WRITTEN STATEMENT

OF

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Good Morning Chairwoman Maloney and Ranking Member Gillmor. I am a partner in the law firm of Morrison & Foerster, and I practice in the firm's Washington, D.C. office. Prior to joining Morrison & Foerster, I was an Associate General Counsel in the Legal Division of the Board of Governors of the Federal Reserve System for over 15 years. Prior to that, I worked at the Federal Reserve Banks of Boston and Chicago. In all, I have over 30 years of experience in banking and other financial services issues, including issues relating to credit cards. During that time, I have had the opportunity to be intimately involved in both drafting and interpreting regulations as a regulator and in advising financial institutions on how to interpret and comply with regulations. I have witnessed first hand the changes in industry practices brought about by regulatory changes and costs and other difficulties incurred in compliance. I am pleased to appear before you today to discuss important issues involving the credit card industry.

Credit Cards

Today, credit cards are among the most popular and widely accepted forms of consumer payment in the world. In 2005, the total value of credit card transactions charged by U.S. consumers alone exceeded 1.8 trillion dollars. Credit cards can be used at millions of merchants worldwide. As a result of the convenience, efficiency, security and access to credit that credit cards provide to American consumers, credit cards have become a driving force behind our national economy. Credit cards also have facilitated the development of new markets, such as the Internet, where credit cards play an essential role.

Credit cards offer other benefits to consumers including consolidation of transactions into a single statement payable once a month, the ability to accurately track expenses and freedom from cash dependency when shopping locally or when traveling around the world. In addition, consumers typically enjoy protections that are unavailable in cash transactions when they use credit cards, including protection from loss or theft and preservation of claims and defenses that a consumer may have against the merchant. Credit cards also offer other benefits such as product warranties and airline miles. Approximately half of all cardholders pay their balances in full every month and, therefore, enjoy interest-free loans.

Although fees, and card issuer revenues from fees, have increased in recent years, because of vigorous competition among credit card issuers and the use of individualized pricing models, consumers are enjoying lower interest rates and more access to credit than in the past. For example, according to a recent Government Accountability Office ("GAO") report on credit card disclosure practices ("GAO Report"), the average credit card interest rate 15 years ago was approximately 20 percent and credit cards often had annual fees in excess of $20. Today, according to the same GAO Report, the average interest rate is approximately 12 percent and nearly 75 percent of credit cards have no annual fees (report available at http://www.gao.gov/new.items/d06929.pdf). In addition, although there has been much concern about levels of credit card debt, the GAO found that credit card debt is a small portion of overall consumer debt and has actually declined as a portion of overall consumer debt.

Despite the benefits that credit cards offer, in recent years, credit card practices, such as so called "universal default" and "double-cycle billing," have been criticized as unfair to consumers in large part because these practices are inconsistent with consumers' expectations for their credit card accounts. These criticisms call into question whether the current credit card disclosure regime has kept up with the market.

Regulation of Credit Card Practices

Credit cards are subject to extensive statutory and regulatory disclosure requirements and, to a lesser extent, limitations on terms of credit card accounts under the Truth in Lending Act ("TILA") and Regulation Z adopted by the Board of Governors of the Federal Reserve System ("FRB") to implement TILA. TILA was adopted in 1968 to promote the informed use of consumer credit, comparison shopping and to promote economic stabilization through competition among financial institutions. TILA established comprehensive, cradle-to-grave disclosures and other requirements for credit cards. TILA and Regulation Z require credit card issuers to provide solicitation disclosures when marketing credit cards, initial disclosures when a new account is established, monthly statement disclosures during the life of an account and advance notice of the change in terms when terms are changed.

In addition, the federal bank regulatory agencies also have the power under the Federal Trade Commission Act, coupled with their enforcement authority under the

Federal Deposit Insurance Act, to address unfair and deceptive acts and practices by the federally supervised or insured banks that issue credit cards. This authority provides the bank regulators with the flexibility to address credit card issuer practices on a case-by-case basis. For example, in 2004, the Office of the Comptroller of the Currency ("OCC") issued guidance to alert national banks to the OCC's concerns regarding certain credit card practices that may entail unfair or deceptive acts or practices, including the practice of automatically repricing a cardholder's annual percentage rate or otherwise increasing a cardholder's cost of credit when the circumstances triggering the increase have not been fully or prominently disclosed. While noting that repricing accounts "may well be appropriate measures for managing credit risk on the part of a credit card issuer," the OCC urged national banks to fully and prominently disclose the circumstances under which accounts may be repriced and whether the bank reserved the right to do so unilaterally.

There is a general recognition that the current federal disclosures under Regulation Z have become far too detailed, far too complicated and focus on the wrong information for effective credit cost comparisons. In this regard, it is important to understand that the flexibility and features that support the benefits of credit cards also result in credit cards being inherently complex products that require the disclosure of information that is not required in simpler transactions, such as fixed-rate closed-end loans. At the same time, despite the changes in credit cards over the years, and although the FRB has the power to revise Regulation Z at its discretion, the FRB has not completed a comprehensive review of the credit card disclosure requirements required by

Regulation Z since 1982. Although the FRB began such a review in 2004, and is expected to propose regulations to modify the current disclosure framework soon, it is too early to tell how any proposed changes will affect credit card practices.

Potential Improvements

I believe that improved disclosures offer the potential to address current concerns about credit card billing practices. Although there could be credit card practices that are so unfair and, at the same time, so resistant to market pressures that they cannot be addressed through an improved disclosure regime, it is premature to conclude that improved disclosures cannot resolve these issues. New approaches to disclosures may be able to simplify disclosures for these transactions. For example, there appears to be broad recognition of the effectiveness of the Schumer-box disclosure format for credit card solicitations. The GAO Report notes that the Schumer-box disclosures have "helped to significantly increase consumer awareness of credit card costs." The Schumer box uses a tabular format box to help consumers compare key credit terms of competing credit offers and make informed decisions.

The approach used in the Schumer box is similar to the approach used in a proposal recently published by the federal banking agencies in response to concern about the length and complexity of the Gramm-Leach-Bliley Act ("GLBA") privacy notices. The federal banking agencies proposed a standardized model GLBA privacy form that would provide limited information in a uniform manner (similar to the Schumer box) to facilitate consumer understanding. Research underlying the proposed model privacy form indicated that "consumers are overwhelmed by too many words, complex information, and vague words and phrases." However, the model privacy notice goes beyond the Schumer box tabular format to simplify disclosures. The model privacy notice uses terminology that emphasizes simplicity as opposed to accuracy and precision, something that credit card issuers cannot do lest they face class action liability under TILA or litigation over the terms of the account agreements themselves.

Improved simplified disclosures could offer several potential benefits. First, a consumer would have an improved ability to compare the terms of credit card accounts and, therefore, to choose on account that minimizes potential problems for the way that he or she manages his or her account. Second, simplified disclosures could give the consumer a better understanding of how the credit card that he or she chooses functions so that rate changes and charges do not come as a surprise. Third, as Louis Brandeis said almost a century ago, "sunlight is said to be the best disinfectant; electric light is the best policeman." Simplified disclosures for credit card accounts can themselves lead to changes in creditor practices. In highly competitive markets, such as the market for retail credit cards, an increased transparency provided by simplified disclosures practices will limit credit card practices that take unfair advantage of consumers. Consumers will close existing accounts in favor of accounts with other creditors and concerns about brand risk will cause creditors to abandon such practices to avoid account closures. Over the last few months, we have already seen publicity surrounding credit card billing practices coincide with changes in those practices by credit card issuers.

Experience with the practice of universal default illustrates the potential for market pressures to regulate credit card practices. Universal default, the practice of increasing a consumer's credit card rate based on a failure to pay another creditor on time, has engendered criticism recently. Although in reality such a failure may be an indication that the consumer is encountering financial difficulties and, therefore, poses increased credit risk, it also may simply reflect a consumer with a busy schedule resulting in an occasional late or missed payment. The GAO Report, however, found that the largest credit card issuers have generally ceased practicing universal default. This change is likely due, at least in part, to the likelihood that if a consumer misses a single payment with another creditor and the card issuer increases the consumer's interest rate, the card issuer stands a good chance of losing the consumer's account to a competing credit card issuer that continues to see the consumer as a good credit risk through a balance transfer. When compared to the substantial cost of attracting and establishing a new credit card account, there is little economic incentive for a card issuer to then lose that account by repricing the account based on an isolated incident, such as a single missed payment. Other practices, such as two-cycle billing, which reflects the loss of a grace period where a consumer who has previously paid his or her account in full fails to do so, will either be accepted by consumers or abandoned by creditors once they are fully understood through improved and simplified disclosures.

Achieving these benefits through disclosures in the context of open-end credit, however, is not without challenges. First, as noted above, open-end credit accounts are inherently more complex than many other transactions and their terms will necessarily reflect this complexity. Second, disclosures cannot be consumers' only source of education about financial issues. That is, a higher level of financial literacy can enable disclosures to focus on key issues without the need to include detailed explanations or examples of the consequences. For example, the fact that the practice of making minimum payments will increase the overall cost of credit and the repayment period is probably more properly an issue of general consumer education rather than individual disclosures. Third, it seems clear that there is a tension between simple disclosures and legal liability for any failure of those disclosures to reflect the details of complex transactions. Thus, some sort of a safe harbor for simplified disclosures may be necessary.

Despite these challenges, TILA provides the FRB with broad authority to implement TILA. I believe that TILA, coupled with the banking agencies' other powers, provides ample authority for addressing these issues. We will have to await the FRB's proposed rules to see how the FRB will use its authority under TILA to address these issues.

Finally, although some may argue that disclosures are not a solution to concerns relating to credit card practices and that limitations on the terms of credit card accounts are necessary, such limitations would carry a significant risk of unintended consequences. Current credit card pricing is based on individual risk factors. Individual pricing allows a credit card issuer to offer credit cards with lower rates to lower-risk cardholders while still providing credit cards at higher rates to higher-risk consumers who otherwise might be unable to obtain credit even though they are fully capable of using it wisely. Limiting credit card practices is likely to result in more rigid pricing structures that overcharge customers at one end of the risk spectrum and curtail credit to customers at the other end of that spectrum.

I appreciate the opportunity to appear before you today, and I would be pleased to answer your questions.