August 1, 2008

Jennifer J. Johnson
Secretary, Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

RE: **Docket No. R-1314**, Proposal to amend Regulation AA, Unfair and Deceptive Acts or Practices

Dear Ms Johnson and the Federal Reserve Board of Governors:

Thank you for providing me with the opportunity to comment regarding the proposed amendments to Regulation AA.

My name is Darrell Schmith and I have been involved in the credit card industry in some form for most of my professional career. Through my employment with Touche Ross & Co. (now Deloitte & Touche), I had the ability to audit financial institutions with substantial credit card portfolios. This employment was followed by careers with Citibank (South Dakota), NA and BANKFIRST, both in Sioux Falls, SD and both with their primary business line in the credit card industry. I am currently employed with First PREMIER Bank, a state chartered financial institution in southeast South Dakota that in addition to traditional banking activities, issues Visa and MasterCard credit cards where the balances are owned by and the accounts are serviced by our affiliate organization, PREMIER Bankcard LLC.

The recent proposal to amend Regulation AA has some provisions that are beneficial for cardholders and should be embraced by the industry. I believe those positive provisions should be regulated and applied consistently for each issuer of credit cards. My current employer, First PREMIER Bank and PREMIER Bankcard LLC, in our operational and procedural activities, was already complying with many of the existing and proposed regulations before they were actual requirements. In addition, as regulatory focus increased in an area of question, we would communicate with our primary regulators to find a solution that accomplishes the shared objectives. I agree that inadequate disclosures and questionable practices need to be stopped, and in general I agree with the proposed provisions that accomplish that objective.

Where I begin to get concerned is when the proposal attempts to limit, prohibit and restrict pricing rather than keep the focus on ensuring there is adequate disclosure, customer education and consumer accountability. Moving down a path of price controls to "protect the consumer" is a dangerous path and I believe will have some unintended consequences. I would like to address a few of my concerns.

This will Restrict Access to Credit

We must understand that consumers who have less than stellar credit histories present more risk of default and charge off to the issuer. These risk behaviors and increased pricing dynamics can be seen in a number of areas, including general consumer loan activities, life insurance premiums, health insurance pricing, automobile insurance rates. Even on a pooled basis, companies can see their health insurance rates increase if the loss experience of their population is higher and riskier.

There is definitely a correlation in each of these areas that mirrors credit card pricing. If you place limits on or prohibit certain pricing dynamics, the issuers will be forced into either taking a loss because the pricing does not compensate for the risk, **or more likely, they will simply not provide credit to large segments of potential customers who are riskier and have a higher probability of not paying what they owe.** When looking at one or two customers, sometimes the pricing may seem high, but when we take the time to fully understand that pricing is based on groups of individuals who demonstrate similar behaviors, either good or bad, we can see that the issuers will not be able to provide credit to those riskier segments.

Estimates of the exact number of consumers that will loose their availability to credit may vary, but in almost every article or study that I've seen, the numbers are staggering.

Access to Credit is More than a Credit Card Pricing

Almost every aspect of our lives is impacted by our credit profile. Car insurance rates are driven by loss rates, but they may also be affected by one's credit score. Employers may do a credit check before hiring a new employee. Before leasing an apartment, the landlord may do a credit check before allowing the person to move into the apartment. Utility companies may verify credit worthiness before turning on power or providing telephone service, just in case you don't pay your bill as promised. Many hotels will not even allow you to rent a room unless you have a credit card. Car rental companies are the same. No credit card, no rental car. The assumption is that if you cannot handle your credit, you may not be a worthy employee, tenant or customer.

In fact have you ever tried to make a telephone or online reservation for game tickets, a hotel room, a rental car, or concerts with no credit card? Have you ever tried to order something online from a catalogue with no credit card? Try to perform these necessary functions and tell the customer service representative or indicate in the comments section online that you are holding cash in your hand as you attempt to buy or reserve and I don't believe you will be successful.

By limiting or prohibiting appropriate risk based pricing, access to credit for a large segment of the population will be denied and the "protection" that was promised to the consumer through this proposed regulation has now turned into a restriction because they cannot perform necessary day to day functions available to those with better credit.

Forcing the Upfront Payment of Fees still Restricts Credit Availability

If you force the upfront payment of fees before allowing issuers to grant credit, in essence, access to credit will still be restricted. Consumers who have the lower credits scores where higher fees are charged, probably have had some issues within their credit history and may have limited capacity to pay the upfront fee. They are attempting to work their way out of the issue that was created and simply may not have the cash to make that upfront payment. Without that payment, access to credit will again be denied.

Charging Security Deposits or Fees to a Credit Card is not Necessarily Unfair or Deceptive

My understanding is that under Section 5 of the Federal Trade Commission Act, charging a security deposit or fees to a credit card account for the issuance or availability of credit is an acceptable practice. Again, this type of activity is driven by the need to compensate for the risk profiles of the consumers in this segment and is fully justified given that risk profile and cost of servicing.

If this practice is limited or prohibited it could again have a dramatic effect on the availability of credit to consumers.

Costs to Service

Beyond the credit risks and costs of default and charge off, the cost to service generally increases as the credit scores decline. Because these consumers are likely attempting to rebuild their credit or work through a financial issue, they make more telephone calls to check their balance or check when the next payment is due. They may need education and reminders so that we can help them understand why it is important to make timely payments on their outstanding balance.

Each one of these contacts is an expense to the issuers, but each contact also gives issuers an opportunity to provide the service the customer needs. Fees that are charge can cover the credit risk, but also assist in covering the servicing costs.

Economic Effects

If pricing limits or prohibitions are put in place, not only will the consumer be affected, but it will potentially have a negative effect on the economy. As previously discussed, the size of the population that has the potential to have their access to credit restricted is substantial. If they cannot rent a car, take a vacation, buy groceries or gas, make a car repair or buy school clothes and supplies, the businesses that provide these products and services will suffer and in turn the businesses that support them will suffer.

In addition, if a large segment of the population is not provided credit, the people who have the customer service jobs supporting these credit card accounts have the potential to have their jobs eliminated, because they are no longer needed. Again the negative economic effects cascade.

No Chance to Rebuild Credit

As discussed throughout this letter, it is highly probable that access to credit will be eliminated for a large segment of the population if the pricing limits and prohibitions of the proposed regulation are implemented. Without this access, people who have had credit troubles in the past will be denied the opportunity rebuild their credit status. The FDIC even recently acknowledged that it is very difficult to build wealth without access to credit.

Conclusion

In summary, I believe this regulation should focus on enhancing disclosures, providing customer education, creating consistent application across the industry and the regulatory exam process for all agencies, and offering a full refund of fees if after receiving the first statement, the customer decides this type of product is not what they really desire. We should empower the consumer with the ability to make an informed decision, not make the decision for them.

Implementing limits and price controls will have an adverse effect on the very consumers this proposed regulation is attempting to protect. Access to credit will be restricted and there will be negative effects on the economy because of the number of people potentially affected. Without access to credit, consumers will not be able to participate in normal functions like car rentals and hotel reservations, they may pay higher premiums for car insurance, and they may even be denied the opportunity for employment.

I am urging you to revisit certain sections of this proposed regulation, specifically those sections dealing with limited or restricted pricing, because I believe the unintended consequences are significant. We need to provide adequate disclosures and education and let the pricing be market driven and determined by risk, competition, and customer preference.

Respectfully submitted,

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