Comments submitted by the Competitive Enterprise Institute, Todd J. Zywicki, Americans for Tax Reform & 60 Plus Association

May 3, 2023

In the matter of the proposed rule
"Credit Card Penalty Fees (Regulation Z)"
Consumer Financial Protection Bureau
Docket No. CFPB–2023–0010; RIN 3170–AB15

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To Whom It May Concern,

We are non-profit public interest groups, scholars, and advocates on behalf of consumers, small-business entrepreneurs, taxpayers and seniors. We have long supported consumer choice and competition and have highlighted the harms of price controls in any sector of the economy. We thus submit these comments on the proposed rule with a great deal of concern.

The proposed rule would sharply curtail penalty fees for late payments on credit card bills – slashing the maximum fee by more than two-thirds to $8 or less with no adjustment for inflation. In putting forth this rule, the Consumer Financial Protection Bureau (CFPB) has gone beyond what the law requires in an arbitrary and capricious manner. The rule is arbitrary and capricious because in interpreting the language of the law, it disregards standard regulatory and statutory interpretations of the word "reasonable" in setting rates and fees. In addition, the proposed rule raises constitutional concerns by potentially depriving banks and credit unions that issue cards of their property rights to a return on capital invested.

We view with alarm these legal violations and their ramifications. The likely effects of this rule will raise costs on the vast majority of consumers who pay their credit card bills on time. The shrinking availability of credit for all consumers will likely be worsened. Strong evidence shows that this rule would harm in particular some of the most vulnerable consumers, including seniors on fixed incomes. We believe this rule could put the numerous regional banks and credit unions that issue credit cards in further peril by snatching away a significant chunk of their revenue streams.

Introduction: Collectively, the organizations and individuals signing this letter have decades of experience educating, advocating and litigating on behalf of consumers, entrepreneurs, taxpayers and seniors.

The **Competitive Enterprise Institute** (CEI) is a Washington-based free-market public policy organization, founded in 1984, that studies the effects of regulations on job growth and economic well-being. Our mission is to advance the freedom to prosper for consumers, entrepreneurs, and investors. At CEI, we have long championed private-sector innovation that promotes financial inclusion and warned about government red tape that contributes to the problem of the unbanked. CEI also pursues public-interest litigation on behalf of consumers and small businesses to ensure that federal agencies follow the requirements of the underlying laws and, when applicable, the Administrative Procedures Act, and that agencies act within the constraints of the U.S. Constitution. In *State National Bank of Big Spring v. Mnuchin,* CEI challenged as unconstitutional the restrictions on presidential removal of the director of the CFPB and the funding mechanism that allows the CFPB to bypass the accountability of congressional appropriations. The Supreme Court sided with CEI's argument on presidential removal in *Seila Law v. CFPB*, and the Fifth Circuit Court of Appeals has recently ruled in favor of CEI's position on CFPB funding in *CFSA et al. v. CFPB,* which the Supreme Court will soon hear on appeal.

Todd J. Zywicki, a board member of CEI, is George Mason University Foundation Professor of Law at Antonin Scalia Law School at George Mason University and a Research Fellow of the George Mason Law & Economics Center. From 2015-2017 he was Executive Director of the George Mason Law and Economics Center. From 2020-2021 he served as Chair of the Consumer Financial Protection Bureau Taskforce on Federal Consumer Financial Law. Professor Zywicki is the author of more than 130 articles in leading law reviews and peer-reviewed economics journals. He is one of the Top 10 most-cited law professors in the field of Commercial Law, one of the Top 25 law professors on Twitter as measured by engagement levels, and one of the Top 50 most downloaded Law Authors of the Social Science Research Network.

Americans for Tax Reform is a nonprofit, 501(c)(4) taxpayer advocacy organization that opposes all tax increases and supports limited government, free-market policies. In support of these goals, ATR opposes

heavy regulation and taxation of financial services. ATR was founded at the request of President Ronald Reagan in 1985.

The **60 Plus Association** is a 31-year-old nonpartisan organization working for death tax repeal, saving Social Security and Medicare, affordable prescription drugs, lowering energy costs and other issues featuring a less government, less taxes approach as well as a strict adherence to the Constitution. 60 Plus calls on support from over 10 million activists. 60 Plus has been called, “an increasingly influential senior citizen’s group,” and recognized as a center-right alternative to the AARP.

Background: The CFPB is exceeding its statutory authority to impose draconian price controls that contravene the intent of the underlying legislation.

The Credit Card Accountability Responsibility and Disclosure Act of 2009 (CARD Act) requires that credit card late fees be “reasonable and proportional” to the cost of the late payments. To give card issuers some legal certainty as to fees that would be deemed “reasonable and proportional,” the legislation also authorized regulators to create a “safe harbor” by which a maximum late fee could be charged by credit card issuers without being in violation of the “reasonable and proportional” requirement. Initially enforcement and rulemaking authority for the CARD Act was housed with the Federal Reserve, but when Congress created the CFPB through the Dodd-Frank financial overhaul in 2010, it transferred this authority to this newly formed financial regulator.

The governing statutes require a measured, data-driven process in writing rules governing credit card fees. The legislative language states that in issuing rules, the CFPB “shall consider the cost incurred by the creditor” from cardholders violating the payment deadline and the “deterrence” effect such a fee would have in discouraging future late payments.[1]

The statutory language also specifically requires the CFPB to consult with prudential regulators in charge of safety and soundness for banks and credit unions – such as the Federal Reserve, Federal Deposit Insurance Corporation, and National Credit Union Administration – in proposing rules and setting the safe harbor. The “consultation” requirement reflects the concerns of lawmakers about the CFPB – tasked solely with the mission of consumer protection -- inadvertently creating rules seemingly beneficial to consumers that could nevertheless harm the financial system as a whole.

Initially, in 2010, the Federal Reserve set safe harbor amounts at $25 for the first late payment and $35 for subsequent late payments and made these amounts subject to an annual adjustment for inflation. The most recent inflation adjustment came in 2021, when the CFPB set the safe harbor amounts at $30 for the first late payment and $41 for subsequent late payments.[2]

The tortured logic of $8 price controls calls into question the rule’s reasonableness

Early this year, the CFPB shocked consumer finance observers by issuing this proposed rule that slashes the current safe harbor maximum fee by more than 70 percent to the *lesser* of $8 or 25 percent of a

[1] 15 U.S.C. Sec. 1665(d).
[2] Rohit Chopra, “Remarks of Director Chopra on Credit Card Late Fees,” Consumer Financial Protection Bureau, June 22, 2022, https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-director-chopra-on-credit-card-late-fees-anpr-press-call/.

cardholder's minimum payment due. No increase is allowed for the cardholder's subsequent late payments. And during a time of escalated inflation this rule ends the annual adjustment for inflation.

The CFPB's reasons for this drastic change are difficult to decipher. This proposal puts the rule on a collision course with the CARD Act's requirement that late fees be "reasonable" in their calculation, a mandate that applies to both the CFPB and card issuers in deciding the fee amounts that are appropriate. Also, the CFPB's ignoring both of relevant data and skirting of required procedures in promulgating this rule could be deemed "arbitrary and capricious" under a court's review.

In the rule, the CFPB admits that many consumers will be paying more and that it lacks data on important potential economic effects. The motives underlying this rule appear to be simple anger at what the CFPB perceived to be as ill-gotten gains by credit card issues and a misguided sense of paternalism on behalf of late payers it labels as "naïve," contrary to survey evidence of consumers' knowledge of deadlines and penalties.[3]

Another rationale seems to be for the CFPB to play a part in the Biden administration's war on what the president and administration officials call "junk fees." At a White House ceremony that included CFPB Director Rohit Chopra, President Biden defined "junk fees" loosely as "unfair hidden fees" and "surprise charges that companies sneak into bills because they can."[4]

Yet even by the president's broad definition of "junk fees," charges for late payments do not fit the bill. There is nothing "hidden" or "surprising" about late fees. They are ubiquitous throughout American consumers dealings with both the private sector and the government. The Internal Revenue Service (IRS), for instance, charges a "failure to pay" penalty for overdue taxes up to 25 percent of the amount a taxpayer owes.[5]

Surveys show that a large majority of consumers are familiar with credit card late fees, and also approve of them – perhaps more than they approve of sizable IRS late payment penalties. A recent poll from North Star Opinion Research found that 74 percent of cardholders know that their card issuer levies a late fee for payments not made on time.[6]

The same poll also found that 82 percent of cardholders always pay their credit card bills on time.[7] This is consistent with other data showing strong majorities, of nearly every demographic group, pay at least the minimum payment and don't incur late fees, even if they incur interest from carrying a balance.

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[3] Consumer Financial Protection Bureau, "Credit Card Penalty Fees (Regulation Z," Federal Register, Vol. 88, No. 60 (March 29, 2023), p. 18935, https://www.govinfo.gov/content/pkg/FR-2023-03-29/pdf/2023-02393.pdf (Referred to herein after in footnotes as "Federal Register.").
[4] Joe Biden, "Remarks by President Biden on Protecting American Consumers from Junk Fees," The White House, October 26, 2022, https://www.whitehouse.gov/briefing-room/speeches-remarks/2022/10/26/remarks-by-president-biden-on-protecting-american-consumers-from-junk-fees/.
[5] Internal Revenue Service, "Failure to Pay Penalties," accessed May 2, 2023, https://www.irs.gov/payments/failure-to-pay-penalty.
[6] "Credit Card Fee Survey," North Star Opinion Research, March 16, 2023, https://www.northstaropinion.com/credit-card-fee-survey. Quoted in Bill Hulse, "CFPB Moves to Punish People Who Pay Their Credit Card Bills On Time," U.S. Chamber of Commerce, April 21, 2023, https://www.uschamber.com/finance/the-cfpb-moves-to-punish-people-who-pay-their-credit-card-bills-on-time.
[7] Ibid.

Given these trends – and the fact that capping late fees will likely increase costs for those who pay on time – the proposed rule struggles at times to say just who would actually benefit from capping late fees. The rule admits, for instance, that "cardholders who never pay late will not benefit from the reduction in late fees and could pay more for their account if maintenance fees in their market segment rise in response - or if interest rates increase in response and these on-time cardholders carry a balance."[8]

The CFPB skirts Administrative Procedure Act by ignoring data and shortcutting review mechanisms

The "ifs" in the previous sentence regarding whether other cardholder fees and costs will increase is an example of the CFPB throwing up its proverbial hands in the rule in evaluating the negative economic effects. "Quantifying the benefits, costs, and impacts requires quantifying consumer and card issuer responses to the proposed changes, and the Bureau finds the body of knowledge on relevant behavioral responses and elasticities incomplete," states the proposed rule.[9]

It is the proposed rule itself that leaves the "body of knowledge" incomplete. In a potential violation of the Administrative Procedure Act, which requires a thorough review of relevant data, the CFPB ignores studies showing this rule would almost certainly increase costs and reduce availability of credit for many consumers – including lower-income consumers and seniors on fixed incomes.

The CFPB, for instance, ignores the findings of its own *Taskforce on Federal Consumer Financial Law Report* that even the relatively modest decreases in late fees that resulted from the initial enactment of the CARD Act "had substantial adverse unintended consequences for many other consumers in terms of card access, credit availability, and other prices, especially for nonprime borrowers."[10] Also overlooked by the CFPB are findings of recent studies that forced reductions in late fees cause credit card interest rates to rise.[11] The CFPB also never looks at the potential negative effects of this rule on seniors,[12] who already face burdens in getting credit based on their mix of assets and fixed income, and could fall victim to any policy that forces financial institutions to curb credit availability.

The proposed rule also appears to circumvent statutory requirements of rulemaking for the CARD Act and the CFPB's own rulemaking procedures. According to its own documentation in the proposed rule, the CFPB has apparently not completed the "consultation" with prudential bank and credit union regulators, which the CARD Act requires. It merely "offered to consult with the appropriate prudential

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[8] Federal Register, p. 18934.
[9] Ibid, p. 18931.
[10] Todd Zywicki et al., *Taskforce on Federal Consumer Financial Law Report*, Consumer Financial Protection Bureau, January 5, 2021, Vol. 1, p. 597, https://www.consumerfinance.gov/data-research/research-reports/taskforce-on-federal-consumer-financial-law-report/.
[11] Interview with Todd Zywicki, Consumer Finance Monitor podcast (Season 6, Episode 10), March 9, 2023, transcript available here. https://www.ballardspahr.com/-/jssmedia/Main/Podcast-Transcripts/CFM0610.pdf?rev=60009dc5bdcf468db31f3f91bc9de46d&hash=BB82C04E1DCD32737FA404A120231E99. See Daniel Grodzicki et al., "Consumer Demand for Credit Card Services," *Journal of Financial Services Research* (April 25, 2022), https://doi.org/10.1007/s10693-022-00381-4; Nadia Massoud et al., "The Cost of Being Late? The Case of Credit Card Penalty Fees," *Journal of Financial Stability*, Vol. 7, No. 2 (June 2011), pp. 49–59, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=890826.
[12] Erin Hurd, "Is It Harder for Seniors to Get Credit Cards," NerdWallet, August 18, 2020, https://www.nerdwallet.com/article/credit-cards/is-it-harder-for-seniors-to-get-credit-cards.

regulators."[13] Such consultation is especially important now, given recent bank failures, as the prudential regulators would have specialized knowledge as to whether the revenue losses resulting from the proposed rule could worsen volatility of the financial system.

The CFPB also uses faulty logic to bypass requirements of reviews and panels for rules that significantly affect small businesses. Although the CFPB estimates that there are more than 3,000 small banks and credit unions that issue credit cards, it absurdly states that this doesn't matter because data – which the CFPB admits is incomplete – shows that these cards are a "small share of revenue" for these institutions.[14] Even if this were the case, credit cards are part of a bundle of services these banks and credit unions offer their customers, who may go to larger financial institutions if these cards weren't offered. There is no serious argument that a rule making it difficult for small financial institutions to issue credit cards would not have a significant impact on small businesses.

The rule's excluding of costs conflicts with the law and potentially the Constitution

The proposed rule states explicitly that certain significant costs are not being considered in setting the new safe harbor. Specifically, the CFPB excludes in the proposed rule the cost of "charging off" delinquent accounts.[15] Data shows delinquent accounts often correlate with late payments, and late fees also discourage credit card delinquencies. Once again, responsible card holders who pay on time will likely end up paying more under this rule.

Also, this exclusion of costs conflicts with the CARD Act legislation and potentially the U.S. Constitution. As we stated previously, the CARD Act requires that the CFPB "shall consider the cost incurred by the creditor." It does not authorize the excluding of any relevant costs. Also, the term "reasonable" in statutes in the of context of rate-setting – unless specified otherwise – most commonly has the meaning total costs plus a minimal rate of return.[16]

In addition to potentially being deemed arbitrary and capricious by courts, the proposed rule may come into conflict both the Due Process and Takings Clauses of the 5th Amendment, as it may be found to deprive banks and credit unions that issue cards of their property rights to a return on capital invested. The Supreme Court case *Duquesne Light v. Barasch,*[17] affirmed 8-1 that a government-set "rate is too low if it is so unjust as to destroy the value of the property for all the purposes for which it was acquired."

Conclusion: withdraw the rule

American consumers face many headwinds today with high gas and food prices and inflation. The vast majority of these consumers who may struggle, yet succeed, in paying their credit card bills on time

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[13] Federal Register, p. 18931.
[14] Federal Register, pp. 18940-18941.
[15] Federal Register, p. 18914.
[16] Bonbright, James C., Danielson, Albert L. and Kamerschen, David R., *Principles of Public Utility Rates, 2nd Edition*, Public Utilities Reports, Inc. (1988), p. 109.
[17] 488 U.S. 289 (1989).

should not be punished by this rule that aims to subsidize those consumers who aren't as prudent. Because this rule conflicts with most Americans' values of freedom and responsibility – as well as potentially the underlying statutes and the U.S. Constitution – the CFPB should live up to its name and protect consumers by withdrawing this rule.

Thank you for this opportunity to present our views. If you have any questions, please feel free to contact John Berlau at John.Berlau@cei.org or (202) 331-1010.

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[i] Title listed for identification purposes only.