Addressing top of mind issues for credit card issuers

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Strategy

With 2024 presidential election results finalized, credit card issuers are speculating and scenario planning about what a second Trump administration will entail—specifically related to antitrust and the regulatory oversight of certain agencies such as the CFBP which recently introduced a late fee cap earlier this year. Industry professionals generally expect some pullback from the previous administration's antitrust agenda, which will favor the proposed Capital One–Discover transaction. However, there is still some uncertainty as senators from both parties voiced concerns on the Visa-Mastercard "duopoly" in the Senate Judiciary Committee hearing held in mid-November, with many agreeing interchange fees were too high. There were also calls for interest rate caps on credit cards.

Consumer cards: Concerns continue to mount as US credit card debt rose to a new high of $1.17 trillion, according to the most recent Federal Reserve Bank of New York report. Further the average annual percentage rate on credit cards assessed interest remains at a 20-year high of just over 23 percent even though the Federal Reserve has cut rates by 75 basis points in 2024. Credit card interest margins are at their highest level recorded since the Federal Reserve began collecting this data in 1994, which is great for card issuer profitability but reflects higher interest rates paid by customers. As consumer card issuers look to 2025, they remain mindful of the macroeconomic environment and anxiously await the new administration. They are also sizing up the impacts of CFBP's Section 1033 rule and potential implications to card usage. Lastly, issuers continue to compete with one another in creating an ecosystem of partnerships—with US Bank announcing its new travel center with Booking.com in late November 2024.[1]

Business cards: The battle for partnerships also extends into the small- to medium-sized businesses, commercial, and corporate cards arena, where card issuers continue to team with fintechs and payment platforms to build out expense and spend management capabilities, as well as an integrated end-to-end experience.

[1] US Bank, U.S. Bank Launches New Travel Center With Booking.com for Credit Cardholders" (November 18, 2024)

Potential actions to include:

- Conduct **scenario planning** related to the various headwinds facing the industry and evaluate your current and future business strategies.
- Review and assess your current **partnership strategy**
- Review your **current rewards program and related customer segmentation** to determine if your current program is competitive and meets customer needs
- Determine if your **virtual card program** is competitive and complementary to your existing business-to-business payment offerings.

Contacts

Jonathan Langlois

Financial Services Risk, Regulatory, and Compliance

KPMG US

T 704 497 3937
E jlanglois@kpmg.com

Michelle Swiec

Financial Services Risk, Regulatory, and Compliance

KPMG US

T 404 222 3000
E mswiec@kpmg.com

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Risk and regulatory

With a new presidential administration incoming, the regulatory environment may undergo significant shifts that impact the regulatory and compliance landscape. One of three areas that may experience increased focus is "critical security," which may result in more focus on cyber and information protections to mitigate operational losses from fraud and financial crimes. A second area that is likely to experience increased focus is market and competition resiliency, with an emphasis on addressing critical sector dependencies. A third anticipated focus area is the administration targeting overall reductions in regulatory burden, with the administration potentially lessening supervisory enforcement activity in the areas of governance and controls as well as fairness and protection. Overall, the credit card industry should be prepared to understand and quickly adapt to the shifting environment while preparing for the future.

During the presidential campaign, the incoming administration expressed its desire to implement a cap on credit card interest fees. Credit card issuers should closely monitor the incoming administration's position on interest fee caps, as well as its position on caps on other fees, such as late fees.

Late fees cost American cardholders around $14 billion each year, according to the CFPB. The agency issued a final rule[2] on March 5, 2024 that would amend Regulation Z to "better ensure" credit card late fees are "reasonable and proportional" to late payments. The final rule adopts a late fee safe harbor threshold of $8 for card issuers that have one million or more open credit card accounts (larger card issuers). However, a Texas federal district court entered a preliminary injunction, which has stayed the final rule from going into effect. The timing of the resolution of the litigation, and therefore the implementation of the rule, is uncertain.

Potential actions to include:

- Monitor the developments in interest fee caps and the late-fee-rule, including possible litigation, and **assess the operational and information technology (IT) system impacts** of the interest and late-fee caps, including any updates to customer disclosures.

Thought leadership

- Post-Election Shift
- Regulatory Shift 2025

Contact

Damian Plioplys

Financial Services Risk, Regulatory, and Compliance

KPMG US

T 212 872 7959

E dplioplys@kpmg.com

[2]Consumer Financial Protection Bureau, "Credit Card Penalty Fees (Regulation Z)"(January 2024)

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Credit

The Federal Reserve Bank of New York published its most recent Quarterly Report on Household Debt and Credit, noting that household debt balances increased by $147 billion in Q3'2024, now reaching $17.94 trillion outstanding[3]. Credit card balances increased by $24 billion between Q2'24 and Q3'24 and are approximately $1.17 trillion in outstanding balance.[3] The change represents an 8.1 percent increase over the previous-year balance. The Federal Reserve Bank of New York reported that aggregate delinquency rates rose slightly in Q3'2024 with 3.5 percent of outstanding debt in some stage of delinquency. Between Q2'23 and Q2'24, approximately 9.1 percent of credit card balances transitioned into delinquency.[3]

Despite aggregate delinquency rates rising, the Federal Reserve Bank of New York noted that credit card delinquency rates have improved, with 8.8 percent of balances transitioning to delinquency at an annual rate, a decrease from 9.1 percent as of Q2'2024.[3]

In November 2024, The Federal Reserve announced its second interest rate cut in 2024, lowering the rate by 25 basis points. In December 2024, the Federal Reserve announced another rate cut, lowering the rate by 25 basis points. Borrowers are expected to benefit from the year-to-date decrease in rates, which totaled 100 basis points.

Credit performance continues to be challenging in the current environment. Further, predicting credit loss may become even more difficult as the economy potentially approaches an inflection point for interest rates and inflation. There will likely be a lag before slowly decreasing interest rates and lower inflation begin to have a positive effect on credit. However, the results of recent elections may create uncertainty around the economic environment over the next few years.[4] Further, at the AICPA Banking Conference in September 2024, federal banking regulators highlighted a focus on the allowance for credit losses as an essential risk management function.[5] As a result, when estimating loss and managing credit, banks should continue to monitor model performance and recent trends and analyze historical data reflective of a similar economic scenario. Banks should also continue to coordinate among various functions, including credit and accounting, to make sure that effective management review and challenge is being performed and is documented.

[3]Federal Reserve Bank of New York, "Quarterly Report on Household Debt and Credit" (August 2024)

Potential actions to include:

- Assess **current reserving methodologies** to ensure they accurately incorporate relevant macroeconomic factors and industry trends.
- If defaults and losses have not yet been reflected by current models, then evaluate **whether model adjustments or overlays are required** to accurately predict the expected future losses in the portfolio.
- **Assess the level of consumer credit risk**, with a particular focus on nonprime borrowers who are more susceptible to higher rates of delinquencies and defaults.
- **Assess loan portfolios and implement early warning indicators** to identify high-risk customers and segments.

Thought leadership

- CECL Pulse Check Q4 2024
- [4]Policy shifts & the economy: Inflation & higher interest rates
- [5]2024 AICPA Conference on Banks & Savings Institutions

Contact

Karen Silverman

Financial Services Partner
KPMG US

T 212-954-1377
E ksilverman@kpmg.com

KPMG

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Capital

The capital rules for banking institutions continue to evolve. In a speech before the Brookings Institution in September 2024, Federal Reserve Board Vice Chair of Supervision Michael Barr discussed potential changes to the Basel III Endgame and G-SIB Surcharge proposals originally proposed in July 2023.[6] Further, due to a new presidential administration, there is additional uncertainty regarding the finalization of these rules.

One proposed change would change the tiering of institutions that are impacted, exempting Category III firms (with assets between $250 and $700 billion) from the frameworks for market risk and credit valuation adjustment (CVA) capital change unless they engage in significant trading activity. In addition to the impacts above, Category IV firms (with assets between $100 and $250 billion) would be exempt from the credit risk and operational risk frameworks of the expanded risk-based approach. Many card issuer institutions fall within these categories and could be directly impacted by the revised rules.

Additional changes in the re-proposal could impact all major areas of the rule—credit risk, operational risk, and market risk. The direct impact on certain rules that could impact credit card issuers is not yet clear, but the re-proposal should provide further clarity.

While an issuance date was not provided for the re-proposal, it is expected to be considered in an open board meeting and subject to a 60-day comment period. Implementation would be expected one year after the final rule is released.

Potential actions to include:

- Monitor developments in the **rulemaking process** for proposed “Basel III Endgame” rules.
- Assess the **potential impact of the proposed rulemaking** on capital for unused lines of credit, including an understanding of the impact of capital impact on credit limits not utilized.
- **Assess the operational and IT system impacts** of obtaining and maintaining the data required to demonstrate the “transactor” status of customers.

Thought leadership

- [6]Capital: FRB Remarks Outlining Basel III Endgame Re-proposal

Contacts

Jonathan Langlois

Financial Services Risk, Regulatory, and Compliance

KPMG US

T 704 497 3937
E jlanglois@kpmg.com

Mark Nowakowski

Financial Services Risk, Regulatory, and Compliance

KPMG US

T 404 222 3192
E mnowakowski@kpmg.com

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Legislative landscape

The Credit Card Competition Act (the Act) was first introduced in 2022 and was introduced again in 2023. The legislation is bipartisan and has the stated purpose of enhancing competition and choice as it relates to credit card networks. The bill remains stalled in Congress, and the likelihood and timing of passing the bill are both uncertain.

The bill proposes to inject more and fairer competition in the credit card industry by requiring credit card issuers that have assets over $100 billion to have a minimum of two payment networks, with one being outside the two largest networks. By requiring a network outside of the two largest, the Act intends to create more competition among networks, ultimately resulting in lower processing fees.

The legislation, as currently drafted, may impact the products and services offered as certain revenue streams would be impacted by the legislation if passed. Further, some have raised questions about the impact on credit card reward programs as a result of lower processing fees.

Potential actions to include:

- Monitor developments in the legislative process as they relate to the proposed Act.
- Assess the potential impact of the proposed Act on revenue streams and rewards programs.

Contact

Damian Plioplys

Financial Services Risk, Regulatory, and Compliance

KPMG US

T 212 872 7959
E dplioplys@kpmg.com

KPMG

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Accounting

On October 10, 2024, the Financial Accounting Standards Board (FASB) met to continue deliberations on its proposed Accounting Standards Update (ASU) related to purchased financial assets with credit deterioration. The proposed update would expand the scope of financial assets accounted for using the gross-up approach at acquisition. The proposed update would apply to “seasoned” financial assets and would eliminate the concept of purchased financial assets that have experienced a “more than insignificant” credit deterioration. Therefore, it would eliminate the need for an acquirer to make the judgmental assessment of whether a purchased asset has experienced such credit deterioration.

Companies that purchase credit card portfolios may face operational challenges due to the proposed standard, including the distinction between acquired and originated loans for revolving credit arrangements. Moreover, the retrospective application would require restating prior purchase arrangements due to the unavailability of relevant data and limitations of current IT systems for analysis.

Investors, accounting firms, and other stakeholders have submitted comment letters to the FASB regarding these concerns along with suggestions to ease the operational burden for credit cards, including practical expedients. While some comment letters were in favor of the project, others, along with the Joint Banking Regulators, were opposed. At the 2024 AICPA Conference on Banks & Savings Institutions, the FASB noted that preparers of financial statements are focused on possible scope exceptions or practical expedients to address the operational complexities associated with credit cards.[7]

During the October 2024 meeting, the FASB board and staff discussed the gross-up approach related to revolving credit arrangements and directed the staff to perform additional research on credit cards and other consumer revolvers to determine which assets should be included in a scope exception. The timing of a future ASU is currently uncertain.

Potential actions to include:

- **Review the current IT and data infrastructure,** assessing whether changes are required to capture incremental information for the new accounting model for purchased loans.
- Establish **a dialogue with investors and analysts** to help them understand the impact of the proposed changes on yield due to portfolio acquisitions. This communication can help stakeholders to better understand the changes so they can make informed decisions.
- **Continue to monitor updates** from the FASB Board and Staff regarding the treatment of revolving credit arrangements, including potential scope exceptions.

Thought leadership

- ASU Topic page
- [7]2024 AICPA Conference on Banks & Savings Institutions

Contact

Karen Silverman
Financial Services Partner
KPMG US

T 212-954-1377
E ksilverman@kpmg.com

KPMG

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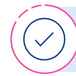

Contacts

Peter Torrente

US Sector Leader,
Banking & Capital Markets

ptorrente@kpmg.com

Diana Kunz

Audit Sector Leader,
Banking & Capital Markets

dmesch@kpmg.com

Stephen Kennedy

Industry Insights Leader,
Banking & Capital Markets

stephenkennedy@kpmg.com

Andrew Ellis

Banking Consulting Leader

alellis@kpmg.com

Agnel Kagoo

Capital Markets Consulting Leader

akagoo@kpmg.com

Mark Price

Tax Industry Leader,
Banking & Capital Markets

mhprice@kpmg.com

Liz L'Hommedieu

National Tax Industry Deputy Leader,
Banking & Capital Markets

elhommedieu@kpmg.com

Henry Lacey

Deal Advisory Leader,
Banking & Capital Markets

hlacey@kpmg.com

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