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TESTIMONY OF

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of the

U.S. SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

HEARING ON *TAKING ACCOUNT OF FEES AND TACTICS IMPACTING AMERICANS' WALLETS*

JULY 26, 2023

[1] The views expressed in this testimony are my personal views and do not represent the views of Patomak Global Partners LLC or any other organization with which I am affiliated.

Chairman Warnock, Ranking Member Tillis, and members of the subcommittee, thank you for the opportunity to testify today about the fee practices of financial institutions and the appropriate federal regulatory response.

My name is Brian Johnson. I am Managing Director of Patomak Global Partners, a financial services regulatory consultancy, where I advise clients on matters relating to compliance with federal consumer financial laws. I previously served as the Deputy Director of the Consumer Financial Protection Bureau (CFPB or Bureau), where I provided strategic direction to the agency's rulemaking, supervision, and enforcement efforts. Prior to that, I served as the Chief Financial Institutions Counsel for the House Committee on Financial Services.

Today's hearing is timely. For over two years now, the American people have suffered from abnormally high inflation, which has worked as a hidden tax eating away at our savings and purchasing power. In February 2021, the Consumer Price Index stood at just 1.7 percent, but then spiked to 5.0 percent just three months later, on its way to a peak of 9.1 percent by June 2022, marking a historic 40-year high.[2] According to the Bureau of Labor Statistics, because of inflation, a dollar today can only buy 86 percent of what it could buy, on average, just over two years ago.[3] According to the Census Bureau, real median household income in 2021 was $70,784.[4] Thus, inflation has eroded about $9,909 of median household purchasing power in the last two years alone, placing an acute strain on many household budgets. Frustration with inflation likely contributes to the mood of the electorate, with public polling now finding that approximately 74 percent of registered voters feel that things in the nation are "on the wrong track."[5]

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[2] Bureau of Labor Statistics, *12-month percentage change, Consumer Price Index*, https://www.bls.gov/charts/consumer-price-index/consumer-price-index-by-category-line-chart.htm. This spike correlates with American Rescue Plan Act (Pub. L. No. 117-2), the $1.9 Trillion stimulus spending plan that became law in March 2021. The inflationary effect of this law was predicted. See, e.g., Larry Summers, Op-Ed, *The Biden Stimulus Is Admirably Ambitious. But It Brings Some Big Risks, Too,* THE WASHINGTON POST (Feb. 4, 2021), https://www.washingtonpost.com/opinions/2021/02/04/larry-summers-biden-covid-stimulus/.

[3] Bureau of Labor Statistics, *CPI Inflation Calculator*, https://www.bls.gov/data/inflation_calculator.htm. Stated another way, the purchasing power of the dollar has declined about 14 percent between February 2021 and June 2023.

[4] U.S. Census Bureau, *Median Household Income* (Sept. 13, 2022), https://www.census.gov/library/visualizations/2022/comm/median-household-income.html.

[5] NBC, *NBC News Survey* (June 16-20, 2023), https://s3.documentcloud.org/documents/23858265/230169-nbc-june-2023-poll_625-first-release.pdf.

Considering these recent events, it is not surprising that the Administration would seek to demonstrate that it is "taking inflation very seriously by enacting policies to bring down costs for people."[6] Accordingly, and as relevant to today's hearing, last year President Biden announced an initiative to combat so-called "junk fees," calling on federal agencies "to reduce or eliminate hidden fees, charges, and add-ons for everything from banking services to cable and internet bills to airline and concert tickets."[7] The campaign to combat these fees has become a significant part of the Administration's political rhetoric. The characteristic feature of the initiative thus far has been the application of political pressure to companies to secure commitments regarding changes to fee disclosure practices.[8] Fee disclosures are of course not fee reductions, but the argument seems to be that all-in pricing disclosures will encourage more comparison shopping, which will in turn encourage greater competition among providers, which will in turn reduce costs for consumers over time.

The CFPB, for its part, has been the most enthusiastic among federal financial regulators in heeding the President's call to action. The CFPB Director has joined the President at the White House and delivered remarks for a press conference about Administration's efforts,[9] and the President prominently featured a CFPB initiative in his most recent State of the Union address to the nation.[10] The CFPB has also taken several recent regulatory actions regarding many of the fees under consideration today. While the President's agenda is more far reaching

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[6] The White House, *Remarks by President Biden at the Third Meeting of the White House Competition Council* (Sept. 26, 2022), https://www.whitehouse.gov/briefing-room/speeches-remarks/2022/09/26/remarks-by-president-biden-at-the-third-meeting-of-the-white-house-competition-council/.

[7] Brian Deese, Neale Mahoney, Tim Wu, *The President's Initiative on Junk Fees and Related Pricing Practices* (Oct. 26, 2022), https://www.whitehouse.gov/briefing-room/blog/2022/10/26/the-presidents-initiative-on-junk-fees-and-related-pricing-practices/. According to reporting about this initiative, the White House is convinced it is "good politics," particularly as the President "tries to improve his standing with the public on the economy as the U.S. rebounds from 40-year high inflation." See Joey Garrison, *Biden muscles Ticketmaster, SeatGeek to scrap hidden ticket fees after Taylor Swift debacle* USA TODAY (June 15, 2023), https://www.usatoday.com/story/news/politics/2023/06/15/live-nation-seatgeek-scrap-hidden-fees-amid-pressure-from-biden/70319147007/.

[8] See, e.g., Emma Kinery, *Ticketmaster parent Live Nation, others agree to show 'junk fees' after Biden pressure*, CNBC (June 15, 2023), https://www.cnbc.com/2023/06/15/biden-pushes-ticketmaster-seatgeek-to-show-junk-fees-upfront.html.

[9] Emma Kinery, *White House hammers economic issues with attack on 'junk fees' two weeks out from Election Day* CNBC (Oct. 26, 2022), https://www.cnbc.com/2022/10/26/white-house-hammers-economic-issues-with-attack-on-junk-fees-two-weeks-out-from-election-day.html.

[10] President Biden, *State of the Union Address* (Feb. 7, 2023), https://www.whitehouse.gov/state-of-the-union-2023/.

than the CFPB and fees among financial service providers, I will focus my remarks on the CFPB's activity based on my first-hand experience at the Bureau and in the field.

When I testified before a House Financial Services Subcommittee in March, I argued that the primary metric by which the CFPB's actions should be judged is the extent to which the CFPB has adhered to the rule of law.[11] By this measure, the CFPB's recent actions are deeply concerning.

But before examining each of the CFPB's actions in turn, I will make a few general observations regarding financial institution fee practices. First, I think we can agree that all consumers generally desire the highest quality products and services for the least possible amount of money. Financial institutions, like all companies, engage in various pricing strategies to try to discover consumer preferences and best satisfy consumer demand. Sometimes the price is presented as an all-inclusive, up-front cost; sometimes the price is partitioned. These pricing strategies evolve over time to meet changing consumer preferences, and different firms competing within the same industry may adopt different pricing strategies.

I would assert that fees or other costs to a consumer that are not optional and are material to a consumer's decision to obtain a financial product or service should be disclosed up-front, and consumers should not be charged for products or services they did not agree to purchase. However, that is not to say that an all-inclusive pricing structure is necessarily preferable to a partitioned pricing structure.[12] When evaluating policy relating to firm fee or pricing strategies, it is useful to remember the iron law of economics that there is no such thing as a free lunch. In our highly complex and dynamic financial services markets, any isolated effort to reduce or eliminate a particular fee will typically benefit one group of consumers and burden other less-favored groups.[13] Relatedly, any claim that a fee price control will result in consumer savings should be scrutinized because its true economic effect is usually a mixed result involving cross-

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[11] Brian Johnson, *Testimony before the Subcommittee on Financial Institutions and Monetary Policy of the House Committee on Financial Services* (March 9, 2023), https://docs.house.gov/meetings/BA/BA20/20230309/115384/HHRG-118-BA20-Wstate-JohnsonB-20230309.pdf

[12] Sometimes government regulation even effectively prohibits all-in pricing, such as with the various fees that must be separately disclosed and assessed during the home-buying process.

[13] For example, the Durbin amendment's price ceiling on debit interchange fees adversely affected millions of households, particularly lower-income households. *See* Todd J. Zywicki, Geoffrey A. Manne, and Julian Morris *Unreasonable and Disproportionate: How the Durbin Amendment Harms Poorer Americans and Small Businesses* *https://laweconcenter.org/images/articles/icle-durbin_update_2017_final.pdf*

subsidies that transfer wealth between different groups of consumers.[14] Whenever government policymakers intervene in the market to fix prices, they predictably tout the expected cost savings to intended beneficiaries but often omit reference to other consumers who are made worse off by the decision, whether through lower investment returns or through higher prices for, lower quality of, or diminished access to financial products and services. These consumers must be accounted for in honest consideration of the costs and benefits of a regulatory action.

Second, the most important goal for public policy in a market economy must be ensuring that consumers are free to choose the products and services that best serve their individual needs. Consumers must have adequate information to make informed decisions, and Congress has enacted laws to reduce information search costs for consumers, promoting consumer choice and reinforcing the market economy.[15] Congress has also played a critical role in enacting market-reinforcing laws to support private property rights and to combat fraud, deception, anti-competitive behavior, and discriminatory conduct, all of which undermine consumer choice.[16] Correlatively the government should refrain from engaging in market-replacing price-fixing or product design, which takes away choice from consumers. The failure of planned economies in the 20th Century and associated human misery demonstrates the superiority of the price mechanism in allocating capital efficiently to satisfy consumer demand, and that misguided government price controls generally make consumers worse off.[17]

There has been a troubling trend in recent years of Congress empowering executive agencies to engage in these practices, such as by establishing price-fixing schemes for debit card interchange fees or credit card late fees or by imposing "plain vanilla" mortgage product requirements under the Ability-to-Repay/Qualified Mortgage rule. Accordingly, to preserve consumer choice and the market economy, Congress should scrutinize executive agency regulatory proposals seeking to intervene in the free operation of markets. This scrutiny is

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[14] See Daniel Heil, *What Goes Wrong When Government Interferes with Prices*, The Hoover Institution (Jan. 12, 2021), https://www.hoover.org/research/what-goes-wrong-when-government-interferes-prices.

[15] See Brian Johnson, *Toward a 21st century approach to consumer protection: Remarks to Consumer Action* (Nov. 15, 2018), https://www.consumerfinance.gov/about-us/newsroom/toward-21st-century-approach-consumer-protection/.

[16] Id.

[17] Id.

especially critical where the specific focus of the effort is ambiguously defined, as is the case with the President's "junk fee" initiative.

Indeed, the term "junk fee" is not defined in statute or in regulation. In fact, to date, President Biden has offered at least four different meanings of the phrase.[18] His former White House National Economic Council Director, Brian Deese, provided still another,[19] while the Federal Trade Commission led by Chair Khan has supplied at least three more,[20] and the CFPB led by Director Chopra has supplied another two.[21] None of these ten proffered definitions are fully consistent, and each is subjective. The term thus functions primarily as a pejorative label to be attached to any lawful fee the Administration now disfavors. The lack of a precise and fixed definition of a "junk fee" has sown confusion among market participants, which needlessly complicates the task of regulatory compliance.

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[18] See *Competition Council Remarks*, supra note 6 ("unnecessary hidden fees"); The White House, *FACT SHEET: President Biden Highlights New Progress on His Competition Agenda* (Feb. 1, 2023), https://www.whitehouse.gov/briefing-room/statements-releases/2023/02/01/fact-sheet-president-biden-highlights-new-progress-on-his-competition-agenda/ ("unfair hidden fees"); *State of the Union Address*, supra note 10 ("those hidden surcharges too many companies use to make you pay more"); The White House, *Remarks by President Biden on Protecting Consumers from Hidden Junk Fees* (June 15, 2023), https://www.whitehouse.gov/briefing-room/speeches-remarks/2023/06/15/remarks-by-president-biden-on-protecting-consumers-from-hidden-junk-fees/ ("hidden charges these companies sneak into your bill to make you pay more and without you really knowing it initially").

[19] *The President's Initiative*, supra note 7, ("fees designed either to confuse or deceive consumers or to take advantage of lock-in or other forms of situational market power").

[20] Chair Lina Khan, *Statement Regarding the Advanced Notice of Proposed Rulemaking on Unfair or Deceptive "Junk" Fees* (Oct 20, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/R207011ChairJunkFeesStatement.pdf ("extra charges associated with unnecessary or worthless services"); FTC Press Release, *Federal Trade Commission Explores Rule Cracking Down on Junk Fees* (Oct. 20, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/10/federal-trade-commission-explores-rule-cracking-down-junk-fees ("unnecessary, unavoidable, or surprise charges that inflate costs while adding little to no value"); FTC Advance Notice of Proposed Rulemaking: Unfair or Deceptive Fees Trade Regulation Rule (Nov. 8, 2022), 87 Fed. Reg. 67413, https://www.govinfo.gov/content/pkg/FR-2022-11-08/pdf/2022-24326.pdf ("fees for goods or services that are deceptive or unfair … whether or not the fees are described as corresponding to goods or services that have independent value to the consumer").

[21] CFPB, *Request for Information Regarding Fees Imposed by Providers of Consumer Financial Products or Services* (Feb. 2, 2022), 87 Fed. Reg. 5801, 5802 https://www.govinfo.gov/content/pkg/FR-2022-02-02/pdf/2022-02071.pdf ("exploitative, back-end, hidden, or excessive fees"); CFPB, Deputy Director Martinez's Prepared Remarks at the Consumer Law Scholars Conference (Mar. 3, 2023), https://www.consumerfinance.gov/about-us/newsroom/deputy-director-martinezs-prepared-remarks-at-the-consumer-law-scholars-conference/ ("any unnecessary, unavoidable, or surprise charge that inflates a product or service's price, while adding little value to no value").

But the indeterminate and subjective nature of the definition has not prevented the CFPB from taking significant action on "junk fees."

Overdraft and Returned Deposited Item Fees

CFPB Blog Posts

On February 1, 2023, the White House released a fact sheet highlighting the President's "new progress on his competition agenda."[22] This fact sheet contained an extraordinary statement. Regarding the CFPB's efforts to support the Biden agenda, the White House reported: "The CFPB targeted overdraft and bounced check fees …, driving 15 of the 20 largest banks to agree to put an end to bounced check fees." What the White House took credit for can best be described as an *ultra vires* campaign to coerce institutions into abandoning lawful practices; at worst it is an example of the Bureau using the implied threat of regulation and enforcement to do the same. And unfortunately, the White House's description of the CFPB's activities is accurate.

Beginning in December 2021, the CFPB began to publish a series of blog posts purporting to compare the overdraft and non-sufficient fund (NSF) practices of the nation's largest banks. But the true purpose of the posts was quite clear: to apply political pressure to named institutions until they changed their practices.[23] The CFPB was not particularly coy about what it was doing, either. For instance, in a February 10, 2022 post, CFPB staff stated that "[a]s the CFPB has been focusing on this issue again, there has been a notable trend of banks announcing changes to their overdraft programs" to include "eliminating NSF fees" and "reducing the size of the overdraft fee."[24] CFPB staff stated that "these changes represent an

[22] The White House, *FACT SHEET: President Biden Highlights New Progress on His Competition Agenda* (Feb. 1, 2023), https://www.whitehouse.gov/briefing-room/statements-releases/2023/02/01/fact-sheet-president-biden-highlights-new-progress-on-his-competition-agenda/

[23] This public pressure was backed by non-public pressure applied by the CFPB in the confidential process of supervisory examination. See, e.g., CFPB, *Prepared Remarks of CFPB Director Rohit Chopra on the Overdraft Press Call* (Dec. 1, 2021), https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-cfpb-director-rohit-chopra-overdraft-press-call/ ("I've asked the CFPB's bank examiners to prioritize examinations of banks that are heavily reliant on overdraft. Financial institutions that have a higher share of frequent overdrafters or a higher average fee burden for overdrafting should expect us to be paying them close supervisory attention.").

[24] Rebecca Borné and Amy Zirkle, *Comparing overdraft fees and policies across banks* (Feb. 10, 2022), https://www.consumerfinance.gov/about-us/blog/comparing-overdraft-fees-and-policies-across-banks/

encouraging step by some banks in the right direction."[25] In another blog post dated April 13, 2022, CFPB staff stated that "[i]n recent months, a number of large banks have announced that they are eliminating [NSF] fees on their checking accounts. This is a positive development."[26] CFPB staff lamented, however, that "many banks are continuing to charge these fees," warning that the CFPB "is closely scrutinizing whether and when charging these fees may be unlawful" and committing to "work to ensure that banks continue to evolve their businesses to reduce the impacts of overdraft and NSF fees."[27]

Notably, none of the CFPB's posts assert that the services provided by the named institutions were unlawful. Rather, the posts measured the progress of the CFPB's initiative by estimating the overall reduction in fee revenue, notwithstanding that existing regulations permit institutions to provide "overdraft service[s],"[28] that consumers must affirmatively opt-in to receiving overdraft protection,[29] that overdraft services can serve as an source of liquidity for cash-strapped consumers, and that many institutions offer features such as grace periods to bring accounts positive, limits on the number of daily charges, and cover *de minimus* transactions without incurring fees. So considerations of consumer choice took a back seat to political imperative.[30] The inappropriate coercive tactics being employed by the CFPB should be universally condemned as a violation of due process and contrary to our democratic norms.

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[25] Id. This post explicitly tied the pressure campaign to the junk fees initiative, stating: "Our work on overdraft/NSF fees is part of a larger CFPB initiative to save Americans billions of dollars by promoting competition and reducing junk fees."

[26] Rebecca Borné and Ashwin Vasan, *Consumers on course to save $1 billion in NSF fees annually, but some banks continue to charge these fees* (Apr. 13, 2022), https://www.consumerfinance.gov/about-us/blog/consumers-on-course-to-save-one-billion-in-nsf-fees-annually-but-some-banks-continue-to-charge-them/.

[27] Id.

[28] See, e.g., Reg E (12 C.F.R. 1005.17) which implements the Electronic Fund Transfer Act and Reg DD (12 C.F.R 1030.11), which implements the Truth in Savings Act.

[29] 12 C.F.R. 1005.17(b).

[30] In fact, empirical research presented to the CFPB as part of its 2021 Research Conference finds that overdraft restrictions come at the cost of reducing banking services for low-income households. See, e.g., Jennifer L. Dlugosz, Brian T. Melzer, and Donald P. Morgan, *Who Pays the Price? Overdraft Fee Ceilings and the Unbanked*, working paper (Apr. 15, 2021), https://files.consumerfinance.gov/f/documents/cfpb_morgan_overdraft-fee-ceilings-and-the-unbanked.pdf.

CFPB Bulletin 2022-06

On October 26, 2022, the CFPB issued an enforcement bulletin on returned deposited item fee assessment practices.[31] Specifically, the bulletin sets forth the CFPB's legal analysis and conclusion that fees incurred when checks are deposited but do not clear are "likely unfair" under the Consumer Financial Protection Act.[32] In its discussion, the CFPB focuses on the fact that a customer depositing a check may not know that the check is "bad," so returned deposit item fees are not "well-tailored to recoup costs from the consumers actually responsible for the costs to depository institutions of expected losses."[33] What the CFPB fails to acknowledge is that in many circumstances, as a convenience to check-depositing customers, receiving banks will make funds available before the check actually "clears." This customer convenience shifts the clearance risk to the bank. Accordingly, the returned deposited item fee is intended to offset some of the bank's costs that occur when bad checks are deposited, and this offset supports the receiving bank's continued ability offer deposited funds more quickly to customers or free checking accounts without annual fees or account minimums. By curbing this offset, the CFPB's Bulletin will foreseeably jeopardize these customer benefits and the availability of lower cost accounts.

As a procedural matter, the CFPB claims that the Bulletin is a "general statement of policy under the Administrative Procedure Act [APA]."[34] But this statement mischaracterizes the substance of the Bulletin. For APA purposes, statements of policy are "statements issued by an agency to advise the public prospectively of the manner in which the agency proposes to exercise a discretionary power."[35] The Bulletin considers a practice (returned deposited item fees), applies the elements of an applicable law (the "unfairness" prong of UDAAP) to that practice, and concludes that blanket policies of engaging in the practice likely violates the law. By construing UDAAP to prohibit the imposition of certain returned deposited item fees, the

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[31] CFPB, *Bulletin 2022-06: Unfair Returned Deposited Item Fee Assessment Practices* (Oct. 26, 2022), https://files.consumerfinance.gov/f/documents/cfpb_returned-deposited-item-fee-assessment-practice_compliance-bulletin_2022-10.pdf (hereinafter, "Bulletin").

[32] Bulletin at 1.

[33] Bulletin at 5.

[34] Bulletin at 8.

[35] See, e.g., Attorney General's Manual on the Administrative Procedure Act 30 n.3 (1947); *Nat'l Min. Ass'n v. McCarthy*, 758 F.3d 243, 251 (D.C. Cir. 2014) ("An agency action that merely explains how the agency will enforce a statute or regulation ... is a general statement of policy.").

Bulletin functions not to describe how the CFPB will exercise its discretion in bringing enforcement actions, but rather to advise the public of its view of what the law means. The Bulletin is therefore best categorized as an "interpretive rule," which is defined for APA purposes as a "rule or statement issued by an agency to advise the public of the agency's construction of the statutes and rules which it administers."[36] Notably, the most consequential difference between these two forms of guidance under the APA is that true statements of policy are not subject to judicial review, while interpretive rules are.[37] By mislabeling its Bulletin as a statement of policy rather than an interpretive rule – but shrewdly appreciating that industry will view the statement as a change in law – the CFPB reduces the likelihood that its interpretation of law will be challenged on a pre-enforcement basis in federal court.

CFPB Circular 2022-06

On the same day the CFPB issued its Bulletin, it also issued another guidance document that it calls a "Circular" on "[u]nanticipated overdraft fee assessment practices."[38] The Circular focuses on instances in which a customer initiates and the bank authorizes a transaction when the customer's account balance is positive, but the transaction later settles when the account balance is negative, triggering an overdraft fee. This situation arises because of the order in which all pending debits from and credits to a customer's account are settled, which can create different available balances and ledger balances for the account. In its Circular, the CFPB asserts that such overdraft fees are not reasonably anticipated by the account holder, even if they are fully disclosed in the account agreement, and are therefore "likely unfair," even if permissible under TILA and Reg Z and EFTA and Reg E.[39]

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[36] Attorney General's Manual on the Administrative Procedure Act 26 n.3 (1947).

[37] *Nat'l Min. Ass'n*, supra note 30, at 251 ("The APA divides agency action, as relevant here, into three boxes: legislative rules, interpretive rules, and general statements of policy. A lot can turn on which box an agency action falls into. In terms of reviewability, legislative rules and sometimes even interpretive rules may be subject to pre-enforcement judicial review, but general statements of policy are not.") See, e.g., *Whitman v. American Trucking Associations*, 531 U.S. 457, 477-49 (2001) (reviewable interpretive rule); *National Park Hospitality Association v. Department of the Interior*, 538 U.S. 803, 809-11 (2003) (non-reviewable policy statement).

[38] CFPB, *Consumer Financial Protection Circular 2022-06: Unanticipated overdraft fee assessment practices* (Oct. 26, 2022), https://files.consumerfinance.gov/f/documents/cfpb_unanticipated-overdraft-fee-assessment-practices_circular_2022-10.pdf (hereinafter, "Circular").

[39] Circular at 1.

Like the Bulletin, the CFPB has labeled its Circular a general statement of policy.[40] And like the Bulletin, the Circular presents a legal question, provides legal analysis, and supplies a legal conclusion, construing UDAAP to likely apply to "unanticipated" overdraft fees, including so-called "authorize-positive, settle-negative" overdrafts.[41] Accordingly, the Circular (and indeed all Circulars issued by the CFPB to date) should at a minimum be recategorized as an interpretive rule under the APA. However, unlike the Bulletin, which technically governs only the CFPB's own enforcement efforts, the CFPB specifically issues its Circulars "to the broad set of government agencies responsible for enforcing federal consumer financial law" in order "to promote consistency among enforcers."[42] The Circular is therefore designed to limit the discretion of these various enforcers to conclude that fully disclosed overdraft fees are not unanticipated or unfair, which means that it intends for its Circular to speak with the force of law. Thus, in substance the CFPB's Circular likely meets the definition of a legislative rule under the APA and was issued without following required notice-and-comment procedures.[43]

Convenience Fees

On June 29, 2022, the CFPB issued a guidance document called an "advisory opinion" that interprets the language in Section 808(1) of the Fair Debt Collection Practices Act (FDCPA).[44] At issue is whether the FDCPA permits debt collectors to collect convenience fees from borrowers. In relevant part, the FDCPA prohibits a "debt collector" from collecting "any amount…unless such amount is expressly authorized by the agreement creating the debt or permitted by law."[45] Convenience fees that are not prohibited by law and are agreed to by a borrower in a contract recognized as valid under state law would seem to fit the definition of

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[40] Circular at 13

[41] Circular at 1.

[42] See CFPB, *Consumer Financial Protection Circular 2022-01: System of Consumer Financial Protection Circulars to agencies enforcing federal consumer financial law* (May 16, 2022), https://www.consumerfinance.gov/compliance/circulars/circular-2022-01-system-of-consumer-financial-protection-circulars-to-agencies-enforcing-federal-consumer-financial-law/.

[43] *Nat'l Min. Ass'n*, supra note 30 at 251-52 ("An agency action that purports to impose legally binding obligations or prohibitions on regulated parties ... is a legislative rule.").

[44] CFPB, *Debt Collection Practices (Regulation F); Pay-to-Pay Fees (June 29, 2022)*, https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_convenience-fees_advisory-opinion_2022-06.pdf (hereinafter, Advisory Opinion). An advisory opinion is a type of interpretive rule for APA purposes. See CFPB, *Final Advisory Opinions Policy*, https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_advisory-opinion_policy_2020-11.pdf.

[45] 15 U.S.C. 1692f(1).

"permitted by law." However, in its advisory opinion, the CFPB interpreted the phrase "permitted by law" in the FDCPA to mean "*expressly* permitted by law,"[46] meaning that such fee is prohibited unless state law specifically authorizes the convenience fee. The CFPB simply read an additional word into the statute.[47] Congress used the word "expressly" in the very same sentence to modify the phrase "authorized by the agreement creating the debt;" it did not use this word to modify the phrase "permitted by law." The CFPB's interpretation is a naked act of legislation.

Additionally, the CFPB went through an extensive rulemaking process to write Reg F, the FDCPA's first implementing regulation. In its Small Business Regulatory Enforcement Fairness Act (SBREFA) outline of proposals for the regulation, the CFPB stated it was "considering clarifying that incidental fees, including payment method convenience fees, that are collected either directly or indirectly by the collector are permissible only if…state law expressly permits them."[48] However, the CFPB's final regulation issued in 2020 declined to adopt this interpretation, and so the resulting language of Reg F closely tracks the statute.[49] Accordingly, by reading the word "expressly" into the FDCPA, the CFPB's interpretive rule also effectively amends Reg F without going through the necessary APA notice-and-comment rulemaking process.

Even worse than these interpretive and procedural errors, the CFPB's advisory opinion will hurt consumers. It is helpful to understand the context in which the CFPB issued the opinion, which was to bolster an amicus brief it had filed with the 9th Circuit Court of Appeals in support of a class action.[50] The underlying case involved a challenge to the validity of a $5 convenience fee charged by a mortgage servicer to enable a borrower to avoid late payments by

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[46] Advisory Opinion at 6.

[47] The CFPB's interpretation essentially inverts the legal maxim that "everything which is not forbidden is allowed," to mean "everything which is not allowed is forbidden."

[48] CFPB, *Small Business Review Panel for Debt Collection and Debt Buyer Rulemaking: Outline of Proposals Under Consideration and Alternatives Considered* (July 28, 2016), at Appendix H, pg. 2, https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/20160727_cfpb_Outline_of_proposals.pdf

[49] See 12 C.F.R 1006.22(b).

[50] Brief for CFPB as Amici Curaie Supporting Plaintiffs-Appellants, *Thomas-Lawson et al. v. Carrington Mortgage Services, LLC*, Case No, 21-55459 (9th Cir. 2021), https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_thomas-lawson-v-carrington-mortgage-services-llc_amicus-brief_2021-10.pdf.

submitting payments online or by telephone rather than sending a check in the mail.[51] To be clear, there was no legal obligation for the servicer to provide these additional payment options to borrowers. Moreover, the servicer fully disclosed the fee to the borrowers, the borrowers affirmatively consented to the fee, and borrowers could always avoid the fee by sending their checks by mail early enough to ensure they are received by the due date.[52] The expedited payment options, however, helped borrowers who realized that they forgot to send in their check, especially since there was a late fee equal to 4 percent of the monthly mortgage payment (which would have been $58.49 for the lead plaintiff), not to mention adverse credit reporting.[53]

The CFPB's amicus brief took the position that the convenience fee was impermissible under the FDCPA because the underlying loan agreement between the borrower and the mortgage originator did not expressly authorize online or telephone payments, and state law, while not prohibiting the convenience fee, did not *expressly* authorize the fee either.[54] While the case ultimately settled, let's understand the consequences of the CFPB's new legal position for mortgage borrowers and other consumers. By prohibiting convenience fees in most circumstances, servicers and debt collectors will be less likely to voluntarily assume the costs of maintaining staff and systems to provide expedited payment options, and borrowers will therefore be more likely to make late payments outside of the grace period, to pay higher late fees, and harm their credit.

Additionally, because mortgage originators (much less mortgage servicers) have limited ability to make changes to uniform loan agreements with borrowers and because most mortgages have a term of 30 years, prohibiting a mortgage servicer from contracting separately with a borrower to accept new and more convenient forms of payment effectively locks a borrower into making payments using technologies only in existence at the time of origination (unless and until state laws are amended to specifically permit each and every new technology). Today's first-time homebuyers could conceivably be making payments until 2053. Should they be locked into using only today's existing payment technologies to pay their mortgage until then? The CFPB's answer is "yes."

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[51] *Thomas-Lawson v. Carrington Mortg. Servs., LLC*, 2021 WL 1253578, at *1–2 (C.D. Cal. Apr. 5, 2021).
[52] Id. At *3.
[53] Id.
[54] CFPB Amicus Brief, supra note 43, at pp. 12-23.

<u>Credit Card Late Fees</u>

On February 1, 2023, the CPFB issued a notice of proposed rulemaking (NPRM) regarding credit card late fees.[55] Specifically, this proposed rule would (if finalized) amend Section 1026.52(b) of Reg Z, which implements Section 149 of the Truth in Lending Act, which was amended in 2009 by the Credit Card Accountability Responsibility and Disclosure Act of 2009 (CARD Act) to require that the amount of any penalty fee imposed by a card issuer for violating the cardholder agreement, including any late payment fee or any other penalty fee or charge, must be "reasonable and proportional" to the violation.[56] The CARD Act originally assigned the Board of Governors of the Federal Reserve System (FRB) responsibility for implementing this price-fixing provision, and in 2010 the FRB promulgated a rule that established a $25 (and $35 for subsequent violations) threshold for credit card late fees (adjusted annually for inflation), where fees assessed for late payments in amounts at or below the threshold are presumed to be "reasonable and proportional."[57] The Dodd-Frank Act subsequently transferred TILA rulemaking authority to the CFPB.[58] The CFPB's NPRM would lower the current credit card late fee safe harbor threshold from the current inflation-adjusted level of $30 (and $41 for subsequent late payments) to $8, eliminate annual inflation adjustments to this dollar amount, and cap late fee amounts at 25 percent of the required minimum payment.[59]

The CFPB's rulemaking suffers from several significant flaws, as explained below.

Predetermined Outcome

One significant flaw in the CFPB's rulemaking is that the rushed timeline established for the rulemaking process as well as public statements made to date strongly support the conclusion that the CFPB has already predetermined the outcome of the rulemaking, which contravenes the requirements of the APA.[60]

[55] CFPB, *Notice of Proposed Rulemaking: Credit Card Penalty Fees (Regulation Z)*, 88 Fed. Reg. 18906 (Mar. 29, 2023), https://www.govinfo.gov/content/pkg/FR-2023-03-29/pdf/2023-02393.pdf.
[56] Id.
[57] Board of Governors of the Federal Reserve System, *Final Rule: Truth in Lending*, 75 Fed. Reg. 37526 (June 29, 2010), https://www.govinfo.gov/content/pkg/FR-2010-06-29/pdf/2010-14717.pdf.
[58] Pub. L. No. 111-203 (2010).
[59] CFPB NPRM, supra note 49.
[60] After publishing a required notice of proposed rulemaking, an agency must "give interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments." 5 U.S.C.

Regarding the rushed process being employed, it is worth noting that the CFPB submits its regulatory agenda to the White House Office of Management and Budget (OMB) twice annually for inclusion in the unified regulatory agenda released to the public. In the preamble of its Spring 2022 submission to OMB dated April 1, 2022, the CFPB indicated that the five regulatory actions listed in its submission (none of which related to credit card late fees) were the only actions that it "reasonably anticipates having … under consideration during the period from June 1, 2022 to May 31, 2023."[61] It therefore came as a complete surprise when on June 22, 2022, the very day after OMB published the unified agenda,[62] the CFPB issued an Advance Notice of Proposed Rulemaking (ANPR) seeking comment on credit card late fees.[63]

Additionally, the deadline established by the CFPB for submitting public comments in response to the ANPR was unreasonably short. The CFPB typically selects comment submission deadlines of 60 to 90 days after the ANPR is published in the *Federal Register* to allow adequate time for the public to comment.[64] For the credit card late fee ANPR, however, the CFPB imposed a comment deadline only 30 days after its initial announcement (July 22, 2022). On June 24, 2022, just two days after the CFPB issued its ANPR, several trade associations representing card issuers wrote to the CFPB requesting a 60-day extension to the comment

553(c). The opportunity for comment must be a meaningful opportunity. See *Gerber v. Norton*, 294 F.3d 173, 179 (D.C. Cir. 2002). And to satisfy this requirement, an agency must also remain sufficiently open-minded. See, e.g., *Fed. Express Corp. v. Mineta*, 373 F.3d 112, 120 (D.C. Cir. 2004); *McLouth Steel Prods. Corp. v. Thomas*, 838 F.2d 1317, 1323 (D.C. Cir. 1988).

[61] CFPB, *Preamble to Semiannual Regulatory Agenda*, https://www.reginfo.gov/public/jsp/eAgenda/StaticContent/202204/Preamble_3170_CFPB.pdf

[62] The White House, *The Spring Regulatory Agenda* (June 21, 2022), https://www.whitehouse.gov/omb/briefing-room/2022/06/21/the-spring-regulatory-agenda/

[63] CFPB, *Advance Notice of Proposed Rulemaking: Credit Card Late Fees and Payments* (June 22, 2022), https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_credit-card-late-fees_anpr_2022-06.pdf.

[64] See CFPB, *Advance Notice of Proposed Rulemaking Relating to Home Mortgage Disclosure (Regulation C) Data Points and Coverage* (May 8, 2019), https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_anpr_hmda-comment-period-extension.pdf (Provided a 60-day comment period, extended 99 days); CFPB, *Advance Notice of Proposed Rulemaking: Debt Collection (Regulation F)* (Nov. 12, 2013), https://www.federalregister.gov/documents/2014/01/14/2014-00453/debt-collection-regulation-f (Provided a 90-day comment period, extended 18 days); CFPB, *Advance Notice of Proposed Rulemaking: Property Assessed Clean Energy Financing* (Mar. 4, 2019), https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_anpr_residential-property-assessed-clean-energy-financing.pdf (Provided a 60-day comment period); CFPB, *Advanced Notice of Proposed Rulemaking: Dodd-Frank Act Section 1033 – Consumer Access to Financial Records* (Oct. 22, 2020), https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_section-1033-dodd-frank_advance-notice-proposed-rulemaking_2020-10.pdf (Provided a 90-day comment period).

period, citing the surprise nature of the CFPB's announcement and the additional time needed to gather, validate, and analyze the large and complex volume of information being requested.[65] The CFPB did not publicly respond to the request until July 18, a mere four days before the comment submission deadline, when it extended the deadline by only ten days, to August 1.[66] There was no legitimate reason for the CFPB to arbitrarily limit its ANPR comment period to just 40 days. Doing so seemed calculated to ensure that the public did not have sufficient time to submit information to inform the rulemaking process.

The CFPB also conducted an inadequate regulatory flexibility analysis in its NPRM. The Regulatory Flexibility Act,[67] as amended by the SBREFA,[68] requires the CFPB to convene a small business review panel to consider its proposal unless the Director certifies that the proposal, if adopted, would not "have a significant economic impact on a substantial number of small entities."[69] Convening such a panel obviously lengthens the rulemaking process. In its NPRM, the CFPB stated that "the proposed rule would affect small entities that issue credit cards most directly by reducing late fee revenue from credit cards."[70] Accordingly, it stated that "[t]o assess whether the proposed rule would have a significant economic effect on small entities, the Bureau considers the significance of credit card late fee revenue as a share of the total revenue of affected small entities."[71] However, the CFPB then admitted that it "does not have data with which to precisely estimate the effect of the proposed rule on late fee revenue."[72] Despite this admission, the Director still provided the certification, meaning that the CFPB would not convene a small business review panel to provide feedback on its rulemaking. The CFPB even seemed to invert the burden of proof needed for certification by blaming its lack of data on ANPR commenters, stating "these commenters did not provide specific data that leads the Bureau to doubt the conclusions from the analysis."[73] The Bureau thus used its decision to

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[65] See *Letter of Associations to Director Chopra* (June 24, 2022), https://www.nafcu.org/system/files/files/Request%20for%20Extension%20of%20CFPB%20Late%20Fees%20ANPR.pdf
[66] 87 Fed. Reg. 42662 (July 18, 2022), https://www.govinfo.gov/content/pkg/FR-2022-07-18/pdf/2022-15245.pdf
[67] 5 U.S.C. 601 et seq.
[68] Pub. L. 104-121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C. 601 et seq.
[69] 5 U.S.C. 609(b).
[70] 88 Fed. Reg. 18940.
[71] Id.
[72] Id.
[73] Id. At 18941.

deprive commenters of a reasonable period to respond to its ANPR to further justify its decision not to convene a small business review panel. Notably, the Small Business Administration's Office of Advocacy filed a comment letter with the CFPB asserting that "the information provided [in support of the Director's certification] is insufficient" and concluding the CFPB "does not have the necessary data to develop an adequate factual basis for its certification."[74]

A review of public statements made regarding the CFPB's rulemaking provides further evidence that its outcome is predetermined. For instance, on February 7, 2023, President Biden delivered his State of the Union Address before both houses of Congress.[75] In his Address, the President referred to the CFPB's NPRM, emphatically stating: "We're cutting credit card late fees by 75 percent, from $30 to $8."[76] The President has since been similarly emphatic on social media, for instance stating that "We're cutting credit card late fees by 75%."[77] Because Director Chopra serves at the President's pleasure,[78] the Director now has no discretion to finalize the rule other than substantially as proposed without breaking the President's promises. Accordingly, his ability to consider the public comments submitted in response to the NPRM with an open mind has been fundamentally compromised.

Finally, further evidence that the CFPB's rulemaking is predetermined can be found in the CFPB's inexplicable failure to follow its own regulation. Reg Z, which implements TILA as well as the CARD Act, requires that the CFPB annually adjust the credit card penalty fees safe harbors to reflect changes in the Consumer Price Index.[79] Although the CFPB dutifully published rules in years past to make this adjustment along with other HOEPA and ATR/QM threshold adjustments, the rule that the CPFB released to adjust the amounts in effect for 2023

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[74] U.S. Small Business Administration Office of Advocacy, *Comment Letter re Credit Card Penalty Fees (Regulation Z), Docket No. CFPB–2023–0010, RIN 3170–AB15*, pp. 3-4 (May 3, 2023), https://advocacy.sba.gov/wp-content/uploads/2023/05/Comment-Letter-CFPB-Credit-Card-Penalty-Fees-508c.pdf.

[75] *State of the Union Address*, supra note 10.

[76] Id. It is unlikely that the President's statement was made off-the-cuff or in error; being part of a major Presidential address, White House speechwriters and policy staff likely chose the words carefully and vetted them with relevant agencies for accuracy. It is therefore likely that the CFPB received an advance draft of the Address for review and comment. It is also possible that the CFPB supplied the language itself to the White House. Reviewing communications between the CFPB and the White House about the language in the Address could provide further evidence of the state of mind of decision-makers regarding the rulemaking.

[77] President Joe Biden (@POTUS), Twitter (Mar. 1, 2023, 5:15 PM), https://twitter.com/POTUS/status/1631055470831054852?lang=en.

[78] See *Seila Law LLC v. CFPB*, 140 S. Ct. 2183 (2020).

[79] 12 C.F.R. 1026.52(b)(1)(ii).

conspicuously omitted the adjustment for the credit card penalty fees safe harbor.[80] Because the CFPB had already released its credit card late fees ANPR and would soon release its NPRM, which proposed to eliminate annual inflation adjustments, one possible explanation for the CFPB's failure to make the required annual adjustment is that it had already determined such adjustments would not be required in the future and were acting as though the proposed rule had already been finalized.

Unrepresentative Data

Another significant flaw in the CFPB's rulemaking is that the data it used to generate the cost estimates supporting its proposed $8 safe harbor dollar amount is not representative and excludes small issuers. The CFPB used a Y-14 (and Y-14+) data set from the Federal Reserve Board of Governors for its analysis.[81] However, this data set only covers bank holding companies with total consolidated assets exceeding $50 billion, which accounts for less than 70 percent of the outstanding balances of U.S. consumer credit cards as of the end of 2020.[82] The Bureau itself admitted in its 2021 CARD Act report that "the Y-14 data cover a large but not representative portion of the credit card market … the remaining uncovered portion is still substantial, and the Y-14+ data should similarly not be considered representative of that uncovered portion."[83] Because the CFPB's data was not representative, the Bureau could not ascertain whether the costs or other characteristics of smaller issuers were meaningfully different from the larger issuers in the data set. Rather than take the time to obtain the necessary data and to carefully study this vital segment of the market, the CFPB's NPRM simply admitted that "the data and research are not sufficient to fully quantify the potential effects of the proposal for consumers and issuers."[84]

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[80] See CFPB, *Final Rule: Truth in Lending (Regulation Z) Annual Threshold Adjustments (Credit Cards, HOEPA, and Qualified Mortgages)* (Dec. 23, 2022), https://www.govinfo.gov/content/pkg/FR-2022-12-23/pdf/2022-28023.pdf.
[81] 88 Fed. Reg. 18901.
[82] Id.
[83] CFPB, *The Consumer Credit Card Market*, pg. 17, fn. 29 (Sept. 2021), https://files.consumerfinance.gov/f/documents/cfpb_consumer-credit-card-market-report_2021.pdf.
[84] 88 Fed. Reg. 18931-32

Improper Exclusion of Costs

Another significant flaw in the CFPB's rulemaking is its improper exclusion of costs in its analysis. Section 149(b) of TILA requires the CFPB to issues rules to "establish standards for assessing whether the amount of any penalty fee or charge … is reasonable and proportional to the omission or violation to which the fee or charge relates."[85] TILA further specifies four factors the CFPB must consider in setting the standards, one of which is "the cost incurred by the creditor from such omission or violation."[86] Accordingly, the costs incurred by a card issuer as a result of late payments may include the costs associated with the *collection* of late payments, but such collection costs are not the *exclusive* costs that may be considered in determining a reasonable and proportional late fee. However, the CFPB's NPRM impermissibly limits consideration to collection costs, and then further limits permissible costs only to pre-charge-off collection costs, reasoning that "any cost in collecting amounts owed to a card issuer that are incurred post-charge-off is related to mitigating a loss as opposed to the cost of a violation of the account terms."[87] But this interpretation defies common sense; the costs incurred for collecting against a charged-off account necessarily relate to the customer's missed payments. Congress provided the CFPB no authority in TILA to limit consideration of costs in this manner, and the CFPB's impermissible exclusion of costs in its analysis enabled it to propose a lower safe harbor dollar threshold (of $8) than would otherwise be supported by the data when all costs are appropriately considered.

Admission of Consumer Harm

Perhaps the most concerning flaw in the CFPB's rulemaking is the CFPB's admission that the proposed rule, if finalized, will harm most credit-card holding consumers. As part of the 1022 analysis within the NPRM, the CFPB states:

> "Any offsetting changes, like the decrease in late fees, would affect different consumers differently depending, for example, on how often they pay late and whether they carry a balance. Cardholders who never pay late will not benefit from the reduction in late fees and could pay more for their account if

[85] 15 U.S.C. 1665d(b).
[86] 15 U.S.C. 1665d(c).
[87] 88 Fed. Reg. 18913

> maintenance fees in their market segment rise in response—or if interest rates increase in response and these on-time cardholders also carry a balance. Frequent late payers are likely to benefit monetarily from reduced late fees, even if higher interest rates or maintenance fees offset some of the benefits. Cardholders who do not regularly carry a balance but occasionally miss a payment would benefit from the proposed changes so long as any increase in the cost of finance charges (including the result of late payments that eliminate their grace period) is smaller than the drop in fees. Cardholders who carry a balance but rarely miss a payment are less likely to benefit on net."[88]

According to the CFPB's own "Credit Card Late Fees" report issued March 2022, approximately 74 percent of credit card accounts incurred no late fees in 2019.[89] The NPRM does not define "frequent late payers," but if defined as accounts that incurred three or more late fees in 2019, these frequent late payers comprised only 10.43 percent of credit card accounts in 2019.[90] Using card accounts as a proxy for cardholders, these figures provide a rough estimate of how the CFPB expects that different groups of consumers will be affected by its rulemaking. In sum, the many cardholders across the country who pay their credit bills on time will be made to subsidize the relatively few who repeatedly pay their bills late.[91] There is no such thing as a free lunch. When the CFPB claims in its press releases that "the proposal could reduce late fees by as much as $9 billion per year,"[92] its representation is deceptive because it omits the material fact that its own economic analysis expects that the costs of the late fee reduction will ultimately be transferred to and borne by most cardholders who never incur late fees.

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[88] 88 Fed. Reg. 18934.

[89] CFPB, *Report: Credit Card Late Fees*, pg. 7, fig. 3 and 4 (Mar. 2022, https://files.consumerfinance.gov/f/documents/cfpb_credit-card-late-fees_report_2022-03.pdf.

[90] Id.

[91] Economic research demonstrates that regulation of late fees makes consumers overall pay higher interest rates to compensate for charge-offs. See Nadia Massoud, Anthony Saunders, and Barry Scholnick, *The Cost of Being Late? The Case of Credit Card Penalty Fees*, 7 J. OF FIN. STABILITY 49 (2011). The CFPB also expects that the frequency of late payments will increase because of its rule. See 88 Fed. Reg. 18921. Recent research also supports this expectation, finding that when the size of late fees is reduced, the frequency of late payments increases. See Daniel Grodzicki, et al., *Consumer Demand for Credit Card Services*, 63(3) J. OF FIN. SERVS. RES. 273 (June 2023).

[92] CFPB, *Press release: CFPB Proposes Rule to Rein in Excessive Credit Card Late Fees*, https://www.consumerfinance.gov/about-us/newsroom/cfpb-proposes-rule-to-rein-in-excessive-credit-card-late-fees/.

Conclusion

Today’s hearing explores the important topic of “Taking Account of Fees and Tactics Impacting Americans' Wallets,” and efforts to eliminate what some label as “junk fees.” In my testimony, I have urged Congress to look more closely at the negative effect those efforts may have on the vast majority of consumers who meet their financial obligations and on the consumers the efforts claim to benefit. Further, Congress should pay special attention to agency efforts that privilege certain consumers over others and run afoul of rules and laws that make the system fair for everyone. I applaud the Committee’s effort to shine a light on the burden shouldered by consumers under the weight of inflation. In doing so, Congress should evaluate the efforts of each agency based on that agency’s compliance with the laws that govern it. As my testimony shows, in the case of the CFPB, the Bureau has strayed time and again based on its own convenience in executing a political agenda that amounts to price fixing in a manner that ultimately hurts consumers and subverts the orderly function of the marketplace.

Thank you, again, for the chance to testify on this important issue, and I welcome the opportunity to answer any questions that you may have.