



**Listening to the People
What Effect Will it Have on Congress and State
Government Action?**

by Jim Romeo

The saga of the financial services industry continues and it seems that there could not be a dirtier word than "banker" nowadays. The fever is spilling over into all corners of the financial services industry and it continues to fertilize the soil of Congress to muscle up on legislation that would put a much tighter grip on credit cards and many other financial instruments.

For the card industry there are many facets to new legislation making many within it nervous.

"Right now I am most concerned about some of the cardholder protection bills circulating in Congress," says Duncan Douglass, an attorney with the law firm of Alston and Bird in Atlanta, Georgia. "The bill with most traction in the House and Senate right now looks to be the Credit Cardholders' Bill of Rights, championed by Representative Maloney, who saw the bill to passage in the House late last year, and Senator Schumer. It is not the substance of the CCBR that is the most troubling, but rather the timing on which the legislation would become effective if enacted. The substance of the CCBR is, for the most part, already due to take effect in mid 2010 thanks to December 2008 rulemaking by federal banking regulators, but as currently drafted the CCBR would become effective 90 days after enactment. This compressed time schedule from enactment to effectiveness would afford card issuers very little time to revise their lending practices and processing systems to comply with the new requirements. The resulting reaction from issuers to such a short compliance fuse may prove detrimental to cardholders, contrary to the intent of the legislation, if issuers adjust pricing and practices assuming worst-possible-case scenarios because they have inadequate time to make informed decisions based on modeling of the likely effects of required changes."

"The provision of the new Federal Reserve Regulations that causes me most concern is the one that states that card issuers will be prohibited from raising interest rates during the first year of a new account," Ben Woolsey, Director of Marketing and Consumer Research for CreditCards.com, a leading online source for consumer credit card information. "While this is a very consumer-friendly provision, it may have the unintended consequence of artificially increasing interest rates for everyone and reducing access to new credit."

Outside of the Federal Government are the states that are doing their best to inject many measures in the hope of protecting their constituents against any abuse by vendors within the card industry.

"Legislation at the state level is what makes me most nervous," says Henry Helgeson, president and co-CEO of Merchant Warehouse. His firm has offices in all 50 states and if legislation and policies differ from state to state, it will make it extremely hard to conduct business logistically. At the federal level, any legislation would be the same across the board making it easier to adapt to new rules and regulations.

Part of the debate over how much oversight is too much, or how much oversight is effective, begs the question: can heightened federal watchdogs over the card industry improve the overall security for everyone in the industry? Some think that the state disclosure laws might be more effective.

"I don't believe that the current directions that federal regulators are taking will have much security impact," says Gene Hoffman, CEO and founder of Vindicia, an on-demand payment management provider for on-line merchants. "I see most of the current direction to be much more about issuers' interactions with consumers. I think instead that state disclosure laws are going to have a larger impact on security practices as they really heighten the reputation risk for all participants. A few painful disclosures forced by one of the state laws will [provides] incentive [for] more merchants, issuers, acquirers and ISOs to take internal security more seriously."

Semantics are important in this debate. "Legislating" may be displaced by a focus on "regulating" according to Duncan Douglass. "I do believe there is a role for federal oversight or involvement in promoting the protection of cardholder information, but I believe most of that oversight should be guided by regulation rather than legislation," he says.

"I emphasize a regulatory rather than a legislative role because I believe that legislation is too blunt an instrument and too slow moving to be responsive to the ever-changing threats to data security," adds Douglass. "That being said, I still believe that industry self-regulation, operating within broader regulatory and even broader still legislative mandates, is the most appropriate first line of oversight because the industry is best positioned to react quickly to new security threats."

Andrew Rueff, Senior Vice President of Corporate Development for TransFirst concurs. "I do not believe this [federal watchdog approach] will have a positive impact, says Rueff. "I believe it is up to our industry to solve these problems as it has done in the past, and that if we do not, market forces will force us to."

Looking forward, the outlook one takes of the industry in the next few years seems to change by the month.

According to Duncan Douglass, issuers have accepted and begun responding to the final rules promulgated by federal banking regulators in December of 2008, providing building blocks for a more tightly regulated consumer card-lending environment are solidly in place. "As we move into 2010 and 2011, I would not be surprised to see the FTC and FDIC continue to focus on bank-issued and non-bank issued prepaid card programs, both in terms of consumer protection, largely the domain of the FTC with respect to non-bank issued cards, and with respect to safety and soundness concerns, largely the domain of the FDIC with respect to bank issued cards, particularly where the issuing bank is seen as exercising too little control and oversight over the actual operation of the program."

However, by 2010, it is likely we will have new card rules as the FTC and FDIC will be watching card issuers heavily. One thing that they cannot ignore is data breaches.

"Any industry which stores sensitive data could be a target of techno-crimes. Even federal and state government entities have experienced breaches," says Rueff of TransFirst. "For this reason, and because I do not believe banking or commerce oversight agencies are best equipped to address cutting edge technology crimes, a separate agency might be developed in the long term to provide

oversight of technology related business that are storing and keeping sensitive data. I believe we may see a separate set of rules which would apply to these kinds of companies with oversight by an agency which is well equipped to handle cutting edge technology crimes."

Nevertheless, many in our industry are ever hopeful that the industry can successfully organize and self-regulate to rid risk and take self-imposed measures. "We are the ones who know what the problems are and the potential solutions for them," says Henry Helgeson. "Federal intervention may end up making things far more complex and expensive for ISOs. I think it is important for the solutions to come from the people who are involved in the day-to-day aspects of the industry."

Another change in the industry is likely to be consolidation and mergers, narrowing the playing field and bringing card fees and interest rates backward in time.

"The credit card landscape will probably include fewer large players due to mergers, acquisitions, liquidations and current issuers exiting the credit card business," says Ben Woolsey. "The credit card business model may become radically altered due to restrictions on the application or risk-based pricing and penalty fees, the two main drivers of profits for the industry. In reaction to regulatory changes we could even see a return to the pricing structures of the 70's and early 80's, when 18% APR and \$20 annual fees were standard credit card product features. If this were to occur, consumer demand could shift toward other types of electronic payments such as standard debit and prepaid debit."

Henry Helgeson differs a bit from Woolsey's view and feels that it will not consolidate greatly, though there may be fewer ISOs. "In 2011 the industry will be much more consolidated. There will be fewer ISOs in 2011 than there are today," he says. "With that being said, as poor as the current economic situation is, there are still positive business developments happening and it looks like the payments industry is about to introduce some revolutionary products in the near future."

"Beyond the new laws and regulations being placed on the banking and finance industries, there is a movement growing that focuses on average citizens," says Doug Muir, chief executive officer and founder of Credit Justice Services, the fourth-largest credit verification and repair company in the United States. "Consumers are waking up to the injustices caused by the banking and finance industries and they are also footing the bill for mistakes on Wall Street. Finally, Congress is listening to the people." ■