August 4, 2008

By Electronic Delivery

Ms. 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

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

Re: RIN 3133-AD47

To whom it may concern:

This comment letter is submitted by the Consumer Bankers Association ("CBA") in response to the Proposed Rule ("Proposal") regarding unfair or deceptive acts or practices ("UDAP") published by the Board of Governors of the Federal Reserve System ("Board") and the Office of Thrift Supervision ("OTS") (collectively, "Agencies") in the *Federal Register* on May 19, 2008. CBA is the recognized voice on retail banking issues in the nation's capital. CBA's member institutions are the leaders in consumer, auto, home equity and education finance, electronic retail delivery systems, privacy, fair lending, bank sales of investment products, small business services and community development. CBA was founded in 1919 to provide a progressive voice in the retail banking industry. CBA represents over 750 federally insured financial institutions that collectively hold more than 70% of all consumer credit, and approximately 75% of insured deposits, held by federally insured depository institutions in the United States. CBA appreciates the opportunity to share its views on the Proposal with the Agencies.

General Comments

CBA supports the Agencies' efforts to review the status of consumer protection regulations pertaining to credit cards and deposit accounts. As we stated in our various comments to the Board in connection with its revisions to Regulation Z, we believe it is

critically important that consumer protections keep pace with the ever-changing marketplace. We therefore support the Agencies efforts to engage in a review of credit card issuer practices and overdraft-related issues. As we discuss below, however, we are concerned that the Agencies' process in this case has not been thorough enough. Indeed, the Board's current review of Regulation Z provides a relevant contrast to the process used by the Agencies for purposes of this Proposal. Whereas the Board's efforts to revise a *portion* of the disclosure requirements under Regulation Z has, appropriately, spanned a few years, the Agencies are attempting to tackle the crux of the current credit card and deposit business models in the span of a few months. CBA urges the Agencies to be more deliberate and to take advantage of the resources they have to produce appropriate substantive revisions to regulations governing industry practices.

CBA also believes that the Proposal, although well intentioned, would cause significant harm to consumers and banks alike. Although it may be appropriate for the Agencies to consider changes in certain approaches to consumer protection, CBA does not believe the UDAP authority is the most appropriate vehicle when trying to alter commonly accepted and widely employed practices. Not only are other regulations better tailored to these issues, but the present application of this authority by the Agencies may result in significant numbers of state court lawsuits that will require significant resources to defend. Even these meritless suits could result in significant liabilities for banks.

We believe that a closer, more deliberate review of the desired consumer protections and available statutory authority would lead the Agencies to an approach that relies less on UDAP authority and more on revisions to existing regulations promulgated under other statutory authority. We believe that the practices addressed in the Proposal should be regulated under existing statutory and regulatory constructs. This is the better approach, not only because Regulations Z, E, DD, CC, and others have provided meaningful guidance and governance to regulated institutions in the past, but also because the nature of UDAP actions make them more suited to uncommon practices or case-by-case enforcement. Not only does the application of a UDAP rule to common practices create the liability risks, but the Agencies must recognize that such an application without a fulsome record leaves its validity open to challenge.[1]

As we discuss in much greater detail below, the Proposal will harm a significant number of consumers. The Agencies' actions could limit the ability of banks to offer inexpensive deposit and credit card products to consumers who demonstrate less risky behaviors. The benefit of the Agencies' intervention, however, would flow largely to those consumers whose behavior warrants additional price modifications or other risk management tools.

[1] It is also worth noting that the credit card legislation pending in both the House and the Senate do not declare any practice to be unfair or deceptive, as such terms are used in the Federal Trade Commission Act. Rather, the authors of the legislation appear to prefer that credit card issuer practices are addressed in the Truth in Lending Act and, therefore, Regulation Z. We do not believe such legislation, is necessary, to grant the Board additional authority to implement the provisions in the Proposal using existing law.

Lack of Record or Basis for Sweeping Proposal

It is surprising that the Agencies have not provided any demonstrable amount of objective, statistical, or other firm support for their allegations that perfectly legitimate practices (in some cases specifically permitted practices) will now be considered unfair.[2] We understand that the full panoply of obligations imposed on the Federal Trade Commission in the Federal Trade Commission Act ("FTC Act") is not explicitly imposed on the Agencies under Section 18(f) of the FTC Act. However, given the nature of the delegation of congressional authority to the Agencies in the FTC Act, we believe that there should be a full administrative fact finding and record to support the Agencies' findings. We do not believe such a process or record exists with respect to the Proposal.

If the Agencies intend to apply their UDAP authority, especially if such authority will be used to completely redesign the pricing models for well-established financial products used every day by consumers, we believe a more thorough process should be observed. Specifically, CBA believes the Agencies should develop a substantial and supportable factual record. Not only is this necessary for purposes of soliciting meaningful comment from the public, but we believe it is necessary as a matter of basic administrative law. The Proposal, however, does not provide a detailed, factual record. Instead, in many circumstances, important issues are discussed in a matter of a few sentences and decided with relatively perfunctory and conclusory statements. Regardless, we do not believe that the factual record for the Proposal is adequate to determine that the practices identified are "unfair" for purposes of the FTC Act. Only the OTS issued an Advance Notice of Proposed Rulemaking, and even that requested comment on very general matters. Furthermore, to our knowledge, there have been no studies, no surveys, and no other significant activity designed in the context of the Proposal to gather information or to support the Agencies' assertions. CBA recognizes that the Agencies need not necessarily engage in detailed econometric analysis providing incontrovertible results, but we do believe that there must be some level of quantifiable analysis performed. It does not appear that this has occurred.

Litigation Risk

We believe the consumer harm and lack of firm support for many of the provisions in the Proposal should be sufficient to cause the Agencies to reconsider the Proposal in its entirety. However, we also urge the Agencies to review the potential litigation risk they are inadvertently creating for banks in connection with the Proposal. Specifically, the Agencies have chosen to use an unwieldy instrument to effectuate

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[2] For example, the Comptroller of the Currency ("OCC") has testified to Congress regarding the repricing of existing accounts as a risk mitigation tool for national banks. *See*, John C. Dugan, Testimony before the House Financial Services Subcommittee on Financial Institutions and Consumer Credit, June 7, 2007. The OCC also issued Advisory Letter 2004-10 informing banks how they could engage in repricing credit card accounts in an acceptable manner. As another example, in the context of mailing or delivering periodic statements, the Board has specifically permitted a card issuer to mail or deliver the statement 14 days prior to a due date. *See* 12 C.F.R. § 226.5(b)(2)(ii). The Agencies have also affirmatively recognized that banks charge fees in connection with account overdrafts. *See* Joint Guidance on Overdraft Protection Programs.

change regarding near universal practices that have been widely accepted, condoned, or even specifically permitted for years. The sudden declaration that these practices are unfair, as a matter of law, has consequences. Although we strongly encourage the Agencies to adopt any final rules prospectively after the effective date of the final rule, there may be others (*e.g.*, plaintiffs' attorneys, state attorneys general) who attempt to use the Agencies' reasoning and findings in law suits brought under state law against banks for *past practices*. The potential liability facing banks from even frivolous lawsuits of this type could be *enormous*.

CBA strongly urges the Agencies to mitigate the unnecessary litigation risk that would follow any determination that a widespread practice is, by definition, unfair or deceptive. Of course, the most effective way to mitigate the risk is to regulate the practices identified by the Agencies under other existing statutory authority other than Section 18(f) of the FTC Act. For example, as we discuss below, most if not all of the objectives sought by the Agencies could be achieved through amendments to Regulations Z and E.[3] Amendments to these regulations are much more likely to be enforced by all parties strictly on a "going forward" basis.

If the Agencies determine that they simply cannot achieve the desired consumer protections without adopting some form of a UDAP rule, we ask the Agencies to consider possible mitigations as noted in the recommendations below. In particular, it is critical for the Agencies to use every tool available to declare their findings to be prospective only so as to avoid inappropriate litigation risk for past behaviors, many of which have been sanctioned by repeated use and ongoing compliance oversight. Since this may not be enough alone, we encourage the Agencies to clarify that these are procedural rules created to prevent unfair practices prospectively, and that the rules do not in and of themselves constitute the delineation between fair and unfair practices in these areas.

DEPOSIT ACCOUNTS

Overdrafts

In General

CBA supports the adoption of safe and sound banking practices, including the discretionary honoring of overdrafts. This is an appropriate banking practice. Its discretionary nature allows the bank to provide a convenience and accommodation to its customers, while still granting the bank the flexibility to deny overdrafts that pose a risk to the institution. It is also important, however, that consumers understand their obligations to manage their accounts responsibly, the fees associated with overdrafts, and the possible options that may be available to avoid incurring overdraft fees.

[3] This is not to say that the Agencies cannot use UDAP authority to take enforcement actions or to issue a UDAP regulation without creating litigation liability. However, the Agencies simply must be cognizant of the fact that when they choose to declare a variety of accepted, condoned, and permitted practices affecting millions of accounts as suddenly unfair, there are consequences to that approach.

General Requirement

The Agencies propose to prohibit a bank from assessing a fee to a consumer's account in connection with an "overdraft service" (*i.e.*, honoring an item that overdraws an account) unless the bank provides the consumer with the right to opt out of the bank's payment of overdrafts and a reasonable opportunity to exercise that opt-out right, and the consumer has not opted out. The Proposal states that the consumer must receive notice and the opportunity to opt out prior to the bank's assessment of the fee, and subsequently at least once during, or for, any periodic statement cycle in which any fee or charge for paying an overdraft is assessed. The Agencies provide very limited exceptions to this requirement. Furthermore, the bank must provide a consumer the option of opting out only for the payment of overdrafts at ATMs and for POS transactions initiated by debit cards, in addition to the choice of opting out of the payment of overdrafts for all transactions.

Serious Unintended Consequences

Banks May Take Additional Risk, Potentially Increasing Costs to Consumers

Under the Proposal, if a consumer opts out, a bank will likely be forced to honor items that overdraft an account regardless. This is due to the numerous situations where overdrafts can occur notwithstanding the bank's processes designed to prevent them. If the bank does not have the right to charge a fee to cover the increased risk, it may be forced to revisit the economics of its deposit account offerings. For example, a bank may not be able to offer free checking, free debit cards, or free ATM access if it must dedicate resources to the uncompensated risks that are forced upon it by the adoption of the Proposal. Additional costs may be absorbed by a wider range of consumers solely for the purpose of not charging the consumers who present additional risk to the bank. Banks may also be less able to offer deposit accounts to the unbanked and the underbanked, if the costs cannot be justified. Therefore, we are recommending that the Board clarify the many situations in which these inadvertent overdrafts may occur and be charged notwithstanding an opt out; provide for a good faith standard to be applied; and make associated adjustments in the required opt-out notices. Banks should also be permitted to change the features, terms and conditions of an account for those who opt out, in order to offset the uncompensated risk. Nevertheless, as noted elsewhere, we oppose the use of opt outs in these situations precisely because the numerous exceptions will confuse the consumer even more than the opt out itself is likely to do.

Banks May Be Forced to Delay Funds Availability

Regulation CC governs the time in which a bank must make deposits available to consumers. CBA members report that in many instances they make funds available to consumers more expeditiously than is required under Regulation CC. We believe this is a benefit to consumers, and one which the Agencies would otherwise encourage assuming it is done in a safe and sound manner. We believe, however, that the Proposal

would force banks to reduce the speed with which they make funds available, although such time frames would not exceed those permitted under Regulation CC.

There is no doubt that the Proposal, if adopted, would increase returned items. If a consumer deposits a check, and the check is returned, the consumer is going to be more likely to overdraw his own account. Because a bank cannot be compensated for the risk associated with the consumer's overdraft, if the consumer opts out, the bank may hold the consumer's deposits longer than it otherwise would before allowing the consumer to access those deposits. The bank may ultimately deny more of its consumer's transactions, but at least the bank is not left in the position of honoring those transactions only to have a deposit return, resulting in an uncompensated overdraft risk.

CBA does not believe that this issue is one that will necessarily affect only those consumers who opt out. As more consumers opt out of overdrafts—as the proposed notice under Regulation DD essentially encourages them to do—there will be significantly more returned items within the payment system generally. It is not unthinkable that the volume of returned items, and the impact on the payment system more generally, could require banks of all sizes to reconsider their funds availability processes and policies. This would have a negative impact on all consumers, regardless of whether they opted out or not.

Consumers May Not Understand Nature of Opt Out

Despite the best efforts of the Agencies and banks, there are significant risks that consumers may misinterpret what it means to opt out of having overdrafts honored. For instance, they may assume that it means that the bank will not honor overdrafts, and that a debit card transaction that would put them into overdraft, for example, will be denied. This is not necessarily the case, since there are a variety of reasons why a debit card transaction will not be denied even if the consumer does not have good funds at the time of the transaction.[4] Consumers who opted out but are charged may be surprised and dismayed, even to the point of believing incorrectly that the bank is in violation of the law.

It is also likely that consumers will not understand the discretionary nature of a bank's decision to honor an overdraft. If the consumer is told that he can opt out of overdrafts, the consumer may (wrongly) believe that the lack of an opt out means that the bank automatically *will* honor overdrafts. As the Agencies know, this is not necessarily true. The consumer's confusion becomes even more understandable if the consumer is told that he can opt out of certain overdrafts, while expressly not opting out of others. This seems like a false choice to us, since the bank will not necessarily honor any overdrafts regardless of the lack of opt out.

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[4] Not all debit transactions involve a real-time authorization, such as those below a floor limit, those authorized using stand-in authority, or for other reasons.

CBA is also concerned that consumers will not understand the exceptions to the opt out. Although the Agencies have proposed only a few minor exceptions to the opt out, we believe a much broader list would be necessary to make the Proposal workable for banks. Regardless of the size of the list of exceptions, so long as there are any they will be difficult to explain to consumers. Therefore, there may be circumstances in which the consumer is surprised that the bank has assessed an overdraft fee, although such a fee is permissible. Not only is this disappointing to the consumer, but it may also result in significant customer service issues for the bank in the likely event that the consumer challenges the validity and appropriateness of the fee.

Consumers Will Bounce More Checks

As we note above, the adoption of the Proposal will result in more returned items and denied transactions. We question whether the Agencies should adopt a Proposal, in the name of consumer protection, if the Proposal will result in more bounced checks but not result in fewer fees or consequences to consumers. We describe many of the unintended consequences of this throughout our comments. It is important to note, however, that one obvious result is that consumers will incur additional fees in connection with returned items, and they will suffer increased consequences administered by the payees. If the payee is a creditor, this could have a "snowball" effect on the consumer whereby a bounced check results in: (i) an NSF fee assessed by the account holding institution; (ii) a returned check fee assessed by the payee; (iii) a late payment fee assessed by the payee; and (iv) additional consequences such as adverse reporting to a consumer reporting agency. We discuss this issue in more detail below in connection with the UDAP analysis offered by the Agencies.

Consumers Who Opt Out May Not Have an Alternative Means to Make Payments

The Agencies appear to believe that a consumer who opts out of honoring a POS debit card overdraft would simply use another convenient form of payment if the debit card transaction is not authorized. This is not necessarily true. Many consumers do not carry cash, or sufficient amounts of it for anything more than a minor purchase. Most do not carry a checkbook with them. Furthermore, a significant minority of consumers do not have or do not choose to use a credit card. Therefore, a consumer may not be able to switch payment forms on the spot. By this point, everyone is aware of the anecdote involving a $4 cup of coffee purchased with a debit card costing the consumer $44 due to a $39 overdraft fee. More frequently, however, the debit card purchase that overdraws an account involves gasoline to get to work, groceries to feed a family, or other purchases more appropriately categorized as "necessities." CBA believes the picture is much less clear when the consumer's opt out (even if limited to debit cards) means that necessities cannot be purchased. According to CBA members, a significant portion—perhaps well over a majority—of transactions that are authorized at a time when there are insufficient funds in the account actually settle into good funds. These transactions would be denied, however, under the Proposal.

Merchants May Be Less Willing to Accept Checks

The Proposal will make checks an even less appealing form of payment for both consumers and merchants than they are today. Merchants will be less likely to accept checks if the checks are more likely to be returned, or if their check guarantee/verification costs increase.[5] Not only will merchants be less likely to take checks at all, but even those who do accept checks will be less likely to accept a given consumer's check. This is because if a consumer bounces a check as a result of an ill-advised opt out, and that consumer is reported to a bad check database, the consumer may have difficulties writing checks to a variety of merchants afterwards as many merchants have services to review such databases before a given check is accepted.

The Agencies Do Not Adequately Support a UDAP Finding

CBA does not believe that the Agencies have met the standard they have set for purposes of finding industry's overdraft practices to be unfair. According to the Agencies, a practice will not be "unfair" unless three conditions are met: (i) the practice causes substantial injury to consumers; (ii) the injury is not reasonably avoidable; and (iii) the practice does not produce countervailing benefits to consumers or competition.

In justifying the proposed classification of overdraft fees assessed in a manner inconsistent with the Proposal as being potentially unfair, the Agencies state that consumers incur substantial injury due to overdraft fees. Furthermore, according to the Agencies, consumers cannot reasonably avoid this injury if overdrafts are honored without the consumers having the opportunity to opt out. The Agencies support this claim with the assertion that consumers often lack sufficient information about their account to avoid overdrafts. Finally, the Agencies declare that there is no countervailing benefit associated with the lack of an opt out that outweighs the purported injury, particularly in instances of ATM withdrawals or POS debit card transactions. We strongly disagree.

Charging a fee to a consumer for a service—one that clearly and unarguably benefits the consumer—does not cause substantial injury to the consumer. If the cost of a product or service was deemed, *per se*, to be an injury, as the Agencies appear to have done, the first prong of the unfairness doctrine would be meaningless. We do not believe that citing the existence of a fee is sufficient to declare substantial consumer injury. This is especially true in light of the fact that the fees are clearly disclosed, they are triggered by affirmative behavior by the consumer, and the consequences associated with avoiding the fee (*i.e.*, by opting out) may be more injurious than the overdraft fee itself.

Regardless of whether an overdraft fee is an "injury" in the UDAP context, there is simply no question that the fee is *reasonably* avoidable, even in the absence of an explicit opt out. In effect, a consumer "opts out" of paying the fee by not writing a check, or using a debit card, when there are insufficient funds in the account. The

[5] If check guarantee services see an increase in bad checks that they guarantee, the costs for those guarantees will almost certainly increase.

Agencies appear to concur with this view, but then allege that a consumer cannot necessarily know what the available balance is in a checking account. We think a consumer can *reasonably* know whether there are sufficient funds in a deposit account to cover a check or debit transaction. There are, in fact, a variety of regulations, such as Regulations DD, CC, and E, specifically designed to ensure that consumers have sufficient information about their accounts to maintain their checking account balances appropriately.

When attempting to determine who is in the best position to avoid an overdraft, the clear conclusion is that it is the consumer. Consumers understand this, too. CBA members have reported that the majority of consumers do not incur an overdraft fee in any given year. Furthermore, consumers make *active* use of tools to manage their checking accounts, such as online banking, e-alerts, ATM balance inquiries, telephone balance inquiries, etc. to manage their accounts properly. Why do they do this? Because they recognize it is their responsibility to do so, and because they would prefer to avoid the consequences of an overdraft (honored or not).

The examples provided by the Agencies indicating that overdraft fees are not reasonably avoidable are not persuasive. For example, if there is a hold on the consumer's deposit, the consumer is provided an appropriate notice under Regulation CC. In terms of crediting returned merchandise, this would be an issue for the merchant to address, not the bank. Regardless, it would seem that circumstances in which a consumer's item is returned due to a delayed crediting by a merchant are relatively rare, and certainly do not rise to the level of causing overdraft fees generally to not be reasonably avoidable. In short, the Agencies have provided no measurable evidence that overdraft fees are not reasonably avoidable.

CBA also urges the Agencies to reconsider whether there are countervailing benefits associated with current practices. It would seem that the Agencies themselves have already stated in their consumer protection pamphlet, "Protect Yourself from Overdraft and Bounced-Check Fees," that having an overdraft honored, and paying the fee associated with it, is preferable to having the check returned.[6] For the reasons we describe above, the harms of having a check bounce are far greater than having it honored.

This leaves the issue of whether a debit card transaction should be permitted to overdraw the account if the consumer will have to pay a fee. Based on the Supplementary Information to the Proposal, CBA surmises that this is the Agencies' primary concern. The Agencies believe that if a consumer presents a debit card at the point of sale, and the consumer's account would be overdrawn by the transaction, that the consumer would likely rather decline to continue with the debit card and switch to another form of payment. As we stated above, this is not necessarily true. The Agencies assume that consumers would carry sufficient cash, a checkbook (which would be

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[6] The pamphlet also states clearly that consumers should monitor their account balances carefully so as to avoid overdrafts, suggesting that the Agencies do not view this as an unreasonable expectation.

overdrawn), or a credit card. The Agencies do not provide data to support this supposition, and we question whether these facts may reliably be assumed.

Recommendations

Address Issues, as Appropriate, through Other Rulemaking Authority

For the reasons stated above, we do not believe that these policies and practices are inherently unfair or deceptive, and we disagree with the Agencies' findings. Thus, regardless of the merits of the policy determinations, rulemaking under section 18(f) of the FTC Act by the Agencies is inappropriate. As noted, we are also very concerned about the potential liability that may ensue from the Agencies' finding that services and practices that have been widely offered by financial institutions should be denominated "unfair" *per se*. Even if the Agencies issue rules with strictly prospective application, as we strongly encourage them to do, the industry could potentially face meritless but costly law suits under state laws for past practices that have now been deemed by the Agencies to be unfair. Therefore, any rulemaking in this area ought to be considered under other regulatory authority. For example, the Board could amend Regulation DD as necessary to ensure that consumers understand overdraft fees associated with an account. The Board also has ample authority under Regulation E to address debit card POS and ATM overdrafts, which appear to be the driving concern.[7] This is where, as the Agencies note, small transactions can most easily lead to comparably large overdraft protection fees through negligence or inadvertence by the consumer. Further, as we have said, we believe the proposed opt outs send the wrong message to consumers: the false message that bouncing checks, with all the attendant fees and consequences is necessarily a better alternative than paying an overdraft protection fee when the bank pays the overdrawn item.[8]

Agencies Should State That The Practices Described in the Proposal are not Per Se Unfair or Deceptive and Are Prospective in Application

We have stated our serious opposition to the use of the FTC Act by the Agencies to address these issues, due to the litigation risks it would create for financial institutions. Should the Agencies continue to consider opt outs for overdraft, as proposed, however, we strongly recommend that they clarify that, as a matter of law, that the acts or practices identified in the regulation are procedural rules created to prevent unfair practices prospectively, and that the rules do not in and of themselves constitute the delineation between fair and unfair practices in these areas. Thus, for example, the failure to provide

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[7] Of course, because not all banks would necessarily be able to effectuate an opt out only for debit/ATM transactions, such banks should be permitted the flexibility to disclose to the consumer that the opt out will apply to all transactions.

[8] One suggestion that has been offered is to require that financial institutions provide consumers at account opening: (i) a disclosure whether the institution approves debit card POS transactions when the consumer does not have available funds at authorization; and (ii) alternatives offered by the institution, such as how to prevent such authorizations or choose other accounts that do not have the feature. These alternatives should not be required, however.

notices and opt outs as set forth in any final rule would not be *per se* "unfair" as that term is defined in the FTC Act, but would constitute a possible violation of these procedural rules created to prevent unfair practices prospectively. Regardless, it is critical for the Agencies to state in the regulation that the rules are prospective only so as to avoid retroactive application.

Do Not Require Both Full and Partial Opt Outs

As we have noted, the partial opt out as the alternative presented to the consumer is not only costly to implement, but sends a false message—that the institution will then be required to pay for those overdrafts that the consumer is choosing not to "opt out" of. We believe that consumers will be confused by the signal that the choice is theirs in this matter. It is imperative that the institution retain the discretion whether or not to pay, or discretionary overdraft protection ceases to be discretionary at all.

Aside from consumer confusion, this is not a viable option for many banks. For example, many very large and sophisticated banks could not offer only a "partial" debit card/ATM opt out unless they incurred significant costs. The Agencies appear to recognize this in the abstract, although they have not attempted to quantify or otherwise estimate the regulatory burden associated with this portion of the Proposal. Specifically, the Agencies state that they understand this limitation exists, but that it appears that the benefits of providing a partial opt out option outweighs the potential (unmeasured) programming costs. This assertion is not accompanied by any supporting facts or data in the Supplementary Information, nor is there any estimate of the Proposal's "benefits" against which the significant costs could be measured. Also troubling, however, is the implication that a bank should honor check overdrafts if the consumer opts out of only the debit/ATM overdrafts. CBA does not believe that this can be the Agencies' meaning, and we therefore assume that a bank would still be permitted to dishonor all overdraft items even if the consumer wanted to opt out of only the debit/ATM overdrafts.

If Opt-Out Requirement Is Adopted, Expand Exceptions and Establish a "Good Faith" Standard

As we have noted, numerous situations arise where accounts can overdraw notwithstanding the efforts of the institution to prevent them. The Board notes two situations that it would propose as exceptions, where the institution may still charge an overdraft fee even when the consumer has opted out. These are inadequate to address all the possible situations that might arise. There may be many circumstances in which the bank is forced to overdraft a consumer's account, regardless of the consumer's opt out. In those circumstances, the bank should be permitted to charge a fee. For example, a bank may authorize a debit card transaction because, at the time of the authorization, the transaction would not overdraw the account. However, after the authorization, the bank may post several items to the account. The authorized transaction may settle several days later, putting the account into an overdraft status. In another typical case, funds attributable to deposited checks may be made available to a consumer the day after the

deposit as required by Regulation CC, although the bank has not yet received collected balances on account of those check deposits. The items may have to be returned by the maker's bank for various reasons, including insufficient or unavailable funds or an unauthorized maker or endorser signature. The available funds in the customer's account must then be reduced to account for the return. In case the account then becomes overdrawn, the bank should be entitled to charge the customer an overdraft fee. If the Agencies go forward with an opt-out requirement as proposed, it would be essential to include these additional exceptions and the many others that have been noted by commenters.[9] However, we would also recommend that the Agencies establish a "good faith" standard, so that, if a consumer opts out, the institution would be required to make a good faith effort to prevent overdrafts from occurring on the account. We believe the notice of opt out needs to be clarified in any case to make it clear to the consumer that overdrafts would not necessarily stop, but would be less likely to occur if the consumer opts out. This would also reinforce a good public policy goal of encouraging consumers to continue to monitor their accounts, rather than abdicating their responsibility to the bank.

Debit Holds

General Requirement

The Proposal would also prohibit a bank from assessing a fee or charge on a consumer's account for honoring an overdraft if the consumer's overdraft would not have occurred but for a hold placed on funds in the consumer's account that is in excess of the actual purchase or transaction amount. Although the proposed regulatory text does not specify whether the hold pertains to a bank hold or one resulting from a merchant's authorization request of an amount in excess of the actual amount, the Supplementary Information suggests that it could be either circumstance.

Authorization Holds Prohibition Is Unworkable

This portion of the Proposal forces banks to make decisions based on facts that they cannot know at the time the decision must be made. Specifically, a bank will not know whether the merchant has requested authorization—intentionally or not—for an amount in excess of the actual amount settled. The bank, therefore, cannot know until after the settlement of the authorized debit transaction whether it is prohibited from charging an overdraft fee for items that clear during the time between which the transaction is authorized and later settled. This timeframe of uncertainty can be as much as three days, assuming the bank can match the authorization to the settlement.

We believe that this prohibition on "holds" generally leaves banks with unappealing options. For example, the bank could refrain from charging overdraft fees

[9] Banks should also be specifically authorized to charge for overdrafts where there is express customer consent. Banks should be permitted to contact customers in order to obtain authorization to pay an item and charge, even if the consumer has opted out.

on any overdraft that is honored while a debit authorization is pending (assuming the settlement of the debit amount would place the account into overdraft). This is not acceptable from a risk mitigation standpoint. The bank could also refrain from "holding" authorized transaction amounts that have not settled. This is also unwise and unsafe. It also appears that the bank could simply return items and deny authorizations during the pendancy of debit authorization holds that, if settled, would place the account into overdraft.

The Agencies Do Not Adequately Support a UDAP Finding

The Agencies state that consumers are injured by overdraft fees resulting from debit holds that exceed the amount of the transaction. Consumers cannot reasonably avoid these fees, according to the Agencies, because consumers may not be aware of the hold or the length of time it could remain. The Agencies state that there is generally no countervailing benefit resulting from the assessment of overdraft fees being assessed in connection with an account that appears overdrawn due to a debit hold.

We repeat our view here that the fact that there is a cost associated with a practice does not mean that there is significant injury associated with the practice. With respect to debit holds, the Agencies have not attempted to actually study or quantify the costs associated with debit holds. Without such analysis, we do not believe that the Agencies can conclude, as a matter of law, that there is substantial consumer injury associated with assessing an overdraft fee in connection with an overdraft that is caused *solely* by a debit hold.

We also do not believe that the Agencies should automatically concede the fact that consumers cannot be made aware of debit holds, thereby making the overdraft fees in question reasonably avoidable. In fact, we are aware that there are state laws that attempt to address this issue by requiring the merchant to notify consumers if the merchant is going to request authorizations greater than the transaction amount.[10] The Agencies do not state whether they are aware of such statutes, whether they have reviewed them, or whether they are helpful in educating consumers about debit holds. It would seem feasible, however, to have a merchant inform the consumer of the hold that the merchant may place on a debit card, such as on the debit card receipt that is already provided due to the requirements of Regulation E.

In addition to giving consumers the tools to avoid overdrafts resulting from debit holds, such as merchant disclosures, we believe that this issue will likely become relatively moot due to market forces and their impact on the major card networks. It is our understanding that Visa, for example, has announced an initiative to reduce the likelihood that a debit hold on a gasoline transaction will remain for more than a few minutes. CBA believes that such private sector initiatives will further reduce any likelihood that overdrafts result from debit holds.

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[10] *See, e.g.*, Tenn. Code Ann. 47-18-128 (2008).

Recommendations

We oppose the Agencies' proposal to prohibit authorization holds because, as we have noted, we believe it is unworkable and creates safety and soundness problems. To the extent this issue is not addressed by industry initiatives, we believe the Agencies should attempt to quantify the harm associated with overdrafts and debit holds. If there is, in fact, significant consumer injury that results, we believe it would be more appropriate to explore whether a requirement under Regulation E applicable to merchants would be a more appropriate approach to educating consumers about debit holds in light of the practical difficulties associated with this portion of the Proposal.

CREDIT CARDS

Time to Make Payments

General Requirement

The Proposal states that an issuer must not treat a payment on a credit card account as late for any purpose unless the consumer has been provided a reasonable amount of time to make the payment. The prohibition does not apply to the current 14-day rule in Regulation Z as it relates to grace periods.[11] The Agencies provide a safe harbor for issuers that have adopted reasonable policies and procedures designed to ensure that periodic statements specifying the payment due date are mailed or delivered to consumers at least 21 days before the payment due date. In providing for the 21-day safe harbor, the Agencies state that they believe it is important for the cardholder to have seven days to review the periodic statement and the additional 14 days is to allow for mail delivery in each direction.

Increased Consumer Costs with Little Corresponding Benefit

As the Agencies note, this portion of the Proposal will likely result in increased costs to consumers. In effect, the Proposal would essentially mandate that grace periods be at least 21 days[12] and extend the time during which a card issuer must bear the costs of the float. This is not a cost-free result for card issuers, who will be forced to recover costs in other ways. CBA also notes that the Proposal will not necessarily result in a significant reduction in consumers who pay late. The Proposal may simply result in consumers waiting to mail their payment until a later date, as they attempt to take

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[11] If the Agencies truly intend to permit a bank to offer a 14-day payment period for purposes of a grace period, and a 21-day period for all other purposes, the Board must revise Regulation Z accordingly for purposes of periodic statement disclosures of these two dates.

[12] It is almost certain to be longer, if one factors in the time to close the billing cycle and prepare the statement before it is mailed. Further, although the Agencies preserve the option of having only a 14-day grace period, that would require setting, disclosing, and administering two different due dates (one for the 14-day grace period, and one for the new 21-day requirement regarding late fees and other consequences of late payments). We suspect that, rather than take on this complexity, issuers will follow the "lowest common denominator" and be forced to provide a longer grace period.

advantage of the extended payment time afforded by the Proposal. Therefore, we suspect that there will not be a significant reduction in late payments, as this game of "beat the clock" will continue to result in some consumers not making timely payments.

Postmarking

CBA does appreciate that the Agencies have refrained from proposing a requirement that banks review the postmark on the payment for purposes of whether it is made in a timely fashion. For purposes of bank accounting and other systems requirements, what is important is the date on which the consumer's payment is received, not when it was sent. Furthermore, even if the date of mailing were relevant for purposes of timeliness, a bank cannot be expected to find and decipher a postmark on millions of pieces of mail each month (assuming the envelope has a legible postmark at all). Such a requirement is unreasonable in the extreme, and we applaud the Agencies for not suggesting it as a viable alternative.

The Agencies Do Not Adequately Support a UDAP Finding

The Agencies state that late payments cause late fees, increased APRs, and possibly the reporting of negative information to consumer reporting agencies. According to the Agencies, these injuries are not reasonably avoidable unless consumers have a reasonable amount of time to make a payment, including a reasonable opportunity to review a periodic statement. By essentially mandating a 21-day rule on billing statements (which would likely translate into a mandated 25-day grace period), the Agencies concede that the Proposal may increase costs on consumers, but state that it does not appear that the costs outweigh the benefits to consumers of receiving a reasonable amount of time to make a payment.

CBA agrees with the Agencies that cardholders should have a sufficient amount of time to receive a statement, review it, and make a payment without incurring a late fee. Indeed, we believe that the Board specifically considered this issue when it adopted the provision in Regulation Z that *specifically permits* a card issuer to send a periodic statement 14 days before the date on which a late fee may be assessed. The Board's 14-day rule is based on the 14-day rule enacted by Congress as it relates to payments sent on accounts that have a grace period. Presumably Congress intended for the grace period to be "real," not illusory. In order for there to be an effective grace period on an account, a cardholder must have sufficient time to receive a statement, review it, and make a timely payment. Hence, Congress provided the 14-day rule in the Truth in Lending Act.

Although the Agencies apparently have the same goals that Congress had when it enacted the 14-day rule, the Agencies have determined that the current 14-day rule is insufficient. We are unaware, however, of evidence suggesting that consumers do not have such a reasonable opportunity today. It does not appear that the Agencies have actually surveyed consumers on this point or conducted any other objective analysis. The lack of any tangible support for the assertion that the current 14-day rule is inadequate is surprising. CBA believes that hard evidence would be necessary to declare that the

Board's existing treatment of the matter will be *per se* unfair.[13] Such a result, especially in light of the clear congressional imprimatur on current practices relying on a 14-day rule, appears to us to be arbitrary.

Recommendation

It appears the Agencies' true objective is to ensure that consumers have a reasonable period of time to review a periodic statement, and that the Agencies believe seven days is a reasonable period of time. If this is true, we urge the Agencies to evaluate current practices using sound methodology to determine whether this objective is largely met today. If the evaluation suggests that it is not, we believe the Agencies should then consider requiring card issuers to adopt reasonable policies and procedures designed to ensure that a cardholder has seven days to review a periodic statement and make a timely payment. Based on the Agencies' stated concerns about the need for a 21-day rule given the inconsistency of mail delivery, there is no reason for a 21-day rule if the statement and payment are provided electronically, for example, or if the issuer has procedures reasonably designed to ensure that statements are delivered promptly.

Account Repricing

General Requirement

The Proposal would prohibit a card issuer from increasing the APR applicable to an "outstanding balance" on a credit card account, unless an exception applies. A card issuer may increase the APR applicable to an outstanding balance if the APR increase is due to: (i) the operation of an index that is not under the issuer's control and is available to the general public; (ii) the expiration or loss of a promotional rate; or (iii) if the issuer has not received the consumer's payment within 30 days after the payment due date. If the issuer increases the APR on a category of transaction on the account, but is prohibited from applying the increased APR to outstanding balances in that category, the issuer must provide the consumer with a method of paying the outstanding balance that is no less beneficial than a 5-year amortization or one resulting from the doubling of the percentage of the balance used to calculate the minimum payment. In these circumstances, the issuer would also be prohibited from assessing any fee based solely on the outstanding balance.

Increased Cost of Credit for All Consumers

The effect of this portion of the Proposal on consumers is simple. If the Proposal is adopted, card issuers will likely offer accounts with higher APRs (and/or with higher fees) to allow them to hedge against future risks associated with the account. In essence, every account must have the risk prepriced because the Agencies would eliminate the flexibility to modify only the price of those accounts that ultimately pose additional risk

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[13] CBA recognizes that the 21-day provision is a safe harbor, not an explicit requirement. However, the Agencies are certainly aware that examiners, compliance officers, and others will likely give a strong presumption to the notion that 21 days is, in fact, the substantive requirement.

to the bank. Based on the Supplementary Information, it appears that the Agencies fully understand that the Proposal is likely to have this effect on credit card accounts. CBA questions whether this is a desirable outcome in terms of a UDAP rulemaking.

Mandated Product Design: Variable Rate Accounts

We also note that the Proposal would essentially deny consumers the opportunity to hold nonvariable rate accounts. The Agencies appear to believe it is appropriate and justified to increase the APR on a balance if the increase in APR results from the operation of an index outside the control of the card issuer. Conversely, the Agencies believe it is problematic—to the point that it would be *per se* unfair—for a card issuer to increase the APR on an account with a nonvariable rate, even if the rate is well below the issuers' cost of funds. This is an unusual dichotomy, because the injury/reasonable avoidability/countervailing benefit test would appear to be the same for both types of APR adjustments. We are not suggesting the Agencies determine that the variable APR should therefore not be applied to an existing balance, but rather that they reexamine the reasons why they condone the operation of a variable APR on an existing balance, but not an adjustment of a nonvariable APR.

Secondary Market Impact

Although a bank may be able to change terms on an account, it is not clear that similar adjustments can be made as smoothly in the secondary markets. It does not appear that the Agencies have considered how the Proposal would affect current or future credit card securitizations. Just as credit card issuers have priced credit card accounts based on the ability to adjust for credit and other risks, purchasers of the securitized credit card debt and similar obligations have made similar assumptions. CBA believes the Agencies should consider the impact of the Proposal on current and future securitizations to determine how its implementation could adversely affect credit card lenders and their cardholders. For example, if the Proposal makes it more difficult for banks to securitize the receivables or otherwise fund credit card operations, the Agencies may tighten the credit squeeze even beyond what is expected if the Proposal is adopted.

The Agencies Do Not Adequately Support a UDAP Finding

The Agencies claim that the application of an increased APR on existing balances results in consumer injury in the form of higher interest charges. The Agencies also state that such injury is not reasonably avoidable as a general matter for a variety of reasons, including that: (i) consumers may not be aware of when an APR could increase; (ii) disclosures of such circumstances apparently cannot be made effectively; (iii) consumers may not be able to transfer a balance to a comparable account; and (iv) consumers are not in control of how an issuer assesses their creditworthiness. The Agencies claim that the Proposal will benefit a limited number of consumers greatly, although a larger number of consumers may incur smaller incremental increases in the cost for credit. The Agencies assert that, as a result, "it appears that consumers…may benefit as a whole."

CBA is troubled by the Agencies UDAP analysis as it relates to this portion of the Proposal and the impact this portion of the Proposal will have on consumers and banks. We do not believe the Agencies' justifications for the prohibition on repricing of account balances are, in fact, correct. Furthermore, we believe that the Agencies' statements could be interpreted to undermine the fundamental basis of all consumer lending—not just in connection with credit card accounts. Regardless of the substantive provisions that are adopted in the final rule, we strongly urge the Agencies to revisit the claims made in the Supplementary Information to the Proposal and not only revise them, but affirmatively reject them when issuing the final rule.

The Agencies state that a cardholder may not be aware of when an APR on an existing account balance could increase, and therefore such a factor contributes to increasing an APR on an existing balance as being unfair. Indeed, a consumer may not always control the circumstances in which an APR will increase, but that does not appear to be a relevant factor in terms of whether a practice is unfair. The Agencies explicitly recognize this fact as they (correctly) allow for the operation of a variable APR on a credit card account to apply to an existing balance despite the fact that consumers will not know ahead of time if or when the index to which the APR is tied will increase or decrease.

The Agencies believe that the fact that a consumer could not transfer a balance to a comparable account is evidence of the fact that an increased APR on an existing balance is unfair. To the contrary, it is evidence that the card issuer has correctly priced (or even underpriced) the risk the balance poses, such that other card issuers are not willing to offer a better deal. The Agencies also apparently believe that a consumer has an implicit right to the existing account terms on an open-end credit balance. This is not the nature of open-end credit, and a card issuer's need to change terms occasionally has been long recognized at the federal and state level.

The Agencies also apparently believe that the fact that a consumer cannot control how a lender assesses risk is at least a contributory factor to an unfair lending practice. Yet consumers have historically had no control over the risk factors assessed by lenders, nor have lenders ever been expected to give consumers a detailed explanation of underwriting methodology. The Agencies' declaration that consumers apparently should have some control over what a lender considers, and that a lender should publicize its underwriting methods, jeopardizes the legitimacy of credit underwriting generally.

Recommendation

If the Agencies believe that they must address how card issuers reprice existing balances, we urge them to consider first the impact the Board's proposed revisions to Regulation Z disclosures will have on consumer understanding of credit card products. Although we do not believe all of the Board's proposed revisions are necessary or appropriate, they are a preferable alternative to the price controls proposed by the Agencies in this portion of the Proposal. Another alternative worthy of consideration would be for the Board to amend Regulation Z to provide cardholders with a federal right

to opt out of changes in terms. Indeed, notice and opt out appears to be the Agencies' cure to an unfairness determination regarding overdrafts, and it is logically inconsistent that no similar proposal was offered here. Despite the Agencies' claims to the contrary, we believe consumers read these notices and would opt out if it were the appropriate choice to make.[14] It is our understanding, in fact, that banks have meaningful opt-out rates in connection with change in terms notices, suggesting that this has been an effective approach. We see no evidence in the Supplementary Information that the Agencies have surveyed the opt-out rates of the large card issuers, and we would encourage them to do so. A notice and opt-out alternative would actually *empower* consumers to determine which credit products they would like, as opposed to forcing creditors to increase the cost for them or not make them available.

Payment Allocation

General Requirement

If different APRs apply to different balances on a credit card account, the Proposal would require the issuer to allocate any amount paid by the consumer in excess of the required minimum payment among the balances in a manner that is "no less beneficial" than three methods provided in the Proposal (*e.g.*, pro rata allocation). Furthermore, if an account has one or more balances at a promotional rate or on which interest is deferred, the Proposal would prohibit the issuer from allocating any payment in excess of the minimum payment to those balances unless others are repaid first (with a small exception relating to deferred interest balances). Finally, an issuer would not be permitted to require a consumer to pay any portion of a promotional rate or interest-deferred balance on a credit card account to receive any grace period available on other balances.

Fewer Options for Consumers, Increased Costs

The Agencies note that they understand that the Proposal will have a negative impact on the availability of promotions and the cost of credit generally. We agree. We do not believe, however, that consumers are better off if they lose low-cost credit options as a result of this Proposal. Indeed, these options tend to be key drivers in the competitive credit card marketplace. Issuers understand that their cardholders have options, including many appealing promotions enticing them to switch card issuers. If the Agencies decide to curtail these, we question whether consumers will truly benefit.

Aside from losing at least a significant amount of the breadth of promotions, consumers may also see a general increase in the cost of credit as a result of the payment

[14] The assertion in the Supplementary Information that such an opt out is not appropriate because it would not be economically rational for a consumer to keep the account is false. Indeed, as part of their discussion on this point, the Agencies recognize that the increased APR may still be the best deal the consumer can find, suggesting the consumer may prefer, as a matter of a rational economic decision, to keep the account rather than close it. Of course, there may be other entirely valid reasons why a cardholder would want to keep the account rather than have the account closed.

allocation provisions. For example, a card issuer may retain several key aspects of a promotion, but simply increase the purchase APR to make up for the lost revenue elsewhere. Or, a card issuer may simply increase the other rates applicable to an account to recover the lost revenue associated with the change in payment allocations generally.

The Agencies Do Not Adequately Support a UDAP Finding

The Agencies note that consumers pay increased interest when payments are allocated to balances with lower APRs first, or if they do not receive a grace period on purchases due to the existence of a promotional or deferred-interest balance. To support their contention that these injuries are not reasonably avoidable, the Agencies state that consumers have no control over the allocation of payments, that they do not understand payment allocation disclosures, that they do not understand the loss of grace periods in connection with promotions, and that it is unreasonable to expect a consumer to use a different credit card to make purchases than the card on which there is a promotional balances. Again, the Agencies concede that the Proposal may result in increased costs and/or fewer benefits for many consumers, but they propose that these (unmeasured) costs would be outweighed by enhanced pricing transparency.

CBA does not believe that the fact that consumers cannot control how payments are allocated is a predicate for an unfair practice, just as it would not be a justification to outlaw variable APRs due to cardholder's lack of control of the LIBOR or other index. Rather, the key is whether consumers understand payment allocation at the time they choose the product. The Agencies declare that consumers do not understand such disclosures. This topic has been the subject of litigation, among other things, and we believe the disclosures that have resulted are appropriate. If the Agencies do not believe that consumers understand payment allocation practices, we believe the more appropriate solution would be to improve disclosures. The Board, through amendments to Regulation Z, could build on the current disclosures that have been used as a result of litigation and other reasons which appear to be acceptable to many. To the extent they could be improved, we urge the Board to test additional disclosures. Finally, consumer behavior suggests that consumers do, in fact, understand how the loss of a grace period works in connection with the use of a promotional or interest-deferred offer. In fact, the Agencies clearly attempt to argue both sides of this issue by claiming that consumers do not understand how the product operates while simultaneously claiming that consumers do understand it but should not have to segregate their card usage to take advantage of the promotional rate on one card and a grace period on another.[15]

Recommendation

For the reasons stated, we believe that the Board should further consider the applicability of disclosures in this area. Although we do not believe consumers have

[15] The Agencies state that a consumer should not have to segregate card usage to preserve a grace period when taking advantage of a promotion. However, consumers are not entitled to a grace period, and the loss of a grace period in connection with the use of a credit card is obviously not an unfair practice.

difficulties today with the payment allocation/grace period concepts addressed in the Proposal, any remedies could be afforded through amendments to Regulation Z to improve disclosures.

Effective Dates

The Agencies are proposing *significant* changes to product business models, information technology requirements, and disclosure requirements. These changes would be adopted contemporaneously with the complete revision of Regulation Z. Many banks are also facing significant regulatory burdens associated with other product lines, such as mortgages. It is also not clear if the Board and the Treasury Department intend to finalize regulations pertaining to Internet gambling in the near future. In short, banks' compliance, legal, and information technology departments are going to be overwhelmed with regulatory burdens in connection with the finalization of the Proposal and other regulatory initiatives.

CBA reiterates the request made it its comments to the Board on the recent proposed amendments to Regulations Z and DD. Specifically, we ask the Agencies to provide at least two years for banks to comply with any final rule. We believe this is entirely appropriate given the scope of the regulatory changes being made and the demands that are being placed on very limited and strained bank compliance resources. We are confident that the Agencies would prefer that compliance efforts be done thoroughly, diligently, and carefully. A two-year time period is the *minimum* necessary for banks to meet those objectives.

Thank you for the opportunity to provide these comments. We would be pleased to work with the Agencies to help develop solutions to the issues we have identified in this letter.

Sincerely,

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