PREMIER Bankcard ®

July 31, 2008

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Attention: Docket No. R-1314

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attention: OTS-2008-0004

Ms. Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428
Attention: RIN 3133-AD47

Dear Ladies and Gentlemen:

This letter is submitted by PREMIER Bankcard ("Premier") in response to the May 2008 proposed rulemaking issued by the Federal Reserve Board ("FRB"), the Office of Thrift Supervision and the National Credit Union Administration (collectively, the "Agencies") seeking comment on a number of proposed revisions to Regulation AA concerning unfair or deceptive acts or practices ("UDAP Proposal"). Premier appreciates the opportunity to comment on this critical matter. We applaud the Agencies for efforts to ensure that consumers are not harmed by unfair or deceptive credit card practices. Moreover, Premier supports empowering customers with clear and conspicuous disclosures and commends the Agencies for moving towards this goal.

Premier is a leading provider of credit to the non-prime credit rehabilitation segment of the consumer lending market. We are the tenth largest issuer of Visa and MasterCard credit cards, and we focus on providing credit products to the sub-660 FICO segment of the market. We pride ourselves in being an industry leader, having responsible lending practices, employing top-quality and highly-seasoned management, and maintaining strong relationships with state and federal regulators.

Executive Summary

- While Premier believes that the overall intent of the Agencies to address specific unfair or deceptive acts or practices is laudable, we strongly disagree with the suggestion that the mere posting to a credit card account of deposits and/or fees for the issuance or availability of credit is an unfair act or practice within the meaning of Section 5 of the Federal Trade Commission Act ("FTC Act").

- Low limit credit cards are vitally important to consumers, and provide them with significant benefits. In particular, low limit credit card accounts provide access to credit for consumers who otherwise would have no credit, and provide an invaluable tool, in many cases the only tool available, to assist families recovering from financial emergencies. In doing so, low limit credit cards allow consumers to participate in many basic consumer transactions, including purchasing goods or services by telephone or over the Internet, rentals and engaging in preauthorized transactions for bridge and highway tolls.

- Importantly, low limit credit cards can, and actually do, enable many consumers to rebuild a positive credit history. And, by improving his or her credit score, a consumer can qualify for other credit, and can save thousands of dollars through better rates on a mortgage or automobile loan, and even insurance. Millions of cardholders successfully rehabilitate their credit and graduate to higher limit credit cards. At Premier, 22.5% of our low limit credit card holders "graduate" to higher limit credit card accounts within 24 months. Further, 35% of consumers with low limit credit cards improve their credit score within 24 months. In other words, these consumers accepted and successfully used low limit credit card accounts to rebuild their credit record and advance to higher limit credit accounts, mostly with card issuers who would not offer them credit cards when Premier was willing to do so.

- The imposition of upfront fees, even significant fees, is justified given the risk and expense associated with offering low limit credit cards. By design low limit credit cards are structured to factor in the substantially higher risk. From an account management standpoint, it is critical that Premier and other card issuers have the ability to deal with this risk on the front end. A prime credit card issuer commonly has a 4% to 5% delinquency rate, while a low limit credit card issuer experiences about a 20% delinquency rate. While approximately 22.5% of Premier's cardholders "graduate" to higher limit credit card accounts, many other cardholders do not; approximately 30% of our customers charge off without paying all or part of the balance due. Thus, it is critical for card issuers to price their products in a manner that allows them to absorb the losses by those who default, while giving other consumers the opportunity to demonstrate their ability to handle credit responsibly and graduate to other products.

- Conversely, eliminating the ability to charge and collect upfront fees, including posting such fees to credit card accounts, would make it difficult, if not impossible, for Premier and other low limit credit card issuers to continue to offer such accounts. And, eliminating low limit credit cards would have a significant adverse impact on both the local and national economy. An independent financial analyst suggested that the UDAP Proposal will result in a significant reduction in credit availability over the next two years,[1] and such a reduction in the availability of credit before the financial markets have fully recovered could further harm economic growth and impede economic recovery.

[1] Meredith Whitney at Oppenheimer & Co. Inc.; Oppenheimer Industry Update, US Banks, *Far From Over: We Believe The Credit Crisis Will Extend Well Into 2009* (May 19, 2008).

- In lieu of prohibiting the posting of such upfront fees and security deposits to credit card accounts, Premier urges the FRB to implement a code of best practices, even a mandatory code of practices, as described more fully below, including clear and repeated disclosure, the right to either pay the fees up front or post them to the account, and the right to reject the credit card when sent by the issuer and receive a full refund or credit for fees paid or posted to the account.

* * * *

Charging to a credit card account a security deposit or fees for the issuance or availability of credit is not an unfair practice under FTC Act

Premier commends the well-intended efforts of the Agencies, but believes that the Agencies have mischaracterized the mere posting to an account of a security deposit or fees for the issuance or availability of credit as an unfair practice under Section 5 of the FTC Act. Specifically, the Agencies claim that consumers suffer substantial injury when security deposits and/or fees for issuance or availability of credit are charged to a credit card account. Based on our extensive experience, however, consumers do not incur substantial injury, or for that matter any injury at all. Instead, low limit credit cards are valuable to millions of consumers who do not have access to traditional credit.

It is undeniable that low limit credit cards provide vitally important access to credit to consumers who otherwise would have no credit. Millions of consumers do not have access to traditional credit and low limit credit cards provide an invaluable tool, and in many cases the only tool available, to assist families in recovering from financial emergencies. In fact, as can be seen from the FRB's public comment letter files, many consumers attest to the fact that low limit credit card issuers were the only issuers willing to issue them credit cards, given their insufficient or poor credit history, and the importance to them of receiving those credit cards.

In fact, one of the primary benefits of having a low limit credit card account is the ability to rebuild a positive credit history. Once a consumer has been able to improve his or her credit score by consistently making payments on a low limit credit card account, he or she can qualify for better credit terms in the future, and can also save thousands of dollars in connection with better rates on mortgage or automobile loans, and even on insurance premiums. Over the years, Premier has received letters from consumers confirming this very point, similar to the many positive comments submitted to the FRB by consumers in connection with the UDAP Proposal. For example, one Premier cardholder wrote that her Premier credit card allowed her to re-establish her credit following a divorce, and that she is no longer worried about her ability to care for her children. Another cardholder wrote that his medical bills had adversely affected his credit rating, but through careful use of his Premier credit card, he was able to restore his credit, which enabled him to finance an automobile he needed for his job. Another cardholder wrote that her Premier credit card allowed her to improve her credit score and helped her continue her college education. There are thousands of similar success stories resulting from Premier's credit card practices that cannot fairly be characterized as either unfair or deceptive.

It is also important to understand that low limit credit cards allow consumers to participate in many of the most basic consumer transactions, including purchasing goods or services over the telephone and Internet, renting a car, booking a hotel, participating in membership plans, renting DVDs, and using preauthorized transactions for services like bridge and highway tolls. The ability to be able to participate in such basic consumer transactions gives consumers hope that financial security is obtainable and a sense of their ability to participate in society. It is fundamentally important that consumers with impaired credit histories not be precluded from engaging in such activities, and that they continue to have the ability to improve their financial situation. Thus, Premier believes that the Agencies have unjustifiably characterized the posting of upfront fees as "unfair" without fully understanding the benefit and value of such cards to consumers—that is, the benefit such credit can provide notwithstanding the imposition of such upfront fees.

The Agencies also suggest that consumers cannot avoid the injury caused by financing security deposits and fees on their credit card accounts. To the contrary, Premier strongly believes that through clear and conspicuous disclosures consumers can and do understand that fees will be posted to their credit card accounts and that the fees will reduce the credit available on those accounts until the fees are repaid. While Premier agrees that the current Regulation Z disclosure scheme could be improved, we also believe that consumers are fully capable of understanding the structure of low limit credit card accounts and the related pros and cons of having such accounts. It has been our experience that given Premier's layered disclosure approach, our cardholders fully understand the fees imposed and that financing those fees will reduce the credit line available to them. Further, most of our cardholders have found low limit credit card accounts to be beneficial. Specifically, based on a 2008 survey of Premier customers, 93% of customers surveyed gave positive ratings relating to their overall account satisfaction. In addition, 91% of consumers said that they understood that high fees would be imposed and the reason for imposing such high fees. Also, 91% of consumers were not opposed to the fees they paid to obtain access to a credit card.

Consistent with proposed revisions to Regulation Z, Premier also has long provided consumers with the ability to obtain a full refund of fees if, after receiving the account-opening disclosures, the consumer decides not to open the credit card account. Specifically, at the time of application or solicitation a consumer is informed of his or her right to close the account within 30 days of receiving the credit card contract and before purchases are made on the account. In addition, Premier, as a leader in the industry, would be willing to take the additional significant step of foregoing the imposition of finance charges on any fees for the issuance or availability of credit a new cardholder elects to post to his or her account, provided that Premier could first apply payments on the account to repayment of such fees.

The Agencies also suggest that the benefits associated with low limit credit card accounts do not outweigh the cost of financing such fees. In fact, many consumers indicate that low limit credit card accounts have been extremely beneficial, and that such cards provide vital financial assistance to consumers who have encountered emergencies and other unforeseen circumstances, such as medical expenses, death of a spouse, loss of a job, divorce or bankruptcy.

It is undeniable that low limit credit cards can and do help consumers re-establish good credit. Millions of cardholders successfully rehabilitate their credit and graduate to higher limit credit cards. On average among leading card issuers, 20% of low limit credit card holders "graduate" to higher limit cards within 24 months. And, Premier actually experiences a higher "graduation" rate of 22.5%. Since Premier, like other leading card issuers, reports to all of the major credit reporting agencies on a monthly basis, cardholders have a readily available way to re-establish their credit. Credit rehabilitation, especially for members of minority groups, has been instrumental in helping consumers obtain long-term financial goals.

Premier also provides credit education for its cardholders and follows customer-friendly practices, such as providing additional grace period days, in an attempt to encourage and assist cardholders in making timely payments so that they can "graduate" to more traditional products. For example, Premier provides numerous positive educational messages to consumers through statement messaging, consumer brochures and VRU messages encouraging consumers to make timely payments and keep balances under prescribed credit limits. Also, when an account begins to go delinquent, Premier provides a message alerting the consumer about the consequences of missing the next payment.

Imposing upfront fees is justified given the additional risk and expenses related to the accounts

Premier believes that the Agencies inappropriately characterize the imposition of upfront fees as unfair when, in fact, the imposition of such fees is justified given the additional risks and expenses associated with offering such cards. It is important for the Agencies to fully understand the costs and risks associated with low limit credit cards, and the need for issuers to impose upfront fees. It also is important to understand that most low limit credit card issuers do not approve accounts indiscriminately to simply gather such fees. To the contrary, for example, Premier's overall approval rate for credit card applications was only 33.2% for 2007, because Premier is very selective with respect to the applicants it will accept for its credit card accounts. So, contrary to claims by some consumer group representatives, low limit credit card issuers do not accept unqualified credit applicants merely to generate fee revenue. At Premier, we use underwriting criteria which is designed to approve applicants who have the most promise of successfully performing on their accounts, and hopefully then obtaining higher credit limits with Premier and with prime creditors.

Furthermore, it is critically important for the Agencies to understand that by design low limit credit cards are structured to address substantially higher risks and costs. From an account management standpoint, it is critical for Premier to have the ability to address credit risk on the front end. A prime credit card issuer normally has a delinquency rate of between 4% and 5%, while low limit credit card issuers typically experience a delinquency rate of about 20%. While a significant number of cardholders "graduate" to higher limit cards by repaying their balances as agreed, many cardholders do not. Thus, it is critical for card issuers to be able to price their products in a manner that allows them to absorb the losses by those who default. Also, as discussed above, consumers understand that there are fees imposed for opening these accounts and many consumers believe that the fees associated with the opportunity to re-establish credit through the use of a low limit credit card account are an acceptable price to pay for the thousands of dollars that they can save in the future with better rates on auto, mortgage, and other loans, and even on other products like insurance, once they have restored their credit history.

Moreover, low limit credit cards are more expensive to issue and maintain, including higher operational expenses and reserve requirements. Reserve requirements, for example, can be up to 56% for low limit credit card issuers, while as little as 8% for prime credit card issuers. Thus, for example, the reserve for losses would be $8 million per $100 million prime portfolio, whereas the reserve for losses could be up to $56 million per $100 million in a portfolio of low limit credit card accounts. In addition, the servicing costs for low limit issuers are higher than a prime issuer. For example, a prime customer contacts the issuer on an average of once per year, while a low limit customer contacts the issuer on average once or twice a month.

Prohibiting the posting of upfront fees could have a dramatic impact on the availability of credit to consumers and on the national economy

While Premier offers consumers the ability to pay fees upfront, rather than to post them to the account, the simple fact is that most new cardholders prefer not to pay the fees upfront. Given the additional costs and risks associated with low limit credit card accounts, companies like Premier simply would not be able to provide credit to consumers in this higher risk population. And, eliminating low limit credit cards at a time when consumers most need credit could hurt millions of consumers. With the increased price of gas and food, the average consumer is finding it increasingly difficult to make ends meet, and at times must use credit to do so. Moreover, limiting access to credit for millions of people, especially given current economic challenges, could have a significant impact on both the local and the national economy.

The UDAP Proposal, even if modified to address industry concerns, will inevitably result in the most significant changes in credit card operations since the adoption of the Truth in Lending Act ("TILA") in 1968. For example, one financial analyst[2] has projected that certain of the regulatory proposals would reduce outstanding credit lines by $2 trillion over the next two years. There also are concerns about the macroeconomic effects of the UDAP Proposal. A loss of confidence in the ability of credit card issuers to effectively price risk could cause the panic currently being experienced in the mortgage securitization market to spread to the credit card securitization market. This would increase the costs and decrease the availability of credit, with a corresponding reduction in the volume of credit card transactions and consumer purchases generally. And, a reduction in the availability of credit because of the UDAP Proposal before the financial markets have fully recovered could further harm economic growth and impede economic recovery.

Although the potential market impact may be similar, it is critically important that the Agencies understand that the policy issues relating to low limit credit accounts are dramatically different than those relating to subprime mortgage lending. Low limit credit cards are designed to limit high risk consumers from incurring debt they cannot handle and most of these credit card accounts are unsecured. Thus, low limit credit cards cannot burden consumers with substantial debt, nor do they put consumer homes at risk. In fact, the availability of low limit credit card accounts may assist consumers in responding to the credit report damage being done by the current mortgage crisis.

In this regard, it has been estimated that wealth for people of color has been reduced by up to $213 billion in connection with subprime mortgage loans, and many of these individuals will need the opportunity to re-establish their credit.[3] Specifically, for African Americans and Latinos, who have been especially hurt by the mortgage crisis, the considerable gap in wealth that already exists between whites and people of color will likely widen. In fact, a Boston-based

[2] Meredith Whitney at Oppenheimer & Co. Inc.; *See* Industry Update, *supra* note 1.
[3] Charles Steele Jr., Op-Ed, *The Color of Credit*, Wash. Post, June 23, 2008, at A15.

organization, United for a Fair Economy, estimated in its recent report, *Foreclosed: State of the Dream 2008*, that the "total loss of wealth for people of color to be between $164 billion and $213 billion for subprime loans taken during the past eight years. We believe this represents the greatest loss of wealth for people of color in modern US history."[4]

Instead of prohibiting the posting of upfront account-opening fees, the FRB should consider implementing or mandating a code of practices

In lieu of prohibiting the posting of upfront account-opening fees, and thereby effectively eliminating the ability of card issuers to offer low limit credit card accounts, Premier strongly recommends that the FRB consider requiring compliance with a set of best practices, including layered full and clear disclosure of key terms. Such a code of practices would protect consumers by ensuring that issuers fully disclose key account terms in a clear and conspicuous manner and by facilitating consumer education and understanding, including an understanding of the costs associated with the upfront fees and the consequences of financing those fees, such as reduced available credit. Unlike an outright prohibition, best practices would continue to allow consumers who believe that low limit credit card accounts are beneficial to obtain such products. In this regard, the following is a list of practices that could be included in such a code of practices:

- Full disclosure on or with applications, solicitations and the fulfillment educational kit accompanying the card of the total of the account-opening fees, the total credit limit for the account, and the remaining available credit after posting the account-opening fees;
- Clear right of the consumer either to pay the account opening fees up front or post those fees to the account;
- Disclosure of such fees and the remaining credit limit in a written statement separate from the TILA disclosure and/or cardholder agreement;
- Right to a full and immediate refund if the consumer changes his or her mind within 30 days of receiving the card and the separate fee disclosure;

[4] Amaad Rivera et al., *Foreclosed: State of the Dream 2008,* United for a Fair Economy, at vii (Jan. 15, 2008), *available at* http://www.faireconomy.org/dream.

- Reporting of the account to all three major credit reporting agencies;
- No reporting if the consumer changes his or her mind and opts for a refund (or alternatively, report the account as closed at the consumer's request).

If the Agencies are determined to address this issue under Regulation AA through the UDAP Proposal, they could characterize the imposition of unauthorized account-opening fees as an unfair or deceptive act or practice, but provide a safe harbor for a card issuer that is in substantial compliance with the code of practices specified by the FRB in their final rule. In addition, other practices could be encouraged or required. For example, as indicated above, Premier would be prepared to forego the imposition of finance charges on any account-opening fees that the consumer elects to charge to his or her new account, provided that Premier could apply the initial payments on the account to repay those account-opening fees.

Thank you again for the opportunity to comment on this important matter. Please contact me at 605/357-3410 if you should have any questions about these comments.

Sincerely,

Miles K Beacom

Miles Beacom
President and Chief Executive Officer
Premier Bankcard