The CARD Act ONE YEAR LATER

a cfpb conference

Overview

One year ago today, on February 22, 2010, many of the provisions of the Credit Card Accountability, Responsibility, and Disclosure Act (CARD Act) took effect.

When the CARD Act was signed into law in May 2009, it was clear the credit card market was in need of serious reform. Congress concluded that certain practices in the credit card industry were not fair and transparent to consumers, and the CARD Act passed with very strong bipartisan support in both the House and the Senate. As President Obama said when he signed the CARD Act into law, the Act was intended to uphold "basic standards of fairness, transparency, and accountability."

Later this summer, the new Consumer Financial Protection Bureau (CFPB) will assume responsibility for administering the CARD Act. To help guide it in performing these responsibilities, the CFPB has convened a conference, *The CARD Act: One Year Later*. To provide a factual basis for the discussion, the CFPB conducted a voluntary survey of the nine largest card issuers, who together represent approximately 90 percent of the credit card marketplace, about their current practices and future plans. Several other studies were also developed for this conference, including a report by the Office of the Comptroller of the Currency (OCC) that looks specifically at changes in the pricing practices of card issuers. To explore the impact of the CARD Act's new disclosure requirements on the consumer experience, the CFPB also commissioned a survey of cardholders.

These studies demonstrated that one year after the effective date of many provisions of the CARD Act, industry practices have changed in four significant ways.

- The long-standing practice of hiking interest rates on existing cardholder accounts has been dramatically curtailed.
- The amount of late fees consumers are paying has been substantially reduced.
- Overlimit fees have virtually disappeared in the credit card industry.
- Consumers report that their credit card costs are clearer, but significant confusion remains.

Interest Rate Hikes Dramatically Curtailed

Background: Prior to the enactment of the CARD Act, it was quite common for credit card companies to raise customers' interest rates, including the rates applied to existing balances. Often the hike was put into effect with little or no advance notice. The CARD Act has two provisions to address increases in interest rates:

- Card issuers generally are prohibited from increasing the interest rate on an existing balance unless the cardholder has missed two consecutive payments.

- Card issuers generally are permitted to increase the interest rate prospectively on new purchases, but must give the consumer 45 days advance notice – during which time the consumer may cancel the account.

One Year Later:

- The OCC study shows that as a result of the CARD Act, interest rate hikes on existing accounts have been dramatically curtailed. Prior to the CARD Act, approximately 15 percent of accounts were repriced over the course of a year; today that number is under 2 percent.

- The CFPB industry survey found that only one of the nine issuers currently has a practice of periodically reviewing the APR on existing accounts and raising interest rates for new purchases. Five of the top nine card issuers have increased, or plan to increase, the interest rate on new purchases for customers who are delinquent on past balances. A sixth bank plans to test such "delinquent pricing." The CARD Act does not prohibit issuers from doing so, and a number of card issuers have reserved the right to change rates if a cardholder is one day late. This is among the evolving market practices that CFPB will be called upon to monitor.

Unfair or Excessive Late Fees Reduced Substantially

Background: Prior to the enactment of the CARD Act, there were a variety of practices that could cause a cardholder to be assessed a late fee. Often, those fees were disproportionate to the harm or risk resulting from the cardholder's action. The CARD Act took a number of steps to curb excessive or unfair fees:

- Credit card bills must be due on the same date each month and payments received by 5:00 p.m. on the due date must be treated as timely. Card issuers generally cannot charge a late fee unless consumers are given at least 21 days to pay their bill.

- Under the Act, late fees and other penalty fees must be "reasonable and proportional" to the violation of the account terms in question. The Federal Reserve Board's implementing rule establishes a "safe harbor" benchmark for "reasonable and proportional" penalty fees, which the Board set at $25 for a first violation and $35 for a second violation within the next six months. Late fees also may not exceed the minimum payment due.

One Year Later:

- The OCC study shows that the CARD Act has substantially curbed late fees. The total amount of late fees paid by consumers dropped by more than half, from $901 million in January 2010 (before the effective date of the new late fee rules) to $427 million in November 2010 (the latest month for which data are available). The number of accounts assessed at least one late fee declined by almost 30 percent, and the average size of the late fee declined from $35 to $23.

- In the CFPB industry survey, six of the largest nine issuers reported that they have increased the amount of the minimum payment they charge. This change may reduce the total interest paid by certain cardholders, but also may result in increasing late fees.

Overlimit Fees Virtually Eliminated

Background: Prior to the CARD Act, card issuers could process transactions which exceeded a cardholder's credit limit, and then charge an overlimit fee in connection with the transaction – typically $39. If the cardholder was unable to pay enough to bring the balance back under the credit limit, overlimit fees could be charged month after month. The CARD Act has a number of provisions designed to address these practices, including the following:

- Card issuers are prohibited from charging an overlimit fee unless the cardholder expressly opts in to permit the issuer to process overlimit transactions. Such opt-ins are revocable at any time by the consumer, and the consumer must be notified of the right to revoke any time an overlimit fee is assessed.

- Card issuers may not charge more than one overlimit fee on any one billing statement.

- Overlimit fees also are generally subject to the same limits as those applicable to late fees.

One Year Later:

- The OCC study finds that overlimit fees have virtually disappeared in the credit card industry. The number of accounts charged an overlimit fee dropped from approximately 12 percent per year to about 1 percent.

- The CFPB industry survey found that all nine of the top issuers have continued to process some overlimit transactions -- but now, in many cases, without charging overlimit fees. Six of the nine never charge overlimit fees, while three sometimes do so but only for consumers who opt in.

Credit Card Costs Clearer

Background: Prior to the CARD Act, monthly statements provided consumers with limited information about their balances and obligations, and about the interest, finance charges, and other fees they were incurring. This information was presented with confusing terminology and in a format that could make it hard to find key information. This made it difficult for consumers to determine how much they were paying for their credit card. The CARD Act and related Federal Reserve Board rules made a number of changes, including the following:

- Each monthly statement must include how long it will take to pay off the bill and the total cost to the consumer as a result of paying only the minimum amount due.

- Each monthly statement must include how much the consumer should pay each month to pay the bill off in three years, the total cost to the consumer in doing so, and the savings compared to paying only the minimum payment.

- Regulations issued by the Federal Reserve Board, which took effect along with the CARD Act implementing rules, require each monthly statement to include the total amount of interest charged year to date, and a similar disclosure relating to the total amount of fees.

One Year Later: The CFPB's consumer survey, taken in context with other independent research conducted over the past six months, indicates that consumers have a better understanding of the costs of their credit card, but that they still do not feel very well informed:

- 57 percent of cardholders who are at least somewhat familiar with the CARD Act believe that the Act has been personally beneficial to them. However, awareness of the Act is modest: only 46 percent of cardholders report being very or somewhat familiar with the CARD Act, and 30 percent say they are not at all familiar with the law.

- Awareness of most of the changes made in monthly billing statements is higher than awareness of the CARD Act itself:

    - 80 percent of cardholders have noticed that their payments are now due on the same day of each month

    - 77 percent have noticed that the monthly statements contain a warning about the cost of making a late payment

    - 70 percent of cardholders have noticed that monthly statements now contain information about the consequences of making only minimum payments

    - 48 percent of consumers recall that their bill now tells them how much to pay each month in order to pay off the balance within three years

- 31 percent of cardholders who recall seeing the new information on their statement report that this information has caused them either to increase the payments they make or to reduce their use of credit.

- Of the cardholders who have noticed at least one of the changes in their monthly billing statements, 60 percent say that their monthly statements are easier to read and understand than they were a year ago. Additionally, 60 percent say that the terms of their credit card are clearer than they used to be.

- At the same time, 32 percent of those who carry a balance from month to month say they do not know how much interest they paid on their primary credit card last year. Other research on the consumer credit experience found that only 32 percent of consumers report that they understand their credit card terms completely.[1]

[1] J.D. Power and Associates, 2010 Credit Card Satisfaction Study

A Note About the CFPB Surveys

The CFPB industry survey with respect to pricing practices was sent to the largest nine bankcard issuers. Because the CFPB is not yet authorized to supervise these financial institutions, participation in the CFPB's data collection was voluntary. Each issuer agreed to respond, but to preserve anonymity, the issuers elected to retain an outside law firm to receive their individual responses and to submit an aggregated report to the CFPB.

The CFPB Consumer Survey was conducted by Synovate, a market research firm, between February 3 and February 8, 2011. An explanation with respect to the survey methodology and its limitations can be found at www.consumerfinance.gov/credit-cards/credit-card-act/.