Statement of Bill Caywood
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U.S. House Financial Services Committee
Subcommittee on Financial Institutions and Consumer Credit
Hearing: "Improving Credit Card Consumer Protection: Recent Industry & Regulatory Initiatives"
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Good morning, Chairwoman Maloney, Ranking Member Gillmor, and Members of the Subcommittee. My name is Bill Caywood, and I am the Consumer Operational Risk and Compliance Officer for Bank of America.

Bank of America is one of the world's largest financial services institutions. We provide a full range of financial services to individual consumers, small- and middle-market businesses, large corporations and government entities.

In the retail world, Bank of America serves more than 52 million consumer relationships — nearly half of all U.S. households. We operate more than 5,700 local banking centers and 17,000 ATMs, in 30 states and the District of Columbia. Our Web site, bankofamerica.com, is America's leading financial services Web site and the 14th busiest site overall, including Google, Amazon, Yahoo and eBay. Our site attracts 37% of total online banking customers and 65% of online bill payment customers where Bank of America credit card customers may pay their bill for free. We are also the second largest payment processing provider for small businesses.

Bank of America Credit Card Services is one of the largest issuers of credit cards in the world. We operate in the United States, Canada, Ireland, Spain and the U.K. Our primary business is to make unsecured loans through credit cards. We also process credit card transactions for small businesses and large corporations through our Merchant Services business.

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I am pleased to have the opportunity to participate in today's hearing on "Improving Credit Card Consumer Protection: Recent Industry and Regulatory Initiatives." I will focus my comments on recent initiatives to improve practices in the credit card sector. First, I will focus on the Federal Reserve Board's proposed revisions to Regulation Z. Next, I will highlight our own efforts to enhance consumer understanding of credit card terms. Third, I will comment on the importance of free competition in the credit card industry. Finally, I will respond to the Committee's questions with respect to subprime lending.

I'd like to note at the outset that Bank of America takes pride in its relationships with its customers. We continually update our practices to respond to changing consumer demand. And we believe that a well informed consumer is fundamental to a competitive market, and our ability to meet customer demand and create innovative products. We have taken numerous steps, which I will describe, to educate consumers about the terms of their credit products, thereby allowing them to obtain the best value and avoid potentially costly choices. But there is a limit to what we can do. We operate in a highly regulated industry. Regulation Z governs the common disclosures among all issuers. These disclosures are necessary to allow effective comparison shopping.

Regulation Z

Background

The Committee has asked us for our views on the Federal Reserve Board's proposal to substantially revise its Regulation Z, which implements the Truth in Lending Act. The Board's proposal was just released, and we expect to file a detailed comment letter before the comment period ends in October. Today, I will outline what we see as some of the major effects of the rule, but I will not attempt to provide comprehensive comments, and ask the Subcommittee to recognize that this analysis is preliminary. The proposed rule would require issuers to redesign: 1) applications and solicitations; 2) disclosures provided to consumers at account-opening and subsequently; 3) periodic billing statements; and 4) on-going advertising materials. This will mean significant reengineering of all related processes and computer systems. In order to provide comprehensive comments, we need to work through the practical effects of making such substantial changes, and that work will take time.

We believe that revisions to Regulation Z are appropriate. Over time, in response to consumer requests, credit cards have become more flexible, feature-laden products. Risk-based pricing now allows more consumers to qualify for credit by varying the price of credit based on individual customer behavior and circumstance. With the increase in flexibility and eligibility, the job of describing how the product works has become increasingly complex and has resulted in a need to update the applicable regulations. Certainly, card agreements were simpler when the product was offered only to wealthier customers who paid an annual fee and were required to repay the balance in full each month, but the current system has democratized access to credit and made the credit card a more useful instrument for more consumers than ever before.

We believe that consumers can readily understand the credit card terms that are of most importance to them. In essence, consumers need to understand: (1) what their standard interest rate will be if they decide to carry a balance on the account; (2) what conduct might cause them to pay a higher interest rate or incur fees, and what those rates or fees are; and (3) certain service fees (such as annual fees or foreign exchange fees) that they may be charged. We believe that the existing disclosures serve this purpose, and that customers use these disclosures effectively when they compare issuers and use their cards.

Overview

Our initial review suggests that the proposed revision to Regulation Z is an improvement on the existing regulation. It will provide customers meaningful disclosures in an even clearer format, and it will facilitate comparison shopping and better assist consumers in modifying their behavior, potentially reducing their cost of credit.

The Board and its staff obviously have devoted considerable thought to the proposal. The vast majority of the proposal explains how and why the Board arrived at the content of those disclosures. We appreciate the fact the Board has explained the research and thinking behind the proposal.

In its proposal, the Board has amended the required account-opening disclosures to provide a tabular summary. While implementing the new format will impose significant costs on Bank of America and other issuers, we believe that the new disclosures will provide consumers relevant information in a clear and more easily understood form.

The Board's proposal also requires a tabular disclosure on the periodic billing statements under specified circumstances. Furthermore, transactions, interest charges and fees will be grouped together in a new way that we think will be more easily understood by customers. Although the reformatting of the periodic statement will result in a significant redesign effort, we believe that the revised statement will quickly and more clearly provide customers relevant information about their accounts, and assist them to better understand the cause of any credit-related fees incurred during the previous cycle and help them to better avoid those fees in the future.

While our overall reaction to the proposal is favorable, the proposed changes to Regulation Z, if finalized, would not be easy to implement and would require issuers to incur considerable time and resources to rewrite the vast majority of communications we make with our customers and to change the ways these communications are delivered. It would also require substantial time to prepare and test, and it will be important for the Board to allow sufficient time for this to occur. Nevertheless, we support what the Board is doing and believe it will, over time, produce even better informed customers.

Although we generally support the changes to Regulation Z, we have identified one area where we believe the proposal can be improved.

45-Day Notice Prior to Default Repricing

Section §226.9(g) of the proposed rule requires an issuer to notify a customer 45 days prior to the effective date of any "Penalty Pricing" – that is, an increased rate of interest based on a customer's violation of the card agreement. The notice states that the goal of this provision is to provide prior notice before a changed term can be imposed and thereby "to better allow consumers to obtain alternative financing or change their account usage." We understand the goal behind the proposal but believe that, as drafted, it risks having the opposite effect.

As a matter of practice, Bank of America currently imposes default repricing only after *two* defaults in a twelve month period. (In our case, a default means going over the credit limit or paying late.) Some of our competitors use one-default repricing. Because the 45 day notice requirement delays the effect of an interest rate increase, we presume that the likely effect of the Board's proposal will be to push more issuers into repricing after a single default. The result will be more customers being repriced, and being repriced sooner, albeit after having received the Board-mandated notice.

This result is readily avoidable through a minor change to the proposal. The Board could allow issuers who reprice only after two (or more) defaults to notify the customer after the first default, as a warning that a future default will result in a higher interest rate. Such a notice should have a greater impact than the initial disclosures, because it would be less hypothetical – as the customer has engaged in conduct that he or she has agreed will trigger, if repeated, a higher rate.

Such a notice would also avoid punishing issuers who choose to give customers a second chance before imposing a higher rate. And, consistent with the purpose of the provision, consumers would be free after receiving this warning to seek alternative financing *or* to change their account usage – in our case, by not making a late payment or going over the credit limit again.

Summary

In summary, our preliminary analysis is that the Board has done a good job of revising Regulation Z. We will use the remaining months of the comment period to determine whether the proposal creates any other potential unintended consequences for consumers, as we believe the 45-day-notice provision could, or produces any unreasonable operational costs to the business. We look forward to providing our comprehensive feedback to the Board.

<u>Bank of America's Credit Card Practices</u>

Some specific credit card practices have been the focus of recent criticism. We believe it is important to reiterate Bank of America's position on these issues:

- Bank of America has never engaged in double-cycle billing.
- Bank of America has never engaged in universal default – that is, automatically repricing a customer, without further notice or consent, based only on the customer's default with another lender.
- Bank of America limits the frequency of risk-based re-pricing by amendment. In addition, when we determine that an account's risk has increased, and proposes a change in terms (an increased rate), the customer can reject the proposed change in terms and pay down their account over time under the existing terms.
- Bank of America limits the number of consecutive over limit fees; we have a hard stop at three.
- Bank of America increasingly allows customers to cure from default pricing to a lower rate if they have no late or over limit events for six consecutive months.
- Bank of America customers can pay their bills free in various ways, including: (1) through the mail, (2) at one of our 5,700 banking centers nationwide (3) by using the voice response unit (VRU) and paying with a Bank of America account or (4) online at bankofamerica.com. We charge a $15 fee for those customers who want to pay by phone through a customer service representative, or through VRU using a non-BAC account. Both methods require exception handling, and we charge a fee for that service.

I am proud to say that we arrived at these policies some time ago by listening to our customers and implementing practices designed to meet their financial needs and concerns.

<u>Bank of America's Customer Education</u>

In fact, it is from listening to our customers that we learned that they have a growing desire for improved information and more control over their finances. That is why we offer easy-to-use tools like Online Banking and Alerts to help our customers manage their accounts responsibly with the greatest flexibility and freedom:

- **Online Banking** allows customers to view information about their credit card and other accounts. Customers can track intraday activity, transfer funds and pay bills any time, anywhere they have Internet access.

- **Alerts** are messages sent to customers' computers, PDAs or mobile phones to inform or protect customers. They can warn the customer when he or she is approaching a credit limit or has an upcoming payment due date. They help combat identity theft. Customers choose the alerts they wish to receive. We have a dozen different alert triggers specific to credit cards. They are either automatic or can be set and/or adjusted by the customer. These free options include triggers like a warning of an account balance approaching a credit limit, an upcoming payment due date, a low balance threshold being reached, the availability of a deposit, etc., as well as a host of ID theft type alerts. The alerts can go by e-mail or text message or both.

We have gone beyond required disclosures to provide customers with brochures that are simple, straightforward and easy to understand. Our brochures like "Credit Cards & You" and "Our Account Fees Explained" describe *in plain language* how credit cards work and how to avoid fees.

- **"Credit Cards & You"** provides clear information about interest rates, grace periods, how cash advances work, how balance transfers are treated, how payments are allocated among outstanding balances, and the importance of paying on time and staying within your credit limit. We started inserting this brochure to new customers in June.

- **"Our Account Fees Explained"** provides clear descriptions of some common account-related charges that could be incurred and explains how they can easily be avoided. This brochure has been available for several years in our banking centers.

To increase awareness of these resources, Bank of America has launched online advertising under the theme, **"A Little Knowledge Is a Powerful Thing,"** to educate consumers about these and other tools to manage their accounts wisely.

In addition, Bank of America believes that financial literacy is best taught early. That is why we sponsor basic money management programs for high school and college students with our partner, Monster.com. For example, we are the only lender partnering with Monster's "Making It Count" division to offer "Ultimate Money Skills," a program that educates college students and their parents on financial products, how to establish a solid credit history and maintain identity theft protection. Between August 2006 and March 2007, we made nearly 240 "Ultimate Money Skills" presentations to more than 13,000 students on college campuses.

Why are we engaged in these financial education efforts for all of our customers? First, our research shows that customers who are empowered with this information are more satisfied. Second, our business does best when our customers manage their credit responsibly. One of the great myths we hear is that credit card companies prefer customers to default on their obligations, so that we can earn higher fees. That is simply not the case. Our average annual net credit losses on credit card loans for the last two years exceeded by a wide margin our revenue from late and over-limit fees.

While we are proud of these efforts and believe they will be useful to our customers, we note that those efforts are not a substitute for the modernization of Regulation Z. We believe that an improved Regulation Z is the best way to provide consumers the information they need, and that competition will benefit from fully informed consumers.

<u>The Importance of Competition</u>

As noted, we believe that the Board's proposal is an important step forward, and will improve a market that is already highly competitive. We believe that Congress should consider the results of the Board's regulation before taking the extraordinary step of legislating the price and terms of credit.

The credit card industry is intensively competitive, and has produced products that are extraordinarily popular with the millions of customers served by the industry. Prescriptive restrictions of price and terms risk undoing many of the benefits that competition has produced – flexibility in terms, a democratization of credit – by imperiling risk based-pricing and innovation. Such efforts are also notorious for triggering the law of unintended consequences: by regulating one price it forces another higher. Therefore, we respectfully suggest that Congress give the Board's significant effort and a competitive market the opportunity to work before taking more invasive steps.

<u>Subprime</u>

The Committee has asked us to review industry reforms in the subprime market, and to advise it on whether additional information gathering is necessary.

Bank of America's role in the subprime credit card market is very limited. We offer a secured card product for consumers who might not qualify for an unsecured loan. The customer must provide us with funds (either by writing a check or having funds transferred from a Bank of America deposit account) to create the security that we will hold, and the credit line is generally set at the amount of that security deposit. These accounts represent an extremely small part of our portfolio, but we offer them as a way of developing what we hope will be a lasting relationship with a new customer. While we have unique risk-control and pricing strategies that we apply to our secured cards, they generally operate in the same manner as unsecured cards. The goal of the program is to graduate the customer to an unsecured credit card product.

While we have chosen to limit our activity in the subprime credit card market, it is worth noting that Regulation Z applies to all credit card lenders, including subprime lenders. The banking regulators and the FTC also have authority to punish any unfair and deceptive trade practices, and have done so in the past.

<u>Conclusion</u>

Thank you for this opportunity to address the Subcommittee. I would be happy to respond to any questions the Members might have.