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The Honorable Christopher J. Dodd
Chairman
The Honorable Richard C. Shelby
Ranking Minority Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Barney Frank
Chairman
The Honorable Spencer Bachus
Ranking Minority Member
Committee on Financial Services
House of Representatives

Subject: *Federal Reserve System; Department of the Treasury, Office of Thrift Supervision; and National Credit Union Administration: Unfair or Deceptive Acts or Practices*

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Federal Reserve System; Department of the Treasury, Office of Thrift Supervision; and National Credit Union Administration (the agencies), entitled “Unfair or Deceptive Acts or Practices” (Docket No. R-1314, RIN: 1550-AC17, and RIN: 3133-AD47). We received the rule on February 18, 2009. It was published in the *Federal Register* as a final rule on January 29, 2009, with a stated effective date of July 1, 2010. 74 Fed. Reg. 5498.

The final rule prohibits institutions from engaging in certain acts or practices in connection with consumer credit card accounts that the agencies have determined are unfair or deceptive. The agencies have the authority to prohibit such practices under section 5(a) of the Federal Trade Commission Act. 15 U.S.C. § 45(a). The agencies do not intend this rule to be a complete list of all unfair or deceptive acts and practices; other acts or practices may raise concerns regarding unfairness or deception and the agencies plan to continue to address those practices on a case-by-case basis through supervisory and enforcement actions.

The acts and practices prohibited by this rule include, first, a prohibition on institutions from treating a payment as late for any purpose unless consumers have been provided a reasonable amount of time to make the payment. The rule contains

a safe-harbor provision stating that if institutions adopt reasonable procedures designed to ensure that periodic statements are mailed or delivered at least 21 days before the payment due date, the institutions will have complied with this requirement. Second, the rule requires institutions to allocate amounts paid in excess of the minimum payment either by applying the entire amount first to the balance with the highest annual percentage rate or by splitting the amount *pro rata* among the balances. Third, the rule requires institutions to disclose at the opening of an account the rates that will apply to the account and prohibits institutions from increasing annual percentage rates unless expressly permitted. Fourth, the rule prohibits institutions from imposing finance charges based on balances for days in prior billing cycles because of the loss of a grace period. And last, the rule prohibits institutions from financing security deposits or fees for the issuance or availability of credit if, during the first year after account opening, the financed deposits and fees consume the majority of the available credit on the account. In addition, the rule requires deposits and fees exceeding 25 percent of the credit limit to be spread over no less than the first 6 months.

Enclosed is our assessment of the agencies' compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. Our review of the procedural steps taken indicates that the agencies complied with the applicable requirements.

If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to the subject matter of the rule, please contact Shirley A. Jones, Assistant General Counsel, at (202) 512-8156.

signed

Robert J. Cramer
Managing Associate General Counsel

Enclosure

cc: Robert M. Fenner
General Counsel, National Credit
Union Administration

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON A MAJOR RULE
ISSUED BY THE
FEDERAL RESERVE SYSTEM;
DEPARTMENT OF THE TREASURY,
OFFICE OF THRIFT SUPERVISION; AND
NATIONAL CREDIT UNION ADMINISTRATION
ENTITLED
"UNFAIR OR DECEPTIVE ACTS OR PRACTICES"
(DOCKET NO. R-1314, RIN: 1550-AC17, RIN: 3133-AD47)

(i) Cost-benefit analysis

The Federal Reserve System; Department of the Treasury, Office of Thrift Supervision; and National Credit Union Administration (the agencies) published information on the costs and benefits of this final rule. 74 Fed. Reg. 5552. The Office of Thrift Supervision (OTS) noted that the costs and benefits were difficult to measure with precision and that it relied on cost projections submitted by the credit card industry and reduced those estimates where they appeared overstated. Benefits such as protecting consumers from unfairness are intangible and are more difficult to quantify. OTS studied the benefits and the costs of this rule from its perspective as part of its analysis under Executive Order 12,866.

According to the agencies, the most important benefit of this final rule is that it will protect consumers from certain practices that meet well established standards for unfairness. In doing so, the agencies expect the rule to increase consumer confidence in the financial system. OTS expects that this final rule will further liquidity in the consumer credit card market by providing certainty to the industry, consumers, and other members of the public as to rules governing such transactions in the future. In addition, OTS anticipates that provisions of the final rule that are designed to ensure greater safety and soundness for financial institutions may also yield a beneficial economic result for the taxpayers who ultimately bear the cost of a program such as the Federal Reserve Board (the Board) Term Asset-Backed Securities Loan Facility program, which will make and insure loans backed by credit card securities.

The agencies state that this rule will promote more efficient functioning of the economy by creating more transparency for consumers as they make credit card agreements. According to the agencies, consumers currently are confused by the complexity of credit card agreements and are surprised by unexpected terms. In several of the areas addressed by the rule, disclosures have been inadequate to make the terms understandable. Consequently, the clear standards set by this rule are expected to promote more efficient credit decisions by consumers. As analyzed by the agencies, the rule will create stability, predictability, and standardization in the

credit card market and its receivables, and will help foster steady sources of funding that would otherwise avoid some risk and uncertainty. Another identified benefit of the rule is that it will create a uniform playing field for credit card issuers, not only because the federal financial regulators are issuing consistent rules, but also because of its clarity. Furthermore, issuers that have tried to provide better and clearer terms for consumers will no longer face a competitive disadvantage for doing so. By substantially limiting behavioral risk pricing, the rule is expected to foster more efficient risk-based pricing by credit card issuers at the initial underwriting stage. Consequently, this rule is expected to improve credit risk management. Issuer interest in assessing the cost of risk should be more closely aligned with the consumer interest in taking on more credit and being able to repay it. Finally, because the rule clearly defines several examples of unfair practices, the agencies expect to be able to monitor and supervise the credit card market more efficiently. Similarly, the reduced uncertainty should simplify issuer efforts to act in compliance with the law.

In analyzing the costs of this rule, OTS notes that most of the rule's provisions will have no economic impact on the vast majority of the institutions under OTS jurisdiction because the vast majority do not issue credit cards. OTS used the unverified revenue loss data submitted by the industry commenters to estimate the costs of this final rule to the industry at between \$97,223,000 and \$284,473,000. OTS believes that the consumers will incur significantly reduced interest charges as a result of this rule so they will have an overall benefit from this rule. Lastly, the costs on OTS will be insignificant, but rather are expected to make supervision and enforcement more efficient, less time consuming, and less burdensome.

The agencies conclude that the monetary costs and benefits of this rule have a net positive effect. Particularly, as a result of the payment allocation and retroactive rate increase provisions, some card issuers will experience reduced revenues and additional expenses, but the cost of credit will be substantially reduced for many consumers.

(ii) Agency actions relevant to the Regulatory Flexibility Act, 5 U.S.C. §§ 603-605, 607, and 609

The Board concluded that this final rule will have a significant economic impact on a substantial number of small entities, and, accordingly, prepared a Final Regulatory Flexibility Analysis. The analysis includes a succinct statement of the need for and objectives of the rule; a summary of the significant issues raised by public comments, an assessment of such issues, and a statement of changes made as a result of such comments; a description of the small entities to which the final rule will apply; a description of the recordkeeping, reporting, and other compliance requirements of the final rule; and a description of steps taken to minimize the significant economic impact on small entities. The analysis states that the rule is needed to protect consumers from specific unfair or deceptive acts or practices regarding consumer credit card accounts. The analysis further states that a wide

variety of alternatives were considered but the conclusion was reached that the restrictions in the final rule achieve the appropriate balance between providing effective protections for consumers and minimizing the burden on institutions that offer credit cards.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

OTS has determined that this final rule will not result in expenditures by state, local, or tribal governments in excess of \$100 million (\$133 million adjusted for inflation) but may result in expenditures by the private sector in excess of this amount. Accordingly, OTS states that it prepared a budgetary impact statement and addressed the alternatives considered.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 et seq.

On June 14, 2007, the Federal Reserve Board published a proposed rule on the amendments to the open-end credit (not home-secured) rules, to which it received more than 2,500 comments. 72 Fed. Reg. 32,948. On August 6, 2007, OTS published an advance notice of proposed rulemaking, to which it received 29 comment letters. 72 Fed. Reg. 43,570. On May 19, 2008, the agencies published proposed rules addressing unfair or deceptive acts or practices in connection with consumer credit card accounts and overdraft services. 73 Fed. Reg. 28,904. In total, the agencies received approximately 66,200 comments, the overwhelming majority of which came from individual consumers. The final rule notes that a substantial majority of individual consumers expressed support for the proposed rules, and many urged the agencies to go further in protecting consumers.

Paperwork Reduction Act, 44 U.S.C. §§ 3501-3520

The agencies determined that this final rule contains information collection requirements under the Act. The information collection requirements have Office of Management and Budget (OMB) Control Number 7100-0199. The total estimated annual burden is 19,416 hours.

Statutory authorization for the rule

The agencies stated that this final rule is promulgated under the authority of section 57a of title 15 and sections 1462a, 1463, and 1464 of title 12, United States Code.

Executive Order No. 12,866 (Regulatory Planning and Review)

OTS anticipates that this final rule will be economically significant under the Order because it will have an annual effect on the economy of \$100 million or more. OTS

states that it has provided OMB an economic analysis of the rule as required by the Order. OTS does note that its estimate of the annual effects of this rule may overstate the actual costs borne by institutions under OTS jurisdiction. The estimates may be high because (1) OTS-supervised institutions account for only a small part of the credit card market, (2) several provisions of the proposed rule are not included in the final rule reducing the overall economic impact, (3) many OTS-supervised institutions already do not engage in the practices prohibited by this final rule, (4) industry comments on the fee and interest income may have been overstated, and (5) OTS anticipates the credit card industry shrinking.

Executive Order No. 13,132 (Federalism)

OTS and NCUA determined that their portion of the final rule does not have any federalism implications for the purposes of the Order.