American Express Company
200 Vesey Street
New York, NY 10285

March 27, 2015

Via Electronic Delivery

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

Re: Credit Risk – Revisions to the Standardised Approach

Ladies and Gentlemen:

American Express Company ("American Express") appreciates the opportunity to provide comments to the Basel Committee on Banking Supervision (the "BCBS") on its consultative document (the "Consultation") that proposes revisions to existing approaches to the calculation of credit risk capital requirements for banking organizations.[1] American Express believes that the Consultation inappropriately increases the credit conversion factor ("CCF") for certain types of off-balance sheet exposures specific to banks which engage in the issuing of credit cards, resulting in increased capital requirements that are not commensurate with the risks posed by such exposures. As described in further detail in this letter, American Express urges the BCBS not to increase the CCF for unconditionally cancellable commitments or, alternatively, to treat credit card lending as a separate category of unconditionally cancellable commitment, subject to the currently applicable CCF.[2]

I. Background

Under the standardised approach, off-balance sheet exposures are assigned a CCF and the notional amount of such off-balance sheet exposure is multiplied by the applicable CCF to generate a credit-equivalent amount. This amount is then assigned a

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1 BCBS, Consultative Document: Revisions to the Standardised Approach for credit risk (Dec. 2014), *available at* http://www.bis.org/bcbs/publ/d307.pdf.

2 These comments are also supported by the comments submitted to the BCBS by The Clearing House and The American Bankers Association in response to the Consultation, as they pertain to the application of CCFs to credit cards.

corresponding risk weight. The Consultation proposes to raise the CCF for off-balance sheet exposures that a bank may cancel unconditionally and at any time, without prior notice ("Unconditionally Cancellable Commitments" or "UCCs") to 10%. This would result in a significant capital charge for banks with various UCC exposures, including unused credit card lines of credit.

The Consultation explains that "[i]ncreasing overall capital requirements under the standardised approach for credit risk is not an objective of the [BCBS]; rather, capital requirements should be commensurate with underlying risk." American Express believes that the proposed 10% CCF and resulting capital charge for unused lines of credit is disproportionate to the underlying risk posed by credit card lending, unsupported by historical data and, therefore, inappropriate. In this letter, we focus our comments on (i) demonstrating, through historical data and experience, that credit cards have a different risk profile than other financial instruments, particularly during a financial crisis, (ii) the willingness and ability of credit card issuers to promptly and prudently cancel or reduce credit card lines, (iii) the potential negative impacts to consumers and small businesses that may result from application of the proposed 10% CCF to credit card lines, (iv) the need for international harmonization in the implementation of the Consultation, (v) the need for additional data collection and (vi) the need to consider the overall impact resulting from the Consultation together with other recent proposed changes to the standardised approach. American Express recommends that the proposed 10% CCF not be adopted. As an alternative proposal, American Express recommends that undrawn credit card lines be excluded from the category of UCCs subject to the proposed 10% CCF and continue to be subject to the currently applicable CCF. American Express considers exposures related to credit card lending to be sufficiently different from other types of UCCs[3] to merit separate consideration and treatment.

II. Overview of American Express

American Express is a global services company whose principal products and services include credit payment card products and services for consumers and businesses around the world. While certain types of credit lines are designed to provide a borrower with access to cash, credit cards are not designed to provide access to cash or liquidity; instead, they are used primarily to make purchases. Credit card borrowers must either pay their bill in full each month or pay a minimum amount due and carry a monthly balance on their cards to finance the purchase of goods or services. Credit card customers may generally borrow up to a specified limit established and communicated to the customer by American Express. At any given moment, the overwhelming majority of

[3] Other types of UCCs include home equity lines of credit ("HELOCs"), a type of loan where a lender provides a line of revolving credit to a borrower who in turn pledges his or her home as collateral.

American Express' credit card customers have not fully drawn on the credit lines available to them on their credit card account (generally utilizing less than 20% of available credit). American Express maintains robust risk management capabilities that enable it to, in real-time, prudently reduce or cancel credit lines, as appropriate. American Express may, consistent with applicable laws, reduce or cancel unused portions of credit lines extended to credit card customers. As a result, such credit lines can be classified as UCCs.

III. Draw-Down Rates for Credit Cards and Other Commitments

The Consultation proposes to apply a 10% CCF to UCCs, which include commitments that are "unconditionally cancellable at any time without prior notice, or that effectively provide automatic cancellation due to deterioration in [a] borrower's creditworthiness." Question 18 of the Consultation asks whether "respondents agree that instruments allocated to each of the CCF categories share a similar probability of being drawn and that the probabilities implied by the CCFs are accurate?" The proposal fails to distinguish between the inherently distinct characteristics and risk profiles of credit lines that a borrower draws on in times of stress and credit card lines of credit. Therefore, American Express does not agree that all instruments allocated to the UCC category share a similar probability of being drawn, particularly during times of financial market stress. American Express believes that the proposed CCF increase should not be adopted or, in the alternative, credit card lines should be excluded from the existing UCC category and continue to be subject to the currently applicable CCF, which is appropriate based on the risk profile of credit card lending.

As credit card accounts generally utilize less than 20% of available lines, the inclusion of 10% of unused credit capacity is unsupported by historical data and would imply an 8% increase[4] in utilization. This would bring the utilization of the entire portfolio to approximately 28%, which exceeds industry experience even in the recent financial crisis. An increase from 20% to 28% also implies a 40% increase in balances across the entire portfolio and such an increase would be inconsistent with both issuer and customer behavior during the recent financial crisis.

Economic and industry data demonstrates that in recent periods of financial stress, consumers and small business borrowers have attempted to reduce spending and reserve available cash. Unlike other forms of credit, credit cards are not designed to provide liquidity and instead are primarily used to make purchases. To the extent customers reduce their overall purchasing, credit card usage also generally decreases. According to

[4] 10% x (total credit line at 100% - 20% utilized)

the U.S. Financial Crisis Inquiry Commission,[5] "during the financial crisis consumer spending in the United States fell at an annual rate of 3.5% in the second half of 2008."[6] As consumer spending as a whole decreased during the financial crisis, credit card balances also fell. The Federal Reserve Bank of New York Quarterly Report on Household Debt and Credit ("FRBNY Debt Report") shows that there were $2.7 trillion of unused credit card lines[7] in the fourth quarter of 2008, the beginning of the crisis period. Instead of increasing, as the Consultation would suggest, the FRBNY Debt Report indicates that balances actually declined through the crisis. In fact, credit card balances decreased by approximately 8% from the fourth quarter of 2008 to the fourth quarter of 2009.[8] Furthermore, a report published by the Consumer Financial Protection Bureau ("CFPB")[9,10] suggests that overall credit card utilization rates in the U.S. were actually *lower* during the recent crisis than in the years that followed, as conditions improved.

Historical data also shows that credit card activity differs from other types of credit products designed to provide liquidity. The FRBNY Debt Report shows that while credit card balances decreased during the recent financial crisis, HELOC balances increased and in fact were at the highest point in the last 10 years during the first quarter of 2009.[11] Over the same crisis period during which credit card balances decreased, as

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5 The U.S. Financial Crisis Inquiry Commission was established as part of the Fraud Enforcement and Recovery Act of 2009 and composed of a 10-member panel of private citizens with experience in areas such as housing, economics, finance, market regulation, banking, and consumer protection.

6 Financial Crisis Inquiry Report. Financial Crisis Inquiry Commission (Feb. 2011) p 393-394, *available at* http://www.gpo.gov/fdsys/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf.

7 The FRBNY Debt Report indicates that, also in the fourth quarter of 2008, such accounts maintained a utilization rate of only 25%.

8 Quarterly Report on Household Debt and Credit, Federal Reserve Bank of New York (November 2014) p 7, *available at http://www.newyorkfed.org/householdcredit/2014-q3/data/pdf/HHDC_2014Q3.pdf.*

9 Some of this increase is seasonal as credit usage customarily increases during the holiday season.

10 CARD Act Report, Consumer Financial Protection Bureau (Oct. 1, 2013) p 53, *available at http://files.consumerfinance.gov/f/201309_cfpb_card-act-report.pdf* explaining that "[f]rom Q2 2008 to Q4 2012, total unused line[s] fell by 35.0% yet at the end of 2012 consumers with accounts represented in [the bureau's database] still enjoyed $1.9 trillion in available credit on their credit cards. This implies that 20.5% of the extended credit line has actually been utilized by consumers, up from 17.4% in Q2 2008." According to the CFPB Report, the database contains information on the full consumer and small business credit card portfolios, representing between 85% and 90% of credit card industry balances.

11 FRBNY Debt Report at 7.

described above, HELOC balances actually increased, by 1%. This data suggests that consumers utilized HELOCs for liquidity in a time of economic crisis. Conversely, as consumers reduced purchases during the financial crisis, credit card usage decreased. Since credit card spending does not generally increase during period of market stress, borrowers are unlikely to draw further on their available credit. As a result, the assumption of an increased probability that credit card UCCs would be drawn on during a period of market stress is unsupported by historical data.

While a higher CCF may be appropriate for certain types of UCCs, such as HELOCs, whose utilization increases during periods of financial stress, it is inappropriate for credit card exposures whose balances actually *decreases* during market stress. Therefore, it is unnecessary to increase the CCF for UCCs that are related to credit card lending to 10% because the underlying inherent risk in this type of exposure remains consistent with the existing CCF.

IV. Ability to Cancel Credit Card Commitments

The Consultation explains that the BCBS believes the existing CCF for UCCs is inappropriate, and proposes a new 10% CCF because "consumer protection laws, risk management capabilities and reputational risk considerations may constrain banks' ability to cancel such commitments." American Express believes that such considerations would not restrict banks' ability to cancel credit card lines and, therefore, the proposed 10% CCF would be inappropriate for such exposures.

A. Risk management capabilities

American Express maintains robust risk management capabilities including real-time risk assessment of every transaction. When risks rise, American Express may take responsible lending actions and immediately reduce lines or restrict spending on riskier borrowers. Credit risk management policies and economic logic support key decision points throughout the customer life cycle, including line management and account closure. During the recent financial crisis, American Express took actions to appropriately manage risk; notably, American Express decreased credit lines and cancelled accounts resulting in a reduction of unused lines by approximately 12% between 2007 and 2009.

Other credit card issuers reported lowering credit card limits during the financial crisis, as well. The Board of Governors of the Federal Reserve System's Senior Loan Officer Opinion Surveys on Bank Lending Practices during 2008 and 2009 ("FRB

Surveys") consistently show that banks lowered limits for credit card accounts.[12] The 2013 CFPB report indicated that, during the financial crisis "in an attempt to protect against further deterioration in credit performance, credit card issuers sought to reduce their exposure by closing accounts, decreasing unused credit lines, and tightening the criteria for granting new credit or for increasing lines on existing accounts."[13] Other types of UCCs (such as HELOCs), however, may not maintain the same real-time, automated risk management capabilities as credit card issuers. This, in turn, may suggest that treating credit card exposure differently from other UCCs is appropriate.

Finally, the FRBNY Debt Report shows aggregate credit card limits in the United States decreasing quarter-over-quarter from a peak in the third quarter of 2008 to the first quarter of 2011.[14] The credit card lending industry reduced aggregate credit card limits by over $1 trillion during this period of time.[15] The speed and scope of these reductions demonstrate the capability of credit card issuers to identify risks and take appropriate action to mitigate them. Of note, aggregate credit card limits in the U.S. have only moderately increased from their low in 2011, demonstrating a continued commitment to prudent risk management by credit card lenders, including American Express.

B. Consumer protection laws

Applicable U.S. law does not prohibit a credit card issuer from reducing or canceling a customer's credit line without prior notice. In the event that a creditor takes an adverse action on an existing account, such as reducing or, in some cases canceling a credit line, the Equal Credit Opportunity Act and implementing regulation (commonly referred to as "Regulation B"), requires that the creditor send written notice of the action to the applicant within 30 days after taking such action. However, applicable consumer

[12] *See e.g.* Board of Governors of the Federal Reserve System, The October 2008 Senior Loan Officer Opinion Survey on Bank Lending Practices, Table 1, Question 21, *available at*: http://www.federalreserve.gov/BoardDocs/snloansurvey/200811/table1.htm and Board of Governors of the Federal Reserve System, The January 2009 Senior Loan Officer Opinion Survey on Bank Lending Practices, Table 1, Question 21, *available at*: http://www.federalreserve.gov/BoardDocs/snloansurvey/200902/table1.htm.

[13] CARD Act Report at 16.

[14] FRBNY Debt Report at 7.

[15] *Id.*

law does not prohibit prudently managing risk through reducing or canceling open credit card lines.[16]

Following the 2008 financial crisis, new law governing consumer credit was enacted in the United States.[17] This law and implementing regulation set forth various requirements for credit card issuers, such as limits on fees and interest charges, along with certain disclosure requirements. Importantly, these post-crisis consumer law developments did not negatively impact credit card issuers' ability to manage its risk through appropriate line reduction and cancellation.

The application of consumer protection laws, at least in the United States, to credit cards are different from other products that may also be classified as UCCs, such as HELOCs. In the United States, Regulation Z generally prohibits lenders from changing the terms of a HELOC, subject to several exceptions.[18] In order to reduce the available credit to a HELOC borrower, a lender must undertake a number of required steps, some of which must be completed *prior* to the reduction of the available credit line.[19]

Different requirements under consumer protection laws for credit cards and other types of UCCs, may further suggest the need to treat credit card exposure differently from other UCCs. In the United States, applicable consumer protection laws would not impair a credit card issuer's ability to prudently reduce or cancel open credit card lines, consistent with American Express' actions during the recent financial crisis. Therefore, applicable consumer protection laws do not provide an appropriate rationale for increasing the CCF applicable to credit card exposures.

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[16] According to the Consumer Financial Protection Bureau's Ask CFPB Website, "[c]ard issuers generally can increase or decrease credit limits without giving you notice, including reducing your credit limit so that you no longer have any available credit." *Available at* http://www.consumerfinance.gov/askcfpb/74/i-just-discovered-that-the-card-issuer-has-reduced-my-credit-limit-and-i-no-longer-can-charge-anything-can-they-do-that.html.

[17] *See e.g.* Credit Card Accountability, Responsibility and Disclosure Act of 2009, Pub. Law 111-24, May 22, 2009.

[18] FDIC Financial Institution Letter FIL-58-2008 (June 26, 2008), p 2, *available at https://www.fdic.gov/news/news/financial/2008/fil08058.pdf*. Also *see* 12 C.F.R. § 226.5b(f)(3).

[19] *See* "Regulation Z," § 12 C.F.R. 226, *available at http://www.ecfr.gov/cgi-bin/text-idx?tpl=/ecfrbrowse/Title12/12cfr226_main_02.tpl*.

C. Reputational risk considerations

The Consultation posits that reputational risk considerations may constrain an issuer's ability to cancel credit cards lines. American Express, however, believes that such risks did not impede its ability to prudently manage risk and cancel lines during the recent financial crisis, nor did such actions result in significant impairment to its reputation. In fact, throughout the crisis and in each year since, American Express has ranked #1 in credit card customer satisfaction by J.D. Power and Associates.[20]

Furthermore, any such reputational risk is mitigated when significant portions of an industry take similar actions, under similar circumstances. As the FRB Surveys, CFPB report, and FRBNY Debt Report indicate, many other credit card issuers reduced credit card lines during the 2008 financial crisis.[21] Appropriately reducing available credit card lines is a legally permissible and responsible lending practice common to credit card issuers. Therefore, reputational risk to an individual card issuer may not serve as an impediment to appropriately reducing or cancelling credit card lines.

V. Impact to Consumers and Economy

A stated principle of the Consultation is that "[c]apital charges from the standardised approach should reflect to a reasonable extent the risk of the exposures and provide the correct incentives for banks, considering the overall policy objectives..."[22] The proposed 10% CCF for UCCs would result in an increased capital charge to credit card issuing banks and American Express believes this is disproportionate to the actual level of risk posed by exposure to these UCCs, as set forth above.

Given this disproportionate impact on credit card issuing banks, increasing the CCF for UCCs to 10% would create incentives for such banks to take actions that may be harmful to consumers and small business, as well as the overall economy. In order to mitigate the impact of the resulting capital charge, credit card issuing banks would be incented to reduce credit card lines, even in periods of financial growth. This reduction of an available credit would remove an important source of funding for purchases to consumers and small businesses. With diminished purchasing power, consumers and small businesses would likely reduce spending or turn to more expensive sources of funding which, in both cases, would negatively impact several economic metrics and

[20] See, e.g. http://businesscenter.jdpower.com/news/pressrelease.aspx?ID=2008141.

[21] *See e.g.* FRB Surveys and FRBNY Debt Report at 7.

[22] Consultation at 5.

potentially slow economic growth. Moreover, consumers seeking additional sources of credit may turn to less-regulated non-bank providers resulting in higher costs.

VI. Local Implementation

The standarised approach described in the Consultation is intended to ensure that a simple methodology remains available for a wide range of jurisdictions and non-internationally active banks, where the cost of compliance with more complex standards may not be warranted. The Consultation also "recognizes that, in order to allay level-playing-field concerns, equal risks should attract the same amount of capital requirements and national discretions, where not necessary, should be removed."[23] However, U.S. regulators have already indicated that the proposal would likely be applied only to large, internationally active banking organizations and not to community banks.[24] This intent to not to apply broadly in the U.S. would inject variation in implementation approaches at the national level, and may put firms subject to the proposed requirements at a competitive disadvantage. American Express urges the BCBS as well as national regulators to ensure that the application of the proposals in the Consultation apply to similar institutions across jurisdictions.

VII. Data Collection

In order to ensure that capital requirements reflect the inherent riskiness of underlying exposures, the BCBS intends to review the overall impact resulting from the combined revisions to the standardised approaches (including operational, market and counterparty credit risk) prior to finalizing the proposals set forth in the Consultation.[25] American Express supports the BCBS' efforts to conduct a qualitative impact study and thoroughly review potential impact of the proposal on banks with various business models. Specifically, we suggest that the BCBS study the impact of this Consultation on banks conducting credit card lending issuing businesses, as well as operating a credit card payment network, in order to evaluate whether the impact to capital requirements is appropriate given the underlying level of risk of these activities. We also encourage the BCBS to analyze the distinction between credit cards and other off-balance sheet exposures categorized as UCCs, as we believe that credit card exposure is sufficiently

[23] Consultation at 7.

[24] Banking Agencies' Statement Regarding The Basel Committee's Consultative Paper "Revisions to the Standardized Approach for Credit Risk" *available at* http://www.federalreserve.gov/newsevents/press/bcreg/20141222a.htm.

[25] Consultation at 1.

different from other UCCs as to warrant different treatment under the standardised approach.

VIII. Cumulative Impact with Other Recent BCBS Proposals

American Express urges the BCBS to consider the impact of the Consultation in combination with other recently proposed revisions to the standardised approach.[26] American Express has concerns that the cumulative impact to regulatory capital charges for banks with significant credit card lending portfolios would be unfairly punitive and incongruent with underlying risk. Although American Express' comments in this letter focus exclusively on the Consultation, we strongly urge the BCBS to consider the cumulative impact of all proposed changes in any QIS exercise and in the finalization of this Consultation, as well as others.

IX. Conclusion

American Express believes that the Consultation's proposed CCF for unused credit card lines would result in a disproportionate capital charge to credit card issuing banks. The BCBS should distinguish between the risk profiles of credit lines that a borrower draws on in times of stress, such as HELOCs, and credit card lines. Although both may be categorized as UCCs, they feature different risk profiles, consumer protection requirements, and historical usage by customers. It is important to recognize the ability of credit card issuers to prudently cancel or reduce credit card lines, thus obviating the need for the proposed increase in CCF applicable to credit card exposures. The BCBS should also consider the potential negative impacts to consumers, small businesses and overall economy that may result from application of the proposed 10% CCF, and the resulting capital charge, to undrawn credit card lines. Competitive impacts should be limited by ensuring harmonized and consistent implementation of the proposal by national regulators. Ultimately, the BCBS should refrain from finalizing the proposal until additional data has been collected and an impact study has been completed. American Express urges the BCBS to reconsider increasing CCF for UCCs to 10%. Alternatively, the BCBS should acknowledge the material differences between credit card exposure and other UCCs and continue to apply the currently applicable CCF to open credit card lines of credit.

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[26] American Express submitted comments to the BCBS regarding its consultative document "Operational risk – Revisions to the simpler approaches." The letter is available at: http://www.bis.org/publ/bcbs291/americanexpress.pdf.

Thank you for considering our comment letter. We appreciate the opportunity to share our views with the BCBS. If we may be of further assistance, please contact Richard Petrino at Richard.Petrino@aexp.com and +1-212-640-5516.

Sincerely,

Jeffrey Campbell Executive Vice President & Chief Financial Officer	Ashwini Gupta Chief Risk Officer & President, Risk Information & Management

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