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HSBC

By electronic delivery

July 18, 2008

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

Re: Docket No. R-1286

Dear Ms. Johnson:

This comment letter is submitted by HSBC Finance Corporation ("HSBC") in response to the Proposed Rule issued by the Board of Governors of the Federal Reserve System ("Board") to amend the open-end credit provisions of Regulation Z (the "May 2008 Proposal"). Among other companies, HSBC Finance Corporation wholly owns HSBC Auto Finance Inc., HSBC Consumer Lending (USA) Inc., Beneficial Company LLC, HSBC Mortgage Services Inc., HSBC Card Services Inc., HSBC Bank Nevada, N.A., and HFC Company LLC. HSBC is part of the HSBC Group, one of the largest financial services organizations in the world which serves over 128 million customers worldwide. In the United States and Canada, HSBC businesses provide financial products to nearly 68 million customers. In the United States HSBC Bank Nevada, N.A. is a top ten issuer of general purpose and private label credit cards. HSBC appreciates the opportunity to provide its comments on the Proposed Rule to the Board.

I. Section 226.5 General Disclosure Requirements

The Board has proposed to revise content requirements for several disclosures required by 226.5. HSBC is generally satisfied with the Proposed Rule revisions, and provides the following comments:

A. E-sign comments.

The Board proposes to add comment 5(a)(1)(ii)(A)–1 to clarify that certain disclosures, not required to be provided in writing, could be provided to consumers without regard to the Electronic Signatures in Global and National Commerce Act (E-Sign Act), 15 U.S.C. 7001 *et seq.* The Board further proposed adding comment 5(a)(1)(iii)–1 to clarify that the disclosures specified in §

226.5(a)(1)(ii)(A) also may be provided in electronic form without regard to the E-Sign Act when the consumer requests the service in electronic form, such as on a creditor's Web site. Lastly, the Board has proposed to modify Comment 5(b)(1)(ii)–1 in its June 2007 proposed revisions to Regulation Z, Docket No. R-1286 (the "June 2007 Proposal"), to clarify that disclosures under § 226.6(b)(4) may also be provided without regard to E-Sign Act compliance.

HSBC supports the Board's E-Sign related proposals. Consumer's expectations have changed – if they communicate with you electronically they expect an electronic reply without having to go through a consent process to receive an electronic communication. The clarifying comments will allow financial institutions to provide important disclosures to consumers without unnecessary formality and delay.

B. <u>Rates applied to permanently terminated accounts</u>.

Current comment 5a(b)(1)–7 specifies that a credit card issuer need not disclose an increased rate that would be imposed if credit privileges are permanently terminated. Based on consumer comment to the Board's June 2007 Proposal, the Board is now proposing to delete that provision which would require issuers to disclose an increased rate that would be imposed if credit privileges are permanently terminated. HSBC has two comments with respect to this proposal.

First, HSBC notes that the Board's Regulation AA § 227.24(b) exceptions to the proposed prohibition against increasing the annual percentage rate with respect to existing balances does not contemplate an issuer's ability to apply increased rates to existing balances once an account has been permanently closed by an issuer. To be clear, HSBC does not increase an APR in the event a cardholder acts upon a right to opt-out of changes in terms to the credit agreement. Such an action entitles a consumer to close an account and pay any remaining account balance under current account terms. However, HSBC believes a bank should have the discretion to impose a higher APR when account privileges are otherwise permanently terminated, as the higher APR provides an incentive for consumers to promptly pay in full any outstanding balances existing on the terminated account. In consideration of the Board's stated position that a bank may impose a penalty or other increased APR once credit privileges have been permanently terminated, HSBC believes this was merely an oversight. We therefore ask the Board to address the interplay between a closed account APR which will be required to be disclosed under § 226.5a(b)(1), but would be prohibited as a practice under other proposal.

Second, given current comment 5a(b)(1)-7, a financial institution who intended to impose a higher APR upon permanent termination of credit privileges would not have disclosed this right. Therefore, HSBC requests this new disclosure requirement apply prospectively only as to new accounts originated after the effective date of any final rule.

C. <u>Grace period label and content</u>.

Based on feedback from consumer testing, the Proposal modifies the existing requirements, and the June 2007 Proposal, regarding utilization of the term ‘‘grace period.” The Board’s consumer testing found that consumers are generally confused with the “grace period” terminology, and therefore has proposed using the phrase “how to avoid interest” (or “paying interest” if no grace period exists) or substantially similar terminology instead.

HSBC agrees with the Board’s May 2008 Proposal. HSBC’s own research regarding the term “grace period” resulted in similar findings. For example, some consumers believed “grace period” was a reference to the number of days a consumer could be late with a payment without penalty.

In regards to the substantive content within the grace period disclosure, HSBC is concerned with the Boards May 2008 Proposal to revise § 226.5a(b)(5). As noted by the Board, it conducted consumer testing utilizing the wording ‘‘Your due date is [at least] ___ days after the close of each billing cycle. We will not charge you interest on purchases if you pay your entire balance (excluding promotional balances) by the due date each month.’’ While the Board concluded that participants who read this language appeared to understand it correctly, HSBC believe this approach could lead to customer confusion and complaint with respect to certain credit promotions.

For example, it is somewhat prevalent in the retail credit industry to offer consumers “same as cash” promotions which give the consumer an opportunity to pay what is often a large purchase in full by the stated end date and avoid paying any interest whatsoever on that purchase. These promotions offer significant economic value to consumers, who may delay full payment on a purchase for 12-24 months [or longer] and avoid paying finance any charges with respect to such purchases. However, if these purchases are not paid in full by the expiration of the promotional period, the creditor will often bill finance charges calculated from the date of the transaction. Applying payments to all other balances before applying payments to these promotional balances will hurt consumers by making these same as cash promotions very difficult, if not impossible, to manage to a consumer’s reasonable expectation. HSBC will provide similar comment separately in response to the Board’s Regulation AA § 227.23(b) payment allocation proposals.

D. <u>Minimum interest charge</u>.

The May 2008 Proposal would add a de minimus dollar amount trigger of $1.00 for the required disclosure of minimum interest or finance charges. Currently, card issuers must disclose in the summary table at application and account opening any minimum interest or finance charge. The $1.00 trigger would be adjusted when cumulative percentage changes to the Consumer Price Index added to the $1.00 trigger equals or exceeds the next whole dollar. HSBC supports the Board's Proposal, as it does not believe such a de minimus fee is something consumers actively comparison shop when looking for a credit card.

E. <u>Membership Fees</u>

Currently and under the June 2007 Proposal, creditors may collect or obtain the consumer's promise to pay a membership fee before the disclosures are provided, so long as the consumer can reject the plan after receiving the disclosures. If a consumer rejects the plan, the creditor must promptly refund the fee, if it has been paid, or take other action necessary to ensure the consumer is not obligated to pay the fee.

HSBC appreciates the additional clarity being provided on this topic, but it is concerned about the May 2008 Proposal's comment 5(b)(1)(iv)(3) which provides, in part:

> "3. *Using the account.* A consumer uses an account by obtaining an extension of credit after receiving the account-opening disclosures, such as by making a purchase or obtaining an advance. *A consumer does not ''use'' the account by activating the account, such as for security purposes.*" [Emphasis added]

While generally in support of the concept that activation does not in of itself indicate acceptance of the credit plan, HSBC is alarmed at any suggestion that a customer should activate an account he/she does not intend to use *for security purposes*. HSBC does not recommend a consumer do this, as activation of a card increases the potential that the cardholder will be a victim of fraud. Once activated, a card may be taken by a wrongdoer. This is particularly dangerous in the event a person activates a card he/she does not intend to use, as that could lead to unsafe storage of the credit card and unnoticed absence in the event it is taken. HSBC is opposed to a suggestion or inference in any regulation that the practice of activating an account for security purposes serves this purpose. HSBC suggests a simple mention that card activation, without actual use, does not indicate acceptance.

II. Section 226.6 Account-opening Disclosures.

The Proposal would require creditors assessing fees at account opening that comprise 25% or more of the minimum credit limit to provide a notice of the consumer's right to reject the plan after receiving the disclosures if the consumer has not used the account or paid a fee (other than certain application fees). HSBC understands the Board's reasoning for suggesting enhanced disclosures in the event account opening fees may exceed 25% of the possible minimum credit line, and does not object to the Proposal's enhanced disclosures.

III. Subsequent disclosure requirements.

A. Checks that Access Credit Card Accounts.

The June 2007 Proposal required creditors to disclose on the front of the page containing the checks that access credit card accounts information such as the rates that will apply if the checks are used, any transaction fees, and whether or not a grace period exists. The May 2008 Proposal would add a subsection §226.9(b)(3)(A) to require disclosure of any date by which consumers must use the check to receive the disclosed rates. HSBC currently provides a date by which account access checks must be used.

B. Changes in Consumer's Interest Rate and Other Account Terms.

The June 2007 Proposal proposed that when a change-in-terms notice accompanies a periodic statement, creditors provide a tabular disclosure on the front of the periodic statement of the key terms being changed. Consistent with the 2008 Regulation AA Proposal that restricts creditors' ability to apply increased rates to certain existing balances, creditors would be required to clarify how existing or new balances would be affected by any rate increase.

Other than above comment concerning a need to create an exception to address a bank's ability to impose a closed account APR on outstanding balances, HSBC will provide further comment to the Board within its comment letter in response to Regulation AA proposals.

IV. Prompt Crediting of payments.

The May 2008 Proposal seeks to add a new Section 226.10(b)(2)(ii) which would codify that a cut-off hour for mailed payments prior to 5:00 p.m. on the due date would be deemed an unreasonable instruction. The banking industry has historically required transactions to take place prior to the close of business to allow for timely processing of transactions. It is HSBC's belief that most credit card issuers use a reasonable late afternoon (e.g. 3:00 p.m.-4:00 p.m.) cut-off hour for mailed payments, which allows an ability to process the vast majority of payments received that day, without incurring significant increases in after-business-hours operational expenses. Extending the cut-off time for mailed payments to the proposed 5:00 p.m. deadline could significantly increase operational costs which may be passed on to the consumer without consumers receiving significant benefits in return.

Therefore, HSBC advocates that current cut-off hours, established at different times by different creditors consistent with their mail-receipt operations, are already sufficiently regulated by the established "reasonableness" standard and protect consumers from abuses. This portion of the May 2008 Proposal should not be adopted and rules should only require that a creditor must clearly disclosure a reasonable cut-off time for all payment channels and payments methods used by consumers that would allow the majority of borrowers to make conforming payments.

V. Investigating Allegations of Unauthorized Use or Billing Errors

The May 2008 Proposal clarifies that a creditor may not deny a claim solely if the consumer does not comply with a request to sign a written affidavit or file a police report, and for consistency extends guidance for reasonably investigating claims of unauthorized transactions to allegations of billing errors.

In its proposal, the Board makes changes to the Regulation and Commentary dealing with consumer claims of unauthorized use. One of the changes, duplicating the Commentary to 226.12(b) regarding unauthorized use to apply also to 226.13(f), makes sense and is appropriate. However, we do have some concern with the second change, namely, an addition to that Commentary that adds a provision that a credit grantor may not require a consumer to provide an affidavit or a police report to substantiate their claims of unauthorized use. The Board's justification for this addition is that they believe that such requirements could create a "chilling effect" for consumers who wish to assert their rights in this area. We agree that requiring that the consumer obtain a police report could have such an effect[1]. However, it is hard to imagine how requiring a consumer to provide a credit grantor with a signed statement of their claim could dissuade the consumer from making the assertion.

Claims of unauthorized use are rarely straight forward. In most cases, the unauthorized user is either a family member or an acquaintance of the consumer making the claim. Moreover, in many cases, the consumer's signature as compared to the signature appearing on a sales slip is the key piece of evidence

[1] Although we would note that California in Civil Code Section 1788.18, and New York in the newly passed General Business Law Article 29-HH, both require a consumer to obtain a police report in order to substantiate claims of identity theft to debt collectors.

in the credit grantor's investigation. But, in today's electronic signature world, the credit grantor may not have an exemplar of the consumer's signature with which to compare the allegedly unauthorized signature appearing on the sales slip.

The most common solution employed by credit grantors to resolve this dilemma is to request that the consumer provide a signed statement stating that he/she did not make the purchase in question. Such a request is not burdensome, and it establishes that the consumer is genuine in their claim. Moreover, it provides the credit grantor with a current exemplar of the consumer's signature to use in its investigation. While in most cases an unsworn and unwitnessed statement is sufficient, in those cases where the perpetrator is a family member or friend, having a witnessed signature may be the only way to verify its authenticity. Additionally, such a witnessed statement may be used by the credit grantor in convincing local authorities to prosecute the perpetrator. While obtaining a notary's jurat is an additional step for the consumer, it is one that is easily accomplished and should not chill the sincere claimant from asserting their claim. In summary, we would urge the Board to reconsider its exclusion of an affidavit as an investigating tool.

VI. Advertising Provisions.

The May 2008 Proposal includes new disclosure requirements for advertising promotional and deferred interest credit programs. HSBC respectfully disagrees that requiring additional disclosures in the actual advertisements for these programs would aid consumers in their understanding of how these products operate. To the contrary, these additional disclosures would create wordy and sometimes confusing disclosures. Consumers are familiar with these long standing programs and have access to credit applications and other documents which contain the full terms and conditions of the specific credit program offered.

The May 2008 Proposal's requirement that the deferred interest period or the date by which the consumer must pay the balance in full to avoid finance charges on the balance in a clear and conspicuous manner in immediate proximity to each statement of "no interest," "no payment;" "deferred interest" or analogous terms is excessive. Disclosure of this information in this manner will neither be more noticeable nor more understandable to consumers. In fact, such disclosures may cause consumer confusion since the addition of more text may prevent the reader from fully understanding the product being advertised. There is no evidence that consumers have been confused by current advertisements for these types of promotional offers.

<u>Promotional rates</u>. Creditors would not be able to succinctly advertise the "date the promotional rate will end or the promotional period" or "the annual percentage rate that will apply after the end of the promotional period" (Proposed

Section 226.16(e)(4)) as this information would be determined by certain action taken by the consumer, whether that action is opening an account, posting a transaction, or otherwise. Therefore, this detailed explanation of product terms is better positioned within the credit application, billing statement or the other documents that fully explain the promotional offer.

Deferred interest offers. The proposed additional regulations regarding deferred interest, namely explanations regarding accrued interest, default interest, and amortization are also detailed explanations of possible, not probable or expected scenarios a consumer may confront. Therefore, requiring creditors to include these detailed disclosures in advertisements is unnecessary.

HSBC respectfully requests that this portion of the May 2008 Proposal not be adopted since creditors should have the authority to craft disclosures that are appropriate for advertising materials. Strict rules regarding placement and content of disclosures may lead to potential customer confusion and could cause more harm than benefit.

VII. Effective Date

As noted in its comments to the June 2007 Proposal, HSBC strongly urges the Board to provide card issuers with sufficient time to review and implement any Final Rule published as a result of this comment process. As the Board knows, the Proposed Rule is extremely comprehensive and its implementation will require significant systems work, operational revisions, and testing. We note that the Board granted creditors a year to implement the significant revisions to Regulation Z published in 1981 and has in other instance provided for a long implementation period. In light of the increased complexity of systems and products since 1981, we believe it would be appropriate to grant card issuers no less than 18 months, and preferably 24 months, to implement any Final Rule.

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Again, HSBC appreciates the opportunity to provide its comments on the May 2008 Proposal. Please do not hesitate to contact me at (952) 358-4847 in connection with this comment.

Sincerely,

James S. Hanley
Senior Counsel