving this record consumer demand by offering attractive and competitive rewards programs that deliver value to a wide range of cardholders. In fact, dramatic growth in rewards spans all consumer credit categories and is not limited to higher credit quality applicants.[34]

We are not aware of evidence indicating that consumer awareness or understanding of rewards terms is declining.

In fact, overall credit card customer satisfaction, in which rewards play a key role, is at a record high, and the percentage of customers who say they "completely" understand how to earn rewards increased in 2014 to 63 percent.[35] Additionally, increases in utilization strongly suggest that cardholders are satisfied with the value they are deriving from rewards products.

Issuers share in the goal of improving customer understanding of rewards terms. There is widespread recognition that engagement with rewards has major benefits in terms of loyalty, retention, and wallet share. Recent strategies for enhancing awareness and comprehension include sending email service alerts recapping program terms, explaining redemption options in plain English, and prompting customers

[32] *See* http://www.aba.com/Press/Documents/092914ABACreditCardMonitorSpecialStudy.pdf
[33] *Ibid.*
[34] *Ibid.*
[35] *See* http://www.jdpower.com/de/node/5916

to redeem earned rewards. Issuers have also taken steps to simplify programs, with offerings that allow customers to earn rewards for all purchases, regardless of spend category, and points that do not expire.

Additionally, through consumer research and other methods, issuers are constantly seeking out ways to make rewards more meaningful and relevant to new and existing cardholders. For example, analyzing customer spend segmentation to align rewards and benefits with cardholders' most frequent purchases is a common practice.

To further demonstrate that rewards programs are functioning well, it is helpful to analyze consumer complaint data – including data contained in the CFPB's own complaint portal.

CFPB complaint data shows that rewards-related complaints make up a miniscule share of credit card grievances.

Rewards comprised roughly 2.4% of the more than 25,000 credit card complaints received by the CFPB through 2013.[36] In 2014, the CFPB's annual complaints report does not mention rewards at all in the context of credit cards. In fact, rewards are not included in the top-10 complaint types representing 74% of complaints.[37] Additionally, rewards are not a primary source of the most common agent-handled call types with Customer Service.[38] Anecdotal evidence corroborates these observations. Every issuer we spoke with indicated that rewards rank extremely low in terms of cardholder complaints.

We agree that deceptive or misleading practices, such as marketing the dollar-value equivalent of points-based schemes, misrepresenting bonuses in promotional materials, or overpromising on benefits, are problematic, and that the CFPB should supervise for and correct the incidence of such practices. If these practices are prevalent, however, or if issuers are failing to make rewards disclosures in a clear and transparent manner, we would expect this to be reflected in consumer complaints related to rewards. As discussed, this does not appear to be the case.

Based on the above observations, the CFPB's objectives relative to rewards are unclear. We believe the market is functioning well overall, evidenced by robust demand, heavy utilization, and very low incidence of cardholder dissatisfaction and complaints. As a result, we do not believe significant action pertaining to rewards products is necessary at the industry level.

(h) Add-On Products

Uncertain regulatory expectations have driven many issuers to withdraw from the market for add-on products, including services such as debt protection and credit score monitoring that provided inherent value to cardholders. The majority of issuers we spoke with have ceased offering these products in recent years.

The end result is reduced choice for consumers and the elimination of optional products that serve a clear purpose, particularly for vulnerable borrowers.

Debt protection, for instance, filled a gap in coverage for less affluent consumers, providing indemnity against unexpected events such as job loss and disability at a low borrower cost. In the event of such hardships, debt protection policies cancel or suspend protected balances. Large segments of cardholders, including young people and low-wage, hourly workers, do not have access to more comprehensive insurance coverage that may protect against such events. For many customers, adding

[36] *See* http://inpirg.org/sites/student/files/reports/INP%20CFPB%20Credit%20Cards%20Web.pdf
[37] Consumer Response Annual Report (January 1 - December 31, 2014). *See* http://files.consumerfinance.gov/f/201503_cfpb_consumer-response-annual-report-2014.pdf
[38] ACG Credit Card Customer Service Quarterly Benchmark Study

debt protection to a credit line was an affordable alternative that offered protection for that loan without requiring the purchase of additional, more expensive insurance plans.

Consumer survey data indicates high levels of satisfaction among cardholders enrolled in debt protection. In 2012, 77 percent of those who purchased debt protection on credit cards expressed a favorable attitude toward the product.[39] Additionally, the penetration rate of enrolled cardholders declined between 2001 and 2012, from 20 percent to 14 percent.[40] This seems inconsistent with the CFPB's claim that products such as debt protection were marketed in an aggressive manner during that timeframe.

Credit score monitoring, a service designed to detect suspicious activity and mitigate the impact of fraud, is another product that has been largely eliminated despite clear consumer demand and value. Many issuers view optional credit monitoring as a natural extension of the banking relationship, and demand for the service remains high. Issuers continue to receive inquiries from cardholders interested in enrolling in credit score monitoring despite no longer offering such services. In fact, credit reporting agencies and other providers continue to offer these features.

We understand that the CFPB's concern over add-on products lies primarily with marketing practices, including whether products are sold in an unfair, abusive, or deceptive manner, rather than the value associated with such products. We also recognize that certain marketing practices, such as free-trial periods designed to mislead customers or have them forget they are paying for a product, are deceptive. We believe there should be limitations on such trial periods and ongoing efforts, such as statement reminders, to make customers aware they have been enrolled in and are required to pay for such programs.

However, rather than discouraging deceptive marketing practices, the CFPB's actions have caused the outright elimination of many add-on products. This reflects a larger issue raised earlier in this commentary. Without clear guidance, issuers are unable to confidently keep practices within the boundaries of regulatory expectations. In the context of add-on products, the result has been reduced choice for consumers and the elimination of products that were inherently valuable to cardholders.

(k) Debt Collection

In February 2014, ACG submitted comments to the CFPB in response to the Bureau's advance notice of proposed rulemaking (ANPR) for debt collection.[41] Our commentary focused on two specific components of the request: debt collection communications and UDAAP.

First, we emphasized that modernization of the Fair Debt Collection Practices Act (FDCPA) is necessary to improve debt collection contact and alleviate risk of non-compliance with key provisions of the law, including (1) prohibitions on communicating with a debtor at an inconvenient time or place; (2) communications with third parties; and (3) harassment or abuse in connection with the collection of a debt.

In the context of UDAAP, our response highlighted the need for greater definition and clearer standards to facilitate compliance. The response covered questions on sections 806, 807, and 808 of the FDCPA, including proposed bright-line prohibitions on repeated communications, the use of predictive dialers, and mobile phone consent requirements.

[39] *See* http://www.federalreserve.gov/pubs/bulletin/2012/pdf/consumer_debt_products_20121227.pdf
[40] *Ibid.*
[41] *See* http://www.acg.net/wp-content/uploads/2014/03/Ltr_ANPR-Response-Letter_MJackson_02_28_14_LB.pdf

(I) Ability To Pay

The CARD Act requires issuers to assess an applicant or cardholder's ability to make the required minimum payments before opening or increasing a credit line. Rules implementing the CARD Act require issuers to consider repayment ability based on the consumer's income or assets and current debt obligations. As a result, issuers have established policies and procedures that consider a consumer's ratio of debt to income or assets, commonly referred to as the "DTI ratio."

Determining whether applicants have sufficient income or assets to cover an extension of new credit is a fairly unambiguous process, as it has become standard practice for issuers to collect this information from applicants upfront at account opening.

Determining whether a cardholder has sufficient income or assets to qualify for a credit line increase, on the other hand, is problematic for a number of reasons, including (1) inconsistent inter-agency guidance regarding the types of income data issuers may consider; and (2) lack of guidance on how long customer-provided income data remains valid.

First, the extent to which modeled income may be used in considering eligibility for a line increase varies by regulator. It is our understanding that the Federal Deposit Insurance Corporation (FDIC) and Federal Reserve permit reliance on "statistically sound" income estimator models, while the Office of the Comptroller of the Currency (OCC) prohibits issuers from using such models as the primary source of income information when evaluating for a limit increase (i.e., in the absence of accompanying customer-stated data). As a result, regulated entities may be unable to offer proactive credit line increases without recent, customer-stated income information. Income estimators may be used under a limited set of circumstances, including for segmentation purposes or as a proxy for preliminary screening at acquisition (e.g., to assist with application approval, determining whether to offer credit). Estimated income may also be used to supplement or validate stated income.

Second, absent clear guidance from regulators, many issuers have taken the conservative stance that income information must be no more than 12 months old. While the CARD Act does not address the time period for using existing income data, regulatory uncertainty has caused many issuers to conform to this approach. This complicates evaluations beyond the first year an account is on the books, during which time issuers are generally comfortable with the validity of data collected at account opening.

Ability to pay requirements have created operational complexity and may be partially responsible for the reduced access to credit outlined earlier in this letter. As discussed, the size and frequency of credit limit increases has declined substantially since implementation of the CARD Act.

Issuers have turned to alternative methods to comply with the law in a manner that mitigates disruption to business processes. To the extent they have access, issuers are capturing income information (e.g., deposit data) from across the banking relationship. These issuers feel strongly confident in such data. However, this option is only available to full-service banks and those offering deposit products. For monoline issuers or those that do not offer such products, collecting and validating income for the purposes of ongoing limit increases is less feasible, particularly beyond the first year an account is on the books. These issuers are at a disadvantage in this respect.

Alternative strategies, such as customer solicitations for the purposes of collecting updated income information, are generally viewed as risky. There is concern that these scenarios generate an adverse selection, whereby cardholders with a greater need for credit are significantly more likely to respond. Additionally, issuers have no method for ensuring the accuracy of such information. This raises larger questions regarding the validity of customer-provided income information, which may be either over or understated and is largely unsubstantiated. This stands in stark contrast to other indicators, such as behavior and credit scores, that use verifiable data and have been shown to be more closely related to risk and ability to pay.

Correlation to Risk

While issuers are complying with the requirement to assess repayment ability based on income and debt obligations, such requirements rest on the assumption that income and risk are closely related. Efforts by several issuers to substantiate this relationship have either failed to produce a demonstrable correlation or, contrary to expectations, revealed an inverse relationship between income and likelihood of default.

One issuer recently examined the incidence of charge-off in the context of discrete, 10-point DTI bands.

The analysis revealed an inverse relationship between DTI and risk, which is counter-intuitive.

- For all accounts, the highest charge-off rate resided in the lower 10-20 point DTI range.
- When transformed into a cumulative charge-off, the same trend appeared and showed that risk is virtually identical with a 100-point maximum DTI ratio as a 60-point maximum DTI ratio.
- Overall, the results indicate that risk is lower for accounts with higher DTI ratios.

A number of issuers we spoke with have conducted similar analyses, particularly when making decisions relative to underwriting guidelines, and have been similarly unable to establish a strong correlation between DTI and risk.

Our interpretation of these findings centers on information that DTI does not reflect, including credit history, payment behavior, and customer relationship data. This information may exert a greater influence on ability to pay than levels of income, assets, or debt. Additionally, it is important to note that measures of ability do not account for *willingness* to pay.

Such measures also fail to capture qualitative factors such as how individuals manage debt and deal with financial distress. One issuer noted that during the Great Recession, borrowers with lower-range prime FICO scores outperformed all other risk groups including superprime accounts. More borrowers within this population managed to maintain minimum-due monthly payments and demonstrated a greater overall ability to cope with unemployment. Conversely, superprime borrowers were less equipped to manage debt once they became unemployed. Bankruptcy filings were proportionately higher for the issuer's superprime borrowers, particularly those with FICO scores higher than 740. Many of these accounts exhibited few risk indicators before rapidly deteriorating.

DTI is relevant in some circumstances, particularly when a customer loses his or her source of income altogether. Assuming a customer has steady income, DTI as an indicator of risk becomes less reliable.

It is worth noting that, in the context of credit cards, required minimum-due payments are unlikely to "move the needle" on DTI – even in the case of large, fully-utilized credit lines. For example, a $20,000 credit card balance requires a minimum payment of approximately $400.

Conclusion

On behalf of the issuers and retailers that contributed to this commentary, we appreciate the Bureau's consideration of our response. These organizations share in the goals of enhanced transparency and strong consumer safeguards.

Such protections, including reduced fees and restrictions on repricing activity, come at a cost. This cost may be reflected in higher upfront prices, limited availability of credit, or diminished consumer choice. Since implementation of the CARD Act, we believe there is evidence of each. Rigid restrictions on issuer practices, including practices that have historically facilitated the extension of credit to underserved communities, have required fundamental changes in the industry’s approach.

We believe that strong consumer safeguards can be upheld. However, such protections must be weighed against the tradeoffs that accompany them. As discussed throughout this commentary, there are opportunities to adjust restrictions to balance them with sound management principles and more fully realize their intent.

We look forward to ongoing dialogue with the Bureau in its efforts to assess the functioning of the credit card market overall.