American Bankers Association
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March 7, 2012

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Re: Proposed prototype credit card contract

The American Bankers Association[1] (ABA) is pleased to submit our comments to the Bureau of Consumer Financial Protection's (Bureau) proposed prototype credit card agreement, released on December 7, 2011 and designed "to make it easier for consumers to understand their credit cards." The proposed prototype would include two printed pages of important terms, a one-page summary of those important terms as required under Regulation Z, and eight pages of definitions available on-line. In addition, other terms of the contract as well as informational explanations of undetermined length would have to be provided in print or made available on-line.

ABA appreciates and supports the Bureau's efforts and goal to ensure that people understand the important terms of their credit card agreement and its outreach to the industry in those efforts. We look forward to continuing that dialogue. However, the best way of facilitating this goal responsibly and effectively is not through the proposed model agreement which is in fact lengthy and seems both complicating and legally uncertain absent a federal safe harbor. Instead of developing government-designed contract provisions that raise legal questions and will discourage innovation and competition, the Bureau, if necessary, should build on or modify its existing one-page agreement summary of important terms already required under Regulation Z (Truth in Lending Act), which was based on comments from the public as well as consumer testing. In addition, to complement the improved agreement summary, the Bureau should create a generic "User's Manual" or Guide that instructs consumers generally on how credit cards work, as ABA recommended in its 2005 and 2007 comment letters to the Federal Reserve Board on proposed revisions to credit card disclosures.

Any new disclosures or documents should be based on analytically sound, meaningful data that can withstand scrutiny and peer review and consumer testing – not just public comment or nonrandom public voting. Such data and testing should focus on balancing three goals: that consumers (1) are likely to read the document, (2) understand what they read, and (3) find the information they receive meaningful and useful. Testing and analysis should also reflect the diversity of customers and how they use their account and the diversity of products in a highly competitive market. Finally, analysis and

[1] The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's $13 trillion banking industry and its two million employees. The majority of ABA's members are banks with less than $165 million in assets.

conclusions should reflect customers' responsibilities to make efforts to understand their credit card agreement and "be responsible for their financial decisions." [2]

Discussion.

The industry has worked cooperatively with the Bureau since its creation to identify means to ensure customers understand their credit card agreements. Issuers have met with Bureau staff individually as well as jointly with ABA and other issuers. ABA has also shared with the Bureau issuers' comparison of credit card agreements and explanations of why credit card contracts contain certain language and terms.

In response to the Bureau's concerns, many issuers have made great strides in improving customer understanding of their agreements. Many have simplified their contracts, using plain English and improved formatting, so that contracts are more readable, understandable, and user- friendly. Some have also designed their own, short, simplified notices to enhance the existing regulatory disclosure scheme.

We also note that the industry has a long history of supporting meaningful disclosures. ABA supported the Fair Credit and Charge Card Disclosures Act (1988) and the Federal Reserve Board's revised table of important terms for applications as well as its new one-page summary agreement that went into effect in July 2010. The purpose of those disclosures was to improve consumer understanding of the important terms of their credit card at application and throughout the life of the credit card contract.[3]

While the industry supports measures that will help to ensure their customers understand the terms of their agreement, efforts to simplify and shorten the legal embodiment of the agreement as proposed will not achieve the Bureau's goal of ensuring consumers understand the important terms of their credit card account or how it works:

- The proposed prototype contract is not in fact short. It is simply broken into several separate pieces found at different locations, raising questions about its readability and the likelihood it will be read.

- The legal and financial risks to any issuer adopting the proposed prototype contract present significant obstacles and safety and soundness concerns that must be addressed before the prototype could be adopted.

- The prototype does not comply with the Bureau's own Regulation Z requirements or with various state laws.

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[2] September 20′ 2012 speech by Bureau Deputy Direct Raj Date, http://www.consumerfinance.gov/speeches/page/4/ .

[3] See 74 Fed. Reg. 5244 *et seq.* for discussion of consumer testing and regulations that went into effect in July 2010.

Assuming the goal is to ensure consumer comprehension and value to consumers rather than prescribe the legal embodiment of the agreement, the Bureau should instead use its regulatory power under the Truth in Lending Act to require that all issuers provide uniform meaningful, effective disclosures about important terms. Specifically, if testing concludes that its current Regulation Z one-page agreement summary needs improvement, the Bureau should revise it based on qualitative, reliable testing of consumers' willingness to read and understand important credit card provisions. In doing so, the Bureau should not assume that this one-page summary box will be overlooked if additional information accompanies it, as testing has found that consumers gravitate to and use the current "box" that highlights important costs and terms.[4] In addition, the Bureau should consider complementing that issuer-specific account agreement summary with a general Bureau-designed Users' Manual that not only explains how credit cards work generally, but also provides tips and advice based on the diversity of customers and products. This approach achieves the Bureau's goal for a document that is "shorter, written in plain language, and explains the key prices and features upfront and separate from the legalese," [5] but avoids the legal uncertainty and risks associated with the proposed prototype agreement. It also offers greater usability and usefulness to consumers because all issuers must use a uniform format, and allows more flexibility and more robust competition than the proposed prototype.

The proposed prototype is not short, is of uncertain legal validity, and is not consumer-friendly.

True length of prototype contract. The proposed prototype in fact is not two-pages as advertised. It includes:

- Two printed pages;[6]
- The one-page summary of important terms (including repetition of some terms contained in the two printed pages) as required under Section 1026.6(b)(2) of Regulation Z;
- Eight pages of definitions and other terms available online; and
- Presumably and necessarily a "users' manual" or other document that provides other contract provisions and important information and explanations not included elsewhere.

Indeed, the press release states that the printed portion of the contract is 1100 words. However, when definitions alone are added, it increases by an additional 3,334 words, for a total of 4,434 words, just short of the 5,000 words the Bureau states is the average for a credit card agreement. Assuming there may be links to some of the terms in the printed portion, the document is even longer. In addition, important omissions, including contractual terms not contained in the prototype agreement, important non-contractual information, and information required to be disclosed under the Bureau's Regulation Z

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4 *Design and Testing of Effective Truth in Lending Disclosures,* Calverton, Md., Macro International Inc., May 16, 2007. (http://federalreserve.gov/newsevents/press/bcreg/bcreg20081218a7.pdf) p.9.

5 Consumer Financial Protection Bureau press release, December 7, 2011.

6 The "printed portion" of the contract will refer to the two pages of the proposed prototype contract that outline important provisions and are provided directly to the consumer with the card, thus presumably in printed form. However, they may be provided electronically.

will lengthen the contract when added, whether or not housed elsewhere (e.g., online or in a separate document).

Examples of terms and explanations that are not in the proposed prototype agreement include:

1. Numerous Regulation Z disclosure requirements (as discussed later), including fees not included in the printed portion of the contract that the Federal Reserve Board's consumer testing found consumers find important:[7] the credit limit and information related to billing and dispute rights and lost and stolen cards, which are referenced, but not included in the proposed printed portion of the contract;
2. Complete required federal privacy notice;
3. Explanation of the minimum payment formula. Under the heading "What do I have to pay and when?" the amount of space place holder for the minimum payment formula is unrealistic;
4. Arbitration agreement;
5. Information to contact consumer including consumer permissions;
6. Conversion of checks to electronic form;
7. Non-conforming definitions;
8. Informational explanations;
9. Explanations about joint cardholder liability;
10. Prohibition against using the card for Internet gambling;
11. Collection process;
12. Information related to reporting information to credit bureaus;
13. Monitoring calls for customer service;
14. Increases to rates related to servicemembers who no longer qualify for the Servicemember Civil Relief Act rate reduction or to failure to comply with a temporary hardship program; and
15. State law requirements for changes to terms.

That the proposed prototype agreement is so lengthy even without these missing provisions vividly illustrates the difficulty of designing a "short" contract that complies with legal requirements and ensures customers will have information they need or may need, either at the time they receive the card or at a later time.

Challenges of disjointed contract. Not only is the proposed prototype contract not short, the detachment from the printed portion of the contract of the related definitional sections, as proposed, may make it difficult for customers to understand or reference their credit card account terms. Under the proposal, definitions are available online or customers may request a printed copy of them. However, it is not clear whether it is anticipated that issuers would have the option of automatically providing in printed form definitions and other information not in the proposed printed part of the contract.

[7] *Op.cit.* Macro International Inc.. p.6.

While there are instances when online availability may appropriately replace routine distribution of paper, the prototype contract as proposed is not designed to encourage people to read it, because important related sections and terms (including related terms) are available at different locations. Such a piecemeal approach discourages customers from attempting to familiarize themselves with important aspects of the contract because of the excess effort in locating all the related parts. For example, some aspects of the contract important to consumers provided in the printed portion of the contract can only be understood when read in conjunction with certain definitions and other important terms found elsewhere. Customers need to have many of the definitions and other information handy when reviewing -- and also later referencing -- the printed portion of the contract. If customers have to look elsewhere for those important terms, they are less likely to look – and therefore understand.

Moreover, housing important portions of the contract online, separate from the related printed portion may be inconvenient to those without access or easy access to the Internet, many who will be low and moderate income. Some will not have access, others may have unpredictable, unreliable, or slow Internet connectivity, especially in rural areas. This means that they will not have the definitions at the time they are most likely to review the printed portion of the contract, i.e., when they receive the card or are checking terms at a later date. First, they have to request the missing section of the contract and then wait for it to arrive in the mail. When it arrives, they must locate and retrieve the printed portion of the contract. In effect, the moment is lost. Many are likely not to return to reviewing the agreement.

Further, it is not just a question of whether customers have "access" to the Internet. Some are not inclined to access the Internet when the printed portion arrives, the most likely time for reviewing the contract. Many people are not continually tethered to an electronic device, nor do they have available connection to the Internet at all times, nor find it convenient to connect, especially if the connection is slow.

In addition, by necessity, the Bureau's definition section has to clarify up front certain important information, e.g., that "we" has the meaning given by the issuer, that the Bureau is not a party to the contract, and that if the word or phrase is not underlined in the issuer's contract, it should not assume the definitions in the Bureau's document. These disclosures, which are necessary for the proposed prototype, are nevertheless confusing and distracting and add to the length of the contract. The additional length and confusion is avoided with credit card agreements not adopting the Bureau's definitions.

Enforceability of contract. The proposal relies heavily on the assumption and hope that all relevant courts and all states will recognize as part of the contract important terms that are not provided with the printed portion of the contract, but incorporated by reference and available elsewhere. This is a risky assumption, absent a federal safe harbor, that, even with the Bureau's support, all states will recognize the incorporation by reference concept in the context of financial products. One reason is that the printed portion of the contact must be read in conjunction with many of the definitions and other information to be provided online to ensure comprehension of key aspects of the printed portion. Indeed, courts have found that terms that **were actually disclosed with the contract *in toto*** were

unenforceable because they were not prominent enough e.g., were unfair or deceptive or not clear and conspicuous.[8] Thus, it is highly speculative that all courts will accept incorporation by reference for credit cards, which is critical for the proposal to be viable.

We understand that the Bureau wants to avoid "legalese" in the legal agreement, but under our legal system a certain amount of legalese is unavoidable, required. Simplification of contractual text has limitations, as the Bureau appreciates – we understand that it was only able to reduce the definitions section to an 11th grade reading level. However, if issuers do not comply with contract law, the contract or certain of its provisions is not enforceable. There is no escaping that reality.

Concerns about litigation risks and costs should not be dismissed as over-caution. Even if an issuer ultimately prevails in court, it incurs huge costs both financial (e.g., for legal defense) and reputational. If it loses, the financial loss is potentially astronomical, raising safety and soundness concerns.

Missing, confusing, or inaccurate information. Missing, confusing, or inaccurate information will have to be addressed by adding or correcting information to avoid legal uncertainty under contract law and customer confusion. For example:

- The proposed prototype provides generally, "You may use your card for purchases, cash advances, or balance transfers. Each type of charge will have its own balance. Each balance may have a separate interest rate." This suggests that there are only three types of balances. However, different interest rates might apply to promotional balances or transactions subject to a penalty rate, for example.

- The definition of balance transfer does not account for differences in issuer practices. For example, some issuers treat any balance transfer made via check after the offer date as a cash advance.

- Under the definition of due date, the proposal states that the due date will be "at least 25 days from the end of your most recently ended billing period." This does not take into account that issuers cannot provide a grace period of at least 25 days in February.

- The proposed definition of grace period will not capture some practices, for example, continuing to provide a grace period on purchases, so long as the payments cover the purchase balance, even if another balance such as transfer balance has not been paid in full.

- The proposed prototype agreement allows reasonable attorneys' fees and costs in collection cases. However, they may only be imposed if permitted by state law.

While a general disclosure required by regulation or a Bureau-designed general Users' Manual does not have to be so precise so as to reflect nuances that may not be critical to consumers such as some of

[8] *Gutierrez v. Wells Fargo Bank, N.A.,* 730 F. Supp. 2d 1080 (N.D. Cal 2010); *Barrer v. Chase Bank,* USA, 566 F.3d 833 (9th Cir. 2009; *Strand v. U.S. Bank*, 693 N.W.2d 918 (N.D. 2005))

those described above, the legal contract does. It is a necessary and unavoidable aspect of contract law, borne out in countless lawsuits. Accordingly, any document purporting to be the contract must address even minor inaccuracies and omissions.

Compliance with other state laws. Different states have different disclosure requirements that may or may not be consistent with the proposed contract. Issuers would have to alter or lengthen the contract accordingly.

Lack of compliance with Regulation Z. In addition to contract and other state laws, the proposed prototype agreement does not comply with the Bureau's Regulation Z. For example:

- Section 1026.5(b)(1) requires the account opening disclosures be provide before the first transaction is made under the plan, and Section 1026.5(a)(1) requires that they be "integrated." Under comment 4 to the latter section, "the creditor may make both the account-opening disclosures and the periodic-statement disclosures on more than one page, and use both the front and the reverse sides, . . . ***so long as the pages constitute an integrated document. An integrated document would not include disclosure pages provided to the consumer at different times or disclosures interspersed on the same page with promotional material."*** (Emphasis added.) Some of the provisions required to be disclosed are included in the proposed definitions to be provided online, which would not meet the requirement for an integrated disclosure document.

- The proposed prototype does not comply with the requirement of Section 1026.5(b) that certain disclosures be provided in the tabular format similar to the Regulation's models. The option is to provide, in addition to the proposed printed portion of the contract, a duplicative Regulation Z account summary table.

- Under "additional Information" the proposed prototype incorrectly states that if a cardholder defaults, the issuer cannot request payment in full of any "protected balances." This isn't technically accurate because if an account goes to collection, the statement may not apply.[9]

In addition, the proposed printed portion of the contract does not include, as Regulation Z requires:

- A description of the event that might trigger a penalty rate and how long it will be in effect (Section 1026.6(b)(2)(i)(D));

- Common fees such as annual fees, overlimit fees, minimum interest charges, returned check fees (Section 1026.6(b)(2));

[9] This illustrates the problem with the proposed prototype because for legal reasons, the contract has to be very specific, but required disclosures would have not have to be as precise or complete.

- The available credit (Section 1026.6(b)(2)(xiii));

- With the exception of late fees, the circumstances under which disclosed fees will be imposed (Section 1026.6(b)(3)). Instead, they are contained in the definitions;

- The Bureau's website reference where consumers may obtain information about shopping for and using credit cards (Section 1026.6(b)(2)(xiv)), though website for definitions is provided;

- Each periodic rate (expressed as a periodic rate) that may be used to calculate interest and the balance computation method (Section 1026.6(b)(4)(i));

- The "effects of an increase" for variable rate accounts, e.g., if a variable rate increases, a cardholder will pay more in interest and the minimum payment due may increase (Section 1026.6(b)(4)(ii)); and

- The explanation of billing rights (Section 1026.6(b)(5)).

Confusing format. The horizontal format of the "cost" section of the proposed prototype is confusing. The interest rate on purchases is linked by an arrow to the "interest rate after [period] on purchases." Presumably, this is the "go to" rate, but it is not easily grasped from the diagram. The first three "charges" in the left column are related to charges in the column to their right, suggesting that the same pattern would apply to the charges below them. However, the remainder of the charges in the left column is in fact unrelated to those to their right. Such formatting is not user-friendly as it slows the readers' understanding as suggested by the Federal Reserve Board's consumer testing of credit card disclosures.[10]

In brief. As illustrated, when one combines the text required by contract law, Regulation Z disclosures, and non-contractual information consumers need and want, the document cannot be a two or three-page document. For this reason, the Bureau should focus on improving, if necessary, the Regulation Z agreement summary and complementing it with a generic "User's Manual" that explains how credit cards work generally and provides tips and advice.

The summary agreement required under Regulation Z coupled with a Bureau's generic Users' Manual or Guide to credit cards is a superior approach to the proposed prototype contract. It achieves the Bureau's goal of ensuring customers understand what they need to understand about their credit card agreement, but avoids the legal issues and ensures uniform adoption, which facilitates consumer familiarity and comprehension.

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[10] *Op.cit.,* Macro International Inc..p.26. The study suggested better understanding when different APRs were disclosed in separate rows with two columns: "Subsequent interviews showed that disclosing these rates in separate rows helped participants distinguish between them. It also increased the likelihood that readers would notice and understand the significance of the Default APR. Therefore, this design was used in the proposed Schumer Box model (p. ii). "Findings from the Kansas City showed that listing APRs for balance transfers and cash advances in separate rows helped participants distinguish between rates for different transaction."

All issuers must provide the Regulation Z disclosures, including the agreement summary currently required. In contrast the proposed prototype is "voluntary" (though regulators may use supervisory pressure to "encourage" adoption as discussed below). In addition, while the Regulation Z summary agreement must be consistent with the contract, it avoids the legal issues of the proposed prototype, because it is a required disclosure reflecting the agreement, but not its legal embodiment, which must comply with separate and various vigorous state contract law requirements.

Moreover, the Federal Reserve Board's consumer testing found that consumers are aware of, like, and use Regulation Z's "box" or table.[11] As demonstrated by that test result, people will still gravitate to and read a well-formatted useful summary, even if it is accompanied by additional and even lengthy material.

To complement the issuer-specific account agreement, the Bureau could make available a generic Users' Manual or Guide. As the ABA had recommended to the Federal Reserve Board in response to its proposed credit card disclosure requirements, the Bureau should "develop a Credit Card Users' Manual or Credit Card Instruction Manual to assist consumers in understanding credit cards and credit card offers. Such a document would complement specific product disclosures to improve consumers' understanding of credit card practices generally to assist them in shopping and selections." [12] In addition, the Bureau could include in the manual tips and advice on how to select and use credit cards.

In effect, the proposal moves toward the concept of a standard government-designed agreement, contrary to Congressional intent.

The Bureau assumes and anticipates that issuers will generally adopt the government definitions and terms of the proposed prototype agreement. While issuers may vary from the Bureau's definitions, any variations from the Bureau's online definitions must be included in the printed section of the contract, which necessarily will lengthen that document. Because the goal is a shortened printed contract, any variations from the Bureau's definitions will be expected and encouraged to be minimal. In addition, supervisory pressure from the Bureau on the institutions it regulates to adopt the prototype and the potential legal challenge (whether or not legitimate) that failure to adopt the Bureau's prototype is unfair or deceptive will, as a practical matter, strongly promote adoption. Though issuers may still determine fees and some other terms, as a practical matter, they will have limited flexibility with critical definitions and terms. In effect, the Bureau is introducing the concept of a plain vanilla, government-designed product, which Congress specifically rejected when it created the Bureau. [13]

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11 *Ibid.*, p.9.

12 Letter from the ABA to the Federal Reserve Board, March 29, 2005, Docket No. 1217(page 2). Also see letter from the ABA to the Federal Reserve Board, October 12, 2007. Docket No. R-1286, (page 10).

13 The current Administration had originally included in its recommendations and drafts for the legislation that ultimately became the Dodd-Frank Wall Street Reform and Consumer Protection Act a provision giving the Bureau power to define standards for "plain vanilla" products that all providers and intermediaries would have had to provide. As described in its white paper, alternative products would have been "subject to more scrutiny, and violations with respect to alternative products" would have carried higher penalties. However, after public debate, Congress chose to exclude those provisions in the final bill that created the Bureau.

The result will be to inhibit competition and innovation. Credit card companies, like all businesses, must innovate and differentiate themselves to compete – and not only on the few terms the government selects, as demonstrated in the description and discussion of agreement variances from the Bureau's proposal. It simply isn't pro-consumer to limit issuers' ability to offer variations from the government's envisioned product. Moreover, as discussed, the goal of ensuring consumer understanding can be achieved without creating government-designed credit agreements.

When testing, the Bureau should define its goals and compare comparable documents.

The Bureau should determine its goal before testing the prototype and agreement summary or other alternative and measure:

1. Customer comprehension of features, functionality and consequences for intended use;

2. ***Value*** to customers of what is comprehended, taking into account when they are likely to need and use the information and that different customers may need and value different information and terms; and

3. Likelihood customers will read the material.

We advise that the Bureau be thoughtful and realistic about what information people need, want, and will read. The testing should recognize that it is not necessary or helpful for all customers to understand every word of the legal embodiment of their agreement. Nor is it necessary or helpful that they understand certain provisions at the time they choose or receive a credit card any more than it is necessary for a person purchasing a car, appliance, or software to understand every aspect of that product when selecting or using it.[14] Testing and conclusions should also reflect that credit card customers are very diverse, as are credit card products. Finally, the Bureau should assume and promote consumer role and responsibility for reviewing credit card materials and understanding the important terms of their credit card. As Bureau Deputy Director Raj Date noted in his September 20th speech, "Now, no one denies that borrowers have to be responsible for their financial decisions. In fact, that is a bedrock premise of the Bureau's approach to markets."

Assuming that the Bureau is planning to test the complete contract, it should include not only the printed portion and definitions of the proposed prototype, but other legally required information, including language required by contract and regulations as discussed earlier. Otherwise, the comparison will be of two very different documents and the outcome likely -- and misleading. If the Bureau plans to only test the printed portion of the proposed prototype agreement, then it should compare it with the current Regulation Z one-page summary of the agreement as they are both designed to focus the customer on important terms and do not reflect the entire agreement. Such testing might offer ways to

[14] This was approach taken when adopting the Regulation Z summary agreement: identifying most important terms to most people. Indeed, changes to Regulation Z recognized that the teachable moment for understanding some terms is not at account opening, but when the customer contracts for that particular service (e.g. expedited delivery of a credit card).

improve the Regulation Z agreement summary. Testing could also determine the preferred formats for providing the entire agreement that could be applied to the prototype agreement or any other credit card agreement.

The Bureau should consider the costs of duplicative efforts.

As discussed, in response to Bureau's concerns that credit card contracts were too complicated, many issuers went to considerable expense and effort to engage legal and language experts to revise their agreements with the goal of using plain English. We believe that as a result, credit card contracts are more easily understood. For those reasons, issuers may be hesitant to again revise their contracts so soon after such major revisions, especially if there is significant risk that the contract may not be enforceable in whole or in part. In addition, the Bureau should take into account before revising new disclosures or recommending new contracts that the disclosure requirements for credit cards (including those for applications, account opening, periodic statements, and change in terms) were only implemented in July 2010 at significant cost and after several years of study and consumer testing and multiple opportunities for the public to provide input. We believe that those changes have significantly improved consumer understanding of their credit card fees and terms. Given the recent significant actions that have increased customers' ability to understand their credit card terms and agreement and the volume of more pressing issues and initiatives demanding the Bureau's attention, spending valuable resources on a project to address issues already addressed raises questions about the Bureau's priorities and use of valuable resources.

Conclusion

ABA shares the Bureau's important goal to ensure that customers understand their credit card agreements and indeed, in response to the Bureau's concerns, many issuers have simplified their contracts as well as taken steps to facilitate communication with their customers so they better understand their account. However, we believe that the proposed credit card prototype is not the most effective way to achieve that goal. Rather than attempt to up-end long-established contract laws, we recommend that the Bureau instead pursue revisions of the existing agreement summary already required under Regulation Z coupled with a generic Users' Manual. Any new disclosures or document should be based on analytically sound, meaningful data and should not simply test whether consumers understand all aspects of the credit card agreement. The critical goal is to ensure they are likely to notice and read the terms that are important to them with regard to their card.

We look forward to continuing our dialogue with the Bureau and expect to provide further comments as the process continues. We are happy to provide additional information.

Regards,

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