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April 14, 2010

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave., NW
Washington, DC 20551
Attention: Docket No. R-1384

Re: Proposed Rule on CARD Act Requirements Effective August 22, 2010

Dear Ms. Johnson:

This comment letter is submitted by Barclays Bank Delaware ("BBD") in response to the proposed rule ("Proposed Rule" or "Rule") issued by the Federal Reserve Board ("Board") to implement the "Credit Card Accountability Responsibility and Disclosure Act of 2009" (the "CARD Act" or "Act") provisions that are scheduled to become effective on August 22, 2010.

BBD is a partnership focused issuer of credit cards with $10+ billion in credit card receivables and 6 million credit card accounts. Some of its credit card partnerships cards include the LL Bean card, the US Airways Card, the Barnes and Noble card and the Carnival Cruise lines card. As a bank wholly focused on the issuance of credit cards, BBD appreciates the opportunity to make its views known on this important matter.

SUMMARY

BBD appreciates the efforts by the Board to come up with a balanced rule consistent with the provisions of the Act. BBD supports the Board's proposal in coming up with the two "safe harbor" options for penalty fees (the "percentage" and "dollar" options). A meaningful safe harbor option is fair, will increase transparency and will make compliance easier. We also support the flexibility incorporated into the biannual evaluations of all Annual Percentage Rate increases made since January 1, 2009. That stated, BBD does have some recommendations that it believes will make the Rule more consistent with the provisions of the Act.

First we urge that the Board, in coming up with the proposed dollar "safe harbor" option, to consider both the costs reasonably incurred by issuer as a result of the event giving rise to the penalty fee and the amount of the penalty fee reasonably necessary to deter that event. Consideration of both factors is consistent with the Act and is fair in that those cardholders whose actions cause issuers to incur incremental costs should pay for those costs. Similarly, issuers who establish their own penalty fee amounts should be permitted to include both costs and deterrence in their calculations. Second, we submit that credit costs (along with reserves) should be one of the factors included in the determination of the total costs incurred by the card issuer as a result of the violation giving rise to the penalty fee. Third, we urge that the percentage safe harbor be a percentage of the total amount due – not just the minimum amount due – otherwise the percentage safe harbor is just not that meaningful. Finally, we also have some suggestions for disclosures regarding the penalty fees and the reevaluation of rate increases.

LIMITATIONS ON PENALTY FEES

Costs Plus Deterrence Plus Other Factors

The Proposed Rule's standards for determining whether a penalty fee is reasonable and proportional to the violation, as currently drafted, are inconsistent with the CARD Act and will significantly reduce issuers' ability to recoup their actual costs incurred as a result of the violation. Section 102 of the CARD Act directs the Board, in establishing reasonable and proportional penalty fees, to consider both the costs incurred by an issuer as a result of the violation giving rise to the penalty fee and the deterrence of such violations by the consumer, as well as any other factors deemed necessary or appropriate. However, instead of allowing issuers to consider both costs and deterrence as well as other relevant factors, the Proposed Rule would require an issuer to justify its penalty fee structure based on only one of the first two factors or to accept a safe harbor fee established by the Board. A related concern is that the Board in coming up with its safe harbor dollar amount should similarly consider both costs and deterrence.

Accordingly, consistent with the CARD Act, we strongly recommend that the Board amend the Proposed Rule to establish standards that not only reflect the actual total costs incurred as a result of a violation, but also are sufficient to deter such violations. We also urge the Board to adopt a safe harbor penalty fee dollar amount that reflects both costs incurred by issuer and deterrence.

Safe Harbor – Data Analysis

BBD supports the Proposed Rule insofar as it includes a safe harbor provision that would permit issuers to impose penalty fee amounts established by the Board. Specifically, an issuer would be deemed to have complied with the reasonable and proportional penalty fee requirement if the dollar amount of the penalty fee does not exceed the greater of: (1) a specific dollar amount set by the Board (to be established); or (2) five percent of the dollar amount associated with the violation, provided the dollar amount does not exceed an upper dollar amount set by the Board (which also has yet to be established).

The Board has requested commenters to submit data supporting what would be an appropriate safe harbor amount. In particular, the Board requested that issuers submit data regarding the costs incurred as a result of a particular type of violation and the dollar amounts reasonably necessary to deter violations, as well as the methods used to determine those amounts.

A number of credit card issuers, in response to the Board's request, working through Argus Information & Advisory Services ("Argus"), have compiled data regarding both the costs they incur as a result of late payments, and as to the dollar amount reasonably necessary to deter late payments. The firm of Morrison & Foerster, on behalf of those issuers will be submitting details as to Argus' findings regarding both data sets. BBD as a participant in that analysis urges the Board to consider that data carefully in its calculation of the safe harbor dollar amount. As can be seen in that submission, the industry average costs incurred as a result of late payment, per late payment, range greatly. The reason for variance is what is included in the cost calculation. One approach is to consider only those direct and indirect expenses attributable to late payments and collections activities and to exclude all credit losses and reserves from the calculation. That resulted in an industry average cost per late payment of $28.40. Another approach is to include such direct and indirect expenses plus late fees that are not recovered (either as part of a workout program or because they are assessed on accounts that are written off) and to exclude loss principal or interest – this would result in an average industry cost of $32.45 per late payment. Including a portion of credit losses and reserves that issuers incur as a result of late payment would cause that industry average number to go up exponentially. BBD also submits that since the issuers participating in the analysis are primarily the larger issuers, the cost incurred by smaller issuers who do not have the larger issuer's economies of scale may be higher than the numbers in the Argus analysis.

BBD urges the Board to consider all costs in coming up with a safe harbor dollar amount (see "Costs incurred as a result of violation" supra). The Board acknowledges that an issuer may incur greater costs than the amount of any penalty fees assessed as a result of the Proposed Rule. While the Board suggests that an issuer may recoup these costs by spreading them evenly among all other consumers by charging higher upfront costs, we believe that this result to be unfair to consumers who make payments in accordance with their account terms. Consumers who are making timely payments should not have to subsidize the cost of credit for those consumers who choose to violate the terms of their accounts by making late payments or by using convenience checks after engaging in other transactions that delete their available credit.

In addition, Argus conducted a survey 2,076 credit cardholders and asked them what level of fee would serve to deter them from paying late. The survey found that a fee in the amount of $30-$34 was required for 50% of respondents to say the fee was high enough to deter late payment behavior. Interestingly, a fee amount of over $50 was required for over 80% of respondents to say the fee amount is high enough to deter late payment behavior. Modeling conducted by Argus confirmed that there is a positive correlation between the amount of the late fee and deterring delinquency. The modeling found that in practice, late fees begin to deter delinquency at $28, with the deterrent effect increasing as the amount of the fee increases (this is consistent with the survey in that $28 would deter less than 50% of cardholders from making late payments). It is important that the Board set safe harbor to be at a level which significantly deters violations. Otherwise it will be difficult to manage credit risk as the issuer will not know if the consumer is paying late because the consumer cannot repay at all or because the consumer is indifferent to being assessed late fee at such a low level. Moreover, given the current inability to raise rates on existing balances pursuant to the CARD Act, the rate of late fees in deterring late payments may be more important than it has been historically.

Accordingly, BBD urges that the Board at a minimum establish a safe harbor amount that is sufficient to compensate issuers for their costs incurred as a result of the violation plus serves as a deterrence for at least 50% of cardholders.

Second, we urge that the so called percentage safe harbor be a percentage of the total account balance, subject to a cap, and not a percentage of the minimum payment amount. The cardholder is required to repay the full account balance under the terms specified in the credit card agreement. If the cardholder does not make or is late in making a payment under the credit card agreement, the full account balance is the amount which is at risk of non-payment – not just the required minimum payment. Moreover, making the safe harbor a percentage of the minimum payment amount reduces the percentage safe harbor amount to an amount which not only represents a tiny fraction of costs, it provides no deterrent effect whatsoever. For example, if the required minimum periodic payment is $50 (1% of a $5,000 balance) pursuant to the formula in the Proposed Rule, the issuer could not impose a late fee greater than $2.50 – if it is $100, (1% of a $10,000 balance) the late fee could not exceed $5. Even if the minimum payment due calculation was double to 2%, the amount of late fee on very large balances would be limited to $5 and $10 respectively. On smaller (average size) balances, the Proposed Rule's linkage of the amount of the penalty fee to a percentage of the minimum amount due ($15-25 range resulting in a late fee of $0.75 to $1.25) reduces that fee to an almost evanescent level. All the above situations clearly represent an insignificant penalty fee that does not come close to approximating costs, nor would it be a deterrent. Similarly, if consumer submits a payment by check that is returned, we urge that the amount associated with the violation is at least the amount of that check, not the required minimum payment.

<u>Prohibited Fees</u>

Tying the amount of the violation to the required minimum payment is especially problematic in the context of the fee prohibition included in the Proposed Rule. That is, the Proposed Rule would prohibit penalty fees that exceed the dollar amount associated with a violation. For example, if a consumer has a required minimum payment of $15, an issuer would be prohibited from charging a late fee that exceeds $15, even though the issuer's costs incurred in connection with such a late fee far exceed $15. As demonstrated above, this could result in late fees which do not come close to allowing issuers to recover their costs nor to deter late payments.

Similarly, under the Proposed Rule, an issuer would be prohibited from imposing a fee in connection with transactions that the card issuer declines to authorize. Prohibiting an issuer from imposing a fee for declining a transaction may be understandable in the context of a point-of-sale transaction; however, the Board should distinguish between declinations at the point of sale and declinations in connection with convenience checks or similar instruments. That is, the Board should not prohibit an issuer from assessing a penalty fee for the return of a convenience check where there is no available credit or when the convenience check has expired, because issuers frequently incur costs for the return of such instruments similar to the costs incurred in connection with returned checks.

Costs incurred as a result of a violation

BBD urges the Board to consider as a part of the cost of late payments, at an absolute minimum, those direct and indirect expenses that can reasonably be directed to late payment and collections expenses, including reasonable proportions of corporate overhead allocations, systems expense, credit risk department expense as well as the lost use of the funds the consumer has not paid.

In addition, the Proposed Rule would not permit an issuer to include any portion of credit losses incurred by the issuer as a result of such violations nor the costs associated with holding reserves against such losses when the issuer makes its cost analysis. In other words, even though the Board states that an issuer should be able to consider its "total costs," the Proposed Rule prohibits the issuer from considering two of the principal elements of its total costs. BBD thinks this would be a mistake. Late payments positively correlate with credit losses. Therefore we strongly urge the Board to reconsider the prohibition against including at least some portion of costs relating to losses and loss reserves in an issuer's cost analysis – similarly BBD urges the Board to consider such costs when it comes up with a safe harbor dollar amount.

Without the ability to consider losses, the penalty fee amount will not accurately reflect the true costs incurred in connection with certain types of violations and issuers will incur costs that exceed the penalty fee amounts. As acknowledged in the supplemental information, "the proposed limitation…may encourage card issuers…to build costs into upfront rates and fees" in order to recoup total costs incurred. As a result, issuers will be forced to increase rates on new and existing accounts. In essence, without including credit losses and reserve costs into the calculation, cardholders who pay on time each month will end up subsidizing cardholders who pay late. This is especially true now that issuers are limited by the CARD Act in what actions they can take as a result of late payments. We therefore recommend that the Board revise the Rule to permit issuers to factor in some portion of costs related to their actual losses resulting from such violations and that the Board itself considers such costs when coming up with its safe harbor dollar amount.

In addition, we request that the Proposed Rule be clarified to provide that, while an issuer must make an independent determination as to whether a specific dollar amount is reasonable and proportional, the issuer is permitted to use aggregate industry numbers regarding the nature and amount of the costs caused by various types of violations when making its determination that its own penalty fees are reasonable and proportional. Specifically, the costs incurred standard should be modified to allow an issuer to use any reliable information that is available to the issuer concerning the costs of such violations. This is especially important when the issuer does not currently have data on such costs, such as, in connection with a new account offering or when changing to a new service provider. It also is important for smaller issuers and new entrants to the marketplace. Without these modifications, most issuers will not be able to utilize the proposed cost standard and will be forced to use the safe harbor price fixed by the Board under the Rule.

Deterrence of violation

The Proposed Rule would permit an issuer, as an alternative to "impose a [penalty] fee for violating the terms or other requirements of an account if the card issuer has determined that the dollar amount of the [penalty] fee is reasonably necessary to deter that type of violation using an empirically derived, demonstrably and statistically sound model that reasonably estimates the effect of the amount of the [penalty] fee on the frequency of violations."

The proposed standard is problematic because of the stringent conditions that would be required for determining whether a particular penalty fee is necessary to deter violations (*i.e.*, independent of all other variables, the imposition of a lower fee would result in an increase in violations). It would be difficult, if not impossible, for an issuer to use the proposed deterrence standard as a basis for establishing the amount of a penalty fee. To meet this standard, an issuer would be required to test the effect of various penalty fee amounts that are lower and higher than the amount ultimately found to be reasonably necessary to deter a particular type of violation. For most issuers, it will be impossible to gather the necessary data by the August 22, 2010 effective date. In this regard, the Proposed Rule states that if an issuer cannot complete deterrence testing prior to the effective date, the issuer must assess penalty fees based on costs incurred by the issuer or on the safe harbor discussed below. Thus, under the proposal, if an issuer cannot complete the deterrence testing before the August 22, 2010 effective date, the issuer would effectively be precluded from ever testing higher penalties fees because such amounts may not fall within the safe harbor limits.

Disclosures

Under the Proposed Rule, an issuer would be required to revise all disclosures relating to the amount of any late fee or other penalty fee. Specifically, the Proposed Rule would permit an issuer to disclose either a range of penalty fees or an "up to" amount. BBD submits that there are several important clarifications regarding the "up to" disclosure requirement that should be made, including:

- Clarification that the imposition of a lower penalty fee or the waiver of a penalty fee would not trigger a 45-day advance notice and the right to reject the penalty fee "increase" before assessing a penalty fee that is within the "up to" amount disclosed to the consumer;
- Clarification regarding the use of a percentage of the minimum payment (or hopefully of the total balance) for the late fee. Specifically, the Board should clarify that the late payment warning display of the maximum late payment fee on the periodic statement is a static disclosure, rather than a variable field. BBD urges that issuers not be required to display the actual late payment fee associated with each particular billing cycle based on the percent of the minimum payment (or hopefully on a percent of the total balance);
- Clarification that a partial payment does not require an issuer to adjust the calculation of the "amount of the violation." For example, for late payment purposes, the percentage of the required minimum periodic payment (or percent of total balance) can be used notwithstanding the receipt of a partial payment on the account. In this

regard, at the time the late fee is imposed, the issuer likely will not know that a partial payment has been or will be made;

- A clear statement in the text of the regulation or commentary clarifying that there is no notice requirement for any reduction in a penalty fee, even if the way in which the fee is determined or calculated will change. A change in how the fee is determined (*i.e.* a percentage of the required minimum payment) should not require an issuer to provide any notice if the amount of the fee is being reduced;
- In recognition of the short amount of time issuers will have to revise account-opening disclosures and other related disclosures to reflect fee reductions and related changes, BBD urges the Board to include implementation guidance clarifying that for a reasonable period of time, an issuer can continue to use existing disclosure forms that include higher penalty fees so long as the issuer complies with the fee restrictions contained in the final rule and any penalty fee or fees imposed by the issuer are equal to or less than the fee(s) included in those disclosure forms. Given the compressed compliance time frame, it simply will not be possible for issuers to substitute new disclosures prior to the effective date, particularly at point-of-sale locations.

Reevaluation of Penalty Fees

The Proposed Rule also requires an issuer to reevaluate its cost or deterrence determination at least once every 12 months. If an issuer determines that a penalty fee should be lower, the issuer must begin imposing the lower penalty fee within 30 days after completing its reevaluation. In contrast, if an issuer determines that a penalty fee should be higher, the issuer must comply with the 45-day advance notice requirements before imposing the higher fee.

Since penalty fee increases will have to be based either on costs incurred by the issuer or deterrence of the particular account violation, the Board should clarify that the right to reject does not apply in this context by amending the requirements to expressly exempt penalty fee increases pursuant to cost or deterrence determinations. Application of the right to reject to increases based on an issuer's annual reevaluation inappropriately interferes with the ability of an issuer to make adjustments in fees that would otherwise be permitted under the Rule. Similarly, BBD urges the Board to clarify that neither the 45 day notice nor the right to reject applies to increases in penalty fees resulting from adjustments to the Consumer Price Index.

REEVALUATION OF RATE INCREASES (PROPOSED SECTION 226.59)

Proposed Section 226.59 implements the CARD Act provision requiring an issuer who increased the rate on an account based on risk or other factors to consider changes in "such factors" when subsequently determining whether to reduce the rate on that account. Specifically, an issuer will be required to review, every six months, any account where the rate has been increased since January 1, 2009. The CARD Act expressly states that this provision should "not be construed to require a reduction in any specific amount."

We commend the Board for not proposing rigid standards that an issuer must consider in connection with reevaluating a rate increase. Rigid standards setting forth specific factors which an issuer must include or exclude would constrain an issuer's ability to establish and to modify underwriting standards that are consistent with existing external environmental factors. As the Board stated, factors used to implement a rate increase may be out of date by the time of the reevaluation. Accordingly, we support the clarification in the Proposed Rule than an issuer would not be required "to base its review . . . on the same factors on which a rate increase was based" and that an issuer would be permitted to "review either the same factors on which the rate increase was originally based, or to review the factors that it currently considers when determining the [rate] applicable" to the account.

As presently drafted, the Proposed Rule could require an issuer to review an account with a rate increase until the issuer reduces the rate to a rate applicable to the account immediately prior to the increase, subject to changes in the applicable index. We recommend that the Board limit how long an issuer is required to review an account to avoid a potentially indefinite obligation to reevaluate an account every six months. We propose that the Board amend the Rule to permit an issuer to cease reviewing a rate increase when the rate is at the level it would be if the consumer were a new customer subject to a review of the issuer's current factors. This approach is consistent with the Proposed Rule that permits an issuer to review current factors, and could benefit consumers and issuers alike by encouraging issuers to implement rate reductions more quickly so that issuers can cease reevaluations. As an alternative to the limitation mentioned above, we recommend that the Board amend the Rule to limit an issuer's duty to reevaluate a rate increase to a period of three years; thus, an issuer would only have to perform six such reviews for any specific account.

The Proposed Rule also addresses the application of the proposed requirement to acquired credit card portfolios. With some exceptions, the obligation to review risk changes would be applicable to accounts that an issuer acquires. Significantly, under the Proposed Rule, an issuer would be permitted to use the factors that the issuer itself currently considers in determining the rates applicable to its own accounts. We support this essential flexibility, since it is unlikely that issuers will have sufficient information about the selling issuer's pricing practices to do otherwise.

We also support the clarification under the Proposed Rule that the reevaluation requirement only applies to rate increases for which 45 days' advance notice is required; and support the inclusion of two exceptions to the reevaluation requirement – rate increases following a rate reduction pursuant to the Servicemembers Civil Relief Act and rate increases in connection with charged off accounts. In addition, the Proposed Rule should not require an issuer to review a rate increase pursuant to a 60-day delinquency (due to provision for an automatic decrease if consumer makes 6 consecutive on-time payments).

We recommend that in addition to the above, the Board amend the Rule to clarify that a rate increase resulting from the loss of a promotional rate pursuant to contractual requirements does not trigger the reevaluation of rate increase requirements. The loss of a promotional rate is not based on credit risk or market conditions, that an issuer typically considers in connection with rate increases on an entire portfolio or to a certain class of accounts. Rather, a rate increase based on the loss of a promotional rate is a contractual determination. In this regard, an issuer does not consider specific factors as part of the rate increase; rather, the rate increase is pursuant to the terms of the promotional offer. Failure to comply with these terms results in the loss of the promotional rate. Accordingly, the requirement to review such rate increases should not apply in this context.

Proposed Section 226.59(a)(2) states that if a card issuer is required to reduce the rate applicable to an account pursuant to § 226.59(a)(1), the card issuer must reduce the rate no later than 30 days after completion of its evaluation. In the context of a rate reduction, the Proposed Rule is not clear concerning the application of the reduced rate. Consistent with the requirement that a rate increase be prospective and for ease of compliance, an issuer should be permitted to apply the reduced rate to the outstanding balances that were subject to the rate increase reevaluation. Requiring the reduction to apply to all outstanding balances would be operationally difficult to implement.

If you have any questions regarding these comments, please do not hesitate to contact me at (302) 255-8700 or at cwalker@barclaycardus.com.

Sincerely,

Clinton W. Walker

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