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July 26, 2010

Attention Credit Card Issuers: Time to Review Your Credit Card Disclosures

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On July 21, the U.S. Court of Appeals for the Ninth Circuit provided important guidance on a credit card issuer's obligation to disclose to consumers, in a "clear and conspicuous" manner, the annual percentage rate ("APR") set forth in credit card solicitations. In Rubio v. Capital One Bank,[1] *the court held that the "clarity" of credit card APR disclosures is a question of law and that Rubio stated a Truth in Lending Act ("TILA")[2] claim, because the issuer failed to show, as a matter of law, that it made its APR disclosures "clearly and conspicuously" as required by Regulation Z.[3] In so holding, the court focused on the issuer's use of the term "fixed" and on disclosures outside the "Schumer Box" that the issuer could change the APR.*

The *Rubio* opinion: At issue was whether a direct-mail credit card solicitation had disclosed "[e]ach annual percentage rate applicable to extensions of credit" under the credit card agreement in a "clear and conspicuous" manner in the Schumer Box, as required by TILA and Regulation Z. Rubio alleged that in 2004 she had received a solicitation, which stated that she had been pre-selected for a MasterCard featuring a "fixed rate of 6.99% on balance transfers and purchases." In the Schumer Box of the solicitation, the credit card's APR for purchases was described as a "fixed rate of **6.99%,**" with the number printed in bold type. Next to the Schumer Box's heading "ANNUAL PERCENTAGE RATE (APR) for purchases," was an asterisk linked to a paragraph printed just below the Schumer Box. The paragraph listed three conditions under which the APR could increase: (i) late payment, (ii) overdrawn account or (iii) returned payment. Outside the Schumer Box, on the same page towards the bottom, but not linked by an asterisk, the solicitation said: "Terms of Offer. I will receive the Capital One Customer Agreement and am bound

[1] __ F. 3d __, No. 08-56544, 2010 WL 2836994 (9th Cir. July 21, 2010) available at http://www.ca9.uscourts.gov/datastore/opinions/2010/07/21/08-56544.pdf.

[2] See 15 U.S.C. §§ 16379(c)910(A)(i)(I); 1632(c)(2)(A) (2006).

[3] See 12 C.F.R. pt.226 (2009).

by its terms and future revisions thereof. My Agreement terms (for example, rates and fees) are subject to change."

About three and a half years after Rubio received the MasterCard, the issuer increased the interest rate on purchases and balance transfers to 15.9%, even though none of the three triggering conditions had occurred. The issuer notified Rubio in writing that she could avoid the higher interest rate by paying off her balance and closing the account.

Rubio filed suit, ultimately alleging violations of TILA, the California Unfair Competition Law ("UCL")[4], and breach of contract. The district court granted the issuer's motion to dismiss the action for failure to state a claim.

On appeal, Rubio argued that the solicitation "misleadingly" and inaccurately disclosed the APRs that could be charged under the Cardholder Agreement. She argued that by describing the APR as "fixed" at 6.99% and listing only three conditions under which the APR could be changed, the Schumer Box misled her into believing that the 6.99% rate could increase only if one of the three specified events occurred.

The issuer argued that the disclosure was truthful because the 6.99% rate could change under any of the three listed conditions, because the term "fixed" does not mean "unchangeable" but rather not tied to an index, and because the disclosure had clarified any ambiguity by stating, on the same page, "[m]y Agreement terms (for example, rates and fees) are subject to change."

The Ninth Circuit held that the issue of the "clarity" of an APR disclosure is a question of law, not fact. (Judge Graber dissented on this point. She stated that she would have reversed the dismissal but would have held that the clarity of this disclosure was a question of fact to be resolved by the trier of fact on remand, and not by an appellate court as a matter of law. She also said that the decision creates a split among the circuits.) The court further held that the issuer could not show, as a matter of law, that its APR disclosure was "clear and conspicuous."

In reversing the dismissal as to the TILA and UCL claims[5], the court held that TILA and Regulation Z "require absolute compliance by creditors" and that "[e]ven technical or minor violations of the TILA impose liability on the creditor." TILA requires that credit card APR disclosures must be "clear and conspicuous," a phrase defined in the official staff commentary to Regulation Z as "in a reasonably understandable form and readily noticeable to the consumer."

The court focused on use of the term "fixed," which it held made the disclosures less than clear. Although the solicitation had occurred in 2004, the court placed heavy emphasis on new amendments to Regulation Z (effective July 1, 2010) that generally prohibit creditors from using the term "fixed" in APR disclosures. Under the new regulations, the term "may not be used to describe the [APR] unless the creditor also specifies a time period that the rate will be fixed and the rate will not increase during that period, or if no such time period is provided, the rate will not increase while the plan is open." *See* Truth In Lending, 74 Fed. Reg. 5244, 5246-48 (Jan. 29, 2009). Although amendments effective in 2010 do not govern disclosures made in 2004, the consumer surveys on which the amendments are based suggest that many customers understand "fixed" to mean a rate that "does not change" –a confusion relevant to whether the disclosures were less than clear when made.

The court also identified several issues it saw with the APR disclosures:

[4] See Cal. Bus. & Prof. Code § 17200 (West 2008).

[5] The Court affirmed the dismissal of the breach of contract claim.

First, the disclosures linked to the Schumer Box listed only three events under which the APR could increase, not including the event (world economic trends and rising interest rates) that caused the issuer to raise the APR here; therefore, the use of the term "fixed" was not clear. A reasonable consumer could conclude that the issuer explicitly mentioned the three conditions precisely because they were the **only** reasons that the APR could change.

Second, the use of the term "fixed" can reasonably be interpreted to mean "unchangeable." Therefore, use of the term "fixed," while reserving the right to change the APR for any reason, rendered the disclosure unclear and ambiguous. The reservation of rights statement was located outside the Schumer Box and not linked to it by an asterisk. The court suggested without holding that this alone might preclude consideration of the statement. But even if considered, the statement was ambiguous because it failed to state clearly that the APR was subject to change for reasons other than the three reasons the Schumer Box disclosed.

Third, the term "fixed" can also reasonably be interpreted to mean "not tied to an index." Since a reasonable consumer could interpret the term "fixed" in more than one way, the APR disclosure is ambiguous, and under TILA and Regulation Z, any ambiguity must be resolved in favor of the consumer.

Lessons: *Rubio* shows that a credit card issuer must exercise great care in drafting APR disclosures to avoid anything that a clever lawyer could characterize as ambiguous or unclear. An issuer should follow the new Regulation Z requirements precisely if it intends to use the term "fixed" in its APR disclosures and should seriously consider avoiding the term "fixed" altogether. An issuer also should place all qualifying language in the Schumer Box or in a manner clearly and conspicuously linked to the Schumer Box.

If you have any questions about the content of this client alert, please contact the Pillsbury attorney with whom you regularly work or the attorneys below.

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