

**From:** carl@sercher.net on 03/24/2005 06:21:33 PM

**Subject:** Truth in Lending

Jennifer L. Johnson, Secretary  
Board of Governors  
Federal Reserve System  
20th and Constitution Ave., N.W.  
Washington, DC 20551

By email: [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov) or go to the [FRB website](#) to comment  
By fax: 202-452-3819

Re: Comments to Docket No. R-1217, Regulation of Credit Cards

Dear Ms. Johnson,

I am writing to comment on the Federal Reserve Board's recent advance notice of proposed rulemaking (ANPR) on open-ended credit, specifically on the regulation of credit cards. I believe that the current abusive practices of the credit card industry are placing millions of consumers, just like me, in financial jeopardy. Because of the persistent assertions of preemption of state credit laws by the credit card industry and the federal banking regulators, it is up to the Board and Congress to address these abuses.

I urge the Board to:

- improve the clarity and effectiveness of disclosures;
- tighten up the finance charge rules so that the APR is a more accurate gauge of the cost of credit;
- require the use of a "typical" APR in solicitations, applications, and at account opening to give consumers information that is more meaningful than just a periodic rate;
- retain the effective APR in billing statements;
- urge Congress to provide for substantive protections against the abuses of the credit card industry.

I discuss these recommendations more fully below.

## **An Industry Out of Control**

The virtually unregulated credit card industry – lending more than \$800 billion in revolving credit as of January 2005\* – must be reined in. The amount of credit card debt juggled by a majority of American households has exploded in the past decade. Much of this debt is caused not by consumers borrowing irresponsibly, but by the harsh – and exorbitantly expensive – tactics of the credit card industry

Credit card companies start by flooding consumers with billions of credit card solicitations, offering credit to just about anyone and heavily marketing to young consumers such as college students. They extend credit to anyone who has a decent credit score (or offer predatory subprime cards to those who do not) without actually assessing the consumer's ability to repay the amount of credit offered. As a result, the amount of credit card debt in America has almost quadrupled since 1981.

Once credit card companies have consumers in their grasp, they set up such an intricate trap of terms, fees, and penalties that many Americans find it hard to pay off their balances. They set minimum payments at tiny amounts, so that it takes consumers decades to pay off credit card debt and generates hundreds if not thousands of dollars in finance charges for the lenders.

Credit card lenders have rushed to increase junk fees since the fees were deregulated in 1996, jacking up late payment and over-limit fees from an average of \$14 to over \$30. They have been quick to impose these fees for even transgressions of a single day. They have created traps for unwary consumers with early morning cut-off times for payment.

Other offensive tactics include deceptive marketing, such as bait and switch tactics and trumpeting low APRs that only apply to certain transactions. Then the lenders take the consumers' payments and apply them to the low-APR balances, leaving the high-APR transactions to accrue hefty interest charges. Lenders also slip balance transfer, currency conversion, and other little-noticed fees into the consumer's balance.

Some of the most destructive tactics include imposing penalty rates of 30% to 40% APR for a single late payment or over-limit transaction of even \$1. Credit card issuers also employ universal default schemes, in which they impose sky-high APRs for late payments to *other* creditors or a simple drop in credit score.

Last but not least, is the fundamental issue of change-in-terms. All of the major credit card lenders have slipped in charge in terms provisions that allow them to change at will any aspect of a consumer's credit card account, including raising the APR, adding new fees, raising existing fees, lowering credit limits, and shortening the grace period. This is the only product in America where the seller can change the terms of the bargain after the sale is made, defying traditional contract law. In addition, unilateral change-in terms are unfair and undermine the whole concept of comparison shopping. What is the use of being a savvy consumer -- reviewing disclosures and comparing terms, - if a credit card company can change any of those terms with 15 days notice? As one court has described it, change-in-terms provisions create "an Orwellian nightmare, trapped in agreements that can be amended unilaterally in ways they never envisioned."

## **Credit Card Reforms Are Needed to Protect Consumers**

I ask the Federal Board to take action to address these abuses by the credit card industry. First, I ask the Board to use its authority under the Truth in Lending Act to amend Regulation Z to create an effective disclosure scheme that would truly inform consumers of the real costs of credit cards. Second, I urge the Board to ask Congress to pass laws that substantively regulate the credit card industry by limiting the rates, fees and practices they can engage in.

### **Credit Card Issuers helping to facilitate Identity Theft**

Many Credit Card issuers have adapted or initiated application policies which allow potential clients to apply for their credit cards over the phone or internet. The immediate problem that arises from these practices is that the Credit Card Issuer has no idea or proof that person applying for the credit card is actually the person they are claiming to be. The problem is further complicated by Credit Card Issuers who utilize these application procedures and then fail or refuse to send a written credit application/agreement to the address provided for review and the consumer's signature.

Many victim's of Identity Theft only learn that they have been victims after they start receiving past due notices phone calls or Court Summons from the Issuers or a debt collector. Even when consumers file Identity Theft reports with local law enforcement agencies, Credit Card Issuers will routinely sell these accounts to third party debt buyers or collectors to avoid taking a total loss on the account. It is common practice by debt collectors to file lawsuits in the name of the credit card issuer in an attempt to collect on these fraudulent debts. As one Debt Collector reportedly stated, "It's not are our responsibility to verify the validity of a debt, it's our job to get you to pay regardless". When this occurs, Consumer's are then forced to spend thousands of dollars to hire an attorney to defend them from these bad faith/frivolous lawsuits. If a consumer does not have the funds to hire an attorney, they are usually forced, through court

order (judgments), to pay these debts with funds they do not have and can not spare. The Board is in a position to help protect consumers from just such practices. By enacting or mandating some very simple procedures.

- That Credit Card Issuers who takes applications over the phone or internet shall be required to send out a written notice to the stated address within 24-48 hours after the phone or internet application has been approved.
- That within 15 days of approval of a phone or internet application, a Credit Card Issuer shall supply and obtain a signed credit agreement from the applicant.
- That a sworn to and dated copy of the written credit card application/agreement must be maintained and shall accompany any and all sales, transfers or assignment(s) of the account and/or debt.
- That Credit Card Issuers upon receiving a written notice from a consumer requesting a copy of the written credit agreement shall within 30 days provide the consumer a sworn to and dated copy of the agreement.

## **Clear and Effective Disclosures**

The Truth in Lending Act itself provides all of the tools necessary to ensure that credit card companies more effectively and clearly disclose their rates, fees, and terms. The Board has broad authority to issue regulations and impose requirements regarding disclosure. With this authority, the Board could help to ensure that consumers receive useful information in a readable format for credit cards.

I ask that the Board create a simple, effective, and understandable format for disclosures. Currently, some credit card disclosures, especially change in terms and initial disclosures, are in tiny print and full of dense technical jargon that the ordinary consumer has no hope of understanding. The one disclosure that a consumer has a hope of understanding is the “Schumer box” for applications and solicitations. To assist consumers in deciphering the terms of their credit cards, I urge the Board to require use of an improved Schumer box at every stage of the credit card process, including initial disclosures, periodic statements, and change in terms notices. This will help a consumer know whether the credit card he or she received from the lender has the same terms that were advertised in the solicitations. If changes-in-terms are still permitted, at least a consumer can easily compare the change by comparing the Schumer box of the change-in-terms notice with the Schumer box before the change.

Furthermore, I recommend that the Schumer box disclose all of the fees that a credit card company may impose. For applications and solicitations, it should include both the periodic rate that the lender is actually offering as well as a “typical” APR for the particular credit card program being offered. The typical APR is *far more* informative than the periodic rate provided under the current regime in the Schumer box because this APR is an average APR based on actual fee income produced. The typical APR would be extremely helpful to customers in their efforts to comparison shop. The periodic rate does not take into account the effect on the cost of credit of the fees that creditors charge. When shopping by use of the periodic rate and the dollar amount of advertised fees alone, the consumer cannot make an apples-to-apples comparison.

## **More Inclusive Finance Charge and Accurate APR**

At its core, TILA requires disclosure of all finance charges, defined as “ the sum of all charges, payable directly or indirectly by the person to whom the credit is extended, and imposed directly or indirectly by the creditor as an incident to the extension of credit.” This is a simple and inclusive definition that could capture all of the junk fees imposed by credit card lenders. It is the current exceptions and loopholes in Regulation Z that permit junk fees to escape disclosure as a finance charge and in the effective APR. I ask the Board to go back to the roots of TILA, and eliminate these exceptions and loopholes for junk fees so that they are properly included in the finance charge.

## Substantive Protections

While clear and inclusive disclosures are a necessary reform to protect American consumers from credit card abuse, they will never fully do the job. For that, we need a new federal law regulating credit card terms. I request that the Board accompany its regulatory changes with a strong recommendation to Congress. The message should be: pass federal legislation that will protect American consumers from the increasingly unfair, abusive, and virtually unavoidable practices of the credit card industry. Real, substantive limits on the terms of credit, and the cost of the credit, including the interest rate and all fees and charges, must be re-imposed. We recommend substantive regulation along the following lines—

- A cap on all periodic finance charge, for example, prime plus 10%.
- A cap on all other charges, whether considered a finance charge or not, to an amount the card issuer can show is reasonably related to cost.
- No unilateral change in terms allowed.
- No penalties allowed for any behavior not directly linked to the specific card account at issue.
- No improvident extensions of credit – real underwriting of the consumer’s ability to pay should be required.
- No mandatory arbitration, either for consumers’ claims, or for collection actions against consumers.
- Meaningful penalties for violating any substantive or disclosure rules which sting the issuer sufficiently to provide real incentives to obey the rules.
- A private right of action to enforce Section 5 of the Federal Trade Commission Act, which prohibits unfair or deceptive practices by businesses, including banks.
- Restore TILA’s authorization to states to add consumer protections by overturning contrary interpretations of the National Bank Act.

Finally, the Federal Reserve Board should advise Congress that it should amend the National Bank Act to overturn the OCC’s overbroad regulation purporting to extend preemption under the National Bank Act to virtually all aspects of the credit process. The Schumer box was based on innovations pioneered in a state legislature. States’ desires to protect their residents should be honored, not defeated, by federal law.

The Truth in Lending Act contemplates that states may in fact add stronger consumer protections, yet interpretations of the National Bank Act threaten to eviscerate that authorization as applied to nationally chartered banks. The Board should recommend that Congress reaffirm the role of the states in adding protections for credit consumers regardless of the type of charter held by the creditor.

## Conclusion

The Federal Reserve Board has a unique and critical role in how one of the most prevalent forms of consumer credit is regulated. It could take the easy road and simply tweak the TILA regulations for open end credit, essentially maintaining the current uneven playing field between a giant, well financed credit industry and individual consumers. It could take the low road, and bow to heavy pressures from this powerful, well-connected industry and make an already intolerable situation for American consumers, much worse, by reducing open end protections under TILA. Finally, it could take the high road and make serious changes in the regulations as permitted by current law to provide some balance to the current regulatory structure, as well as encourage Congress to make more significant statutory changes to protect individual consumers, facilitate the reduction in household debt and the increase family savings. In the interests of the American consumer, and the future of the American economy, I urge the Board to do the latter.

Thank You.

CarlM FI