TOTAL CARD, INC.

August 4, 2008

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

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

Mary Rupp, Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314–3428

Re: Docket No. R–1314
OTS–2008–0004
RIN 3133–AD47
Proposed Changes to Regulation AA
Unfair or Deceptive Acts or Practices
73 *Federal Register* 28904, May 19, 2008

Dear Sir or Madam:

This letter provides comments of Total Card, Inc. concerning the Unfair or Deceptive Acts or Practices Proposed Rule (the "Proposed Rule") described above, which was published by the Board of Governors of the Federal Reserve System (the "Board"), the Office of Thrift Supervision (the "OTS"), and the National Credit Union Administration (the "NCUA") in the *Federal Register* on May 19, 2008. Our comments address the proposed prohibitions and limitations on financing fees for the issuance or availability of credit if such fees utilize the majority of available credit on the account.

Total Card, Inc. ("Total Card") is a credit card marketer and servicer located in Sioux Falls, South Dakota. Total Card also has a second processing facility in Luverne, Minnesota. Total Card has 215 employees in Sioux Falls and 92 in Luverne, for a total of 307 employees

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company wide. Total Card markets credit cards and also provides back-office services, such as application processing, customer service, transaction services, collections, settlements, and payment processing. Total Card also purchases a portion of the receivables from credit card issuers for which it provides marketing services. Total Card has been in the credit card industry since 2000 and currently services approximately 260,000 accounts.

The Board, the OTS, and the NCUA (collectively, the "Agencies") have proposed a number of new provisions intended to protect consumers against certain credit card practices that the Agencies have determined to be unfair. We support the Agencies' efforts to protect consumers against unfair or deceptive acts or practices, but we believe any rules as to the fairness of a particular practice should not be adopted until the impact of the Federal Reserve Board's recent proposed amendments to Regulation Z can be assessed. We also believe that many of the practices outlined in the Proposed Rule do not constitute unfair or deceptive acts or practices. Further, we strongly disagree with the Agencies' contention that charging a high level of up-front fees to a low limit credit card account is an unfair practice. The Agencies' assertions as to whether the practice constituted an unfair act contained only conclusory assertions as to the harm to the consumer, the avoidability of the injury, and the benefits associated with the practice in question. Further, such conclusory assertions were unsupported by any economic analysis as to the direct and indirect consequences of the proposed restrictions. With respect to this, we believe the Agencies significantly underestimated the adverse economic impact of the proposed restrictions. Finally, we believe the Agencies failed to adequately consider the costs incurred by credit card issuers to issue and maintain subprime accounts.

PROPOSED RESTRICTIONS REGARDING SECURITY DEPOSITS AND FEES FOR THE ISSUANCE OR AVAILABILITY OF CREDIT

The Proposed Rule would prohibit institutions from financing security deposits and fees for the issuance or availability of credit during the 12 months following account opening if, in the aggregate, those fees constitute more than half of the initial credit limit. The term "fees for the issuance or availability of credit" is defined to include any annual or other periodic fee, any fee based on account activity or inactivity, and any non-periodic fee that relates to opening an account. The "initial credit limit" is defined as the limit in effect when the account is opened. The Proposed Rule would also prohibit institutions from charging to the account during the first billing cycle security deposits and fees for the issuance or availability of credit that, in the aggregate, constitute more than 25% of the initial credit limit. Under the Proposed Rule, any additional security deposits and fees must be spread equally among the 11 billing cycles following the first billing cycle.

AGENCIES SHOULD GIVE THE FREE MARKETPLACE AN OPPORTUNITY TO WORK AFTER CREDITORS ARE PERMITTED TO PROVIDE ENHANCED DISCLOSURES IN SOLICITATIONS AND AT ACCOUNT OPENING

We believe that the Agencies' should wait to consider any new rules attempting to define "fairness" until the Federal Reserve Board's proposed changes to Regulation Z have been adopted, implemented, and evaluated. The proposed changes to Regulation Z will greatly enhance a consumer's understanding of the fees related to a low limit, high fee credit card account and will provide the consumer with the information necessary to make better decisions with respect to such an account. As the Agencies are aware, creditors are prohibited, for the most part, from placing any additional information in the tabular disclosures required pursuant to Regulation Z Section 226.5a(b), i.e. the so-called "Schumer box." Thus, under the current regulation, creditors cannot put the credit limit, the amount of credit after fees, or the refund policy in the Schumer box, even though these are important terms to consumers.

The proposed changes to Regulation Z will remedy this situation. As to high fee, low available limit credit cards, the revised Regulation Z provisions will require disclosure of the amount of the credit limit, the total itemized amount of all fees for the issuance or availability of credit, and the amount of available credit after such fees. Further, the newly required account opening disclosures require a disclosure informing consumers about their right to reject a plan when fees have been charged and the consumer receives the account opening disclosures but has not used the account or paid a fee after receiving a billing statement. In addition, the revisions to Regulation Z require account opening disclosures that, in addition to the refund policy, contain many of the same disclosures required in the Schumer box.

The proposed Regulation Z changes require creditors to disclose fee and credit availability information that is important to the consumer's credit decision, and which, in the past, the creditor was legally prohibited from disclosing in the prescribed segregated disclosures. Total Card believes these additional disclosures and the required formatting changes will significantly improve the consumer's ability to understand and weigh the desirability of the fees associated with a low limit, relatively high fee credit card account and will facilitate the consumer's ability to make better decisions with respect to such an account. Of equal importance, we believe the proposed Regulation Z changes are sufficient to address the various fairness concerns raised by the Agencies in the Proposed Rule.

AGENGIES FAILED TO PROPERLY CONSIDER BENEFITS OF SUBPRIME CREDIT CARDS

We believe the Agencies seriously underestimated the benefits that low limit cards provide to subprime consumers. Without any supporting economic analysis, the Agencies have decided for consumers that there is little benefit to consumers from the access to credit offered by low limit cards. We believe that if the regulators recognized and appropriately considered the benefits to be realized by consumers from low limit credit cards, the benefits of such cards to

individual consumers and the overall economy would by far outweigh any alleged injury caused by the fees imposed in connection with such cards.

In fact, the Agencies completely ignore any benefits experienced by consumers with respect to subprime credit cards. We believe that subprime credit cards are indeed valuable to individuals who do not have access to traditional forms of credit, such as immigrants, those without an established credit history or a damaged credit history, and low income individuals. In many cases low limit credit cards serve as the only tool available to assist these individuals and their families in entering the traditional credit market or in recovering from a financial emergency and restoring credit.

Despite the relatively low credit limits of subprime credit cards, the additional access to credit provided by such cards can provide vital financial assistance to consumers encountering unexpected "budget breaker" expenses (where too often the only alternative is a payday loan or incurring NSF check charges). Small credit limit accounts really address these situations. Further, low limit credit cards provide subprime consumers the convenience of plastic, allowing these consumers to participate in many of the most basic consumer transactions, including purchasing goods or services over the internet, renting a car, and booking a hotel room.

Low limit credit cards are also one of the few resources available to help subprime consumers establish or re-establish a good credit rating. It is indisputable that it takes credit to build credit. We believe nearly all banks that issue credit cards, and the subsequent purchasers of credit card accounts, consistently report cardholder performance to all of the major credit reporting agencies on a monthly basis. However, to take advantage of such reporting, cardholders must be able to both obtain a credit card and meet the payment requirements of such card.

FICO scores and VantageScores are both creditworthiness indicators used by credit card issuers in determining a consumer's repayment ability. A consumer's FICO score is an indicator of overall creditworthiness, and is based upon the consumer's payment history, amounts owed, length of credit history, new credit, and types of credit used. A consumer's VantageScore is a predictor of the likelihood that the consumer will become 90 or more days delinquent during the next 24 months.

It is universally accepted that a record of ongoing payments that are timely made in accordance with the terms of an outstanding credit relationship will result in favorable consideration under credit scoring models, a position that is readily supported by statements from the credit reporting agencies. For example, in the discussion of strategies for improving credit scores posted on its website, Experian states that "Paying your bills on time is the single most important contributor to a good credit score. Even if the debt you owe is small, it is crucial that you make payments on time." The website, "myFICO.com," operated by Fair Isaac Corporation, shows that of the five categories that go into determining a FICO score the largest single one is payment history, representing 35%. The first tip listed on the myFICO.com website for improving a FICO score is "Pay your bills on time."

It is apparent from the FICO scores categories (i.e., payment history, amounts owed, length of credit history, new credit, and types of credit used) that simply sitting on the sidelines will not improve the consumer's credit score. While the passage of time may cause negative factors to drop off the consumer's credit report, the mere passage of time will not add positive factors to the consumer's credit report. Thus, it is crucial that individuals trying to establish or re-establish their credit rating have access to credit products that they can both afford and manage.

A study of subprime accounts performed by TransUnion, one of the three major consumer reporting agencies, demonstrated that a consumer's low limit credit card can, in fact, assist the consumer in improving his or her credit score, and in turn, his or her access to additional credit.[1] The TransUnion study analyzed 365,000 accounts for the period beginning in December 2005 and ending in January 2008. One component of the study was an analysis as to the change in a cardholder's VantageScore, a predictor of the likelihood that the consumer will become 90 or more days delinquent during the next 24 months. In general, an increase in a consumer's VantageScore correlates to an increased access to credit. The study also looked at the number of new bank-issued tradelines acquired by each cardholder and the number of non-subprime promotional offers made to such cardholders within the 12-month period from January 2007 to January 2008. Both of these latter attributes are indicators of a consumer's access to traditional forms of credit with traditional pricing structures.

During the period from December 2005 to January 2008, approximately 35% of the cardholders experienced an increase in their VantageScore, while over 17% of the cardholders experienced a VantageScore increase of 40 or more points.[2] Nearly 20% of the cardholders with a subprime VantageScore in December 2005 increased their score to near-prime, prime, or super-prime by January 2008. In addition, over 11,000 cardholders who were unscoreable in December 2005 had a valid VantageScore in January 2008. These statistics illustrate that low limit, high fee credit card products provide a viable means by which consumers can improve their credit rating.

The study also showed that improved credit scores resulted in additional access to credit. Over the 12-month period from January 2007 to January 2008, 14% of the cardholders with an improved VantageScore opened at least one bank-issued credit card account with a credit limit of $1,000 to $2,499, another 14 % of the cardholders with an improved VantageScore opened at least one bank-issued credit card account with a credit limit of $2,500 or above, and over 58% of the cardholders with an improved VantageScore received at least one promotional offer of credit from a non-subprime lender. Further, of the cardholders with an improved VantageScore, 3.6% opened two or more bank-issued credit card accounts with a credit limit of $1,000 to $2,499, another 4.4% of such cardholders opened two or more bank-issued credit card accounts with a credit limit of $2,500 or above, 25% of such cardholders received between one to 10 promotional

[1] The data analyzed by TransUnion was provided by two financial institutions that issue subprime credit cards and by two companies that market and service subprime credit cards.
[2] VantageScore shifts of 40 or more points are considered significant.

offers of credit from non-subprime lenders, and 33% received 11 or more promotional offers of credit from non-subprime lenders. [3]

The foregoing illustrates the strong correlation between an improved credit rating and access to credit, especially credit on more traditional, non-subprime terms. The proposed restriction on low limit, high fee accounts will most likely significantly limit the options by which a high-credit-risk consumer can enter or re-enter the credit market and, in turn, with good performance gain access to both additional and more affordable credit.

The credit rehabilitation aspect of low limit credit cards is an important benefit and should not be discounted. Those cardholders who successfully manage their credit card accounts, thereby improving their credit score, will, going forward, be eligible for a wider range of credit products and services, at lower rates, than they were before. In 2005 the Consumer Federation of America and Fair Isaac jointly released Your Credit Scores. According to this publication, improving credit scores can help a consumer, among other things, lower his or her interest rates, speed up credit approvals and "[g]et better credit card, auto loan and mortgage offers."[4] Also, a review of the myFICO.com website demonstrating that increases in credit scores result in decreases in decreases in interest rates and monthly payments.

In discussing the importance of low limit credit cards in establishing or re-establishing a consumer's credit, Charles Steele Jr., the president and chief executive of the Southern Christian Leadership Conference, stated in a recent opinion piece in the Washington Post:

> Our government should protect every consumer—regardless of race, religion or credit score—from fraud and fly-by-night lenders. Policymakers should also promote a consumer credit market that helps people whose credit scores are less than stellar to bridge their way back to prime.
>
> Lack of access to credit for those with low credit scores, or no credit whatsoever, is an important and growing problem. Credit scores, traditionally used for mortgages and auto loans, are increasingly used in determining eligibility for employment, auto insurance, apartment rentals, utility connections, and opening and maintaining checking accounts.
>
> Like homeownership, credit is a cornerstone of wealth creation. The FDIC recently stated that "it is very difficult to build wealth with access to credit." That's an extreme understatement. It is almost impossible to build wealth in America without credit.

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[3] When the test population as a whole is considered, over the 12-month period from January 2007 to January 2008, over 10% of such cardholders opened at least one bank-issued credit card account with a credit limit of $1,000 to $2,499 and another 9% of such cardholders opened at least one bank-issued credit card account with a credit limit of $2,500 or above.

[4] Your Credit Scores, page 3.

> Dr. Martin Luther King Jr. often said that the cause of economic justice is the cause of social justice. We must continue to work together to achieve that timeless goal in lending and, more broadly, in our nation's economic sector.[5]

The American Legislative Exchange Council echoes these sentiments. In a recent article authored by the Council, it states:

> Many consumers with poor credit scores cannot obtain traditional loans and thus have little hope of moving up the economic ladder and achieving the American dream. These consumers will have a difficult time acquiring wealth because they are unable to purchase a home or take out a loan to start a business.
>
> Credit scores are used by public utilities when determining whether consumers can connect to the utility, by landlords when deciding whether to rent to a consumer, and by insurance companies when setting insurance premiums.
>
> Clearly, the use of an individual's credit score and having a good credit score have evolved to impact American consumers in more ways than just determining their creditworthiness. For these reasons, public policymakers need to understand the social and economic importance of encouraging high credit scores.[6]

For the many reasons discussed above, the Agencies should reevaluate the actual benefit to subprime consumers from the use of low limit credit card account.

AGENCIES DETERMINED HARM WITHOUT ANY EMPIRICAL SUPPORT AND DID NOT CONSIDER HIGH COSTS ASSOCIATED WITH ISSUING SUBPRIME CARDS

The Agencies' assertion as to alleged harm seems to assume that there are alternative credit products available to subprime consumers. However, it is unlikely that there are more attractive credit products available to subprime consumers or that the proposed restrictions will lead to an increase in more attractive products. As Mr. Steele stated in his recent opinion piece "[w]hile one might hope that capping fees for sub-prime credit products would result in better credit terms for borrowers, it is more likely that many issuers will cut back on offerings or simply exit the market."[7] Furthermore, if the proposed restriction on fees is adopted, there are unfortunately a vast number of unregulated lenders who would be more than willing to step in and meet the credit needs of the subprime population, including payday lenders, unregulated loan companies, internet-based lenders, pawnshops, and even private individuals payday offering loans over the internet.

[5] Charles Steele, Jr., *The Color of Credit*, Washington Post, June 23, 2008, at A15.
[6] American Legislative Exchange Council, *Access to Credit Means Access to the American Dream*, The State Factor, July, 2008, at 1 (hereinafter "Access to Credit").
[7] *The Color of Credit* at A15.

It is also unlikely that many subprime consumers who can pay up-front fees when such fees are charged to the card and spread over a longer period could afford to pay such fees at the time of account opening. As Mr. Steele stated: "Because an ability to pay over time makes such cards affordable for many consumers, the provision would effectively deny credit to million of those whose rights such reforms are meant to protect."[8]

The analysis also ignores the high cost to card issuers of issuing and servicing subprime credit card accounts. Low limit credit cards are simply more expensive than prime credit cards to issue and maintain. These increased expenses include higher reserve requirements and higher operational expenses. The reserve for loan losses is substantially higher for a subprime portfolio. A subprime credit card portfolio, however, will generally establish a loan loss reserve of 30% to 50% of its loans which is much higher than the 3% to 6% loan loss usually established in connection with a prime credit card portfolio. The greatest risk is the first time default user who obtains a credit card, uses substantially all available credit, and never makes a payment. The Proposed Rules would promote this abuse by some consumers, further driving up the cost of credit for all consumers.

Low limit credit cards are also much more expensive to maintain. We estimate that our costs for each subprime account average $16 for marketing and origination, $5.50 per month for servicing, $2.25 per month for processing. Further, the cost of funding for each charged-off account is estimated to be $46.

AGENCIES DID NOT PROVIDE SUPPORTING ECONOMIC ANALYSIS AND UNDERESTIMATED THE ADVERSE IMPACT OF PROPOSAL ON CONSUMERS AND THE ECONOMY

The proposed limitation on up-front fees charged in connection with a subprime credit card will have serious adverse economic consequences for high-credit-risk consumers. The inability to access credit could severely limit the ability of such consumers to withstand any additional downturn in the economy or their personal financial situation. Although the Agencies appear to acknowledge that the proposed limitations will result in decreased credit availability for subprime consumers, the Agencies have apparently conducted no analysis as to the true impact of such limitations on individual consumers or on the economy as a whole.

Only the OTS mentioned the number of impacted consumers, commenting that "[s]ubprime credit cards represent just 5% of all credit cards issued." The reality is, however, that the subprime credit card market is comprised of almost 13 million consumers,[9] and the proposed limitations are likely to have a significant negative impact on these consumers.

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[8] Id. (referring to up-front fee restrictions in the Credit Cardholders' Bill of Rights Act (HR 5244)).

[9] Source: Experian National Consumer Database (Orion File), June 2008. Some place the estimate of subprime consumers much higher. See, e.g., "Access to Credit," in which the American Legislative Exchange Council estimates there could be as many as 91 million adult Americans classified as sub-prime in 2006.

In addition, the effect of the proposed limitations will go well beyond subprime consumers. The diminished access to credit by subprime consumers will curb consumer spending by this segment of the economy. This diminished consumer liquidity and resulting decreased spending will impact not only those consumers whose access to credit has been curtailed, but also the various merchants and individuals with whom such consumers would have conducted credit transactions, which merchants and individuals will then have fewer dollars to spend, and so on. Thus, adoption of the proposed limitations is likely to adversely affect the entire economy.

Oppenheimer & Co., Inc. ("Oppenheimer"), an investment firm, in its Industry Update on U.S. Banks paints a grim picture of the probable effect of the Proposed Rule on an economy already destabilized by the issues in the securitization market. Oppenheimer states:

> However, we argue the far more important consequence of the "buyers strike" in the securitization market is the impact on overall consumer liquidity, consumer spending, and ultimately on consumer defaults. Herein, we tie a direct correlation between spiking loan losses and last summer's shutdown in the securitization markets.
>
> . . . .
>
> We estimate that the "buyers strike" in the securitization market has created considerable stress for consumer liquidity. So far, $1.4 trillion of liquidity has been extracted from the capital markets, and by year-end, we expect over $3 trillion of liquidity to be expunged. This continues to wreak havoc on consumer losses and bank earnings, and we believe the effects have only begun to be seen. In fact, we believe new and unforeseen strains on consumer liquidity will push more consumers into precarious credit positions and cause consumer credit losses to be far worse than what is currently estimated, even by the most draconian estimates.[10]

In discussing the Regulation AA proposal, the Oppenheimer report states:

> We believe the entire credit card industry is about to face a "game changing" regulatory environment in which the current economics of the business will decline to such levels that lenders will ultimately choose to provide credit lines to far fewer customers. In fact, we expect that ultimately greater than $2 trillion of credit card lines will be reduced, lowering the total available credit to U.S. consumers by more than 45 percent.
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> . . . .

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[10] Oppenheimer, "Proposal on Unfair and Deceptive Practices," Industry Update, 2-3 (May 2008).

> [W]e believe a clear "unintended" consequence will be higher borrowing rates and less credit available to consumers. Without a doubt, we believe the profitability of credit card lending will decline meaningfully, but we also believe lower liquidity will drive higher consumer defaults across all consumer loan product buckets.[11]

The foregoing suggests that while the Agencies appear unconcerned about the economic impact of the Proposed Rule's restrictions, industry analysts predict that the adverse impact of such restrictions will be quite severe.

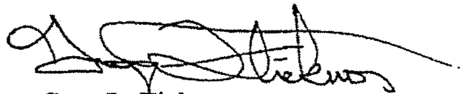
Because millions of consumers will experience a direct negative impact due to the proposed limitations on charging fees to a credit card account, and because the impact to the overall economy could be dire, we believe the Agencies must conduct further research as to the true costs of the proposed restrictions before adopting and implementing such restrictions.

CLOSING

In closing, Total Card would like to commend the Agencies in their efforts to address fairness concerns with respect to credit card products. However, we strongly disagree with the proposed prohibitions and limitations on financing fees for the issuance or availability of credit if such fees utilize the majority of available credit on the account. We believe the Agencies should first give the Federal Reserve Board's recent amendments to Regulation Z's credit card disclosure requirements an opportunity to work in the marketplace. Only then should further consideration be given to whether particular practices are unfair. Then when considering limitations on low limit, relatively high fee cards, it is imperative that the Agencies appropriately assess the benefits, costs, and alternatives to such cards. Further, this assessment must include an analysis as to the economic impact of the proposed restriction on both individual consumers and the economy as a whole.

Total Card appreciates the opportunity to comment on the Proposed Rule, and thanks you for your consideration of our comments.

Sincerely,



Greg L. Ticknor
President & CEO

[11] Id. at 11.