DISCOVER
FINANCIAL SERVICES

Via Electronic Mail: baselcommittee@bis.org

April 16, 2010

Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002
Basel, Switzerland

Re: Consultative Document: *Strengthening the Resilience of the Banking Sector*

Ladies and Gentlemen:

Discover Financial Services ("Discover") is a leading credit card issuer in the United States and an electronic payment services company. It is the parent company of Discover Bank, an FDIC insured state-chartered bank and issuer of the Discover Card. As of February 28, 2010, Discover had $45.8 billion in credit card receivables.

Discover appreciates the opportunity to submit this letter in response to the request for comment by the Basel Committee on Banking Supervision (the "Committee") on the Consultative Document, *Strengthening the Resilience of the Banking Sector*. Discover supports the goals of the Committee to improve the banking sector's ability to absorb shocks arising from financial and economic stress, however we are concerned with potential impacts of certain aspects of the Consultative Document. Discover is a member of the American Bankers Association ("ABA") and the Financial Services Roundtable, both of which have submitted separate comment letters on the Consultative Document. Many of the comments contained in the ABA and Financial Services Roundtable's comment letters touch directly on areas of concern to Discover, and we would like to express our support for the comments and suggestions in both of those comment letters.

This comment letter focuses on matters raised in the Consultative Document that are of particular importance to Discover. In particular, the inclusion of off-balance sheet items in the exposure measure of the leverage ratio. We believe that this particular proposal could have a significant negative impact on the pricing and availability of credit for creditworthy consumers and businesses without a corresponding reduction in risk to financial institutions. This, in turn, would therefore reduce the ability of banks to serve as an engine of economic recovery from the current stressed economic environment.

The Committee has stated that one of the underlying features of the recent financial crisis was the build up of excessive on- and off-balance sheet leverage in the banking system and that in many cases banks built up excessive leverage while still showing strong risk based capital ratios. The Committee is therefore proposing a leverage ratio designed to put a floor under the build-up of leverage in the banking sector to help mitigate the risk of destabilizing deleveraging processes which can damage the financial system; and introduce additional safeguards against model risk and measurement error by supplementing the risk based measure with a simple, non-risk based measure based on gross exposure. The Committee has proposed that off-balance sheet items be included in the exposure measure of the leverage ratio using a flat 100 percent credit conversion factor.

Discover does not believe the solution to the Committee's concerns is to include all off-balance sheet exposures in the leverage ratio at a 100 percent conversion factor. This approach would not reflect appropriately the risks of many of these exposures, based either on the risk profile of the exposure or the presence of risk mitigation, or both, that reduce a financial institution's risk. The proposal ignores that the financial and economic risk in off-balance sheet assets in many cases are not equivalent to the risks in on-balance sheet assets. For example, a commitment that is fully cancellable by the bank is far less risky than a committed line of credit or an on-balance sheet loan. The Committee should carefully consider the wisdom of sweeping all of these off-balance sheet exposures into the leverage ratio without consideration of the economic risks that they in fact present. We believe that off-balance sheet exposures with historically low risk profiles, such as commitments that the bank has the unilateral right to cancel, should be exempt from the calculation of any leverage ratio.

As noted above, Discover is a leading credit card issuer. As of February 28, 2010, Discover had unused commitments to extend credit for consumer and commercial loans of approximately $170 billion. Such commitments arise primarily from unused lines of credit on credit cards. Discover may terminate substantially all of these commitments at any time pursuant to the agreement we have with our customers. These unused commitments are periodically reviewed based on account usage and customer creditworthiness and are reduced where appropriate.

The Consultative Document would include 100% of the amount of these unused credit lines in the calculation of the leverage ratio even though there are substantial mitigating controls in place with respect to these unused lines of credit. First, periodic reviews of unused lines are conducted at the individual account level based on account usage and customer creditworthiness, which can result in credit line reductions or closures where appropriate. Second, we have sophisticated real-time credit usage reporting and monitoring at the individual customer level, which can inform us of unusual behavior. This includes an authorization system that makes decisions at the individual point-of-sale level. Consequently, if we see unusual behavior, we have the ability to take immediate action to reduce or close a line so as to mitigate risk. Third, we have robust reporting of sales volume and payment behavior at an aggregate level to identify any unusual trends in the use of unused credit lines.

Banks are currently required to hold capital against credit card loan receivables, including, after recent U.S. accounting changes, receivables in securitization trusts. In addition, banks are required to maintain appropriate loan loss reserves to absorb estimated probable losses in the

loan portfolio. Adding yet an additional buffer through the proposal to include cancellable, unused consumer lines of credit in the leverage ratio is unnecessary and inconsistent with the risk posed by these cancellable credit lines. As such, the proposal would do little to mitigate the concerns of the Committee and would only serve to reduce available credit to consumers and businesses and slow the economic recovery. For these reasons, we strongly encourage the Committee to reconsider its position with regard to the inclusion of cancellable, unused lines of credit in the leverage ratio.

Discover very much appreciates your consideration of our comments to the proposals contained in the Consultative Document. Should you have any questions concerning our views and recommendations, please do not hesitate to contact me at 224.405.1076.

Sincerely,

Roy A. Guthrie
Executive Vice President and
Chief Financial Officer

cc: BaselComments-April2010@frb.gov