Comments of the

National Consumer Law Center
(On behalf of its Low-Income Clients)
and
Center for Consumer Affairs - Univ. of Wisconsin-Milwaukee
Consumer Federation of America
Consumers Union
Demos: A Network for Ideas and Action
National Association of Consumer Advocates
U.S. Public Interest Research Group
Woodstock Institute

Regarding

Advance Notice of Proposed Rulemaking
Review of the
Open-End (Revolving) Credit Rules of Regulation Z

Federal Reserve System
12 CFR Part 226

Docket No. R-1217

These comments are submitted by the National Consumer Law Center (on behalf of its low income clients),[1] the Center for Consumer Affairs,[2] Consumer Federation of America,[3] Consumers Union,[4] Dēmos: A Network for Ideas and Action,[5] the National

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[1] The **National Consumer Law Center**, **Inc. (NCLC)** is a non-profit Massachusetts corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes a series of sixteen practice treatises and annual supplements on consumer credit laws, including Truth In Lending, (5th ed. 2003) and Cost of Credit (2nd ed. 2000) and Repossessions and Foreclosures (5th ed. 2002) as well as bimonthly newsletters on a range of topics related to consumer credit issues and low-income consumers. NCLC attorneys have written and advocated extensively on all aspects of consumer law affecting low income people, conducted training for tens of thousands of legal services and private attorneys on the law and litigation strategies to deal predatory lending and other consumer law problems, and provided extensive oral and written testimony to numerous Congressional committees on these topics. NCLC's attorneys have been closely involved with the enactment of the all federal laws affecting consumer credit since the 1970s, and regularly provide comprehensive comments to the federal agencies on the regulations under these laws. These comments are written by Carolyn Carter, Elizabeth Renuart, Margot Saunders, and Chi Chi Wu, except as noted in Section II.B.

[2] The **Center for Consumer Affairs** is part of the School of Continuing Education at the University of Wisconsin in Milwaukee. Professor James Brown, director of the Center for Consumer Affairs, is the primary author of Section II.B. of these comments.
[3] The **Consumer Federation of America** is a non-profit association of 300 organizations that, since 1968, has sought to advance the consumer interest through research, advocacy and education.

Association of Consumer Advocates,[6] the U.S. Public Research Interest Group,[7] the Woodstock Institute,[8] Diane Thompson,[9] and Sheila Canavan.[10] These national organizations and individuals collectively represent a broad swath of American low and middle income consumers.

We welcome the Board's thorough review of the Truth in Lending Act ("the TILA") rules applicable to open-end credit as this federal law essentially applies the only restraints on the financial services industry in the open-end credit relationship with consumers. We encourage the Board to take its mandate – "to protect consumers against inaccurate and unfair credit bill and credit card practices"[11] – seriously and propose meaningful changes to the TILA regulations, as well as recommend to Congress significant changes in federal law to protect consumers from the escalating abusive practices of the credit card industry.

It is incumbent on the Board to recognize the unique position it has at this crossroads for consumer protection. The virtually unregulated credit card industry – responsible for the $730 billion in credit card debt owed by American households – must be reined in. The amount of credit card debt juggled by a majority of American households has exploded in the past decade – much of it fueled by business practices that are often deceptive and abusive.

The Board has a variety of choices. One – perhaps the easiest – would be to simply tweak the TILA regulations for open-end credit, essentially maintaining the current uneven playing field between a giant, well financed credit industry and individual consumers. Two – as is our objective – the Board could make serious changes in the regulations as currently permitted by the TILA to provide some balance to the regulatory structure, as well as encourage Congress to make more significant changes to federal law

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[4] **Consumers Union**, the nonprofit publisher of Consumer Reports magazine, is an organization created to provide consumers with information, education and counsel about goods, services, health, and personal finance; and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers. Consumers Union's income is solely derived from the sale of Consumer Reports, its other publications and from noncommercial contributions, grants and fees. Consumers Union's publications carry no advertising and receive no commercial support.

[5] **Dēmos** is a non-partisan, national public policy organization based in New York. Our work centers on expanding economic opportunity and creating a more robust democracy.

[6] The **National Association of Consumer Advocates (NACA)** is a non-profit corporation whose members are private and public sector attorneys, legal services attorneys, law professors, and law students, whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers.

[7] The **U.S. Public Interest Research Group** is the national lobbying office for state PIRGs, which are non-profit, non-partisan consumer advocacy groups with half a million citizen members around the country.

[8] The **Woodstock Institute** is a Chicago-based nonprofit research organization dedicated to promoting community reinvestment, credit access, and sound financial services among lower-income and minority neighborhoods both locally and nationally. For over thirty years, Woodstock has supported legislation and regulation in the best interest of low-income consumers. Woodstock also convenes the Chicago CRA Coalition, a group of nearly 100 area organizations with an interest in promoting reinvestment in underserved communities.

[9] Member of the Consumer Advisory Council to the Federal Reserve Board.

[10] Member of the Consumer Advisory Council to the Federal Reserve Board.

[11] 15 U.S.C. § 1601(a).

to protect individual consumers, facilitate the reduction in debt in overburdened households, and increase family savings. Three, the Board could bow to heavy pressures from the consumer credit industry and make an already intolerable situation for American consumers much worse, by reducing open-end protections under TILA.

It is our goal in these comments to convince the Board to take the high road. We hope that the Board will seize this opportunity to push the envelope on regulatory changes under TILA's open-end rules and comprehensively propose disclosure reforms that recognize TILA's unique control over open-end credit in this nation as well as the fact that consumers need the Board to exercise this control in a much more proactive way. We also urge the Board to accompany these regulatory changes with strong encouragement to Congress to pass substantive federal legislation that will protect American consumers from the increasingly unfair, abusive, and virtually unavoidable practices of the credit card industry. Given the preemption of state laws applicable to open-end credit provided by most financial institutions, and the huge difference in bargaining power between consumers and the credit card industry, even perfect disclosures will not adequately protect consumers.

In these comments, we intend to accomplish several objectives. First, we will build a case for significant improvement to all of the rules applicable to open-end credit. Second, we outline the improvements to federal law that we hope that the Board will recommend to Congress to provide substantive protections to consumers. Third, we recommend a series of specific and necessary changes to the TILA's regulations to address *some of* the extensive problems we describe. In this process we will answer the questions posed in the ANPR. These comments are organized into the following sections:

I. Substantive Problems Caused by the Credit Card Industry and the Need for New Substantive Protections.

A. Escalating Credit Card Debt is Hurting Consumers
1. Escalating Debt Loads Are Caused By Industry Practices
2. Six-Year Struggle to Repay Debt – A Story of Unending Fees
3. Credit Card Companies Enjoy Growing Profits

B. Abuses by Credit Card Companies Are Proliferating (Q 26, Qs 35-36, Q 51)
1. Punitive Junk Fees
2. Other Abusive Practices
3. Change-In-Terms

C. The System is Broken and Improved Disclosures Will Not Address the Problems

D. Recommendations for Statutory Reform (Q 56)

II. Regulatory Reforms of Truth In Lending Disclosures

A. The Inclusive Finance Charge Definition in the Act Should Be Retained and the Board Should Revise Regulation Z to Reflect Congressional Intent in Order to Address Marketplace Problems (Qs 13-20)

1. Broad Scope of the Finance Charge Definition in TILA
2. The Importance of the Finance Charge Disclosure and the Related APR as the Core Disclosures Under TILA
3. The Purposes of the Truth in Lending Act, the Finance Charge Definition, and the APR Disclosure
4. Current Market Conditions and Consumer Troubles
5. The Proliferation of Exceptions to the Finance Charge for Open-End Credit
6. Categories of Fees and Their Effects on Disclosure and the APR
7. The Board Endorsed a Highly Inclusive Definition of the Finance Charge in 1998
8. The Current Finance Charge Definition Should Guide the Board in its Decisions
9. Suggested Breakdown of Credit Card Fees into "Finance" and "Other" Charges

B. Over-Limit Fees are Finance Charges and Should Be Treated as Such (Qs 21-22)

C. A Typical Effective APR Should be Disclosed in Solicitations and at Account Opening; The Actual Effective APR Should be Disclosed on Periodic Statements (Qs 23-25)

D. The Board Should Reverse the Gaping Hole in the Finance Charge Definition Created By Its Application of the "Comparable Cash Transaction" Exclusion

E. The Board Should Require a Clear and Uniform Schumer Box in Applications/Solicitations, Initial Disclosures, Periodic Statements, and Change-of-terms Notices. (Qs 2-3, Qs 6-11, Q 24, Qs 29-30)

1. The Manner of Making Disclosures Must be Improved
2. Rationale for Using A Revised Uniform Schumer Box
3. Our Proposed Schumer Box
4. The Schumer Box Should Include Those Terms Most Important for Credit Shopping
5. Other Information Should be Disclosed Immediately After, But Not In, the Schumer Box
6. Regulation Z's Requirements for the Format and Language of Disclosures Should be More Specific
7. Responses to ANPR Questions

F. Exemptions and Tolerances (Q 37, Q 41, Q 53)
1. The Board Should Not Exempt Any Transactions Under § 1604(a) or (f)
2. The Board Should Not Exempt Transactions for Persons with Income and Assets Over Specified Amounts
3. The Board Should Clarify the Scope of State Exemptions
4. The Board Should Not Adopt Tolerances for Open-End Credit
5. The Board Should Seek Legislative Authority to Adjust All Numerical Figures in the TILA

III. Next Generation and Special Product Issues

A. Electronic Disclosures: The Interim Rule Should Be Amended to Comply with E-Sign

B. Subprime and Secured Credit Cards (Q 39, Q 43, Q 56)

IV. Fair Credit Billing Act & Special Credit Card Substantive Protections

A. The Definition of "Cardholder" Should Include Identity Theft Victims

B. Regulation Z Should be Amended to Protect Telemarketing and Internet Fraud Victims

C. Next Generation Credit Cards (Q 44)

D. Regulation Z Should Affirm That Various Rights Do Not Depend Upon Sending a Billing Error Notice

E. Increasing the Penalties for Fair Credit Billing Act Violations (Q 56)

V. Other Issues

A. The Staff Should Not Provide Informal Guidance on the TILA's Application (Q 52)

B. The Board Should Not "Federalize" the Definition of "Refinancing" (Q 58)

VI. The Cost To Implement An Amended Disclosure Regime Is Not Prohibitive (Q 38)

I. SUBSTANTIVE PROBLEMS WITH THE CREDIT CARD INDUSTRY AND THE NEED FOR REFORM IN THE LAW.

A. Escalating Credit Card Debt Is Hurting Consumers

As the Board is well aware, the use of open-end credit is pervasive in American society. Credit cards have become an increasingly integral part of our lives. Three-quarters of all households have at least one credit card, and over half of cardholders carry credit card debt from month to month.[12] There are now almost 1.5 billion cards in circulation – over a dozen credit cards for every household in the country.[13] The amount of credit card debt outstanding at the end of 2004 was $796 billion,[14] over three times as much as in 1993.[15]

While the explosion of credit card debt has fueled the U.S. economy,[16] it has had devastating impacts on millions of American consumers. Americans across all but the lowest income levels have experienced dramatically increased credit card debt in the past ten years:

- Between 1989 and 2001 credit card debt in America almost tripled from $238 billion to $692 billion. Worse, the savings rate steadily declined and the number of personal bankruptcies filed climbed 125%.[17]
- Credit card debt among older Americans with incomes under $50,000 (70 percent of seniors) has also increased. About one in five older families with credit card debt is in debt hardship -- spending over 40 percent of their income on debt payments, including mortgage debt**.**[18]
- The average credit card debt among young adults increased by 55% between 1992 and 2001 to $4,088 dollars, and these households now spend nearly 24% of their income on debt payments. In fact, among these young households with incomes

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[12] Ana M. Aizcorbe, Arthur B. Kennickell, & Kevin B. Moore, *Recent Changes in U.S. Family Finances: Evidence from the 1998 and 2001 Survey of Consumer Finances,* Fed. Res. Bull. at 25 (Jan. 2003), *available at* http://www.federalreserve.gov/pubs/bulletin/2003/0103lead.pdf .

[13] U.S. Census Bureau, Statistical Abstract of the United States: 2003 at 751, *No. 1190*: *Credit Cards – Holders, Numbers, Spending, and Debt, 1990 and 2000, and Projects, 2005*, *available at* http://www.census.gov/prod/2004pubs/03statab/banking.pdf; U.S. Bureau of the Census, *Projections of the Number of Households and Families in the United States: 1995 to 2010* at 9 (1996), *available at* http://www.census.gov/prod/1/pop/p25-1129.pdf (projecting 108.8 million households by 2005).

[14] http://www.federalreserve.gov/releases/g19/Current/**;** *See also***,** Consumer Federation of America, *Credit Card Issuers Expand Marketing and Available Credit, Consumers Increasingly Say No*, (2002) (citing data from the Federal Reserve Board and Veribanc, Inc.), *available at http://www.consumerfed.org/081492bankruptcy_credit_card_report_02_2.html.*

[15] Office of the Comptroller of the Currency, Advisory Ltr., 96-7 (Sept. 26, 1996), *available at* http://www.occ.gov/ftp/advisory/96-7.txt; FDIC Quarterly Banking Profile Graph Book (Dec. 31, 1997), *available at* http://www2.fdic.gov/qbp/1997dec/grbook/QBPGR.pdf.

[16] Patrick McGeehan, *Plastic Trap—Debt That Binds: Soaring Interest Compounds Credit Card Pain for Millions*, N.Y. Times, Nov. 21, 2004.

[17] Tamara Draut & Javier Silva, *Borrowing to Make Ends Meet; The Growth of Credit Card Debt in the 1990s* (Sept. 18, 2003), *available at* http://www.demos-usa.org/pubs/borrowing_to_make_ends_meet.pdf.

[18] Heather G. McGee & Tamara Draut, *Retiring in the Red: The Growth of Debt Among Older Americans* (Jan. 19, 2004), *available at* http://www.demos-usa.org/pub101.cfm.

below $50,000, nearly one in five with credit card debt is in debt hardship – spending over 40% of their income servicing debt (including mortgages and student loans).[19]

- The average credit card-indebted family between 55 and 64 now spends one third of their income on debt payments, a 10 percentage point increase over the decade.[20]

The negative consequences of this escalating mountain of debt on individual consumers as well as the American economy cannot be minimized. Personal bankruptcy rates increasing on an annual basis,[21] and families become destabilized due to the financial pressures.[22]

1. *Escalating Debt Loads Are Caused By Industry Practices*

A significant amount of the debt load facing American households is caused not so much by consumer borrowing, but by the harsh – and exorbitantly expensive – tactics of the credit card industry. We hear frequently from attorneys representing consumers who are struggling to "do the honorable thing" and meet their obligations and pay their creditors, yet most consumers in debt trouble fail to appreciate that credit card companies **will not take steps to facilitate the pay off of these debts. These issuers often act as if they intend to keep consumers on this treadmill of debt, paying fees and charges, for as long as possible.** Credit card debt has caught millions of households in a trap they simply cannot extricate themselves from without feeling the pressure to file bankruptcy.

Credit card companies make huge profits even on consumers who file bankruptcy. Consider a case about a consumer from Cleveland, Ohio who did play by the rules, but who was driven hopelessly into default by her credit card company.

2. *Six-Year Struggle to Repay Debt – A Story of Unending Fees*

In May 1997, Ruth Owens stopped using her credit card, made no further purchases or cash advances, and tried to pay off her debt to Discover Bank. At that time, she owed $1,963. Over the next six years, Ms. Owens made $3,492 in payments to Discover Bank. One might assume this was enough to pay off her debt. After all, if Ms. Owens had made the same payments on a $2,000 loan with interest at 21% annual percentage rate (the usury limit in many states), her debt would be paid off.

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[19] Tamara Draut & Javier Silva, *The Growth of Debt Among Young Americans* (Oct. 2004), *available at* http://www.demos-usa.org/pub295.cfm.

[20] Tamara Draut & Heather G. McGee, *Retiring in the Red: The Growth of Debt Among Older Americans* (Jan. 19, 2004), *available at* http://www.demos-usa.org/pub101.cfm.

[21] The number of personal bankruptcy filings has increased steadily since TILA was enacted in 1968, reaching 1,624,272 in 2004. Administrative Office of the U.S. Courts News Release, Number of Bankruptcy Cases Filed in Federal Courts Down Less Than One Percent (Aug. 27, 2004), *available at* http://www.uscourts.gov/Press_Releases/june04bk.pdf. Personal bankruptcy filings declined by a small number, 13,111, between 2003 and 2004

[22] *See* Elizabeth Warren & Amelia Warren Tyagi, *The Two-Income Trap* (Basic Books 2003).

From May 1997 until her account was sent for collection in May 2003, not one penny of Ms. Owens' $3,492 in payments went to reduce her debt. During this time, Discover Bank charged Ms. Owens various fees that consumed all of her payments and caused her debt to grow even larger. The following fees and interest were charged to Ms. Owens' account:

Fees and Interest

Item	Amount
Over-limit Fees	$ 1,518.00
Late Fees	$ 1,160.00
Credit Insurance (CreditSafe)[23]	$ 369.62
Interest and Other Fees	$ 6,008.66
Total	$ 9,056.28

So despite having received substantial payments for six years from Ms. Owens (all that she could really afford), Discover Bank claimed that she still owed $5,564 when it filed a collection lawsuit against her in an Ohio court. ***In other words, after having paid $3,492 on a $1,963 debt, Ms. Owens' balance grew to $5,564.***

Card companies make huge profits off customers like Ms. Owens. Rather than work with these consumers to reduce their debt by curbing the excess fees and interest, card companies prefer to get as much out of consumers for as long as possible until they eventually stop paying or file bankruptcy.

In this case, Ms. Owens would have been far better off if she simply stopped paying Discover Bank years earlier and had them sue her in state court. If Discover Bank had obtained a court judgment for $2,000, all of the card fees and high-rate interest would have stopped and Discover would have then been entitled to 10% or less interest per year under Ohio law. Rather than have her debt increase, Ms. Owens' payments would have paid off the debt in full in approximately 4 years.

When Discover Card sued Ms. Owens in state court, she submitted the following handwritten statement to the court:

> *I would like to inform you that I have no money to make payments. I am on Social Security Disability. After paying my monthly utilities, there is no money left except little food money and sometimes it isn't enough. If my situation was different I would pay. I just don't have it. I'm sorry.*

[23] Like many card customers, Ms. Owens was being charged for one of the numerous insurance-like products sold by card companies. Often, these products are sold through high-pressure telemarketing sales. In this case, Ms. Owens was charged approximately $10 per month for a Discover card product called CreditSafe Plus, which apparently provided for a suspension of payments and finance charges if Ms. Owens became unemployed, hospitalized, or disabled. Since Ms. Owens was already on Social Security Disability and unemployed, the CreditSafe product presumably would apply only if she became hospitalized. Ms. Owens was no doubt paying for a product that would likely never benefit her.

The Ohio judge assigned to the collection case rightly found that Ms. Owens was not a deadbeat. He stated that her *"instincts were always that she wanted to plug away at meeting her financial obligations. While clearly placing her on the moral high road, that same highway unfortunately was her road to financial ruin. How is it that the person who wants to do right ends up so worse off? It is plain to the court that the creditor also bears some responsibility."*[24]

In barring Discover Card from collecting any more money from Ms. Owens, the Ohio judge stated: *"This court is all too aware of the widespread financial exploitation of the urban poor by overbearing credit-card companies. [Ms. Owens] has clearly been the victim of plaintiff's unreasonable, unconscionable and unjust business practices."*[25]

3. *Credit Card Companies Enjoy Growing Profits*

Credit card earnings have been consistently higher than returns on all commercial bank activities.[26] According to a Board Report, profitability increases reached 13.7% in 2003 when the credit card banks included in the sample were held constant.[27] When the cost of funds declines for the banks, the profit margins stay high; when the cost of funds increases, these expenses are passed along to consumers. Even when all other economic indicators are problematic, credit card companies experience increased profits.[28] We have no complaint about the fact that these companies are making huge profits – our concern is

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[24] Discover Bank v. Owens, 822 N.E.2d 869 (Ohio Mun. 2004).

[25] Another example is the bankruptcy case of Josephine McCarthy from the Eastern District of Virginia (*In re* McCarthy, No. 04-10493-SSM (Bankr. E.D. Va. filed July 14, 2004)), which also illustrates how consumers are routinely subjected to compounding fees and escalating interest charges, combined with unilateral changes to the terms of credit, and other abusive practices. The exhibits to the decision include two accounts the debtor had with one credit card company.

On one account, the debtor made $3,058 in payments over a two year period during which her balance on the account increased from $4,888 to $5,357. She had made only made only $218.16 (net of store credit) in purchases during this time. All of her payments went to pay finance charges (at a 29.99% interest rate), late charges, over-limit fees, bad check fees, and phone payment fees. On the other card, she made $2,008 in payments over the same period and the account balance increased from $2,020.90 to $2,607.66. This time she made all of $203.06 in purchases.

	Total Payments	Purchases	Balance *Increase*	**Total Interest and Fees** in 2 year period[25]
Account 1	$3,058.00	$218.16	$469.00	**$3,308.84**
Account 2	$2008.00	$203.06	$586.76	**$2,391.79**

In re Josephine McCarthy, No. 04-10493-SSM (Bankr. E.D. Va. filed 2004).

[26] Board of Governors of the Federal Reserve System, *The Profitability of Credit Card Operations of Depository Institutions* (June 2004), *available at* http://www.federalreserve.gov/boarddocs/rptcongress/creditcard/2004/ccprofit.pdf. While the profitability of the credit card industry as a whole has fluctuated somewhat over these years, this is largely due to the changeability of the group of banks included in the sample. *Id.* at 2.

[27] *Id.*at 3.

[28] Lavonne Kuykendall, *Review 2004: Card Lenders Earned More Despite Weak Portfolio Growth*, American Banker (Jan. 3, 2005).

simply that these profits are based on abusive practices, and in the process American households are being seriously harmed. *The root of these problems is that open-end credit in this nation is now completely unregulated – and this must change.*

B. Abuses by Credit Card Companies Are Proliferating

Credit card abuses are not limited to one or a handful of practices. Instead, card issuers have devised a myriad of schemes and traps to squeeze every last penny out of consumers, particularly consumers who are carrying heavy debt loads or beginning to exhibit signs of financial distress. Furthermore, it is not just one or a handful of credit card companies that engage in abusive practices, but a great number of the top ten credit card issuers.[29] It is this pattern of heavy-handed and manipulative conduct by an entire industry that shows that credit card issuers have altered their fundamental treatment of consumers from a fair, respectful business relationship to an abusive, exploitative one.

Credit card companies were not always so free to engage in reprehensible behavior. Credit card deregulation, and the concomitant spiraling credit card debt of Americans, began in 1978, with the Supreme Court's decision in *Marquette National Bank of Minneapolis v. First of Omaha Service Corp.*[30] This case gave national banks the green light to take the most favored lender status from their home state across state lines, and preempt the law of the borrower's home state.[31] As a result, national banks and other depositories established their headquarters in states that eliminated or raised their usury limits, giving them free rein to charge whatever interest rate they wanted.[32] Therein lies the reason why so many of those credit card solicitations sent by mail every week come from Delaware or South Dakota: credit card issuers moved there to export those

[29] For example, *see* information about the civil penalties assessed against Providian and other issuers, http://www.pirg.org/consumer/bankrupt/bankrupt2.htm; and the recent suit initiated against Capital One by the state of Minnesota, http://www.ag.state.mn.us/consumer/PR/PR_041230CapitalOneBank_FSB.htm

[30] Marquette Nat'l Bank of Minn. v. First of Omaha Serv. Corp., 439 U.S. 299, 99 S. Ct. 540, 58 L. Ed. 2d 534 (1978).

[31] It is worth noting that there was no interstate banking when the National Bank Act was passed.

[32] Other depository institutions obtained the same most favored lender status when Congress enacted § 521 of the Depository Institutions Deregulation and Monetary Control Act of 1980 (codified at 12 U.S.C. § 1831d).

unregulated states' *lack* of consumer protections nationwide.[33] As of 1978, credit card debt had grown to $50 billion, up from just $5.3 billion when the TILA was passed.[34]

1. ***Punitive Junk Fees***

A significant contributor to the snowballing credit card debt of American consumers is the enormous increase in both the number and amount of non- periodic interest fees charged by credit card issuers. These "junk" fees include both fees considered to be finance charges (cash advance, balance transfer, wire transfer fees) and non-finance charge "other" fees. Most important among the latter are late payment and over-limit fees. See Chart 1 showing the increase in fee income from these two fees alone. Credit card issuers have made these fees higher in amount, impose them more quickly, and assess them more often.

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[33] South Dakota and Delaware, at the beginning of the explosive growth of the financial services industry around 1980, sought to attract that industry as part of their economic development strategy. They wanted to "provide [their] citizens with the jobs and benefits a large national credit card operation can provide (attracted by the ability to export limitless credit card rates to other states)," while, it should be noted, protecting their local banks from competition with the exporting banks. Indep. Cmty. Bankers' Ass'n of S.D. v. Board of Governors, Federal Reserve Sys., 838 F.2d 969, 975 (8th Cir. 1988). *Cf.* Richard Eckman, *Recent Usury Law Developments*: *The Delaware Consumer Credit Bank Act and Exporting Interest Under § 521 of the Depository Institutions Deregulation and Monetary Control Act of 1980*, 39 Bus. Law. 1251, 1264 (1984).

It worked, too. South Dakota's tax revenue from banks went from $3.2 million in 1980 to almost $27.2 million in 1987, with the comparable figures for Delaware rising from $2.4 million to almost $40 million. The Economist, July 2, 1988, at 26.

[34] Diane Ellis, *The Effect of Consumer Interest Rate Deregulation on Credit Card Volumes, Charge-Offs, and in the Personal Bankruptcy Rate,* FDIC--Division of Insurance, Bank Trends, 98-05 (Mar. 1998), *available at* http://www.fdic.gov/bank/analytical/bank/bt_9805.html.

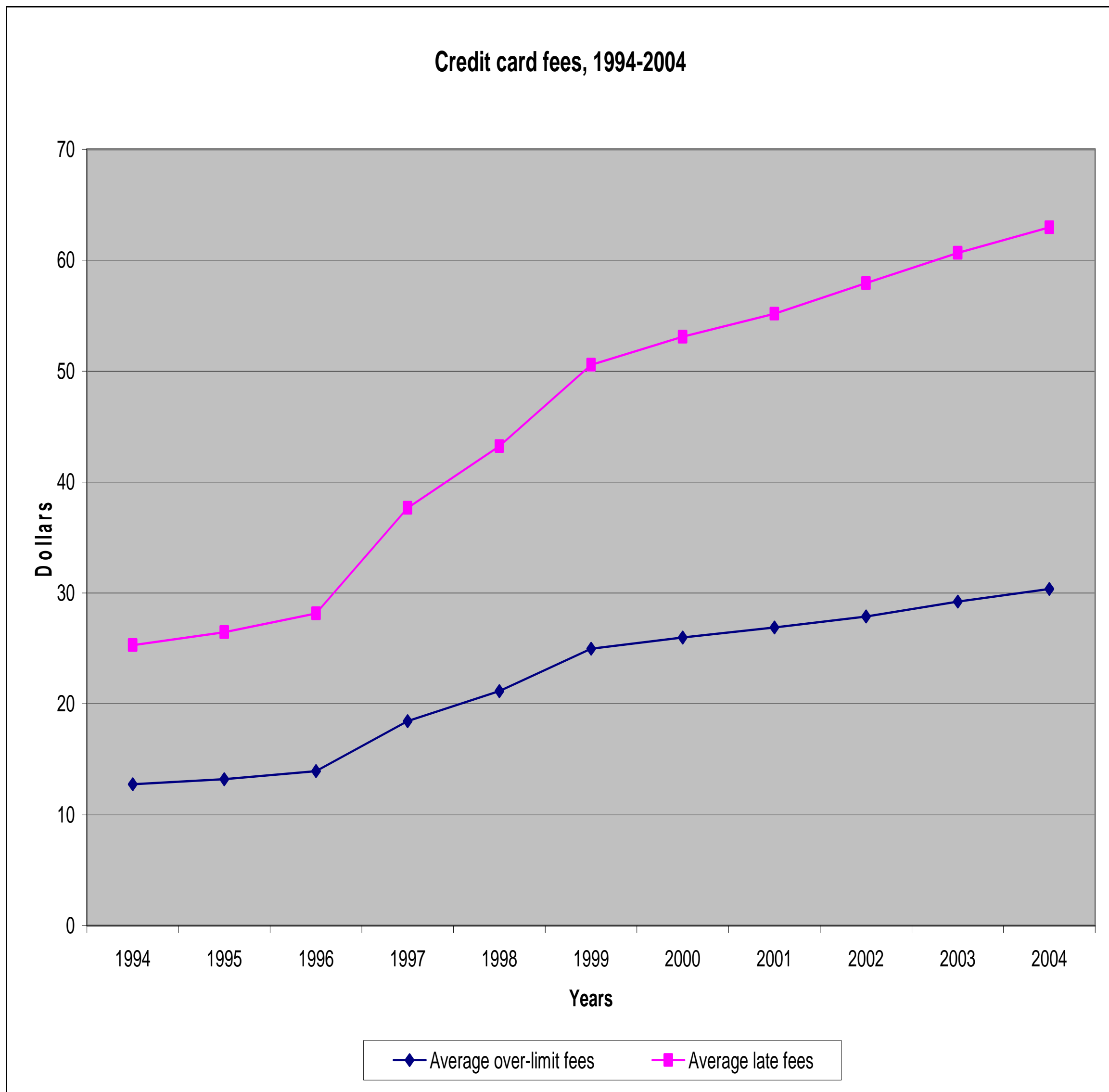

Chart 1

Sources: "Over-limit Fees" (2 February 2005). The U.S. Payment Card Information Network Website. Friday, March 4, 2005. http://www.cardweb.com/cardtrak/news/2005/february/2a.html, "Late Fees" (28 January 2005). The U.S. Payment Card Information Network Website. Friday, March 4, 2005. http://www.cardweb.com/cardtrak/news/2005/january/28a.html.

From 1978 to 1995, credit card debt increased six-fold to $378 billion.[35] In 1996, the Supreme Court paved the way for credit card banks to increase their income stream even more dramatically. In *Smiley v. Citibank (South Dakota), N.A.*, the court approved of the Office of Comptroller of Currency's definition of interest that included a number of credit card charges, such as late payment, over-limit, cash advance, returned check, annual, and membership fees.[36] As a result, national banks and other depositories can charge fees in any amount to their customers as long as their home-state laws permit the fees and so long as the fees are "interest" under the Office of the Comptroller of the

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[35] *See,* Fed. Res. Bull., *available at* http://www.federalreserve.gov/releases/g19/hist/cc_hist_mt.txt.
[36] Smiley v. Citibank (S.D.), Nat'l Assn., 517 U.S. 735, 116 S. Ct. 1730, 135 L. Ed. 2d 25 (1996). The OCC definition of interest is found in 12 C.F.R. § 7.4001(a).

Currency ("OCC") definition. Uncapping the amount of fees that credit card banks can charge nationwide has resulted in the rapid growth of and reliance on fee income by credit card issuers.

After *Smiley*, banks rushed to increase late charges, over-limit fees, and other charges. The average late payment fee has soared from $14 in 1996 to over $32 in 2004.[37] Over-limit fees have similarly jumped from $14 in 1996 to over $30 in 2004.[38]

Now banks impose these fees, not as a way to curb undesirable behavior from consumers – which used to be the primary justification for imposing high penalties – but as a significant source of revenue for the bank. Since *Smiley*, penalty fee revenue has increased nearly nine-fold from $1.7 billion in 1996 to $14.8 billion in 2004.[39] The income from just three fees – penalty fees, cash advance fees and annual fees – reached $24.4 billion in 2004,[40] Fee income topped $30 billion if balance transfer fees, foreign exchange, and other fees are added to this total.[41] Concurrently, card issuer profits, though declining somewhat between 1995 to 1998, have steadily increased between 1999 and 2004. These profits rose from 3.1% in 1999 to 4.5% in 2004.[42]

Not only has the size of fee income for credit card issuers grown enormously, the types of fees have mushroomed as well. The Board provides a list of fees to consumers in a brochure titled "Choosing a Credit Card."[43] The most common fees incurred in credit card transactions include:

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[37] Cardweb.com, *Late Fees* (Jan. 28, 2005), *at* http://www.cardweb.com/cardtrak/news/2005/january/28a.html.

[38] Cardweb.com, *Overlimit Fees* (Feb. 2, 2005), *at* http://www.cardweb.com/cardtrak/news/2005/february/2a.html.

[39] Cardweb.com, *Fee Party* (Jan. 13, 2005), *at* http://www.cardweb.com/cardtrak/news/2005/january/13a.html.

[40] *Id.*

[41] *Id.* If merchant-paid fees are combined with consumer-paid fees, the total fee income is estimated at $50.8 billion.

[42] Cardweb.com, *Card Profits 04*, (Jan. 24, 2005), at http://www.cardweb.com/cardtrak/news/2005/january/24a.html.

[43] Federal Reserve Board, *Choosing a Credit Card*, at http://www.federalreserve.gov/pubs/shop, (last visited March 22, 2005).

NAME OF FEE	DESCRIPTION OF FEE
Annual fee (sometimes billed monthly).	Charged for having the card. Fees range from zero to $130.
Cash advance fee.	Charged when the card is used to obtain a cash advance; the fee is usually 3% of the advance, with a minimum of $5 and no maximum.
Balance-transfer fee.	Charged when the consumer transfers a balance from another credit card. Fees range from 2% to 3% of the amount transferred, with a minimum.
Late-payment fee.	Charged if the consumer's payment is received after the due date. Fees range from $10 to $49.
Over-the-credit-limit fee.	Charged if the consumer goes over the credit limit. Fees range from $10 to $39.
Credit-limit-increase fee.	Charged if the consumer asks for an increase in her/his credit limit.
Set-up fee.	One-time fee, charged when a new credit card account is opened.
Return-item fee.	Charged if the consumer pays the bill by check and the check is returned for non-sufficient funds.
Expedited payment fee.	Charged when the consumer makes a payment over the phone. Fees range from $10 to $14.95.
Expedited delivery fee.	Charged when the consumer requests an additional credit card and requests that it be delivered in an expedited way.
Replacement card fee.	Charged when the consumer's credit card is lost, stolen, damaged, or otherwise needs to be replaced.
Additional card fee.	Charged when the consumer requests a card for a family member or otherwise wishes an additional card.
Other fees.	Some credit card companies charge a fee to cover the costs of reporting to credit bureaus, reviewing the consumer's account, or providing other customer services.

The problem with these punitive charges, especially in combination with the penalty interest rates, is that they exacerbate the problems of consumers who have hit hard times. Too often these charges drive consumers into bankruptcy, resulting in cascading losses to individuals, families and neighborhoods—of lost savings, lost homes, forced moves, with all of the consequential financial and emotional tolls.

In the example of Ruth Owens discussed above, $2,678 of her credit card debt was attributable to late fees and over-limit fees alone. Bankruptcy decisions shed further light on how high finance charges and junk fees, not irresponsible spending, may be the root cause of overwhelming credit card debt. In one proceeding, a bankruptcy court forced Capital One to break out principal versus interest and fees in its claims against 31 separate debtors. The bankruptcy court's order reveals that on average, 57% of the debts consisted of interest and fees.[44]

Some problems with specific fees include:

Balance transfer fees. Balance transfer fees can be insidious because they often involve consumers who have been carrying a large balance from month to month. Credit card issuers lure these consumers into transferring large balances by heavily advertising low or 0% APRs, but not disclosing the balance transfer fee as prominently. For example, the MBNA card solicitation at Attachment 1 trumpets a "low 2.9% Fixed APR" for balance transfers using large type, repeating the 2.9% APR several times. It only discloses the balance transfer fee of 3% on the reverse page in 8 point type.[45] A consumer transferring a balance of $2,000 would be faced with a $60 fee. As a result of a balance transfer, this consumer would add more to her debt burden, yet MBNA's advertising would have led her to believe that a balance transfer would save her money.

Currency conversion fees. Currency conversion fees constitute a double whammy, in that they are imposed in many cases twice – once by the card issuer and once by the MasterCard or VISA network. These fees were previously hidden by deceptively "padding" the exchange rate, i.e., giving the consumer a worse exchange rate than that obtained by the card issuer.[46]

Late payment fees. Issuers have been quicker to impose late payment fees. Previously, credit card issuers gave consumers a leniency period of a few days before imposing late fees.[47] Now, card issuers will impose late fees if the consumer is even one day over the due date. In fact, some issuers have imposed late fees for payments received on the payment due date but after a certain cut-off time, a practice discussed more fully in the next section on abusive practices.

Over-limit fees. Over-limit fees are particularly unfair because the card issuer technologically has the ability to decline over-limit transactions, but chooses to permit them and then reap penalty fee income. These technological improvements and creditor practices implemented to minimize losses are discussed in Section II.B below. Card issuers have also been known to lower customers' credit limits during the middle of the

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[44] Amended Order Overruling Objection to Claims, *In re* Blair (W.D.N.C. Feb. 10, 2004).
[45] Credit Card solicitation (on file with the authors).
[46] *In re* Currency Conversion Fee Antitrust Litigation, 265 F. Supp.2d 385 (S.D.N.Y. 2003).
[47] The *Role of FCRA in the Credit Granting Process*: *Hearing before the subcommittee on Financial institutions and Consumer Credit*, at 7 (June 12, 2003) (statement of Dr. Robert D. Manning, Caroline Werner Gannett Professor of Humanities, Rochester Institute of Technology), at http://www.creditcardnation.com/pdfs/061203rm.pdf

billing cycle, then charge over-limit fees when unsuspecting consumers exceed the new limit at the end of the cycle.[48]

2. *Other Abusive Practices*

Credit card companies use a variety of means to lure unsuspecting consumers into the trap of financial exploitation created by exorbitant interest and fees. Even cautious consumers, who are attempting to manage their personal finances wisely, too often find themselves caught up in the web of deception and abusive practices.

Penalty Rates and Universal Default. A penalty rate is an increase in the initial APR triggered by the occurrence of a specific event, such as the consumer's making a late payment or exceeding the credit limit. These penalty interest rates can be as high as 30% to 40%.[49] The new terms apply to the old balance – leaving consumers stuck to pay often high balances at interest rates far higher than was originally agreed, with devastating consequences.[50]

The existence of penalty rates for minor transgressions alone would be enough to draw criticism by consumer advocates. Raising an APR from the mid-teens to 30% or higher, simply on the basis of a single transgression, itself is unjustified and unfair. After all, the card issuer has already collected a one-time charge for that late payment or over-limit transaction, which probably more than covers its costs. Increasing the consumer's APR is simply a way for the card issuer to reap additional profit by playing gotcha with unsuspecting consumers – trip once and they impose sky-high rates.

This practice is particularly problematic when it is applied retroactively. There is simply no legal or economic justification for assessing a penalty interest rate to an existing balance. No other industry in the country is allowed to increase the price of a product once it is purchased. Issuers have already assessed a consumer's risk of not repaying the loan and presumably offered an interest rate based on that risk. Issuers should be required to allow a consumer to pay off his or her existing balance at that interest rate.

Card issuers have recently added insult to injury with universal default, the latest tactic to squeeze every drop of revenue from struggling consumers. With universal default, credit card issuers impose penalty rates on consumers, not for late payments or any behavior with respect to the consumer's account with that particular issuer, but for late payments to any of the consumer's other creditors. In some cases, issuers will

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[48] *See* Complaint, State of Minnesota v. Capital One Bank, *available at* http://www.ag.state.mn.us/consumer/PDF/PR/CapitalOneComplaint.pdf .

[49] *See* Kathleen Day & Caroline Mayer, *Credit Card Fees Bury Debtors*, Washington Post, Mar. 7, 2005, at A1.

[50] Penalty interest rates usually are about 30 percent, with some as high as 40 percent, while late fees now often are $39 a month, and over-limit fees, about $35. According to Robert McKinley, CEO of Cardweb, "[i]f you drag that out for a year, it could be very damaging …. Late and over-limit fees alone can easily rack up $900 in fees, and a 30 percent interest rate on a $3,000 balance can add another $1,000, so you could go from $2,000 to $5,000 in just one year if you fail to make payments." *See id*.

impose penalties simply if the credit score drops below a certain number, whether or not the drop was due to a late payment or another factor.[51] A survey of credit card issuers found that 44% of banks surveyed had a universal default policy.[52]

An analysis of recent credit card solicitations shows that credit card issuers have been disclosing universal default policies in a less than prominent or understandable manner. These solicitations typically state:

> "All your APRs may increase if you default under any Card Agreement that you have with us because you fail to make a payment to us or any other creditor when due, you exceed your credit line, or you make a payment to us that is not honored."

These disclosures are usually outside the Schumer box, sometimes in smaller type, and cross-reference to the penalty rate as a footnote. While these solicitations mention briefly that a late payment to "any other" creditor will trigger a penalty rate, none of the solicitations disclosed that a mere drop in credit score may be the trigger. This is problematic because a drop in credit score is not always caused by late payments – it could be caused by having an unfavorable balance/limit ratio (sometimes a "utilization" greater than 50%, is enough to cause a score decline) on revolving accounts, an excessive number of inquiries, or a number of other factors that have little to do with the consumer's ability or willingness to repay the credit.[53]

The solution to this problem is not simply better disclosure, however. It is fundamentally unfair to impose a penalty rate on a consumer who has not made a late payment or defaulted on the obligation, especially when this rate increase is applied retroactively. Another concern with using credit reports to trigger a penalty rate is the enormous problem with inaccuracies in credit scoring and credit reporting. A review of over 500,000 consumer credit files by the Consumer Federation of America and the National Credit Reporting Association found that 29 percent of consumers have credit scores that differ by at least 50 points between credit bureaus, while 4 percent have scores that differ by at least 100 points.[54] Other studies have found that between 50 to 70 percent of credit reports contain inaccurate information.[55]

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[51] *See* Patrick McGeehan, *Plastic Trap—Debt That Binds: Soaring Interest Compounds Credit Card Pain for Millions*, N.Y. Times, Nov. 21, 2004; Complaint, State of Minnesota v. Capital One Bank, at www.ag.state.mn.us/consumer/PDF/PR/CapitalOneComplaint.pdf. The New York Times article was the companion piece to the PBS Frontline television episode *The Secret History of the Credit Card*, (PBS Frontline broadcast, Nov. 23, 2004), which focused on among other issues, universal default and change-in-terms.

[52] Linda Sherry, *Annual Credit Card Survey 2004*, Consumer Action (Spring 2004), *available at* http://www.consumer-action.org/English/CANews/2004_May_CreditCard/.

[53] *See* Fair, Isaac & Co., *What's In Your Score?*, *at* www.myfico.com/CreditEducation/WhatsInYourScore.aspx?fire=5.

[54] Consumer Federation of America and National Credit Reporting Association, *Credit Score Accuracy and Implications for Consumers* at 24 (Dec. 17, 2002), *available at* http://www.consumerfed.org/121702CFA_NCRA_Credit_Score_Report_Final.pdf

[55] U.S. Public Interest Research Group, *Mistakes Do Happen: Credit Report Errors Mean Consumers Lose* (1998), *available at* http://uspirg.org/uspirg.asp?id2=5970&id3=USPIRG&; Consumer Reports, *Credit Reports: How Do Potential Lenders See You?,* at (July 2000)(on file with the authors).

Deceptive Marketing. Some card issuers have engaged in questionable marketing practices when soliciting consumers. “Bait and switch” tactics are common. For example, card issuers have marketed "no annual fee" credit cards, then imposed an annual fee six months later using a change-in-terms notice.[56] They heavily advertise low “fixed” rates, but subsequently raise rates through change-in-terms notices and use penalty fees with punitive late payment and over-limit policies to trip consumers up.[57]

Another deceptive practice is that of “downselling” consumers by prominently marketing one package of credit terms, but then approving consumers only for accounts with less favorable terms, and touting the approved account in a fashion designed to mislead the customer about the fact that the received card is more expensive.[58]

Moreover, discussion of deceptive marketing is almost secondary given the existence of expansive change-in-terms provisions. Avoiding bait and switch abuse would require that advertising honestly reflect the terms of the credit card contract. If these terms can be changed at will by card issuers with a 15 day notice, no amount of honesty in advertising will help consumers because the advertising will only reflect the terms of the contract at that moment and cannot reflect future changes by issuers.

Payment Allocation Order (Q 35-36). Many credit card companies heavily advertise low APRs in their solicitations that are only applicable to one category of transactions. They then allocate payments first to the balances with lower APRs. The Board asks (Question 35) whether card issuers disclose their payment allocation methods. According to published cases, the disclosure of payment allocation order has been very minimal,[59] or nonexistent.[60] A review of several recent solicitations show some banks disclosing their payment allocation order, but in smaller print and as a footnote to the Schumer box, in contrast to the prominence of the promotion for low APRs.

The Board has requested comment (Question 36) about whether payment allocation order should be disclosed under the TILA. While better disclosure -- conspicuous enough to counterbalance a prominently promoted low APR -- would be helpful, that is not the fundamental issue. The very practice of allocating a consumer’s payment to the lowest-rate balance first is a deceptive and unfair practice. It is an additional indication that credit card banks have shed any sense of fair play and good customer treatment in their relationships with consumers. Instead of treating customers with respect and honesty, banks aggressively mine for profit on every aspect of credit

[56] Rossman v. Fleet Bank (R.I.) Nat’l. Assn., 280 F.3d 384 (3d Cir. 2002).
[57] Roberts v. Fleet Bank (R.I), Nat’l Assn, 342 F.3d 260 (3rd Cir. 2003); Gaynoe v. First Union Direct Bank, Nat’l Assn., 571 S.E.2d 24 (N.C. Ct. App. 2002). For an interesting analysis of the deceptiveness of Capital One’s heavy promotion including its prolific TV ad campaign, *see* Complaint, State of Minnesota v. Capital One Bank, *available at* http://www.ag.state.mn.us/consumer/PDF/PR/CapitalOneComplaint.pdf.
[58] *See, e.g.,* Consent Order, *In re* Direct Merchants Credit Card Bank, No. 2001-24 (Dept. of Treasury, Office of the Comptroller of the Currency, May 3, 2001), *available at* http://www.occ.treas.gov/ftp/eas/ea2001-24.pdf.
[59] Broder v. MBNA Corp., 722 N.Y.S.2d 524 (N.Y. Sup. Ct. 2001) (promotional material ambiguously disclosed in small print footnote that card issuer “may” allocate payments to promotional balances first.)
[60] *See* Johnson v. Chase Manhattan Bank USA, 784 N.Y.S.2d 921 (N.Y. Sup. Ct. 2004).

card lending. These practices do nothing but prolong the debt of consumers and provide an additional revenue stream for banks.

Posting Cut-offs (Q 51). As the Board knows, card issuers have established cut-off times for posting payments. Some of these hours have been set ridiculously early, established deliberately to result in the imposition of late payment fees. In reported cases, creditors have used times as early 9:00 or 10:00 AM as the cut-off time for crediting payments received that day.[61] Consequently, if a consumer's payment is received on the payment due date, it will be considered late because in all likelihood, the U.S. Postal Service will not have delivered the mail so early in the morning. Furthermore, when due dates fall on a weekend or holiday, card issuers will consider the payment late if not received on the prior business day. Non-business day due dates are inherently deceptive.

The Board has asked whether it should require issuers to post payments as of the date of receipt, regardless of time (Question 51). While such a change might be a step in the right direction, it is important to consider this practice in the broader context of a pattern of unfair behavior by card issuers. Creditors should not be allowed to rig the system to trap unwary consumers. Consumers need the protections of a general prohibition against unfair conduct by card issuers, such as the one contained in section 5 of the Federal Trade Commission Act. The ability of consumers to enforce section 5 would go a long way toward curbing abuses, of which posting cut-offs are but one example.

Changes to Credit Limits. Another recent abuse is sudden changes in credit limits by card issuers. The Minnesota Attorney General's Office has documented how Capital One engaged in this practice. In one case, two days after lowering the consumer's limit and before the consumer had received any notice of the change, Capital One charged this consumer an over-limit fee. To pour salt on the wound, Capital One then imposed a penalty rate.[62]

Debt Collection Abuses. Credit card issuers, like many creditors, have been known to engage in plain old debt collection abuse – harassment, deception and abuse.[63] However, there are a few practices that are unique to credit card companies and their collectors.

Most important is the fact that credit card companies, or the debt buyers to whom they sell the debt, often initiate collection cases against consumers without any

[61] *See, e.g.*, Lawrence v. Household Bank, 343 F.Supp.2d 1101 (M.D. Ala. 2004) (9 AM cut-off for payment posting); Landreneau v. Fleet Financial Group, 197 F. Supp.2d 551 (M.D. La. 2002) (9 AM cut-off for payment posting); Schwartz v. Citibank (S.D.), Nat'l Assn, Clearinghouse No. 53,023, Case No. 00-00078 (JWJX) (C.D. Cal. May 5, 2000) (class action settlement notice in case challenging 10 AM cut-off). At one point, MBNA supposedly set the cut-off time as early as 6:00 AM. Kevin Hoffman, *Lerner's Legacy – MBNA's Customers Wouldn't Write Such Flattering Obituaries*, Cleveland Scene, Dec. 18, 2002, *available at* http://www.clevescene.com/issues/2002-12-18/news/feature.html.
[62] Complaint, State of Minnesota v. Capital One Bank, *available at* http://www.ag.state.mn.us/consumer/PDF/PR/CapitalOneComplaint.pdf.
[63] *See, e.g.*, Order Granting Motion for Temporary Injunction, State of Minnesota v. Cross County Bank, No. MC 03-5549 (Minn. Dist. Ct. 4th Dist. Nov. 10, 2004).

documentation of a credit card agreement signed by the consumer or even periodic statements to show transaction activity. Instead, they simply offer up an affidavit from an employee in their loss recovery department and/or sue on an account stated theory.[64] This deprives the consumer of the ability to challenge erroneous transactions or demonstrate how much of their debt is due to purchases versus finance charges and junk fees.

Indeed, there is evidence that credit card issuers would be unable to offer up the original agreement or application signed by the cardholder. In one case, a major card issuer admitted in litigation that it does not retain the original account application of cardholder's beyond five years.[65] Yet these same issuers may sue the consumer, claiming that the terms of the now-destroyed documents justify charges, fees, and the liability of co-signers.

Another practice peculiar to credit card debt is "zombie debt collection,"[66] where card issuers buy old credit card debts, then offer the debtors new credit cards to revive the old debt. Oftentimes, the debts are time-barred by the statute of limitations and would constitute stale information on the consumer's credit report under the Fair Credit Reporting Act.[67] Of course, the debt-buying card issuers deceptively omit this critical fact or bury it in fine print. In addition, the debt buyer/card issuers fail to provide required disclosures as debt collectors under the Fair Debt Collection Practices Act.[68]

Use of Mandatory Arbitration Clauses. The use of arbitration provisions in credit card agreements has been a tremendous barrier for consumers seeking redress under the TILA. Most of the reported cases have been about consumers who have filed suit as plaintiffs attempting to enforce their rights under the TILA. Consumers who complain about deceptive TILA disclosures, late posting of payments, payment allocation abuses, and failure to follow the Fair Credit Billing Act ("FCBA") procedures have lost their day in court due to arbitration provisions (added using change-in-terms notices discussed below).[69]

Arbitration provisions also burden the ability of consumers to use the TILA's substantive protections. Mandatory arbitration renders nugatory the right to dispute erroneous charges, because creditors can ignore consumer disputes and the consumer's

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[64] Citibank (S.D.) Nat'l Assn. v. Whiteley, 149 S.W.3d 599 (Mo. Ct. App. 2004).
[65] Johnson v. MBNA, (4th Cir. 2004).
[66] The term is taken from Liz Pulliam Weston, *Zombie Debt Collectors Dig Up Your Old Mistakes*, MSNMoney.com, *at http://moneycentral.msn.com/content/Savinganddebt/Managedebt/P74812.asp.*
[67] Brink v. First Credit Resources, 185 F.R.D. 567 (D. Ariz. 1999).
[68] Carbajal v. Capitol One, F.S.B., 2003 WL 22595265 (N.D. Ill. Nov. 10, 2003).
[69] *See, e.g,,* Lawrence v. Household Bank, 343 F.Supp.2d 1101 (M.D. Ala. 2004) (compelling arbitration of TILA and FCBA claims challenging a 9 AM cut-off for payment posting); Kurz v. Chase Manhattan Bank, 319 F. Supp.2d 457 (S.D.N.Y. 2004) (compelling arbitration of FCBA claims as well as retaliation under the ECOA). *Cf.* Johnson v. Chase Manhattan Bank USA, 784 N.Y.S.2d 921, (N.Y. Sup. Ct. 2004) (compelling arbitration of state law claims challenging payment allocation abuse); Providian v. Screws, 2003 WL 22272861 (Ala. Oct. 3, 2003) (compelling arbitration of state law claims challenging bait & switch APRs, billing errors, and late fees).

only option for relief is an expensive arbitration proceeding (often conducted by arbitration providers that are amazingly biased against consumers).[70]

Most shockingly, card issuers are now using arbitration provisions offensively, as a lopsided method to obtain judgments against unsuspecting consumers. Some of these consumers include victims of unauthorized use and identity theft. A report recently issued by NCLC documents how credit card debt buyers use arbitration proceedings to obtain judgments for thousands of dollars against identity theft victims.[71]

Aggressive Solicitation. Many card issuers now make offers of credit based solely on the credit score. Credit scores measure the propensity to repay and the ratio of revolving credit used, but they do not measure whether the consumer's income is adequate to repay a new debt, or include a debt-to-income ratio that would show if the consumer is already overextended. As a result, card issuers often grant new credit cards to consumers who are already overextended. Federal regulators have issued guidance urging card issuers to consider repayment capacity when granting new credit,[72] but this guidance is not mandatory or enforceable by injured consumers. Federal law should prohibit card issuers from issuing credit cards without first engaging in real underwriting that considers the consumer's ability to repay the debt.

Tiny Minimum Monthly Payments. [73] Creditors have decreased the minimum monthly payments from 4% to 2% to 3% of the consumer's balance.[74] With lowered monthly minimum payments, consumers who pay only the minimum will take much longer to pay off the credit card debt and will pay substantially more in finance charges. Worse, the combination of the minimum monthly payments and the penalty interest rates often results in negatively amortizing debt. Even when the consumer is making the payments as requested and not incurring any new charges, the debt keeps climbing. A few issuers have begun reversing this trend in response to federal guidelines in recent months, but minimum payment rates are still well under 3 percent.[75]

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[70] According to documents produced by the National Arbitration Forum itself, the consumer prevailed in just 87 out of 19,705 arbitrations conducted by NAF for First USA Bank. Thus, the credit card company prevailed a disturbing 99.56% of the time!

[71] National Consumer Law Center & Trial Lawyers for Public Justice, *New Trap Door for Consumers: Card Issuers Use Rubber-Stamp Arbitration to Rush Debts Into Default Judgments* (Feb. 27, 2005), *available at* http://www.consumerlaw.org/initiatives/model/content/ArbitrationNAF.pdf.

[72] Federal Financial Institutions Examination Council, *Credit Card Lending Account Management and Loss Allowance Guidance* (Jan. 2003), *available at,* http://www.federalreserve.gov/BoardDocs/press/bcreg/2003/20030108/attachment.pdf.

[73] We support the comments filed by the Center for Responsible Lending on this issue.

[74] Linda Sherry, *Annual Credit Card Survey 2004*, Consumer Action (Spring 2004), *available at* http://www.consumer-action.org/English/CANews/2004_May_CreditCard/

[75] Jane J. Kim, *Minimums Due On Credit Cards Are on the Increase*, Wall Street Journal, March 24, 2005; at D2. Although federal regulators admit concern over this widespread practice, new rules addressing the problem have been delayed. *See* Kathleen Day & Caroline Mayer, *Credit Card Fees Bury Debtors*, Washington Post, Mar. 7, 2005, at A1.

3. *Change-in-terms (Q 26)*

The expansive change-in-terms provisions in many credit card agreements are the mechanism that permits card issuers to impose excessive junk fees and engage in abusive practices. Many issuers place extremely expansive change-in-term provisions in their credit card agreements, which allow the issuers to change any of the terms in the agreement at any time. A typical change-in-terms agreement provides:

> We may amend or change any part of your Agreement, including the periodic rates and other charges, or add or remove requirements at any time. If we do so, we will give you notice if required by law of such amendment or change. Changes to the annual percentage rate(s) will apply to your account balance from the effective date of the change, whether or not the account balance included items billed to the account before the change date and whether or not you continue to use the account. Changes to fees and other charges will apply to your account from the effective date of the change.[76]

Some states even permit changes in the terms of a credit agreement without such a clause in the credit agreement.[77]

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[76] Stone v. Golden Wexler & Sarnese, P.C., 341 F.Supp.2d. 189, 191 (E.D.N.Y. 2004).

[77] Del. Code Ann. tit. 5, § 952 (a) (1999) states:

> [A] bank may at any time and from time to time amend [an open-end credit plan] in any respect, whether or not the amendment or the subject of the amendment was originally contemplated or addressed by the parties or is integral to the relationship between the parties. Without limiting the foregoing, such amendment may change terms by the addition of new terms or by the deletion or modification of existing terms, whether relating to plan benefits or features, the rate or rates of periodic interest, the manner of calculating periodic interest or outstanding unpaid indebtedness, variable schedules or formulas, interest charges, fees, collateral requirements, methods for obtaining or repaying extensions of credit, attorney's fees, plan termination, the manner for amending the terms of the agreement, arbitration or other alternative dispute resolution mechanisms, or other matters of any kind whatsoever. Unless the agreement governing a revolving credit plan otherwise expressly provides, any amendment may, on and after the date upon which it becomes effective as to a particular borrower, apply to all then outstanding unpaid indebtedness in the borrower's account under the plan, including any such indebtedness that arose prior to the effective date of the amendment. An agreement governing a revolving credit plan may be amended pursuant to this section regardless of whether the plan is active or inactive or whether additional borrowings are available thereunder. Any amendment that does not increase the rate or rates of periodic interest charged by a bank to a borrower under § 943 or § 944 of this title may become effective as determined by the bank, subject to compliance by the bank with any applicable notice requirements under the Truth in Lending Act (15 U.S.C. §§ 1601 et seq.), and the regulations promulgated thereunder, as in effect from time to time. Any notice of an amendment sent by the bank may be included in the same envelope with a periodic statement or as part of the periodic statement or in other materials sent to the borrower. . .

Thus, even when a TILA disclosure shows and the terms of a credit agreement provide for a fixed APR, the reality is that the creditor may be able to change the APR in fifteen days with a change-in-terms notice.[78]

There are two problems with these changes in terms notices. First, these expansive change-in-terms provisions deprive consumers of any "benefit of bargain" and thus undermine the TILA's purpose in ensuring effective disclosure. They make a mockery of contract law because the terms of the "bargain" are illusory. A savvy consumer can select a credit card after reviewing TILA application and solicitation disclosures, comparing terms, reading articles about picking a credit card – in other words, be the smart shopper that the TILA envisioned – then be faced with a change-in-terms notice that totally changes the APR and other terms of the credit card. One court has described change-in-terms provisions as "an Orwellian nightmare, trapped in agreements that can be amended unilaterally in ways they never envisioned."[79]

Second, the vast majority of consumers probably don not read or understand change-in-terms notices. While not involving credit cards, the case of *Ting v. AT&T*, 319 F.3d 1126 (9th Cir. 2003) is instructive. In that case, AT& T mailed a consumer services agreement to its customers that, among other provisions, added a mandatory arbitration clause. Before mailing this agreement, AT&T conducted extensive market research designed to predict how consumers would react to the mailing. AT&T then designed its mailing to ensure that consumers were less likely read and understand the details of the agreement.

Furthermore, AT&T's research found that very few customers actually would read the agreement, especially if it was sent in a separate mailing. For a mailing separate from a monthly statement, AT&T's research found that only 25% were likely to open the envelope. If the customer did open the envelope, AT&T's research found that only 30% of consumers would read the entire agreement.[80]

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[78] Creditors may even attempt to avoid the reach of TILA entirely by using a change-in-terms tactic. For example, a card issuer could offer a credit card account with a credit limit over $25,000, thus allegedly qualifying for the exemption for when a "creditor makes a firm commitment to lend over $25,000" under Official Staff Commentary § 226.3(b)-2. Then if the creditor subsequently used a change-in-terms notice to decrease the credit limit to below $25,000, it might argue that it was still exempt. Regardless of any other action the Board takes on change-of-terms notices, it should amend that section of the Commentary by adding this proviso: "If the creditor reduces the credit limit to $25,000 or less, the plan is no longer exempt and the creditor must comply with all of the requirements of the regulation including, for example, providing the consumer with an initial disclosure statement."

[79] Perry v. FleetBoston Financial Corp., 2004 WL 1508518 at *4 n.5 (E.D. Pa. Jul. 6, 2004). This court went on to say that it was "reminded of George Orwell's 1946 work, Animal Farm, in which the pigs assume power and change the terms of the animals' social contract, reducing the original Seven Commandments, which included 'All animals are equal,' to one—'All animals are equal, but some animals are more equal than others.'"

[80] An article by Bill Burt at Bankrate.com reports similar data, i.e. a survey by Auriemma Consulting Group finding that only one-third of consumers who received change-in-terms notices were aware of the changed terms. Bill Burt, *Ignoring Credit Changes Can Cost You*, (Jan. 30, 2004) *at* http://www.bankrate.com/brm/news/cc/20040129a1.asp.

The separate mailings for credit card change-in-terms notices are not any more likely to be opened by consumers. When opened, or when they are "bill stuffers," they are no more likely to be read. The market research data uncovered in *Ting* suggests that the vast majority of consumers don not read change-in-terms disclosures. It would be naïve to believe that the credit card industry is unaware of this data and does not conduct similar market research. It would also be naïve to believe that the industry does not design its disclosures around similar market research.

Furthermore, even when consumers do open and read change-in-terms notices, the notices are full of dense, impenetrable legal jargon that even lawyers and seasoned consumer advocates have difficulty understanding. For example, a sample change-in-terms notice at Attachment 2 states:

> Your Daily Periodic Rate and corresponding APR may increase or decrease from time to time according to the movements up or down of the Index, which is the highest Prime Rate published in the "Money Rates" section of the Midwest Edition of *The Wall Street Journal* in the last 90 days, before the date on which the billing cycle closed (in other words, the "statement date"). Any variable rate adjustment based on an Index change will be effective as of the first day of the billing cycle, and will apply to the new and outstanding Account balances and transactions subject to that variable rate.

Using the Flesch Reading Ease score built into Microsoft Word, this text rates at a mere 29.7 out of 100 (the higher the better, standard documents score around 60 to 70), and requires a 12th grade reading level.[81] In addition, this particular change-in-terms agreement was written in 4 ½ (-point type, in a bill stuffer consisting of 16 folded panels. (The actual size is shown in the attached copy.)

The Board asks (Question 26) whether 15 days is sufficient time for a change-in-terms notice. The 15-day notice period is entirely inadequate, and is also so full of exceptions that it is nearly meaningless. The issue, however, is not whether consumers need more time for a change-in-terms notice, but that changes in terms should not be permitted at all in credit card contracts. Thus, we urge the Board to seek legislation banning changes in terms altogether for credit card agreements.

Furthermore, we believe that the Board has the authority under the TILA to prohibit changes in terms for at least the term of the credit card agreement. As discussed earlier, changes in terms undermine the TILA disclosure requirements. The change-in-terms provisions of Regulation Z exacerbate the problem because they legitimize the

[81] *See also* Alan M. White & Cathy Lesser Mansfield, *Literacy and Contract*, 13 Stan. L. & Pol'y Rev. 233 (2002) (according to National Adult Literacy Survey, only 3-4% of the American adult population has the documentary literacy skills necessary to utilize a table comparing the features of two credit cards, so as to identify two differences between the cards).

practice of changing terms. In other words, "if you disclose it, it's okay." Rather than merely increase the time for change-of-terms notices, the Board should amend Regulation Z to provide that for open-end credit other than home equity plans, the creditor may not change the terms during the term of the credit card: We recommend that § 226.9(c)(1) (and (2) be replaced with a single paragraph reading:

> *(1) Any term required to be disclosed under section 226.6 must remain in effect until the renewal disclosures required by subsection (e). However, the creditor may change a term if the consumer agrees to the specific change by signing or initialing a revised agreement or if the consumer agreed at the time the credit card was issued that a specific change would occur on a specific date or upon the occurrence of a specific event not within the control of the creditor. If the creditor changes a term as permitted by this paragraph, it shall mail or deliver written notice of the change to each consumer who may be affected, at least 15 days prior to the effective date of the change. Creditors may not evade the requirements of this paragraph by issuing credit cards with terms shorter than twelve months.*

This proposal is consistent with the Third Circuit's decision in *Rossman v. Fleet Bank* (R.I.) N.A.[82] that the Truth in Lending Act requires open-end credit disclosures to be true and that a disclosure that there is "no annual fee" must remain true for at least a year.

C. The System is Broken and Improved Disclosures Will Not Address the Problems

Because of the deregulation of bank credit, virtually no state regulation on creditor conduct applies to the practices of the credit card industry.[83] While there are some – very few – limits placed on the most outrageous abuses of consumers by banks by the federal banking regulators,[84] the TILA is the primary regulatory structure applicable to the relationship between credit card issuers and their customers. The TILA was intended to be – and remains – primarily a disclosure statute. Through its enactment and enforcement, Congress intended to enable consumers to compare the costs of credit.[85] However, the TILA was never intended to stand on its own – to be the sole and primary means of regulating and limiting a powerful industry vis-à-vis the individual consumers who borrow money for personal, family or household purposes. Indeed, when the TILA passed in 1968, state usury and fee caps applied to credit card transactions.

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[82] Rossman v. Fleet Bank (R.I.) Nat'l. Assn, 280 F.3d 384 (3d Cir. 2002).

[83] For example, when the state of California tried to address the issue of tiny minimum payments by requiring creditors to provide information to each consumer on how long it would take to pay off a sample credit card balance if only the minimum payment was paid each month, a federal district held the statute was preempted by federal banking statutes. American Bankers Association v. Lockyer, 239 F. Supp.2d 1000 (E.D. Cal 2002).

[84] *See* Section III.B regarding the handful of enforcement actions taken by bank regulators against subprime credit card lenders.

[85] 15 U.S.C. § 1601(a).

Uniform and accurate disclosures *are* useful for consumers, but they cannot substitute for real regulation. The best proof of this is the unbalanced and dangerous situation that the American consumers find themselves in with the open-end credit industry today.

Disclosures are only useful for consumers when all of the following conditions exist –

- The consumer has the opportunity to read the disclosures fully;
- The disclosures are unambiguous and understandable;
- The disclosures are true and apply to the entire term of the contract;
- The consumer has the knowledge and sophistication to understand the meaning of the information provided in the disclosures;
- The consumer has the opportunity to make choices based on the information gained through the disclosures.

None of these conditions exist today with regard to open-end credit. More importantly, even if the Board were to make every recommended improvement to the TILA disclosures, the most critical of these conditions would not exist – **the consumer would not have the opportunity to make choices to avoid the onerous and abusive terms of open-end credit**. This is because most large issuers of open-end credit engage in a reverse competition to provide the most exploitative terms of credit that will maximize profits, regardless of the effect on the consumer, the community, or the nation's household debt or rate of savings.

Disclosures alone are not sufficient to protect consumers from over-reaching creditors. This is because --

- Consumers lack equal access to information – most consumers will not have the knowledge to understand the legal consequences of the terms of credit.
- Consumers lack equal bargaining power – no consumer has the market power to call up a credit card company and negotiate either the basic terms or those in the adhesion contract.
- The credit card market does not provide real choices. With the increasing consolidation of credit card providers, the industry guarantees *less* meaningful competition. There is generally competition only on the surface, on a few prominently-advertised terms such as the periodic rate and annual fee. Consumers have little or no meaningful choices on the terms that create the bulk of the cost of open-end credit.
- Without some basic substantive regulation, there will continue to be competition between industry players only as to which can garner the most profit from the most consumers – regardless of the fairness, or the effects on consumers.

As the majority of the questions posed in the ANPR relate to disclosures, and ways to improve the disclosures required under the current Truth in Lending statute, these

comments provide extensive answers to these questions. There is no doubt that the disclosures relating to open-end credit can be dramatically improved – and we hope that our suggestions along these lines will be heeded. However, our primary message to the Board in these comments is that **disclosures are not sufficient. The Board should recommend to Congress that it impose substantive regulation of open-end credit terms and charges.**

For the past two decades substantive credit regulation has been steadily whittled away, with no discernable benefits for consumers. The twin justifications for this diminution in credit regulation have been that too much regulation limits access to credit, and that consumers can adequately protect themselves so long as they are armed with full information about the costs of the credit. The pendulum has swung too far – there is no lack of available credit; indeed for many families there is far too much available credit.

The current financial condition of many American households and the escalating credit card debt is an indication that disclosures, standing alone, do not adequately protect consumers. Even dramatic improvements to the current disclosure regime required by the TILA will not equalize the differences between consumers and industry – consumers will still lack equal access to information regarding meaning and consequences and they will still lack sufficient bargaining power to protect themselves from onerous charges and terms.

D. Recommendations for Statutory Reform (Q 56)

It is time for the re-regulation of open-end credit.[86] Real, substantive limits on the terms of credit, and the cost of the credit, including the interest rate and all fees and charges, must be re-imposed. We recommend substantive regulation along the following lines–

- A cap on all periodic interest rates, for example, prime plus 10%.
- A cap on all other charges, whether considered a finance charge or not, to an amount the card issuer can show is reasonably related to cost.
- No unilateral change-in-terms allowed.
- No retroactive interest rate increases allowed.
- No penalties allowed for behavior not directly linked to the specific card account at issue.
- No over limit fees allowed if issuer permits credit limit to be exceeded.
- No improvident extensions of credit –require real underwriting of the consumer's ability to pay.
- No mandatory arbitration, either for consumers' claims, or for collection actions against consumers.
- Meaningful penalties for violating any substantive or disclosure that provide real incentives to obey the rules.

[86] We also advocate the re-regulation of closed end credit. However, as that issue is not addressed in the Board's ANPR, we will leave that discussion for another day.

- A private right of action to enforce section 5 of the Federal Trade Commission Act, which prohibits unfair or deceptive practices by businesses, including banks.

It is no longer a question of balancing the appropriate regulation with the need to assure access to credit. The increasing mountain of debt held by American consumers, coupled with the growing number of abusive practices practiced by the credit card companies, illustrate amply de-regulation has not worked. Since biblical times government has recognized that consumers need strong, enforceable limits placed on the power of lenders to exert their far greater bargaining power in the marketplace. The age old protection of borrowers from over-reaching lenders needs to be reinstituted.

II. REGULATORY REFORMS OF TRUTH IN LENDING DISCLOSURES

Despite the huge need for significant statutory reform of federal laws governing the substantive terms of open-end credit, there are substantial and meaningful changes that the Board has the statutory authority to make. While improved disclosures will not balance the grossly unequal bargaining power between the credit card industry and the individual consumer, improved disclosures could actually inform consumers of the real costs and risks associated with open-end credit. These improved disclosures are well within the statutory authority of the Board, and this opportunity to do what it can to improve the situation should not be lost.

A. The Inclusive Finance Charge Definition In The Act Should Be Retained And The Board Should Revise Regulation Z To Reflect Congressional Intent in Order to Address Marketplace Problems (Qs 13-20)

The broad definition of "finance charge" in TILA accurately reflects the cost of credit. On the other hand, Regulation Z, while adopting the same general definition, has created so many exceptions that the finance charge for open-end credit no longer is a true measure of the cost of credit. We urge the Board to tighten up Regulation Z to more accurately implement the purposes of the Act.[87]

The reasons supporting this position follow. We start by reviewing the definition of the finance charge in the Act and the centrality of the APR and finance charge to TILA's purposes. We follow with the legislative history, the language of the 1968 Act and subsequent amendments, the state of the credit marketplace in 1968, and relevant developments since that time. Next, we discuss finance charges in the open-end credit context and the Board-created exceptions to the finance charge definition. We end with suggestions on how the Board should amend Regulation Z to make the finance charge definition more truly reflect Congressional intent and to address current problems in the credit card market

[87] 15 U.S.C. § 1601(a). The statutory definition of a finance charge was designed to implement the Act's mandate to "assure a meaningful disclosure of credit terms" and enable informed comparison-shopping by consumers.

1. *Broad Scope of the Finance Charge Definition in TILA*

The definition of a finance charge under the TILA has remained the same since 1968.[88] That definition is:

> [T]he sum of all charges, payable directly or indirectly by the person to whom the credit is extended, and imposed directly or indirectly by the creditor as an incident to the extension of credit.

This definition is broad and inclusive in its coverage. It is intended to make the finance charge a measure of the cost of credit to the consumer, not merely a measure of compensation to the creditor. For example, some charges are finance charges even though they are not retained by the creditor, as long as they are *imposed* directly or indirectly by the creditor. The Board confirmed this reading of the finance charge definition in the model forms it crafted to ease creditor compliance.[89]

Congress did not explicitly discuss the phrase "incident to" an extension of credit in the legislative history of the original Act. However, the purposes of the Act as described in the House Report make clear that Congress believed that the uniform disclosure regime it created would not function properly unless all mandatory charges were included in the finance charge and reflected in the APR.[90]

In 1996, the Board interpreted the "incident to" language of the Act to mean "in connection with" and "part of the cost of credit." [91]At that time, the Board rejected the notion that a fee for a product or feature that the consumer may voluntarily select is *per se* excluded from the finance charge.[92]

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[88] *Compare* Pub. L. No. 90-321, § 106(a), 82 Stat. 146, 1968 U.S.C.C.A.N. 178, *with* 15 U.S.C. § 1605(a).
[89] *See, e.g.,* Model Form H-11 in which the "Finance Charge" is described as: "The dollar amount the credit will cost you." Reg. Z § 226.4, App. H.
[90] H.R. Rep. No. 1040 (1967), *reprinted in* 1968 U.S.C.C.A.N. 1962, 1971, 1980. The 1968 edition of Black's Law Dictionary defines "incident" as denoting "anything which is usually connected with another, or connected with some purposes, though not inseparably." Black's Law Dictionary 904 (4th ed. 1968). The more recent 1999 edition defines "incident" as: "Dependent upon, subordinate to, arising out of, or otherwise connected with." Black's Law Dictionary 765 (7th ed. 1999).
[91] 61 Fed. Reg. 49237, 49239 (Sept. 19, 1996).
[92] On this subject, the Board went on at some length: "The Board has generally taken a case-by-case approach in determining whether particular fees are ''finance charges,'' and does not interpret Regulation Z to automatically exclude all 'voluntary' charges from the finance charge. As a practical matter, most voluntary fees are excluded from the finance charge under the separate exclusion for charges that are payable in a comparable cash transaction, such as fees for optional maintenance agreements or fees paid to process motor vehicle registrations. In the case of debt cancellation agreements, however, the voluntary nature of the arrangement does not alter the fact that debt cancellation coverage is a feature of the loan affecting the total price paid for the credit. Thus, even though a lender may not require a particular loan feature, the feature may become a term of the credit if it is included. For example, borrowers obtaining variable-rate loans may have an option to convert the loan to a fixed interest rate at a subsequent date. Even though the lender does not require that particular feature, when it is included for an additional charge (either paid separately at closing or paid in the form of a higher interest rate or points), that amount properly represents part of the finance charge for that particular loan, even though less costly loans may be available without that feature. This is also the case with debt cancellation coverage, which alters the fundamental nature of the borrower's repayment obligation. Although the same loan may be available

In a recent case, the Supreme Court discussed the "incident to" language when deciding whether the Board exceeded its authority by excluding over-limit fees charged by credit card issuers from the finance charge.[93] The Court was unsure whether the phrase requires a substantial or remote connection to the credit transaction. Given this uncertainty, the Court deferred to the Board's characterization of the over-limit fee as a penalty for violating the creditor's agreement, rather than related to the extension of new credit.[94] Nonetheless, the Court recognized that "incident to" means "connection to."

The broad scope of the finance charge definition provides the context in answering the questions 13 through 25 posed by the Board in its ANPR.

2. *The Importance of the Finance Charge Disclosure and the Related APR as the Core Disclosures under TILA*

The disclosure of the finance charge and the APR is at the heart of Truth In Lending. An accurately disclosed APR depends on having an accurately calculated finance charge.[95] The finance charge is the cost of credit as a dollar amount, and the APR reflects the cost on a yearly percentage rate basis. Together, these two disclosures are designed to provide an accurate price tag for credit. For this reason, they are the two most important disclosures required under TILA and Congress mandates that they be disclosed more conspicuously than any other.[96]

Moreover, Congress created a universal definition of the finance charge that is meant to apply equally to both open-end (including revolving credit card accounts) and closed-end (fixed term) transactions. The finance charge rules are found in section 1605, located in the "General Provisions" part of the Act called "Part A." Section 1637 dealing specifically with open-end disclosures is located in Part B, the "Credit Transactions" part. Accordingly, the discussion about the meaning of the words Congress used to define the finance charge applies equally to open-end credit.

3. *The Purposes of the Truth In Lending Act, the Finance Charge Definition, and the APR Disclosure*

In 1968 when Congress enacted the TILA, it expressed several concerns about the credit marketplace. First, Congress acknowledged the burgeoning credit market and the

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without that feature, with respect to a loan that has been structured in this manner, the debt cancellation fee is one that has been imposed as an incident to that particular extension of credit. The same rationale applies to premiums for voluntary credit insurance, which generally are finance charges under the TILA but may be excluded if specified disclosures are given." *Id.*

[93] Household Credit Servs. Inc v. Pfennig, 541 U.S. 232, 124 S. Ct. 1741, 158 L. Ed. 2d 450 (2004).

[94] *Id*. at 1749.

[95] The APR is derived from the relationship of the finance charge to the amount financed, given the repayment schedule, rather than applied, like an interest rate. Ralph Rohner, *The Law of Truth In Lending* ¶ 4.01[2][c][I] (Business Law American Bar Association) (1984).

[96] 15 U.S.C. § 1632(a). The Board repeated this requirement for open-end credit in Regulation Z, § 226.5 (a)(2).

heavy reliance by consumers on credit in their everyday lives.[97] It noted that as of 1968, outstanding consumer credit exceeded $95.8 billion, up from just $5.6 billion in 1945.[98] Congress also recognized the "rapidly" growing open-end or revolving credit segment of the industry. In one year alone, revolving credit rose from $3.5 billion in 1967 to $5.3 billion in 1968. Congress adopted the remarks of President Lyndon B. Johnson who stated that:

> The consumer has the right to know the cost of this key item [credit] in his budget just as much as the price of any other commodity he buys. If consumers are to plan prudently and to shop wisely for credit, they must know what it really costs.[99]

Second, Congress discussed certain credit practices at the time that triggered special concerns. The credit industry used various methodologies for calculating interest, some of which resulted in an understatement of the simple interest rate. These types of calculations generated "add-on" interest or "discount" interest.[100] Other parts of the credit industry employed monthly interest rates. Some creditors disclosed no rate. Finally, Congress recognized the fact that some creditors added a number of additional fees or charges to the transactions. "This permits a creditor to quote a low rate while actually earning a higher yield through the additional fees and charges….The end result of these inconsistent and noncomparable practices is confusion in the public mind about the true costs of credit."[101]

Third, the Senate Report specifically noted the high bankruptcy rate in the United States at the time.[102]

Consequently, Congress believed: "that by requiring all creditors to disclose credit information in a uniform manner, and by requiring all additional mandatory charges imposed by the creditor as an incident to credit be included in the computation of the applicable percentage rate, the American consumer will be given the information he needs to compare the cost of credit and to make the best informed decision on the use of credit."[103] This conviction appears in the Act itself. [104]

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[97] H.R. Rep. No. 1040 (1967), *reprinted in* 1968 U.S.C.C.A.N. 1962, 1965.
[98] *Id.* at 1966.
[99] *Id.* at 1965 (quoting President Lyndon B. Johnson's remarks in speeches made on February 16, 1967 and March 15, 1967).
[100] *Id.* at 1970. For a discussion of these calculations, *see* Kathleen E. Keest & Elizabeth Renuart, *The Cost of Credit: Regulation and Legal Challenges* § 4.3 (2d ed. 2000 & Supp.).
[101] *Id.* at 1970. Congress cited to a study of 800 families who were asked to estimate the rate of finance charge they were paying. The study showed that they dramatically underestimated what they actually paid.
[102] S. Rep. No. 392, at 1 (June 29, 1967).
[103] *Id.* at 1971 (emphasis added).
[104] 15 U.S.C. § 1601(a) states: "[T]he purpose of this subchapter is to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit…" .

4. *Current Market Conditions and Consumer Troubles*

Since the TILA was enacted, the problems observed by Congress have increased in severity. The amount of credit card debt has mushroomed, caused in part by the proliferation of credit card fees and the practices discussed in Section I.B. As of January 2005, credit card debt had risen to almost $800 billion. Income from just late, over-limit, cash advance, and annual fees grew to $24.4 billion in 2004.[105] Meanwhile, as discussed in Section I.A., card issuer profits steadily increased rising from 3.1% in 1999 to 4.5% in 2004.[106]

Significantly, the portion of overall consumer debt attributed to credit card debt has skyrocketed. In 1968, credit card debt represented about 5.5% of total outstanding consumer credit.[107] By 2004, revolving credit represented 37% of the total outstanding consumer credit.[108]

It is noteworthy that many of the fees that help to create this alarming level credit card debt are not included in the finance charge. Of the four fees that generated the $24.4 billion in fee income last year, only one fee (cash advance fees) is considered to be a finance charge and included in the APR. The other three fees (late, over-limit, and annual fees) are excluded. Thus, as in 1968, creditors are permitted to "quote a low rate while actually earning a higher yield through additional fees and charges" resulting in "inconsistent and incomparable practices" and "confusion in the public mind about the true costs of credit."

Bankruptcy filings have also increased dramatically since 1968. In that year, consumers filed 189,627 bankruptcies.[109] By 2004, that number rose to 1,624,272 Chapter 7 and Chapter 13 filings.[110]

Consequently, the concerns that Congress hoped to address by enacting the TILA are *more* relevant today than they were in 1968.

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[105] Cardweb.com, *Fee Party* (Jan. 13, 2005), *at* http://www.cardweb.com/cardtrak/news/2005/january/13a.html.

[106] Cardweb.com, *Card Profits 04* (Jan. 24, 2005), *at* http://www.cardweb.com/cardtrak.news/2005/January/24a.html.

[107] This percentage is the result of dividing the dollar amounts of credit reported by Congress in 1968, *i.e.,* $5.3 billion of credit card debt by $95.8 billion of total consumer credit outstanding.

[108] This percentage is the result of dividing the dollar amounts of credit reported by the Federal Reserve Board, Federal Reserve Statistical Release G. 19 (Mar.7 2005), *available at* http://www.federalreserve.gov/releases/g19/current/default.htm. The total of revolving credit in 2004 was $796 billion while the total consumer credit outstanding was $2109.6 billion.

[109] U.S. Bankruptcy Courts, Table F, *available at* http://www.uscourts.gov/bnkrpctystats/statistics.htm#june. Scroll to "12-month period ending June" and click on "1983-2003 Bankruptcy filings." These contain 1968 numbers at the end of all of the charts.

[110] *See* Administrative Office of the U.S. Courts News Release, Number of Bankruptcies Filed in Federal Courts Down Less Than One Percent (Aug. 27, 2004), *available at* www.uscourts.gov/Press_Releases/june04bk.pdf.

5. *The Proliferation of Exceptions to the Finance Charge for Open-End Credit*

The TILA itself contains only a limited number of exceptions from the finance charge. The exemptions relevant to open-end credit are:[111]

- charges of the type payable in a comparable cash transaction;[112]
- life, accident, health, or property damage and liability insurance premiums if certain conditions are met;
- fees paid to public official that are required by law to determine the existence of or for perfecting or releasing or satisfying any security related to the credit transaction;
- premiums payable for any insurance in lieu of perfecting a security interest required by the creditor under certain circumstances;
- taxes levied on security instruments or on documents evidencing indebtedness if the payment of such taxes is a precondition for recording the instrument.[113]

This is a fairly short list. On the other hand, over the years, the Board and Staff increased the number of exclusions from the finance charge via Regulation Z and the Commentary. These Board and Staff-created exceptions include:

- third party charges in certain circumstances;
- application fees charged to all applicants whether or not credit is actually extended;
- fees for unanticipated late payments, for exceeding a credit limit, or for delinquency, default, default, or similar occurrence;
- overdraft fees charged by financial institutions, unless the arrangement to pay these fees was previously agreed to in writing;
- annual or other periodic fees for participation in the plan, including membership fees that are a condition of access to the plan itself;
- debt cancellation coverage charges if certain conditions are met.

Over the years finance charge analysis has evolved from "every fee is a finance charge with a few exceptions" to "some are in and some are out," essentially a Swiss cheese approach. This change is a direct result of the Board's decisions to create many more exceptions to the rule than did Congress.

6. *Categories of Fees and their Effects on Disclosure and the APR*

The Board not only created additional exceptions from the finance charge rule, it created exceptions to the exceptions. Currently, fees that are or can be charged in a revolving credit card plan fall into three categories: finance charges, "other" fees, and a third category created by the Commentary of non-disclosed fees.

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[111] This discussion is limited to open-end credit not secured by real estate.
[112] We discuss this exemption is more detail in Section II.D.
[113] 15 U.S.C. § 1605.

A fee that constitutes a finance charge is subject to certain disclosure requirements and will affect the calculation of the APR. Finance charges must be disclosed at the time of solicitation and application, at the time of account opening, and on the periodic billing statements.[114] In addition, an explanation of how the amount of the finance charge is determined must be provided in the account opening information. Most importantly, the APR disclosed on periodic billing statements must include the finance charges incurred in that billing period. We refer to this APR as the "effective" APR (also sometimes referred to as the "historical" APR). The "nominal" APR is merely the periodic rate imposed by the creditor without the addition of fees that are finance charges. This periodic rate is the only APR disclosed in solicitation, application, and account-opening disclosures.

In 1980, Congress created a category for non-finance or "other" charges.[115] At that time, Congress amended section 1637 and required that "other" charges be identified and their method of computation be described in the account-opening disclosures. Charges that do not meet the finance charge definition are treated as "other" charges. "Other" charges must be listed both on the initial disclosure and on periodic statements if debited to the account during the billing cycle.[116]

Following the statutory revision, the Board defined "other" charges as "any charge other than a finance charge that may be imposed as part of the plan."[117] However, the Staff added the condition that the fee must be "significant" in order to count as an "other" charge.[118] The Staff also added to the Commentary two lists: (1) a list of fees that are considered "other" charges and (2) a list of fees that are neither finance charges or significant" enough to be considered an "other" charge.[119] This created a third category of fees that are neither finance charges or "other" charges, and need not be disclosed at all under TILA exception when actually imposed. However, there is no clear definition of "significant" to help clarify why some fees fall into this category and off the TILA radar screen altogether.

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[114] 15 U.S.C. § 1637; Reg. Z §§ 226.5a (applications and solicitations), 226.6 (account opening disclosures), 226.7 (periodic statements).
[115] Pub. L. No. 96-221, 94 Stat. 132, 178 (Mar. 31, 1980).
[116] Reg. Z §§ 226.6(b), 226.7(h).
[117] Reg. Z § 226.6(b); 46 Fed. Reg. 20892 (Apr. 7, 1981).
[118] Official Staff Commentary § 226.6(b)-1.
[119] Fees that fall into the "other" category include: membership fees, except in certain circumstances; late, delinquency, or default charges; over-limit fees; fees for providing copies of documents in connection with billing error procedures; taxes imposed on a credit transaction; fees for use of an automatic terminal to obtain a cash advance; charges imposed on cash and credit customers to the extent the charge to the credit customer exceeds the fee to the cash customer. Official Staff Commentary § 226.6 (b)-1. Fees that fall out of the reach of TILA altogether include: fees for providing copies of documents for purposes outside the scope of the billing error procedures; collection charges; reinstatement fees; fees for reissuing a card; voluntary insurance premiums; monthly service charges for a checking account with an overdraft feature; automatic teller charges imposed by another institution; taxes, filing fees, or notary fees if excluded from the finance charge; NSF fee for a check submitted as payment that is returned as unpaid; fees to expedite payment; fees to expedite delivery of a credit card. Official Staff Commentary § 226.6 (b)-2.

7. *The Board Endorsed a Highly Inclusive Definition of the Finance Charge in 1998*

In 1998, the Board and the Department of Housing and Urban Development issued a joint report to Congress regarding reform to the TILA and the Real Estate Settlement Procedures Act.[120] While that report dealt with mortgage transactions, the Board's position is instructive to this ANPR. The Board endorsed the APR as a valuable piece of information that allows consumers to evaluate competing products with one variable.

To make the APR more meaningful, the Board recommended a more comprehensive definition of the finance charge. The APR would then become a more accurate and reliable measurement of the cost of credit. In other words, the Board opted to put the truth back into Truth In Lending. Further, a more inclusive definition would create brighter lines for creditors and reduce creditor judgment calls.[121] The Board urged that the finance charge include "the costs the consumer is required to pay to get the credit." Under this standard, most fees incurred by a consumer in a mortgage transaction would be treated as finance charges.[122]

In the credit card context, we believe that the current definition is broad enough to encompass most of the common charges imposed by creditors. Accordingly, we do not recommend a change to the definition of open-end credit. Rather, we recommend that the Board close the loopholes that it has created, as discussed more fully below.

8. *The Current Finance Charge Definition Should Guide the Board in Its Decisions*

As discussed previously, the current finance charge definition in the Act closely matches the Congressional intent that consumers be able to comparison shop and make more informed decisions about when to take on additional debt and at what cost.

This definition breaks down into three components:

- payable directly or indirectly by the consumer;
- imposed directly or indirectly by the creditor;
- as an incident to the extension of credit.

When its components are viewed separately, this definition creates bright lines for creditors, consumers, and enforcement agencies in assessing how a whole range of fees ought to be disclosed and whether they should be included in the calculation of the APR.

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[120]Board of Governors of the Federal Reserve System & the Department of Housing and Urban Development, *Joint Report to the Congress Concerning Reform to the Truth and Lending Act and the Real Estate Settlement Procedures Act* (July 17, 1998), (hereinafter "BOARD/HUD Report"), *available at* http://www.federalreserve.gov/boarddocs/press/general/1998/19980717/default.htm.

[121] *Id.* at 15-16.

[122] For a chart showing which real estate related fees would be in the finance charge, *see* App. C of the Board/HUD Report.

These components should guide the Board in its decisions. They should also provide the analysis for the answers to the Board's questions.

The first component broadly recognizes that what is crucial is not so much *how* the fee may be presented to the consumer, but rather that the consumer ultimately is *paying* that fee, regardless of format or characterization The directly/indirectly language is essential to prevent creditors from circumventing Congress's intent that the finance charge definition be virtually all-inclusive if the APR is to have meaning.

The second component covers a wide variety of charges and makes clear that the creditor does not have to retain the fee or set the amount of the fee. This condition is broader than the standard suggested in Question 16 of the ANPR:[123] that the creditor need only "require" the fee. If that standard were adopted, the intent of the Act would be severely undermined because third party fees that the consumer pays in order to obtain credit may not be directly "required" by the creditor. Further, the amount of the fee usually is not set by the creditor. In addition, certain "voluntary" charges, that, under current law, are *included* in the finance charge if not disclosed properly, would be *excluded*.[124] Finally, the whole question of when a fee is required or optional creates a factual quagmire in every instance and unnecessarily complicates the disclosure regime. For example, should each time the consumer "chooses" to pay a fee trigger disclosures to the consumer about the voluntary nature of this decision, just like the disclosures regarding credit insurance? Disputes about whether the charge was truly voluntary will arise regularly, much as they have in the credit insurance context.[125]

The third component was designed to make clear that the fee must be "related to," "connected to," or "part of" the extension of credit.[126] This very helpful line eliminates fees from the finance charge if they have no relation to the extension of credit. By not stating that the fee must be "significantly" or "substantially" (as opposed to "remotely") related to the extension of credit, Congress speaks loudly that the definition is meant to be inclusive. This element of the finance charge definition rejects the suggestion in Question 17 of the ANPR[127] that the finance charge affect the amount of credit available or the "material" terms of credit. The notion of materiality has had no place in the

[123] Question 16: Some industry representatives have suggested a rule that would classify fees as finance charges only if payment of the fee is required to obtain credit. How would creditors determine if a particular fee was optional? Would costs for certain account features be excluded from the finance charge provided that the consumer was also offered a credit plan without that feature? Would such a rule result in useful disclosures for consumers? Would consumers be able to compare the cost of the of the different plan? Would such a rule be practicable for creditors?

[124] These include credit insurance premiums and charges for debt cancellation products. The Board rejected the argument that voluntary fees are excluded from the finance charge on that basis alone. 61 Fed. Reg. 49237, 49239 (Sept. 19, 1996).

[125] Elizabeth Renuart & Carolyn Carter, *Truth In Lending* § 3.9.4.5.2 (5th ed. 2003 & Supp.).

[126] The Board affirmed these definitions in 61 Fed. Reg. 49237, 49239 (Sept. 19, 1996).

[127] Question 17: Some industry representatives have suggested a rule that would classify a fee as a finance charge based on whether the fee affects the amount of credit available or the material terms of the credit. How would such a standard operate in practice? For example, how would creditors distinguish finance charges from "other charges"? What terms of a credit plan would be considered material?

finance charge definition.[128] If it were injected into the mix, the bright lines that are better achieved with the current definition fall apart. Factual disputes about what is material would inevitably arise.

We agree wholeheartedly with the Board's position, expressed in its Board/HUD Report, that the finance charge should be more inclusive. We believe, as shown below in the finance charge chart, that the current statutory definition can accomplish this goal. Amendments to the Act are unnecessary. As shown in the historical overview presented previously, it has been the Board, *not* Congress, that has expanded the Swiss cheese approach of what is in and not in the finance charge.

9. *Suggested Breakdown of Credit Card Fees Into "Finance" and "Other" Charges*

The following chart sets forth our recommendations as to the treatment of the major types of fees charged in connection with a credit card plan. The categorizations in the chart are based upon the current statutory definition of a finance charge. The fees are bifurcated between finance charges and other charges. The third category of non-finance charge, non-"other" fees is eliminated. We contend that this most closely fits Congress' intent manifested by the 1980 amendments and reflected in section 1637(a)(5).

In addition to our recommendations, this chart includes the rationale for each categorization:

FEE	CHARACTERIZATION (FINANCE CHARGE OR OTHER)	RATIONALE
Annual fee (sometimes billed monthly).	FINANCE CHARGE	Imposed directly or indirectly by creditor; payable directly or indirectly by consumer; incident to the extension of credit. Federal banking agencies define annual fees as "interest" and therefore, this falls into § 1605(a)(1).[129] Also, comparable to a "service or carrying charge" in § 1605(a)(2).
Cash advance fee.	FINANCE CHARGE	Imposed directly or indirectly

[128] The only significant place where the TILA uses a "materiality" standard is in the context of the right of rescission related to non-purchase money mortgage loans. There, the right to rescind is extended up to three years, if the creditor fails to provide the "material" disclosures. 15 U.S.C. § 1635(a); Reg. Z § 226.15(a)(3). However, by regulation, the Board identified defined exactly which disclosures constituted the material disclosures for purposes of the right to rescind. It would be impossible to define what constitutes the material terms of credit in the open-end context as the contract terms vary from plan to plan and creditor constantly change plans.

[129] *See* 12 C.F.R. § 7.4001(a).

		by creditor; payable directly or indirectly by consumer; incident to the extension of credit. Comparable to a "service or carrying charge" in § 1605(a)(2). Federal banking agencies define cash advance fees as "interest" and therefore, this falls into § 1605(a)(1).
Balance-transfer fee.	FINANCE CHARGE	Imposed directly or indirectly by creditor; payable directly or indirectly by consumer; incident to the extension of credit. Comparable to a "service or carrying charge" in § 1605(a)(2).
Late-payment fee.	FINANCE CHARGE	Imposed directly or indirectly by creditor; payable directly or indirectly by consumer; incident to the extension of credit. Federal banking agencies define late fees as "interest" and therefore, this falls into § 1605(a)(1). This definition of interest was upheld by the Supreme Court in *Smiley v. Citibank (South Dakota), N.A.* [130]
Over-the-credit-limit fee.	FINANCE CHARGE	Imposed directly or indirectly by creditor; payable directly or indirectly by consumer; incident to the extension of credit. Federal banking agencies define over-limit fees as "interest" and therefore, this falls into § 1605(a)(1).
Credit-limit-increase fee.	FINANCE CHARGE	Imposed directly or indirectly by creditor; payable directly or indirectly by consumer; incident to the extension of credit. Comparable to a "service or carrying charge" in § 1605(a)(2).

[130] Smiley v. Citibank (S.D.), Nat'l Assn. 517 U.S. 735, 116 S. Ct. 1730, 135 L. Ed. 2d 25 (1996).

Set-up fee.	FINANCE CHARGE	Same rationale as for annual fees.
Return-item fee.	FINANCE CHARGE	Federal banking agencies define NSF fees as “interest” and therefore, this falls into § 1605(a)(1).
Expedited payment fee.	OTHER	Not imposed directly or indirectly by the creditor if the consumer requests this method of payment and if the consumer may make payments on the account by another reasonable means.
Expedited delivery fee.	OTHER	Not imposed directly or indirectly by the creditor provided that delivery if the card is also available by first class mail without paying a fee.
Replacement card fee.	OTHER	Not imposed directly or indirectly by the creditor where the replacement card is not required by the creditor.
Additional card fee.	OTHER	Not imposed directly or indirectly by the creditor where the additional card is not required by the creditor.
Credit insurance premiums	OTHER	As long as the conditions set forth in Reg. Z § 226.4(d) are met.
Debt cancellation coverage	OTHER	As long as the conditions set forth in Reg. Z § 226.4(d) are met.

B. Over-Limit Fees Are Finance Charges And Should Be Treated As Such (Qs 21-22)[131]

In the chart in the previous section, we argue why over-limit fees should be treated as finance charges and not "other" charges. The following section sets forth some factual background in support of this argument.

The Board's decision to exclude over-limit fees from the finance charge dates back to at least 1981.[132] At that time, the credit card industry employed additional steps[133] to authenticate the identity of the customer before approving a specific extension of credit, *e.g.*, a purchase, but *only* if the proposed purchase submitted by the consumer presenting her card exceeded a certain floor limit. Proposed purchases under that limit were in effect automatically approved. This was (and remains) a normal business practice within the banking industry: simply put, it is sometimes *more expensive* to take additional steps to achieve a higher level of authentication and thus authorize a particular transaction than is gained in terms of loss experience from doing so.[134] In this way, credit card issuers built the risk of an acceptable number and amount of mistakes into their cost of doing business by deciding that the resulting losses were acceptable in relation to the cost of authenticating *all* transactions.

Over time, technological developments reduced the costs of authentication to the card issuers, allowing enhanced authentication techniques to be efficiently extended to a broader range of transactions. Specifically, approximately 8 to 10 years ago, VISA and MasterCard began employing electronic authorization on effectively *all* card-based transactions originated in the United States. Thus, authorizations were effectively obtained for *all* such transactions virtually instantaneously The floor limit was effectively reduced to zero for such transactions, and authentication has been substantially improved and losses further controlled within what are to the issuing banks acceptable limits. Floor limits still apply to some foreign transactions.

In addition, card issuers typically now "pad" the nominal credit limit. For example, a consumer enters into a credit card agreement that specifies a credit limit of $2,000. Usually, after a relatively brief period during which the customer manages the account in an acceptable manner, the *pad* is instituted. The card issuer may increase the

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[131] The main author of this section is James Brown, Associate Professor, Center for Consumer Affairs, University of Wisconsin at Milwaukee. Professor Brown's information is based upon his reading and information provided to him by members of the credit card industry through his tenure as: (1) Member, Board of Directors, TYME Corporation (1st shared EFT network in the U.S.), 1982-2002; (2) Member, Board of Directors, Electronic Funds Transfer Association, 1992-present; (3) Expert witness in the *In re* Visa Check/MasterMoney Antitrust Litigation, No. CV 96-5238 (E.D.N.Y.), *see* http://www.constantinecannon.com/pdf_etc/8Constantinedeclaration.pdf at ¶ 69. Professor Brown was also a Member of the Consumer Advisory Council to the Federal Reserve Board from 1979-1981.

[132] *See* 46 Fed. Reg. 20, 892 (Apr. 7, 1981).

[133] For example, comparing the card number with a so-called 'hot card list' or by making a telephone call to obtain an explicit authorization.

[134] A similar dynamic involves the routine practice of a bank *not* comparing signatures of drawers on checks below a certain amount with original signatures on file; i.e., it is *cheaper* for a bank to have to pay on an occasional forged signature than to compare *all* such signatures.

effective credit limit up to $2,500. The *effective* credit limit has become $2,500, even though the consumer may still believe the credit limit is the *nominal* amount of $2,000. This *effective* credit limit, or "break" point, may vary among customers and even for the same customer over time depending on the customer's standing with the card issuer.

Here is an example of how the pad or break point works in practice: Assume that the consumer has a current balance of $1,800[135] on the account. She goes to a store to buy a new television that costs $300. The break point for the card issuer on this account is $2,500. When the consumer presents her card to pay for the merchandise, the request for authorization is forwarded through the system to the issuing bank. The bank compares the impact the requested amount -- $300 – would have on what it relies upon to be the outstanding balance in the account against the 'break point', and authorizes the extension of credit. The purchase is electronically approved, even though the new effective outstanding balance of $2,100 exceeds the nominal credit limit. The consumer will typically pay an over-limit fee for this transaction. However, if the customer attempted to charge an item with a price of $800, the break point would be exceeded and the transaction would be denied. Accordingly, the issuing bank has, in effect, made a *specific* determination to extend the additional $300 worth of credit, notwithstanding that doing so brings the balance, as perceived by the bank at that point in time, *beyond* such (nominal) credit limit.

Card issuers routinely build this pad into the consumer's account, unbeknownst to the customer. The understandable (indeed, laudable) purpose originally was primarily to avoid customer relations problems stemming from denials for proposed charges that would have resulted in a balance exceeding the nominal credit limit *only* by a relatively modest amount. However, with the proliferation of fees, an additional impetus to do so has arisen for card issuers, namely, to generate substantial over-limit fees.

Based upon how the industry actually works, we believe that Question 22[136] mis-characterizes what is actually occurring *functionally*. For those instances in which the consumer is proposing a transaction that is not instantaneously and electronically authorized,[137] the credit card systems and the issuing banks collectively have made a determination that it is, on net, *less* expensive to allow consumers to exceed their nominal credit limits in such relatively limited circumstances than to employ back-up or

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[135] This balance is the amount the issuing bank believes, *at the time of the requested extension of credit,* to be the outstanding balance in the account. Whether other charges or credits may be pending against the account at that time is not relevant for purposes of this analysis. What is indisputable, however, is that the issuing bank *must* have such an *exact* amount against which to make all authorization determinations. If the Bank did *not* have such an amount, it would be unable to distinguish (and authorize) a proposed extension of credit which, while it would result in the *nominal* credit limit being exceeded would *not exceed* the 'break point' from a proposed extension of credit that would exceed *both* the nominal credit limit *and* the break point (and would thus be denied).

[136] Question 22, in pertinent part, states: Because of the technological limitations or other practical concerns, credit card transactions may be authorized in circumstances that do not allow the merchant or creditor to determine at the moment of the transaction whether the transaction will cause the consumer to exceed the previously established credit limit.

[137] For example, certain foreign transactions, or transactions presented when systems are not running in 'real-time', due, for example, to routine maintenance or reconciliation activities.

alternative systems to achieve the prevailing level of authentication that otherwise would be obtained. Doing so, *in effect*, then entails making a determination -- albeit *in advance* -- to authorize such extensions of credit to consumers.

Consequently, such extensions are *not* 'unilateral' on the part of the consumer. Rather, they are decisions *effectively made* by the credit card systems and their member banks. The fact that they are effectively made when the system architecture was created, as opposed to being made at the time the particular consumer presents the card to the particular merchant is frankly irrelevant. It is still a determination by the issuing bank to authorize the transaction. As such, any fees imposed by the issuing banks for exceeding the *nominal* credit limit are "imposed" when they are assessed against the consumer's account, *i.e.*, when the consumer becomes liable for their payment.

Based on this analysis, such extensions are now effectively made pursuant to individualized, conscious determinations by issuers. Further, the practice of explicitly authorizing extensions in excess of the nominal credit limit is increasingly *intended* to generate additional fee income. Thus, these fees should clearly be included within the 'finance charge' as being 'incident to' an extension of credit.

For these reasons, over-limit fees are finance charges because they meet the definition in the Act as they are imposed on the consumer directly by the creditor and are payable by the consumer as incident to the extension of credit. There are no insurmountable practical concerns that mandate a different result. Furthermore, fees imposed for exceeding the credit limit in each month in which the consumer does not bring the account balance below the agreed upon credit limit should be considered finance charges as well. If the credit card agreement allows the creditor to collect fees in this situation, then the first billing statement on which an over-limit fee appears should contain a statement warning the consumer of the effect of failing to pay down the account balance during the next billing period.

C. A "Typical" Effective APR Should Be Disclosed in Solicitations and When the Account is Opened; The Effective APR Should Be Disclosed on Periodic Statements (Qs 23-25)

By itself, the dollar amount of the finance charge is not significantly helpful when a consumer wants to comparison shop or to determine the real effect of certain charges incurred after the account is opened. Consequently, Congress created the concept of the annual percentage rate which expresses the true[r][138] cost of credit as a yearly rate. As Board-sponsored research has shown, consumer reliance upon and appreciation for the APR has grown dramatically since 1967. At that time, 27% of holders of bank-type credit cards were "aware" of the APR. By 2000, that percentage had increased to 91%, using a broad definition.[139]

[138] Depending upon how the finance charge is defined.
[139] Thomas A. Durkin, *Credit Cards: Use and Consumer Attitudes 1970-2000,* Fed. Res. Bull. 623, 631 (Sept. 2000), *available at* http://www.federalreserve.gov/pubs/bulletin/2000/0900lead.pdf.

In the open-end credit context, Congress defines the APR differently depending on when the disclosure is made. A creditor must provide the periodic rate or "nominal" APR before the account is opened.[140] On periodic billing statements, card issuers must disclose the "effective" APR, defined as the total of all finance charges for the period to which it relates divided by the amount upon which the finance charges for that period are based, multiplied by the number of such periods in a year.[141] The Act is silent as to the calculation of APR that must be listed in applications and solicitations.[142] The Board, however, decided that the APR disclosed at the time of solicitation, application, and account opening would be based solely upon the periodic rate.[143]

We recommend the use of a third type of APR, to be disclosed at the time of application, solicitation, and account opening. This APR is a "typical" effective APR, calculated as follows: the sum of all of the effective APRs disclosed on the periodic billing statements over the last three years for all customers with credit card accounts of the same or similar product type to that being offered to the new customer, divided by the number of these effective APRs disclosed to these other customers.[144]

This "typical" APR would be extremely helpful to customers in their efforts to comparison shop for two reasons. First, the periodic rate does not take into account the effect that fees have on the cost of credit that creditors charge. The consumer cannot make an apples-to-apples comparison when shopping by use of the periodic rate and the dollar amount of advertised fees alone. For example, which plan is better? One with a periodic rate of 10.9%, an over-limit fee of $25, balance transfer fee of 3%, and late fee of $29 OR one with a periodic rate of 11.9%, an over-limit fee of $25, balance transfer fee of 2%, and late fee of $39? There is no way to tell because the math is too complicated for most consumers, the late fee and over-limit fees are not finance charges under the present regime, and the actual fee income that this particular card with its particular terms has generated over a period of time is unknown to the consumer.

Second, this "typical" APR is *far more* informative than the periodic rate provided under the current regime in the Schumer box.[145] The "typical" APR is an average APR based on actual fee income produced. As a result, the "typical" APR will reflect the reality of how much this credit card in fact costs for the average consumer who uses it. With an appropriate explanation accompanying the effective APR, the consumer will easily understand the difference between the periodic rate information and the typical APR. For example, the periodic rate could be listed as "the periodic rate." The typical APR could be listed as: "typical APR including fees."

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[140] 15 U.S.C. § 1637(a)(4).
[141] 15 U.S.C. §§ 1606(a)(2), 1637 (b)(6). This is sometimes referred to as the "historical APR."
[142] 15 U.S.C. § 1637(c)(1)(A)(i), merely uses the phrase "annual percentage rate" without specifying whether it is means the periodic rate or the effective APR.
[143] Reg. Z § 226.5a (b)(1).
[144] The three year time period could be defined as: the first 12 quarters of the last 14 quarters preceding the date on which the disclosures are made. This calculation has the advantages of including recent APRs and easing the burden on the creditor of updating the typical APR.
[145] We discuss recommendations for an improved Schumer box that would be provided throughout the life of the credit card account in Section II.E. of these comments.

Providing both the periodic rate and the typical APR at the time of solicitation, application, and account opening would be beneficial to consumers and would fit comfortably within the purposes of the Act.

The disclosure of the effective APR in the billing statement should be retained, and not modified as suggested in Question 25.[146] In the Board/HUD Report issued in 1998, the Board endorsed the APR as a valuable piece of information that allows consumers to evaluate competing products with one variable. The effective APR furthers this goal because it reflects the true cost of a credit plan including both periodic interest and fixed fees, expressed as a percentage. This gives consumers more information than periodic rate alone, allowing the consumer each month to decide whether to keep the credit card or to switch to another plan. Equally important is the sticker shock that consumers may feel when they observe the effect of the finance charges upon the periodic rate. This sticker shock serves a salutary purpose. It can persuade a consumer to decide, for example, not to obtain cash advances using a credit card or to transfer balances to the credit card in the future.

The information that the consumer receives on the periodic statement in conjunction with the effective APR should be improved. Many consumers do not understand the difference between the periodic rate and an effective rate. This difference can be explained quite easily. For example, next to the effective APR, the billing statement could say: "XX% APR (reflects the cost of the credit card plan to you during this month when we take into account A, B, and C (list the finance charges)). Your periodic rate is currently Y%; this rate includes only interest."

The need for retaining, supporting, and expanding disclosures regarding the effective APR in the billing statement is even more crucial given the fact of the proliferation of fees that credit card companies now charge consumers. Credit card fees now produce significant revenue streams for creditors. Consumers need to have the information necessary to decide if they want to open the account, incur certain charges, or switch to another plan, or use a debit card instead. The effective APR, in conjunction with a broad definition of a finance charge, is critical to achieve the goals of TILA.

Simply disclosing the total of fees charged during the billing cycle gives the consumer no sense of the total cost of credit during that period. It is the *combination* of the interest generated by the periodic rate and the finance charges that alerts the consumer to the true cost of the credit. The effective APR most appropriately represents this blend.

D. **The Board Should Reverse the Gaping Hole in the Finance Charge Definition Created By Its Application of the "Comparable Cash Transaction" Exclusion**

If the Board remains as serious as it was in 1998 in tightening up the definition of a finance charge to make disclosures more meaningful for the consumer, it should also

[146] Question 25, in part: Are there alternative frameworks for disclosing the costs of credit on periodic statements that might be more effective than disclosing individual fees and the effective APR?

tackle the issue of comparable cash transactions. Congress added the “comparable cash transaction” exception to § 1605(a) in 1980 to exempt items from the finance charge when the same charge was imposed regardless of whether the consumer used cash or credit. The statutory examples given of fees that satisfy this exemption are sales taxes, license fees, and registration fees.[147] As these fees are charged in both cash and credit situations, it would not make sense to include them in the finance charge, as they have nothing to do with the extension of credit. Were these items included in the finance charge, credit would seem more expensive (relative to cash transactions) than it actually is.

However, the intent of this provision—neutrality between cash and credit transactions as a matter of public policy—has no logical application in the context of non-purchase money credit. While it is easy to envision a cash transaction that is comparable to a credit *sale*, the notion of a cash transaction comparable to a loan of money breaks down conceptually.

Particularly in the context of checking account fees, the Board has construed the “comparable cash transaction” exclusion from the finance charge far too broadly. The use of a check *as a payment mechanism* is not comparable to a loan. Bounce loans are the prime illustration of the pitfalls of the Board’s current approach, which allows lenders to exclude bounce loan fees from the definition of finance charge to the extent that the fee does not exceed that imposed for NSF checks. NSF charges and bounce loan fees are not cash and credit alternative means of completing the same transactions; they are associated with entirely different transactions, in both concept and reality. NSF fees are penalties for consumer mistakes; bounce fees are charges for the use of highly marketed short-term credit. Thus, the “comparable cash transaction” exception should simply not be an issue in analyzing bounce loan transactions.

An exploration of the regulatory history of 12 C.F.R. § 226.4(b)(2) reveals that this is an exception that has extended far beyond the original statutory concept of a comparable cash transaction. Section 226.4(b)(2) [then numbered 12 C.F.R. § 226.4(a)(2)] finalized in 1969 simply provided that “[s]ervice, transaction, activity, and carrying charges” constituted finance charges.[148] The regulation was later amended in 1981 after TIL Simplification, at which time the Board added the comparable cash transaction analysis to its current text. This amendment stated that the finance charge also includes “any charge imposed on a checking or other transaction account to the extent that the charge exceeds the charge for a similar account without a credit feature.”[149] The section was moved at that time and became section 226.4(b)(2).

[147] *See* S. Rep. No. 96-73, at 12 (1979) (“The bill will eliminate some current confusion by making clear that charges which would also be incurred in a similar transaction for cash, such as sales taxes, license and registration fees, are not to be included in the finance charge.”); S. Rep. No. 96-368, at 26 (1979) (same). “The Board has given examples such as “fees for optional maintenance agreements or fees paid to process motor vehicle registrations.” 61 Fed. Reg. 49237, 49239 (Sept. 19, 1996)

[148] Final Rule, Truth in Lending, 34 Fed. Reg. 2002, 2004 (Feb. 11, 1969). In 1980, the Board re-affirmed its longstanding position that such transaction and account charges constituted finance charges. 45 Fed. Reg. 80,656 (December 5, 1980).

[149] 46 Fed. Reg. 20,848, 20,894 (Apr. 7, 1981). At the same time, section 226.4(a) was amended to reflect the comparable cash transaction analysis, and like Congress, the Board stated the intent of this amendment

When section 226.4(b)(2) was promulgated in 1969 and amended in 1981, there were only three ways of dealing with an overdrawn check – bounce products did not exist.[150] Furthermore, the history of this provision makes clear that it addressed only account activity and maintenance fees, not the fee for the extension of credit itself. For example, the 1969 version stated in a footnote to § 226.4(b)(2) that checking account charges were finance charges to the extent they exceeded "any charges the customer is required to pay in connection with such an account *when it is not being used to extend credit.*"[151] The Board reinforced this line-drawing in its 1980 proposal when it listed examples of charges that were not intended to be finance charges, such as fees for "issuance, payment, or handling of checks or for account maintenance…"[152] Consequently, the Board never intended section 226.4(b)(2) to exempt charges specifically imposed for the extension of credit itself.

Furthermore, this history indicates that the Board necessarily assumed that the "charge" at issue was for *the same service, feature, or product*. For example, under this provision, it would not make sense to exempt from the definition of "finance charge" a cash advance fee simply because it did not exceed the fee for a completely different service, such as a wire transfer.

Similarly, the Staff Commentary to section 226.4(b)(2), which specifically deals with overdraft charges, was written to address an exemption from the finance charge for overdraft fees at a time when banks were routinely and actively discouraging overdrafts. Indeed, the Board has recognized that its regulatory scheme contemplates a traditional courtesy overdraft program, when a bank may have paid a customer's insufficient funds check on an ad hoc, discretionary basis.[153] While this exception to inclusion in the finance charge may work for these types of bank decisions, it is currently being deliberately exploited by banks for the sole purpose of avoiding application of the consumer protections of the TILA to bounce loan products. The Board surely recognizes that the current bounce loan product is very different from the ad hoc situation discussed above, even if some banks now argue otherwise. Indeed, bankers on the Consumer Advisory Council consistently have indicated at CAC meetings that the marketed bounce loan programs significantly deviate from ad hoc programs.

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was to exempt "charges imposed uniformly in cash and credit transactions, such as sales taxes or license or registration fees…" *Id.* at 20,854-55.

[150] The three ways were: 1) by returning the check and charging an NSF for compensating the bank for the special handling of the check which was intended as a disincentive to the consumer to engage in this practice; significantly, the bank's own funds are not extended to cover the consumer's check; 2) by *ad hoc* payment of the check for an NSF fee, charged for the same reasons as when the check is returned unpaid; and 3) by payment of the check by accessing a line of credit or another account.

[151] Final Rule, Truth in Lending, 34 Fed. Reg. at 2004, n.2 (emphasis added).

[152] 45 Fed. Reg. 29,701, 29707 (May 5, 1980). In addition, the Supplementary Information states that this provision "clarifies that the portion of *checking account maintenance fees* that are attributable to the existence of a credit feature (for example, overdraft line of credit) are included in the finance charge." *Id.* (emphasis added).

[153] "Paying consumers' occasional or inadvertent overdrafts is a long-established customer service provided by depository institutions. The Board recognized this longstanding practice when it initially adopted Regulation Z in 1969…" Proposed Rule, 69 Fed. Reg. 31,760, 31,761 (June 7, 2004).

We understand the desire to preserve the exemption for traditional, *ad hoc*, occasional overdrafts. However, this logic simply does not extend to bounce loan fees for the reasons we have articulated in previous comments to the Board. With traditional courtesy overdrafts, the penalty nature of the overdraft fee gives some basis for a claim of comparability. With bounce loan fees, the fee is no longer a penalty, because the bank has encouraged the overdraft in order to reap the fee amount. The fee is now a revenue generator for high-priced credit, a totally different creature than a penalty NSF fee.

We urge the Board and Staff to update Regulation Z and the Commentary by eliminating the exception to the finance charge rule for bounce loans. The exception would still apply to true *ad hoc* courtesy overdraft decisions by banks. For example, we suggest that Regulation Z and the Commentary be amended as follows. [Note: Changes are italicized.]

> *Regulation Z § 226.4(b)(2):*
>
> "Service, transaction, activity, and carrying charges, including any charge imposed on a checking or other transaction account to the extent that the charge exceeds the charge *for the same service, feature, or product* for a similar account without a credit feature."
>
> *Commentary § 226.4(b)(2)-1:*
>
> Checking account charges. A checking or transaction account charge imposed in connection with a credit feature is a finance charge under section 226.4(b)(2) to the extent the charge exceeds the charge *for the same service, feature, or product* for a similar account without a credit feature. If a charge for an account with a credit feature does not exceed the charge *for the same service, feature, or product* for an account without a credit feature, the charge is not a finance charge under section 226.4(b)(2). *For example:*
>
> i. A $5 *per check issuance fee* is imposed on an account with an overdraft line of credit (where the institution has agreed in writing to pay an overdraft), while a $3 *per check issuance fee* is imposed on an account without a credit feature; the $2 difference is a finance charge. (If the difference is not related to account activity, however, it may be excludable as a participation fee. See the commentary to section 226.4(c)(4).)
>
> ii. A $5 service charge is imposed for each item that results in an *unanticipated, occasional* overdraft, while a $25

> service charge is imposed for returning each item on a similar account without a credit feature; the $5 charge is not a finance charge. *An overdraft is be considered "unanticipated" if an institution does not solicit or encourage overdrafts, advertise, publicize, or promote the availability or ability to overdraft, communicate to consumers a maximum "limit" for which overdrafts may or will be paid, and there is no overdraft line of credit. An overdraft is not considered "unanticipated" if an institution knowingly or deliberately permits overdrafts by non-check methods. An overdraft is considered "occasional" if the institution does not pay more than one overdraft per quarter. An institution may pay more than one (1) overdraft in a quarter if the overdrafts are the result of a single incident, such as a deposit that does not clear before checks are paid. An institution, however, must document the reason that multiple overdrafts were permitted, in these instances.*

E. <u>The Board Should Require a Clear and Uniform Schumer Box in Applications/Solicitations, Initial Disclosures, Periodic Statements, and Change-of-terms Notices (Q 2-3, 6-11, 24, 29-30)</u>

1. The Manner of Making Disclosures Must be Improved

Disclosure alone is insufficient to bring fairness to the open-end credit marketplace. Nonetheless, the disclosures required for open-end credit can and should be substantially improved. The previous section of these comments discussed the critical need to improve the *content* of open-end credit disclosures, by returning to Congress' original vision of the finance charge as an accurate reflection of the cost of credit. This section discusses the need to improve the *manner* in which disclosures are made: which disclosures are made when, and in what format.

The key question in evaluating the current open-end disclosure requirements is whether consumers are getting the information they need, in a usable form, at the time they need it. Unfortunately, the answer too often is no. The terms of open-end credit are disclosed bit-by-bit across multiple documents, in formats that differ from document to document and from creditor to creditor. Too often, important credit terms are buried in densely-packed columns of microscopic type.

In its request for comments, the Board recognized the need to make open-end credit disclosures simpler and easier to navigate. We recommend that the Board use the Schumer box concept to achieve this goal. The Schumer box is the most successful part of the disclosures for open-end credit at the application/solicitation stage. Our proposal is to expand the Schumer box requirement so that it applies not just to applications and

solicitations but also to initial disclosures, periodic statements, and change of term notices. We also recommend changes to enhance the uniformity, readability, and usefulness of the disclosures.

2. *Rationale for Using a Revised Uniform Schumer Box*

Under the current version of the TILA and Regulation Z, applications and solicitations for credit cards must display certain information in a table known as the Schumer box.[154] The Schumer box is helpful to consumers because it makes it possible to compare various credit card offers at the application or solicitation stage. However, credit shopping is just as important after the application/solicitation stage.

Including a Schumer box disclosure as part of the initial disclosures is important because the creditor may have provided the consumer credit card terms different from those the consumer expected. Including a Schumer box in the initial disclosures would reveal these discrepancies. It would enable the consumer to compare the card that was provided with the card that was offered, and also with other available cards that the consumer might acquire and use. Making information about the actual terms of their own credit cards readily available to consumers would increase knowledgeable credit shopping and enhance competition. Adding a Schumer box to the initial disclosures would also help solve the information overload problem, because it would capsulize the most important information in an easy-to-read format that is already familiar to the consumer.

Consumers continue to need a clear, simple display of the basic terms of their credit cards after the initial disclosure stage. This is especially important if creditors continue to be allowed to change credit card terms, a practice that, as we argue elsewhere in these comments, should be greatly restricted. As long as creditors are allowed to change terms, including a Schumer box on periodic statements and change-of-terms notices would help the consumer determine whether to shop for a different card. Without a table showing all the current terms of the credit card, a consumer who receives a change-of-terms notice must hunt through the application/solicitation disclosures, the initial disclosures, and any earlier change-of-terms notices to assemble a current set of terms. Including a Schumer box on periodic statements would also alert the consumer to the potential charges and fees actually charged on the card, making it easier for the consumer to avoid them.

In order for the Schumer box to be continued past the application/solicitation stage, there need to be changes in its content. For example, we recommend that the Schumer box provided with solicitations and applications and at the time the account is opened include a “typical” APR. We suggest that the typical APR be replaced with the actual effective APR on the billing statements. Some changes are also necessary to simplify the content of the Schumer box and make the terms and format more uniform. In addition, creditors must not be allowed to obscure the terms they are actually offering.

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154 15 U.S.C. § 1632(c); Reg. Z § 226.5a(a)(2).

These issues are discussed in the following subsections, concluding with responses to certain specific questions that the Board asked in its ANPR.

The Board's broad authority over the content and format of open-end credit disclosures enables it to make these changes without additional Congressional authority. 15 U.S.C. § 1632(a) allows the Board to set the order and terminology of disclosures except as otherwise provided. Section 1632(c)(1)(B), which requires the Schumer box, allows the Board to depart from the order and terminology set forth in the statute, except for use of the term "grace period." Section 1632(c)(2) gives the Board even greater authority, allowing it to determine whether it is "practicable and appropriate" for the Schumer box to include the information specified in the statute. Section 1637(c)(5) gives the Board authority to require applications and solicitations to include additional disclosures not mentioned in the statute and to modify any of the required disclosures. Even more broadly, § 1604(a) provides that the Board's regulations "may contain such classifications, differentiations, or other provisions, and may provide for such adjustments and exceptions for any class of transactions, as in the judgment of the Board are necessary or proper...."

3. *Our Proposed Schumer Box*

ACCOUNT TERMS[155]

PERIODIC RATE for purchases	0.0% for the first six billing cycles. After that, 12%. (The periodic rates disclosed here and in the next box do not include fees and charges other than interest.)
Other periodic rates	Cash advance: 12% Balance transfer: same as for purchases Default periodic rate (see conditions below*): 21%
Typical **ANNUAL PERCENTAGE RATE (APR)**[156] including fees [on periodic statements this would read "Your APR including fees"]	18.4% (This APR includes fees and charges.)
Variable rate information	Your APRs may vary. The rate for purchases (after the first six billing cycles), cash advances, and balance transfers is determined quarterly by adding 15% to the Prime rate.° The rate for the Default APR is determined quarterly by adding 16.4% to the Prime rate.°
Annual fee	None
Minimum **finance charge**	For each billing period that your account is subject to a finance charge, a minimum total FINANCE CHARGE OF $1.00 WILL BE IMPOSED.
Late charge	$29 if your payment is more than ten days late
Over-the-credit-limit fee	$29
Cash advance fee	3% of the amount of the advance, but not less than $10.00
Balance transfer fee	3% of balance transferred (minimum $10, maximum $75)
Miscellaneous fees	Set-up charge: $10 Credit limit increase charge: $10 Expedited payment fee: $10
Credit limit	$10,000
Security interest required	None
Grace period	20 days, but none for balance transfers or convenience checks

*Your APR will increase to the default APR if your payment is late twice in any six-month period.
°The "Prime Rate" is [explain].

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[155] Our inclusion of an improved manner of disclosing a particular fee should not be construed as supporting the imposition of or the amount of the fee.
[156] The APR and finance charge disclosures must be disclosed more conspicuously than all of the other information. 15 U.S.C. § 1632(a).

4. The Schumer Box Should Include Those Terms Most Important For Credit Shopping

In order to foster comparison shopping by consumers, the Schumer box should include the most important financial terms for credit cards. At the same time, the Schumer box must avoid information overload. Otherwise, the important terms may be buried in a welter of unimportant or unintelligible information. In addition, the Board should require some measure of uniformity in terminology and format, so that consumers can make comparisons readily. The specific items in the proposed Schumer box are discussed one-by-one below, followed by a discussion of one specific item - the balance calculation method - that should be excluded from the Schumer box.

Periodic Rates. Regulation Z currently requires the periodic rates that apply to different types of transactions to be disclosed in applications/solicitations, the initial disclosures, and periodic statements. [157]It is common for creditors to disclose the periodic rate for purchases on a separate line in the Schumer box, because of the special type size requirements for teaser rates.

The periodic rate should continue to be required as part of the Schumer box. To promote competition and comparison shopping, the Schumer box, with this same information, should be required on the initial disclosures, the periodic statement, and any change of term notices that are allowed. If the creditor changed the periodic rate at any stage, then the Schumer box on the periodic statement would reflect the new periodic rate.

In addition, the Board should require that applications and solicitations disclose the actual periodic rate that the creditor is offering. The Schumer box on one application or solicitation we reviewed for these comments disclosed the following about the periodic for purchases:

> A 0% APR until the first day of the billing cycle that includes 8/01/03. After that, 8.9%[1] variable, 10.9% variable or 12.9% variable, depending on our review of your application and credit history.
>
> [1]Your APR for purchases and balance transfers after the introductory period will be based on our review of your application and credit history. You understand that the terms of your Account, including the APRs, are subject to change. Any such changes will be made in accord with the Cardmember Agreement.

This disclosure provides no helpful information. It does not tell the consumer what he or she is applying for. Even the three rates quoted are illusory, since the footnote reserves the right to change them. Allowing such a meaningless disclosure fosters bait and switch tactics. Regulation Z should be amended to require the Schumer box to disclose the actual periodic rate (and the actual other terms) that the creditor is offering. We recommend that the Board add the following at the end of Reg. Z § 226.5(c):

[157] Reg. Z §§ 226.5a(b)(1), 226.6(a)(2), 226.7(d).

(c) In applications and solicitations the disclosure must reflect the actual terms offered, not a range of terms.

"Typical" Rate. Under the present disclosure rules, at the time of applying for open-end credit, and at account opening, the only APR that is disclosed to the consumer is the periodic rate. This periodic rate represents only one portion of the finance charges that the consumer can expect to incur upon using the credit. For example, it does not take into account minimum finance charges, balance transfer fees, transaction fees, and annual fees, all of which we argue are finance charges in part II.A.. The consumer is given an APR reflecting all finance charges only after using the card. The result is that at application and account opening the consumer is given only an artificially low APR.

One credit card solicitation we reviewed for these comments exemplifies the abuses that can occur when creditors are allowed to disclose an APR that does not reflect all finance charges. This solicitation trumpets, in large type, "Low **2.9%** Fixed APR for CASH ADVANCE CHECKS *and* BALANCE TRANSFERS until August 2005." In fact, however, in addition to the periodic rate, the terms of the offer require the consumer to pay a cash advance or balance transfer fee of 3%, with a minimum of $10 and a maximum of $75. As a result, the consumer would *always* pay an effective APR considerably higher than 2.9% for cash advances and balance transfers.

Our proposal is that, at the application and account opening stages and in change-of-term notices, the creditor be required to disclose a "typical" APR, including fees and charges, that consumers pay for the particular open-end credit product, using the term "Typical APR including fees." As explained in Section II.C, this APR would be calculated as the average effective APR disclosed on periodic statements over the last three years for customers with that same or similar credit card product. On periodic statements, the disclosure would be replaced by the effective rate as defined in Reg. Z, § 226.14(c) using the term "Your APR including fees." The term "APR" should be used only for these typical and effective APRs, not for the periodic rates that make up just one component of the APR.

By disclosing the "typical" APR including fees and charges, creditors would give consumers a much more accurate picture of the cost of credit than is now required. Accurate information about the cost of credit is critical if consumers are to be able to shop for credit. Having to disclose an APR that includes fees and charges would also place some downward pressure on these elements of the charges. The current disclosure requirements allow creditors to trumpet low periodic rates while soft-pedaling the other real components of the costs of the credit.

Effective APR. In part II.C, we strongly recommend that the Board retain the disclosure of the effective APR on the billing statement. We suggest that the language regarding the typical APR be removed on the billing statement Schumer box and the following language would substitute: "XX% ANNUAL PERCENTAGE RATE, Your APR include fees." This APR would be the actual APR for that billing statement based upon the periodic rate in effect and the finance charges, if any, imposed by the creditor for that

period. The remainder of the Schumer box would reflect the contract terms in effect during that month, just as it did at the earlier stages of the disclosure regime.

Variable rate information. Regulation Z currently requires variable rate information to be included in the Schumer box on applications and disclosures;[158] in the initial disclosure statement;[159] and in periodic statements.[160] Our proposal is merely to make this disclosure simpler, more uniform, and more reader-friendly by making it part of a Schumer box at all three of these stages, and to expand the requirement to any change of term notices.

Annual fee. As currently written, Regulation Z requires annual fees to be disclosed in the Schumer box in applications and solicitations.[161] The annual fee must also be disclosed as part of the initial disclosure's description of how any non-interest portion of the finance charge will be determined.[162] In periodic statements the annual fee need only be disclosed if it is charged in that cycle.

Since annual fees have been the subject of bait and switch marketing,[163] it is particularly important that they be highlighted in a standard format that can be compared from one document to another and from one stage to another. If the consumer applies for a credit card that advertises no annual fee, the initial disclosure should state - in the same format - whether the card actually issued to the consumer requires an annual fee. As noted elsewhere in these comments, creditors should not be allowed to change their annual fee policies. But until they are prohibited from changing their annual fees, they should be required to disclose the annual fee in a Schumer box along with the other information about the card in every periodic statement and change-of-terms notice. These disclosures will enable the consumer to evaluate whether the card is still a good deal.

Minimum finance charge. Regulation Z currently requires any minimum finance charge to be disclosed in the Schumer box on application and solicitations as well as in the initial disclosures.[164] The impact of our proposal is simply to require this disclosure to be made in a uniform manner at both stages, and to continue it on periodic statements and change-of-terms notices. Since a minimum finance charge can have a significant effect on the cost of credit, converting what appears to be a low APR into something much different, it is the type of information that should be highlighted by including it in a uniform tabular format.

Late Fee. Currently, Regulation Z requires applications and solicitations to disclose the late charge, but it does not have to be in the Schumer box.[165] Late fee information must

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[158] Reg. Z § 226.5a(b)(1)(i).
[159] Reg. Z § 226.6(a)(2) n. 12.
[160] Reg. Z § 226.7(d) n. 15.
[161] Reg. Z § 226.5a(a)(2)(i), (b)(2).
[162] Reg. Z § 226.6(a)(4).
[163] *See* Rossman v. Fleet Bank, 280 F.3d 384 (3d Cir. 2002).
[164] Reg. Z § 226.5a(b)(3), 226.6(a)(4).
[165] Reg. Z § 226.5a(a)(2)(ii), (b)(8).

also be included in the initial disclosures.[166] We propose that the Board require the late fee to be part of the Schumer box, to be included on the application or solicitation, the initial disclosures, the periodic statements, and any change-in-terms notices.

As discussed in Section I.B.1, the amount of the standard late fee has risen dramatically in the past decade, and late fees make up a substantial part of credit card companies' profits. The OCC brought a proceeding against one company, Providian National Bank, for manipulating dates of receipt of payments so that it could charge late charges,[167] Other suits have challenged the generation of late fee income by the use of early morning cut-off times for posting of payments.[168] For these reasons, late charge information should be highlighted more than current Regulation Z requires. It should be included in the Schumer box, which should be included in disclosures at all stages of the transaction.

In addition, Regulation Z should explicitly require that not just the amount of the late charge but also the conditions for imposing it be disclosed. Creditors can use a short payment due date to make it difficult for consumers to avoid late payments. Bringing the conditions for imposing a late charge out into the sunlight is the minimum (but still not sufficient) step necessary to deter some unfair late payment practices. Accordingly, Reg. Z § 226.5a(b)(9) should be amended to require disclosure of:

> (9) Late payment fee. Any fee imposed for a late payment, *and the conditions for imposing it.*

Over-the-credit-limit fee. Under the current version of Regulation Z, the creditor must disclose the over-limit fee on the application or solicitation, but it need not be in the Schumer box.[169] As for the initial disclosures, they must list the amounts of fees other than finance charges that may be imposed as part of the plan.[170] . Even though over-limit fees are not listed specifically in Official Staff Commentary § 226.6(b)-1, they fall within this general description so must be included in the initial disclosures.

Because of their abusive potential, over-limit fees should be restricted, for the reasons explained in Section I.B.2 of these comments. They should be treated as a finance charge, as discussed in Section II.B. To the extent over-limit fees continue to be allowed, their inclusion in the Schumer box should be mandatory rather than optional, so that consumers can easily compare this important term from one credit card to another, and the fee should be disclosed not just on applications/solicitations and in the initial disclosures but also in periodic statements and change of term notices.

Cash advance fee. Currently Regulation Z requires any cash advance fee to be disclosed on applications and solicitations, but the creditor has the option of including it in the

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[166] Reg. Z § 226.6(a)(4).
[167] *In re* Providian Nat'l Bank, No. 2000-53 (Dept. of the Treasury, Office of the Comptroller of the Currency June 28, 2000), *available at* www.occ.treas.gov/FTP/EAs/ea2000-53.pdf.
[168] *See* Section I.B.2 of these comments.
[169] Reg. Z § 226.5a(2)(ii), (b)(10).
[170] Reg. Z § 226.6(b).

Schumer box or disclosing it elsewhere.[171] In the initial disclosures, disclosure of cash advance fees is required.[172] On periodic statements, any cash advance fees that were charged during the billing period must be itemized, but otherwise the schedule of fees need not be disclosed.[173]

We recommend that these fees be disclosed in a uniform Schumer box that creditors would be required to include on applications/solicitations, initial disclosures, periodic statements, and change-of-terms notices. Since cash advance fees can drive up the cost of credit significantly, they are an important term for consumers who are shopping for credit. Consumers should not only be told what the cash advance fee is when they apply for credit, but when credit is granted they should be told, in an easily readable table, whether credit card terms actually include the promised cash advance fee. Repeating this disclosure in the same easily readable format in the periodic statement and any change-of-terms notices helps the consumer keep track of any changes in the fee structure and reduce the cost of credit by minimizing expensive transactions.

Balance transfer fee. Regulation Z treats balance transfer fees the same as cash advance fees. Any balance transfer fee must be disclosed on applications and solicitations, but need not be in the Schumer box.[174] These fees must also be disclosed in the initial disclosures, and any balance transfer fees actually charged during the billing period must be itemized on the periodic statement.[175]

Balance transfer fees should be disclosed in a uniform Schumer box for the same reasons as cash advance fees should. It is particularly important to disclose balance transfer fees in a prominent and uniform manner because of the strenuous marketing of balance transfers in recent years.

Miscellaneous fees. Under the current version of Regulation Z, the only fees other than annual fees and transaction charges for purchases that must be disclosed on applications and solicitations are cash advance fees, late payment fees, over-limit fees, and balance transfer fees.[176] These fees may be, but need not be, disclosed in the Schumer box. The initial disclosures must disclose how the finance charge will be determined, plus the amounts of any charges other than finance charges that may be imposed as part of the plan.[177]

Junk fees have proliferated in credit cards in recent years. While there appears to be some competition, at least of the bait-and-switch sort, in annual percentage rates and annual fees, there is no competition as to other fees. For this reason, disclosure alone is insufficient to rein in junk fees. Nonetheless, disclosing junk fees in a more prominent

[171] Reg. Z § 226.5a(a)(2)(ii), (b)(8).
[172] Reg. Z § 226.6(a)(4).
[173] Reg. Z § 226.7(f).
[174] Reg. Z § 226.5a(a)(2)(ii), (b)(11).
[175] Reg. Z §§ 226.6(a)(4), 226.7(f).
[176] Reg. Z § 226.5a(b)(8)-(11).
[177] Reg. Z § 226.6(a)(4), (b).

and uniform manner may have some effect on the market, if only by alerting consumers to avoid the circumstances in which junk fees can be imposed.

The fee disclosures in the Schumer box should not be limited to certain specified fees. Limiting the disclosure in applications and solicitations to certain specified fees creates the incentive for creditors to devise new fees that do not have to be disclosed so prominently. Instead, the Schumer box - which should appear not just on applications and solicitations, but also on the initial disclosures, periodic statements, and change-of-terms notices - should require disclosure of all fees, whether or not the fee is part of the finance charge.

If the Board excludes any fees, as it currently does in OSC § 226.6(b)-2, the list should be an exclusive list, i.e. a fee must be disclosed unless it appears on the list. Further, if the Board excludes any fees, it should require creditors to report periodically on the volume of excluded fees collected. If a certain type of fee increases in volume, it should be deleted from the list of excluded fees on the ground that it has become a more significant component of the cost of credit.

Credit limit. The credit limit is a key factor for many consumers in shopping for a credit card. It is also a means by which creditors generate junk fees, through the imposition of over-limit fees. We argue elsewhere in these comments that over-limit fees should be substantively restricted. But if they are not substantively restricted, at least the credit limit should be disclosed to the consumer prominently and often, so that the consumer can avoid over-limit fees.

The credit limit has also been subject to bait-and-switch by creditors. The OCC recently cautioned banks against marketing credit cards with credit limits "up to" a stated amount that is far greater than most of the consumers are likely to receive. [178]

Despite the importance of the credit limit, Regulation Z does not require it to be disclosed anywhere - whether on the application/solicitation, the initial disclosures, or the periodic statement. The Board should not only require it to be disclosed, but should require it to be part of the Schumer box to be included on application/solicitations, initial disclosures, periodic statements, and change of term notices. To prevent the sort of deception that the OCC described, the creditor should be required to state a specific credit limit, not an "up to" amount, on the credit card application or solicitation as well as on subsequent disclosures.

Security interest required. Under the current version of Regulation Z, whether the creditor requires a security interest for the credit card need only be disclosed in the initial disclosures.[179] But a security interest is a very important consideration in credit shopping, especially for low-income consumers. Some credit cards marketed to lower-income consumers require a security interest. By not requiring this fact to be disclosed in applications and solicitations, Regulation Z facilitates bait-and-switch tactics by which

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[178] OCC Advisory Ltr. AL 2004-10 (Sept. 14, 2004), *available at* www.occ.treas.gov/Advslt04.html.
[179] Reg. Z § 226.6(c).

consumers think they are applying for unsecured credit cards, only to find out that a security interest is required. In addition, many credit card issued by merchants are secured by the goods that the consumer purchases, but consumers are often unaware of the security interest.

For all of these reasons, any required security interest should be disclosed as part of the Schumer box not only in the initial disclosures but also in applications/solicit-ations, periodic statements, and change-of-terms notices. The disclosure should state whether a security interest is required. If a security interest is required, the disclosure should describe it briefly, such as "in items purchased with card" or "required $200 deposit."

Grace period. The current version of Regulation Z, and the statute itself, require the disclosure of the grace period, using that term, in the Schumer box on applications and solicitations.[180] The initial disclosure must also include this information.[181] The periodic statement must disclose the "free-ride period," which appears from its description to be the same as the grace period.[182] We recommend that the Board mandate a single uniform word or phrase to refer to this term, and that creditors be required to disclose it in a uniform tabular format on all applications/solicitations, initial disclosures, periodic statements, and change of term notices.

5. *Other Information Should Be Disclosed Immediately After, But Not In, the Schumer Box.*

What is *not* included in the Schumer box is just as important as what *is* included. Including unimportant information, or information that is difficult to understand, needlessly increases the length and complexity of the disclosure. Including too much information dilutes the impact of the information that is critical for credit shopping. For these reasons, we recommend that one credit term currently included in the Schumer box - the method of calculating the balance on which the finance charge will be computed for purchases - not be included in the Schumer box. We also recommend that the Board add a requirement that the method of calculating the minimum payment be disclosed, again outside the Schumer box.

Balance Calculation Method. The balance calculation method should *not* be disclosed in the Schumer box.

While our proposal adds several items to the Schumer box, we also recommend that one item - the method of calculating the balance on which the finance charge will be computed for purchases - be deleted from the Schumer box. This information is of little use to consumers in shopping for credit. Only a tiny minority of consumers have any understanding of the different balance calculation methods. Even if consumers understood these shorthand descriptions, they would be of little use because the creditor is only required to use a shorthand description that the actual calculation method most

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[180] 15 U.S.C. § 1632(c)(2)(C); Reg. Z § 226.5a(b)(5).
[181] Reg. Z § 226.6(a)(1).
[182] Reg. Z § 226.7(j).

closely resembles. In other words, Regulation Z allows the shorthand descriptions to be inexact. And, even if the descriptions were exact and consumers understood them, it is highly unlikely that any consumer has ever used the balance calculation method as a factor in shopping for credit. The implications of the balance calculation method on the actual cost of credit are simply too complex and too contingent on future purchasing patterns to be of any use to consumers in shopping for credit.

For these reasons, we recommend that the Schumer box no longer include the balance calculation method. Instead, the balance calculation method should be disclosed - outside the Schumer box - in periodic statements. The balance calculation method is useful at that point for consumers who want to determine whether their balance was calculated correctly. The periodic statement should include not just a shorthand term for the balance calculation method, but a complete mathematical description or a toll-free telephone number and web address where such a description can be obtained. By including this information on the periodic statement when a consumer might actually make use of it, the Board would avoid information overload at other stages.

It appears that the Board has the flexibility to exclude the balance calculation method from the Schumer box. The Truth in Lending Act requires the Board to prescribe tabular format for certain information.[183] Based on a series of cross-references that lead to § 1637(c)(1)(A)(iv), it appears on first reading that the balance calculation method is one of the disclosures that the Act requires the Board to include in the Schumer box.[184] However, a close examination of the Act shows that it only requires the Board to prescribe tabular format for the specified information "to the extent the Board determines to be practicable and appropriate."[185] This language gives the Board the discretion to determine that including the balance calculation method in the Schumer box is not appropriate.

Alternatively, should the Board decide to retain the balance calculation in the Schumer box (or permit them to be provided outside of the box), we urge the Board to adopt the "Energy Star" type of disclosure described in comments to this ANPR filed by the Center for Responsible Lending.

Minimum payment. The amount of the monthly payment is important for many consumers. Perhaps the first question a person asks when contemplating an extension of credit is "Can I afford the monthly payment?" Even though making the minimum monthly payment is sometimes a bad decision in the long-term, consumers should at least know what it is.

At present, Regulation Z does not require the creditor to disclose the method it will use to set the consumer's minimum monthly payment. This disclosure need not be made in advertisements or solicitations or in the initial disclosures. (Nonetheless, of the

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[183] 15 U.S.C. § 1632(c)(2)(A).

[184] *See* 15 U.S.C. § 1632(c)(2)(A), which refers to "such disclosures." That term appears to refer to the disclosures listed in § 1632(c)(1) by cross-reference to § 1637(c)(1)(A), which includes the balance calculation method.

[185] 15 U.S.C. § 1632(c)(2).

applications/solicitations we reviewed, at least one disclosed the minimum payment calculation method quite prominently immediately under the Schumer box). Even the periodic statement need not contain this information under current requirements. In light of the importance of this information, we recommend that the Board require it to be disclosed on applications/solicitations, initial disclosures, periodic statements, and change of term notices.

6. Regulation Z's Requirements for the Format and Language of Disclosures Should Be More Specific

In addition to revising the content of the Schumer box and non-Schumer box disclosures as discussed above, the Board should be more specific in requiring uniformity in the format and language used to make disclosures. First, as stated in Section II.E.3 of these comments, the Board should require cash advance fees, late payment fees, over-limit fees, and balance transfer fees to be disclosed in the Schumer box, rather than giving creditors the option of disclosing these fees elsewhere. The applications and solicitations we reviewed in preparing these comments were inconsistent how they disclosed these fees and where they placed them. This inconsistency makes side-by-side comparison of credit terms difficult. Under the current system, if a fee is not disclosed in the Schumer box, it does not mean that the creditor does not charge that fee. It only means that the consumer has to search through the rest of the application/solicitation to see if the terms include that fee. Uniform, prominent disclosure of fees is especially critical in light of the proliferation of fees in credit card transactions.

Second, creditors should be required to use substantially the same headings, content, format, *and order* as the Board's model forms. Including the same disclosures in the same order facilitates side-by-side comparison. We recommend that Reg.Z § 226.5a(a)(2)(i) be revised to require that the Schumer box disclosures be:

> (i) in the form of a table with headings, content, *order*, and format substantially similar to any of the applicable tables found in appendix G.

Third, the Board should prescribe the exact language to be used in more of the required disclosures. For most terms, Regulation Z does not specify the language that creditors must use, so it is common for different creditors to use different words to describe the same credit term. A particularly important example is the disclosure of penalty rates. The use of penalty rates means that creditors who market to low-income consumers can disclose an APR that is illusory, because the creditor knows that the actual APR will soon rise for many consumers. As discussed elsewhere in these comments, penalty rates should be substantively restricted, but to the extent penalty rates are still allowed the Board should require disclosure using uniform terms so that consumers can easily compare one credit card offer to another. While the two model forms in Appendix G to Regulation Z use the term "penalty rate," none of the applications/solicitations we reviewed in preparing these comments used this term. Instead, they used terms such as "default rate," "delinquent balances fixed," "late payment APR," and "default/closure."

The lack of uniformity in language to describe this important term makes it less likely that consumers will be able to compare one offer to another.

Fourth, the Board should establish an affirmative requirement as to type size, not just for the Schumer box but for all open-end credit disclosures. Official Staff Commentary § 226.5a(2)-1 currently provides a safe harbor for disclosures in applications and solicitations that are in 12-point type or greater, and states that 8-point type is probably too small. Nonetheless, one of the credit card solicitations we reviewed in preparing these comments had a Schumer box in 7-point type. Not only was the font tiny, but the letters were squeezed together, making the text very difficult to read. A New York case involves credit card disclosures made in 6-point type.[186] Examples like this show that Regulation Z's approach of merely encouraging use of a readable typeface, without setting a standard, is inadequate.

Further, Regulation Z provides *no* typeface requirement or even guidance for disclosures other than those in applications and solicitations. The sample change-of-terms notice at Attachment 2 is printed in, at most, *4.5 point* and extremely dense type.

The intent of the Truth in Lending Act is to require disclosures that can be read by the consumer. The examples describe above show that, without a typeface requirement, the provision of disclosures becomes merely a ritualistic but meaningless act. Regulation Z should be amended to require disclosures to be in a 12-point typeface (as opposed to 10-point type or 8-point type). We recommend that Reg. Z § 226.5(a)(1) be revised to read:

> (1) The creditor shall make the disclosures required by this subpart clearly and conspicuously in writing, *in 12-point type or greater,* in a form that the consumer may keep.

Fifth, as discussed in Section II.E.3 above, the Board should require that disclosures in applications and solicitations reflect a set of *actual* terms that the creditor is offering, not a range of *possible* terms. To the extent Regulation Z currently allows disclosure of a range of terms, it makes the disclosures meaningless and fosters bait and switch tactics.

Sixth, the Schumer box should not substitute for the other information required on billing statements. This additional information includes the outstanding balance in the account at the beginning of the statement period, the amount and date of each extension of credit, the total amount credited to the account during the period, the itemization of the finance charge, the balance on which the finance charge was computed, the outstanding balance in the account at the end of the period, the date by which the payment must be made to avoid finance charges, and the address used by the creditor for the purpose of receiving billing inquiries.[187] The box and the additional information can co-exist comfortably.

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[186] Sims v. First Consumers Nat'l Bank, 758 N.Y.S.2d 284 (N.Y. App. Div. 2003).
[187] 15 U.S.C. § 1637(b).

Finally, we recommend that the Board adopt a general requirement that disclosures that need not be made in the Schumer box must be made immediately following the Schumer box. This requirement should apply to applications/solicitations, initial disclosures, and change-of-terms notices. However, because of their unique formatting, it should not apply to periodic statements. At present, Section 226.5(a)(1)-1 of the Official Staff Commentary sets forth a general rule that disclosures need not be segregated from other material or located in any particular place on the disclosure statement. We recommend that this statement be deleted from the Commentary. Instead, the following new subparagraph should be added to Reg. Z § 226.5(a):

> *Any disclosures that are required to be made on applications or solicitations, initial disclosures, or change-of-terms notices but that are not required to be in tabular form must be made immediately following the table and segregated from all other information.*

7. *Responses to ANPR Questions*

The foregoing discussion has addressed a number of the questions the Board posed in its ANPR:

Q2: What formatting rules would enhance consumers' ability to notice and understand account-opening disclosures? We recommend:

- the use of a Schumer box in account-opening disclosures, with uniform terminology and format;
- a requirement that disclosures be in at least 12-point type; and
- a requirement that non-Schumer box disclosures follow immediately after the Schumer box.

Q3: Are there ways to use formatting tools or other navigational aids for the TILA's account-opening disclosures that will make the disclosures more effective for consumers throughout the life of the account? Our basic recommendation is the use of a Schumer box in account-opening disclosures. An executive summary is an interesting alternative approach, but we believe that the uniformity of a Schumer box that would appear not just on applications and solicitations but on all disclosure documents, has the advantage of simplicity and uniformity.

Q6: How could the use of formatting tools or other navigational aids make the disclosures on periodic statements more effective for consumers? We recommend that creditors be required to include a Schumer box on periodic statements, setting forth the terms of the account.

Q7: Is the Schumer box effective as currently designed? Are there format issues the Board should consider? The Schumer box is perhaps the most successful feature of

open-end credit disclosures, but changes are necessary to make it more effective. The Board should:

- Rework the requirements for the content of the Schumer box.
- Require the Schumer box to include a disclosure of the typical APR including fees for solicitations, applications, initial and change-of-terms disclosures; include the effective APR in the Schumer box on the billing statement.
- Require cash advance fees, late fees, over-limit fees, balance transfer fees, and any other fee that constitutes a finance charge to be included in the Schumer box, rather than giving creditors discretion about where to disclose them
- Require the credit limit and any security interest requirement to be disclosed in the Schumer box
- Delete the balance calculation method from the Schumer box
- Require the Schumer box to reflect the actual credit terms offered, not a range of terms
- Require greater uniformity in language and format of the Schumer box

Q8: Should balance transfer fees and cash advance fees be included in the Schumer box? Yes. The Board should explicitly require that these fees, and others, be disclosed in the Schumer box.

Q9: Are there formatting tools or navigational aids that could more effectively link information in the account-opening disclosures with the information provided in subsequent disclosures, such as those accompanying convenience checks and balance transfer checks? We recommend that the Board require the Schumer box to be included in subsequent disclosures.

Q10, Q11: Should the Board revise its model clauses and forms, or promulgate new ones? Our proposal for a revised Schumer box, to be required not just in applications and solicitations but also in account-opening disclosures, periodic statements, and change of term notices, is set forth in these comments.

Q29, Q30: Do consumers understand balance calculation methods? Would additional disclosures at account opening be helpful? How much detail should be disclosed at account opening and on periodic statements? The balance calculation method is difficult for consumers to understand and is of little use in credit shopping. It is primarily useful for consumers who have received a periodic statement and are trying to reconstruct how their balance was calculated. We recommend that the balance calculation method be deleted from the Schumer box. Periodic statements should disclose either the complete mathematical description or a shorthand term with a reference to a toll-free telephone number and website where the complete mathematical description can be obtained.

Q24: Are there ways to improve consumers' understanding of the effective APR, such as providing additional context for this disclosure? We recommend that the effective APR be described as "including fees and charges," and that a similar phrase be

required to indicate that the periodic rate does not include fees and charges other than interest.

F. Exemptions and Tolerances (Q 37, Q 41, Q 53)

1. *The Board Should Not Exempt Any Transactions Under § 1604(a) or (f)*

Question 41 asks whether the Board should exercise its authority under §§ 1604(a) or (f) to exempt certain classes of transactions. We strongly oppose any exemptions. The Truth in Lending Act provides fundamental disclosures regarding the cost of open-end credit. Without these disclosures, price competition is impossible. Any exemptions would undermine the goal of increasing competition. Exemptions would also undermine the goal of uniformity in disclosures, which would increase consumer confusion. The Act's substantive protections for users of open-end credit are equally critical.

The ANPR does not mention any specific proposals for exemptions, and we hope that means that the Board is not actively considering granting any exemptions. If any specific proposals for exemptions surface, we ask that the Board publish a second ANPR so that we can comment specifically on the proposal.

2. The Board Should Not Exempt Transactions for Persons With Income and Assets Over Specified Amounts

Section 1604(g) allows the Board to exempt transactions with high-income or high-asset consumers from all requirements of the Truth in Lending and Consumer Leasing Acts. The transaction must involve a consumer whose annual earned income exceeds $200,000 or whose net assets exceed $1,000,000, and the consumer must sign and date a handwritten waiver. (The Board can adjust the dollar amounts for inflation). In Question 42 the Board asks whether it should exercise this exemption authority.

Allowing high-income or high-asset consumers to waive the TILA's protections would have nothing but negative effects. It is hard to imagine what purpose would be served by not disclosing the annual percentage rate to high-income or high-asset consumers. They have just as much at stake as low and moderate-income consumers. Indeed, the dollar amounts at stake for a high-income or high-asset consumer are likely to be greater. What purpose would be served by denying periodic statements and Fair Credit Billing rights to high-income or high-asset consumers? Those rights are one of the key protections against identity theft, of which these individuals are likely targets. Even if the Board did not want to protect the individuals themselves, it benefits society when identity theft is discovered and prosecuted. Otherwise, identity theft is not deterred and thieves remain free to prey on others.

It is hard to fathom any rationale for exempting high-income or high-asset consumers. It is true that these consumers are more likely to be well-educated than the average consumer, but only a tiny percentage would be likely to know what they were

waiving if they waived their rights under the Truth in Lending and Consumer Leasing Acts. And, having an income over $200,000 does not mean that a consumer will be able to translate a contract interest rate to an APR so that a meaningful comparison of the costs of various credit options can be made.

While an exemption under § 1604(g) would directly affect only high-income or high-asset consumers, it would indirectly affect all consumers, including the low-income consumers on whom the National Consumer Law Center focuses. The disclosures that the TILA requires foster rate competition, or at least create the environment in which rate competition can occur. Precluding rate competition for even a segment of the market makes the whole market less competitive.

Granting such an exemption would do great harm while providing little or no benefit to the consumer credit industry. It would reduce the uniformity that the consumer credit industry prizes. Creditors would have to distinguish between different categories of customers, and would have different disclosure requirements and different documents for different categories. The time and effort to verify the consumer's assets and income, and then obtain the handwritten, signed, dated waiver that the TILA requires would run against the increasing trend toward automating extensions of credit. In short, an exemption under § 1604(g) would have great costs and few benefits. The Board should not grant an exemption.

3. The Board Should Clarify the Scope of State Exemptions

Congress gave the Board the power to exempt any class of transactions within a state from "the requirements" of Parts B, D, and E of the Truth in Lending Act.[188] The Board has used this authority to grant exemptions to Connecticut (Parts B and D), Maine (Parts B, D, and E), Massachusetts (Parts B and D), Oklahoma (Parts b and E), and Wyoming (Part B).[189] However, the Board's wording about the scope of the exemptions has caused confusion and should be corrected. While the ANPR did not list this provision of the Regulation in its questions, Question 58 asks whether there are other sections of the Regulation that should be revised.

When the Board granted these exemptions, it explicitly preserved the federal cause of action provided by the TILA:

> (b) *Civil liability*.
>
> (1) No exemptions granted under this section shall extend to the civil liability provisions of sections 130 and 131 of the Act.
>
> (2) If an exemption has been granted, the disclosures required by the applicable state law (except any additional requirements not imposed by federal law) shall consitute the disclosures required by this Act.

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[188] 15 U.S.C. §§ 1633, 1666j(b), 1667e(b).
[189] Official Staff Commentary § 226.29-4.

The Board has explained this carve-out as "assur[ing] that consumers retain access to both federal and state courts in seeking damages or civil penalties for violations, while creditors retain the defenses specified in those sections." Official Staff Commentary § 226.29(b)-1. Without this carve-out, the Board "would be forced to examine state rules of procedure to see if remedies and methods available in federal court would be available in the state court as well. This would, at the very least, require the Board to acquire expertise in an area foreign to its normal function.[190]

We have no quarrel with the exemption of the five states, and we applaud the Board's preservation of the federal cause of action and liability rules. However, there is an ambiguity in Reg. Z § 226.29(b)(2) that the Board should take this opportunity to correct. That section states that the *disclosures* required by the state law shall constitute the disclosures required by the TILA, but is silent about non-disclosure requirements. For example, § 1637, which is included in Part B of the TILA, requires a creditor who grants a variable-rate home equity line of credit to use a publicly available index for the rate that is not under the creditor's control. To qualify for an exemption from Part B, a state must have a requirement that is substantially similar to this. But does a violation of the state law version of this requirement constitute a TIL violation that is enforceable under the TILA? Of course, the requirement of an objective index for a variable rate is *tied* to a disclosure requirement, because § 1637a(2) requires disclosure of the index. But since Reg. Z § 226.29(b)(2) only says that state *disclosure* requirements constitute the *disclosures* required by the TILA, the answer is unclear.

Part D of the TILA also includes many credit billing requirements that go beyond disclosure. Again, many of these requirements are tied to a disclosure. For example, § 1666(a)(3)(B)(2) requires a creditor who concludes that there was a billing error to correct it and transmit a notice to the consumer about the correction. But other requirements, such as the requirement that payments be promptly credited, are less clearly tied to a disclosure. Does this mean that a consumer has a federal cause of action only for the former, and not the latter?

The same question comes up with respect to the right of rescission in § 1635. Does a consumer in a state that is exempt from Part B have a federal cause of action when a creditor refuses to honor a consumer's rescission notice? A Massachusetts decision, now on appeal to the First Circuit, holds that there is no federal cause of action for rescission, but only for TIL damages.[191] This holding turns the TILA on its head, denying a federal cause of action for rescission, often a significant remedy involving forgiveness of tens of thousands of dollars in finance charges and closing costs, while allowing federal jurisdiction over damage claims which are capped at $2000.

As presently phrased, Reg. Z § 226.29(b)(2) causes uncertainty and needless complications in TIL litigation. There is no rationale that would support classifying disclosure requirements and non-disclosure requirements differently for purposes of the

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[190] *Ives v. W.T. Grant Co.,* 522 F.2d 749, 756 n. 10 (2d Cir. 1975) (summarizing an amicus brief submitted by the Board in support of the retention of federal court jurisdiction).

[191] Belini v. Washington Mutual Bank, CA Nos. 04-30083 MAP, 03-CV-301175-MAP, *appeal docketed*, No. 04-2532, 04-2533 (1st Cir.).

consumer's cause of action. By suggesting such a distinction, the current phrasing of the Regulation needlessly prolongs and complicates TIL litigation by introducing a set of complex jurisdictional questions.[192]

Preserving the federal cause of action only for disclosures and not for the TILA's other requirements is inconsistent with the reasons for the rule that the Board articulated in the commentary and in the *Ives* brief that was written soon after the state exemptions were first granted. Since the Act itself allows the Board to exempt states from the *requirements* of various Parts of the TILA, the Board should rephrase Reg. Z § 226.29(b) as follows to track the TILA's language:

> (b) *Civil liability*.
> (1) No exemptions granted under this section shall extend to the civil liability provisions of sections 130 and 131 of the Act.
> (2) If an exemption has been granted, the requirements of the applicable state law (except any additional requirements not imposed by federal law) shall constitute the *requirements* of this Act.

In addition, to clarify that consumers in exempt states retain a federal cause of action for rescission claims, Official Staff Commentary § 226.29(b)-1 should be rephrased to read:

> 29(b) *Civil liability*.
> 1. *Not eligible for exemption.* The provision that an exemption may not extend to sections 130 and 131 of the Act assures that consumers retain access to both federal and state courts in seeking damages, civil penalties, *rescission*, or other relief for violations, while creditors retain the defenses specified in those sections.

4. The Board Should Not Adopt Tolerances for Open-end Credit (Q 37)

Question 37 asks whether the Board should adopt tolerances for open-end credit disclosures under § 1631(d). This section allows the Board to establish tolerances for numerical disclosures other than the annual percentage rate if tolerances "are *necessary* to facilitate compliance" with the TILA. The test of necessity sets a high bar. In addition, if the Board adopts any tolerances, the statute requires that they be narrow enough to prevent disclosures from becoming misleading and to prevent circumvention of disclosure requirements.

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[192] The reference to "the disclosure requirements" of state law and TILA in current Reg. Z § 226.29(b)(2) has been carried over from Reg. Z § 226.12(c)(2) as originally adopted in 1971. *See* 40 Fed. Reg. 1040, 1041 (Jan. 22, 1971). Perhaps this language can be explained by the fact that most of the non-disclosure requirements of TILA were added after 1971. For example, the Fair Credit Billing Act was added in 1974, the substantive restrictions on home equity lines of credit were added in 1988, and the HOEPA restrictions were added in 1994.

Tolerances are particularly unnecessary because of the nature of open-end credit disclosures. The initial disclosures primarily set forth the rules of the account. These disclosures require no difficult mathematical calculations. Asking the creditor to disclose its own rules accurately is a simple matter. There can be no credible claim that allowing inaccuracy in these initial disclosures is *necessary* to facilitate compliance. To the contrary, allowing inaccuracies in the initial disclosures would encourage bait-and-switch tactics, already a serious problem in the credit card industry.[193]

Likewise, the numerical disclosures on the periodic statement require no complicated mathematical calculations. By the time the periodic statement is issued, the transactions reflected on it have *already occurred,* and the creditor is *asking the consumer to pay the amounts shown.* Creditors cannot claim that it is necessary to disclose imprecise amounts when they have kept track of the exact amounts for their own purposes and are asking the consumer to pay those amounts.

The Board asks in particular whether it should allow an overstatement of the finance charge. The answer is unequivocally "no." First, there no showing that such a tolerance is *necessary*. Since all the events and transactions on which the finance charge is based have already occurred by the time the creditor sends the periodic statement, and since the creditor *is billing the consumer for the finance charge*, it cannot be difficult for creditors to state the amount of the finance charge. If creditors claim that the problem is determining whether a particular charge is a finance charge, that is simply another reason to adopt the bright-line rules for the finance charge that we propose in Section II.A of these comments.

Second, allowing overstatement of the finance charge would violate the statutory mandate that any tolerances be designed so that disclosures do not become misleading. In fact, it is difficult to imagine how a tolerance would work. Would the periodic statement ask the consumer to pay the exact amount of the finance charge, but elsewhere disclose an inaccurate amount? Such a rule would be a recipe for consumer confusion. Or would the creditor not only disclose an overstated finance charge, but also bill the consumer for it? Certainly the Board does not want to countenance this sort of bill-padding.

Allowing inaccurate disclosure of the finance charge would be particularly harmful because of the enormous growth of fees in credit card transactions. The differences in disclosure requirements between the APR and fees have encouraged creditors to trumpet low APRs while expecting to make most of their profits from fees that are less prominently disclosed. Any reduction in the accuracy of disclosure of the finance charge would only add to this problem, because if the finance charge is inaccurately disclosed the consumer cannot accurately compare the terms of one credit card to another. Rather than undercutting the accuracy of the disclosure of fees, the Board should require that fees be disclosed more prominently, as discussed in Section II.E.3 of these comments.

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[193] *See* Rossman v. Fleet Bank (R.I.), Nat'l Assn., 280 F.3d 384 (3d Cir. 2002).

5. *The Board Should Seek Legislative Authority to Adjust All Numerical Figures in the TILA (Q 53)*

Question 53 asks whether the Board should adjust certain exceptions to Regulation Z that are based on *de minimis* amounts. Adjustment of these *de minimis* amounts is appropriate, but *the Board must also seek Congressional authority to adjust the TILA's other numerical thresholds.*

In the ANPR, the Board mentions two *de minimis* amounts. First, Reg. Z § 226.5(b)(2)(i) allows a creditor not to send a periodic statement if the outstanding debit or credit balance is $1.00 or less and no finance charge is imposed. The $1.00 figure has been in effect since Regulation Z was adopted in 1969.[194] Updating the $1.00 figure to account for inflation is justified. According to the Department of Labor's cost of living calculator at www.bls.gov, if this figure were increased to $5.15 it would equal the same purchasing power as $1.00 in 1969. (Whether or not the amount is increased, the Regulation should be revised to make clear that the creditor can dispense with the periodic statement only if nonpayment carries *no* negative consequences to the consumer, including not just finance charges but also late charges and negative credit reports.)

The second *de minimis* amount that the Board mentions is the simplified way to calculate the effective APR on periodic statements when a minimum finance charge is assessed that is 50 cents or less.[195] The 50 cent figure has also been in effect since 1969,[196] and should also be updated. Increasing it to $2.50 or $3.00 would take inflation since 1969 into account.

Far more important, however, is updating both the TILA's jurisdictional amounts for non-mortgage transactions and the statutory damage amounts. The Act currently only covers non-mortgage transactions in which the total amount financed exceeds $25,000. This limit leaves a significant number of consumer car sales and leases without even the disclosure protections of the TILA and Consumer Leasing Act. The erosion of these amounts due to inflation significantly undermines the Truth in Lending Act. According to the Department of Labor's cost of living calculator, the purchasing power of $25,000 had eroded to $4857.10 by 2004. When the exception for transactions over $25,000 was adopted in 1969, it excluded only a few very high-end consumer transactions. Increasing this figure to $128,678 would account for inflation only through 2004, so it should be updated to at least $250,000 to account for future inflation.

Likewise, the $1000 statutory damage figure adopted in 1969 is now the equivalent of just $194.28. Increasing it to $5147.14 would account for inflation only through 2004. It should be increased to at least $10,000 to take future inflation into account.

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[194] *See* Reg. Z § 226.7(b), *adopted by* 34 Fed. Reg. 2007 (Feb. 11, 1969).
[195] 12 C.F.R. § 226.14(c)(4).
[196] *See* Reg. Z § 226.5(a)(3), *adopted by* 34 Fed. Reg. 12004 (Feb. 11, 1969).

If the Board adjusts the *de minimis* amounts to account for inflation, it must also seek Congressional authority to adjust the far more significant figures for jurisdictional coverage and statutory penalties in the Act itself.

III. NEXT GENERATION AND SPECIAL PRODUCT ISSUES

A. Electronic Disclosures: The Interim Rule Should Be Amended to Comply with E-Sign

In 2001, the Board announced interim rules for electronic disclosures under the TILA, as well as other consumer protection statutes.[197] At the time these rules were first proposed, the consumer community vehemently objected to the several significant omissions and problems. While the effective date for the rules was suspended indefinitely,[198] improvements and clarifications of these problems are still very necessary.

Rather than providing an even playing field for electronic disclosures, the Interim Rule makes accessing and retaining electronic disclosures much more difficult, and considerably more risky than the use of paper disclosures. The Interim Rule allows the use of electronic disclosures in situations which will facilitate - if not encourage - fraud. We are particularly concerned about the following ways, among others, which the Interim Rule is contrary to E-Sign:

- The Rule fails to follow the mandates of E-Sign's consumer consent provision, requiring that the method of consent "reasonably demonstrates" the consumer's ability to access and retain electronic information. This failure is particularly evident in face-to-face situations where the Interim Rule appears to condone a consumer's electronic consent using computer equipment supplied by the creditor.
- The Rule allows creditors to deliver important pre-application disclosures without consumer consent, even in face-to-face situations, when no such exemption is permitted by E-Sign's consumer consent provision.
- The Rule allows creditors to "deliver" the TILA notices to a consumer by posting them on a website and sending a paper notice notifying the consumer to access the website to obtain the disclosures. This requires a burdensome process for the consumer to actually obtain the disclosure. E-Sign specifically contemplates that electronic delivery will have the same degree of assurance of actual receipt as paper copies, not less assurance.
- The Rule appears to allow creditors to remove disclosures from their website after 90 days without providing consumers another method of obtaining copies of the disclosures. This ignores two mandates in E-Sign: one, that consumers be permitted to request paper copies; and two, that electronic records be accessible to all parties to the transaction.

The Board should address these problems with electronic disclosures.

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[197] 66 Fed. Reg. 17329 (Mar. 30, 2001).
[198] 66 Fed. Reg. 41439 (Aug. 8, 2001).

B. Subprime and Secured Credit Cards (Q 39, 43, Q 56)

The Board at Question 39 asked whether there should be special disclosures for subprime or secured credit cards. We believe that the problems with subprime and secured credit cards go beyond disclosure issues. Instead, they are related to how banks fundamentally treat consumers unfairly, without respect, and attempt to squeeze every penny possible, especially from consumers in difficult financial situations. Singling out subprime credit cards will not sufficiently address the abusive practices in the industry as a whole.

The abuses peculiar to subprime credit cards have been documented by the federal banking regulators in the few consumer protection enforcement actions they have taken. These include:

- "Downselling" consumers by prominently marketing one package of credit card terms, but then approving consumers only for accounts with less favorable terms.[199]
- Issuing credit cards with low credit limits, then adding mandatory fees or "security deposits" resulting in little or no available credit when the consumer receives the card.[200]
- Deceptively marketing credit "protection" products.[201]

State Attorneys General have taken action against some subprime card issuers as well. For example, Cross County Bank is a major subprime credit card issuer that allegedly earned half a billion dollars in the last 8 years.[202] A number of state Attorneys General have sued Cross County Bank for debt collection abuse and electronically withdrawing payments from consumers' bank accounts without their permission.[203]

While these cases shed light on the particular abuses in the subprime industry, they are in some ways an extension of the harsh practices of "mainstream" credit card lenders. Also, a "prime" credit card can quickly become "subprime" with a change-in-terms notice, the imposition of a penalty rate, or one of the other abusive practices discussed in Section I.B. For example, a single late payment on a "prime" credit card

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[199] Consent Order, *In re* Direct Merchants Credit Card Bank, No. 2001-24 (Dept. of Treasury, Office of the Comptroller of Currency, May 3, 2001)

[200] *In re* First Nat'l Bank in Brookings, No. 2003-1 (Dept. of the Treasury, Office of the Comptroller of the Currency January 17, 2003); *In re* First Nat'l Bank of Marin, No. 2001-97 (Dept. of the Treasury, Office of the Comptroller of the Currency December 3, 2001).

[201] *In re* Providian Nat'l Bank, No. 2000-53 (Dept. of the Treasury, Office of the Comptroller of the Currency June 28, 2000)

[202] Mitchell Pacelle, *Pushing Plastic Combative Banker Faces State Suits Over Credit Cards*, Wall St. J, Nov. 5, 2004, at A1.

[203] Cross County Bank v. McGraw, No. 04-C-464 (Cir. Ct. Kanawa County W. Va. Dec. 9, 2004); Order Granting Motion for Temporary Injunction, State of Minnesota v. Cross County Bank, No. MC 03-5549 (Minn. Dist. Ct. - 4th Dist. Nov. 10, 2004); People v. Applied Card Sys., Inc., No. 2073-03 (N.Y. Sup. Ct. May 28, 2004) (transcript of proceedings), *available at* http://www.oag.state.ny.us/press/2004/jul/6a.pdf. *See also*, *Lautenschlager Suing Delaware Credit Card Issuer*, Greater Milwaukee Business Journal, Nov. 21, 2003, *available at* http://www.bizjournals.com/milwaukee/stories/2003/11/17/daily40.html.

account may result in the imposition of a $35 fee and an increase in the APR from a reasonable 10% to a sky-high 28%. This account now bears the hallmarks of a subprime credit card --- high rates and high fees.

Furthermore, each of the abuses discussed above is also committed or reflected in the practices of "prime" credit card issuers.

Subprime Practice	Analogous Industry-wide Practice
Downselling	Promoting low APRs but then not approving the consumer for that APR until after a review of the consumer's credit score. A survey by Consumer Action found that over half of credit card issuers will not provide a firm APR until after a screening the consumer's credit history, even though the creditor likely pre-screened the consumer before mailing the solicitation.[204] Deceptive bait & switch - issuers lure consumers with initially low APRs and no annual fees, then use change-in-terms provisions and penalty rates to increase the APRs and impose annual fees months later. (Section I.B.2)
Issuing cards with little or no usuable credit limit	Similar to this abuse, prime card issuers lower the credit limits of consumers, then charge them over-limit fees (Section I.B.2) For cardholders carrying a large balance, the imposition of multiple junk fees, high finance charges from a penalty rate, and useless credit protection products may push their balances over the limit. (See the case of Ruth Owens in Section I.A.2.)
Deceptively marketing credit protection	Prime card issuers also sell credit "protection" that are of limited value. These products are expensive, only suspend payments when upon a triggering event, and likely have very low loss ratios.[205]
Debt collection abuses	Prime credit card issuers also engage in debt collection abuses (see section I.B.2)

Thus, the abuses of subprime issuers are an extreme version of the abuses that exist in general in the credit card industry. It is easy to go after the very worst abusers in an industry with enforcement actions or heightened disclosures. It's harder to tackle the abusive industry-wide practices. However, American consumers desperately need the Board and Congress to do the latter. Some of the reforms discussed in other parts of this Comment that would address these abuses include:

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[204] Linda Sherry, *Annual Credit Card Survey 2004*, Consumer Action (May 2004), *available at* http://www.consumer-action.org/English/CANews/2004_May_CreditCard/.

[205] Caroline E. Mayer, *Lenders Peddle Protection, at Hefty Profit*: *Debt Coverage Unregulated and Pricey for Consumers*, Wash. Post, Mar. 13, 2004, at E1, *available at* http://www.washingtonpost.com/ac2/wp-dyn/A54467-2004Mar12.

Legislative:

- A cap on all periodic finance charges, for example, prime plus 10%. This would limit the incentive for bait and switch tactics.
- A cap on all other charges, whether considered a finance charge or not, to an amount the card issuer can show is reasonably related to cost. This would limit issuers from packing junk charges onto both prime and subprime cards.
- No unilateral change-in-terms allowed. This is one mechanism that permits bait and switch tactics.
- Most importantly, a private right of action to enforce Section 5 of the Federal Trade Commission Act. Many of the practices discussed above are already deceptive or unfair practices prohibited by the FTC Act. The problem is that injured consumers cannot use the FTC Act to seek relief when victimized.
- Meaningful penalties for violating any substantive or disclosure rules which stings the issuer sufficiently to provide real incentives to obey the rules. Again, many of the above practices are already illegal, but the penalties for violating the law currently do not provide an adequate deterrent for abuse.

Regulation Z:

- Requiring that creditors disclose the actual APR that the creditor is offering in applications and solicitations disclosures.
- Disclosing a "typical" APR, which would give consumers an indication of the issuer's track record of imposing non-periodic rate finance charges and junk fees on a particular card product.
- Requiring a Schumer box at every stage of the credit process. A Schumer box during the initial disclosures will reveal any discrepancies between what the creditor advertised and what the terms of the agreement really are.

IV. FAIR CREDIT BILLING ACT & SPECIAL CREDIT CARD SUBSTANTIVE PROTECTIONS

The Fair Credit Billing Act ("FCBA") and the special credit card provisions at Section 1643 (unauthorized use protection) and Section 1666i (cardholder's right to withhold payment/preservation of claims and defenses) are some of the few substantive protections contained in the TILA. As such, they provide consumers with a modicum of protections for an industry that is thinly regulated outside of disclosures. These protections are especially critical to protect consumers from two common forms of fraud: identity theft and telemarketing/Internet fraud.

A. The Definition of "Cardholder" Should Include Identity Theft Victims

As we all know, identity theft is the fastest growing crime in the U.S., with over 200,000 complaints to the Federal Trade Commission in 2003. According to the FTC, one-third of identity theft complaints in 2003 involved credit card fraud.[206]

A report commissioned by the FTC estimates that the cost of misuse of existing credit cards and credit card accounts costs $50 billion a year, with the average cost per victim being $4,800.[207] This is the most commonly reported form of identity theft.[208] The report estimates that there are 6.68 million victims of this form of identity theft.[209] Sixty seven percent of victims said the thief misused an existing credit card account in their names;[210] 8% reported that the thief opened a new credit card account.[211]

The TILA's credit card protections remain the most effective tool for consumers to defend themselves from fraudulent charges incurred by identity thieves. FCBA permits consumers to challenge fraudulent charges to the consumer's already existing account. As for new accounts, one would assume that the TILA's protections for unauthorized use would protect consumers.

However, one problematic issue is that the TILA's protection for unauthorized use at section 1643 protects "cardholders," which is defined as "any person to whom a credit card is issued" under section 1602(m). Thus, a creditor could argue that a victim of identify theft is not a "cardholder" under the TILA because the creditor did not issue the card to the victim, but actually issued it to the thief. While some courts have rejected that argument,[212] this argument has been accepted by at least one court.[213]

Thus, there is some ambiguity about the definition of "cardholder." However, the language in the Act is broad enough to encompass identity theft victims, as shown by the two courts that have ruled in the victim's favor. Thus, we ask that the Board amend Regulation Z, § 226.2(a)(8) to make clear that a "cardholder" under section 1602(m) includes a victim of identity theft by stating:

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[206] Federal Trade Commission, *National and State Trends in Fraud & Identity Theft: January - December 2003* (, Jan. 22, 2004).
[207] Synovate, Inc., Federal Trade Commission, *Identity Theft Survey Report*, at 6 (Sept. 2003), *available at* http://www.ftc.gov/os/2003/09/timelinereport.pdf.
[208] *Id*. at 11.
[209] *Id*. at 7.
[210] *Id*. at 33.
[211] *Id*. at 34. This was half of all victims who reported that a new account had been opened in their names.
[212] Baker v. Citibank (S.D.) Nat'l Assn., 13 F. Supp.2d 1037 (S.D. Cal. 1998) (construing ''cardholder'' in state law in manner consistent with TILA, court held that identity theft victim was "cardholder" because card was issued in her name, even though imposter received card). *Cf.* Michigan v. Collins, 405 N.W.2d 182 (Mich. App. Ct. 1987) (upholding criminal conviction against identify thief for use of credit card against "cardholder"; victim was "cardholder" despite the fact that she did not request the card and it was not physically issued to her)
[213] Monogram Credit Card Bank v. Morris, 2002 WL 31360695 (N.Y.City Civ. Ct. May 10, 2002) (identity theft victim could not bring claim under TILA against creditor because creditor never issued victim a credit card.)

> (8) "*cardholder*" means a natural person to whom a credit card is issued for consumer credit purposes, *a natural person in whose name a credit card is issued even if the person did not request the card or it was received by another*, or a natural person who has agreed with the card issuer to pay consumer credit obligations arising from the issuance of a credit card to another natural person.

B. Regulation Z Should be Amended to Protect Telemarketing and Internet Fraud Victims

Telemarketing fraud continues to be one of the top scams aimed at consumers, costing consumers an estimated $40 billion according to the FTC.[214] It is quickly being joined by Internet fraud as a problem, with the FTC receiving 166,000 complaints of Internet-related fraud in 2003.[215]

One of the few avenues of redress for telemarketing or Internet fraud victims who has been sold worthless or shoddy goods, or been deceived as to what they would receive, is to withhold payment on a credit card by raising claims or defenses under section 1666i. However, the TILA provides that the right to withhold payment only applies to transactions occurring within the consumer's home state or within 100 miles of that location. With respect to telephone and Internet transactions - which would be the type of transaction at issue in telemarketing and Internet fraud - the Official Staff Commentary at § 226.12(c)(3)(ii)-1 provides that the question of where the transaction occurs is determined under state or other law.

We ask that the Board amend this provision of the Commentary to provide that transactions initiated over the telephone or Internet be considered to have occurred in the consumer's home state. With the tremendous growth in Internet transactions versus "brick and mortar" purchases, the traditional model where most consumers made purchases "close to home" no longer applies. This change is needed to protect consumers as new technology changes the way consumers shop. Thus we request that the Board revise Official Staff Commentary § 226.12(c)(3)(ii)-1 to state:

> 1. *Geographic limitation. A transactions that is initiated or made over the telephone, Internet, or by mail shall be deemed to have occurred in the same state as the cardholder's current designated address.*

C. Next Generation Credit Cards (Q 44)

In Question 44, the Board asks about next generation credit cards that do not involve a physical device. Technological changes may soon render obsolete the

[214] Federal Trade Commission, Telemarketing Facts, *available at* http://www.ftc.gov/os/comments/dncpapercomments/04/lsap3.pdf.

[215] Federal Trade Commission, National and State Trends in Fraud & Identity Theft January - December 2003, (Jan. 22, 2004)

definition of credit card in section 1602(k) as "any card, plate, coupon book or other credit device existing for the purpose of obtaining money, property, labor or services on credit."

Some of the next generation devices may not involve a physical "device." One media report discussed the development of "biometric" credit cards that would link credit card numbers to a consumer's fingerprints, facial characteristics, or eye irises.[216] Not all next generation credit cards are on the cutting edge. One catalog company sent out catalogs with "pre-approved account numbers" to access credit with the company. While the page of the catalog itself was found to be a "credit card" under the TILA,[217] a clever creditor could avoid TILA coverage by using a nonphysical means of conveying the account number.

If these next generation "nonphysical" credit cards are not considered "credit cards" under the TILA, more than just the credit card dispute resolution mechanisms are at issue. Consumers would also lose the protections of the TILA's application and solicitations disclosures, the prohibition against unsolicited issuance, the prohibition against offsetting a deposit account, and the protections for unauthorized use.

However, the definition of "device" need not be limited to a physical object. A device could include an intangible item, such as a method or process. For example, the Merriam-Webster Dictionary includes a definition of "device" as a "plan, procedure or technique."[218]

We ask that the Board amend the definition of Regulation Z to define the "device" under section 1602(k) as broadly as possible. The Board should amend Regulation Z, § 226.2(a)(15) to state:

> (15) ''Credit card'' means any card, plate, coupon book, or other single credit device that may be used from time to time to obtain credit. *A device is any item, whether tangible or intangible, that is used to identify a consumer for purposes of accessing credit on an open-end account. A device can be a physical object or a method or process.*

D. Regulation Z Should Affirm That Various Rights Do Not Depend Upon Sending a Billing Error Notice

Lately, credit card issuers have been sowing confusion (whether or not intentionally) about the independence of the billing error procedures versus the consumer's right to assert claims and defenses against the card issuer and the protections against unauthorized use. Consumer advocates report that the customer service divisions of credit card companies often act like the latter right does not exist. More disturbingly,

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[216] Jathon Sapsford, *Paper Losses: As Cash Fades, American Becomes a Plastic Nation*, Wall St. J., July 23, 2004, at A1.
[217] Munoz v. Seventh Avenue, 2004 WL 1593906 (N. D. Ill. Jul. 15, 2004)
[218] Merriam-Webster Dictionary On-Line, *at* http://www.m-w.com.

card issuers are repeatedly asserting in litigation[219] that any and all disputes related to credit card charges must be raised using the billing error procedures, *i.e.*, the consumer must raise them with a written billing error notice within 60 days, even though such arguments flat out contradict the provisions of the TILA and Regulation Z.

Card issuers continue to make this assertion despite the plain language of the Staff Commentary.[220] While the courts that have analyzed this argument have consistently rejected it,[221] card issuers continue to raise the argument - perhaps hoping if it is repeated enough, it might find a court or two willing to believe it.[222]

Moreover, creditors continue to argue that lack of a billing error notice waives a consumer's rights with regards to other provisions of the TILA or under state or common law. For example, one creditor has argued that failure to send a billing error notice waived the common law defense of payment in a collection action.[223] Another creditor reportedly argued that a claim for violation of the TILA requirement of prompt posting of payments at section 1666c is subject to the billing error procedures. This argument has reportedly even been raised in bankruptcy proceedings, where debt buyers have argued that the debtor cannot object to the amount listed in a proof of claim filed on a credit card debt if the debtor did not send a written billing error notice within 60 days of the relevant periodic statement.

We ask that the Board amend Regulation Z to affirm that the failure to invoke the billing procedures does not preclude a consumer from asserting any other protections or rights under the TILA, any other statute or common law, and that the only penalty for failing to invoke the billing error procedures is loss of the protections granted by those procedures. We ask the Board to add new § 226.13(j) to state:

> *(j) Affect on other sections and laws. The failure of a consumer to timely send a billing error notice does not affect the consumer's rights under any other section of this regulation, the Truth in Lending Act, or any other federal or state law. A consumer's failure to send a billing error*

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[219] Citibank (S.D.) Nat'l Assn. v. Mincks, 135 S.W.3d 545 (Mo. App. Ct. 2004); Crestar Bank v. Cheevers, 744 A.2d 1043 (D.C. App. 2000); People's Bank v. Scarpetti, 1998 WL 61925 (Conn. Super. 1998).

[220] Official Staff Commentary § 226.12(c)-1 (cardholders' preservation of claims and defenses operates independently of the billing error procedures), Official Staff Commentary § 226.12(b)(3)-3. Furthermore, as noted above, not all claims or defenses constitute billing errors, and thus cardholders cannot even invoke the billing error procedures for those claims or defenses.

[221] *See* Citibank (S.D.) Nat'l Assn. v. Mincks, 135 S.W.3d 545 (Mo. App. Ct. 2004)(consumer could assert defenses against card issuer under section 1666i for merchant's failure to provide goods without having sent billing error notice; Crestar Bank v. Cheevers, 744 A.2d 1043 (D.C. App. 2000) (consumer could raise unauthorized use as defense to collection suit without having sent billing error notice); People's Bank v. Scarpetti, 1998 WL 61925 (Conn. Super. 1998) (consumer allowed to raise unauthorized use as defense despite not having given notice and invoked billing error procedures).

[222] *Cf., e.g.,* Asset Acceptance Corp. v. Proctor, 804 N.E.2d 975 (Ohio App. Ct. 2004) (creditor argued lack of billing error notice on summary judgment; court appeared to accept argument but held there was a genuine issue of material fact as to whether periodic statements were sent thus triggering 60 days).

[223] *Id.*

notice only precludes the consumer from invoking the procedures and protections of this Section.

E. Increasing the Penalties for FCBA Violations (Q 56)

Under Section 1666(e), any creditor who fails to comply with the FCBA forfeits any right to collect the disputed amount, but this protection against collection is capped at a mere $50. To avoid liability for the disputed amount over $50, the consumer will need to rely on another provision of the TILA or another federal or state law.[224]

This puts consumers who have billing error disputes ignored by the issuer into a difficult position. The most powerful tools that FCBA provides for consumers are the prohibitions and affirmative responsibilities that it places on creditors, such as the prohibition on collecting disputed amounts and the requirement to conduct an investigation. A mere $50 protection against collection, even with the statutory damages available under the TILA, will not deter a creditor if the disputed amount is significant. A creditor can ignore a consumer's FCBA dispute, report the disputed amount as delinquent to a credit bureau (potentially costing the consumer thousands of dollars in higher interest rates and insurance premiums), and initiate debt collection efforts. The only penalty for these blatant violations is the inability to collect $50 of the balance, as well as potential damages under section 1640. Furthermore, using the Department of Labor's cost of living calculator, the value of $50 since FCBA was passed in 1974 is now the equivalent of $193.41 today.

We request that the Board seek legislative change to eliminate the $50 cap in the protection against collection of disputed items when the card issuer fails to comply with FCBA. We also request the Board to amend Regulation Z to state that consumers have the right to obtain injunctive relief to force a creditor to comply with these provisions of the FCBA, by adding new §226.13(k) stating:

(k) A consumer may seek equitable relief for a creditor's failure to comply with the requirements of this section.

V. OTHER ISSUES

A. The Staff Should Not Provide Informal Guidance on the TILA's Application (Q 52)

Question 52 asks whether Board staff should formalize any informal oral advice about the application of the TILA. We know of no examples of informal oral advice that should be formalized. However, we urge the Board staff to avoid issuing informal advice. One of the reasons that the Truth in Lending Simplification and Reform Act was passed in 1980 was that "[c]reditors ... have encountered increasing difficulty in keeping current with a steady stream of administrative interpretations and amendments...."[225] The

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[224] Beaumont v. Citibank (S.D.) Nat'l. Assn., 2002 WL 87682 (S.D.N.Y. Jan. 22, 2002); Berman v. Nationsbank, 1998 WL 88342 (E.D. Pa. Mar. 2, 1998).
[225] S. Rep. No. 368, 96th Cong., 2d Sess., *reprinted in* 1980 U.S.C.C.A.N. 236, 252.

current structure, with Regulation Z and a single, published, Official Staff Commentary, makes the law much more accessible than the multiple levels of administrative interpretation of the TILA prior to the Simplification Act. The greater ease of determining the administrative interpretation of the Act benefits not only creditors but also consumers who act as private attorneys general to enforce it.

B. The Board Should Not "Federalize" the Definition of "Refinancing" (Q 58)

The Board seeks input regarding an industry request to define "refinancing" as a matter of federal law rather than as a matter of state law, the current rule under the Commentary to Regulation Z.[226] Generally, events occurring subsequent to the delivery of the required disclosures that render the original disclosures inaccurate do not violate the Act.[227] Regulation Z creates some exceptions to this rule, for example, when a credit transaction is later refinanced.[228] In this situation, new disclosures must be provided.

The Board should resist this pressure, particularly at this time, for several reasons. First, the refinancing rule applies most commonly in closed-end credit transactions.[229] This ANPR focuses upon amendments to the rules affecting credit and charge cards. Tinkering with the definition of a refinancing should occur in the broader context of reviewing the rules for closed-end credit, if at all.

Second, the Board permits other important concepts to be defined by state law in Regulation Z or the Commentary. For example, when "consummation" occurs for purposes of the timing of disclosures is an issue of state law.[230] Recently, the Board approved of a change to the Commentary that relies upon state law to define an "agent" for purposes of receipt of cancellation notices in the rescission context.[231]

Third, there may be significant reasons why federalizing the definition could interfere with the refinancing marketplace more than by leaving the status quo intact. It is our understanding that some states permit a mortgage that is refinanced to retain its lien position relative to liens arising on the property subsequent to the original mortgage. Unless a detailed analysis is performed to determine the effect of federalizing the definition of a refinancing might have on state property and lien priority law, the Board's efforts may create havoc.

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[226] Official Staff Commentary § 226.20(a)-1.
[227] 15 U.S.C. § 1634.
[228] Regulation Z § 226.20(a).
[229] The concept of refinancing an open-end revolving account or a home equity line of credit likely renders those transactions "spurious." Refinancing an open-end account into another open-end account is an oxymoron. If a customer needs additional cash, the customer can obtain a cash advance under the current plan up to the credit limit or seek permission to have the credit limit raised. There is no need to close one credit line and open another.
[230] Official Staff Commentary § 226.2(a)(13)-1.
[231] Official Staff Commentary §§ 226.15(a)(2)-1, 226.23(a)(2)-1; 69 Fed. Reg. 16769 (Mar. 31, 2004).

Finally, the concern that courts could arrive at differing conclusions about when a refinancing occurs is not peculiar to the refinancing context. This concern applies equally to all of the places in the TILA where state law is relied upon.

VI. THE COST TO IMPLEMENT AN AMENDED DISCLOSURE REGIME IS NOT PROHIBITIVE (Q 38)

There will be costs to implement the disclosure changes we suggest in these comments. However, we do not believe they are prohibitive for the reasons we discuss below.

A study by the Board's own staff[232] showed that the cost to implement *all* of the new disclosures required by the new Truth In Savings Act in the early 1990s translated into only $29,390 per bank or approximately $337 million for *all banks*. The authors based this conclusion upon actual costs reported by surveyed banks. Further, the authors concluded that economies of scale are achieved (and thus the costs are minimized):

- when all changes are made at once (rather than in a piecemeal fashion);
- because costs are insensitive to the extensiveness of necessary changes (for example, six changes may cost the same or close to the cost of 3 changes);
- for larger depositories and bank holding companies because they make the same changes for a larger number of deposit accounts (thus, the cost per account is less).

Based on the findings of this study and on information about the credit card industry, we believe some projections can be made about the cost to implement a revised disclosure regime under TILA. We suggest that an approximate cost can be calculated by dividing a projected total cost, using $337 million as a starting point, by the number of cards issued through each of the four networks (VISA, MasterCard, AMEX, and Discover). The result is the cost per card. The reason why this number is helpful is that it is likely that the credit card issuers ultimately will spread the cost of making disclosure changes on to their customers. In addition, Elliehausen and Lowery relied upon the cost per account for their study as well.

Let us assume that the cost of implementing our proposed changes is *twice* the cost to implement the Truth In Savings Act ($337 million), *after* accounting for inflation. That number is $916.12 million.[233] The total number of cards outstanding as of the end of 2004 issued through VISA, MasterCard, AMEX, and Discover was 661.4 million.[234] Dividing the cost by the total number of cards results in a per card cost of $1.39. Another

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[232] Gregory Elliehausen & Barbara R. Lowery, *The Cost of Implementing Consumer Financial Regulations: An Analysis of Experience with the Truth in Savings Act,* Fed. Res. Bull. (Dec. 1997), *available at* http://www.federalreserve.gov/pubs/staffstudies/1990-99/ss170.pdf.
[233] We estimate that $337 million in 1992 would increase to $471.85 million in 2005, based upon inflation. To replicate this calculation, go to http:// www.bls.gov and click on the Inflation Calculator. Then enter $337 and 1992 (date of implementation of TISA) and click "calculate."
[234] The Nilsen Report, No. 828 (Feb. 2005), *available at* http://www.nilsonreport.com/issues/2005/828.htm.

source estimates that there will be 1.5 billion credit cards in the hands of customers by 2005.[235] Using this number, the cost per card will be even smaller…$.61. In either case, the per card cost is a proxy for the actual cost since that number will not be known until the changes are actually made. However, Elliehausen and Lowery confirm that the costs are insensitive to the extensiveness of the changes. Consequently, if the changes under a revised TILA regime are more extensive than those involved to implement TISA, the cost to implement the TILA amendments should be roughly similar and should not be exacerbated significantly by the number of changes.

According to the Elliehausen and Lowery survey, the costs to small institutions (assets of less than $100 million) was less in absolute dollars, $16,110, than the cost to medium-sized banks (assets of $100 to $449 million), $25,860, and to the cost of large banks (over $449 million in assets), $194,270.[236] The average cost per consumer account ranged from $3.19 for the smaller banks to $1.23 for the larger banks.[237] The projected cost to implement TILA changes is well within the range that it was for banks in 1992 to implement TISA.

Based upon the conclusions of the Elliehausen and Lowery, we believe that the cost to implement TILA changes will not result in an undue expense that is ultimately borne by consumers, particularly in light of the improvements to consumer understanding and to their ability to comparison shop.

Further, we believe that the costs of making the changes we propose to open-end credit disclosures are likely to be less than the costs to implement the Truth in Savings Act. The Truth in Savings Act imposed an entirely new set of disclosure requirements where none had existed before. Banks therefore had to create systems for compliance from scratch, and bank employees had to familiarize themselves with the requirements of a completely new statute. By contrast, banks are already familiar with Truth in Lending disclosure requirements, are already making Truth in Lending disclosures, and already have systems in place to monitor compliance.

In addition, costs for complying with changes in TILA can be minimized by the provision of model forms. Indeed, one of our key recommendations with regard to disclosures is that the Board should be much more specific in standardizing the format, order, and language of disclosures. By providing specific, fixed, requirements, the Board will reduce the need for creditors - as well as courts - to interpret broad language.

It should also be stressed that the cost of compliance is insensitive to the number of changes made. Unless the Board concludes that the open-end disclosure requirements of Regulation Z need absolutely no revisions, banks will incur compliance costs. If 20

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[235] U.S. Census Bureau, Statistical Abstract of the United States: 2003 at 751, *No. 1190*: *Credit Cards – Holders, Numbers, Spending, and Debt, 1990 and 2000, and Projects, 2005*, *available at* http://www.census.gov/prod/2004pubs/03statab/banking.pdf; U.S. Bureau of the Census, *Projections of the Number of Households and Families in the United States: 1995 to 2010* at 9 (1996), *available at* http://www.census.gov/prod/1/pop/p25-1129.pdf (projecting 108.8 million households by 2005).
[236] Elliehausen & Lowery, *supra* note 215, at 8, 16.
[237] *Id.* at 8, Table 9.

changes are needed in Regulation Z, making only ten of them, or only two of them, will not save compliance costs in any meaningful way.

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Print your name as you would like it to appear on card.

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Mother's Maiden Name or Password (for security purposes) Your Annual Income $

Are you: ☐ Homeowner ☐ Renter ☐ Other Total Household Income‡‡ $

Occupation Years There

Residential Street Address (No P.O. Boxes)‡

City State ZIP

Home Phone (include area code) ( ) Business Phone (include area code) ( )

Indicate your preferred mailing address: ☐ The address above ☐ The street address at right‡ ☐ An alternate address
(Please print alternate address clearly on this form.)

X Date / /

MY SIGNATURE MEANS THAT I AGREE TO THE CONDITIONS ON THE REVERSE SIDE OF THIS FORM AND TO BE BOUND BY EACH OF THE TERMS OF THE CREDIT CARD AGREEMENT, INCLUDING ARBITRATION.

Please send an additional card at no extra cost for:
Name First M.I. Last
Relationship

E-mail Address (optional—see reverse)

☐ **Yes,** keep me informed via e-mail about special marketing offers from MBNA.

‡ Federal law requires us to collect and verify this information. If the address we mailed to was not a street address, we are required to obtain a street address.

‡‡ Alimony, child support, separate maintenance income, or any other source of income (*e.g.*, spousal or investment income), need not be revealed if you do not wish it considered as a basis for repayment.

MONEY-SAVING BALANCE TRANSFER OPTION.* Please list balance transfer requests in order of priority.

Start Saving Now!*

Transfer amount	Make transfer check payable to	Account number
$.		
$.		
$.		

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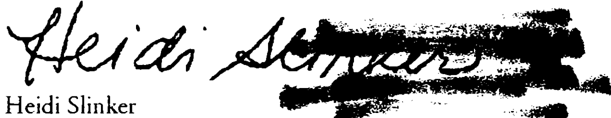

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The Plan is Optional. Purchase of the Plan is optional and you may cancel at any time. Whether or not you purchase the Plan, this will not affect your application for credit or the terms of any existing credit agreement with MBNA.

Plan Limitations. There are eligibility requirements, conditions, and exclusions that could prevent you from receiving benefits.

Additional Information. We will provide the complete Plan Summary and Terms and Conditions before you are required to pay. Read the Plan documents carefully.

Important Restrictions on Enrolled Accounts. While you are receiving benefits, use of your account is suspended. Finance charges continue to accrue.

Plan Fee. The monthly fee is $0.95 per $100 of the Plan balance as described in the Plan documents, which you will receive shortly. 0604.CP

†The Annual Percentage Rate (APR) for Purchases, Balance Transfers, and Cash Advance Checks is a variable rate, currently 7.9%. The APR for Bank and ATM Cash Advances is a variable rate, currently 19.99%. Your APRs may vary in accordance with the Variable-Rate Information accompanying your card. The current introductory APR offer for Balance Transfers and Cash Advance Checks is 2.9%. Transaction fee for Bank and ATM Cash Advances and for purchases of cash equivalents: 3% (min. $10). Transaction fee for Balance Transfers and Cash Advance Checks: 3% (min. $10, max. $75). **MBNA allocates your payments to balances (including new transactions) with lower APRs before balances with higher APRs.** See the enclosed insert for details about rate, fee, and other cost information.

FEATURES

***BALANCE TRANSFERS.** Total value of transfer requests cannot exceed your credit line. MBNA sends either full or partial payment to your creditors in the order you list them. Allow at least 2 weeks from account opening for processing. Continue paying each creditor until the transfer appears as a credit. Transfers are processed as cash advances as described in the Credit Card Agreement. Cash advances incur finance charges from the transaction date. If your available credit cannot accommodate any transaction, fee and/or finance charge, the account will be subject to over-the-credit-limit costs. Balance transfers and/or cash advances may not be used to pay off or pay down any MBNA account. BT.0303

**Certain restrictions apply to each benefit. Details accompany new account materials. Preferred card benefits differ from *Platinum Plus* benefits (*e.g.*, coverage amounts vary and some benefits are not available). PPCR.0703

CONDITIONS

I have read this application, and everything I have stated is true. I am at least 18 years of age and either a United States citizen or a permanent resident of the U.S., or I am at least 21 years of age and a permanent resident of Puerto Rico. I authorize MBNA America Bank, N.A. ("MBNA") to review my credit and employment histories and any other information in order to approve or decline this application, service my account, and manage its relationship with me. I consent to MBNA's sharing of information about me and my account with the organization endorsing this credit card program. I authorize MBNA to share with others, to the extent permitted by law, such information and [illegible] experience with me. In addition, I may as a Customer later indicate a preference to exempt my account from some of the information-sharing with other companies ("opt-out"). If I accept or use an account, I do so subject to the terms of this application, and the Credit Card Agreement as it may be amended; I also agree to pay all charges incurred under such terms. Any changes I make to the terms of this application will have no effect. I understand that if this application is approved for an account with a credit line of less than $2,000, I will receive a Preferred card. I accept that on a periodic basis an account may be considered for automatic upgrade at MBNA's discretion. I consent to and authorize MBNA, any of its affiliates, or its marketing associates to monitor and/or record any of my phone conversations with any of their representatives. (PL/E .0604)

MBNA uses your e-mail address to communicate with you about your application and/or account. See the MBNA Privacy Notice for additional information. The MBNA Privacy Notice is available at MBNA.com and accompanies the credit card.

If you do not want future MBNA credit card offers, send your name and address to: MBNA, PO Box 15728, Wilmington, DE [illegible] Processing typically takes 12 weeks.

If the enclosed postage [illegible] envelope [illegible] nd application to: MBNA, PO Box 981052, El Paso [illegible]

This credit card program is issued and administered by MBNA America Bank, N.A. Travel planning services are provided to MBNA Customers by an independently owned and operated travel agency. MasterCard is a federally registered service mark of MasterCard International Inc., and is used by MBNA pursuant to license. MBNA, MBNA America, MBNA ShopSafe, MBNA.com and *Platinum Plus* are service marks of MBNA America Bank, N.A.

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only decide our or your Claim and may not consolidate or join the claims of other persons who may have similar claims. You may obtain rules and forms by calling the AAA at 800-778-7879. Any arbitration hearing that you attend will take place in the federal judicial district where you reside. At your request, we will advance the first $250 of the filing and hearing fees for any Claim you may file against us; the arbitrator will decide whether we or you will ultimately pay those fees. The arbitrator shall apply applicable substantive law consistent with the FAA and applicable statutes of limitations, and shall honor claims of privilege recognized at law. Judgment upon the award rendered by the arbitrator may be entered in any court having jurisdiction. This Arbitration Provision shall survive repayment of your extension of credit and termination of your Account. This arbitration provision shall be governed by the Federal Arbitration Act, 9 U.S.C. §§ 1 through 16.

45. If you are an Executive Officer of U.S. Bancorp, or any of its bank affiliates, the Bank reserves the right to demand payment at any time.

46. WorldPerks Mileage

a) We will request Northwest Airlines, Inc. ("Northwest") to credit your WorldPerks Account with miles as follows. Monthly Statement Period Award Level: For Net Purchases less than or equal to $10,000, earn 1 mile for every $1. For Net Purchases over $10,000, earn 1 mile for every $2. Annual Award Level: If during the calendar year, Net Purchases exceed $50,000, all miles the rest of the year are earned at a rate of 1 mile for every $2. Exemptions: Northwest WorldPerks Platinum Elite/Gold Elite/Silver Elite members, and WorldPerks Visa AutoPay customers who select the full payment option on the first available payment date after their Statement Date. Miles will be awarded as long as your Account is open and not 5 days or more past due or overlimit at the close of your Visa billing period. We will not request miles for Advances, Convenience Checks or Balance Transfers. We reserve the right to adjust the number of miles we request from Northwest for Purchases or to stop requesting miles for Purchases on the Account, upon notice to you.

b) "Net Purchases" for a billing period are determined by adding all new Purchases recorded to your Account during the billing period and subtracting any credits or other adjustments recorded to your Account during the billing period for returned Purchases. If credit for returned Purchases exceeds new Purchases in any billing period, the excess credits will be carried forward into successive billing periods and subtracted from future new Purchases to determine the net Purchases for those successive periods.

c) Participation in WorldPerks is subject to the terms and conditions of the WorldPerks Program. Please refer to www.nwa.com/freqfly/memguide for complete WorldPerks Program rules. Northwest is solely responsible for the redemption and fulfillment of WorldPerks miles. Northwest may change the WorldPerks program rules, program partners, regulations, benefits, conditions of participation or mileage levels, in whole or in part, at any time with or without notice, even though changes may affect the value of mileage already accumulated. Standard award travel is limited and subject to seat availability. Increased availability is offered through RuleBusterSM pricing option. Visit nwa.com for details. The Bank has no obligation to award miles in the WorldPerks program or to provide or arrange for any service relating to travel or the use of WorldPerks miles. Our sole obligation with regard to the WorldPerks program is to ask that Northwest award miles as expressly provided in this Agreement.

d) The Northwest WorldPerks number on this Account must belong to the primary Cardmember. Changing the WorldPerks number constitutes pooling of miles which violates the WorldPerks member agreement. The Bank will only change the WorldPerks number if we made an error during the set-up and were notified of the error within 120 days of the Account opening.

e) Your Account will be automatically enrolled in the Rewards Network Dining For Miles and Hotels For Miles programs (formerly "WorldPerks Dining For Miles by iDineSM"). This benefit will allow the WorldPerks number associated with your WorldPerks Visa Account to earn additional WorldPerks miles through Rewards Network Dining For Miles and Hotels For Miles programs. WorldPerks miles earned through Rewards Network Dining For Miles and Hotels For Miles programs will be credited automatically to the Northwest Airlines WorldPerks Account and will not be reflected on your WorldPerks Visa statement. If the WorldPerks number associated with your WorldPerks Visa Account is already enrolled in Rewards Network Dining For Miles and Hotels For Miles programs or any other program operated by Rewards Network Inc., this automatic enrollment will not apply. No additional costs will be incurred as a result of enrollment or participation. To facilitate the awarding of WorldPerks miles, your credit card number will be shared with Rewards Network Inc. in order to capture qualifying activity at participating restaurants and hotels. Rewards Network Inc. will periodically send Rewards Network Dining For Miles and Hotels For Miles members marketing materials. Rewards Network Dining For Miles and Hotels For Miles members must have a U.S. mailing address to be eligible for Rewards Network Inc. membership. Other restrictions apply. Visit www.nwa.rewardsnetwork.com to see complete program guidelines. If you do not want to be enrolled in this complimentary program, call toll-free at 1-800-818-2040. If you have previously notified U.S. Bank that you do not wish to participate in this complimentary program, your WorldPerks Visa Card has not been enrolled in the Rewards Network programs. To re-activate the membership, call 1-800-818-2040. The Bank neither endorses nor guarantees any offerings of third party providers and is not liable for the failure of their products and services.

f) Northwest is not a party to this Agreement and has no authority regarding the Account, including with respect to any extension of credit on the Account. The Bank is solely responsible for all credit extended on the Account. Northwest is not a creditor on or owner of the Account. You authorize us to share information about you and your Account to Northwest.

YOUR BILLING RIGHTS
KEEP THIS NOTICE FOR FUTURE USE

This is important information about your rights and our responsibilities under the Fair Credit Billing Act.

In Case of Errors or Questions About Your Bill

If you think that your bill is wrong or if you need more information about a transaction on your bill, please verify the following as soon as possible:

- If other members of your household may have participated in the transaction.
- Review your receipts for this dollar amount as it may have posted to your statement with a different merchant name.
- That you have contacted the merchant in an attempt to resolve the issue.

If you wish to dispute the transaction please call Cardmember Service at 1-800-NWA-VISA (TDD 1-800-846-2580) and have the following information available:

- The date and dollar amount of the transaction you are questioning.
- An explanation of why you believe there is an error or why you need additional information along with any documentation you may have to support your claim.
- The date you contacted the merchant to attempt to resolve this issue and the merchant's response.

Many inquiries can be corrected over the phone, but phoning alone does not preserve your legal rights under the Fair Credit Billing Act. In order to preserve your rights, we must receive your written communication no later than 60 days after we sent you the first bill on which the error or problem appeared. Please send a letter with your name, account number and the above information to: Cardmember Services, P.O. Box 6335, Fargo, ND 58125-6335. You do not have to pay any amount in question while we are investigating, but you still remain obligated to pay the parts of your bill that are not in question. While we investigate your dispute, we cannot report you as delinquent or take any action to collect the amount you question.

If you have authorized us to pay your credit card bill automatically from your savings or checking account, you can stop the payment on any amount you believe is incorrect. To stop the payment, your letter must reach us three business days before the automatic payment is scheduled to occur.

Your Rights and Our Responsibilities After We Receive Written Notice

We must acknowledge your letter within 30 days, unless we have corrected the error by then. Within 90 days, we must either correct the error or explain why we believe the statement was correct.

After we receive your letter, we cannot try to collect any amount you questioned or report your Account as delinquent. We can continue to bill you for the amount you questioned, including FINANCE CHARGES, and we can apply any unpaid amount against your Credit Limit. You do not have to pay any questioned amount while we are investigating, but you are still obligated to pay the parts of your Account that are not in question.

If we find that we made a mistake on your bill, you will not have to pay any FINANCE CHARGES related to the questioned amount. If we did not make a mistake, you may have to pay FINANCE CHARGES and you will have to make up any missed payments on the questioned amount. In either case, we will send you a statement of the amount you owe and the date that it is due.

If you fail to pay the amount that we think you owe, we may report you as delinquent. However, if our explanation does not satisfy you and you write to us within ten days telling us that you still refuse to pay, we must tell anyone we report you to that you have a question about your bill. And, we must tell you the name of anyone we reported you to. We must tell anyone we report you to that the matter has been settled between us when it finally is.

If we don't follow these rules, we cannot collect the first $50.00 of the questioned amount, even if your bill was correct.

Special Rules for Credit Card Purchases

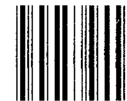
If you have a problem with the quality of property or services that you purchased with your credit card, and you have tried in good faith to correct the problem with the Merchant, you may have the right not to pay the remaining amount due on the property or services. There are two limitations on this right and both must apply:

1) You must have made the purchase in your home state or, if not within your home state within 100 miles of your current mailing address; and

2) The purchase price must have been more than $50.

The conditions do not apply if we own or operate the merchant or if we mailed you the advertisement for the property or services.

SPECIAL RULES FOR CREDIT CARD PURCHASES DO NOT APPLY TO PURCHASES MADE WITH CONVENIENCE CHECKS OR BALANCE TRANSFER CHECKS.



U.S. Bank National Association ND

For Payments	U.S. Bank National Association ND P.O. Box 790408 St. Louis, MO 63179-0408
For General Inquiries	U.S. Bank National Association ND P.O. Box 6352 Fargo, ND 58125-6352

WorldPerks® Visa® Card Important Phone Numbers

U.S. Bank
- 24 Hour Customer Service 1-800-NWA-VISA (1-800-692-8472)
- Travel Accident Insurance Description of Coverage 1-866-464-8472
- Outside United States (call Collect).701-461-2044
- Website ....worldperksvisa.com

Northwest Airlines®
- Reservations 1-800-225-2525
- WorldPerks Information Line 1-800-327-2881
- WorldPerks Award Travel Reservations....1-800-44-PERKS (447-3757)
- Website ....nwa.com

Visa
- Visa Assistance Center 1-800-VISA-911 (847-2911)
- Outside the U.S...............................410-581-9994
- Travelers' Message Service 1-800-253-5664

R20 35012 (6/04)

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WORLDPERKS® VISA® PLATINUM CREDIT CARDMEMBER AGREEMENT AND PRIVACY PLEDGE

(Effective 10/7/04)

CARDMEMBER AGREEMENT

The following new Cardmember Agreement governs the account to which the credit card that you hold relates to. Changes from your prior agreement are shaded. Except where provided below, all changes provided herein will apply to your Account effective on October 7, 2004.

If you do not wish to accept the new terms set forth in SECTION 10 (b), SECTION 14 (d) and SECTION 18, below, you must notify us in writing within 25 days of the effective date. If you notify us that you do not accept those new terms, the Account will be closed, but the balance must be paid off, either all at once or according to the terms of those Sections in this Cardmember Agreement effective 10/7/04 with the exception of SECTION 10 (b), SECTION 14 (d) and SECTION 18 in which the terms of your prior Cardmember Agreement will apply. Correspondence regarding this change in terms should be sent to the address below. Use of the Account after the effective date of change shall be deemed acceptance of all of the new terms, even if the 25 days have not expired. Please note that your Account may be re-opened and subject to the new terms, if after you have notified us as provided in this notice, (1) you use the Account, or (2) charges post to the Account (including recurring/previously authorized charges).

U.S. Bank National Association ND
Attn: Opt Out Depart.
P.O. Box 6352
Fargo, ND 58125-6352

This is a cardmember agreement and disclosure statement ("Agreement") between you and U.S. Bank National Association ND containing the terms that will apply to your WorldPerks Visa Platinum Card Account ("Account") effective 10/7/2004. In this Agreement, "you" and "your" means each individual accepting a solicitation or applying for the Account or otherwise agreeing to be responsible for the Account. "We", "us", "our" and "the Bank" means U.S. Bank National Association ND , the issuer of the Card and your Account creditor. Please read this Agreement carefully and keep it in a safe place to make the best use of the credit cards we issue with this Account (the "Card"). The Agreement becomes effective as soon as you or someone authorized by you (an "authorized signer") uses the Card or Account, but no later than 30 calendar days after we issue and you fail to return the Card. In addition to this agreement, there are also relevant Account disclosures on your Card Carrier.

ACCOUNT FEATURES AND YOUR USE OF THE ACCOUNT

1. Personal Use – You may use the Account only for personal, family or household purposes. Federal or state consumer protection laws may not apply if you use the Account for other than personal, family or household purposes. In addition, we may suspend or cancel your ability to use the Account or Card if they are used for business or commercial purposes.

2. Account Purchases – You may use the Account to buy, lease or otherwise obtain goods or services from participating merchants (including transactions you initiate by mail, telephone or over the Internet), or take advantage of special promotional Convenience Check or Balance Transfer offers that post as Purchase transactions ("Purchases"). We will, in connection with any promotional Balance Transfer or Convenience Check offer we make, provide you with materials that explain whether those transactions will post and be treated as a Purchase. Even if you have not signed a sales draft or the merchant has not supplied you with a written receipt or other proof of sale, you are responsible for all Purchases made through the Account, except as expressly limited by applicable law (see "Your Billing Rights" section below for more details).

3. Account Advances – Advances are transactions other than Purchases that allow you direct access to funds available through your Account. Advances may include Account transactions such as cash advances you obtain directly from us, other participating financial institutions, or automated teller machines ("Cash Advances"), telephone transfers, some Balance Transfers, some Convenience Checks, FastCash, Overdraft Protection Advances and Cash Equivalent Advances. ("Cash Equivalent Advances" include transactions to acquire or initiate wire transfers, travelers checks, money orders, foreign cash transactions, casino gaming and betting transactions and lottery tickets. "Financial institution" or "ATM" advances include Phone (automated phone system), 24 Hour (customer service assisted) and Internet transfers.) Monthly Account statements we issue may refer to Advances as an "Advance", "Cash", "Cash Advances", or by the product or device you used to obtain an Advance. Refer to the Account Fees section for details on Advance Transaction Fees.

4. Advance Limits – No more than 50% of the Credit Limit (defined below) is available for Cash Advances, Cash Equivalent Advances or Advances requested through telephone transfers. Unless we have elected in this Agreement or otherwise to limit the amount, number and/or availability of other Advances you may obtain through Overdraft Protection, Convenience Checks, and FastCash transactions, you may use the Account to obtain those Advances up to the amount available under the Credit Limit.

5. Convenience Checks – From time to time, we may supply Convenience Checks for use by the person(s) named on those checks. Convenience Checks are drafts that look like other checks, but are drawn on credit available in the Account. We may, based on the particular offers we make from time to time, provide Convenience Checks that will post and be treated as an Advance or Convenience Checks that will post and be treated as a Purchase. We will, in connection with any Convenience Check we provide, include materials that explain whether the Convenience Check will post and be treated as an Advance or as a Purchase. Convenience Checks must be written in U.S. dollars.

We may return a Convenience Check unpaid if:

(a) the credit available under your Credit Limit is less than the Convenience Check amount;
(b) the Account is in default; or
(c) the Convenience Check is improperly signed; or
(d) otherwise fails to conform to our regularly accepted standards for check payment.

Convenience Checks may not be used to pay the Account or any obligation you owe us or our affiliates.

6. Paying and Stopping Payment on Convenience Checks – You must use the number and address provided in the "Lost or Stolen Card or Convenience Check" section below to request that payment be stopped on a Convenience Check. You must call us promptly with an oral stop payment request and then provide us with a written confirmation of the stop payment request within 14 calendar days. Any stop payment request we receive will remain in effect for 6 months, unless you renew the request in writing before the end of that time. We may pay Convenience Checks more than 6 months old. There may be circumstances under which a Convenience Check must be paid, even if we have received a stop payment request from you. We will not be liable to you if we do not honor your stop payment request under those circumstances. If it is determined that a Convenience Check should have been paid, but was not, we will not be liable for any consequential, punitive or incidental damages if we acted in good faith. Our only obligation under those circumstances will be to pay the designated payee the amount of the Convenience Check and cancel any charges assessed against your Account as a result of any wrongful failure to honor the Convenience Check.

7. Balance Transfers (if available) – We may permit you to transfer balances and obligations to the Account that you owe other companies or financial institutions, subject to the terms and conditions disclosed in offers we may make to you from time to time. Balance Transfers will post to the Account and be separately reflected on monthly Account statements as Balance Transfer, or, depending upon the offer, may post to the Account and be treated as a Purchase, Cash Advance or some other kind of Advance transaction. We will, in connection with any Balance Transfer offer we make, provide you with materials that explain how the Balance Transfer will post to the Account and be reflected on monthly Account statements. You may not request Balance Transfers of existing obligations you owe us or our affiliates. If you request a Balance Transfer that would cause the Account to exceed its available Credit Limit, we may, at our option, (a) post the entire Balance Transfer requested to your Account and assess an Overlimit Fee; (b) post only a portion of the Balance Transfer requested to your Account up to the amount of credit available under the Credit Limit; or (c) refuse to process the entire amount of the Balance Transfer requested.

8. Overdraft Protection – This section is part of the Agreement only if you have specifically requested and have obtained Overdraft Protection linking the Account with a designated U.S. Bank checking account. An Overdraft Protection Advance allows us to transfer Account funds and prevent overdrafts on the designated checking account. You authorize us to make Overdraft Protection Advances from the Account as provided in this Agreement. Any Overdraft Protection Advance will post and be treated as an Advance drawn on the Account. An Overdraft Protection Advance will be made only once per day, and will be made in multiples of $25 (regardless of the specific overdraft amount). We may cancel Overdraft Protection privileges under the Account, even if the Account remains open for other purposes.

FINANCE CHARGES AND ACCOUNT FEES

9. Account Finance Charges – FINANCE CHARGES reflect the cost of credit. Your total FINANCE CHARGE for any billing cycle will equal the amount of any:

(a) periodic rate FINANCE CHARGES (sometimes referred to as "interest" here and on monthly Account statements);
(b) Advance transaction fees; and
(c) any other transaction fees that are considered FINANCE CHARGES.

In some of the following sections, we have abbreviated the terms "daily periodic rate" as "DPR", "average daily balance" as "ADB"; and "ANNUAL PERCENTAGE RATE" as "APR".

10. Interest Rate -
Variable Rate for "Purchases", Variable Rate for "Balance Transfers", and Variable Rate for "Cash Advances".
a) The Daily Periodic Rate for transactions posting as Purchases, Advances and Balance Transfers is equal to 1/365th of its corresponding ANNUAL PERCENTAGE RATE. The standard Daily Periodic Rate and corresponding ANNUAL PERCENTAGE RATE ("APR") for transactions posting to your Account as Purchases, Advances and Balance Transfers as variable rates that may change from time to time based on changes to a published Index.

b) Your Daily Periodic Rate and corresponding APR may increase or decrease from time to time according to the movements up or down of the Index, which is the highest Prime Rate published in the "Money Rates" section of the Midwest Edition of *The Wall Street Journal* in the last 90 days, before the date on which the billing cycle closed (in other words, the "statement date"). Any variable rate adjustment based on an Index change will be effective as of the first day of the billing cycle, and will apply to the new and outstanding Account balances and transactions subject to that variable rate. We reserve the right to choose a comparable new index if the *The Wall Street Journal* ceases to publish a Prime Rate. The current Index value for your Account is disclosed on your Card Carrier. To determine the standard variable rates for transactions posting to the Account as Purchases, Advances and Balance Transfers, we will add the Index to a Margin. The Margin for Purchases, Advances and Balance Transfers is 9.75%. Refer to your statement for your APR and Daily Periodic Rate (DPR) for Purchases, Balance Transfers, and Cash Advances that will apply to your Account. Any variable rate adjustment will be effective as of the first day of the billing cycle that begins after a change in the Index, and will apply to all new and outstanding Account balances subject to the variable rate. Any increase or decrease to the Index will result in an increase or decrease in the FINANCE CHARGE on the Account, an increase or decrease to your Minimum Payment, and an increase or decrease to your New Balance.

Fixed Delinquency Rate.
c) Upon the occurrence of an "Adjustment Event", each Daily Periodic Rate and corresponding APR in effect for new and outstanding Purchase, Advance and Balance Transfer balances will increase from their standard rates or any introductory or promotional rates to a "Delinquency Rate". The Delinquency Rate will take effect and apply to new and outstanding Purchase, Advance and Balance Transfer balances as of the first day of the billing cycle in which the Adjustment Event occurs.

An Adjustment Event occurs whenever either of the following two situations occurs during the same twelve (12) month period:

a. a Minimum Payment is sixty (60) days past due once; or
b) a Minimum Payment is thirty (30) days past due on two separate occasions.

Your promotional rate will expire upon an Adjustment Event and will be changed to the Delinquency Rate. Each Delinquency Rate is a fixed rate that does not vary based on changes to a published Index. The Delinquency Rate that applies to Purchases, Balance Transfers, and Advance Balances will be disclosed on your Card Carrier. The Delinquency Rate for all Account balances will remain in effect until the closing date of the 12th consecutive billing cycle that your Account is "current" (that is, no Minimum Payments past due). On the first day of the billing cycle following your 12th consecutive current cycle, the Daily Periodic Rate (and corresponding APR) for Purchase, Advance and Balance Transfer balances will decrease to their standard fixed or variable rates (not any introductory, promotional, or discounted rates). An increase or decrease to your Daily Periodic Rate will result in an increase or decrease in the FINANCE CHARGE on your Account, an increase or decrease to your Minimum Payment, and an increase or decrease to your New Balance.

11. Interest FINANCE CHARGE; Method of Computing Amount Subject to Interest – We calculate the periodic rate or "interest" portion of the FINANCE CHARGE by:

(a) multiplying the applicable daily periodic rate ("DPR") by the Average Daily Balance (including new transactions) of the Purchase, Advance and Balance Transfer categories subject to interest ("Amounts Subject to Interest"), and
(b) then adding together the resulting interest from each category.

We determine the Average Daily Balance ("ADB") separately for the Purchases, Advances and Balance Transfer categories.

To get the ADB in each category, we add together the daily balances in those categories for the billing cycle and divide the result by the number of days in the billing cycle.

We determine the daily balances each day by:

(a) taking the beginning balance of those Account categories (including any billed but unpaid interest, fees, credit insurance charges and other charges); and
(b) adding any new interest, fees, and charges, and
(c) subtracting any payments or credits applied against your Account balances that day.

We add a Purchase, Advance or Balance Transfer to the appropriate balances for those categories on the later of the transaction date or the first day of the statement period. Billed but unpaid interest on Purchases, Advances and Balance Transfers is added to the appropriate balances for those categories each month on the statement date. Billed but unpaid Advance transaction fees are added to the Cash balance of the Account on the date they are charged to the Account. Any billed but unpaid fees on Purchases, credit insurance charges, and other charges are added to the Purchase balance of the Account on the date they are charged to the Account. Billed but unpaid fees on Balance Transfers are added to the Balance Transfer balance of the Account on the date they are charged to the Account. In other words, billed and unpaid interest, fees, and charges will be included in the Average Daily Balance of the Account that accrues interest (the "Amount Subject to Interest") and will reduce the amount of credit available to you.

Exception: Credit insurance charges are not included in the ADB calculation for Purchases until the first day of the billing cycle following the date the credit insurance premium is charged to the Account.

12. Grace Period – You have a 20 to 25 day grace period for Purchases (including any promotional Balance Transfers or Convenience Checks that will post as Purchases), provided you have paid your Previous Balance in full by the Payment Due Date shown on your monthly Account statement. In order to avoid additional FINANCE CHARGES on Purchases, you must pay your New Balance in full by the Payment Due Date shown on the front of your monthly Account statement. There is no grace period for transactions that post to the Account as Advances or Balance Transfers. Those transactions are subject to interest from the date they post to the Account until the date they are paid in full.

13. Introductory and Promotional Rates – We may, at our option, offer you for a limited time introductory or promotional interest rates for all or part of the Purchase, Advance, or Balance Transfer balances in the Account. We will tell you the introductory or promotional rate and the period of time during which it is in effect in the offer. Unless an offer states otherwise, an introductory or promotional rate will generally remain in effect until the last day of the billing cycle in which the introductory or promotional rate expires, the date the Account is closed to future transactions, or the date your Account first becomes past due because a Minimum Payment is not received in full on or before its Payment Due Date, whichever occurs sooner (the "Termination Date"). Any introductory or promotional rate that applies to new or outstanding Account balances will increase to the standard rate that would otherwise apply, or, when appropriate under the terms of this Agreement, a Delinquency Rate, if we do not receive at least the Minimum Payment due by the Payment Due Date shown on a monthly Account statement in any month. Any introductory or promotional rate will expire upon an adjustment event (as indicated above) and will be changed to the Delinquency Rate.

14. Account Fees – You agree to pay the following Account fees and FINANCE CHARGES:
(a) We will add a FINANCE CHARGE to the Advance balance of the Account in the form of the Advance Transaction Fees disclosed below for each Advance you obtain during a billing cycle. The fees imposed will equal the greater of the fee based on a disclosed percentage of each Advance or the minimum dollar amount, with the maximum Advance Transaction Fee, shown below. All Advance Transaction FINANCE CHARGE fees listed below are in addition to the interest that accrues on Account Advances.

CASH RECEIVED FROM	PERCENTAGE OF CASH FEE	MINIMUM	MAXIMUM
CASH ADVANCE	3%	$5.00	NONE
CASH EQUIVALENT	4%	$10.00	NONE
ATM	3%	$5.00	NONE
CONVENIENCE CHECK	3%	$5.00	NONE
OVERDRAFT PROTECTION	3%	$5.00	NONE

(b) In addition to interest, your Account may be subject to a FINANCE CHARGE in the form of a Promotional Discount Transaction Fee for each Promotional Discount you receive during the billing cycle, as outlined in any Promotional Discount offer we extend.

(c) The Annual Fee for your Card is printed on the Card Carrier accompanying this Agreement. The Annual Fee will be charged to your Account when your Account is opened and each one-year period after that. Periodically we will waive the annual fee for the first year. If your Card Carrier shows an Annual Fee of $0, your Annual Fee is waived for the first year and will be charged the appropriate fee for your Card every one year period after that.

(d) We will add a Late Payment Fee to the Purchase balance of the Account if your Minimum Payment is not received by the Payment Due Date shown on the monthly Account statement. The Late Payment Fee for your Account is $35.

(e) We will add an Overlimit Fee of $35 to the Purchase balance of the Account if you exceed your Credit Limit on any day on or before your statement cycle date. The Overlimit Fee disclosure will be determined by your state of residence. For KY, MI, OH and TN, the fee will be disclosed as Overlimit Fee FINANCE CHARGE $35. For residents of any other state the fee will be disclosed as Overlimit Fee $35.

(f) We will add a Returned Payment Fee of $35 to the Purchase balance of the Account if any payment on the Account is not honored or if we must return it to you because it cannot be processed. A check that is returned unpaid will be sent for collection.

(g) We will add a Returned Convenience Check Fee of $35 to the Purchase balance of the Account if you write a Convenience Check that we do not honor under the terms of this Agreement. (See "Convenience Checks" and "Paying and Stopping Payment on Convenience Checks" sections above for more details.)

(h) We will add a Duplicate Documentation Fee of $3 to the Purchase balance of the Account for each copy of a monthly statement, sales slip, refund slip, or Advance slip that you request. There will be no charge for documentation requests made in connection with a billing error notice, if our investigation indicates a billing error occurred.

(i) We will add a Phone Pay Fee FINANCE CHARGE of $15 to the Purchase balance of the Account if you call us to make a payment on your Account and are assisted by a customer service representative to make the payment.

(j) We will add an Account Management Fee FINANCE CHARGE of $2.50 per month to the Purchase balance of the Account if you voluntarily close your Account with a balance.

IMPORTANT INFORMATION ABOUT USING YOUR ACCOUNT

15. Insurance Charges – Credit life insurance and disability insurance are not required to obtain credit. If you are eligible, you may participate in a group credit card insurance program, which we have arranged. If you elect insurance coverage, an insurance premium charge (at the rate disclosed to you) will be added to the Purchase balance as of the closing date of each billing cycle based upon the Account balance (including accrued FINANCE CHARGES). The terms of your insurance coverage will be summarized in the Certificate of Insurance, which will be provided to you.

16. Credit Limit – The Account Credit Limit is the maximum amount of credit available and that you may owe under the Account at any time. You may not request or obtain additional Purchases, Advances or Balance Transfers once you have reached your Credit Limit. The initial Credit Limit is shown on the Card Carrier and will also appear on your monthly Account statements. We reserve the right to review your Account at any time and increase or decrease your Credit Limit. You may not increase your Credit Limit by carrying credit balances over the Credit Limit we make available to you. (Also see the "Advance Limits" section above for more information about limits on Cash Advance, Cash Equivalent Advance and telephone transfer transactions).

17. Payment – You must pay us in U.S. dollars with checks or similar payment instruments drawn on a financial institution located in the United States. We may, at our option, choose to make an exception and accept a payment drawn on a foreign bank. However, you will be charged and agree to pay any collection fees required in connection with such a transaction. The date you mail a payment is different than the date we receive that payment. For purposes of this Agreement, the payment date is the day we receive your check or money order at the address specified on your monthly Account statement. If you mail your payment without a payment coupon or to an incorrect address, it may result in a delayed credit to your Account. This may result in additional FINANCE CHARGES, fees, and possible suspension of your Account.

18. Minimum Monthly Payment – Each month, you must pay at least the Minimum Payment and any past due Minimum Payment(s) by the Payment Due Date shown in your monthly Account statement. You may, at your option, pay more than the Minimum Payment or pay the New Balance in full to reduce or avoid the Interest FINANCE CHARGE on the Account. The Base Minimum Payment is equal to the greater of $10 or 2% of your regular New Balance rounded to the next highest dollar or the full amount of any regular New Balance less than $10.00. In addition to the Base Minimum Payment, we may also require payment of one or more of the following items, as incurred:

(1) late, overlimit, annual, and/or Account management fees,
(2) the interest finance charge, and
(3) if your Account is over the Credit Limit, all of the balance amount over your Credit Limit.

Any Minimum Payment or additional amount you pay each month will not prepay any future Minimum Payments required, or change your obligation to make at least a Minimum Payment by the Payment Due Date.

19. Payment Application – We will apply payments to promotional or discounted interest rate Purchase, Advance and Balance Transfer balances before we apply payments to higher rate balances. If we cannot collect your check or other payment item within a reasonable period of time, we may post as an Advance transaction the full amount of any credit previously given and charge interest on this amount from the posting date of the transaction. After a payment has been made, the Bank reserves the right to withhold available credit in the amount of the payment for 7 business days. Any credit available before the payment is made will continue to be available for use during this time.

20. Skip Payment Option – We may, at our option, occasionally offer you an opportunity to "skip" your obligation to make the Minimum Payment due. You may not skip payments unless we make this offer to you. You may skip up to two (2) payments in twelve (12) months without incurring a Late Payment Fee, but those two monthly payments may not be payments that are required in consecutive months. You cannot use a skip payment option if your Account is subject to a Delinquency Rate, is otherwise delinquent, or is in default. When you take advantage of a skip payment option we offer, the interest will continue to accrue on the entire unpaid balance of your Account.

21. Change of address – Your monthly Account statements and notices about your Account will be sent to the address you provided in your application or your response to our Account solicitation. To change your address, you must call us at 1-800-NWA-VISA (TDD 1-800-846-2580) or write to us at the following address: U.S. Bank National Association ND, P.O. Box 6352, Fargo, ND 58125-6352. We must receive this information 15 days before the date a billing cycle closes to provide your Monthly Account statement at your new address. Note: If you have an address change within 45 days of the expiration date of your Card(s), please contact Cardmember Service at 1-800-NWA-VISA (TDD 1-800-846-2580) with that information so your new Card(s) can be mailed to your new address.

22. Authorized signers – You or any other Account obligor may ask us to issue a Card and otherwise give Account access to a person authorized to use the Account. This person is called an "authorized signer". You agree to be responsible for all Account transactions made by any such authorized signer. You agree not to give your Card to anyone else or allow anyone other than an authorized signer to use the Account. If you give your Card or Account number to someone other than an authorized signer, you will be liable for any charges made by that person, unless and except as expressly required by applicable law. You, as a primary or joint Cardmember and Account obligor, must call us at 1-800-NWA-VISA (TDD 1-800-846-2580) or write us at U.S. Bank National Association ND, P.O. Box 6352, Fargo ND 58125-6352 with any request to cancel and remove the Account authority of an authorized signer or any other person given access to the Account.

23. Lost or stolen Card or Convenience Checks – You must notify us immediately if your Card or Convenience Checks are lost or stolen or there is possible unauthorized use of your Card. You will not be liable for unauthorized use of the Account <u>after</u> you notify U.S. Bank National Association ND. You must notify U.S. Bank National Association ND by telephone at 1-800-NWA-VISA (TDD 1-800-846-2580), or in writing at P.O. Box 6352, Fargo ND 58125-6352. If this happens, we will ask you and all other persons given Account access to return all Cards and unused Convenience Checks to our Investigations Department. In addition, we have the right to close your Account and open a new Account. If we do so, new Cards and Convenience Checks will be issued for your new Account.

24. Using Your Card In A Foreign Country –
For VISA Accounts - You may use your Credit Card for retail purchases at foreign (outside the United States) merchants and for cash withdrawals from foreign ATMs that bear either the PLUS System or VISA logos. If you use your card at an ATM that bears only the PLUS System logo (and no VISA logo), the charge will be processed through the PLUS System and will be converted into U.S. dollars at the exchange rate established, from time to time, by the operator of that ATM, plus one percent of the result. If you use your card at a merchant or an ATM that bears the Visa logo (and no PLUS System logo), the charge will be processed through the VISA system and will be converted into U.S. dollars according to the applicable bylaws and rules established by VISA from time to time. If you use your card at an ATM that bears both the VISA and PLUS System logos, the ATM operator will determine whether to send your transaction over the VISA or PLUS System network using such network's respective currency conversion rules then in effect. You understand that the exchange rate in effect when the charge is processed may differ from the rate in effect on the date of the transaction or posting to your Account. The amount of your transaction in dollars if processed through VISA (under its current bylaws and rules) will be:

(a) The amount of the foreign currency times an exchange rate in effect one day prior to the processing date that is:
   (i) the government mandated rate, if there is one, or
   (ii) if there is no government mandated rate, the wholesale market rate, plus
(b) One percent (1%) times the resulting dollar amount, plus
(c) Our fee of 2% times the sum of subparagraphs (a) and (b).

25. Expanded Account Access - Any Card or PIN issued to or selected by you under this Agreement will access multiple checking, savings, line of credit and credit card account(s) in your name at the Bank or any of its bank affiliates; and any Account opened under this Agreement may be accessed by any Card(s) or PIN(s) that you have selected or that has been issued to you or may in the future be selected by you or issued to you by the Bank or any of its bank affiliates.

"Access" means use of a Card or Account number and PIN to conduct a transaction or obtain information at ATMs or via telephone, personal computer banking, or any other available method. There are no additional fees or charges for expanded Account access. The fees and terms disclosed for each Account apply. Expanded Account access may be available for up to five checking, five savings, and five line of credit or credit card accounts, and at other ATMs and with other methods of access, other limitations may apply.

U.S. Bancorp is a diversified financial services company. We offer a range of financial products and services through our family of financial service providers. The following members of the U.S. Bancorp family of financial service providers have adopted this privacy pledge:

Banks, Safe Deposit or Trust

- U.S. Bank National Association
- U.S. Bank Trust National Association
- U.S. Bank Trust National Association SD
- U.S. Bank National Association ND

Brokerage, Investment and Insurance

- U.S. Bancorp Investments, Inc.
- U.S. Bancorp Insurance Services, LLC
- The Miami Valley Insurance Company
- Mississippi Valley Life Insurance Company
- Elan Life Insurance Company
- U.S. Bancorp Insurance Company, Inc.
- U.S. Bancorp Insurance Services of Montana, Inc.
- U.S. Bancorp Insurance and Investments, Inc.

Diversified Services

- U.S. Bancorp National Account Services LLC
- Piper Jaffray Mortgage, LLC
- Gibraltar Mortgage Southwest, LLC
- Home Builders Mortgage, LLC
- Select Mortgage Lending, LLC
- Urban Neighborhoods Mortgage, LLC
- U.S. Financial, LLC
- HMSV-USB Lending, LLC
- U.S. Bancorp Advantage LLC
- U.S. Bancorp Premier LLC
- USbancorp Gold, LLC
- US Bancorp Consumer Finance of Kentucky
- U.S. Bancorp Equipment Finance, Inc.
- Lyon Financial Services, Inc.
- USB Leasing LLC
- USB Leasing LT

Additional Matters

1. Email

We may, from time to time, contact you at an email address belonging to you to tell you of changes or updates to our site, usbank.com. In addition, we may contact you at an email address belonging to you to inform you of products and services we think may be of interest to you. At any time, you may ask us to stop sending promotional information to that email address by simply replying to our email, and telling us of your preference. Or, you can tell us your preference on the 'Update Email Preferences' page at usbank.com.

2. Closed or Inactive Accounts

We will continue to follow the privacy policies and practices explained in our privacy pledge even after your account is closed or becomes inactive.

3. When Will My Choice Take Effect?

If you make a choice as explained on the attached tear-off form, we will process your request.

- **New Customers.** For new customers, we will allow you a reasonable time to express your preference before sharing personal credit information about you or including your name on direct marketing lists.
- **Direct Marketing Preference -- Delayed** Effect. You may make a direct marketing choice at any time. If you have previously permitted direct marketing, and you change your preference, it may take up to 10 weeks to stop receiving mail or telephone offers.

4. Multiple Copies of the Pledge

Although you will receive several copies of this pledge over time, you need to make your choice only once. Your choice remains in effect until you tell us otherwise.

5. To Change Election

If you would like to change a previous decision or choice, please call us at **1-800-370-8580.**

6. Additional Rights and Changes

- You may have other privacy protections under applicable state laws, such as Vermont and California. To the extent these state laws apply, we will comply with them when we share information about you.

This privacy pledge does not apply to your relationship with other financial service providers, such as nonaffiliated insurance companies. We may amend this privacy pledge at any time, and we will inform you of changes as required by law.

7. Want to Learn More?

If you would like to learn more about how we use financial information about clients to deliver better client services and products more efficiently, please come to a branch, contact your financial professional or see our Web site at ***usbank.com.***

Consumer Privacy: A Guide to How We Gather, Share and Protect Customer Information

www.usbank.com

Form #40174

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2/02

34. **Assignment of your Account to another Creditor** – We may assign, sell or transfer your Account and amounts owed by you to another creditor at any time. If we do, this Agreement will still be in effect unless and until amended, and any references made in this Agreement to "we", "us", "our" or "the Bank" will refer to the creditor to which we assigned, sold or transferred the Account or amounts owed under the Account. You may not delegate your obligations and responsibilities to us to any third party without our express written consent.

THE BANK'S LEGAL RIGHTS AND OBLIGATIONS

35. **Collecting credit information about you** – You authorize us to make any credit, employment and investigative inquiries we feel are appropriate related to giving you credit or collecting amounts owed on your Account. You agree that a consumer credit report may be requested periodically from one or more consumer reporting agencies (credit bureaus) and used in connection with your application and any update, renewal or extension of credit. We will provide information about you, your Account or your credit history to consumer reporting agencies and others who may properly receive that information.

36. **Credit bureau disputes** – If you believe we inaccurately reported credit history information about you or the Account to a credit bureau, call us at 1-800-481-9057 or write to us at U.S. Bank National Association ND, Consumer Recovery Department, Attn.: CBR Disputes, P.O. Box 108, St. Louis, MO 63166-9801.

37. **Privacy pledge and disclosure of Account information** – You will receive a copy of our Privacy Pledge when you open your Account and at least once annually while you remain our customer. We also keep copies of our Privacy Pledge in bank offices and post it on our web site at usbank.com. Our Privacy Pledge describes how we collect, protect and use your confidential financial and other information about you and the circumstances in which we might share information about you with members of our corporate family and with unaffiliated third parties.

    The Privacy Pledge also tells you how you can:
    (a) limit the ways we share certain kinds of information about you, and
    (b) request corrections to the information we maintain about you.

38. **Refusal to Honor Transactions** – The Bank and its agents are not responsible if anyone refuses to honor your Card or a Convenience Check, or if authorization for a particular transaction is not given. Although you may have credit available under the Account, we may be unable to authorize credit for a particular transaction. The number of transactions you make in one day may be limited, and the limit per day may vary. These restrictions are for security reasons. And as a result, we cannot explain the details of how this system works. If your Account is over limit or delinquent, authorization of credit for transactions may be declined. We are not responsible for anything purchased with your Card or a Convenience Check, except as expressly required by applicable law (see "Your Billing Rights" section below for more details). You must return goods you purchased with the Card or Account to the Merchant and not to us.

39. **Third party offers** – From time to time, third parties may provide you with benefits not related to the extension of Account credit. We are not liable for these features, services and enhancements, as they are the sole responsibility of the third party provider. The Bank and/or a third party may add, change or delete entirely these benefits without notice or liability to you, to the extent permitted by applicable law. You agree to hold us harmless from any claims, actions or damages resulting from your use of any of these features, services or enhancements, when permitted by applicable law.

40. **Telephone monitoring** – From time to time, we may monitor telephone calls you make to us or our agents.

41. **Severability** – If a court of competent jurisdiction finds any part of this Agreement illegal or unenforceable, the remaining portions of the Agreement will remain in effect as written after any such illegal or unenforceable portion is amended in conformance with applicable law or, if necessary, voided.

42. **Entire Agreement** – This version of the Agreement replaces any previous versions of the Agreement. The Agreement, as modified by any change in terms we may deliver from time to time in accordance with applicable law, constitutes the entire agreement between you and us, and supersedes any prior negotiation or understanding between you and us concerning the subject matter of the Agreement.

43. **Waiver** – We do not give up our rights under the Agreement or applicable law when we fail to exercise or delay exercising those rights. Our failure or delay to exercise any right or remedy we have against you does not mean that we waive that right.

44. **Arbitration** – By requesting an Account from us and accepting this Agreement, you agree that if a dispute of any kind arises out of this Agreement, either you or we can choose to have that dispute resolved by binding arbitration. If arbitration is chosen by any party, neither you nor we will have the right to litigate that claim in court or to have a jury trial on that claim, or to engage in pre-arbitration discovery, except as provided for in the arbitration rules. In addition, you will not have the right to participate as a representative or member of any class of claimants pertaining to any claim subject to arbitration. The Arbitrator's decision will generally be final and binding. Other rights that you would have if you went to court may also not be available in arbitration. It is important that you read the entire Arbitration Provision carefully before accepting the terms of this Agreement.

    Any claim, dispute or controversy (whether in contract, regulatory, tort, or otherwise, whether pre-existing, present or future and including constitutional, statutory, common law, intentional tort and equitable claims) arising from or relating to (a) the credit offered or provided to you, (b) the actions of you, us or third parties or (c) the validity of this arbitration provision (individually and collectively, a "Claim") must, after an election by you or us, be resolved by binding arbitration in accordance with this arbitration provision and the Commercial Arbitration Rules of the American Arbitration Association ("AAA") in effect when the Claim is filed (or, in the event this arbitrator or these arbitration rules are no longer available, then a comparable substitute arbitration procedure and/or arbitration organization that does business on a nationwide basis). There shall be no authority for any Claims to be arbitrated on a class action basis. An arbitration can

YOUR LEGAL RESPONSIBILITY IN THIS AGREEMENT

26. **Responsibility to pay** – You agree to pay us for all Purchases, Advances, Balance Transfers, FINANCE CHARGES, Account Fees and charges, any other transaction charges as provided in this Agreement and, to the extent permitted under applicable law, attorneys fees and collection costs we incur enforcing this Agreement against you. This is the case even if the Account is only used by one of you, or is used by an authorized signer chosen by only one of you. If there is more than one Account Holder, each of you is responsible, together and separately, for the full amount owed on the Account.

27. **Intent to repay** – Every time you use the Account, you represent to us that you intend and have the reasonable ability to repay your Account obligations. We rely on this representation every time you use the Account.

28. **Settling a disputed balance; Payment in Full** – If you want to settle a disagreement with us about any amount you owe by sending a check on which you have written "Payment in Full" or similar language, you must send us a written explanation of the disagreement or dispute and any such check to U.S. Bank National Association ND, P.O. Box 6335, Fargo ND 58125-6335. (See "Your Billing Rights" section below for complete details.) This address is different than the address you use to make Account payments. Writing "payment in full" or similar language on the check will not be enough to resolve the dispute. If we collect a check or any payment instrument marked "Paid in Full" that you sent to an address other than the one provided in this section (such as the address at which you normally make payments), we will not have waived our right to collect any remaining amount you owe us under the terms of the Account.

29. **Default** – You and the Account will be in default if:

    a) you do not make the Minimum Payment by the Payment Due Date disclosed on the monthly Account statement;
    b) you violate any other provision of this Agreement;
    c) you die without a surviving Joint Account Holder;
    d) you become insolvent, assign any property to your creditors, or go into bankruptcy or receivership;
    e) you have made false statements affecting the application or maintenance of your Account;
    f) you go over your Credit Limit;
    g) we have any reason to believe that the Account is in danger of, or is being used for fraud;
    h) you are a married community property state resident and you or we receive a written termination notice of this Agreement from your spouse; or
    i) anything happens that we believe in good faith materially increases the risk that you will not live up to your payment and other obligations under this Agreement.

30. **Illegal Purchases** – The Card must not be used for any unlawful purpose, such as funding any account that is set up to facilitate online gambling. You agree that you will not use or knowingly permit another to use the Card or Account for any transaction that is illegal under applicable law.

THE BANK'S LEGAL RIGHT TO CHANGE OR CANCEL THIS AGREEMENT

31. **Ownership of this Account; Governing Law** – Your Card and any other Account access devices that we supply to you are our property and must be immediately returned to us or our designated agent or otherwise destroyed or surrendered as we instruct. We extend all Account credit to you in and from the state of North Dakota, regardless of where you reside or use the Account. This Agreement is governed by North Dakota law, and, to the extent necessary for interest exportation or consumer protection purposes, by federal law, regardless of the internal conflict of law principles of the state where you reside or use the Account. If a dispute arises and you file a lawsuit against us, service of process must be made on the Bank at the following address: U.S. Bank National Association ND , 4325 17th Avenue SW, Fargo, ND 58103.

32. **Changes to the Account** – We may change all or any part of this Agreement at any time when we notify you in writing. We will give you the notice of any such change in the manner required by North Dakota and federal law. The changed terms will apply to all new and outstanding Account balances and everything you owe under the Account as of the effective date indicated in the notice or otherwise permitted by applicable law. If you do not want to accept the changes, you must provide us with written notice at the address contained in the Change in Terms notice no later than 25 days after the effective date of the change. In this case, we will close your Account and permit you to pay off the outstanding Account balances in full at that time or under the terms of your existing Agreement. You will have accepted any proposed change if the Account is used after the effective date of the changed terms, even if 25 days has not elapsed after any such effective date. Your account may be re-opened and subject to the new terms if (1) you use the Account or (2) charges post to the Account (including recurring/previously authorized charges) after you have notified us as provided in the notice you receive.

33. **Cancellation of your Account** – We may cancel your Account or suspend your ability to obtain Account credit immediately, without notice, if the Account is in default. Even if you are not in default, we may cancel the Account by providing notice to you. You may cancel your Account by notifying us by telephone at 1-800-NWA-VISA (TDD 1-800-846-2580) or in writing at P.O. Box 6352, Fargo ND 58125-6352. If this is a Joint Account, we will honor a request by either of you to cancel the Account. After the Account is canceled, you will not be able to obtain additional Account credit. After the Account is canceled, the Account may continue to receive recurring charges for items such as business subscriptions until you contact and cancel delivery with the company providing the item. After the Account is cancelled, all amounts outstanding on the Account will be immediately due and payable without notice or demand from us. You must cut all Cards and Convenience Checks in half and return them to us. If you do not pay the amount you owe under this Agreement, you will be liable for our collection costs including our reasonable attorney fees and expenses of legal actions, to the extent permitted by applicable law.

Our Privacy Pledge To You

Protecting your privacy is important to the U.S. Bancorp family of financial service providers. We value the trust you have placed in us, and your continued confidence is important to us. As you review our pledge, please remember that:

- We make safeguarding the information we gather about you a priority.
- We maintain security practices to keep personal information about you safe.
- We do not sell or share customer information with unrelated companies so that they can market their products to you.
- When we believe that an unrelated company offers products or services that would be of interest to you, we may communicate to you about them. These companies will not learn about your relationship with us unless you respond to their offer.
- When it comes to privacy, we believe that you have the right to make meaningful choices. If you tell us not to do so, we will not call, or send direct mail to you, for additional products or services. You can also choose how personal credit information about you is shared within the U.S. Bancorp family of financial service providers. It is your choice.
- We will provide you with helpful information about privacy and information security. For example, on our web site, you will find tips to help you protect yourself from identity theft, and limit direct marketing from others.

What Personal Information Is, And How We Gather, Protect And Share It

Our pledge applies to personal information, which is nonpublic information about you that we obtain in connection with providing a financial product or service.

1. Types Of Information We Gather

We may gather the following types of personal information about you:

A. Information about your identity, such as your name, address and social security number;
B. Information about your transactions with us, our affiliates or others, such as your account balance, payment history, credit card usage and Web site and customer service usage;
C. Personal credit information we receive from you on applications or other loan and account forms, such as your assets and income;
D. Personal credit information we receive from credit bureaus and other companies, such as your creditworthiness and payment history; and
E. Other information—Information from other outside sources, such as data from public records, that is not gathered for the purpose of determining eligibility for a product or service.

You may choose whether "personal credit information" described in categories 1C and 1D is shared within the U.S. Bancorp family of financial service providers. This choice is further discussed in Section 4 -- "Your Choices About How We Share Personal Information About You" -- below.

2. What Information We Share

In Section 4, below, we explain your right to choose how we share personal credit information about you. Subject to your choices to limit sharing as explained in Section 4, we may share all of the information we gather with:

A. Our "affiliates" (i.e., U.S. Bancorp family of financial service providers -- companies related to us by common control or ownership) that offer financial products and other services, including those identified in this privacy pledge and our administrative or service units that perform functions, such as servicing your accounts or preparing your account statements.

B. Unrelated companies that work for us, including:
Companies that perform support services for us, such as data processors, technical systems consultants and programmers, check printers, or companies that help us market products and services to you. All such companies that act on our behalf are contractually obligated to keep the information we provide them confidential and to use the information we share only to provide the services we ask them to perform for us.

We do not sell or share customer information with unrelated companies so that they can market their products to you. However, from time to time, we may communicate to you special offers for products or services of unrelated companies, which we believe may be of interest to you. These companies will not learn about your relationship with us unless you respond to their offers.

C. Companies and other entities as permitted by law.

3. We Protect the Confidentiality and Security of the Information We Gather

We restrict access to personal information about you to those employees we believe need to know that information to provide products and services to you. We maintain physical, electronic, and procedural safeguards to keep information about you safe.

4. Your Choices About How We Share Personal Information About You

You have the right to choose how we share certain personal information about you.

A. You May Tell Us Not To Share Personal Credit Information Within The U.S. Bancorp Family Of Financial Service Providers
In order to serve you better, we may share "personal credit information" (described in Sections 1C and 1D) we gather about you within the U.S. Bancorp family of financial service providers. Under the Fair Credit Reporting Act, **you may tell us not to share personal credit information about you within The U.S. Bancorp family by following the instructions on the attached form.** If you make this choice, we may still share information about your identity, and your transactions with our affiliates or us, or Other information.

B. You May Tell Us Not To Call Or Send Direct Mail To You For Additional Products Or Services
From time to time, we may call or write to tell you about additional financial products or services that we think may be of interest to you. **You may, however, tell us not to call or send direct mail to you for additional products and services, by following the instructions on the attached form.** Please note that if you make this choice, we will still call you and send you mail to service your existing relationships, or provide account related information (and, when doing so, the mail we send may include pre-printed marketing materials in those mailings).