**Credit Cards**

Welcome to this podcast on Credit Cards brought to you by CALI. I am Professor Jennifer S. Martin. The topic of this podcast is to introduce the basic attributes of credit cards and how the payment system handles error and fraud. So, how prevalent is the use of credit cards? Most people have at least one. You might not be surprised that credit and debit cards collectively were used for two thirds of all non-cash payments in the United States in 2015. The number of credit card transactions is about half of the number of debit card payments, but the value of those transactions is actually more than that of debit cards. With the heavy use of credit cards as a payment system, even Amazon announced that it would offer its own credit card with special rewards for purchases on Amazon. While many card payments are in person transactions, about 20% of the transactions are remote, such as internet transactions.

Debit cards and credit cards, though, have different attributes and governing law, even though they share some features. For instance, while debit cards are governed by the rules of the Consumer Financial Protection Bureau (CFPB) contained in Regulation E, the rules governing credit cards appear in the CFPB’s Regulation Z at section 1026. The Federal Reserve System also retains regulatory authority over lending and, therefore, credit cards. One of the primary reasons for the distinction in the law is that credit cards are based on debt, a lending relationship, whereas debit cards are not associated with a line of credit, but, rather a checking or savings account owned by the customer provides the source of the funds. It is important to note, though, that Regulation Z focuses on the relationship between the consumer and the card issuer, leaving other relationships outside its scope and subject to contractual arrangements.

When it comes to credit cards there are a number of parties and contracts involved in any credit card transaction. Initially, you might as a cardholder use your Visa card to buy groceries at your local grocery store. Your relationship with the grocery would be a contract for sale of goods. You also have a contractual relationship with the issuer of your Visa card. Likewise, the grocery store has a contractual relationship with its bank in order for it to offer payment by credit card. Both the issuer and the merchant’s bank have contractual relationships with the network that processes the credit card transaction, here, Visa.

So how exactly are credit card transactions processed? The customer uses the card to make the purchase, typically either swiping or inserting the card using a terminal provided by the merchant. The network processes the information through to the card issuer and the data returns to the terminal approving or denying the transaction. In most transactions the customer will then sign to complete the transaction. There are some transactions, such as quick service restaurants, where the customer does not sign at the end. Of note, the card network itself is not a party to any given credit card transaction, it just facilitates the transaction. At some point after a transaction is completed, the issuer will batch deposit credit card slips and pay the merchants. Some time still later, the cardholder will receive a bill from the card issuer with the transactions for the statement period. After receipt of the statement then the cardholder has a number of days to pay the bill.

Let’s turn to the credit card and how the law protects the rights of cardholders. Initially, the first protection comes at the time of issuance of the card. Credit card issuers cannot send cards to consumers that are unsolicited and the application and solicitation for a credit card must include required information, typically presented according to a model disclosure approved by the CFPB.

The law provides consumer protections even after a card is issued. Various subparts to section 1026 contain three primary areas where a cardholder may have a defense to a charge on a credit card: 1) unauthorized transactions; 2) billing errors; and 3) contractual defenses to payment. At times, a cardholder may have more than one defense arising out of a single problem with a credit card transaction, but each of the defenses has its own elements and remedies. Accordingly, the cardholder should carefully review which defense is appropriate in the circumstance. Let’s turn to authorization first.

When it comes to transactions themselves, section 1026.12(b) makes clear that cardholders are responsible for all charges that are authorized, but not those that are unauthorized. An authorized charge is one that the cardholder makes and/or approves. An unauthorized charge would be one the cardholder did not permit someone to make. Regulation Z limits the liability of cardholders for unauthorized use to $50 prior to notification to the card issuer, but most networks, such as MasterCard and Visa, waive the first $50 of liability. While Regulation Z does not specifically require cardholders to notify the card issuer of a lost card or known unauthorized charge, prompt notification can guard against the imposition of even the $50 if it applies, as well as arguments that somehow the transaction was authorized by the consumer.

Sometimes, though, a cardholder may permit someone else to use their card, giving them permission to authorize charges. Authorization is determined under the common law of agency such that the cardholder might grant permission and be responsible for charges if there is actual, implied, or apparent authority to use the card. These are basic concepts associated with the law of agency at common law even though Regulation Z is a federal regulation.

Let’s look at an example. I have a MasterCard credit card. I give the card to my housekeeper, Dale, and send her to the hardware store to purchase some oven cleaner. Dale would have actual authority to use my card and I would be responsible for any charges. However, if Dale also purchased lunch for herself using my credit card, the lunch charge on my card would be unauthorized and I would not be responsible for the charge presuming the network has waived that $50 potential liability.

The second defense to payment under Regulation Z is that of billing errors contained in section 1026.13. A cardholder must report a billing error within sixty days after receiving the statement that reflects the billing error. The card issuer then has thirty days to resolve the matter or to give the cardholder a written acknowledgment, which extends the time of resolution to two billing cycles. The cardholder is not required to pay the disputed amounts during this time and the card issuer cannot take a negative action with respect to the consumer’s credit report. A consumer can assert a billing error even if they have already paid the credit card bill.

As it turns out, the billing error defense is quite broad because of the broad definition of billing error. Billing errors include: unauthorized charges, failure to properly identify the property or services purchased; charges for property or services not accepted by the consumer or not as delivered as agreed; computation or accounting errors; charges requiring clarification or documentation; and charges for which the consumer has not received a bill within twenty days of the end of the billing cycle. I know that is a lot. A simple example of a billing error would be that of a duplicate charge on my credit card statement for the oven cleaner purchased by Dale on my behalf. Of note, the billing error defense overlaps with unauthorized charges, perhaps you noticed that, as well as the basic defenses with respect to dissatisfaction with the property or services purchased.

The third defense under section 1026.12(c) permits the cardholder to assert any contractual defense they would have against the merchant arising out of the transaction, but only allows consumers to withhold payment for charges for which the consumer has not yet paid the card issuer. If the consumer has already paid the credit card bill, then perhaps the cardholder might want to assert a billing error instead. An example of this would be if Dale purchases the oven cleaner using my MasterCard, but the bottle turns out to be defective and unusable, I might be able to withhold payment for the charge under this provision of Regulation Z.

While this defense does not have the sixty day limitation with respect to billing errors, section 1026.12(c) does require the cardholder to attempt to resolve the dispute with the merchant, contains a $50 threshold and only covers disputes occurring in the same state as the cardholder’s address or within 100 miles from the cardholder’s address. As we’ve mentioned, most networks waive the $50 requirement. Likewise, with the advent of Internet purchases spanning large geographic areas, it is unusual for card issuers to assert the 100 mile limitation either. With respect to the oven cleaner, Regulation Z would require me to attempt to resolve the dispute over the oven cleaner with the local hardware store prior to asserting a claim with the card issuer.

At this point, you should be able to identify the primary parties associated with credit card transactions, the applicable legal rules and the defenses of unauthorized charges, billing errors, and contractual defenses.

I hope you’ve enjoyed this podcast on Credit Cards.

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