



February 2009

## **ICBA Regulatory Alert**

### **Final Credit Card and Overdraft Protection Rules**

#### **Summary of Final Amendments to Regulation Z (Truth in Lending Act), Regulation AA (Unfair or Deceptive Acts or Practices Act) and Regulation DD (Truth in Savings Act)**

On December 18, 2008, the Federal Reserve Board published changes to the Truth in Lending Act's Regulation Z to revise the credit card disclosures provided for consumers. These rules provide several changes to credit card disclosures including application/solicitation disclosures, account opening disclosures, periodic statements and change in terms notices. The amendments also contain changes to the advertising provisions, convenience check disclosures, billing error resolution requirements and requirements for the time when a payment is deemed to be received by a creditor. Banks must comply with these new rules by July 1, 2010.

In addition, the Federal Reserve, the Office of Thrift Supervision (OTS) and the National Credit Union Administration (NCUA) released final amendments to Regulation AA (Unfair or Deceptive Acts or Practices rule) which prohibit certain credit card practices that are deemed to be unfair. Specifically, the amendments prohibit practices relating to interest rate changes, application of late fees, payment allocation, double cycle billing and fees charged for certain higher cost credit cards. Banks must also comply with the amendments to Regulation AA by July 1, 2010.

The Federal Reserve also published final amendments to the Truth in Savings Act's Regulation DD to address disclosures relating to overdraft protection services. The amendments require banks to disclose the total amount of any overdraft or returned item fees imposed on an account by the statement period and the year-to-date. Banks must comply with the Regulation DD amendments by January 1, 2010.

Below are specific provisions to each of the final rules.

## I. Final Regulation Z Amendments Regarding Credit Card Disclosures

### Application/Solicitation Disclosures

- The final rule contains format and content changes to credit and charge card application and solicitation disclosures including new format requirements for the summary table of account terms, which include rules regarding type size, the use of boldface type for certain key terms, the placement of information and the use of cross references.
- Card issuers must disclose in the summary table the specific actions that trigger penalty annual percentage rates (APRs) (i.e., such as a late payment), the rate that will apply and the circumstances under which the penalty rate will expire or, if true, the fact that the penalty rate could apply indefinitely. The regulation also requires card issuers to use the term “penalty APR” instead of “default rate,” because this term is deemed to be more clear to the consumer.
- Card issuers must disclose inside the summary table the fees for paying late, exceeding a credit limit or making a payment that is returned, as well as cash advance and balance transfer fees.
- New required disclosures include returned-payment fees; required credit insurance, debt suspension or debt cancellation coverage fees; and foreign transaction fees.
- Variable APR information must be stated as a single phrase indicating the APR varies “with the market,” along with a reference to the type of index used, such as “Prime.”
- For credit cards with higher rates, additional disclosures are required if the card issuer requires fees or a security deposit to issue the card that are 15% or more of the minimum credit limit offered for the account. In addition, the card issuer is required to include an example in the summary table of the amount of available credit the consumer would have after paying the fees or security deposit, if the consumer receives only the minimum credit limit.
- Card issuers must place the name of the balance computation method outside of the disclosure table so it does not detract from the other cost information.
- Card issuers must use the heading “How to Avoid Paying Interest on Purchases” on the row which describes the grace period offered on all purchases, and the phrase “Paying Interest” if a grace period is not offered on all purchases.

## **Account-Opening Disclosures**

- Card issuers must provide a table summarizing key account terms at account-opening. The new table should be substantially similar to the table provided with direct mail credit card applications and solicitations, but should be more detailed.
- The table required at account opening must include disclosure on whether or not there is a grace period for all features of an account.
- For higher priced credit cards, card issuers must provide consumers a notice about the right to reject a plan when fees have been charged but the consumer has not used the plan.
- Card issuers can provide the more specific and inclusive account opening table at application in lieu of the table otherwise required at application/solicitation.
- Card issuers must disclose in writing at account opening interest, minimum charges, transaction fees, annual fees and penalty fees such as a fee for paying late, and these disclosures must be listed in the summary table. Card issuers can disclose other less critical charges orally or in writing before the consumer agrees to or becomes obligated to pay the charge.
- The account opening disclosures now must include disclosure of fees for expedited payment and expedited delivery.

## **Periodic Statement Disclosures**

- Card issuers must group all fees together and separately itemize interest charges by transaction type, without regard to whether the charges are considered “finance charges,” “other charges,” or neither.
- Interest charges must be identified by type (i.e., interest on purchases or interest on balance transfers) and so must fees (i.e., cash advance fee or late-payment fee).
- Card issuers must disclose the total fees and the total interest imposed for the cycle, and also disclose year-to-date totals for interest charges and fees.
- There is no longer a requirement to disclose the “effective” APR, because it is not considered to be a useful consumer disclosure.

- Card issuers must disclose the payment due date on the front side of the periodic statement, and must also disclose, in close proximity to the due date, the amount of the late payment fee and the penalty APR that could be triggered by a late payment.
- The effect of making only the minimum required payment on time to repay balances must also be disclosed, as required by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. Card issuers must disclose that:
  - making only the minimum payment will increase the interest the consumer pays and the time it takes to repay the consumer's balance;
  - a hypothetical example of how long it would take to pay a specified balance in full if only minimum payments are made; and
  - a toll-free telephone number that consumers may call to obtain an estimate of the time it would take to repay their actual account balance using only the minimum payment.
    - The Federal Reserve must establish and maintain, for two years, a toll-free telephone number for creditors that are depository institutions having assets of \$250 million or less, and the FTC must maintain a similar toll-free telephone number for use by customers of creditors that are not depository institutions.
    - The cost estimate will be based on a generic repayment schedule to be created by the Federal Reserve.
    - A card issuer may set up a toll-free telephone number to provide customers with the actual number of months that it will take consumers to repay their outstanding balance instead of providing an estimate based on the Federal Reserve's table. A card issuer that does so does not need to include the hypothetical example on its periodic statements, but must disclose the warning statement and the toll-free telephone number.
  - Card issuers can also provide the actual repayment disclosure on their periodic statements, and if they do, they need not disclose the warning, the hypothetical example and the toll-free telephone number on the periodic statement, nor need they maintain a toll-free telephone number to provide the actual repayment disclosure.

## **Change-in-Terms Notices**

- Card issuers generally must provide 45 days' advance notice prior to a change in any term required to be disclosed in the summary table provided at account-opening.
- Card issuers must provide 45 days' advance notice before interest rate increases due to the consumer's delinquency or default or as a penalty.
- If a changed term is one that must be provided in the account opening summary table, then creditors must provide that change in a summary table in the change-in-terms notice.
- If a notice enclosed with a periodic statement discusses a change to a term that must be disclosed in the account-opening summary table, or announces that a penalty rate will be imposed on the account, then a table summarizing the impending change must appear on the front of the periodic statement, but it is not required to be on the first page.

## **Advertising Provisions**

- Advertisements that state a periodic payment amount for an open-end credit plan must also state, in equal prominence to the periodic payment amount, the time period required to pay the balance and the total number of payments if only periodic payments are made.
- An advertisement may refer to a rate as "fixed" if the advertisement states the time period the rate will be fixed and that the rate will not increase during that period. If a time period is not specified, then the advertisement may refer to a rate as "fixed" only if the rate will not change while the plan is open.

## **Convenience Checks**

- The following key terms must be disclosed in a summary table on the front of the page containing checks that access credit card accounts:
  - any discounted initial rate, and when that rate will expire, if applicable;
  - the type of rate that will apply to the checks after expiration of any discounted initial rate and the applicable APR;
  - transaction fees applicable to the checks;

- whether a grace period applies to the checks, and if one does not apply, that interest will be charged immediately; and
- the date by which the checks must be used in order to receive any discounted initial rate offered on the checks.

### **Cut-off times and Due Dates for Mailing Payments**

- Provides a safe harbor that mailed payments received after 5 p.m. can be applied to the account the next day.
- Payment received on the next business day is timely if the creditor does not receive and accept mail on the due date.

### **Billing Error Resolution**

- Card issuers must complete their billing error investigation within two billing cycles.
- Card issuers cannot reverse credits that were credited to an account if they later determine that an error did not occur after the billing error resolution timeframe has expired.

## II. Final Regulation AA Amendments Regarding Credit Card Accounts

- **Time to Make Payments** - The final rule prohibits creditors from treating a payment as late for any purpose, such as to increase the APR or to impose fees, unless consumers have been provided a reasonable amount of time to make that payment. The rule provides a safe harbor providing that creditors may comply with the requirement by adopting reasonable procedures designed to ensure that periodic statements are mailed or delivered at least 21 days before the payment due date.
- **Allocation of Payments** - When different APRs apply to different balances on a credit card account (for example, purchases, balance transfers, cash advances), the final rule requires banks to allocate amounts paid in excess of the minimum payment either by applying the entire amount first to the balance with the highest APR or by splitting the amount pro rata among balances. The rule does not limit an issuer's ability to determine the amount of the required minimum periodic payment or how that payment is allocated.
- **Increasing Interest Rates** - The final rule requires creditors to disclose at account opening all interest rates that will apply to the account and prohibits increases in those rates, unless expressly permitted. Disclosing a range of interest rates or that an interest rate can be increased up to a certain amount does not satisfy this requirement. There are circumstances where a creditor can increase the interest rate which include:
  - If a rate disclosed at account opening expires after a specified period of time, creditors may apply an increased rate that was also disclosed at account opening. This exception does not permit increased rates that are based on the occurrence of an event, even if the event is disclosed in the account opening disclosures.
  - Creditors may increase a rate due to the operation of an index, such as if the rate is a variable rate.
  - After the first year of the account, creditors may increase a rate for new transactions so long as they comply with the 45-day advance change-in-terms notice requirement in Regulation Z. Creditors cannot apply these increased rates to existing balances.
  - Creditors may increase an interest rate when the consumer is more than 30 days' delinquent on the account, however this provision is subject to the 45 day advance notice requirement under Regulation

Z, and this exception does not include violations such as exceeding the credit limit, or returned checks.

- **Two-Cycle Billing** - The final rule prohibits creditors from calculating interest using a method referred to as “two-cycle billing,” when this method results in more interest charges. Under this method, when a consumer pays the entire account balance one month but does not do so the following month, the creditor calculates interest for the second month using the account balance for days in the previous billing cycle as well as the current cycle.
- **Financing of Security Deposits and Fees** – Creditors are prohibited from financing security deposits or fees for the issuance or availability of credit if, during the first year after account opening, those deposits or fees take up the majority of the available credit on the account. In addition, security deposits and fees exceeding 25% of the credit limit must be spread over no less than the first six months, rather than charged as a lump sum during the first billing cycle.

### III. Final Regulation DD Amendments Relating to Overdraft Protection

- **Disclosure of Aggregate Overdraft Fees** - The final rule extends to all financial institutions the requirement to disclose on periodic statements the aggregate dollar amounts charged for overdraft fees and for returned item fees for the statement period and the year-to-date. Currently, only financial institutions that promote or advertise the payment of overdrafts must disclose aggregate amounts.
- **Disclosure of Balance Information** - The final rule requires financial institutions that provide account balance information through an automated system (including, but not limited to, an ATM, Internet web site, or telephone response system) to provide a balance that does not include additional funds that may be made available to cover overdrafts. Financial institutions may disclose an additional balance that includes funds provided pursuant to a discretionary overdraft service or a line of credit, or funds that could be transferred from a consumer's linked individual or joint account, so long as the institution prominently states that the balance includes these additional amounts.