

STATEMENT OF
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SUBCOMMITTEE ON
FINANCIAL INSTITUTIONS AND CONSUMER CREDIT
COMMITTEE ON FINANCIAL SERVICES
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Chair Maloney, Ranking Member Biggert, and members of the Subcommittee, I appreciate the opportunity to appear before you today to provide the Office of the Comptroller of the Currency's views on H.R. 5244, the "Credit Cardholders' Bill of Rights Act of 2008."

In testimony before this Subcommittee last year, Comptroller Dugan provided extensive information on the credit card industry and the OCC's concerns and responses regarding current credit card disclosures and marketing practices. He also urged certain key principles that should guide any new credit card legislation and regulation:

First, as a matter of safety and soundness, credit card lenders need to be able to manage their risks effectively.

Second, credit card customers should be given meaningful notice of the terms and conditions of their credit cards, and the circumstances under which those terms may change.

Third, credit card customers also should have meaningful choice when faced with certain increases in their credit card interest rates.

My written testimony focuses on these three principles and their application to H.R. 5244. I will briefly summarize some of the key points.

It is important to recognize the type of risk presented by credit card debt. A credit card is an unsecured, revolving, open-end credit, very different from a mortgage or car loan, and requiring different credit risk management techniques. As the customer pays down the balance of a credit card, the customer may make new charges, and the customer is not required to pay off the entire balance each month.

Thus, changes in a customer's creditworthiness affect the lender's credit risk in two ways: new extensions of credit for new transactions by the customer, and continued extension of credit for the customer's unpaid existing balance.

Because credit card lenders qualify customers for interest rate, credit limit, and other terms, based on an assessment of creditworthiness at the time the account is opened, lenders must rely on risk mitigation tools on an ongoing basis to address a customer's changing risk profile. These tools include freezing or reducing credit lines, closing accounts, and "re-pricing" – that is, changing the rate of interest charged for outstanding balances on an account.

From a supervisory perspective, we have concerns with certain provisions of H.R. 5244 that would deprive credit card lenders of some options that are important to effectively manage those risks. Specifically, the lender's ability to price for changing risks presented by an unpaid balance would be limited solely to circumstances where the customer has defaulted on the credit card account itself. So the lender could not use information highly relevant to its risk exposure – such as defaults on other credit or deterioration of a credit score – to adjust its pricing for the risk of a credit card balance that a customer has not repaid.

Comptroller Dugan has advocated an alternative approach, which we believe is consistent with safe and sound credit card lending practices and the principles of meaningful notice and meaningful choice. Under this alternative, if a creditor seeks to increase the interest rate on an account balance to address increased credit risk due to deterioration in a customer's credit score or default on an account with another creditor, it must first provide the customer with 1) a reasonable advance notice, and 2) an opportunity to opt-out of the changed terms and to pay down the outstanding card balance in accordance with the existing terms.

If the customer opted out of the rate increase, the lender could then mitigate its risk on that account by using other risk management tools, such as by reducing the credit line, or allowing the customer to wind down the account over a specified time.

An opt-out structured in this manner strikes a fair balance – preserving the lender's ability to monitor and respond to changes in a customer's creditworthiness, while recognizing that, from the customer's perspective, certain price adjustments should

be preceded by advance notice and an opportunity for the customer to make alternative credit arrangements.

In closing, let me note that the bulk of the bill's provisions do not raise fundamental safety and soundness concerns. They do, however, reflect real customer frustrations with the adequacy of credit card disclosures and with particular credit card practices. Yet, there may well be "trade-offs" between the potential benefits and consequences of some of these measures.

In this complex and competitive business, for example, if credit card lenders are restricted in their ability to price particular customer segments for the risks and costs they pose, the alternative may be to spread those costs over a broader range of credit card customers – raising costs for customers who do not pose higher levels of risk.

Provisions of the bill dealing with payment allocation and certain billing practices may present similar issues of unintended consequences if lenders react to mandated changes by making other changes that reduce card features that benefit customers.

Thank you, Chair Maloney, for the opportunity to testify on these issues. I will be happy to respond to any questions you might have.