FEDERAL RESERVE SYSTEM
12 CFR Part 227
[Regulation AA; Docket No. R–1314]

DEPARTMENT OF THE TREASURY
Office of Thrift Supervision
12 CFR Part 535
[Docket ID. OTS–2009–00__]
RIN 1550–AC17

NATIONAL CREDIT UNION ADMINISTRATION
12 CFR Part 706
RIN 3133–AD62

Unfair or Deceptive Acts or Practices; Clarifications

AGENCIES: Board of Governors of the Federal Reserve System (Board); Office of Thrift Supervision, Treasury (OTS); and National Credit Union Administration (NCUA).

ACTION: Proposed rule; request for public comment.

SUMMARY: In December 2008, the Board, OTS, and NCUA (collectively, the Agencies) exercised their authority under the Federal Trade Commission Act to issue a final rule prohibiting institutions from engaging in specific acts or practices in connection with consumer credit card accounts. See 74 FR 5498 (Jan. 29, 2009). The Agencies understand that clarification is needed regarding certain aspects of the final rule. Accordingly, in order to facilitate compliance, the Agencies propose to amend specific portions of the regulations and official staff commentary.

DATES: Comments must be received on or before **[insert date that is 30 days after the date of publication in the Federal Register]**.

ADDRESSES:

Because paper mail in the Washington DC area and at the Agencies is subject to delay, we encourage commenters to submit comments by e-mail, if possible. We also encourage commenters to use the title "Unfair or Deceptive Acts or Practices" to facilitate our organization and distribution of the comments. Comments submitted to one or more of the Agencies will be made available to all of the Agencies. Interested parties are invited to submit comments as follows:

Board: You may submit comments, identified by Docket No. R-1314, by any of the following methods:

- Agency Web Site: http://www.federalreserve.gov. Follow the instructions for submitting comments at http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm.
- Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions for submitting comments.

- E-mail: regs.comments@federalreserve.gov. Include the docket number in the subject line of the message.
- Facsimile: (202) 452-3819 or (202) 452-3102.
- Mail: Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW, Washington, DC 20551.

All public comments are available from the Board's web site at http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm as submitted, unless modified for technical reasons. Accordingly, your comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper form in Room MP-500 of the Board's Martin Building (20th and C Streets, NW) between 9:00 a.m. and 5:00 p.m. on weekdays.

OTS: You may submit comments, identified by OTS-2009-00__, by any of the following methods:

- Federal eRulemaking Portal- "Regulations.gov": Go to http://www.regulations.gov, under the "more Search Options" tab click next to the "Advanced Docket Search" option where indicated, select "Office of Thrift Supervision" from the agency drop-down menu, then click "Submit." In the "Docket ID" column, select "OTS-2009-00__" to submit or view public comments and to view supporting and related materials for this proposed rulemaking. The "How to Use This Site" link on the Regulations.gov home page provides information on using Regulations.gov, including instructions for submitting or viewing public comments, viewing other supporting and related materials, and viewing the docket after the close of the comment period.
- Mail: Regulation Comments, Chief Counsel's Office, Office of Thrift Supervision, 1700 G Street, NW, Washington, DC 20552, Attention: OTS-2009-00__.
- Facsimile: (202) 906-6518.
- Hand Delivery/Courier: Guard's Desk, East Lobby Entrance, 1700 G Street, NW, from 9 a.m. to 4 p.m. on business days, Attention: Regulation Comments, Chief Counsel's Office, Attention: OTS-2009-00__.
- Instructions: All submissions received must include the agency name and docket number for this rulemaking. All comments received will be entered into the docket and posted on Regulations.gov without change, including any personal information provided. Comments, including attachments and other supporting materials received are part of the public record and subject to public disclosure. Do not enclose any information in your comment or supporting materials that you consider confidential or inappropriate for public disclosure.
- Viewing Comments Electronically: Go to http://www.regulations.gov, select "Office of Thrift Supervision" from the agency drop-down menu, then click "Submit." Select Docket ID "OTS-2009-00__" to view public comments for this notice of proposed rulemaking.
- Viewing Comments On-Site: You may inspect comments at the Public Reading Room, 1700 G Street, NW, by appointment. To make an appointment for access, call (202) 906-5922, send an e-mail to public.info@ots.treas.gov, or send a facsimile transmission to (202) 906-6518. (Prior notice identifying the materials you will be requesting will assist us in serving you.) We schedule appointments

on business days between 10:00 a.m. and 4:00 p.m. In most cases, appointments will be available the next business day following the date we receive a request.

NCUA: You may submit comments, identified by number RIN 3133-AD62, by any of the following methods:

- Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions for submitting comments.
- NCUA Web Site: http://www.ncua.gov/news/proposed_regs/proposed_regs.html. Follow the instructions for submitting comments.
- E-mail: Address to regcomments@ncua.gov. Include "[Your name] Comments on Proposed Rule Part 706" in the e-mail subject line.
- Facsimile: (703) 518-6319. Use the subject line described above for e-mail.
- Mail: Address to Mary Rupp, Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314-3428.
- Hand Delivery/Courier: Same as mail address.
- **Public inspection**: All public comments are available on the agency's website at http://www.ncua.gov/RegulationsOpinionsLaws/comments as submitted, except as may not be possible for technical reasons. Public comments will not be edited to remove any identifying or contact information. Paper copies of comments may be inspected in NCUA's law library at 1775 Duke Street, Alexandria, Virginia 22314, by appointment, weekdays between 9:00 a.m. and 3:00 p.m. To make an appointment, call (703) 518-6540 or send an e-mail to OGCMail@ncua.gov.

FOR FURTHER INFORMATION CONTACT:

Board: Benjamin K. Olson, Attorney, or Ky Tran-Trong, Counsel, Division of Consumer and Community Affairs, at (202) 452–2412 or (202) 452–3667, Board of Governors of the Federal Reserve System, 20th and C Streets, NW, Washington, DC 20551. For users of Telecommunications Device for the Deaf (TDD) only, contact (202) 263–4869.

OTS: April Breslaw, Director, Consumer Regulations, (202) 906–6989; Suzanne McQueen, Consumer Regulations Analyst, Compliance and Consumer Protection Division, (202) 906–6459; or Richard Bennett, Senior Compliance Counsel, Regulations and Legislation Division, (202) 906–7409, at Office of Thrift Supervision, 1700 G Street, NW, Washington, DC 20552.

NCUA: Matthew J. Biliouris, Program Officer, Office of Examination and Insurance, (703) 518–6360; or Moisette I. Green, Staff Attorney, Office of General Counsel, (703) 518–6540, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

SUPPLEMENTARY INFORMATION:

I. Background

In December 2008, the Federal Reserve Board (Board), the Office of Thrift Supervision (OTS), and the National Credit Union Administration (NCUA) (collectively, the Agencies) adopted a final rule under the Federal Trade Commission Act (FTC Act) to protect consumers from unfair acts or practices with respect to consumer credit card accounts. This rule was published in the **Federal Register** on January 29, 2009.

See 74 FR 5498 (January 2009 Rule). On that same date, the Board published a final rule amending the provisions regarding open-end credit (not home secured) in Regulation Z, which implements the Truth in Lending Act (TILA). See 74 FR 5244 (January 2009 Regulation Z Rule). The effective date for both rules is July 1, 2010. See 74 FR 5548; 74 FR 5388-5390.

Since publication of the two rules, the Agencies have become aware that clarification is needed to resolve confusion regarding how institutions will comply with particular aspects of those rules. Accordingly, in order to provide guidance and facilitate compliance with the January 2009 Rule by the effective date, the Agencies propose to amend portions of the rule and the accompanying staff commentary. These proposed amendments are discussed in detail in section III of this **SUPPLEMENTARY INFORMATION**. Similarly, elsewhere in today's **Federal Register**, the Board has proposed to amend certain aspects of the January 2009 Regulation Z Rule.

Although comment is requested on the proposed amendments, the Agencies emphasize that the purpose of these rulemakings is to clarify and facilitate compliance with the final rule, not to reconsider the need for – or the extent of – the protections that the rule affords consumers. Thus, commenters are encouraged to limit their submissions accordingly.

In addition, because the Agencies do not intend to extend the effective date for the January 2009 Rule, any amendments must be adopted in final form with sufficient time for institutions to implement the amended rule by July 1, 2010. The Agencies emphasize that, because this rulemaking focuses on clarifications to discrete aspects of the January 2009 Rule, institutions should continue their efforts to come into compliance with that rule as soon as practicable and, in any event, by July 1, 2010. In order to ensure that final clarifications can be provided as soon as possible, the Agencies are requiring that comments on this proposal be submitted within 30 days from publication in the **Federal Register**.[1]

II. Statutory Authority

Section 18(f)(1) of the FTC Act provides that the Board (with respect to banks), OTS (with respect to savings associations), and the NCUA (with respect to federal credit unions) are responsible for prescribing "regulations defining with specificity * * * unfair or deceptive acts or practices, and containing requirements prescribed for the purpose of preventing such acts or practices." 15 U.S.C. 57a(f)(1). In the **SUPPLEMENTARY INFORMATION** for the January 2009 Rule, the Agencies set forth the standards codified by Congress or adopted by the Federal Trade Commission for determining whether an act or practice is unfair or deceptive and applied those standards to the practices prohibited by the final rule. See 74 FR 5501 et seq. In addition, the OTS relied on its authority under the Home Owners' Loan Act (HOLA) as a secondary basis for its final rule. See, e.g., 74 FR 5505-5506. For purposes of this rulemaking, the Agencies continue to rely on this legal authority and analysis.

[1] Generally, NCUA gives the public 60 days to comment on proposed rules; however, a shorter comment period is appropriate in this instance to ensure compliance with the January 2009 Rule. See IRPS 87-2, 52 FR 35231 (Sept. 18, 1987).

III. Section-by-Section Analysis

The final rules adopted by the Board, OTS, and NCUA under the FTC Act are located in, respectively, parts 227, 535, and 706 of title 12 of the Code of Federal Regulations. For purposes of the discussion in this **SUPPLEMENTARY INFORMATION**, the Agencies use the shared numerical suffix for each provision. For example, § __.21 refers to the Board's 12 CFR 227.21, the OTS's 12 CFR 535.21, and the NCUA's 12 CFR 706.21.

Section __.21—Definitions

Subpart C to the Agencies' rules contains the provisions addressing consumer credit card accounts. Section __.21 defines certain terms used in Subpart C.

Section __.21(a) Annual Percentage Rate

Section __.21(a) defines "annual percentage rate" as the product of multiplying each periodic rate for a balance or transaction on a consumer credit card account by the number of periods in a year. In the text of the regulations and in the commentary, the Agencies sometimes use the term "rate" in place of "annual percentage rate" to conserve space and avoid repetition. To avoid possible confusion, the Agencies propose to add a new comment 21(a)-1, clarifying that, for purposes of Subpart C, "rate" has the same meaning as "annual percentage rate" unless otherwise specified. Furthermore, for clarity and consistency, the Agencies propose to substitute "rate" for "annual percentage rate" in the titles to certain comments. See comments 23-3, 23-6, 24(b)(2)-5, 24(b)(5)-2, 24(c)(1)(i)-2.

Section __.21(c) Consumer Credit Card Account

The provisions of Subpart C apply to "consumer credit card accounts," which are defined in § __.21(c) as accounts provided to a consumer primarily for personal, family, or household purposes under an open-end credit plan that is accessed by a credit or charge card. Based on questions received following issuance of the January 2009 Rule, the Agencies understand that clarification is needed regarding whether an outstanding balance on a consumer credit card account remains subject to Subpart C when the account is closed, when the account is acquired by another institution, and when the balance is transferred to another credit account. In particular, concerns have been raised that permitting institutions to apply an increased rate to an outstanding balance in these circumstances could lead to circumvention of the general prohibition in § __.24 on such increases.

To address these concerns, the Agencies propose to add comments 21(c)-1 through 3, which would clarify that, as a general matter, the protections in Subpart C continue to apply to an outstanding balance following the closure or acquisition of the account or the transfer of the balance to another credit account issued by the same institution (or its affiliate or subsidiary). Accordingly, in these circumstances, an institution must, for example, continue to provide consumers a reasonable amount of time to make payment on such balances pursuant to § __.22; allocate payments in excess of the required minimum periodic payment among such balances consistent with § __.23; and increase the annual percentage rates that apply to such balances only to the extent permitted by § __.24.

Because the protections in Subpart C cannot be waived or forfeited, the proposed comments do not distinguish between closures or transfers initiated by the institution and closures or transfers initiated by the consumer. In the January 2009 Rule, the Agencies determined that, because many of the prohibited practices cannot be effectively disclosed, consumers are unable to reasonably avoid the harm caused by those practices. Thus, as discussed below, allowing institutions to engage in the prohibited practices by obtaining the consumer's agreement could undercut the purpose of the rule.

Although there may be circumstances in which individual consumers could make informed choices about the benefits and costs of waiving the protections in Subpart C, an exception for those circumstances would create a significant loophole that could be used to deny the protections to other consumers. For example, if an institution offered to transfer its cardholder's outstanding balance to a credit product that would reduce the rate on the balance for a period of time in exchange for the cardholder accepting a higher rate after that period, the cardholder would have to determine whether the savings created by the temporary reduction would offset the cost of the subsequent increase, which would depend on the amount of the balance, the amount and length of the reduction, the amount of the increase, and the length of time it would take the consumer to pay off the balance at the increased rate. Based on extensive consumer testing conducted during the preparation of the January 2009 Rule (and the Board's January 2009 Regulation Z Rule), the Agencies believe that it would be very difficult to ensure that institutions disclose this information in a manner that will enable most consumers to make informed decisions about whether to accept the increase in rate. Although some approaches to disclose may be effective, others may not and it would be impossible to distinguish among such approaches in a way that would provide clear guidance for institutions. Furthermore, consumers might be presented with choices that are not meaningful (such as a choice between accepting a higher rate on an outstanding balance and losing credit privileges on the account). Thus, the proposed commentary to § __.21(c) would clarify that, as a general matter, the protections in Subpart C do not depend on whether the consumer agrees to the closure of an account or the transfer of a balance.

Accordingly, proposed comment 21(c)-1 states that, if a consumer credit card account with an outstanding balance is closed by the consumer or the institution, the account continues to be a consumer credit card account for purposes of Subpart C with respect to that balance. Thus, in these circumstances, the institution could not increase the rate that applies to the outstanding balance (except to the extent permitted by § __.24).

Proposed comment 21(c)-2 addresses circumstances in which an institution acquires a consumer credit card account with an outstanding balance by, for example, merging with or acquiring another institution or by purchasing another institution's credit card portfolio. In some cases, the acquiring institution may elect to close the acquired account and replace it with its own credit card account. <u>See</u> 12 CFR 226.12 comment 12(a)(2)-3. The acquisition of an account does not involve any choice on the part of consumers, and the Agencies believe that consumers whose accounts are acquired should receive the same level of protection after acquisition as they did beforehand. Accordingly, the proposed comment states that an institution that acquires a consumer credit card account remains subject to the provisions of Subpart C with respect to any outstanding balances on the account. For example, the institution would generally be prohibited from increasing the annual percentage rate on an outstanding purchase balance to the rate that the institution applies to purchases on its accounts.[2]

Finally, proposed comment 21(c)-3 addresses balance transfers between consumer credit card accounts issued by the same institution (or its affiliate or subsidiary) and balance transfers between accounts issued by different institutions. Balances may be transferred from one consumer credit card account issued by an institution to another consumer credit card account issued by the same institution when, for example, the consumer's account is converted from a retail credit card that may only be used at a single retailer or affiliated group of retailers to a co-branded general purpose credit card which may be used at a wider number of merchants. Because of the concerns discussed above regarding circumvention and informed consumer choice and for consistency with the issuance rules regarding card renewals or substitutions for accepted credit cards under Regulation Z, 12 CFR 226.12(a)(2), the Agencies believe – and proposed comment 21(c)-3 states – that these transfers should be treated as a continuation of the existing account relationship rather than the creation of a new account relationship. See 12 CFR 226.12 comment 12(a)(2)-2. Similarly, proposed comment 21(c)-3 would apply to circumstances where a balance is transferred to a line of credit accessed solely by an account number or another type of credit account issued by the same institution or its affiliate or subsidiary (except for an open-end credit plan secured by the consumer's dwelling).[3] Accordingly, under these circumstances, an institution could not, for example, apply an increased rate to an existing balance in a manner prohibited by § __.24.

In contrast, proposed comment 21(c)-3 also states that, when a consumer chooses to transfer a balance to a consumer credit card account issued by a different institution, Subpart C does not prohibit the institution to which the balance is transferred from applying its account terms to that balance, provided those terms comply with Subpart C. For example, if a consumer credit card account issued by institution A has a $1,000 purchase balance at an annual percentage rate of 15% and the consumer transfers that balance to a consumer credit card account with a purchase rate of 17% issued by institution B, institution B may apply the 17% rate to the $1,000 balance. However, institution B may not subsequently increase the rate that applies to that balance unless permitted by one of the exceptions in § __.24(b).

Although balance transfers from one institution to another raise some of the same concerns as balance transfers involving the same institution, the Agencies believe that transfers between institutions are not contrary to Subpart C because the institution to

---

[2] Thus, the acquiring institution would not be permitted to substitute a new index for the index applicable to an acquired variable rate balance if the change could result in an increase in the applicable annual percentage rate. See comment 24(b)(2)-1. An institution that does not utilize the index used to determine the variable rate for an acquired balance may, however, convert that rate to an equal or lower non-variable rate, subject to the notice requirements of 12 CFR 226.9(c). See comment 24(b)(2)-5.

[3] Proposed comment 21(c)-3 clarifies that Subpart C would not apply to balances transferred from a consumer credit card account issued by an institution to an open-end credit plans secured by the consumer's dwelling issued by the same institution (or its affiliate or subsidiary) because these plans provide protections that are similar to – and, in some cases, more stringent than – the protections in Subpart C. For example, a creditor may not change the annual percentage rate on a home-equity plan unless the change is based on an index that is not under the creditor's control and is available to the general public. See 12 CFR 226.5a(f)(1).

which the balance is transferred is not increasing the cost of credit it previously extended to the consumer. For example, assume that institution A has extended a consumer $1,000 of credit at a rate of 15%. Because § __.24 generally prohibits institution A from increasing the rate that applies to that balance, it would be inconsistent with § __.24 to allow institution A to reprice that balance simply by transferring it to another account. In contrast, in order for the $1,000 balance to be transferred to institution B, institution B must provide the consumer with a new $1,000 extension of credit in an arms-length transaction and should be permitted to price that new extension consistent with its evaluation of prevailing market rates, the risk presented by the consumer, and other factors. Thus, the transfer from institution A to institution B does not appear to raise concerns about circumvention of § __.24 because institution B is not increasing the cost of credit it previously extended.

The Agencies understand that drawing this distinction between balance transfers involving the same institution and balance transfers involving different institutions may limit an institution's ability to offer its existing cardholders the same terms that it would offer another institution's cardholders. Currently, however, the Agencies understand that institutions generally do not make promotional balance transfer offers available to their existing cardholders for balances held by the institution because it is not cost-effective to do so. Furthermore, although many institutions do offer existing cardholders the opportunity to upgrade to accounts offering different terms or features (such as upgrading to an account that offers a particular type of rewards), the Agencies understand that these offers generally are not conditioned on a balance transfer, which indicates that it may be cost-effective for institutions to make these offers without repricing an outstanding balance. Nevertheless, the Agencies solicit comment on the extent to which proposed comment 21(c)-3 would affect institutions' ability to make offers to existing cardholders.

Section___.22—Unfair Acts or Practices Regarding Time To Make Payment

Section __.22(a) provides that an institution must not treat a payment on a consumer credit card account as late for any purpose unless the consumer has been provided a reasonable amount of time to make the payment. Section __.22(b)(1) states that an institution must be able to demonstrate that it has complied with this requirement, and § __.22(b)(2) provides a safe harbor for institutions that have adopted reasonable procedures designed to ensure that periodic statements specifying the payment due date are mailed or delivered to consumers at least 21 days before the payment due date.

Comment 22(b)-3 offers an example of an alternative method of complying with § __.22(a). In this example, an institution that only provides periodic statements electronically and only accepts payments electronically for a particular type of consumer credit card account could comply with § __.22(a) even if it does not provide periodic statements 21 days before the payment due date. The Agencies understand that, although the example states that this type of account must also comply with "applicable law and regulatory guidance," an explicit reference to the consumer notice and consent procedures of the Electronic Signatures in Global and National Commerce Act (E-Sign Act), 15 U.S.C. 7001 et seq., may be helpful to avoid confusion. Accordingly, the Agencies propose to add an explicit reference to the E-Sign Act in comment 22(b)-3.

Section __.23—Unfair Acts or Practices Regarding Allocation of Payments

When different annual percentage rates apply to different balances on a consumer credit card account, § __.23 requires institutions to allocate any amount paid by the consumer in excess of the required minimum periodic payment (the excess payment) among the balances using one of two methods. The institution may apply the excess payment first to the balance with the highest annual percentage rate and any remaining portion to the other balances in descending order based on the applicable rate (the high-to-low method). Alternatively, the institution may allocate the excess payment among the balances in the same proportion as each balance bears to the total balance (the pro rata method).

When the Agencies originally proposed to address payment allocation, the proposed rule contained provisions specifically addressing accounts with a balance subject to a deferred interest program.[4] One of these proposed provisions would have permitted (but not required) an existing practice by some institutions of allocating excess payments first to a balance on which interest is deferred during the last two billing cycles of the deferred interest period so that consumers could pay off that balance and avoid assessment of the accrued interest. See proposed § __.23(b)(1)(ii), 73 FR 28916, 28942 (May 19, 2008). Some industry commenters supported this aspect of the proposal, while others argued that it would require burdensome changes to their systems. Some consumer group commenters argued that, rather than allowing institutions to choose whether to apply excess payments to deferred interest balances in the last two billing cycles, this allocation method should be mandatory. Due to other concerns about deferred interest plans, however, the January 2009 Rule did not include this provision. See 74 FR 5519, 5527-5528.

As discussed in greater detail below with respect to § __.24, the Agencies propose to clarify that – so long as consumers receive sufficient protections – institutions may continue to provide promotional programs under which a consumer will not be obligated to pay interest that accrues on a balance if that balance is paid in full prior to a specified date or expiration of a specified period of time (deferred or waived interest programs).[5] One area in which clarification is needed with respect to such programs is payment allocation. Under the current version of § __.23, if the deferred or waived interest balance is not the only balance on the account, the consumer would generally be required to pay off the entire outstanding balance in order to avoid interest charges on the deferred or waived interest balance.[6] If the consumer is unaware of the need to pay off the entire

[4] Many creditors offer deferred interest programs under which consumers are not obligated to pay interest on purchases if those purchases are paid in full by the end of a specified period. If the purchases are not paid in full when the period ends, these programs generally require the consumer to pay interest that has accrued on the purchases during the period.

[5] For purposes of this **SUPPLEMENTARY INFORMATION**, a waived interest program includes a promotional program where interest is refunded if a balance is paid in full within a specified period of time.

[6] For example, assume that a consumer credit card account has a $2,000 purchase balance with a 20% annual percentage rate and a $1,000 balance on which interest accrues at a 15% annual percentage rate, but the consumer will not be obligated to pay that interest if that balance is paid in full by a specified date. Regardless of whether the institution uses the high-to-low allocation method or the pro rata allocation

balance, the consumer would be charged interest on the deferred or waived interest balance and thus would not obtain the benefits of the promotional program.

To ensure that consumers are adequately protected, the Agencies propose to amend § __.23 to require institutions to allocate excess payments first to deferred or waived interest balances during the last two billing cycles of the promotional period. As noted above, this is consistent with the current practice of many institutions with respect to deferred interest plans and is generally beneficial to consumers insofar as it enables them to avoid interest charges by paying off the accrued interest balance in full prior to expiration without paying off all other balances on the account.[7] Accordingly, the Agencies propose to move the provisions in the current version of § __.23 to § __.23(a), to place the new provision for deferred or waived programs in § __.23(b), and to renumber the existing commentary accordingly. The Agencies also propose to add a new example in comment 23(a)-1 (proposed comment 23(a)(1)-1) illustrating the application of proposed § __.23(b). In addition, elsewhere in today's **Federal Register**, the Board has proposed to amend the disclosure requirements for periodic statements in Regulation Z, 12 CFR 226.7, to ensure that consumers are informed of the amount of interest accrued on the deferred or waived balance and the date by which that balance must be paid in full to avoid those accrued interest charges.[8]

Furthermore, the Agencies propose to amend comment 23-6 to clarify that, for purposes of § __.23, a balance on which interest will not be charged if the balance is paid in full prior to expiration of a specified period should be treated as a balance with an annual percentage rate of zero rather than a balance with the rate at which interest accrues during the promotional period (the accrual rate). As an initial matter, treating the rate as

---

method, the consumer would be required to pay $3,000 in order to avoid interest charges on the $1,000 balance. Indeed, under the current version of § __.23, the only circumstance in which the consumer could pay off the $1,000 balance without also paying off the $2,000 purchase balance would be if the $1,000 balance had a higher annual percentage rate than the $2,000 purchase balance and the institution chose to use the high-to-low method.

[7] As discussed above, for purposes of this proposal, the Agencies continue to rely on the legal authority and analysis contained in the January 2009 Rule. In particular, with respect to the proposed amendment to § __.23, the Agencies rely on the legal analysis regarding unfair payment allocation practices at 74 FR 5514-5517. In addition, the Agencies note that failing to allocate excess payments first to deferred or waived interest balances during the last two billing cycles of the promotional period appears to cause substantial consumer injury insofar as a different allocation method would result in the assessment of accrued interest (unless the consumer pays off all balances on the account). Because one of the intended purposes of a credit card account is to finance purchases over multiple billing cycles, it would be unreasonable to expect consumers to avoid accrued interest charges on a deferred or waived interest balance by paying off all balances on the account. Finally, failing to comply with the proposed amendment does not appear to create any benefits for consumers that would outweigh the injury. Indeed, the Agencies understand that the payment allocation practices of many institutions offering deferred or waived interest programs already comply with the proposed amendment.

[8] Specifically, the Board is proposing to amend 12 CFR 226.7 comment 7(b)-1 to require creditors offering deferred or waived interest programs to disclose on the periodic statement the balance subject to the program and the amount of interest that has accrued on that balance. In addition, the Board is proposing to add a new 12 CFR 226.7(b)(14) that would require creditors to state on the front of the periodic statement for the two billing cycles immediately preceding expiration of the promotional period the date on which the period expires and that the deferred or waived interest balance must be paid in full by a specific date in order to avoid accrued interest charges.

zero is consistent with the nature of the deferred or waived interest program insofar as the consumer will not be obligated to pay any accrued interest if the balance is paid in full prior to expiration. In addition, because § __.23 only applies when different annual percentage rates apply to different balances on the account, using the accrual rate for purposes of § __.23 could significantly narrow the protections of the payment allocation rules. Specifically, when the accrual rate for a deferred or waived interest balance is the same as the rate that applies to purchases (which the Agencies understand is often the case) and there are no other balances on the account, § __.23 would not apply if the accrual rate was used. For example, if an account has a $1,000 purchase balance with an annual percentage rate of 15% and a $2,000 balance on which interest accrues at 15% but will not be charged if that balance is paid in full within a specific period of time, § __.23 would not apply if the accrual rate of 15% was the applicable rate for the $2,000 balance for purposes of payment allocation. The Agencies believe that, in these circumstances, consumers should be afforded the protections in § __.23 (and, in particular, the protections in proposed § __.23(b)).

In addition, for purposes of the high-to-low allocation method in § __.23(a)(1), treating the rate on this type of promotional balance as zero during the accrued interest period ensures that excess payments will be applied first to balances on which interest is being charged, which will generally result in lower interest charges if the consumer pays the deferred or waived interest balance in full prior to expiration of the promotional period. Thus, using the above example, the amendments to comment 23-6 would clarify that an institution using the high-to-low method would allocate excess payments to the $1,000 purchase balance before the $2,000 balance until the last two billing cycles of the accrued interest period (when proposed § __.24(b) would require that excess payments be applied first to any remaining portion of the $2,000 balance). Although treating the rate on the deferred or waived interest balance as zero could prevent consumers who wish to pay off that balance in installments over the course of the promotional period from doing so, the Agencies believe that, on balance, this treatment produces the best overall outcome for consumers when the high-to-low allocation method is used.[9]

Finally, proposed comment 23(b)-1 would clarify that § __.23(b) applies to promotional programs under which the consumer is not obligated to pay interest that accrues on a balance if that balance is paid in full prior to the expiration of a specified period of time, not to grace periods offered by the institution.

Requests for Comment

The Agencies request comment on:

- Whether the provision in proposed § __.23(b) regarding balances on which interest will not be charged if the balance is paid in full by a specified date should apply during the last two billing cycles of the deferred or waived interest period or during a longer or shorter time period.
- Whether proposed § __.23(b) should apply to a grace period offered by the institution. In particular, the Agencies request comment on whether institutions offer grace periods that only require consumers to pay certain balances in full each billing cycle (rather than the entire balance) and, if so

[9] The Agencies note that, if the institution uses the pro rata allocation method, a proportionate amount of the excess payment will be applied to the deferred or waived interest balance each month during the promotional period.

whether proposed § _.23(b) should permit institutions to apply excess payments to those balances first.

Section __.24—Unfair Acts or Practices Regarding Increases in Annual Percentage Rates

Section __.24(a) requires institutions to disclose, at account opening, the annual percentage rates that will apply to each category of transactions on a consumer credit card account. In addition, § __.24(a) prohibits institutions from increasing those rates unless specifically permitted by one of the exceptions in § __.24(b).

As an initial matter, the Agencies understand that clarification is needed regarding the meaning of "category of transactions" for purposes of § __.24. Accordingly, the Agencies propose to add a new comment 24-3 to clarify that, for purposes of § __.24, a "category of transactions" is a type or group of transactions to which an annual percentage rate applies that is different than the annual percentage rate that applies to other transactions. For example, purchase transactions, cash advance transactions, and balance transfer transactions are separate categories of transactions for purposes of § __.24 if an institution applies different annual percentage rates to each. Furthermore, if, for example, the institution applies different annual percentage rates to different types of purchase transactions (such as one rate for purchases of gasoline and a different rate for all other purchases), each type constitutes a separate category of transactions for purposes of § __.24.[10]

In addition, the Agencies understand there is some confusion regarding whether certain changes to a consumer credit card account constitute an "account opening" for purposes of § _.24 generally, and in particular, the general prohibition on increasing rates during the first year after account opening. Accordingly, the Agencies propose to add a new comment 24-4 clarifying that, when a consumer has a credit card account with an institution and the consumer opens a new credit card account with the same institution (or its affiliate or subsidiary), the opening of the new account constitutes an "account opening" for purposes of § __.24 if the consumer retains the ability to obtain additional extensions of credit on both accounts. Thus, for example, if a consumer opens a credit card account with an institution on January 1 and opens a second credit card account with that institution on July 1of year one, the opening of the second account constitutes an account opening for purposes of § __.24 so long as the consumer can engage in transactions using either account. This is the case even if the consumer transfers a balance from the first account to the second. Thus, because the institution has two separate account relationships with the consumer, the general prohibition in § __.24 on increasing rates during the first year after account opening would apply to the opening of the second account.

In contrast, the comment would clarify that an account has not been opened for purposes of § __.24 when an institution replaces one consumer credit card account with another consumer credit card account (such as when a retail credit card is replaced with a cobranded general purpose card that can be used at a wider number of merchants) or when an institution consolidates or combines a credit card account with one or more other credit card accounts into a single credit card account. As discussed above, the Agencies

[10] As noted below, the Agencies request comment on whether institutions establish separate categories of transactions based on factors other than annual percentage rates and, if so, for what reasons.

believe that these transfers should be treated as a continuation of the existing account relationship rather than the creation of a new account relationship. Similarly, the comment would also clarify that the replacement of an acquired credit card account does not constitute an "account opening" for purposes of § __.24. Thus, in these circumstances, the general prohibition in § __.24 on increasing rates during the first year after account opening would not apply. However, when a replacement or consolidation occurs during the first year after account opening, proposed comment 24-4 would clarify that the institution may not increase an annual percentage rate in a manner otherwise prohibited by § _.24.[11] Similarly, the other protections in § __.24 (such as the limitations on repayment of protected balances in § __.24(c)) would still apply following the replacement or consolidation.

Finally, the Agencies understand that the replacement of one consumer credit card account with another generally is not instantaneous. If, for example, a consumer requests that a credit card account with a $1,000 balance be upgraded to a credit card account that offers rewards on purchases, the second account may be opened immediately or within a few days but, for operational reasons, there may be a delay before the $1,000 balance can be transferred and the first account can be closed.[12] Accordingly, the Agencies solicit comment on whether the appropriate amount of time for the replacement of one consumer credit card account with another is 15 days, 30 days, or a different period.[13]

Section __.24(a) General Rule

The Agencies also understand that there is some confusion regarding the relationship between comment 24(a)-1 and Regulation Z, 12 CFR 226.6(b)(2)(i)(D) with respect to the disclosure of penalty rates. Specifically, comment 24(a)-1 states that institutions cannot satisfy the disclosure requirements in § __.24(a) by disclosing a range of annual percentage rates or that a rate will be "up to" a particular amount. In contrast, when more than one penalty rate may apply, 12 CFR 226.6(b)(2)(i)(D) permits creditors to disclose "the highest rate that could apply, instead of disclosing the specific rates or the range of rates that could apply." Because the disclosure requirements in § __.24(a) are intended to ensure that consumers receive notice at account opening of the specific annual percentage rates that <u>will</u> apply to the categories of transactions on the account, those requirements do not apply to rates that may or may not apply depending on a particular event or occurrence (such as penalty rates) or rates that may be applied at the institution's discretion. Therefore, the Agencies propose to amend comment 24(a)-1 accordingly. The Agencies note, however, that this clarification is limited to the <u>disclosure</u> requirements in § __.24(a) and does not alter § __.24(a)'s general prohibition

[11] For example, assume that, on January 1 of year one, a consumer opens a consumer credit card account with a purchase rate of 15%. On July 1 of year one, the account is replaced with a consumer credit card account issued by the same institution, which offers different features (such as rewards on purchases). Under these circumstances, the institution could not increase the annual percentage rate for purchases to a rate that is higher than 15% pursuant to § __.24(b)(3) until January 1 of year two (which is one year after the first account was opened).

[12] As discussed above, the proposed commentary to § __.21 would clarify that, in these circumstances, the institution could not increase the annual percentage rate that applies to the $1,000 balance unless otherwise permitted by § __.24.

[13] Proposed comment 24-4 provides 15 days and 30 days as alternatives.

on applying penalty rates or other contingent rates unless specifically permitted by § __.24(b).

The Agencies also propose the following clarifications and technical corrections to the commentary to § __.24(a):

- Amend the example in comment 24(a)-2.i to clarify that the institution disclosed a penalty rate at account opening.
- Amend the example in comment 24(a)-2.iii to clarify that the 12 CFR 226.9(g) notice states that, if the consumer becomes more than 30 days late on the account, the penalty rate will apply to all balances on the account.
- Amend the example in comment 24(a)-2.iii.C to correct a typographical error.

Section __.24(b)(1) Account Opening Disclosure Exception

Section __.24(b)(1) provides that an annual percentage rate for a category of transactions may be increased to a rate disclosed at account opening upon expiration of a period of time disclosed at account opening. Under this exception, if, for example, an institution discloses at account opening that a 5% rate will apply to purchases for six months and that a 15% rate will apply thereafter, the institution can increase the rate on the existing purchase balance and on new purchases to 15% after six months. These plans are sometimes referred to as "stepped rates."

Comment 24(b)(1)-1 states that, because § __.24(b)(1) is limited to increased rates that <u>will</u> apply after a specified period of time, the exception does not permit application of increased rates that are disclosed at account opening but are contingent on a particular event or occurrence or may be applied at the institution's discretion. For example, as illustrated in comment 24(b)(1)-1.i, § __.24(b)(1) does not permit an institution to apply an increased penalty rate when a consumer makes a late payment even if the institution disclosed that rate at account opening. For clarity, the Agencies propose to move this language into the text of § __.24(b)(1). The Agencies also propose to amend comment 24(b)(1)-1 to clarify that the examples illustrate the application of § __.24, rather than just § __.24(a).

Comment 24(b)(1)-2 clarifies that nothing in § __.24 prohibits an institution from assessing interest due to the loss of a grace period to the extent consistent with the prohibition on two-cycle billing in § __.25. Because the Agencies understand that there is some confusion regarding the relationship between § __.24 and the provision of a grace period, the Agencies propose to add language to this comment clarifying that an institution has not reduced an annual percentage rate on a consumer credit card account for purposes of § __.24 if the institution does not charge interest on a balance when the consumer pays that balance in full prior to the expiration of a grace period. In addition, for organizational purposes, the Agencies propose to redesignate this comment as 24-2 and renumber comment 24(b)(1)-3 accordingly.

Finally, the Agencies understand that there is some confusion as to whether an institution waives the right to impose an increased rate pursuant to § __.24(b)(1) if it does not do so immediately upon expiration of the specified time period. As a general matter, because § __.24 is intended to increase predictability and transparency for consumers, the exceptions in § __.24(b) do not permit institutions to retain the right to increase a rate indefinitely and at their discretion. For example, if at account opening an institution discloses a stepped rate of 15% on purchases for one year and 20% thereafter, the institution can apply a lower rate of 17% at the end of the year but, if it wants to retain its right under § __.24(b)(1) to apply the 20% rate to purchases made during the first year, it must disclose to the consumer (pursuant to 12 CFR 226.9(c)) how long the 17% rate will apply and that the 20% rate will apply thereafter so that the consumer can make informed decisions when using the card. See comment 24(b)(1)-3 (proposed comment 24(b)(1)-2)).

The Agencies understand, however, that applying an increased rate on a specific date can present operational difficulties when that date falls in the middle of a billing cycle. Accordingly, to address this concern, the Agencies propose to add a new comment 24(b)-1 clarifying that, if § __.24(b) permits an institution to apply an increased annual percentage rate on a date that is not the first day of a billing cycle, the institution may delay application of the increased rate until the first day of the following billing cycle without relinquishing the ability to apply that rate.[14]

Section __.24(b)(3) Advance Notice Exception

Section __.24(b)(3) provides that an annual percentage rate for a category of transactions may be increased pursuant to a notice under 12 CFR 226.9(c) or (g) for transactions that occur more than seven days after provision of the notice. The Agencies understand that there has been some confusion regarding the interaction between this seven-day period in § __.24(b)(3) and the requirement in 12 CFR 226.9(c) and (g) that notice of an increased rate be provided at least 45 days prior to imposition of the increased rate. As illustrated in the examples in comment 24(b)(3)-3, the distinction is that the institution may apply the increased rate to any transaction that occurs after the seventh day following provision of the notice, but it must wait 45 days to begin accruing interest at that rate. The reason for this distinction is that the two time periods serve different purposes. The seven-day period is intended to ensure that the consumer receives the notice and is aware of the increased rate before engaging in transactions to which that increased rate will eventually apply (unless the consumer transfers or pays off the balance). See 74 FR 5531. In contrast, the 45-day period is intended to give the consumer sufficient time to evaluate whether to continue using the credit card account at the increased rate or whether better terms can be obtained elsewhere. See 74 FR 5344-5356. For additional clarity, the Agencies propose to amend comment 24(b)(3)-2 to state that, when calculating interest charges, § __.24(b)(3) does not permit an institution to reach back to days before the effective date of the rate increase under 12 CFR 226.9(c) or (g) – in other words, the date 45 days after provision of the notice.

The Agencies also propose to amend comment 24(b)(3)-2 to clarify when a transaction is deemed to have occurred for purposes of § __.24(b)(3). Specifically, the current version of comment 24(b)(3)-2 states that an institution may apply a rate increased pursuant to § __.24(b)(3) to transactions that are authorized within seven days – but are settled more than seven days – after provision of the notice. The Agencies

[14] For example, assume that, at account opening on January 1, an institution discloses that a 10% rate will apply to purchases for six months and a 15% rate will apply thereafter. The first day of the billing cycle for the account is the fifteenth of the month. If the six-month period expires on July 1, the institution may delay application of the 15% rate until July 15 without relinquishing its ability to apply that rate under § __.24(b)(1).

understand, however, that this distinction has created some confusion because, for example, authorization may not be obtained for all transactions and because the term "settled" could refer to different points in the payment process, including settlement between the acquirer and the merchant or settlement between the consumer and the card issuer. Accordingly, for consistency and clarity, the Agencies propose to amend comment 24(b)(3)-2 to clarify that when a transaction occurred for purposes of § __.24(b)(3) is determined by the date of the transaction (without regard to when the transaction is authorized, settled, or posted to the consumer's account). In addition, the Agencies would clarify that, when a merchant places a "hold" on the available credit on an account for an estimated transaction amount when the actual transaction amount will not be known until a later date, the date of the transaction for purposes of § __.24(b)(3) is the date on which the merchant determines the actual transaction amount. The Agencies also propose to amend the examples in comment 24(b)(3)-3 for consistency with these proposed changes.

In addition, the Agencies propose to amend § __.24(b)(3) and its commentary to reflect that notice of an increased rate may be provided under 12 CFR 226.9(b), which applies to supplemental access devices (such as convenience checks) and additional features added to the account after account opening. 12 CFR 226.9(b) requires creditors to disclose the rates and other key terms applicable to the device or feature before the consumer uses the device or feature for the first time. For example, 12 CFR 226.9(b)(3)(A) requires that creditors providing convenience checks to which a temporary promotional rate applies disclose key terms on the front of the page containing the checks, including the promotional rate, the period during which the promotional rate will be in effect, and the rate that will apply after the promotional rate expires. Thus, unlike rates increased pursuant to a 12 CFR 226.9(c) and (g) notice, the seven-day period is not necessary for rate increases disclosed pursuant to 12 CFR 226.9(b) because the device or feature will not be used before the consumer has received notice of the applicable rates and terms. Accordingly, the Agencies propose to amend § __.24(b)(3) to provide that increased rates disclosed pursuant to 12 CFR 226.9(b) must not be applied to transactions that occurred prior to provision of the notice. Section __.24(b)(3) would continue to provide that increased rates disclosed pursuant to 12 CFR 226.9(c) or (g) must not be applied to transactions that occurred within seven days after provision of the notice. The Agencies would also clarify in comment 24(b)(3)-2 that, if a rate increase is disclosed pursuant to both 12 CFR 226.9(b) and 12 CFR 226.9(c), that rate may only be applied to transactions that occur more than seven days after provision of the 12 CFR 226.9(c) notice. In addition, the Agencies would add an illustrative example in new comment 24(b)(3)-4.iv.

Finally, the Agencies understand that clarification is needed regarding the application of discounted promotional rates to existing accounts. As discussed above, § __.24(b)(1) permits stepped rates disclosed at account opening. In addition, comment 24(b)(3)-3 provides some examples of how a stepped rate could be provided pursuant to a 12 CFR 226.9(c) notice. The Agencies did not, however, specifically address circumstances in which a discounted promotional stepped rate is offered after account opening. Consistent with comment 24(b)(3)-3, the Agencies believe that, if the consumer receives advance notice of the term of the discounted rate and the rate that will apply after that term expires, a promotional stepped rate offer on an existing account can provide the same benefits to consumers as a promotional step rate offer at account opening so long as the offer cannot be used to increase the rate that applies to pre-existing balances.

Accordingly, to clarify that such offers are permitted, the Agencies propose to add a new comment 24(b)(3)-4 stating that nothing in § __.24 prohibits an institution from lowering the annual percentage rate that applies to an existing balance or to new transactions. The comment would further state, however, that, if a lower rate is applied to an existing balance, the institution cannot subsequently increase the rate on that balance unless it has provided the consumer with advance notice of the increase pursuant to 12 CFR 226.9(b) or (c). This notice must state the period of time during which the lower rate will apply (or the date until which that rate will apply) and the rate that will apply after expiration of that period. Furthermore, to ensure that the consumer receives notice of the offer before engaging in transactions that are subject to that offer (and will therefore eventually be taken to a higher rate), the comment would clarify that, when an institution applies a decreased rate to transactions that occurred prior to provision of the notice (or, in the case of a 12 CFR 226.9(c) or (g) notice, transactions that occurred within seven days after provision of the notice), the institution may not subsequently increase the rate that applies to those transactions to a rate that is higher than the rate that applied prior to the decrease.[15] Finally, the comment would provide illustrative examples of step rate offers that would comply with these requirements.[16]

Section __.24(b)(5) Workout Arrangement Exception

Section __.24(b)(5) provides that an annual percentage rate may be increased due to the consumer's failure to comply with the terms of a workout arrangement between the institution and the consumer, provided that the annual percentage rate applicable to a category of transactions following any such increase does not exceed the rate that applied to that category of transactions prior to commencement of the workout arrangement. This exception is intended to encourage institutions to continue offering workout arrangements that reduce rates for consumers in serious default, while also ensuring that a consumer who enters into such an arrangement but is unable to comply with its terms is not charged a rate that exceeds the rate that applied prior to the arrangement. See 74 FR 5532.

Because the term "workout" has been used by the Agencies in other contexts,[17] the Agencies understand that there is some confusion as to whether this exception also

---

[15] For example, assume that the annual percentage rate for purchases on an account is 15% and that, pursuant to 12 CFR 226.9(c), the institution provides notice on July 1 that a rate of 5% will apply to purchases until December 31, after which a rate of 17% will apply. If the institution applies the 5% rate to purchases made on or before July 8, the institution may only increase the rate on those purchases to a maximum of 15% on December 31.

[16] For the same reasons, the Agencies propose to amend comment 24(b)(1)-3 (proposed comment 24(b)(1)-2) to clarify that institutions may offer discounted step rates during the first year after account opening so long as the rate that applies after expiration of the discounted rate does not exceed the rate disclosed at account opening for that category of transactions.

[17] See, e.g., Board Supervisory Letter SR 03–1 on Account Management and Loss Allowance Methodology for Credit Card Lending (Jan. 8, 2003) (available at http://www.federalreserve.gov/boarddocs/srletters/2003/sr0301.htm); OTS Regulatory Bulletin RB 37-16

applies to temporary hardship arrangements that assist consumers in overcoming financial difficulties by lowering the annual percentage rate for a period of time. For example, if an account becomes seriously delinquent because of a loss of employment, the institution may reduce the rate that applies to the outstanding balance from the penalty rate to a rate of zero on the condition that the consumer make payments that will cure the delinquency within a specified period of time. If the arrangement is successful, the institution may choose to return the annual percentage rate to raise the annual percentage rate to the rate that applied prior to commencement of the temporary hardship arrangement. Because such arrangements can provide important benefits to consumers, the Agencies propose to amend § __.24(b)(5) and its commentary to clarify that this exception also applies to temporary hardship arrangements and when the consumer completes a workout or temporary hardship arrangement.

Proposed § __.24(b)(6) Servicemembers Civil Relief Act Exception

The Agencies understand that clarification is required regarding the relationship between § __.24 and certain provisions of the Servicemembers Civil Relief Act (SCRA), 50 U.S.C. app. 501 et seq. Specifically, 50 U.S.C. app. 527(a)(1) provides that "[a]n obligation or liability bearing interest at a rate in excess of 6 percent per year that is incurred by a servicemember, or the servicemember and the servicemember's spouse jointly, before the servicemember enters military service shall not bear interest at a rate in excess of 6 percent. * * *" With respect to consumer credit card accounts, this restriction applies during the period of military service. See 50 U.S.C. app. 527(a)(1)(B).[18]

Under the current version of § __.24, an institution that complies with the SCRA by lowering the rate that applies to an existing balance on a consumer credit card account when the consumer enters military service would not be permitted to increase the rate for that balance once the period of military service ends and the protections of the SCRA no longer apply. The Agencies did not intend this result, which appears to be inconsistent with the plain language of the SCRA. Accordingly, the Agencies propose to add a new exception in § __.24(b)(6) stating that an annual percentage rate that has been decreased pursuant to 50 U.S.C. app. 527 may be increased once that provision no longer applies, provided that the increased rate does not exceed the rate that applied prior to the period of military service.

Treatment of Deferred Interest and Similar Promotional Programs

In the final rule, the Agencies concluded that deferred interest programs, as currently designed and marketed, are inconsistent with the general prohibition in § __.24 on the application of increased rates to existing balances. See 74 FR 5527-5528. The Agencies noted that, although such programs provide substantial benefits to consumers who pay the balance in full prior to expiration of the program (thereby avoiding the assessment of interest charges), consumers who do not do so may be unfairly surprised, particularly because these programs are typically marketed as "interest free."

---

on Examination Handbook, Asset Quality Section 218, Credit Card Lending (May 8, 2006) (available at: http://files.ots.treas.gov/74827.pdf).

[18] 50 U.S.C. app. 527(a)(1)(B) applies to obligations or liabilities that do not consist of a mortgage, trust deed, or other security in the nature of a mortgage.

Accordingly, the Agencies determined that the assessment of deferred interest is effectively a repricing of past transactions subject to § __.24 and that prohibiting this practice would improve transparency and enable consumers to make more informed decisions regarding the cost of using credit.

The Agencies specifically stated, however, that § __.24 does not prohibit institutions from offering promotional programs that provide similar benefits to consumers but do not raise concerns about unfair surprise. In particular, the Agencies noted that an institution could offer a program in which interest is assessed on purchases at a disclosed rate for a period of time but the interest charged is waived or refunded if the principal is paid in full by the end of that period.

The Agencies understand that the distinction in the January 2009 Rule between deferred interest and waived or refunded interest has caused confusion with respect to how institutions should structure promotional programs in which the consumer will not be obligated to pay interest that accrues on a balance if that balance is paid in full by a specified date or within a specified period of time. In light of this confusion, the Agencies believe that the January 2009 Rule focused too heavily on the form or technical aspects of these programs.[19] Deferred interest programs should not be categorically prohibited while waived or refunded interest programs are categorically exempt from the requirements of the final rule. Instead, the Agencies believe the better approach is to focus on applying consistent standards to ensure that consumers are not unfairly surprised by the cost of using these types of promotional programs. Accordingly, the Agencies propose the following amendments.

As an initial matter, the Agencies understand that the distinction in the January 2009 Rule between "deferred interest" programs and "waived interest" or "refunded interest" programs could be read to suggest that some programs were covered by the final rule and others were not. Because the protections consumers receive should not depend on this technical distinction, the Agencies propose to amend the commentary to § __.24 to clarify that, although institutions may continue to provide promotional programs under which the consumer will not be obligated to pay interest that accrues on a balance if that balance is paid in full within a specified period of time, those programs are subject to all of the protections in § __.24, including the general prohibition on so-called "hair trigger" or "universal default" repricings of existing balances. See proposed comments 24(a)-2.iv and 24(b)(3)-4.iii. Thus, for example, if a consumer relies on this type of promotional program when making a purchase, the institution cannot deny the consumer the opportunity to avoid interest charges on that purchase by paying the purchase in full prior

[19] In particular, the Agencies understand that the references in the January 2009 Rule to "assessing" or "charging" interest have caused uncertainty about whether, during the promotional period, an institution must treat accrued interest for which the consumer may or may not ultimately be responsible (depending on whether the balance is paid in full prior to expiration) as part of the consumer's debt. The Agencies did not intend to regulate the accounting treatment of this accrued interest. Instead, the Agencies intended to ensure that consumers understand the amount of interest for which they will be responsible if the balance is not paid in full before expiration. As discussed elsewhere in this **SUPPLEMENTARY INFORMATION**, the Board is proposing amendments to Regulation Z in today's **Federal Register** to accomplish this purpose.

to expiration of the promotional period unless the consumer is more than 30 days' delinquent on the account.[20]

Furthermore, as discussed above, the Agencies propose to amend the payment allocation rules in § __.23 to ensure that consumers are not required to pay off all balances on the account in order to receive the benefits of these types of promotional programs. In addition, elsewhere in today's **Federal Register**, the Board has proposed to amend the advertising requirements in Regulation Z, 12 CFR 226.16, to address concerns that the use of terms such as "no interest" to describe deferred or waived interest programs may confuse consumers. Specifically, whenever "no interest" or a similar term is used in an advertisement for a deferred or waived interest program, proposed 12 CFR 226.16(h) would require the creditor to disclose that any balance subject to the program must be paid in full by the end of the promotional period to avoid interest charges (for example, "no interest if paid in full within six months"). In addition, the creditor would be required to state that, if the balance subject to the program is not paid in full within the promotional period, interest will be charged for the date the consumer became obligated for each transaction subject to the program.[21] The Agencies believe that these amendments will ensure that institutions can continue to offer programs that provide substantial benefits to consumers while protecting consumers from unexpected increases in the cost of completed transactions.

Finally, the Agencies understand that there is some confusion regarding implementation of the final rule with respect to existing deferred interest programs. As noted above, the effective date of the January 2009 Rule is July 1, 2010. In the **SUPPLEMENTARY INFORMATION** to that rule, the Agencies provided guidance regarding the implementation of § __.24. See 74 FR 5534. The Agencies did not, however, address the effect of the rule on deferred interest programs established prior to the effective date that expire after that date. The Agencies did not intend to convert these programs into interest-free loans by prohibiting an institution from charging interest if the deferred interest balance is not paid in full prior to expiration of the deferred interest period. However, the Agencies will not permit institutions to continue practices prohibited by the January 2009 Rule after the effective date. Accordingly, if a deferred interest program established prior to the effective date permits a consumer to avoid deferred interest charges by paying the deferred interest balance in full by a date that falls on or after July 1, 2010, the institution may charge deferred interest to the account consistent with the terms of the program, provided that: (1) any periodic statement mailed or delivered on or after July 1, 2010 complies with the disclosure requirements in 12 CFR 226.7 (as amended); and, (2) as of July 1, 2010, the institution fully complies with the protections in the January 2009 Rule (as amended), including the payment allocation requirements in proposed § _.23(b) and the prohibitions on "hair trigger" and "universal default" repricings in § _.24.

---

[20] If, however, the waived or deferred interest balance is not paid in full on or before the date the program expires, the institution is not required to wait an additional 30 days before charging accrued interest. See proposed comment 24(a)-2.iv.

[21] As discussed above, the Board has also proposed to amend the periodic statement disclosures in Regulation Z, 12 CFR 226.7, to ensure that consumers who utilize these types of promotional programs are informed of the date on which the program expires and the amount of interest for which they will be responsible if the promotional balance is not paid in full by that date.

24(c) Treatment of Protected Balances

The Agencies propose to amend comment 24(c)(2)-1 to clarify that § __.24(c)(2) does not prohibit an institution from continuing to assess a periodic fee that was assessed before the account had a protected balance or from assessing fees such as late payment fees if the only balance on the account is a protected balance.

Requests for Comment

The Agencies request comment on:

- Whether institutions establish separate categories of transactions based on factors other than annual percentage rates and, if so, for what reasons and whether proposed comment 24-3 should be revised accordingly.
- Whether the proposed implementation guidance regarding deferred interest plans provides sufficient protections for consumers and flexibility for institutions.

<u>Section __.25—Unfair Balance Computation Method</u>

Section __.25(a) prohibits institutions from imposing finance charges on balances on a consumer credit card account based on balances for days in billing cycles that precede the most recent billing cycle as a result of the loss of any time period provided by the institution within which the consumer may repay any portion of the credit extended without incurring finance charges. The prohibited practice is sometimes referred to as "two-cycle" or "double-cycle" billing.

As discussed above, the Agencies are proposing amendments to § __.23, § __.24, and Regulation Z that would clarify the substantive and disclosure requirements for promotional programs under which a consumer will not be obligated to pay interest that accrues on a balance if that balance is paid in full prior to a specified date or the expiration of a specified period of time. Consistent with these proposed amendments, the Agencies also propose to add a new comment 25(a)-3, clarifying that § __.25 does not prohibit the institution from charging accrued interest under this type of program if the balance is not paid in full prior to the specified date.

IV. Regulatory Analysis

Section VIII of the **SUPPLEMENTARY INFORMATION** to the January 2009 Rule set forth the Agencies' respective analyses under the Regulatory Flexibility Act (5 U.S.C. 601 <u>et</u> <u>seq</u>.) and the Paperwork Reduction Act of 1995 (44 U.S.C. 3506; 5 CFR part 1320 Appendix A.1). <u>See</u> 74 FR 5548-5551. This section also set forth the OTS's determinations with respect to Executive Orders 12866 and 13132 and the Unfunded Mandates Reform Act of 1995 as well as the NCUA's determinations with respect to Executive Order 13132 and the Treasury and General Government Appropriations Act, 1999. <u>See</u> 74 FR 5551-5558. Because the proposed amendments are clarifications and would not, if adopted, alter the substance of the analyses and determinations accompanying the January 2009 Rule, the Agencies continue to rely on those analyses and determinations for purposes of this rulemaking.

OTS and NCUA:

In accordance with section 3512 of the Paperwork Reduction Act of 1995, 44 U.S.C. 3501-3521 ("PRA"), the Agencies may not conduct or sponsor, and the respondent is not required to respond to, an information collection unless it displays a currently valid Office of Management and Budget ("OMB") control number. The information requirements contained in this joint clarification to the final rule on Unfair and Deceptive Acts or Practices have been submitted by the OTS and NCUA to OMB for review and approval under section 3507 of the PRA and section 1320.11 of OMB's implementing regulations (5 CFR part 1320)**.** The review and authorization information for the Board is provided earlier in this section along with the Board's burden estimates. There are no additional collections of information required by the clarifications to the final rule.

OTS: Savings associations and their subsidiaries.

NCUA: Federal credit unions.

Abstract: Under section 18(f) of the FTC Act, the Agencies are responsible for prescribing rules to prevent unfair or deceptive acts or practices in or affecting commerce, including acts or practices that are unfair or deceptive to consumers. On January 29, 2009, the Agencies published a final rule to protect consumers from unfair acts or practices with respect to consumer credit card accounts. See, 74 FR 5498. The Agencies are making several clarifications to that final rule.

Under § __.23(b) the Agencies are clarifying that if an institution offers deferred interest plans to consumers, it must allocate payments above the minimum to the deferred interest balance during the last two billing cycles the offer is in effect. In addition, under § __.24(b), the Agencies are clarifying that increasing an interest rate based on a contingency is prohibited, although an institution may re-instate an interest rate that it had reduced during a workout, temporary hardship or pursuant to 50 U.S.C. 50 app 527, the Servicemembers Relief Act. The clarifications do not impose any additional paperwork burden on institutions.

V. Solicitation of Comments on Use of Plain Language

Section 722 of the Gramm-Leach-Bliley Act requires the Board and OTS to use plain language in all proposed and final rules published after January 1, 2000. Additionally, NCUA's goal is to promulgate clear and understandable regulations that impose minimal regulatory burdens. Therefore, the Agencies specifically invite your comments on how to make this proposal easier to understand.

List of Subjects

12 CFR Part 227

Banks, Banking, Credit, Intergovernmental relations, Trade practices.

12 CFR Part 535

Consumer credit, Consumer protection, Credit, Credit cards, Deception, Intergovernmental relations, Savings associations, Trade practices, Unfairness.

12 CFR Part 706

Credit, Credit unions, Deception, Intergovernmental relations, Trade practices, Unfairness.

National Credit Union Administration

For the reasons discussed in the joint preamble, the Board proposes to amend 12 CFR Part 706 as set forth below:

PART 706—UNFAIR OR DECEPTIVE ACTS OR PRACTICES

1. Revise §706.23 as follows:

§706.23 [Revised].

When different annual percentage rates apply to different balances on a consumer credit card account:

(a) General rule. Except as provided in paragraph (b) of this section, a federal credit union must allocate any amount paid by a member in excess of the required minimum periodic payment among the balances using one of the following methods:

(1) High-to-low method. The amount paid by a member in excess of the required minimum periodic payment is allocated first to the balance with the highest annual percentage rate and any remaining portion to the other balances in descending order based on the applicable annual percentage rate.

(2) Pro rata method. The amount paid by a member in excess of the required minimum periodic payment is allocated among the balances in the same proportion as each balance bears to the total balance.

(b) Special rule for accounts subject to certain promotional programs. When a promotional program provides that a member will not be obligated to pay interest that accrues on a balance if that balance is paid in full prior to the expiration of a specified period of time, a federal credit union must allocate amounts paid by a member in excess of the required minimum periodic payment first to that balance during the two billing cycles immediately preceding expiration of the specified period and any remaining portion to the other balances consistent with paragraph (a) of this section.

2. Amend §706.24 by revising paragraph (b) as follows:

§706.24 [Revised].

* * * * *

(b) * * *

(1) Account opening disclosure exception. An annual percentage rate for a category of transactions may be increased to an annual percentage rate disclosed at account opening upon expiration of a period of time disclosed at account opening. This exception does not permit application of an increased annual percentage rate disclosed at account opening that is contingent on a particular event or occurrence or that may be applied at the federal credit union's discretion.

(2) Variable rate exception. An annual percentage rate for a category of transactions that varies according to an index that is not under the federal credit union's control and is available to the general public may be increased due to an increase in the index.

(3) Advance notice exception. An annual percentage rate for a category of transactions may be increased pursuant to a notice under 12 CFR 226.9(b), (c), or (g), provided that:

(i) If the federal credit union discloses the increased rate pursuant to 12 CFR 226.9(b), that rate must not be applied to transactions that occurred prior to provision of the notice;

(ii) If the federal credit union discloses the increased rate pursuant to 12 CFR 226.9(c) or (g), that rate must not be applied to transactions that occurred within seven days after provision of the notice; and

(iii) This exception does not permit an increase in any annual percentage rate during the first year after an account is opened.

(4) Delinquency exception. An annual percentage rate may be increased due to the federal credit union not receiving a member's required minimum periodic payment within 30 days after the due date for that payment.

(5) Workout and temporary hardship arrangement exception. An annual percentage rate may be increased due to a member's completion of a workout or temporary hardship arrangement between a federal credit union and the member or a member's failure to comply with the terms of such an arrangement, provided that the annual percentage rate applicable to a category of transactions following any such increase does not exceed the rate that applied to that category of transactions prior to commencement of the arrangement.

(6) Servicemembers Civil Relief Act exception. An annual percentage rate that has been decreased pursuant to 50 U.S.C. app. 527 may be increased once that provision no longer applies, provided that the annual percentage rate applicable to a category of transactions following any such increase does not exceed the rate that applied to that category of transactions prior to the decrease.

* * * * *

3. Amend Appendix A to part 706 by revising Subpart C as follows:

Appendix A to Part 706 – Official Staff Commentary

* * * * *

Subpart C—Consumer Credit Card Account Practices Rule

Section 706.21—Definitions

21(a) Annual Percentage Rate

1. Use of "rate." For purposes of Subpart C, "rate" has the same meaning as "annual percentage rate" unless otherwise specified.

21(c) Consumer Credit Card Account

1. Closed accounts. If a consumer credit card account with an outstanding balance is closed, the account continues to be the same consumer credit card account for purposes of Subpart C with respect to that balance. For example, if a federal credit union or a member closes a consumer credit card account with an outstanding balance, the

federal credit union would still be prohibited from increasing the annual percentage rate that applies to that balance unless permitted by one of the exceptions in §706.24(b).

2. Acquired accounts. If, through merger or acquisition, for example, a federal credit union acquires a consumer credit card account with an outstanding balance, the account continues to be the same consumer credit card account for purposes of Subpart C with respect to that balance. For example, if a consumer credit card account has a $1,000 purchase balance with an annual percentage rate of 12% and the federal credit union that acquires that account applies an 15% rate to purchases, the federal credit union would be prohibited from applying the 15% rate to the $1,000 balance unless permitted by one of the exceptions in §706.24(b).

3. Balance transfers.

i. Between accounts issued by the same federal credit union. If a balance is transferred from a consumer credit card account issued by a federal credit union to another credit account issued by the same federal credit union, the account continues to be the same consumer credit card account for purposes of Subpart C with respect to that balance unless the account to which the balance is transferred is an open-end credit plan secured by a member's dwelling. For example, if a consumer credit card account has a $2,000 purchase balance with an annual percentage rate of 12% and that balance is transferred to another consumer credit card account issued by the same federal credit union that applies an 15% rate to purchases, the federal credit union would be prohibited from applying the 15% rate to the $2,000 balance unless permitted by one of the exceptions in §706.24(b). Additional circumstances in which a balance is considered transferred for purposes of this comment include when:

A. A retail credit card with an outstanding balance is replaced or substituted with a cobranded general purpose card that can be used with a broader merchant base;

B. A credit card account with an outstanding balance is replaced or substituted with another credit card account offering different features;

C. A credit card account with an outstanding balance is consolidated or combined with one or more other credit card accounts into a single credit card account; and

D. A credit card account is replaced or substituted with a line of credit that can be accessed solely by an account number.

ii. Between accounts issued by different federal credit unions. If a balance is transferred to a consumer credit card account issued by a federal credit union from a consumer credit card account issued by a different financial institution that is not an affiliate or subsidiary of the federal credit union that issued the consumer credit card account, the account is not the same consumer credit card account for purposes of Subpart C with respect to that balance. Thus, the provisions of Subpart C do not prohibit the federal credit union to which the balance is transferred from applying its account terms to that balance, provided that those terms comply with Subpart C. For example, if a consumer credit card account issued by federal credit union A has a $1,000 purchase balance at an annual percentage rate of 13% and a member transfers that balance to a consumer credit card account with a purchase rate of 15% issued by federal credit union B, federal credit union B may apply the 15% rate to the $1,000 balance. However, federal credit union B may not subsequently increase the rate on that balance unless permitted by one of the exceptions in §706.24(b).

Section 706.22—Unfair Time To Make Payment

* * * * *

22(b) Compliance with General Rule

* * *

3. Example of alternative method of compliance. Assume that, for a particular type of consumer credit card account, a federal credit union only provides periodic statements electronically and only accepts payments electronically (consistent with applicable law and regulatory guidance, including the consumer notice and consent procedures of the Electronic Signatures in Global and National Commerce Act (E-Sign Act), 15 U.S.C. 7001 et seq.). Under these circumstances, the federal credit union could comply with §706.22(a) even if it does not provide periodic statements 21 days before the payment due date consistent with §706.22(b)(2).

* * *

* * * * *

Section 706.23—Unfair Acts or Practices Regarding Allocation of Payments

* * * * *

2. Adjustments of one dollar or less permitted. When allocating payments, the federal credit union may adjust amounts by one dollar or less. For example, if a federal credit union is allocating $100 pursuant to §706.23(a)(2) among balances of $1,000, $2,000, and $4,000, the federal credit union may apply $14 to the $1,000 balance, $29 to the $2,000 balance, and $57 to the $4,000 balance.

3. Applicable balances and rates. * * * * *

4. Use of permissible allocation methods. A federal credit union is not prohibited from changing the allocation method for a consumer credit card account or from using different allocation methods for different consumer credit card accounts, so long as the methods used are consistent with §706.23. For example, a federal credit union may change from allocating to the highest rate balance first pursuant to §706.23(a)(1) to allocating pro rata pursuant to §706.23(a)(2) or vice versa. Similarly, a federal credit union may allocate to the highest rate balance first pursuant to §706.23(a)(1) on some of its accounts and allocate pro rata pursuant to §706.23(a)(2) on other accounts.

* * * * *

6. Balances with the same rate. When the same annual percentage rate applies to more than one balance on an account and a different annual percentage rate applies to at least one other balance on that account, §706.23 generally does not require that any particular method be used when allocating among the balances with the same annual percentage rate. Under these circumstances, a federal credit union may treat the balances with the same rate as a single balance or separate balances. See comments 23(a)(1)-1.iv and 23(a)(2)-2.iv. However, when a member will not be obligated to pay interest that accrues on a balance if that balance is paid in full prior to the expiration of a specified period of time, that balance must be treated as a balance with an annual percentage rate of zero for purposes of §706.23 during that period of time. For example, if an account has a $1,000 purchase balance and a $2,000 balance on which the member will not be obligated to pay interest if that balance is paid in full prior to July 1 and a 15% annual percentage rate applies to both, the balances must be treated as balances with different rates for purposes of §706.23 until July 1. In addition, for purposes of allocating pursuant to

§706.23(a)(1), any amount paid by the member in excess of the required minimum periodic payment must be applied first to the $1,000 purchase balance except during the last two billing cycles of the promotional period (when it must be applied first to any remaining portion of the $2,000 balance). See comment 23(a)(1)-1.v.

23(a)(1) High-to-Low Method

1. Examples. For purposes of the following examples, assume that none of the required minimum periodic payment is allocated to the balances discussed (unless otherwise stated).

* * * * *

v. Assume that on January 1 a member uses a credit card account to make a $1,200 purchase subject to a promotional offer under which interest accrues at an annual percentage rate of 15% but the member will not be obligated to pay that interest if the balance is paid in full on or before June 30. The billing cycles for this account begin on the first day of the month and end on the last day of the month. Each month from January through June, the member uses the account to make $200 in purchases that are not subject to the promotional offer but are subject to the 15% rate. Each month from February through June, the member pays $400 in excess of the required minimum periodic payment on the payment due date, which is the twenty-fifth of the month. Any interest that accrues on the non-promotional purchases is paid by the required minimum periodic payment. A federal credit union using this method would allocate the $400 excess payments received on February 25, March 25, and April 25 as follows: $200 to pay off the non-promotional balance (that is subject to the 15% rate) and the remaining $200 to the promotional balance (that is treated as a balance with a rate of zero). Section 706.23(b), however, requires the federal credit union to allocate the entire $400 excess payment received on May 25 to the promotional balance. Similarly, §706.23(b) requires the federal credit union to allocate the $400 excess payment received on June 25 as follows: $200 to the promotional balance (which pays that purchase in full) and the remaining $200 to the non-promotional balance.

23(a)(2) Pro Rata Method

1. Total balance. A federal credit union may, but is not required to, deduct amounts paid by the member's required minimum periodic payment when calculating the total balance for purposes of §706.23(a)(2). See comment 23(a)(2)-2.iii.

23(b) Special Rule For Accounts Subject to Certain Promotional Programs

1. Grace periods. Section 706.23(b) applies to promotional programs under which the member is not obligated to pay interest that accrues on a balance if that balance is paid in full prior to the expiration of a specified period of time. A grace period during which a member may repay one or more balances on a consumer credit card account is not a "promotional program" for purposes of §706.23(b).

* * * * *

Section 706.24—Unfair Increases in Annual Percentage Rates

1. Relationship to Regulation Z, 12 CFR part 226. A federal credit union that complies with the applicable disclosure requirements in Regulation Z, 12 CFR part 226, has complied with the disclosure requirements in §706.24. See 12 CFR 226.5a, 226.6, 226.9. For example, a federal credit union may comply with the requirement in §706.24(a) to disclose at account opening the annual percentage rates that will apply to each category of transactions by complying with the disclosure requirements in 12 CFR 226.5a regarding applications and solicitations and the requirements in 12 CFR 226.6 regarding account-opening disclosures. Similarly, in order to increase an annual percentage rate on new transactions pursuant to §706.24(b)(3), a federal credit union must comply with the disclosure requirements in 12 CFR 226.9(b), (c), or (g). However, nothing in §706.24 alters the requirements in 12 CFR 226.9(c) and (g) that creditors provide consumers with written notice at least 45 days prior to the effective date of certain increases in the annual percentage rates on open-end (not home-secured) credit plans.

2. Relationship to grace period. Nothing in §706.24 prohibits a federal credit union from assessing interest due to the loss of a grace period to the extent consistent with §706.25. Additionally, a federal credit union has not reduced an annual percentage rate on a consumer credit account for purposes of § 706.24 if the federal credit union does not charge interest on a balance when the member pays that balance in full prior to the expiration of a grace period.

3. Category of transactions. For purposes of §706.24, a "category of transactions" is a type or group of transactions to which an annual percentage rate applies that is different than the annual percentage rate that applies to other transactions. For example, purchase transactions, cash advance transactions, and balance transfer transactions are separate categories of transactions for purposes of §706.24 if a federal credit union applies different annual percentage rates to each. Furthermore, if, for example, the federal credit union applies different annual percentage rates to different types of purchase transactions (such as one rate for purchases of gasoline and a different rate for all other purchases), each type constitutes a separate category of transactions for purposes of §706.24.

4. Account opening.

i. Multiple accounts with same federal credit union. When a member has a credit card account with a federal credit union and the member opens a new credit card account with the same federal credit union (or its affiliate or subsidiary), the opening of the new account constitutes an "account opening" for purposes of §706.24 if, more than 15/30 days after the new account is opened, the member has the ability to obtain additional extensions of credit on each account. For example, assume that, on January 1 of year one, a member opens a credit card account with a federal credit union. On July 1 of year one, the member opens a second credit card account with that federal credit union. On July 15, a $1,000 balance is transferred from the first account to the second account. The opening of the second account constitutes the opening of an account for purposes of §706.24 so long as, on July 17/August 1, the member can engage in transactions using either account. Under these circumstances, the bank could not increase an annual percentage rate on the second account pursuant to §706.24(b)(3) until July 1 of year two (which is one year after the second account was opened).

ii. Replacement or consolidation.

A. Generally. A consumer credit card account has not been opened for purposes of § 227.24 when a consumer credit card account issued by a bank is replaced or consolidated with another consumer credit card account issued by the same bank (or its affiliate or subsidiary). Circumstances in which a consumer credit card account has not been opened for purposes of § 227.24 include when:

(1) A retail credit card is replaced with a cobranded general purpose card that can be used at a wider number of merchants;

(2) A credit card account is replaced with another consumer credit card account offering different features;

(3) A credit card account is consolidated or combined with one or more other credit card accounts into a single credit card account; or

(4) A credit card account acquired through merger or acquisition is replaced with a credit card account issued by the acquiring federal credit union.

B. Limitation. A bank that replaces or consolidates a consumer credit card account with another consumer credit card account issued by the bank (or its affiliate or subsidiary) may not increase an annual percentage rate in a manner otherwise prohibited by § 227.24. For example, assume that, on January 1 of year one, a consumer opens a consumer credit card account with an annual percentage rate for purchases of 15%. On July 1 of year one, the account is replaced with a consumer credit card account that offers different features (such as rewards on purchases). Under these circumstances, the bank cannot increase the annual percentage rate for purchases to a rate that is higher than 15% pursuant to § 227.24(b)(3) until January 1 of year two (which is one year after the first account was opened).

24(a) General Rule

1. Rates that will apply to each category of transactions. Section 706.24(a) requires federal credit unions to disclose, at account opening, the annual percentage rates that will apply to each category of transactions on the account. A federal credit union cannot satisfy this requirement by disclosing at account opening only a range of rates or that a rate will be "up to" a particular amount. The disclosure requirements in §706.24(a) do not apply to annual percentage rates that are contingent on a particular event or occurrence or may be applied at the federal credit union's discretion (such as penalty rates) insofar as those rates may be applied consistent with §706.24.

2. Application of prohibition on increasing rates. Section 706.24(a) prohibits federal credit unions from increasing the annual percentage rate for a category of transactions on any consumer credit card account unless specifically permitted by one of the exceptions in
§706.24(b). The following examples illustrate the application of the rule:

i. Assume that, at account opening on January 1 of year one, a federal credit union discloses that the annual percentage rate for purchases is a non-variable rate of 5% and will apply for six months. The federal credit union also discloses that, after six months, the annual percentage rate for purchases will be a variable rate that is currently 9% and will be adjusted quarterly by adding a margin of 3 percentage points to a publicly available index not under the federal credit union's control. Furthermore, the federal credit union discloses that the annual percentage rate for cash advances is the same variable rate that will apply to purchases after six months. Finally, the federal credit union discloses that, to the extent consistent with §706.24 and other applicable law, a non-variable penalty rate of 15% may apply if a member makes a late payment. The payment due date for the account is the twenty-fifth day of the month and the required minimum periodic payments are applied to accrued interest and fees but do not reduce the purchase and cash advance balances.

* * * * *

iii. Assume that, at account opening on January 1 of year one, a federal credit union discloses that the annual percentage rate for purchases is a variable rate determined by adding a margin of 2 percentage points to a publicly-available index outside of the federal credit union's control. The federal credit union also discloses that, to the extent consistent with §706.24 and other applicable law, a non-variable penalty rate of 15% may apply if a member makes a late payment. The due date for the account is the fifteenth of the month. On May 30 of year two, the account has a purchase balance of $1,000. On May 31, the federal credit union provides a notice pursuant to 12 CFR 226.9(c) informing the member of a new variable rate that will apply on July 16 for all purchases made on or after June 8 (calculated by using the same index and an increased margin of 8 percentage points). On June 7, the member makes a $500 purchase. On June 8, the member makes a $200 purchase. On June 25, the federal credit union has not received the payment due on June 15 and provides the member with a notice pursuant to 12 CFR 226.9(g) stating that the penalty rate of 15% will apply as of August 9 to all transactions made on or after July 3 and that, if the member becomes more than 30 days late, the penalty rate will apply to all balances on the account. On July 4, the member makes a $300 purchase.

* * * * *

C. Same facts as paragraph A. above except the payment due on June 15 of year two is received on July 20. Section 706.24(b)(4) permits the federal credit union to apply the 15% penalty rate to all balances on the account and to future transactions because it has not received payment within 30 days after the due date. Because the federal credit union provided a 12 CFR 226.9(g) notice on June 25 stating the 15% penalty rate, the federal credit union may apply the 15% penalty rate to all balances on the account as well as any future transactions on August 9 without providing an additional notice pursuant to 12 CFR 226.9(g).

iv. Assume that, at account opening on January 1 of year one, the federal credit union discloses a promotional program under which interest on purchases made during January will accrue at a non-variable rate of 10%, but the member will not be obligated to pay that interest if those purchases are paid in full by December 31 of year one. On January 15, the member makes a purchase of $2,000. No other transactions are made on the account. The payment due on April 1 is not received until April 10. Section 706.24 does not permit the federal credit union to deny the member the opportunity to avoid interest charges on the $2,000 purchase by paying that purchase in full on or before December 31 of year one. If, however, the $2,000 purchase remains unpaid on January 1 of year two, §706.24 does not prohibit the federal credit union from charging the interest accrued on that purchase during year one.

24(b) Exceptions

1. Delayed implementation of rate increase. If §706.24(b) permits a federal credit union to apply an increased annual percentage rate on a date that is not the first day of a billing cycle, the federal credit union may delay application of the increased rate until the first day of the following billing cycle without relinquishing the ability to apply that rate. For example, assume that, at account opening on January 1, a federal credit union discloses that a non-variable annual percentage rate of 10% will apply to purchases for six months and a non-variable rate of 15% will apply thereafter. The first day of the billing cycle for the account is the fifteenth of the month. If the six-month period expires on July 1, the federal credit union may delay application of the 15% rate until July 15 without relinquishing its ability to apply that rate under §706.24(b)(1).

24(b)(1) Account Opening Disclosure Exception

1. Prohibited increases in rate. Section §706.24(b)(1) permits an increase in the annual percentage rate for a category of transactions to a rate disclosed at account opening upon expiration of a period of time that was also disclosed at account opening. Section 706.24(b)(1) does not permit application of an increased annual percentage rate disclosed at account opening that is contingent on a particular event or occurrence or may be applied at the federal credit union's discretion. The following examples illustrate rate increases that are not permitted by §706.24:

* * * * *

2. Application of rate that is lower than disclosed rate. Section §706.24(b)(1) permits an increase in the annual percentage rate for a category of transactions to a rate disclosed at account opening upon expiration of a period of time that was also disclosed at account opening. Nothing in §706.24 prohibits a federal credit union from applying a rate that is lower than a disclosed rate either during or upon expiration of the period. However, once the lower rate is applied to an existing balance, the federal credit union cannot subsequently increase the rate on that balance unless it provided the member with advance notice of the increase pursuant to 12 CFR 226.9(b) or (c). This notice must state the period of time during which the lower rate will apply and the rate that will apply after expiration of that period. Furthermore, a federal credit union that applies a lower rate to transactions that occurred during the first year after account opening may not subsequently increase the rate that applies to those transactions to a rate that is higher than the increased rate disclosed at account opening. The following examples illustrate the application of the rule:

* * * * *

ii. Assume that a federal credit union discloses at account opening on January 1 of year one that a non-variable annual percentage rate of 10% will apply to purchases for one year, after which that rate will increase to a non-variable rate of 12%. The federal credit union also discloses that, to the extent consistent with §706.24 and other applicable law, a non-variable penalty rate of 15% may apply if the member's required minimum periodic payment is received after the payment due date, which is the tenth of the month. The required minimum periodic payments are applied to accrued interest and fees but do not reduce the purchase balance.

A. On September 30 of year one, the account has a purchase balance of $1,400 at the 10% rate. On October 1, the federal credit union provides a notice pursuant to 12 CFR 226.9(c) informing the member that the rate for new purchases will decrease to a non-variable rate of 7% for six months (from October 1 through March 31 of year two) and that, beginning on April 1 of year two, the rate for purchases will increase to a non-variable rate of 13%. The federal credit union does not apply the 7% rate to the $1,400 purchase balance. On October 15 of year one, the member makes a $300 purchase at the 7% rate. On January 1 of year two, the federal credit union may begin accruing interest on the $1,400 purchase balance at 12% (as disclosed at account opening). On January 15 of year two, the member makes a $150 purchase at the 7% rate. On April 1 of year two, the 7% rate that applies to the $300 purchase and the $150 purchase expires. The federal credit union may begin accruing interest on the $150 purchase at 13% (as disclosed in the 12 CFR 226.9(c) notice). Because, however, the $300 purchase occurred during the first year after account opening, the federal credit union cannot increase the rate that applies to that purchase to a rate that is higher than the 12% rate disclosed at account opening.

B. Same facts as above except that the required minimum periodic payment due on November 10 of year one is not received until November 15. Section 706.24(b)(1) does not permit the federal credit union to increase any annual percentage rate on the account at this time. The federal credit union may, however, apply the 15% penalty rate to new transactions beginning on January 1 of year two pursuant to §706.24(b)(3) by providing a 12 CFR 226.9(g) notice informing the member of this increase no later than November 16 of year one. On January 1 of year two, §706.24(b)(1) permits the federal credit union to begin accruing interest on the $1,400 purchase balance at 12% (as disclosed at account opening). If the member makes the $150 purchase on January 15 of year two, §706.24(b)(3) would permit the federal credit union to apply the 15% rate to that purchase. On April 1 of year two, the 7% rate that applies to the $300 purchase expires. Because this purchase occurred during the first year after account opening, the federal credit union cannot increase the rate that applies to that purchase to a rate that is higher than the 12% rate disclosed at account opening.

24(b)(2) Variable Rate Exception

* * * * *

5. Changing a variable rate to a non-variable rate. * * * * *

* * * * *

24(b)(3) Advance Notice Exception

* * * * *

2. Transactions that occurred prior to provision of notice or within seven days after provision of notice. Section 706.24(b)(3) generally permits a federal credit union to apply an increased rate to transactions that occur after provision of a 12 CFR 226.9(b) notice or more than seven days after provision of a 12 CFR 226.9(c) or (g) notice. If a rate increase is disclosed pursuant to both 12 CFR 226.9(b) and 12 CFR 226.9(c), that rate may only be applied to transactions that occur more than seven days after provision of the 12 CFR 226.9(c) notice. Section 706.24(b)(3) does not permit a federal credit union to reach back to days before the effective date of the rate increase under 12 CFR 226.9(c) or (g) when calculating interest charges. See comment 24(b)(3)-3. Whether a transaction occurred prior to provision of a notice or within seven days after provision of a notice is determined by the date of the transaction. In some cases, however, a merchant may place a "hold" on the available credit on an account for an estimated transaction

amount when the actual transaction amount will not be known until a later date. In these circumstances, the date of the transaction for purposes of §706.24(b)(3) is the date on which the merchant determines the actual transaction amount. For example, assume that, when a member uses a credit card account to check into a hotel on July 1, the hotel obtains authorization for a $750 hold on the account to ensure there is adequate available credit to cover the anticipated cost of the stay. When the member checks out on July 4, the actual cost of the stay is $850 because of additional incidental costs, and the hotel charges this amount to the account. For purposes of §706.24(b)(3), the transaction occurred on July 4.

3. Examples.

i. Assume that a consumer credit card account is opened on January 1 of year one. On March 14 of year two, the account has a purchase balance of $2,000 at a non-variable annual percentage rate of 5%. On March 15, the federal credit union provides a notice pursuant to 12 CFR 226.9(c) informing a member that the rate for new purchases will increase to a non-variable rate of 8% on May 1. The notice further states that the 8% rate will apply for six months (until November 1) and states that thereafter the federal credit union will apply a variable rate that is currently 9% and is determined by adding a margin of 5 percentage points to a publicly-available index that is not under the federal credit union's control. The seventh day after provision of the notice is March 22 and, on that date, the member makes a $200 purchase. On March 24, the member makes a $1,000 purchase. On May 1, §706.24(b)(3) permits the federal credit union to begin accruing interest at 8% on the $1,000 purchase made on March 24. The federal credit union is not permitted to apply the 8% rate to the $2,200 purchase balance as of March 22. After six months (November 2), the federal credit union may begin accruing interest on any remaining portion of the $1,000 purchase at the previously-disclosed variable rate determined using the 3-point margin.

ii. Same facts as above except that on September 17 of year two (which is 45 days before expiration of the 8% non-variable rate), the federal credit union provides a notice pursuant to 12 CFR 226.9(c) informing the member that, on November 2, a new variable rate will apply to new purchases and any remaining portion of the $1,000 balance (calculated by using the same index and a reduced margin of 3 percentage points). The notice further states that, on May 1 of year three, the margin will increase to the margin disclosed in the March 15 notice (6 percentage points). On May 1 of year three, §706.24(b)(3) permits the federal credit union to increase the margin used to determine the variable rate that applies to new purchases to 5 percentage points and to apply that rate to any remaining portion of the $1,000 purchase as well as to new purchases. The federal credit union is not permitted to apply this rate to any remaining portion of the $2,200 purchase balance as of March 22.

4. Application of a lower rate. Nothing in §706.24 prohibits a federal credit union from lowering the annual percentage rate that applies to an existing balance or to new transactions. However, once the lower rate is applied to an existing balance, the federal credit union cannot subsequently increase the rate on that balance unless it provided a member with advance notice of the increase pursuant to 12 CFR 226.9(b) or (c). This notice must state the period of time during which the lower rate will apply and the rate that will apply after expiration of that period. Furthermore, a federal credit union that applies a decreased rate to transactions that occurred prior to provision of the notice

– or, in the case of a 12 CFR 226.9(c) or (g) notice, transactions that occurred within seven days after provision of the notice – may not subsequently increase the rate that applies to those transactions to a rate that is higher than the rate that applied prior to the decrease. The following examples illustrate the application of the rule:

i. Assume that a federal credit union discloses at account opening on January 1 of year one that a non-variable annual percentage rate of 7% will apply to purchases for one year, after which that rate will increase to a non-variable rate of 9%. The federal credit union also discloses that, to the extent consistent with §706.24 and other applicable law, a non-variable penalty rate of 15% may apply if the member's required minimum periodic payment is received after the payment due date, which is the tenth of the month. The required minimum periodic payments are applied to accrued interest and fees but do not reduce the purchase balance. On June 30 of year two, the account has a purchase balance of $1,000 at the 9% rate. On July 1, the federal credit union provides a notice pursuant to 12 CFR 226.9(c) informing the consumer that the rate for new purchases will decrease to a non-variable rate of 5% for six months (from July 1 through December 31 of year two) and that, beginning on January 1 of year three, the rate for purchases will increase to a non-variable rate of 10%. On July 8 of year two, the member makes a $200 purchase. On July 9, the member makes a $100 purchase. On January 1 of year three, §706.24(b)(3) permits the federal credit union to begin accruing interest on the $100 purchase at 10%. The federal credit union may not apply the 10% rate to the $200 purchase because that transaction occurred within seven days after provision of the 12 CFR 226.9(c) notice. If the federal credit union applied the 5% rate to the $1,000 purchase balance and the $200 purchase, the federal credit union may not increase the rate that applies to those amounts to a rate that is higher than 9% on January 1 of year three.

ii. Same facts as above except that the required minimum periodic payment due on September 10 of year two is not received until September 15 of year two. On September 15 of year two, the federal credit union provides a notice pursuant to 12 CFR 226.9(g) informing the member that the rate for new purchases will increase to the 15% penalty rate on October 31. On October 31, §706.23(b)(3) permits the federal credit union to begin accruing interest at 15% on any purchase made on or after September 23. The federal credit union may not, however, apply the 15% rate to the $1,300 in purchases. Instead, the federal credit union must continue to apply the 5% rate to the $100 purchase until at least January 1 of year three when §706.24(b)(3) permits the federal credit union to begin accruing interest on that purchase at 10%. Similarly, if the federal credit union applied the 5% rate to the $1,000 purchase balance and the $200 purchase, the federal credit union may begin accruing interest on those amounts at 9% on January 1 of year three.

iii. Assume that a federal credit union discloses at account opening on January 1 of year one that the rate that applies to purchases is a variable annual percentage rate that is currently 7% and will be adjusted quarterly by adding a margin of 3 percentage points to a publicly available index not under the federal credit union's control. The federal credit union also discloses that, to the extent consistent with §706.24 and other applicable law, a non-variable penalty rate of 15% may apply if the member's required minimum periodic payment is received after the payment due date, which is the first of the month. On July 30 of year two, the member uses the account for a $1,000 purchase in response to a promotional offer. Under the terms of this offer, interest on purchases made during the months of July through September will accrue at the variable rate for purchases but the member will not be obligated to pay that interest if all purchases made during that three-month period are paid in full by December 31 of year two. The payment due on September 1 of year two is not received until September 6. Section 706.24 does not permit the federal credit union to deny the member the opportunity to avoid interest charges on the $1,000 purchase by paying that purchase in full on or before December 31 of year two. The federal credit union may, however, provide a notice pursuant to 12 CFR 226.9(g) on September 2 of year two informing the member that the promotional offer does not apply to purchases made on or after September 10 and that the rate for such purchases will increase to the 15% penalty rate on October 18. On December 31 of year two, the $1,000 purchase has been paid in full. Under these circumstances, the federal credit union may not charge any interest accrued on the $1,000 purchase.

iv. Assume that a federal credit union discloses at account opening on January 1 of year one that the rate that applies to cash advances is a variable annual percentage rate that is currently 9% and will be adjusted quarterly by adding a margin of 3 percentage points to a publicly available index not under the federal credit union's control. On July 1 of year two, the federal credit union provides checks that access the account and, pursuant to 12 CFR 226.9(b)(3)(A), discloses that a promotional rate of 5% will apply to credit extended by use of the checks until January 1 of year three, after which the cash advance rate determined using the 3-point margin will apply. On July 15 of year two, the member uses one of the checks to pay for a $500 transaction. On January 1 of year three, §706.24(b)(3) permits the federal credit union to apply the cash advance rate determined using the 3-point margin to the $500 transaction.

24(b)(5) Workout and Temporary Hardship Arrangement Exception

1. Scope of exception. Nothing in §706.24(b)(5) permits a federal credit union to alter the requirements of §706.24 pursuant to a workout or temporary hardship arrangement between a member and the federal credit union. For example, a federal credit union cannot increase an annual percentage rate pursuant to a workout or temporary hardship arrangement unless otherwise permitted by §706.24. In addition, a federal credit union cannot require the member to make payments with respect to a protected balance that exceeds the payments permitted under §706.24(c).

2. Variable rates. If the annual percentage rate that applied to a category of transactions prior to commencement of the workout or temporary hardship arrangement varied with an index consistent with §706.24(b)(2), the rate applied to that category of transactions following an increase pursuant to §706.24(b)(5) must be determined using the same formula (index and margin).

3. Examples.

i. Assume that, consistent with §706.24(b)(4), the margin used to determine a variable annual percentage rate that applies to a $5,000 balance is increased from 3 percentage points to 5 percentage points. Assume also that the federal credit union and the member subsequently agree to a workout arrangement that reduces the margin back to 3 points on the condition that the member pay a specified amount by the payment due date each month. If the member does not pay the agreed-upon amount by the payment due date, the federal credit union may increase the margin for the variable rate that applies to the $5,000 balance up to 5 percentage points. 12 CFR 226.9 does not require advance notice of this type of increase.

ii. Assume that a member fails to make four consecutive minimum payments totaling $480 on a consumer credit card account with a balance of $6,000 and that, consistent with §706.24(b)(4), the annual percentage rate that applies to that balance is increased from a non-variable rate of 5% to a non-variable penalty rate of 15%. Assume also that the federal credit union and the member subsequently agree to a temporary hardship arrangement that reduces all rates on the account to 0% on the condition that the member pay an amount by the payment due date each month that is sufficient to cure the $480 delinquency within six months. If the member pays the agreed-upon amount by the payment due date during the six-month period and cures the delinquency, the federal credit union may increase the rate that applies to any remaining portion of the $6,000 balance to 5% or any other rate up to the 15% penalty rate.

24(c) Treatment of Protected Balances

* * * * *

24(c)(1) Repayment

* * * * *

Paragraph 24(c)(1)(i)

* * * * *

2. <u>Amortization when applicable rate is variable</u>. * * * * *

* * * * *

24(c)(2) Fees and Charges

1. <u>Fee or charge based solely on the protected balance</u>. A federal credit union is prohibited from assessing a fee or charge based solely on balances to which §706.24(c) applies. For example, a federal credit union is prohibited from assessing a monthly maintenance fee that would not be charged if the account did not have a protected balance. A federal credit union is not, however, prohibited from continuing to assess a periodic fee that was assessed before the account had a protected balance. Similarly, a federal credit union is not prohibited from assessing fees such as late payment fees or fees for exceeding the credit limit even if such fees are based in part on the protected balance or if the only balance on the account is a protected balance.

<u>Section 706.25—Unfair Balance Computation Method</u>

25(a) General Rule

* * * * *

3. <u>Charging accrued interest at expiration of certain promotional programs</u>. When a federal credit union offers a promotional program under which a member will not be obligated to pay interest that accrues on a balance if that balance is paid in full prior to a specified date or expiration of a specified period of time, §706.25 does not prohibit the federal credit union from charging that accrued interest to the account if the balance is not paid in full prior to the specified date (consistent with applicable law and regulatory guidance).

* * * * *

By the National Credit Union Administration Board, on April 21, 2009.

Mary F. Rupp
Secretary of the Board