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Financial Institutions Voice Strong Opposition to CFPB's Credit Card Late Fee Proposal

Philip R. Stein & Enza G. Boderone

In February, the Consumer Financial Protection Bureau (CFPB) proposed amending the Federal Reserve Board's Regulation Z with respect to the amount of fees that credit card issuers are permitted to charge their customers for late payments. The CFPB announced that it is taking steps to "better ensure that the late fees charged on credit card accounts are 'reasonable and proportional' to the late payment as required under TILA." Currently, credit card companies can charge a customer for late fees up to $41 per missed payment, with generalized immunity from regulatory scrutiny for the fairness of the amount of the fees charged. The CFPB seeks to reduce the general "immunity" amount of late fees, per violation, from $41 to $8, remove annual inflation adjustments for safe harbor dollar amounts, and provide that late fee amounts cannot exceed 25% of the required payment.

Currently, under Regulation Z, a credit card issuer may not impose a late penalty fee unless it has determined that the amount of the fee is reasonable, and proportionate to the total costs incurred by the issuer in connection with the late payment, or the amount complies with the safe harbor amount. Credit card issuers may charge up to $30 for the first violation (i.e., missed payment) and $41 per month for subsequent violations without running afoul of the "reasonable and proportionate" fee requirement set forth in Regulation Z.

The proposed rule would allow credit card issuers to charge above the $8 safe harbor, only if they can prove that the higher fee is necessary to cover their incurred collection costs.

Citing to a March 22 report, the CFPB stated that late fees amount to $12 billion per year, $9 billion of which it claims are not associated with collection costs that companies incur for late payment violations. This measure would "reduce credit card late fees paid by Americans by $9 billion each year," according to the CFPB.

However, financial institutions, especially small banks and credit unions, have voiced strong opposition to the proposed rule, arguing that the rule would pose a significant threat to their operations and place them at a competitive disadvantage to larger institutions. Other industry participants argue that the rule will also negatively affect consumers because it would force credit card issuers to tighten credit standards or raise interest rates, resulting in a decrease in the availability of credit, and/or a reduction in availability of better rates, to those applying for credit cards. They note that financial institutions may be forced to recoup lost revenue through higher interest rates and other means.

In addition, the proposed rule does not appear to consider that late fees may not be confined to collection of credit card debt. They may instead be tied to other products and services offered by the institution. Smaller institutions use late fees to mitigate other costs, including fraud losses, an issue not addressed in the proposed rule. Collection of late fee payments also permits these institutions to offer lower rates and be competitive against their larger counterparts.

Some have called for the proposed rule to be amended to exempt smaller institutions in order to allow them to maintain their ability to cover the costs of offering credit card services and remain competitive in the marketplace. Others note that the CFPB has failed to convene a small business review panel, in conformity with the Small Business Regulatory Enforcement Fairness Act (SBREFA), to offer guidance on this rule. Due in part to this failure, some critics contend that the CFPB has vastly underestimated the aforementioned harmful effects its proposal will have on small financial institutions, and on small business borrowers that will have higher costs of credit.

The proposed rule has also been criticized as "tone-deaf" in that it precludes annual inflation adjustments to the late fee safe harbor amount in the face of record inflation currently affecting the country.

The comment period for the proposed rule ended May 3. The CFPB indicates that the final rule, if adopted, would take effect 60 days after publication in the Federal Register.

Financial institutions must move quickly to consider anew how they assess credit card late fees and evaluate any changes to their internal guidelines, notices and disclosures, to take into account the new safe harbor amount. Credit card issuers may also want to consider conducting a reasonableness and proportionality analysis of their costs in order to get-ahead of the rule, if it is to be implemented in its current form.

Related People

Philip R. Stein
Partner, Litigation

Enza G. Boderone
Of Counsel, Litigation