Discover Financial Services
Form 424B3
March 24, 2008
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Filed pursuant to Rule 424(b)(3)
Registration No. 333-147651

PROSPECTUS

Offer to Exchange

$400,000,000 6.450% Senior Notes due 2017

and

$400,000,000 Floating Rate Senior Notes due 2010

For

$400,000,000 6.450% Senior Notes due 2017

and

$400,000,000 Floating Rate Senior Notes due 2010

Which Have Been Registered Under the Securities Act of 1933

Material Terms to the Exchange Offer and Exchange Notes

We are offering to exchange the notes we sold previously in private offerings (referred to as the old notes) for new registered exchange notes (referred to as the exchange notes).

You may withdraw tenders of old notes at any time prior to the expiration of this exchange offer.

This exchange offer expires at 5:00 p.m., New York City time, on April 28, 2008, unless we extend the offer.

The terms of the exchange notes to be issued in this exchange offer are substantially identical to the old notes, except for the transfer restrictions, and registration rights and the obligation to pay additional interest under specified circumstances.

No public market currently exists for the old notes. We do not intend to list the exchange notes on any securities exchange and, therefore, no active public market is anticipated.

The exchange notes, like the old notes, will be unsecured and will rank equally in right of payment with all of our other existing unsecured senior indebtedness. The exchange notes will effectively rank junior to all indebtedness and other liabilities of our subsidiaries.

Each broker-dealer that receives exchange notes for its own account pursuant to this exchange offer in exchange for old notes that were acquired as a result of market making or other trading activities must acknowledge that it will deliver a prospectus in connection with any resale of the exchange notes.

If the broker-dealer acquired the old notes as a result of market making or other trading activities, such broker-dealer may use this prospectus for the exchange offer, as supplemented or amended, in connection with its resales of the exchange notes.

You should carefully consider the risk factors beginning on page 8 of this prospectus before participating in this exchange offer.

Neither the U.S. Securities and Exchange Commission nor any other federal or state agency has approved or disapproved of the securities to be distributed in the exchange offer, nor have any of these organizations determined that this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is March 24, 2008.

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You should rely only on the information contained in this prospectus or to which we have referred you. We have not authorized any person to provide you with different information or to make any representation not contained in this prospectus.

In this prospectus, the terms Discover, we, us and our refer to Discover Financial Services, a Delaware corporation, and its subsidiaries, taken a a whole and, for the period prior to June 30, 2007, to our predecessor, the Discover segment of Morgan Stanley. The term Morgan Stanley refers to Morgan Stanley, a Delaware corporation, and its subsidiaries, excluding Discover, unless the context indicates otherwise. References to years refer to fiscal years ending November 30 of each year, unless the context indicates otherwise.

We completed our spin-off from Morgan Stanley, our former parent company, on June 30, 2007.

You should not assume that the information contained in this prospectus is accurate as of any date other than the date set forth on the cover. Changes to the information contained in this prospectus may occur after that date, and we undertake no obligation to update the information. You should be aware of certain risks relating to our business and ownership of the exchange notes, which are described under the heading Risk Factors.

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Trademarks, Service Marks and Trade Names

We own or have rights to use the trademarks, trade names and service marks that we use in conjunction with the operation of our business, including, but not limited to: Discover, PULSE, Cashback Bonus, ShopDiscover, Discover Motiva Card, Miles by Discover Card, Discover Open Road Card, Discover Network and Goldfish. All other trademarks, trade names and service marks included in this prospectus are the property of their respective owners.

Industry Data

This prospectus includes industry and trade association data, forecasts and information that we have prepared based, in part, upon data, forecasts and information obtained from independent trade associations, industry publications and surveys and other independent sources available to us. Some data also are based on our good faith estimates, which are derived from management s knowledge of the industry and from independent sources. These third-party publications and surveys generally state that the information included therein is believed to have been obtained from sources believed to be reliable, but that the publications and surveys can give no assurance as to the accuracy or completeness of such information. We have not independently verified any of the data from third-party sources nor have we ascertained the underlying economic assumptions on which such data are based. Similarly, we believe our internal research is reliable, even though such research has not been verified by any independent sources.

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SUMMARY

The following summary contains certain information from this prospectus relating to us and the securities offered in the exchange offer. It does not contain all the details concerning us or the exchange notes, including information that may be important to you. To understand our business and financial position and this exchange offer, you should carefully review this entire prospectus.

Our Company

We are a leading credit card issuer and electronic payment services company with one of the most recognized brands in U.S. financial services. Since our inception in 1986, we have grown to become one of the largest card issuers in the United States with $48.2 billion in managed receivables as of November 30, 2007. We are also a leader in payments processing, as we are one of only two credit card issuers with its own U.S. payments network and the only issuer whose wholly-owned network operations include both credit and debit functionality. In 2007, we processed 3.8 billion transactions through our signature card network (the Discover Network) and PULSE EFT Association (the PULSE Network or PULSE), one of the nation s leading ATM/debit networks.

We issue credit cards in the United States under the Discover Card brand to various segments within the consumer and small business sectors. Most of our cards offer a Cashback Bonus rewards program. In addition, we offer a range of banking products to our customers, including personal loans, student loans, certificates of deposit and money market accounts.

Discover Network cards currently are accepted at millions of merchant and cash access locations primarily in the United States, Mexico, Canada and the Caribbean. In October 2004, the U.S. Department of Justice (DOJ) prevailed in its antitrust lawsuit (the DOJ litigation) against Visa U.S.A., Inc. (together with its predecessors, Visa) and MasterCard Worldwide (together with its predecessors, MasterCard) which challenged their exclusionary rules rules that effectively precluded us from offering network services to financial institutions. Since then, we have accelerated our network growth by entering the debit market with the acquisition of the PULSE Network, and by signing card issuing agreements with a number of financial institutions. We also have significantly expanded our relationships with companies that provide merchants with credit card processing services, which we believe will further increase the number of merchants accepting Discover Network cards.

In addition, we issue credit cards on the MasterCard and Visa networks in the United Kingdom, the world s second-largest credit card market. Our portfolio includes Goldfish, one of the United Kingdom s leading rewards credit cards, as well as several Morgan Stanley-branded credit cards and a number of affinity credit cards. As of November 30, 2007, we had $4.4 billion of managed receivables in the United Kingdom. On February 7, 2008, we entered into an agreement to sell our credit card business in the United Kingdom to Barclay s Bank Plc. The closing is expected to occur by the end of our second quarter of 2008 and is subject to the satisfaction of a number of conditions. See Management s Discussion and Analysis of Financial Condition and Results of Operations Recent Developments Sale of the International Card Segment for more information relating to the sale of our Goldfish business.

Our revenues (net interest income plus other income) have increased over the last three years, from $4.3 billion in 2005 to $5.1 billion in 2007, and net income was $589 million (which included a non-cash impairment charge of $279 million after tax related to our credit card business in the United Kingdom, also referred to as the Goldfish business), $1.1 billion, and $578 million for the years ended November 30, 2007, 2006 and 2005, respectively. For a discussion of more recently released financial information, please see Management s Discussion and Analysis of Financial Condition and Results of Operations Recent Developments.

On June 30, 2007, we were spun-off from our former parent company, Morgan Stanley, through the distribution of our shares to its shareholders (the Distribution or the Spin-Off). We became a subsidiary of Morgan Stanley in May 1997 as a result of the combination of Dean Witter, Discover & Co. and Morgan Stanley Group, Inc. The entity currently named Discover Financial Services was a subsidiary of Sears, Roebuck and Co.

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(Sears) from 1960 until 1993, when it was part of the spin-off of Dean Witter Financial Services Group Inc. from Sears. The Discover Card business was launched in 1986.

We were incorporated in Delaware in 1960. Our principal executive offices are located at 2500 Lake Cook Road, Riverwoods, Illinois 60015. Our main telephone number is (224) 405-0900.

The Exchange Offer

In connection with the issuance of $400,000,000 aggregate principal amount of our 6.450% Senior Notes due 2017 and $400,000,000 aggregate principal amount of our Floating Rate Senior Notes due 2010 (collectively, the old notes), we entered into a registration rights agreement with the initial purchasers of the old notes. Under that agreement, we agreed to deliver to you this prospectus and to use our reasonable best efforts to complete this exchange offer within 360 days after the date of original issuance of the old notes. You are entitled to exchange in this exchange offer each applicable series of old notes for a like principal amount of our 6.450% Senior Notes due 2017 or Floating Rate Senior Notes due 2010, as applicable (collectively, the exchange notes), which are substantially identical to the old notes except that:

- the exchange notes have been registered under the Securities Act of 1933, as amended, referred to as the Securities Act, and will be freely tradable by persons who are not affiliated with us;

- the exchange notes are not entitled to registration rights which are applicable to the old notes under the registration rights agreement; and

- our obligation to pay additional interest on the old notes as described under The Exchange Offer Purpose and Effect of This Exchange Offer does not apply to the exchange notes.

The Exchange Offer	We are offering to exchange up to the entire aggregate principal amount of each series of the exchange notes in exchange for a like aggregate principal amount of the corresponding series of the old notes. We are commencing two separate exchange offers, one with respect to each series of old notes. We refer to these exchange offers, collectively, as the exchange offer in this prospectus. Old notes may be exchanged only in denominations of $2,000 and integral multiples of $1,000 in excess thereof. For a description of the procedures for tendering the old notes, see The Exchange Offer Procedures for Tendering Old Notes.
Resales	Based on existing interpretations of the Securities Act by the SEC staff set forth in several no-action letters to third parties, and subject to the immediately following sentence, we believe that exchange notes issued under this exchange offer in exchange for old notes may be offered for resale, resold and otherwise transferred by the holders thereof (other than holders who are broker-dealers) without further compliance with the registration and prospectus delivery provisions of the Securities Act. However, any purchaser of old notes who is an affiliate of ours or who intends to participate in the exchange offer for the purpose of distributing the exchange notes, or any broker-dealer who purchased the old notes from us for resale pursuant to Rule 144A or any other available exemption under the Securities Act, (i) will not be able to rely on the interpretations of the SEC staff set forth in the above-mentioned no-action letters, (ii) will not be entitled to tender its old notes in the exchange offer, and (iii) must comply with the

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registration and prospectus delivery requirements of the Securities Act in connection with any sale or transfer of the old notes unless such sale or transfer is made pursuant to an exemption from such requirements.

Expiration Date; Withdrawal of Tenders

This exchange offer will expire at 5:00 p.m., New York City time, April 28, 2008, or such later date and time to which we extend it. We do not currently intend to extend the expiration date. A tender of old notes pursuant to this exchange offer may be withdrawn at any time prior to the expiration date. Any old notes not accepted for exchange for any reason will be returned without expense to the tendering holder promptly after the expiration or termination of this exchange offer.

Conditions to this Exchange Offer

This exchange offer is subject to customary conditions, some of which we may waive. See The Exchange Offer Certain Conditions to This Exchange Offer.

Procedures for Tendering Old Notes

If you wish to accept this exchange offer, you must complete, sign and date the accompanying letter of transmittal, or a copy of it, according to the instructions contained in this prospectus and the letter of transmittal. You must mail or otherwise deliver the letter of transmittal, or the copy, together with the old notes and any other required documents, to the exchange agent at the address set forth on the cover of the letter of transmittal. If you hold old notes through The Depository Trust Company (DTC) and wish to participate in this exchange offer, you may use DTC s Automated Tender Offer Program to tender, by which you will agree to be bound by the letter of transmittal.

By signing or agreeing to be bound by the letter of transmittal, you will represent to us that, among other things:

- you are not an affiliate of ours or if you are such an affiliate, you will comply with the registration and prospectus delivery requirements of the Securities Act to the extent applicable;

- you are acquiring the exchange notes in the ordinary course of your business;

- at the time of the exchange offer, you have no arrangement with any person to participate in the distribution (within the meaning of the Securities Act) of the old notes or the exchange notes; and

- if you are a broker-dealer that will receive exchange notes for its own account in exchange for old notes that were acquired as a result of market making or other trading activities, you will deliver a prospectus (or to the extent permitted by law, make available a prospectus to purchasers) in connection with any resale of such exchange notes.

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	See The Exchange Offer Procedures for Tendering Old Notes.
Guaranteed Delivery Procedures	If you wish to tender your old notes and your old notes are not immediately available or you cannot deliver your old notes, the letter of transmittal or any other documents required by the letter of transmittal or to comply with the applicable procedures under DTC s Automated Tender Offer Program prior to the expiration date, you may tender your old notes according to the guaranteed delivery procedures set forth in this prospectus under The Exchange Offer Guaranteed Delivery Procedures.
Effect on Holders of Old Notes	As a result of this exchange offer, and upon our acceptance for exchange of all old notes validly tendered pursuant to this exchange offer, we will have fulfilled a covenant contained in the registration rights agreement applicable to the old notes. Accordingly, we will not be obligated to pay damages as described in the registration rights agreement. If you are a holder of old notes and do not tender your old notes in this exchange offer, you will continue to hold such old notes and you will be entitled to all the rights and limitations applicable to the old notes in the indenture related to the applicable series of old notes, except for any rights under the registration rights agreement that by their terms terminate upon the consummation of this exchange offer.
Consequences of Failure to Exchange	All old notes that are not tendered or that are tendered but not accepted will continue to be subject to the restrictions on transfer provided for in the old notes and in the indenture related to that series of notes. In general, the old notes may not be offered or sold unless registered under the Securities Act, except pursuant to an exemption from, or in a transaction not subject to, the Securities Act and applicable state securities laws. Other than in connection with this exchange offer, or as otherwise required under certain limited circumstances pursuant to the terms of the registration rights agreement, we do not currently anticipate that we will register the old notes under the Securities Act. See The Exchange Offer Consequence of Failure to Exchange.
Summary of Certain United States Federal Income Tax Considerations	The exchange of old notes for exchange notes will not be a taxable event to you for U.S. federal income tax purposes. As a result, (1) you will not recognize taxable gain or loss as a result of exchanging your old notes for exchange notes, (2) the holding period of the exchange notes will include the holding period of the old notes exchanged therefor, and (3) the adjusted issue price and the adjusted tax basis of the exchange notes will be the same as the adjusted issue price and adjusted tax basis of the old notes exchanged therefor immediately before the exchange. See Material U.S. Federal Income Tax Considerations.

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Use of Proceeds	We will not receive any cash proceeds from the issuance of the exchange notes in this exchange offer.
Exchange Agent	U.S. Bank National Association is the exchange agent for this exchange offer. The address, telephone number and facsimile number of the exchange agent are set forth under The Exchange Offer Exchange Agent.
Other	Participation in this exchange offer is voluntary, and you should carefully consider whether to accept. You are urged to consult your financial and tax advisors in making your own decision on what action to take.

The Exchange Notes

The following summary of the terms of the exchange notes is not intended to be complete. For a more complete description of the terms of the exchange notes, see Description of the Exchange Notes.

Issuer	Discover Financial Services
Notes Offered	$400,000,000 aggregate principal amount of Floating Rate Senior Notes due 2010 (the Floating Rate Notes). The Floating Rate Notes will mature on June 11, 2010 (the Floating Rate Note Stated Maturity).
	$400,000,000 aggregate principal amount of 6.450% Senior Notes due 2017 (the Fixed Rate Notes). The Fixed Rate Notes will mature on June 12, 2017 (the Fixed Rate Note Stated Maturity).
Interest	The Floating Rate Notes will bear interest at LIBOR plus 0.53% per annum.
	The Fixed Rate Notes will bear interest at 6.450% per annum.
Interest Payment Dates	Interest on the Floating Rate Notes will be payable in arrears on June 12, September 12, December 12 and March 12 of each year.
	Interest on the Fixed Rate Notes will be payable in arrears on June 12 and December 12 of each year.
Ranking	The Floating Rate Notes and the Fixed Rate Notes (together, the exchange notes) will be unsecured and will rank equally with other unsecured senior indebtedness that we have or that we may incur. The exchange notes will be effectively junior to our secured indebtedness and all of our subsidiaries existing and future obligations. See Description of the Exchange Notes Ranking.

As of November 30, 2007, at the parent holding company level, Discover Financial Services had $799 million of long-term indebtedness and no secured indebtedness. As of November 30, 2007, excluding intercompany amounts, our subsidiaries had $30.9 billion of total indebtedness and other liabilities, including deposits.

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Optional Redemption	We may redeem the Fixed Rate Notes, in whole or in part, at our option at any time at a make-whole redemption price, plus accrued and unpaid interest. The make-whole redemption price is described in Description of the Exchange Notes Optional Redemption By Us.
Tax Redemption	We may redeem the Floating Rate Notes and/or the Fixed Rate Notes as a whole, but not in part, at our option at any time prior to maturity, upon the giving of a notice of tax redemption to the holders, if any, upon the occurrence of specified events relating to applicable tax law. See Description of the Exchange Notes Tax Redemption.
Additional Amounts	We will, subject to certain exceptions and limitations, pay to a holder of any exchange note, as additional interest, such additional amounts as may be necessary in order that every net payment by us or a paying agent of the principal of and interest on the exchange note and any other amounts payable on the exchange note after withholding or deduction for or on account of any present or future tax, assessment or governmental charge imposed or levied by the United States or any political subdivision or taxing authority thereof or therein will not be less than the amount provided for in the exchange note to be then due and payable under the note. See Description of the Exchange Notes Payment of Additional Amounts.
Covenants	Subject to a number of important limitations and exceptions, the indenture governing the exchange notes will contain covenants that will limit our ability to, among other things (i) create, assume, incur or guarantee any indebtedness for borrowed money that is secured by a pledge, lien or other encumbrance on certain voting securities of certain subsidiaries or (ii) merge or consolidate with any other person or sell, lease or convey all or substantially all of our assets to any other person. Other than as described below under Change of Control Offer, there are no covenants or other provisions in the indenture that would afford holders of exchange notes additional protection in the event of a recapitalization transaction, a change of control of our company or a highly leveraged transaction. See Description of the Exchange Notes Covenants Restricting Pledges, Mergers and Other Significant Corporate Actions.
Change of Control Offer	If a Change of Control Triggering Event (as defined in Description of the Exchange Notes Repurchase at the Option of Holders) occurs, holders of the exchange notes may require us to make an offer to repurchase the exchange notes at a price equal to 101% of their principal amount, plus accrued and unpaid interest, if any, on the repurchase date, as described under the heading Description of the Exchange Notes Repurchase at the Option of Holders.
Events of Default	The exchange notes and the indenture will contain certain events of default, consisting of, among others, the following:
	failure to pay the principal when due or failure to pay interest in respect of the exchange notes within 30 days of the due date for an interest payment;

- failure to comply with our covenants, with such failure continuing for 60 days after written notice has been delivered to us;

- default under any mortgage, indenture or other instrument securing or evidencing any of our indebtedness or that of our principal subsidiaries in an aggregate principal amount of $50 million or more and which default (i) constitutes a failure to make any scheduled principal or interest payment when due after giving effect to any applicable grace period or (ii) accelerates the payment of such debt and such acceleration is not rescinded or annulled, or such debt is not discharged, within 15 days after written notice to us of such default by (i) the trustee or (ii) the holders of at least 25% in principal amount of the outstanding exchange notes of such series; and

- events of bankruptcy, insolvency or reorganization.

See Description of the Exchange Notes Events of Default .

Further Issuances	We may from time to time without notice to or consent of the holders of the exchange notes issue an unlimited amount of additional notes of the same series as the exchange notes. Holders of the notes should be aware that additional notes that are treated as the same series as the exchange notes may be treated as separate issues for U.S. federal income tax purposes. See Description of the Exchange Notes The Notes.
Listing	We do not intend to list the exchange notes on any exchange or to include the exchange notes in any automated quotation system.
Governing Law	The indenture and the exchange notes will be governed by the laws of the State of New York.
Trustee, Transfer Agent and Registrar	U.S. Bank National Association.
Risk Factors	Investing in the exchange notes involves substantial risks. See Risk Factors for a discussion of the factors that you should consider.

RISK FACTORS

You should carefully consider each of the following risks and all of the other information contained in this prospectus before participating in the exchange offer. Some of these risks relate principally to our business and the industry in which we operate, while others relate principally to our spin-off from Morgan Stanley, and other risks relate principally to the exchange offer and the exchange notes.

Our business, financial position, results of operations or liquidity could be adversely affected by any of these risks, and, as a result, our ability to comply with our obligations with respect to the exchange notes could be materially and adversely affected.

Risks Related to Our Business

We face competition from other credit card issuers, and we may not be able to compete effectively, which could result in fewer customers and lower account balances and could materially adversely affect our financial condition, cash flows and results of operations.

The credit card issuing business is highly competitive, and we compete with other credit card issuers on the basis of a number of factors, including: merchant acceptance, products and services, incentives and reward programs, brand, network, reputation and pricing. This competition, among other things, affects our ability to obtain applicants for our credit cards, encourage cardmembers to use our credit cards, maximize the revenue generated by card usage and generate cardmember loyalty and satisfaction so as to minimize the number of cardmembers switching to other credit card brands. Competition is also increasingly based on the value provided to the cardholder by rewards programs. Many credit card issuers have instituted rewards programs that are similar to ours, and issuers may in the future institute rewards programs that are more attractive to cardmembers than our programs. In addition, because most domestically issued credit cards, other than those issued by American Express, are issued on the Visa and MasterCard networks, most other card issuers benefit from the dominant position and marketing and pricing power of Visa and MasterCard. If we are unable to compete successfully, or if competing successfully requires us to take aggressive actions in response to competitors actions, our financial condition, cash flows and results of operations could be materially adversely affected.

We incur considerable expenses in competing with other credit card issuers, and many of our competitors have greater scale, which may place us at a competitive disadvantage.

We incur considerable expenses in competing with other credit card issuers to attract and retain cardmembers and increase card usage. A substantial portion of these expenses relates to marketing expenditures; however, traditional customer acquisition methods have become increasingly challenging. Telemarketing has been hampered by the Federal Trade Commission s National Do Not Call Registry, which had increased to almost 152 million phone numbers as of January 2008. Direct mail response rates have fallen, with market researcher Synovate reporting that, in the industry, only five out of every 1,000 offers generated responses in 2006 compared to approximately 28 out of every 1,000 in 1992.

Because of the highly competitive nature of the credit card issuing business and increasing marketing challenges, a primary method of competition among credit card issuers, including us, is to offer low introductory interest rates and balance transfer programs that offer a favorable annual percentage rate or other financial incentives for a specified length of time on account balances transferred from another credit card. This type of competition has adversely affected credit card yields, and many cardholders now frequently switch credit cards or transfer their balances to another card. There can be no assurance that any of the expenses we incur or incentives we offer to attempt to acquire and maintain accounts and increase card usage will be effective.

Furthermore, many of our competitors are larger than we are, have greater financial resources than we do and/or have lower capital costs and operating costs than we have and expect to have, and have assets such as branch locations and co-brand relationships that may help them compete more effectively. In addition, there is an increasing trend toward consolidation among credit card issuers, resulting in even greater pooled resources. We may be at a competitive disadvantage as a result of the greater scale of many of our competitors.

We face competition from other operators of payment networks, and we may not be able to compete effectively, which could result in reduced transaction volume, limited merchant acceptance of our cards, limited issuance of cards on our network by third parties and materially reduced earnings.

We face substantial and increasingly intense competition in the payments industry. We compete with other payment networks to attract third-party issuers to issue credit and debit cards and other card products on the Discover and PULSE Networks. Competition with other operators of payment networks is generally based on issuer interchange fees, other economic terms, merchant acceptance and network functionality. Competition also is based on service quality, brand image, reputation and market share.

Many of our competitors are well established, larger than we are and/or have greater financial resources than we do. These competitors have provided financial incentives to card issuers, such as large cash signing bonuses for new programs, funding for and sponsorship of marketing programs and other bonuses. Visa and MasterCard have each been in existence for more than 40 years and enjoy greater merchant acceptance and broader global brand recognition than we do. In addition, Visa and MasterCard have entered into long-term arrangements with many financial institutions that may have the effect of preventing them from issuing credit cards on the Discover Network or issuing debit cards on the PULSE Network. MasterCard completed an initial public offering, which provided it with significant capital and may enhance its strategic flexibility. Visa also intends to undertake an initial public offering. American Express is also a strong competitor, with international acceptance, high transaction fees and an upscale brand image.

Furthermore, as a result of their dominant market position and considerable marketing and pricing power, in recent years Visa and MasterCard have been able to aggressively increase transaction fees charged to merchants in an effort to retain and grow their issuer volume. If we are unable to remain competitive on issuer interchange and other incentives, we may be unable to offer adequate pricing to third-party issuers while maintaining sufficient net revenues. At the same time, increasing the transaction fees charged to merchants or increasing acquirer interchange could adversely affect our effort to increase merchant acceptance of credit cards issued on the Discover Network and may cause merchant acceptance to decrease. See Our transaction volume is concentrated among large merchants, and a reduction in the number of, or rates paid by, merchants that participate in the Discover Network could materially adversely affect our business, financial condition, results of operations and cash flows. This, in turn, could adversely affect our ability to attract third-party issuers and our ability to maintain or grow revenues from our proprietary network. Similarly, the PULSE Network operates in the highly competitive PIN debit business with well-established and financially strong network competitors (particularly Visa) that have the ability to offer more attractive economics and bundled products to financial institutions.

In addition, if we are unable to maintain sufficient network functionality to be competitive with other networks, our ability to attract third-party issuers and maintain or increase the revenues generated by our proprietary card issuing business may be materially adversely affected. An inability to compete effectively with other payment networks for the reasons discussed above or any other reason could result in reduced transaction volume, limited merchant acceptance of our cards, limited issuance of cards on our network by third parties and materially reduced earnings.

Our business depends on our ability to manage our credit risks, and failing to manage these risks successfully may result in high charge-off rates or impede our growth.

We market our products to a wide range of consumers, and our success depends on our ability to continue to manage our credit risk while attracting new cardmembers with profitable usage patterns. We select our cardmembers, manage their accounts and establish terms and credit limits using proprietary scoring models and other analytical techniques designed to set terms and credit limits such that we are appropriately compensated for the credit risk we accept, while encouraging cardmembers to use their available credit. The models and approaches we use to select, manage and underwrite our cardmembers may not accurately predict future charge-offs due to, among other things, inaccurate assumptions or models. While we continually seek to improve our assumptions and models, we may make modifications that unintentionally cause them to be less predictive. We also may incorrectly interpret the data produced by these models in setting our credit policies. Our ability to manage credit risk also may be adversely affected by economic conditions, legal or regulatory changes (such as bankruptcy laws, minimum payment regulations and re-age guidance), competitors actions and consumer behavior, as well as inadequate collections staffing, techniques, models and vendor performance.

A cardmember s ability to repay us can be negatively impacted by changes in their payment obligations under mortgage loans, including subprime mortgage loans. Such changes can result from changes in economic conditions including increases in base lending rates upon which payment obligations are based and structured increases in payment obligations, which in turn could adversely impact the ability of our cardmembers to meet their payment obligations to other lenders and to us and could result in higher credit losses in our portfolio.

Rising delinquencies and rising rates of bankruptcy are often precursors of future charge-offs. For instance, bankruptcy rates in the United Kingdom have increased significantly in recent years as a result of the relaxation of the bankruptcy laws, which has contributed to increases in charge-off rates in our U.K. operations. There can be no assurance that our lending standards will protect us against high charge-off levels. In addition, because an important source of our funding is the securitization market, an increase in delinquencies and/or charge-offs could increase our cost of funds or unintentionally cause an early amortization event. See We may be unable to securitize our receivables at acceptable rates or at all, which could materially adversely affect our liquidity, cost of funds, reserves and capital requirements.

We have already launched and plan to expand in several card and consumer lending sectors. Areas of particular focus include: a small business card, which we launched in 2006; relaunching the Miles by Discover Card product, which occurred in 2007; launching personal loan and student lending products, which occurred in 2007; and prepaid cards. We also continuously refine and test our credit criteria, which results in some instances in approving applications that did not previously meet our underwriting criteria. We have less experience in these areas as compared to our traditional products and segments, and there can be no assurance that we will be able to manage our credit risk or generate sufficient revenue to cover our expenses in these markets. Our failure to manage our credit risks may materially adversely affect our profitability and ability to grow.

Economic downturns, financial market events and other conditions beyond our control could materially adversely affect our business.

Economic downturns, financial market events and other conditions beyond our control may adversely affect consumer spending, asset values, investments, financial market liquidity, consumer indebtedness and unemployment rates, which in turn can negatively impact our business. If general economic conditions in the United States or United Kingdom deteriorate or interest rates increase, the number of transactions, average purchase amount of transactions, or average balances outstanding on our cards may be reduced, which would reduce transaction fees and interest income and thereby adversely affect profitability. In addition, high levels of unemployment, low levels of spending, deteriorating housing markets, recessions or other conditions, including terrorism, natural disasters or the outbreak of diseases, may adversely affect the ability and willingness of cardmembers to pay amounts owed to us, which would increase delinquencies and charge-offs and could materially adversely affect our business.

Changes in the level of interest rates could materially adversely affect our earnings.

Changes in interest rates cause our interest expense to increase or decrease, as certain of our debt instruments carry interest rates that fluctuate with market benchmarks. If we are unable to pass our higher cost of funds to our customers, the increase in interest expense could materially adversely affect earnings. Some of our managed receivables bear interest at a fixed rate or do not earn interest, and we may not be able to increase the rate on those loans to mitigate our higher cost of funds. At the same time, our variable rate managed receivables, which are based on a market benchmark, may not change at the same rate as our floating rate debt instruments or may be subject to a cap.

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Interest rates may also adversely impact our delinquency and charge-off rates. Many consumer lending products bear interest rates that fluctuate with certain base lending rates published in the market, such as the prime rate and the London Interbank Offered Rate (LIBOR). As a result, higher interest rates often lead to higher payment requirements by consumers under obligations to us or other lenders, which may reduce their ability to remain current on their obligations to us and thereby lead to loan delinquencies and additions to our loan loss provision, which could materially adversely affect our earnings.

In connection with our spin-off from Morgan Stanley, we have incurred additional indebtedness that could restrict our operations.

In recent years, Morgan Stanley provided a significant portion of our funding. Since our spin-off from Morgan Stanley, we finance our capital needs with third party funding. We have entered into a multi-year unsecured committed credit facility of $2.5 billion, which contains customary restrictions, covenants and events of default. See Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources. The terms of this facility and any future indebtedness impose various restrictions and covenants on us (such as tangible net worth requirements) that could have adverse consequences, including,

- limiting our ability to pay dividends to our stockholders;
- increasing our vulnerability to changing economic, regulatory and industry conditions;
- limiting our ability to compete and our flexibility in planning for, or reacting to, changes in our business and the industry;
- limiting our ability to borrow additional funds; and
- requiring us to dedicate a substantial portion of our cash flow from operations to payments on our debt, thereby reducing funds available for working capital, capital expenditures, acquisitions and other purposes.

Our total combined indebtedness as of November 30, 2007 was approximately $30.0 billion, as compared to $21.6 billion at November 30, 2006. The increase in indebtedness primarily represents incremental deposits obtained to establish a liquidity reserve, the balance of which was approximately $8.3 billion and was included in cash and cash equivalents at November 30, 2007. We may also incur additional substantial indebtedness in the future.

We may be unable to securitize our receivables at acceptable rates or at all, which could materially adversely affect our liquidity, cost of funds, reserves and capital requirements.

The securitization of credit card receivables, which involves the transfer of receivables to a trust and the issuance by the trust of beneficial interests to third-party investors, is our largest single source of funding. Factors affecting our ability to securitize our credit card receivables at acceptable pricing levels, or at all, include the overall credit quality of our receivables, negative credit ratings action affecting our asset-backed securities (or Discover Bank), the stability of the market for securitization transactions, investor demand, and the legal, regulatory, accounting and tax requirements governing securitization transactions. For example, the current subprime mortgage crisis has created a disruption in the capital markets and caused a weakening in demand for asset-backed securities, including those for credit card receivables. In addition, changes to Statement of Financial Accounting Standards No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* as amended (Statement No. 140), are being discussed which may make it more difficult for us to maintain sale accounting treatment for our securitizations under accounting principles generally accepted in the United States (GAAP) or may require us to recognize securitized receivables on our consolidated and combined statements of financial condition, which could substantially increase the allowance for loss requirements and Discover Bank s regulatory capital requirements and result in changes in the timing of the recognition of income from securitization transactions.

Our results of operations and financial condition could also be materially adversely affected by the occurrence of events that could result in the early amortization of our securitization transactions. Credit card

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securitizations are normally structured as revolving transactions that do not distribute to securitization investors their share of monthly principal payment on the receivables during the revolving period, and instead use those payments to fund the purchase of replacement receivables. The occurrence of early amortization events may result in termination of the revolving period of our securitization transactions. Early amortization events include, for example, insufficient cash flows in the securitized pool of receivables to meet contractual requirements, certain breaches of representations, warranties or covenants in the agreements relating to the securitization, and bankruptcy or insolvency.

If we are unable to continue to securitize our credit card receivables at acceptable pricing levels, or at all, including by reason of the early amortization of any of our securitization transactions, we would seek to liquidate investment securities, increase bank deposits and use alternative funding sources to fund increases in loan receivables and meet our other liquidity needs. In the event of an economic early amortization, receivables that otherwise would have been subsequently purchased by the trust from us would instead continue to be recognized on our consolidated and combined statements of financial condition since the cash flows generated in the trust would instead be used to repay investors in the asset-backed securities. Recognizing these receivables would require us to obtain alternative funding.

The inability to continue to securitize our credit card receivables at acceptable pricing levels, or at all, could materially adversely affect our liquidity, cost of funds, reserves and capital requirements. In addition, liquidation of investment securities and available alternative funding sources may be insufficient to meet the ongoing funding needs of our business if we are unable to continue to securitize our credit card receivables. For a further discussion of our liquidity and funding needs, see Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources.

An inability to accept or obtain brokered deposits in the future could materially adversely affect our liquidity position and funding costs.

The FDIA prohibits a bank, including our subsidiaries Discover Bank and Bank of New Castle, from accepting brokered deposits or offering interest rates on any deposits significantly higher than the prevailing rate in its normal market area or nationally (depending upon where the deposits are solicited), unless (1) it is well-capitalized or (2) it is adequately capitalized and receives a waiver from the FDIC. A bank that is adequately capitalized and that accepts brokered deposits under a waiver from the FDIC may not pay an interest rate on any deposit in excess of 75 basis points over certain prevailing market rates. There are no such restrictions on a bank that is well-capitalized. While Discover Bank and Bank of New Castle each met the FDIC s definition of well-capitalized as of November 30, 2007, there can be no assurance that they will continue to meet this definition. We rely on third-party brokers to access the brokered deposit market, and brokered deposits may become unavailable to us due to the unwillingness of brokers to sell our deposits, as a result of a decline in our credit ratings or for other reasons. An inability to accept or obtain brokered deposits in the future could materially adversely affect our liquidity position and funding costs.

We rely in part on unsecured and secured debt for our funding and the inability to access the U.S. or U.K. debt markets could materially adversely affect our business, financial condition and results of operations.

While our primary sources of funding are securitizations and brokered deposits, we also are dependent on access to the U.S. and U.K. unsecured debt markets to fund our managed receivables as well as other assets. In general, the amount, type and cost of our funding directly affects the cost of operating our business and growing our assets and is dependent upon outside factors such as our credit rating from ratings agencies. Historically we have benefited from Morgan Stanley s credit ratings. Since our spin-off, Discover Bank has maintained its BBB rating from Standard & Poor s (S&P) and has been assigned a Baa2 deposit and Baa2 senior unsecured rating from Moody s Investor Service (Moody s) and a BBB rating from Fitch Ratings (Fitch). We have been assigned a BBB- long-term rating from S&P, a Baa3 senior unsecured rating from Moody s and a BBB long-term rating from Fitch. A rating is not a recommendation to purchase, sell or hold any particular security. In addition, there can be no assurance that a rating will be maintained for any given period of time or that a rating will not be lowered or withdrawn in its entirety. If our ratings are for any reason reduced or we are unable

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to access the U.S. or U.K. unsecured debt markets for any reason, our business, financial condition and results of operations could be materially adversely affected.

In response to the exploration of the spin-off in 2005, Moody s placed the asset-backed securities issued domestically by the Discover Card Master Trust I under review for a possible downgrade, which we believe contributed to a temporary disruption in our ability to access the securitization markets, increasing our reliance on intercompany funding and deposit markets. This disruption lasted approximately five months, at which time Moody s reaffirmed the ratings on the asset-backed securities.

Declines in the value of, or income earned from, our retained interests in our securitization transactions could materially adversely affect our financial condition, results of operations and cash flows.

We retain interests in the assets transferred to or created in our securitization transactions and earn income from these assets. The value of our retained interests and the amount of income that we earn depend on many factors, including, among others, the revenues, performance and credit risk of the securitized loans, which are subject to the same risks and uncertainties as loans that we have not securitized. The value of our interests may also change because of changes in the assumptions used to estimate their fair value, such as market interest rates and other conditions, increases in bankruptcy or charge-off rates, payment rates and changes in the interpretation and application of accounting rules relating to such valuation. If the income that we earn from our retained interests in securitization transactions were to decrease or the value of our retained interests were to decrease, our financial condition, results of operations and cash flows could be materially adversely affected.

Our investment portfolio may be adversely affected by market fluctuations, which could negatively impact our financial condition.

We have an investment portfolio that we manage in accordance with our internal policies and procedures, including the investment of our liquidity reserve, which had a balance of approximately $8.3 billion as of November 30, 2007. Our investment portfolio may be adversely affected by market fluctuations including, without limitation, changes in interest rates, prices, credit risk premiums and overall market liquidity. Also, investments backed by collateral could be adversely impacted by changes in the value of the underlying collateral. Our fixed income investments are subject to market valuation risks from changes in the general level of interest rates. Recent increases in credit risk premiums can negatively impact the value of our securities. Certain markets have been experiencing disruptions in market liquidity, and the lack of a secondary market may adversely affect the valuation of certain of our investments. In addition, deteriorating economic conditions may cause certain of the obligors, counterparties and underlying collateral on our investments to incur losses of their own, thereby increasing our credit risk exposure to these investments. These risks could result in a decrease in the value of our investment portfolio, which could negatively impact our financial condition. For example, we recorded a loss on an investment in certain asset-backed commercial paper notes during the year ended November 30, 2007. See Note 4: Investment Securities to the audited consolidated and combined financial statements contained in this prospectus for further details.

We may be unable to increase or sustain Discover Card usage, which could impair growth in, or lead to diminishing, average balances and total revenue.

A key element of our strategy is to increase the usage of the Discover Card by our cardmembers, including making it their primary card, and thereby increase our revenue from transaction and service fees and our managed receivables. However, our cardmembers use and payment patterns may change because of social, legal and economic factors, and cardmembers may decide not to increase card usage or may decide to pay the balances within the grace period to avoid finance charges. We face challenges from competing credit card products in our attempts to increase credit card usage by our existing cardmembers. Our ability to increase cardmember usage also is dependent on cardmember satisfaction, which may be adversely affected by factors outside of our control, including competitors actions. As part of our strategy to increase usage, we are seeking to increase the number of merchants who accept cards issued on the Discover Network. If we are unable to increase merchant

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acceptance of our cards, our ability to grow usage of Discover Cards may be hampered. As a result of these factors, we may be unable to increase or sustain credit card usage, which could impair growth in, or lead to diminishing, average balances and total revenue.

We may be unable to grow earnings if we do not attract new cardmembers, or if we attract cardmembers with unfavorable spending and payment habits.

We are seeking to increase managed receivables by attracting new cardmembers who will use their Discover Cards, meet their monthly payment obligations and maintain balances that generate interest and fee income for us. We are subject to substantial competition from other credit card issuers for these new cardmembers. We plan to continue marketing the Discover Card, but we may not have adequate financial resources to permit us to incur all of the marketing costs that may be necessary to maintain or grow our managed receivables or to attract new accounts. The spending and payment habits of these new cardmembers may not be sufficient to make their accounts as profitable as we expect. In addition, our risk models may not accurately predict the credit risk for these new cardmembers, which could result in unanticipated losses in future periods. To the extent that the spending and payment habits of new cardmembers do not meet our expectations, our earnings and growth may be negatively affected.

Our transaction volume is concentrated among large merchants, and a reduction in the number of, or rates paid by, merchants that participate in the Discover Network could materially adversely affect our business, financial condition, results of operations and cash flows.

Discover Card transaction volume was concentrated among our top 100 merchants in 2007. These merchants may pressure us to reduce our rates by continuing to participate in the Discover Network only on the condition that we change the terms of their economic participation. At the same time, we are subject to increasing pricing pressure from third-party issuers as a result of the continued consolidation in the banking industry, which results in fewer large issuers that, in turn, generally have a greater ability to negotiate pricing discounts. In addition, many of our merchants, primarily our small and mid-size merchants, are not contractually committed to us for any period of time and may cease to participate in the Discover Network at any time on short notice.

In addition, actual and perceived limitations on acceptance of credit cards issued on the Discover Network could adversely affect the use of the Discover Card by existing cardmembers and the attractiveness of the Discover Card to prospective new cardmembers. Furthermore, we may have difficulty attracting and retaining third-party issuers if we are unable to add and retain acquirers or merchants who accept cards issued on the Discover or PULSE Networks. As a result of these factors, a reduction in the number of, or rates paid by, our merchants could materially adversely affect our business, financial condition, results of operations and cash flows.

We may be unable to grow earnings if we are unable to increase the number of small and mid-size merchants that participate in the Discover Network.

In seeking to expand our merchant acceptance among small and mid-size merchants, we have recently entered into agreements with and have started to use third-party acquirers and processors to add merchants to the Discover Network and accept and process payments for these merchants on an integrated basis with Visa and MasterCard payments. This strategy could have unanticipated results, such as decreased revenues, higher expenses, degraded service and signage placement levels and retaliatory responses from competitors. There can be no assurance that the use of third-party acquirers and processors will continue to increase merchant acceptance among small or mid-size merchants, or that such third-party acquirers will continue to participate with us if more attractive opportunities arise. If we are unable to increase small and mid-size merchant acceptance, our ability to grow earnings could be adversely affected.

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Our business, financial condition and results of operations may be adversely affected by the increasing focus of merchants on the fees charged by credit card networks.

Merchant acceptance and fees are critical to the success of both our card issuing and payment processing businesses. Merchants have shown increasing concern with the levels of fees charged by credit card companies, and have in the past and may in the future seek to negotiate better pricing or other financial incentives as a condition to continued participation in the Discover Network. During the past few years, merchants and their trade groups have filed approximately 50 lawsuits against Visa, MasterCard, American Express and their card issuing banks, claiming that their practices toward merchants, including interchange fees, violate federal antitrust laws. There can be no assurance that they will not in the future bring legal proceedings against other credit card issuers and networks, including us. Merchants also may promote forms of payment with lower fees, such as PIN debit, or seek to impose surcharges at the point of sale for use of credit cards. The heightened focus by merchants on the fees charged by credit card networks, including us, could lead to reduced merchant acceptance of Discover Network cards or reduced fees, either of which could adversely affect our business, financial condition and results of operations.

Our U.K. operations are currently not profitable, and there can be no assurance when or if they will become profitable.

The U.K. market is currently experiencing high delinquencies and bankruptcy levels, compounded by changing regulations, which have resulted in losses in our U.K. operations. Additionally, the United Kingdom has relatively low levels of interchange and fee income and lower net interest margin, which has resulted in and may continue to result in insufficient revenues to compensate for the current levels of loan losses. Our U.K. operations also have a relatively higher cost structure given their smaller scale. In addition to the challenging market conditions described above, U.K. and European regulators have recently increased their focus on the credit card industry.

On February 7, 2008, we entered into an agreement to sell our credit card business in the United Kingdom to Barclays Bank Plc. The closing is expected to occur by the end of our second quarter of 2008 and is subject to the satisfaction of a number of conditions. See Management s Discussion and Analysis of Financial Condition and Results of Operations Recent Developments Sale of the International Card Segment for more information relating to the sale of our Goldfish business.

Our pending sale of our U.K. credit card business is subject to a variety of conditions and may not be completed.

On February 7, 2008, we and Barclays Bank Plc entered into a definitive sale and purchase agreement relating to the sale of our U.K. credit card business, which represents substantially all of our International Card segment. Completion of this sale is subject to a variety of conditions, many of which are outside of our control. If the transaction is not completed, we may have difficulty retaining key personnel of this business.

We expect to continue to incur significant expenses in the litigation we are pursuing against Visa and MasterCard, and there can be no assurance that we will ultimately be successful in this action.

In October 2004, the DOJ prevailed in its antitrust litigation against Visa and MasterCard which challenged their exclusionary practices. Following this ruling, we filed a complaint against Visa and MasterCard seeking substantial damages for the market foreclosure caused by their anticompetitive rules. The trial date is expected to be no later than Fall 2008. We expect to continue to incur substantial legal expenses in the litigation we are pursuing against Visa and MasterCard. Outside counsel and consultant legal expenses for this litigation were approximately $42 million, $51 million and $8 million in 2007, 2006 and 2005, respectively. Expenses associated with this litigation in 2008 are expected to be slightly lower than 2007 expenses. Furthermore, there can be no assurance that we will be successful in recovering any damages in this action. Upon resolution of the litigation, after expenses, we will be required to pay Morgan Stanley the first $700 million of value of cash or non-cash proceeds (increased at the rate of 6% per annum until paid in full) (the minimum proceeds), plus 50%

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of any proceeds in excess of $1.5 billion, subject to certain limitations and a maximum potential payment to Morgan Stanley of $1.5 billion. All payments by Discover to Morgan Stanley will be net of taxes payable by Discover with respect to such proceeds. If, in connection with or following a change of control of Discover, the litigation is settled for an amount less than the minimum proceeds, Discover will be required to pay Morgan Stanley an amount equal to the minimum proceeds. As a result of our agreement to pay the value of non-cash proceeds, we may be required to pay amounts to Morgan Stanley in excess of cash received in connection with the litigation. The value of non-cash proceeds will be determined by an independent third party.

Visa and MasterCard may impose additional restrictions on issuing banks, merchants or merchant acquirers that materially adversely affect the Discover or PULSE Networks, or the Discover Card issuing business.

Visa and MasterCard aggressively seek to protect their networks from competition and have used their rules and policies to do so. For example, in the past they enacted and enforced rules that prohibited their member banks from issuing cards on competing payment networks such as Discover. These rules were ultimately found to violate the antitrust laws. They have adversely affected our business in the past, and they may have lingering effects going forward. Visa and MasterCard also may enact new rules or enforce other rules in the future, including limiting the ability of issuing banks to use the PULSE Network, which may materially adversely affect our ability to compete.

If fraudulent activity associated with our cards increases, our brands could suffer reputational damage, the use of our cards could decrease and our fraud losses could be materially adversely affected.

We are subject to the risk of fraudulent activity associated with merchants, cardmembers and other third parties handling cardmember information. Credit and debit card fraud, identity theft and related crimes are prevalent and perpetrators are growing ever more sophisticated. Our financial condition, the level of our fraud charge-offs and other results of operations could be materially adversely affected if fraudulent activity were to significantly increase. In addition, significant increases in fraudulent activity could lead to regulatory intervention (such as mandatory card reissuance) and reputational and financial damage to our brands, which could negatively impact the use of our cards and thereby have a material adverse effect on our business.

If our security systems, or those of merchants, merchant acquirers or other third parties containing information about cardholders, are compromised, we may be subject to liability and damage to our reputation.

Our security protection measures, including the security of transaction information processed on our systems or the systems or processing technology of third parties participating in the Discover or PULSE Networks, may not be sufficient to protect the confidentiality of information relating to cardholders or transactions processed on the Discover or PULSE Networks. Cardholder data also may be stored on systems of third-party service providers and merchants that may have inadequate security systems. Third-party carriers regularly transport cardholder data, and they may lose sensitive cardholder information. Unauthorized access to the Discover or PULSE Networks or any other Discover information systems potentially could jeopardize the security of confidential information stored in our computer systems or transmitted by our cardmembers or others. If our security systems or those of merchants, processors or other third-party service providers are compromised such that this confidential information is disclosed to unauthorized parties, we may be subject to liability. The preventive measures we take to address these factors are costly, and may become more costly in the future. Moreover, these measures may not protect us from liability, which may not be adequately covered by insurance, or from damage to our reputation.

The financial services and payment services industries are rapidly evolving, and we may be unsuccessful in introducing new products or services in response to this evolution.

The financial services and payment services industries experience constant and significant technological changes, such as continuing development of technologies in the areas of smart cards, radio frequency and proximity payment devices, electronic commerce and mobile commerce, among others. The effect of technological changes on our business is unpredictable.

We depend in part on third parties for the development of and access to new technologies. We expect that new services and technologies relating to the payments business will continue to appear in the market, and these new services and technologies may be superior to, or render obsolete, the technologies that we currently use in our card products and services. As a result, our future success is in part dependent on our ability to identify and adapt to technological changes and evolving industry standards and to provide payment solutions for our cardmembers and merchant and financial institution customers.

Difficulties or delays in the development, production, testing and marketing of new products or services may be caused by a number of factors including, among other things, operational, capital and regulatory constraints. The occurrence of such difficulties may affect the success of our products or services, and developing unsuccessful products and services could result in financial losses, as well as decreased capital availability. In addition, the new products and services offered may not be attractive to our cardmembers and merchant and financial institution customers.

If key technology platforms such as our transaction authorization and settlement systems become obsolete, or if we encounter difficulties processing transactions efficiently or at all, our revenue or results of operations could be materially adversely affected.

We have a large technology staff utilizing current technology. There is no assurance that we may be able to sustain our investment in new technology to avoid obsolescence of critical systems and applications. Further, our transaction authorization and settlement systems may encounter service interruptions due to system or software failure, fire, natural disasters, power loss, disruptions in long distance or local telecommunications access, terrorism or accident. Some of our transaction processing systems are operated at a single facility and could be subject to service interruptions in the event of failure. Our services could be disrupted by a natural disaster or other problem at any of our primary or back-up facilities or our other owned or leased facilities.

We also depend on third-party service providers for the timely transmission of information across our data transportation network and for other telecommunications and technology services, including ancillary transaction processing services for the PULSE Network. Regardless of whether as a result of natural disaster, operational disruption, terrorism, termination of its relationship with us, or any other reason, if a service provider fails to provide the communications capacity or deliver services that we require or expect, the failure could interrupt our services and operations and hamper our ability to process cardholders transactions in a timely and accurate manner or to maintain thorough and accurate records of those transactions. Such a failure could adversely affect the perception of the reliability of the Discover and PULSE Networks and the quality of our brands, and could materially adversely affect our revenues or results of operations.

Merchant defaults may adversely affect our business, financial condition, cash flows and results of operations.

As an issuer and merchant acquirer in the United States on the Discover Network, and an issuer in the United Kingdom on the MasterCard and Visa networks, we may be contingently liable for certain disputed credit card sales transactions that arise between cardholders and merchants. If a dispute is resolved in the cardholder s favor, we will cause a credit or refund of the amount to be issued to the cardholder and charge back the transaction to the merchant or merchant acquirer. If we are unable to collect this amount from the merchant or a merchant acquirer, we will bear the loss for the amount credited or refunded to the cardholder. Where the purchased product or service is not provided until some later date following the purchase, such as an airline ticket, the likelihood of potential liability increases. See Note 20: Commitments, Contingencies and Guarantees to the audited consolidated and combined financial statements contained in this prospectus.

Our success is dependent, in part, upon our executive officers and other key personnel, and the loss of key personnel could materially adversely affect our business.

Our success depends, in part, on our executive officers and other key personnel. Our senior management team has significant industry experience and would be difficult to replace. Moreover, our senior management team is relatively small and we believe we are in a critical period of competition in the financial services and payments industry. The market for qualified individuals is highly competitive, and we may not be able to attract and retain qualified personnel or candidates to replace or succeed members of our senior management team or other key personnel. The loss of key personnel could materially adversely affect our business.

We may be unsuccessful in protecting our intellectual property, including our brands.

The Discover, Goldfish and PULSE brands are very important assets, and our success is dependent on our ability to protect these and our other intellectual property. We may not be able to successfully protect our intellectual property. If others misappropriate, use or otherwise diminish the value of our intellectual property, our business could be adversely affected.

Increased usage by consumers of credit sources such as home equity loans and mortgage refinancings instead of credit card borrowings could adversely affect our business.

During the last few years, lower interest rates and other factors have led to increased availability to consumers of credit sources such as home equity loans and mortgage refinancings at comparatively attractive interest rates. These and other options for consumer credit compete with our card products as alternative sources for consumer borrowing, as consumers may finance expenditures or refinance account balances with these alternative sources of credit. Increased usage by consumers of such alternative sources of credit could adversely affect our businesses.

Acquisitions that we pursue could disrupt our business and harm our financial condition.

We may consider or undertake strategic acquisitions of businesses, products or technologies. If we do so, we may not be able to successfully finance or integrate any such businesses, products or technologies. In addition, the integration of any acquisition may divert management s time and resources from our core business and disrupt our operations. We may allocate resources, such as time and money, on projects that do not increase our earnings. To the extent we pay the purchase price of any acquisition in cash, it would reduce our cash balances; similarly, if the purchase price is paid with our stock, it could be dilutive to our stockholders.

We are subject to regulation by a number of different regulatory agencies, which have broad discretion to require us to alter our operations in ways that could adversely affect our business or subject us to penalties for noncompliance.

We must comply with an array of banking and consumer lending laws and regulations at the state, federal, U.K. and European levels, and these laws and regulations apply to almost every aspect of our business. We are subject to regulation and regular examinations by the FDIC, the Delaware Commissioner and the FSA. In addition, we are subject to regulation by the Federal Reserve Board, the Federal Trade Commission, state banking regulators, the DOJ and European regulators, as well as the SEC and New York Stock Exchange (NYSE) in our capacity as a public company. From time to time, these regulations and regulatory agencies have required us to alter certain of our operating practices, and may require us to do the same in the future. Our ability to introduce new products may be impaired or delayed as a result of regulatory review or failure to obtain required regulatory approvals. We conduct our business primarily through our banks, and various federal, state and European regulators have broad discretion to impose restrictions on our operations. U.S. federal and state consumer protection laws and rules, and laws and rules of foreign jurisdictions where we conduct business limit the manner and terms on which we may offer and extend credit. Failure to comply with these laws and regulations could lead to adverse consequences such as financial, structural, reputational and operational penalties, including receivership and litigation exposure and fines. In addition, efforts to abide by these laws and regulations may increase our costs of operations or limit our ability to engage in certain business activities, including affecting our ability to generate or collect receivables from cardmembers.

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Changes in regulations, or the application thereof, may adversely affect our business, financial condition and results of operations.

Periodically, legislators and regulatory authorities may enact new laws or regulations, or amend existing requirements to further regulate the industries in which we operate. Such new laws or rules could impose limits on the amount of interest or fees we can charge, curtail our ability to collect on account balances, increase compliance costs or materially affect us or the credit card industry in some other manner. For instance, in the past we have been obligated by industry-wide regulatory guidance to change our re-age policy to alter the terms under which delinquent accounts are returned to a current status, which negatively affected our charge-off and delinquency rates. Also, in response to industry-wide regulatory guidance, we increased minimum payment requirements on certain credit card loans and modified our overlimit fee policies and procedures to stop charging such fees for accounts meeting specific criteria, which have impacted, and we believe will continue to negatively impact, balances of credit card loans and related interest and fee revenue and charge-offs. We cannot predict whether any additional or similar regulatory changes will occur in the future.

Congress is considering legislation to restrict certain practices in the credit card industry, including those relating to grace periods, the two-cycle balance computation method (which we currently utilize on most of our products), risk-based and default-based interest rate changes, the allocation of payments, use of arbitration agreements and fees. It is not clear at this time whether new limitations on credit card practices will be adopted by Congress or at the state level and, if adopted, what impact such new limitations would have on us. The Federal Reserve is also revising disclosure and other rules for credit cards that could impact our business. In addition, the laws governing bankruptcy and debtor relief in the United States, the United Kingdom or other countries where we have cardmembers, could also change, making it more expensive or more difficult for us to collect from our cardmembers. Congress is also considering granting the FDIC rulemaking authority under unfair and deceptive practices laws. Furthermore, various federal and state agencies and standard-setting bodies may, from time to time, enact new or amend existing accounting rules or standards that could impact our business practices or funding transactions.

Regulation of the credit card industry, including regulation applicable to Discover Card and merchants that accept it, has expanded significantly in recent years. For instance, financial institutions, including us, were required to implement an enhanced anti-money laundering program in 2002 pursuant to the USA PATRIOT Act. Various U.S. federal and state regulatory agencies and state legislatures are considering new legislation or regulations relating to credit card pricing, credit card repricing, use of consumer reports, credit card disclosures, patent reform, identity theft, privacy, data security and marketing that could have a direct effect on us and our merchant and financial institution customers.

In the United Kingdom, during the last three years there have been increasing regulatory initiatives with respect to late and overlimit fees, interchange fees and the sale of retail insurance products, a relaxation of bankruptcy laws and an increase in industry-wide consumer protection measures. We expect that these initiatives and measures will continue to increase our compliance costs and the risk of consumer complaints, litigation and regulatory inquiries, as well as materially adversely affect the economics of the International Card segment.

Current and proposed regulation addressing consumer privacy and data use and security could inhibit the number of payment cards issued and increase our costs.

Regulatory pronouncements relating to consumer privacy, data use and security affect our business. In the United States, we are subject to the Federal Trade Commission s and the banking regulators information safeguard rules under the Gramm-Leach-Bliley Act. The rules require that financial institutions (including us) develop, implement and maintain a written, comprehensive information security program containing safeguards that are appropriate to the financial institution s size and complexity, the nature and scope of the financial institution s activities, and the sensitivity of any customer information at issue. Both the United States and the United Kingdom have experienced a heightened legislative and regulatory focus on data security, including, in the United States, requiring consumer notification in the event of a data breach. In the United States, there are a

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number of bills pending in Congress and in individual states, and there have been numerous legislative hearings focusing on these issues. In addition, most states have enacted security breach legislation requiring varying levels of consumer notification in the event of certain types of security breaches, and several other states are considering similar legislation. In the United Kingdom, there are detailed regulations on data privacy under the European Commission Data Protection Directive (Directive 95/46/EC) and the U.K. Data Protection Act of 1998, which are enforced by the Information Commissioner, the United Kingdom s privacy regulator.

Regulation of privacy, data use and security may cause an increase in the costs to issue payment cards and/or may decrease the number of our cards that we or third parties issue. New regulations in these areas may also increase our costs to comply with such regulations, which could materially adversely affect our earnings. In addition, failure to comply with the privacy and data use and security laws and regulations to which we are subject, including by reason of inadvertent disclosure of confidential information, could result in fines, sanctions, penalties or other adverse consequences and loss of consumer confidence, which could materially adversely affect our results of operations, overall business and reputation.

Legislation or regulation could be enacted requiring us to hold higher levels of capital, which we may not be able to obtain and which would reduce our return on capital.

Discover Bank and Bank of New Castle are subject to capital, funding and liquidity requirements prescribed by statutes, regulations and orders. If new legislation or regulations are enacted that increase the levels of regulatory capital that are required, we may be required to obtain additional capital. In addition, regulators have broad discretion to impose additional capital and other requirements on us, including imposing restrictions on the ability of our regulated subsidiaries to pay dividends. Our ability to obtain additional capital would be dependent upon, among other things, general economic conditions, our financial performance and prospects, and our ability and willingness to make capital contributions to Discover Bank and Bank of New Castle. If we were required to increase capital for Discover Bank or Bank of New Castle, it would have the effect of reducing our return on capital. In addition, if Discover Bank and Bank of New Castle were to fail to meet these regulatory capital requirements, it would become subject to restrictions that could materially adversely affect our ability to conduct normal operations.

Litigation and regulatory actions could subject us to significant fines, penalties and/or requirements resulting in increased expenses.

Businesses in the credit card industry have historically been subject to various significant legal actions, including class action lawsuits and patent claims. Many of these actions have included claims for substantial compensatory and/or punitive damages or claims for indeterminate amounts of damages. While we have historically relied on our arbitration clause in agreements with cardmembers, which has limited our exposure to consumer class action litigation, there can be no assurance that we will continue to be successful in enforcing our arbitration clause in the future or that we will not be subject to significant legal actions such as those to which some of our competitors have been subject. In addition, we may be involved in various actions or proceedings brought by governmental regulatory agencies in the event of noncompliance with laws or regulations, which could subject us to significant fines, penalties and/or requirements resulting in increased expenses.

Risks Related to our Spin-Off

Our cost of funding increased after our separation from Morgan Stanley, and our liquidity may decrease.

While Morgan Stanley provided a significant portion of our funding in recent years, it no longer provides any funding following our spin-off. We have lower credit ratings and more constrained liquidity than our former parent company, Morgan Stanley. Although our debt is currently rated investment grade, a credit ratings downgrade to below investment grade would reduce our investor base and increase our cost of funding. Our liquidity may also decrease, and we may be less able to withstand a liquidity stress event. We may also face additional challenges in the future, including more limited capital resources to invest in or expand our businesses.

Certain of our historical financial results are as a business segment of Morgan Stanley and therefore may not be representative of our results as a separate, stand-alone company.

Certain historical financial information we have included in this prospectus has been derived from Morgan Stanley s consolidated financial statements and does not necessarily reflect what our financial condition, results of operations or cash flows would have been had we operated as a separate, stand-alone company during the periods presented. Certain historical costs and expenses reflected in our audited consolidated and combined financial statements include an allocation for certain corporate functions historically provided by Morgan Stanley, including general corporate expenses, employee benefits and incentives. These allocations were based on what we and Morgan Stanley considered to be reasonable reflections of the historical utilization levels of these services required in support of our business. This historical information does not necessarily indicate what our results of operations, financial condition, cash flows or costs and expenses would have been had we operated as a separate, stand-alone entity, nor is it indicative of what our results will be in the future as a publicly-traded stand-alone company.

The obligations associated with being a public company require significant resources and management attention.

In connection with our recent separation from Morgan Stanley, we have become subject to the reporting requirements of the Exchange Act, and the Sarbanes-Oxley Act of 2002 (the Sarbanes-Oxley Act). The Exchange Act requires that we file annual, quarterly and current reports with respect to our business and financial condition. The Sarbanes-Oxley Act requires, among other things, that we establish and maintain effective internal controls and procedures for financial reporting. All of the procedures and practices required of us as a subsidiary of Morgan Stanley were established prior to the spin-off, but we have additional procedures and practices required of us as a separate, stand-alone public company. As a result, we have incurred and will continue to incur significant legal, accounting and other expenses that we did not previously incur. Furthermore, the corporate infrastructure and other resources required to operate as a public company may divert management s attention from implementing our growth strategy, which could prevent us from improving our business, results of operations and financial condition. We have made, and will continue to make, changes to our internal controls and procedures for financial reporting and accounting systems to meet our reporting obligations. We cannot predict or estimate the amount of additional costs we may incur in order to comply with these requirements.

Section 404 of the Sarbanes-Oxley Act requires annual management assessments of the effectiveness of our internal control over financial reporting, starting with the second annual report that we file with the SEC. In connection with the implementation of the necessary procedures and practices related to internal controls over financial reporting, we may identify deficiencies that we may not be able to remediate in time to meet the deadline imposed by the Sarbanes-Oxley Act for compliance with the requirements of Section 404. We will be unable to issue securities in the public markets through the use of a shelf registration statement if we are not in compliance with Section 404. In addition, failure to achieve and maintain an effective internal control environment could have a material adverse effect on our business and stock price.

As a result of our separation from Morgan Stanley we may experience increased costs resulting from a decrease in the purchasing power and other operational efficiencies we previously had due to our association with Morgan Stanley.

Prior to our separation from Morgan Stanley, we were able to take advantage of Morgan Stanley s purchasing power in procuring goods, technology and services, including insurance, employee benefit support and audit services. As a smaller separate, stand-alone company, we may be unable to obtain goods, technology and services at prices and on terms as favorable as those available to us prior to the separation, which could have a material adverse effect on our business, financial condition, cash flows and results of operations. Our tax liability may also increase due to increased state income taxes in the jurisdictions where combined filings were previously made with Morgan Stanley.

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In connection with our separation from Morgan Stanley, we have assumed past, present and future liabilities related to our business, and have entered into agreements relating to the ongoing provision of services and other matters which may be on terms less favorable to us than if they had been negotiated with another party.

Pursuant to certain agreements we entered into with Morgan Stanley in connection with the spin-off, we have agreed to indemnify Morgan Stanley for, among other matters, past, present and future liabilities related to our business. Such liabilities include unknown liabilities, which could be significant.

We entered into these agreements and other agreements relating to the ongoing provision of services and other matters with Morgan Stanley while still a wholly-owned subsidiary of Morgan Stanley. Accordingly, the terms of those agreements may not reflect those that would have been reached with another party. If these agreements were to have been entered into with another party, we may have obtained more favorable terms than under these agreements.

We must abide by certain restrictions to preserve the tax treatment of the distribution of our common stock by Morgan Stanley and we must indemnify Morgan Stanley for taxes resulting from certain actions we take that cause the distribution to fail to qualify as a tax-free transaction.

Morgan Stanley has received a ruling from the Internal Revenue Service that, based on customary representations and qualifications, the distribution of our common stock by Morgan Stanley was tax-free to Morgan Stanley stockholders for U.S. federal income tax purposes. These representations include representations as to the satisfaction of certain requirements that must be met in order for the distribution to qualify for tax-free treatment under the Internal Revenue Code of 1986, as amended (the Code), and state law. If any of the representations and assumptions upon which the ruling is based is untrue or incomplete in any material respect, Morgan Stanley may not be able to rely upon the ruling.

If the distribution were not to qualify for tax-free treatment under sections 355, 368 and related provisions of the Code, Morgan Stanley would recognize taxable gain equal to the excess of the fair market value of our stock over Morgan Stanley s tax basis in our stock. Under certain circumstances, we would be required under the

U.S. tax sharing agreement entered into between Morgan Stanley and us to indemnify Morgan Stanley for all or a portion of this liability. In addition, each holder who received our common stock in the distribution would be treated as receiving a taxable distribution in an amount equal to the fair market value of our common stock received.

Even if the distribution otherwise qualifies as a tax-free distribution under the Code, current tax law generally creates a presumption that the distribution would be taxable to Morgan Stanley (but not to its stockholders) if we engage in, or enter into an agreement to engage in, a transaction that would result in a 50% or greater change, by vote or by value, in our stock ownership during the four-year period beginning on the date that begins two years before the distribution date, unless it is established that the transaction is not pursuant to a plan or series of transactions related to the distribution. Treasury regulations currently in effect generally provide that whether an acquisition transaction and a distribution are part of a plan is determined based on all of the facts and circumstances including, but not limited to, specific factors listed in the regulations. In addition, the regulations provide several safe harbors for acquisition transactions that are not considered to be part of a plan.

Under the U.S. tax sharing agreement entered into between Morgan Stanley and us, for a period of two years following the distribution, generally we may not take certain actions unless Morgan Stanley provides us with prior written consent for such action, or we provide Morgan Stanley with a tax ruling or rulings, or an unqualified opinion of counsel, in each case acceptable to Morgan Stanley, to the effect that the action will not affect the tax-free nature of the separation and distribution, but we will remain liable for any taxes and other liabilities imposed as a result of the separation and distribution failing to qualify as a tax-free transaction, as a result of such action. These restrictions may prevent us from entering into strategic or other transactions which might be advantageous to us or to our stockholders, such as issuing equity securities to satisfy our financing needs, acquiring businesses or assets by issuing equity securities, or mergers or other business combinations.

Our ability to operate our business effectively may suffer if we do not, quickly and cost effectively, establish our own financial, administrative and other support functions to operate as a stand-alone company.

Historically, we have relied on certain financial, administrative and other resources of Morgan Stanley to operate our business. In conjunction with our separation from Morgan Stanley, we have enhanced and will need to continue to enhance our own financial, administrative and other support systems or contract with third parties to replace Morgan Stanley s systems. We will also need to continue to establish our own accounting and auditing policies and systems on a stand-alone basis.

Prior to our spin-off, Morgan Stanley performed many important corporate functions for our operations, including portions of human resources, information technology, accounting, office space leasing, corporate services and treasury. We estimate the annual costs associated with replacing these functions and establishing our own infrastructure related thereto, to be approximately $60 million. Prior to the spin-off, we entered into agreements with Morgan Stanley under which Morgan Stanley will provide some of these services to us on a transitional basis, for which we will pay Morgan Stanley. Upon the occurrence of certain events, including a change of control, Morgan Stanley may terminate these services. These services may not be sufficient to meet our needs and, after these agreements with Morgan Stanley expire or are terminated, we may not be able to replace these services at all or obtain these services at acceptable prices and terms. Any failure or significant downturn in our own financial or administrative policies and systems or in Morgan Stanley s financial or administrative policies and systems during the transitional period could impact our results and could materially harm our business, financial condition and results of operations.

In the United Kingdom, prior to our separation from Morgan Stanley, we shared a brand and bank charter with Morgan Stanley, and our primary card brand was Morgan Stanley. From the date of the spin-off, we have a limited right to use the Morgan Stanley brand for three years, following which we will not be able to use this brand. Our primary brand in the United Kingdom is Goldfish, and we will also utilize other brands. Transitioning to a new brand will result in increased marketing and transitional costs and may result in customer attrition.

Risks Related to the Exchange Offer

Failure to exchange your old notes will leave them subject to transfer restrictions.

Any old notes that remain outstanding after this exchange offer will continue to be subject to restrictions on their transfer. After this exchange offer, holders of old notes will not have any further rights under the registration rights agreement that applies to their notes, with limited exceptions. In general, old notes may not be offered or sold unless registered under the Securities Act, except pursuant to an exemption from, or in a transaction not subject to, the Securities Act and applicable state securities laws. We currently do not anticipate registering the old notes under the Securities Act. As old notes are tendered and accepted in the exchange offer, the aggregate principal amount of old notes will decrease, which will decrease their liquidity. Any market for old notes that are not exchanged could be adversely affected by the conclusion of this exchange offer.

Late deliveries of the old notes and other required documents could prevent a holder from exchanging its notes.

Holders are responsible for complying with all exchange offer procedures. Issuance of exchange notes in exchange for old notes will only occur upon completion of the procedures described in this prospectus under the heading The Exchange Offer Procedures for Tendering Old Notes. Therefore, holders of old notes who wish to exchange them for exchange notes should allow sufficient time for completion of the exchange procedures. We are not obligated to notify you of any failure to follow the proper procedures.

If you are a broker-dealer, your ability to transfer the exchange notes may be restricted.

A broker-dealer that purchased old notes for its own account as part of market making or trading activities must deliver a prospectus when it sells the exchange notes. Our obligation to make this prospectus available to broker-dealers is limited. Consequently, we cannot guarantee that a proper prospectus will be available to broker-dealers wishing to resell their exchange notes.

Risks Related to the Exchange Notes

We are a holding company that conducts all of our business through subsidiaries. The debt and other liabilities of our subsidiaries will be effectively senior to the exchange notes.

We conduct all of our business through our subsidiaries. Our cash flow and, consequently, our ability to pay interest in cash and to service our debt, including the exchange notes, are dependent to a certain extent upon the cash flow of our subsidiaries and the payment of funds to us by those subsidiaries in the form of loans, dividends or otherwise. Our subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to pay any amounts due on the exchange notes or to make cash available for that purpose. In addition, many of our operating subsidiaries are highly regulated and may be subject to restrictions on their ability to pay dividends to us. These subsidiaries may use the earnings they generate, as well as their existing assets, to fulfill their own direct debt service requirements.

The exchange notes will be our senior unsecured obligations and will rank equally with all of our existing and future senior unsecured indebtedness. To the extent that any of our subsidiaries have outstanding indebtedness, the exchange notes will effectively rank junior to such indebtedness and other liabilities, including deposits. See Description of the Exchange Notes Ranking.

There are no covenants in the indentures governing the exchange notes relating to our ability to incur future indebtedness or pay dividends and limited restrictions on our ability to engage in other activities, which could adversely affect our ability to pay our obligations under the exchange notes.

The indenture governing the exchange notes does not contain any financial covenants. The indenture permits us and our subsidiaries to incur additional debt, including secured debt. Because the exchange notes will be unsecured, in the event of any liquidation, dissolution, reorganization, bankruptcy or other similar proceeding regarding us, whether voluntary or involuntary, the holders of our secured debt will be entitled to receive payment to the extent of the assets securing that debt before we can make any payment with respect to the exchange notes. If any of the foregoing events occurs, we cannot assure you that we will have sufficient assets to pay amounts due on our debt and the exchange notes. As a result, you may receive less than you are entitled to receive or recover nothing if any liquidation, dissolution, reorganization, bankruptcy or other similar proceeding occurs.

The indenture will not limit our subsidiaries ability to issue or repurchase securities, pay dividends or engage in transactions with affiliates. Our ability to use our funds for numerous purposes may limit the funds available to pay our obligations under the exchange notes.

There may not be a public market for the exchange notes.

The exchange notes constitute a new issue of securities with no established trading market. We do not intend to list the exchange notes on any securities exchange or to include the exchange notes in any automated quotation system. Accordingly, no market for the exchange notes may develop, and any market that develops may not last. If the exchange notes are traded, they may trade at a discount from their initial offering price, depending on prevailing interest rates, the market for similar securities, our performance and other factors. To the extent that an active trading market does not develop, you may not be able to resell your exchange notes at their fair market value or at all.

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FORWARD-LOOKING STATEMENTS

This prospectus and materials we have filed or will file with the Securities and Exchange Commission (the SEC) (as well as information included in our other written or oral statements) contain or will contain certain statements that are forward-looking within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Actual outcomes and results may differ materially from those expressed in, or implied by, our forward-looking statements. Words such as expects, anticipates, believes, estimates and other similar expressions or future or conditional verbs such as will, should, would and could are intended to identify such forward-looking statements. You should not rely solely on the forward-looking statements and should consider all uncertainties and risks throughout this prospectus, including those described under Risk Factors. The statements are only as of the date they are made, and we undertake no obligation to update any forward-looking statement.

Possible events or factors that could cause results or performance to differ materially from those expressed in our forward-looking statements include the following:

- the actions and initiatives of current and potential competitors;
- our ability to manage credit risks and securitize our receivables at acceptable rates;
- changes in economic variables, such as the number and size of personal bankruptcy filings, the rate of unemployment and the levels of consumer confidence and consumer debt;
- the level and volatility of equity prices, commodity prices and interest rates, currency values, investments and other market indices;
- the availability and cost of funding and capital;
- access to U.S. or U.K. debt markets;
- the ability to increase or sustain Discover Card usage or attract new cardmembers and introduce new products or services;
- our ability to attract new merchants and maintain relationships with current merchants;
- material security breaches of key systems;
- unforeseen and catastrophic events;
- our reputation;
- the potential effects of technological changes;

the effect of political, economic and market conditions and geopolitical events;

unanticipated developments relating to lawsuits, investigations or similar matters;

the impact of current, pending and future legislation, regulation and regulatory and legal actions;

our ability to attract and retain employees;

the ability to protect our intellectual property;

the impact of our separation from Morgan Stanley;

the impact of any potential future acquisitions;

investor sentiment; and

the restrictions on our operations resulting from indebtedness incurred during our separation from Morgan Stanley.

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The foregoing review of important factors should not be construed as exclusive and should be read in conjunction with the other cautionary statements that are included in this prospectus. These factors expressly qualify all subsequent oral and written forward-looking statements attributable to us or persons acting on our behalf. Except for any ongoing obligations to disclose material information as required under U.S. federal securities laws, we do not have any intention or obligation to update forward-looking statements after we distribute this prospectus, whether as a result of new information, future developments or otherwise.

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THE EXCHANGE OFFER

We are commencing two separate exchange offers with respect to each series of old notes. We refer to these exchange offers, collectively, as the exchange offer in this prospectus. When we refer to exchanging old notes for exchange notes, we mean exchanging old notes of an applicable series for exchange notes of a corresponding series. The following is a summary of the exchange offer relating to the old notes. As a summary, this section does not contain all of the information you might find useful. For further information, you should read the registration rights agreement with the initial purchasers of the old notes and the form of letter of transmittal, copies of which have been filed as exhibits to the registration statement of which this prospectus forms a part.

Purpose and Effect of This Exchange Offer

In connection with the sale of the old notes, we entered into a registration rights agreement with the initial purchasers of the old notes in which we agreed to file a registration statement relating to an offer to exchange the old notes for the exchange notes. The registration statement of which this prospectus forms a part was filed in compliance with this obligation. We also agreed to use our reasonable best efforts to cause such offer to be consummated within 360 calendar days following the issuance of the applicable series of old notes. The exchange notes will have terms substantially identical to the old notes except that the exchange notes will not contain terms with respect to transfer restrictions, registration rights and additional interest payable for the failure to have the registration statement of which this prospectus forms a part declared effective within 330 calendar days after the issuance of the applicable series of old notes or this exchange offer consummated within 360 calendar days after the issuance of the applicable series of old notes.

Each holder of old notes that wishes to exchange old notes in this exchange offer will be required to make the representations discussed below under Procedures for Tendering Old Notes.

If: (i) because of any change in law or in currently prevailing interpretations of the SEC staff, we are not permitted to effect the exchange offer with respect to a series of notes, (ii) the exchange offer with respect to a series of notes is not consummated within 360 calendar days of the date of issuance of the old notes, (iii) in the case of any holder of any series of notes that participates in the exchange offer, such holder does not receive exchange notes of such series on the date of the exchange that may be sold without restriction under state and federal securities laws (other than due solely to the status of such holder as an affiliate of ours within the meaning of the Securities Act or as a broker-dealer), or (iv) we so elect, then in each case we will (1) promptly deliver to the holders written notice thereof and (2) at our sole expense, (a) file, as promptly as practicable (but in no event more than 45 days after so required pursuant to the registration rights agreement), a shelf registration statement covering resales of such notes, (b) use our reasonable best efforts to cause the shelf registration statement to be declared effective under the Securities Act and (c) use our reasonable best efforts to keep effective the shelf registration statement until the earlier of two years (or, if Rule 144(k) is amended to provide a shorter restrictive period, such shorter period) after the date of the issuance of the old notes or such time as all of the applicable notes have been sold thereunder. We will, if a shelf registration statement is filed with respect to one or more series of notes, provide to each holder of such notes copies of the prospectus that is a part of the shelf registration statement, notify each such holder of such notes when the shelf registration statement for such notes has become effective and take certain other actions as are required to permit unrestricted resales of such notes. A holder that sells notes pursuant to the shelf registration statement will be required to be named as a selling security holder in the related prospectus, to provide information related thereto and to deliver such prospectus to purchasers, will be subject to certain of the civil liability provisions under the Securities Act in connection with such sales and will be bound by the provisions of the registration rights agreement that are applicable to such a holder (including certain indemnification rights and obligations). We will not have any obligation to include in the shelf registration statement holders who do not deliver such information to us.

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Resale of Exchange Notes

Based on existing interpretations of the Securities Act by the SEC staff set forth in several no-action letters to third parties, and subject to the immediately following sentence, we believe that exchange notes issued under this exchange offer in exchange for old notes may be offered for resale, resold and otherwise transferred by the holders thereof (other than holders who are broker-dealers) without further compliance with the registration and prospectus delivery provisions of the Securities Act provided that such exchange notes are acquired in the ordinary course of such holder s business and such holder has no arrangement with any person to participate in a distribution of such exchange notes. However, any purchaser of old notes who is an affiliate of ours or who has an arrangement or understanding with any person to participate in a distribution of the exchange notes, or any broker-dealer who purchased the old notes from us for resale pursuant to Rule 144A or any other available exemption under the Securities Act, (i) will not be able to rely on the interpretations of the SEC staff set forth in the above-mentioned no-action letters, (ii) will not be entitled to tender its old notes in the exchange offer, and (iii) must comply with the registration and prospectus delivery requirements of the Securities Act in connection with any sale or transfer of the old notes unless such sale or transfer is made pursuant to an exemption from such requirements. We do not intend to seek our own no-action letter, and there can be no assurance that the SEC staff would make a similar determination with respect to the exchange notes as it has in such no-action letters to third parties.

This prospectus may be used for an offer to resell, for the resale or for other retransfer of exchange notes only as specifically set forth in this prospectus. With regard to broker-dealers, in connection with any resale of the exchange notes, any broker-dealer who acquired the exchange notes for its own account as a result of market-making or other trading activities (a Participating Broker-Dealer) must deliver a prospectus meeting the requirements of the Securities Act. The SEC has taken the position that Participating Broker-Dealers may fulfill their prospectus delivery requirements with respect to the exchange notes, other than a resale of an unsold allotment from the original sale thereof, with the prospectus contained in the exchange offer registration statement. Under the registration rights agreement, to the extent required by the applicable rules of the SEC, we will make this prospectus and any amendment or supplement thereto available to any broker-dealer for use in connection with any resale of any exchange notes for a period of not less than 90 calendar days after the consummation of the exchange offer. Please see Plan of Distribution for more details regarding these procedures for the transfer of exchange notes.

Terms of this Exchange Offer

Upon the terms and subject to the conditions set forth in this prospectus and in the letter of transmittal, we will accept for exchange any old notes properly tendered and not properly withdrawn prior to the expiration date, as defined below. We will issue a like principal amount of exchange notes in exchange for the principal amount of old notes surrendered under this exchange offer. The exchange notes will bear interest from the most recent date to which interest has been paid on the old notes, or if no interest has been paid, from the issue date of the applicable series of old notes. Accordingly, registered holders of exchange notes on the relevant record date for the first interest payment date following the completion of the exchange offer will receive interest accruing from the most recent date to which interest has been paid or, if no interest has been paid, from the issue date of the old notes. Old notes accepted for exchange will cease to accrue interest from and after the date of completion of the exchange offer. Accordingly, holders whose old notes are accepted for exchange will not receive any payment in respect of accrued interest on such old notes otherwise payable on any interest payment date the record date for which occurs on or after completion of the exchange offer. Old notes may be exchanged only in denominations of principal amount of $2,000 and integral multiples of $1,000 in excess thereof.

The form and terms of the exchange notes will be substantially identical to the form and terms of the old notes except the exchange notes will be registered under the Securities Act, will not bear legends restricting their transfer, will not be subject to the registration rights relating to the old notes and will not provide for any additional interest upon our failure to fulfill our obligations under the registration rights agreement to file, and cause to be effective, a registration statement. The exchange notes will evidence the same debt as the old notes. The exchange notes will be issued under and entitled to the benefits of the same indenture that authorized the issuance of the old notes. Consequently, both series will be treated as a single class of debt securities under the applicable indenture.

This exchange offer is not conditioned upon any minimum aggregate principal amount of old notes being tendered for exchange.

This prospectus and the letter of transmittal are being sent to all registered holders of old notes. There will be no fixed record date for determining registered holders of old notes entitled to participate in this exchange offer.

We intend to conduct this exchange offer in accordance with the provisions of the registration rights agreement, the applicable requirements of the Securities Act and the Securities Exchange Act of 1934, as amended, referred to as the Exchange Act, and the rules and regulations of the SEC. Old notes that are not tendered for exchange in this exchange offer will remain outstanding and continue to accrue interest and will be entitled to the rights and benefits such holders have under the indenture relating to the old notes but will not retain any rights under the registration rights agreement except as specified therein.

We will be deemed to have accepted for exchange properly tendered old notes when we have given oral or written notice of the acceptance to the exchange agent. The exchange agent will act as agent for the tendering holders for the purposes of receiving the exchange notes from us and delivering exchange notes to such holders.

Subject to the terms of the registration rights agreement, we expressly reserve the right to amend or terminate this exchange offer because of any change in law or in currently prevailing interpretations of the SEC staff, which prevents us from effecting the exchange offer with respect to a series of notes. See Certain Conditions to This Exchange Offer.

Expiration Date; Extensions; Amendments

This exchange offer will expire at 5:00 p.m., New York City time on April 28, 2008, which we refer to as the expiration date, unless, in our sole discretion, we extend it. As soon as practicable after the close of the exchange offer, we will accept for exchange all outstanding old notes properly tendered and not validly withdrawn prior to 5:00 p.m., New York City time, on the expiration date in accordance with the terms of this prospectus and the letter of transmittal.

In order to extend this exchange offer, we will notify the exchange agent in writing of any extension of the expiration date. We will notify each registered holder of old notes by making a public announcement or by press release of any extension no later than 9:00 a.m., New York City time, on the business day after the previously scheduled expiration date.

We reserve the right, in our sole discretion:

- to delay accepting for exchange any old notes;
- to extend this exchange offer;
- to terminate this exchange offer because of any change in law or in currently prevailing interpretations of the SEC staff which prevents us from effecting the exchange offer with respect to a series of notes; or
- subject to the terms of the registration rights agreement, to amend the terms of this exchange offer in any manner.

We will promptly notify the exchange agent and the registered holders of the old notes of any delay in acceptance, extension, termination or amendment by written notice or by public announcement. During any extension, all old notes previously tendered will remain subject to this exchange offer, and we may accept them for exchange unless they have been previously withdrawn. We will return any old notes that we do not accept for exchange for any reason without expense to their tendering holder promptly after the expiration or termination of this exchange offer.

If we amend this exchange offer in a manner that we determine to constitute a material change, including the waiver of a material condition, we will promptly disclose such amendment in a manner reasonably calculated to inform the holders of old notes of such amendment and will extend this exchange offer to the extent required by law, if necessary. Generally we must keep this exchange offer open for at least five business days after a material change.

Without limiting the manner in which we may choose to make public announcements of any delay in acceptance, extension, termination or amendment of this exchange offer, we shall have no obligation to publish, advertise, or otherwise communicate any such public announcement, other than by issuing a timely press release to a financial news service.

Certain Conditions to This Exchange Offer

Despite any other term of this exchange offer, we will not be required to accept for exchange, or exchange any exchange notes for, any old notes, and we may terminate or amend this exchange offer as provided in this prospectus before accepting any old notes for exchange if this exchange offer, or the making of any exchange by a holder of old notes, would violate applicable law or any applicable interpretation of the SEC staff. This condition is for our sole benefit and may be asserted by us regardless of the circumstances giving rise to it. Our failure at any time to exercise the foregoing right shall not be deemed a waiver of such right, and such right shall be deemed an ongoing right that may be asserted at any time and from time to time.

In addition, we will not accept for exchange any old notes tendered, and will not issue exchange notes in exchange for any such old notes, if at such time any stop order will be threatened or in effect with respect to the registration statement of which this prospectus is a part or the qualification of the applicable indenture under the Trust Indenture Act of 1939, as amended.

Procedures for Tendering Old Notes

Only a holder of old notes may tender such old notes in this exchange offer. To tender in this exchange offer, a holder must:

- complete, sign and date the letter of transmittal, or a copy of the letter of transmittal; have the signature on the letter of transmittal guaranteed if the letter of transmittal so requires; and mail or deliver such letter of transmittal or copy to the exchange agent prior to the expiration date; or

- comply with DTC s Automated Tender Offer Program procedures described below.

In addition, either:

- the exchange agent must receive the tendering holder s old notes along with the letter of transmittal;

- the exchange agent must receive, prior to the expiration date, a timely confirmation of book-entry transfer of such old notes into the exchange agent s account at DTC according to the procedures for book-entry transfer described below or a properly transmitted agent s message (as defined below); or

- the holder must comply with the guaranteed delivery procedures described below.

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To be tendered effectively, the exchange agent must receive any physical delivery of the letter of transmittal and other required documents at the appropriate address set forth below under Exchange Agent prior to the expiration date.

The tender by a holder that is not withdrawn prior to the expiration date will constitute an agreement between such holder and us in accordance with the terms and subject to the conditions set forth in this prospectus and in the letter of transmittal.

The method of delivery of old notes, the letter of transmittal and all other required documents to the exchange agent is at the holder s election and risk. Rather than mail these items, we recommend that holders use an overnight or hand delivery service. In all cases, holders should allow sufficient time to assure delivery to the exchange agent before the expiration date. Holders should not send us the letter of transmittal or old notes. Holders may request their respective brokers, dealers, commercial banks, trust companies or other nominees to effect the above transactions for them.

Any beneficial owner whose old notes are registered in the name of a broker, dealer, commercial bank, trust company or other nominee and who wishes to tender should contact the registered holder promptly and instruct it to tender on such beneficial owner s behalf. If such beneficial owner wishes to tender on its own behalf, it must, prior to completing and executing the letter of transmittal and delivering its old notes, either:

- make appropriate arrangements to register ownership of the old notes in such beneficial owner s name; or

- obtain a properly completed bond power from the registered holder of the old notes.

The transfer of registered ownership may take considerable time and may not be completed prior to the expiration date.

Signatures on a letter of transmittal or a notice of withdrawal described below must be guaranteed by a member firm of a registered national securities exchange or of the Financial Industry Regulatory Authority Inc., a commercial bank or trust company having an office or correspondent in the United States or another eligible institution within the meaning of Rule 17Ad-15 under the Exchange Act (each referred to as an eligible institution), unless the old notes tendered pursuant thereto are tendered:

- by a registered holder who has not completed the box entitled Special Issuance Instructions or Special Delivery Instructions on the letter of transmittal; or

- for the account of an eligible institution.

If the letter of transmittal with respect to any old notes is signed by a person other than the registered holder of such old notes, such old notes must be endorsed or accompanied by a properly completed bond power. The bond power must be properly signed by the registered holder and an eligible institution must guarantee the signature on the bond power.

If the letter of transmittal or any old notes or bond powers are signed by trustees, executors, administrators, guardians, attorneys-in-fact, officers of corporations or others acting in a fiduciary or representative capacity, such persons should so indicate when signing. Unless waived by us, they should also submit evidence satisfactory to us of their authority to deliver the letter of transmittal.

The exchange agent and DTC have confirmed that any financial institution that is a participant in DTC s system may use DTC s Automated Tender Offer Program to tender. Participants in the program may, instead of physically completing and signing the letter of transmittal and delivering it to the exchange agent, transmit their acceptance of this exchange offer electronically. They may do so by causing DTC to transfer the old notes to the exchange agent in accordance with its procedures for transfer. DTC will then send an agent s message to the

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exchange agent. The term agent s message means a message transmitted by DTC, received by the exchange agent and forming part of the book-entry confirmation, to the effect that:

- DTC has received an express acknowledgment from a participant in its Automated Tender Offer Program that is tendering old notes that are the subject of such book-entry confirmation;
- such participant has received and agrees to be bound by the terms of the letter of transmittal (or, in the case of an agent s message relating to guaranteed delivery, that such participant has received and agrees to be bound by the applicable notice of guaranteed delivery); and
- the agreement may be enforced against such participant.

By signing or agreeing to be bound by the letter of transmittal, each tendering holder of old notes will represent, among other things:

- that it is not an affiliate of ours or if it is such an affiliate, such holder will comply with the registration and prospectus delivery requirements of the Securities Act to the extent applicable;
- the exchange notes will be acquired in the ordinary course of its business;
- at the time of the exchange offer, it has no arrangement with any person to participate in the distribution (within the meaning of the Securities Act) of the old notes or the exchange notes; and
- if such holder is a broker-dealer that will receive exchange notes for its own account in exchange for old notes that were acquired as a result of market making or other trading activities, that it will deliver a prospectus (or to the extent permitted by law, make available a prospectus to purchasers) in connection with any resale of such exchange notes.

We will determine in our sole discretion all questions as to the validity, form, eligibility (including time of receipt), acceptance of tendered old notes and withdrawal of tendered old notes. Our determination will be final and binding. We reserve the absolute right to reject any old notes not properly tendered or any old notes the acceptance of which would, in our opinion or the opinion of our counsel, be unlawful. We also reserve the right to waive any defects, irregularities or conditions of tender as to any old notes. Our interpretation of the terms and conditions of this exchange offer (including the instructions in the letter of transmittal) will be final and binding on all parties. Unless waived, any defects or irregularities in connection with tenders of old notes must be cured within such time as we shall determine. Although we intend to notify holders of defects or irregularities with respect to tenders of old notes, neither we, the exchange agent nor any other person will incur any liability for failure to give such notification. Tenders of old notes will not be deemed made until such defects or irregularities have been cured or waived. Any old notes received by the exchange agent that are not properly tendered and as to which the defects or irregularities have not been cured or waived will be returned to the exchange agent without cost to the tendering holder, unless otherwise provided in the letter of transmittal, promptly following the expiration date.

Book-entry Transfer

The exchange agent will make a request to establish an account with respect to the old notes at DTC for purposes of this exchange offer promptly after the date of this prospectus, and any financial institution participating in DTC s system may make book-entry delivery of old notes by causing DTC to transfer such old notes into the exchange agent s account at DTC in accordance with DTC s procedures for transfer. Holders of old notes who are unable to deliver confirmation of the book-entry tender of their old notes into the exchange agent s account at DTC or all other documents of transmittal to the exchange agent on or prior to the expiration date must tender their old notes according to the guaranteed delivery procedures described below.

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Guaranteed Delivery Procedures

Holders wishing to tender their old notes but whose old notes are not immediately available or who cannot deliver their old notes, the letter of transmittal or any other required documents to the exchange agent or comply with the applicable procedures under DTC s Automated Tender Offer Program prior to the expiration date may tender if:

- the tender is made through an eligible institution;
- on or prior to the expiration date, the exchange agent receives from such eligible institution either a properly completed and duly executed notice of guaranteed delivery by facsimile transmission, mail, overnight courier or hand delivery or a properly transmitted agent s message and notice of guaranteed delivery:
  - setting forth the name and address of the holder, the registered number(s) of such old notes and the principal amount of old notes tendered;
  - stating that the tender is being made thereby; and
  - guaranteeing that, within three New York Stock Exchange trading days after the expiration date, the letter of transmittal or facsimile thereof together with the old notes or a book-entry confirmation, and any other documents required by the letter of transmittal will be deposited by the eligible institution with the exchange agent; and
- the exchange agent receives such properly completed and executed letter of transmittal or facsimile thereof, as well as all tendered old notes in proper form for transfer or a book-entry confirmation, and all other documents required by the letter of transmittal, within three New York Stock Exchange trading days after the expiration date.

Upon request to the exchange agent, a notice of guaranteed delivery will be sent to holders who wish to tender their old notes according to the guaranteed delivery procedures set forth above.

Withdrawal of Tenders

Except as otherwise provided in this prospectus, holders of old notes may withdraw their tenders at any time prior to the expiration date.

For a withdrawal to be effective:

- the exchange agent must receive a written notice, which notice may be by telegram, telex, facsimile transmission or letter of withdrawal at the appropriate address set forth below under Exchange Agent, or
- holders must comply with the appropriate procedures of DTC s Automated Tender Offer Program.

Any such notice of withdrawal must:

- specify the name of the person who tendered the old notes to be withdrawn;

- identify the old notes to be withdrawn, including the principal amount of such old notes; and

- where certificates for old notes have been transmitted, specify the name in which such old notes were registered, if different from that of the withdrawing holder.

If certificates for old notes have been delivered or otherwise identified to the exchange agent, then, prior to the release of such certificates, the withdrawing holder must submit:

- the serial numbers of the specific certificates to be withdrawn; and

- a signed notice of withdrawal as set forth above with signatures guaranteed by an eligible institution unless such holder is an eligible institution.

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If old notes have been tendered pursuant to the procedure for book-entry transfer described above, any notice of withdrawal must specify the name and number of the account at DTC to be credited with the withdrawn old notes and otherwise comply with the procedures of such facility. We will determine all questions as to the validity, form and eligibility, including time of receipt, of such notices, and our determination shall be final and binding on all parties. We will deem any old notes so withdrawn not to have been validly tendered for exchange for purposes of this exchange offer. Any old notes that have been tendered for exchange but that are not exchanged for any reason will be returned to their holder without cost to the holder (or, in the case of old notes tendered by book-entry transfer into the exchange agent s account at DTC according to the procedures described above, such old notes will be credited to an account maintained with DTC for old notes) as soon as practicable after withdrawal, rejection of tender or termination of this exchange offer. Properly withdrawn old notes may be retendered by following one of the procedures described under Procedures for Tendering Old Notes above at any time on or prior to the expiration date.

Exchange Agent

U.S. Bank National Association has been appointed as exchange agent for this exchange offer. You should direct questions and requests for assistance, requests for additional copies of this prospectus or of the letter of transmittal and requests for the notice of guaranteed delivery to the exchange agent, addressed as follows:

By Overnight Delivery, Registered or Certified Mail:

U.S. Bank National Association

West Side Flats Operations Center

Attn: Specialized Finance Offer

60 Livingston Avenue

Mail Station EP-MN WS2N

St. Paul, MN 55107-2292

By Facsimile Transmission:

(651) 495 8158

By Hand:

U.S. Bank National Association

West Side Flats Operations Center

Attn: Specialized Finance Offer

60 Livingston Avenue

Bond Drop Window

St. Paul, MN 55107-2292

For informational requests:

(651) 495 3511

Delivery of the letter of transmittal to an address other than as set forth above or transmission via facsimile other than as set forth above will not constitute a valid delivery of such letter of transmittal.

Fees and Expenses

We will not make any payments to brokers, dealers or others soliciting acceptances of this exchange offer. The principal solicitation is being made by mail; however, additional solicitations may be made by telephone or in person by our officers and employees and those of our affiliates.

Except for certain expenses incurred in connection with a shelf registration statement, expenses incurred in connection with the exchange offer will be paid by us. Such expenses include, among others, SEC registration fees, the fees and expenses of the trustee and the exchange agent, accounting and legal fees, printing costs and other related fees and expenses. In the event that we are required to file a shelf registration statement, the holders who tender old notes pursuant to a shelf registration statement shall pay all underwriting discounts and commissions, brokerage commissions and transfer taxes, if any, with respect to such sale or disposition of old notes.

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Transfer Taxes

Except for transfer taxes incurred in connection with sales pursuant to a shelf registration statement and as described below, we will pay any transfer taxes applicable to the exchange of old notes under this exchange offer. Holders of old notes who tender their old notes for exchange notes will not be obligated to pay any transfer taxes in connection therewith, except that holders who instruct us to register exchange notes in the name of, or request that old notes not tendered or not accepted in the exchange offer be returned to, a person other than the registered tendering holder will be responsible for the payment of any applicable transfer tax thereon. In these cases, if satisfactory evidence of payment of such taxes is not submitted with the letter of transmittal, the amount of such transfer taxes will be billed to that tendering holder.

Consequence of Failure to Exchange

Holders of old notes who do not exchange their old notes for exchange notes under this exchange offer will remain subject to the restrictions on transfer of such old notes as set forth in the legend printed on the old notes as a consequence of the issuance of the old notes pursuant to exemptions from, or in transactions not subject to, the registration requirements of the Securities Act and applicable state securities laws. In general, you may not offer or sell the old notes unless they are registered under the Securities Act, or if the offer or sale is exempt from registration under the Securities Act and applicable state securities laws. Except as required by the registration rights agreement, we do not intend to register resales of the old notes under the Securities Act.

Other

Participation in this exchange offer is voluntary, and holders of old notes should carefully consider whether to accept. Holders of old notes are urged to consult their financial and tax advisors in making their own decision on what action to take.

We may in the future seek to acquire untendered old notes in the open market or privately negotiated transactions, through subsequent exchange offers or otherwise. We have no present plans to acquire any old notes that are not tendered in this exchange offer or to file a registration statement to permit resales of any untendered old notes.

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USE OF PROCEEDS

We will not receive any cash proceeds from the issuance of the exchange notes. In consideration for issuing the exchange notes as contemplated in this prospectus, we will receive in exchange old notes in like principal amount, which will be canceled and as such will not result in any increase in our indebtedness. The net proceeds from the 6.450% Senior Notes due 2017 and the Floating Rate Senior Notes due 2010 were used to repay intercompany lending from Morgan Stanley and for general corporate purposes.

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CAPITALIZATION

The following table sets forth our cash and cash equivalents and our capitalization on a consolidated basis as of November 30, 2007. You should read this table together with Selected Historical Consolidated and Combined Data, Management s Discussion and Analysis of Financial Condition and Results of Operations, Unaudited Pro Forma Condensed Consolidated and Combined Financial Statements and our historical financial statements and the notes to those statements included elsewhere in this prospectus.

	As of November 30, 2007 (dollars in millions)
Cash and cash equivalents	$ 8,787
Long-term borrowings:	
6.450% Senior Notes due 2017	$ 399
Floating Rate Senior Notes due 2010	400
Other long-term borrowings	1,335
Total long-term borrowings	2,134
Stockholders equity:	
Preferred stock	
Common stock	5
Additional paid-in capital	2,846
Retained earnings	2,718
Accumulated other comprehensive income	32
Treasury stock, at cost	(2)
Total stockholders equity	5,599
Total capitalization	$ 7,733

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UNAUDITED PRO FORMA CONDENSED CONSOLIDATED AND

COMBINED FINANCIAL STATEMENTS

Our unaudited pro forma condensed consolidated and combined financial statements presented below have been derived from our audited consolidated and combined financial statements as of and for the year ended November 30, 2007. The pro forma adjustments and notes to the unaudited pro forma condensed consolidated and combined statement of income give effect to (i) the distribution of our common stock by Morgan Stanley and the other transactions contemplated by the separation and distribution agreement (the Distribution) and (ii) the expected sale of our International Card segment (the U.K. Sale). The pro forma adjustments and notes to the unaudited pro forma condensed consolidated statement of financial condition give effect to the proposed U.K. Sale. The unaudited pro forma condensed consolidated and combined financial statements should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our audited consolidated and combined financial statements and the notes to those statements included elsewhere in this prospectus.

Our unaudited pro forma condensed consolidated and combined statement of income as of and for the year ended November 30, 2007 has been prepared as though the Distribution and proposed U.K. Sale had occurred as of December 1, 2006. The unaudited pro forma condensed consolidated statement of financial condition has been prepared as though the proposed U.K. Sale had occurred on November 30, 2007. The pro forma adjustments are based upon available information and assumptions that management believes are reasonable, that reflect the expected impacts of events that are directly attributable to the Distribution as well as the proposed U.K. Sale, and that are factually supportable and expected to have a continuing impact on us. Such adjustments are estimates and may not prove to be accurate.

Prior to our spin-off, Morgan Stanley provided portions of certain corporate functions on our behalf and allocated these costs to us. As a stand-alone public company, and as a direct result of our separation from Morgan Stanley, we incrementally incur expenses in respect of these functions. Such functions include but are not limited to corporate communications, community affairs, government relations, human resources and benefit management, company management functions, treasury, investor relations, internal audit, business technology and corporate legal and compliance. Morgan Stanley has agreed to provide certain of these services to us on a transitional basis, primarily during the first year following the Distribution. The annual costs associated with replacing these functions and establishing our own infrastructure related thereto, which we estimate subject to finalization of our plans to be approximately $60 million, have not been reflected in the unaudited pro forma condensed combined statements of income presented below. Prior to the spin-off, we also incurred expenses in the form of corporate allocations from Morgan Stanley for the corporate functions they provided to us that will not recur after the distribution. The total amount of these allocations from Morgan Stanley was approximately $52 million for the year ended November 30, 2007. The net reduction in expenses associated with replacing these functions and establishing our own infrastructure related thereto have not been reflected in the unaudited pro forma condensed combined statements of income presented below. This net reduction in expenses is not expected to be realized until the transition is complete. During the transition, expenses will be greater than historical levels, reflecting transition related expenses.

The pro forma adjustments related to the Distribution include the following items:

- compensation expenses related to equity awards granted under Discover s Omnibus Incentive and Directors Compensation plans;

- the costs related to replacement of intercompany debt payable to Morgan Stanley with deposits and other funding sourced by us; and

- the costs related to additional liquidity sources in conjunction with our liquidity and funding policies to replace liquidity previously sourced by Morgan Stanley. These sources will provide us with liquidity to satisfy the necessary regulatory, rating agency and contingency funding requirements.

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On February 7, 2008 we entered into a definitive sale and purchase agreement with Barclays Bank Plc relating to the sale of £129 million of net assets (equivalent to approximately $258 million) of our U.K. credit card business, which represented substantially all of our International Card segment. The aggregate sale price under the agreement is £35 million (equivalent to approximately $70 million), payable in cash at closing and subject to a post-closing adjustment. The closing is expected to occur by the end of our second quarter of 2008. The sale is subject to the satisfaction of a number of conditions, including clearance from the U.K. Office of Fair Trading, a minimum value of receivables to be transferred and consents under material contracts. There can be no assurance that the sale will occur by the end of the second quarter of 2008, if at all.

The pro forma adjustments related to the U.K. Sale include the following items:

- removal of assets and liabilities of the U.K. credit card business, including intercompany debt;
- the proceeds of the sale and related transaction costs; and
- removal of results of operations of the U.K. credit card business.

The unaudited pro forma condensed consolidated and combined financial statements are provided for illustrative and informational purposes only and do not reflect what our consolidated and combined financial condition and results of operations would have been had the Distribution and/or proposed U.K. Sale occurred at the beginning of all periods presented and are not necessarily indicative of our future financial condition and future results of operations.

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Discover Financial Services

Unaudited Pro Forma Condensed Consolidated Statement of Financial Condition

November 30, 2007	Actual	Pro Forma Adjustments for the U.K. Sale	Pro Forma
		(dollars in millions)	
Assets			
Cash and cash equivalents	$ 8,787	$ (161)[a]	$ 8,686
		70[b]	
		(10)[c]	
Investment securities	525		525
Loan receivables	23,954	(3,123)[a]	20,831
Allowance for loan losses	(917)	157[a]	(760)
Net loan receivables	23,037	(2,966)	20,071
Amounts due from asset securitization	3,093	(52)[a]	3,041
Other assets	1,934	(161)[a]	1,773
Total assets	$ 37,376	$ (3,280)	$ 34,096
Liabilities and Stockholders Equity			
Deposits	$ 24,725	$ (14)[a]	$ 24,711
Short-term borrowings	3,175	(2,925)[a]	250
Long-term borrowings	2,134		2,134
Accrued expenses and other liabilities	1,743	(151)[a]	1,592
Total liabilities	31,777	(3,090)	28,687
Stockholders equity	5,599	(190)[d]	5,409
Total liabilities and stockholders equity	$ 37,376	$ (3,280)	$ 34,096

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Discover Financial Services

Unaudited Pro Forma Condensed Consolidated and Combined Statement of Income

For the Year Ended November 30, 2007	Actual	Pro Forma Adjustments Distribution[e]	Pro Forma Adjustments U.K. Sale[a]	Pro Forma
		(dollars in millions, except per share amounts)		
Interest income	$ 2,888	$ 61[f]	$ (304)	$ 2,645
Interest expense:				
Deposits	1,045	100[g]		1,145
Short-term borrowings	232	(123)[h]	(75)	15
		(19)[i]		
		85[j]	(85)	
Total short-term borrowings	232	(57)	(160)	15
Long-term borrowings	105	(31)[k]		143
		28[l]		
		41[m]		
Total long-term borrowings	105	38		143
Total interest expense	1,382	81	(160)	1,303
Net interest income	1,506	(20)	(144)	1,342
Provision for loan losses	950		(216)	734
Net interest income after provision for loan losses	556	(20)	72	608
Other income	3,546		(169)	3,377
Other expense	3,157	12[n]	(682)	2,491
		4[o]		
Income from continuing operations before income tax expense	945	(36)	585	1,494
Income tax expense	356	(13)[p]	211	554
Net income from continuing operations	$ 589	$ (23)	$ 374	$ 940
Earnings per share				
Basic	$ 1.23	$ (0.05)	$ 0.79	$ 1.97
Diluted	$ 1.23	$ (0.05)	$ 0.78	$ 1.96
Weighted average shares outstanding (000s)				
Basic	477,328			477,328
Diluted	478,879			478,879

Notes to Unaudited Pro Forma Condensed Consolidated and Combined Financial Statements

(a) Represents the removal of the International Card segment from continuing operations of the Company to reflect the proposed U.K. Sale.

(b) Represents proceeds from the proposed U.K. Sale.

(c) Represents legal and broker fees related to the proposed U.K. Sale.

(d) Represents loss on the proposed U.K. Sale.

(e) All Distribution adjustments are through June 30, 2007, the date of our spin-off from Morgan Stanley.

(f) Represents incremental interest income on a targeted minimum balance in our liquidity reserve of $5.0 billion, funded principally by interest-bearing deposits at an interest rate of approximately 5.2% estimated using the Federal Funds rate minus 10 basis points. The impact on interest income from a $^{1}/_{8}$ of 1% change in interest rates is approximately $1.5 million.

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(g) Represents incremental interest expense on additional deposits sourced by us principally to provide funding to establish a minimum of a $5.0 billion liquidity reserve, replace externally sourced Federal Funds and amounts payable to Morgan Stanley. Interest expense on these deposits reflects an interest rate of approximately 5.5% estimated using 2-year brokered deposit rate swapped to a 3-month LIBOR floating rate basis and using a sweep deposit rate equal to the Federal Funds rate plus 20 basis points. The impact on interest expense associated with these deposits from a $^{1}/_{8}$ of 1% change in interest rates is approximately $4.1 million.

(h) Represents the elimination of interest expense on short-term borrowings from Morgan Stanley composed of inter-company loans and Morgan Stanley Bank Federal Funds purchased, which carried an average interest rate of approximately 5.4%.

(i) Represents the elimination of interest expense on externally sourced Federal Funds, which carried an average interest rate of approximately 5.4%.

(j) Represents interest expense related to the execution of new secured borrowing arrangements established to finance receivables previously funded through both short-term borrowings and long-term debt sourced by Morgan Stanley. Incremental interest expense on this financing reflects a rate of approximately 6.2% estimated using secured financing pricing of 1-month LIBOR plus 88 basis points. The impact on interest expense associated with these borrowing arrangements from a 1/8 of 1% change in interest rates is approximately $1.8 million.

(k) Represents the elimination interest expense related to long-term Morgan Stanley inter-company funding, which carried an average interest of approximately 5.3%.

(l) Represents the interest expense related to incremental long-term funding, sourced by us through the 6.450% Senior Notes due 2017 and the Floating Rate Senior Notes due 2010 to replace a portion of long-term inter-company funding previously sourced by Morgan Stanley at an interest rate of approximately 6.1% estimated using pricing from unsecured debt issuance executed June 2007. The impact on interest expense associated with this long-term debt from a 1/8 of 1% change in interest rates is approximately $0.7 million.

(m) Represents interest expense related to new secured borrowing arrangements established by us to finance the loans from the cash collateral accounts, used as credit enhancement for the securitization program and previously funded through short-term borrowings sourced by Morgan Stanley. Incremental interest expense on this financing reflects a rate of approximately 5.9% estimated using pricing from a secured borrowing transaction in June 2007 priced at one-month LIBOR plus 54 basis points. The impact on interest expense associated with these borrowing arrangements from a 1/8 of 1% change in interest rates is approximately $0.9 million.

(n) Represents an estimated $12 million of incremental compensation expense related to earned benefit from equity awards granted under Discover s Omnibus Incentive and Directors Compensation plans. The earned benefit estimates were derived based on plan vesting schedules and include accelerated expense recognition reflecting timing of award vesting and upfront recognition for employees qualifying as fully vested under plan guidelines.

(o) Represents an estimated $4 million of incremental fees and expenses associated with establishing a new unsecured bank facility and asset-backed commercial paper conduit facilities.

(p) Pro forma effective state tax rate has been increased from 1.8% to 2.3% to reflect additional state tax liability as a consequence of not being combined with Morgan Stanley. Income tax has been adjusted for a revaluation of the net deferred state income tax asset to reflect the higher rate.

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SELECTED HISTORICAL CONSOLIDATED AND COMBINED DATA

The following table presents our selected historical financial data and operating statistics. The statement of income data for each of the years in the three-year period ended November 30, 2007 and the statement of financial condition data as of November 30, 2007 and 2006 have been derived from our audited consolidated and combined financial statements included elsewhere in this prospectus. The statement of income data for the years ended November 30, 2004 and 2003 and the statement of financial condition data as of November 30, 2005, 2004 and 2003 are derived from the audited and unaudited combined financial statements not included elsewhere in this prospectus. The unaudited financial statements have been prepared on the same basis as the audited financial statements, and in the opinion of our management include all adjustments, consisting of only ordinary recurring adjustments, necessary for a fair presentation of the information set forth in this prospectus.

The selected historical financial data and operating statistics presented below should be read in conjunction with our audited consolidated and combined financial statements and accompanying notes and Management s Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this prospectus. The combined financial information may not be indicative of our future performance and does not necessarily reflect what the financial position and results of operations would have been had we operated as a separate, stand-alone entity during the periods presented, including changes that occurred in our operations and capitalization as a result of our spin-off from Morgan Stanley. On March 19, 2008, we announced unaudited financial results for the quarter ended February 29, 2008. See Management s Discussion and Analysis of Financial Condition and Results of Operations Recent Developments.

Included in the selected historical financial data are certain amounts and statistics reported on a managed basis. Our senior management evaluates business performance and allocates resources using financial data that is presented on a managed basis. Managed loans consist of our on-balance sheet loan portfolio, loans held for sale and loan receivables that have been securitized and against which beneficial interests have been issued. Owned loans, a subset of managed loans, refer to our on-balance sheet loan portfolio and loans held for sale and include the undivided seller s interest we retain in our securitizations. A managed basis presentation, which is not a presentation in accordance with GAAP, involves reporting securitized loans with our owned loans in the managed basis statements of financial condition and reporting the earnings on securitized loans in the same manner as the owned loans instead of as securitization income. See Management s Discussion and Analysis of Financial Condition and Results of Operations GAAP to Managed Data Reconciliations.

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Discover Financial Services

Selected Historical Data

	For the Years Ended November 30,				
	2007	2006	2005	2004	2003
	(dollars in thousands, except per share amounts)				
Statement of Income Data:					
Interest income	$ 2,888,169	$ 2,458,526	$ 2,174,811	$ 1,859,504	$ 2,048,695
Interest expense	1,382,415	940,040	776,479	647,622	789,667
Net interest income	1,505,754	1,518,486	1,398,332	1,211,882	1,259,028
Other income	3,546,119	3,538,939	2,937,037	3,248,386	3,313,478
Revenue net of interest expense	5,051,873	5,057,425	4,335,369	4,460,268	4,572,506
Provision for loan losses	950,165	755,637	878,486	925,549	1,266,113
Other expense[1]	3,156,512	2,719,483	2,532,627	2,315,812	2,279,485
Income before income tax expense[1]	945,196	1,582,305	924,256	1,218,907	1,026,908
Income tax expense[1]	356,566	505,689	346,341	442,654	378,277
Net income[1]	$ 588,630	$ 1,076,616	$ 577,915	$ 776,253	$ 648,631
Statement of Financial Condition Data (as of):					
Loan receivables	$ 23,954,295	$ 23,742,750	$ 22,803,166	$ 20,129,415	$ 19,379,086
Total assets	$ 37,376,105	$ 29,067,242	$ 26,943,923	$ 24,122,009	$ 24,032,743
Total stockholders equity	$ 5,599,422	$ 5,774,772	$ 4,600,449	$ 4,021,349	$ 3,809,285
Allowance for loan losses	$ 916,844	$ 832,483	$ 838,848	$ 942,721	$ 1,001,656
Long-term borrowings	$ 2,134,093	$ 1,507,578	$ 863,745	$ 1,198,406	$ 931,554
Total average interest-earning assets	$ 31,651,619	$ 25,546,145	$ 23,783,731	$ 20,627,761	$ 22,862,081
Total average interest-bearing liabilities	$ 25,897,063	$ 19,830,983	$ 18,656,289	$ 15,717,897	$ 17,802,398
Per Common Share:					
Basic EPS[1]	$ 1.23	$ 2.26	$ 1.21	$ 1.63	$ 1.36
Diluted EPS[1]	$ 1.23	$ 2.26	$ 1.21	$ 1.63	$ 1.36
Weighted average shares outstanding (000 s)[2]	477,328	477,236	477,236	477,236	477,236
Weighted average shares outstanding (fully diluted) (000 s)[2]	478,879	477,236	477,236	477,236	477,236
Cash dividends	$ 0.06				
Dividend payout ratio	4.88%				
Ratios:					
Ratio of earnings to fixed charges[3]	1.7	2.7	2.2	2.9	2.3
Net interest margin	4.76%	5.94%	5.88%	5.88%	5.51%
Return on average equity[1]	10%	20%	13%	18%	14%
Return on average assets[1]	1.73%	3.93%	2.29%	3.54%	2.68%
Average stockholders equity to average total assets	17%	21%	18%	20%	19%
Selected Statistics:					
Total Credit Card Loans					
Credit card loans owned	$ 23,703,101	$ 23,646,901	$ 22,496,211	$ 19,723,758	$ 18,929,973
Average credit card loans owned	$ 22,814,043	$ 21,656,295	$ 19,931,636	$ 17,608,445	$ 19,530,515
Owned interest yield	10.58%	10.38%	10.12%	10.05%	10.02%
Owned net principal charge-off rate	3.82%	3.79%	4.84%	5.53%	6.05%
Owned delinquency rate (over 30 days)	3.50%	3.22%	3.69%	4.08%	5.36%
Owned delinquency rate (over 90 days)	1.63%	1.53%	1.62%	1.97%	2.53%
Credit card loans managed	$ 52,302,410	$ 50,350,328	$ 46,936,274	$ 48,261,402	$ 48,357,810
Average credit card loans managed	$ 51,338,135	$ 48,216,546	$ 47,330,143	$ 47,386,940	$ 50,863,666
Managed interest yield	12.44%	12.36%	11.72%	11.84%	11.93%
Managed net principal charge-off rate	4.08%	4.08%	5.23%	6.00%	6.60%
Managed delinquency rate (over 30 days)	3.73%	3.50%	3.98%	4.55%	5.97%
Managed delinquency rate (over 90 days)	1.74%	1.65%	1.75%	2.18%	2.82%

Total Credit Card Volume					
Domestic	$ 106,620,818	$ 102,901,893	$ 98,224,437	$ 94,509,183	$ 93,746,658
International[(4)]	14,254,621	11,881,465	5,907,089	5,077,478	4,128,177
Total	$ 120,875,439	$ 114,783,358	$ 104,131,526	$ 99,586,661	$ 97,874,835

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Discover Financial Services

Selected Historical Data (continued)

	For the Years Ended November 30,				
	2007	2006	2005	2004	2003
	(dollars in thousands)				
Credit Card Sales Volume					
Domestic	$ 90,262,556	$ 86,385,577	$ 81,664,000	$ 76,035,714	$ 73,974,819
International[4]	12,955,968	10,335,331	4,291,675	3,466,893	2,845,322
Total	$ 103,218,524	$ 96,720,908	$ 85,955,675	$ 79,502,607	$ 76,820,141
Other Consumer Loans					
Domestic loan receivables	$ 251,194	$ 95,849	$ 176,329	$ 287,909	$ 404,514
International loan receivables			130,626	117,749	44,600
Total	$ 251,194	$ 95,849	$ 306,955	$ 405,658	$ 449,114
Transactions Processed on Networks (000 s)					
Discover Network	1,486,366	1,399,933	1,301,024	1,226,414	1,208,505
PULSE Network[5]	2,285,061	1,856,477	1,555,782		
Total	3,771,427	3,256,410	2,856,806	1,226,414	1,208,505
Domestic Credit Card Loans					
Credit card loans owned	$ 20,579,923	$ 20,694,395	$ 20,434,977	$ 18,606,211	$ 17,586,884
Average credit card loans owned	$ 19,845,880	$ 19,120,946	$ 18,644,660	$ 16,228,520	$ 17,938,722
Owned interest yield	10.75%	10.50%	10.16%	10.13%	10.15%
Owned net principal charge-off rate	3.41%	3.64%	4.95%	5.75%	6.34%
Owned delinquency rate (over 30 days)	3.28%	3.05%	3.69%	4.19%	5.54%
Owned delinquency rate (over 90 days)	1.53%	1.44%	1.61%	2.03%	2.62%
Credit card loans managed	$ 47,929,242	$ 45,706,222	$ 44,261,121	$ 45,690,728	$ 46,141,977
Average credit card loans managed	$ 46,811,570	$ 44,277,249	$ 44,736,702	$ 45,018,288	$ 48,590,494
Managed interest yield	12.66%	12.53%	11.78%	11.91%	12.05%
Managed net principal charge-off rate	3.84%	3.96%	5.30%	6.12%	6.75%
Managed delinquency rate (over 30 days)	3.59%	3.39%	3.98%	4.65%	6.09%
Managed delinquency rate (over 90 days)	1.68%	1.59%	1.75%	2.24%	2.88%
International Credit Card Loans					
Credit card loans owned[4]	$ 3,123,178	$ 2,952,506	$ 2,061,234	$ 1,117,547	$ 1,343,089
Average credit card loans owned[4]	$ 2,968,163	$ 2,535,349	$ 1,286,976	$ 1,379,925	$ 1,591,793
Owned interest yield	9.42%	9.51%	9.63%	9.13%	8.51%
Owned net principal charge-off rate	6.56%	4.94%	3.28%	2.94%	2.80%
Owned delinquency rate (over 30 days)	4.91%	4.36%	3.78%	2.23%	2.93%
Owned delinquency rate (over 90 days)	2.27%	2.16%	1.73%	0.96%	1.41%
Credit card loans managed[4]	$ 4,373,168	$ 4,644,106	$ 2,675,153	$ 2,570,674	$ 2,215,833
Average credit card loans managed[4]	$ 4,526,565	$ 3,939,297	$ 2,593,441	$ 2,368,652	$ 2,273,172
Managed interest yield	10.11%	10.38%	10.72%	10.62%	9.44%
Managed net principal charge-off rate	6.54%	5.45%	4.10%	3.87%	3.44%
Managed delinquency rate (over 30 days)	5.25%	4.58%	3.95%	2.78%	3.29%
Managed delinquency rate (over 90 days)	2.43%	2.22%	1.81%	1.22%	1.60%

(1) 2007 includes a $391 million pretax ($279 million after tax) non-cash impairment charge related to our International Card segment.

(2) On June 30, 2007, the distribution by Morgan Stanley was completed to the Morgan Stanley stockholders of one share of Discover Financial Services common stock for every two shares of Morgan Stanley common stock held on June 18, 2007 (the Distribution). As a result, on July 2, 2007, Discover had 477,235,927 shares of common stock outstanding and this share amount is being utilized for the calculation of basic EPS for all periods presented prior to the

date of Distribution. For all periods prior to the date of Distribution, the same number of shares is being used for diluted EPS as for basic EPS as no common stock of Discover Financial Services was traded prior to July 2, 2007 and no Discover equity awards were outstanding for the prior periods.

(3) For purposes of calculating the ratio of earnings to fixed charges, earnings represent income before income taxes, fixed charges and losses from unconsolidated investees. Fixed charges consist of interest expense and an estimated interest portion of rental expense.

(4) The Goldfish and Liverpool Victoria portfolios were acquired in 2006.

(5) PULSE was acquired in January 2005.

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MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our audited consolidated and combined financial statements and related notes included elsewhere in this prospectus. Some of the information contained in this discussion and analysis constitutes forward-looking statements that involve risks and uncertainties. Actual results could differ materially from those discussed in these forward-looking statements. Factors that could cause or contribute to these differences include, but are not limited to, those discussed below and elsewhere in this prospectus particularly under Forward-Looking Statements and Risk Factors.

Unless otherwise specified, references to Notes to the audited consolidated and combined financial statements are to the Notes to our audited consolidated and combined financial statements as of November 30, 2007 and 2006 and for the three-year period ended November 30, 2007.

Introduction and Overview

We are a leading credit card issuer and electronic payment services company with one of the most recognized brands in U.S. financial services. We offer credit and prepaid cards and other financial products and services to qualified customers in the United States and the United Kingdom, and provide payment processing and related services to merchants and financial institutions in the United States. Our year ends on November 30 of each year.

We strive to increase net income and achieve other business objectives by growing loan receivables and increasing volume on our payments networks to generate interest and fee revenue, while controlling loan losses and expenses. Our primary revenues come from interest income earned on loan receivables, securitization income derived from the transfer of credit card loan receivables and subsequent issuance of beneficial interests through securitization transactions, and fees earned from cardmembers, merchants and issuers. Our primary expenses include funding costs (interest expense), loan losses, cardmember rewards and expenses incurred to grow and service our loan receivables (e.g., compensation expense and marketing).

We are actively pursuing a strategy to increase acceptance of Discover Network cards among small and mid-size merchants. We have entered into arrangements with major merchant acquirers to sign new and service existing small and mid-size merchants for acceptance of Discover Network cards.

We undertook a number of initiatives in an effort to restore profitability to our U.K. operations over the long term and offset the impact of higher loan losses and lower interchange and fee revenues. These initiatives included insourcing of our processing platform, consolidation of our operational centers, reductions in staffing and achieving procurement efficiencies. In addition, we revised certain risk policies, modified pricing for portions of the portfolio, implemented annual fees for certain customers, introduced new fee products and modified certain transaction based fees. On February 7, 2008, we announced that we had entered into a definitive sale and purchase agreement to sell our U.K. credit card business, which represents substantially all of the International Card segment, to Barclay s Bank Plc. See Recent Developments Sale of the International Card Segment below for further discussion.

Our business activities have been funded primarily through the process of asset securitization, the raising of consumer deposits, and, prior to the Distribution, intercompany lending from Morgan Stanley which has been replaced with asset-backed financing and both secured and unsecured debt. In a credit card securitization, loan receivables are first transferred to securitization trusts, from which beneficial interests are issued to investors. We continue to own and service the accounts that generate the securitized loans. The trusts utilized by us to facilitate asset securitization transactions are not our subsidiaries and are independent from us. These trusts are excluded from our consolidated and combined financial statements in accordance with GAAP. Because our securitization activities qualify as sales under GAAP and accordingly are not treated as secured financing transactions, we remove credit card loan receivables equal to the amount of the investor interests in securitized loans from the

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consolidated and combined statements of financial condition. As a result, asset securitizations have a significant effect on our consolidated and combined financial statements in that the portions of interest income, provision for loan losses and certain components of other income related to the securitized loans against which beneficial interests have been issued are no longer recorded in our consolidated and combined statements of income; however, they remain significant factors in determining the securitization income we receive on our retained beneficial interests in those transactions. Securitization income is our second most significant revenue category.

Our senior management evaluates business performance and allocates resources using financial data that is presented on a managed basis. Managed loans consist of our on-balance sheet loan portfolio, loans held for sale and loan receivables that have been securitized and against which beneficial interests have been issued. Owned loans, a subset of managed loans, refer to our on-balance sheet loan portfolio and loans held for sale and include the undivided seller s interest we retain in our securitizations. A managed basis presentation, which is a non-GAAP presentation, involves reporting securitized loans with our owned loans in the managed basis statements of financial condition and reporting the earnings on securitized loans in the same manner as the owned loans instead of as securitization income. The managed basis presentation generally reverses the effects of securitization transactions; however, there are certain assets that arise from securitization transactions that are not reversed. Specifically, these assets are the cash collateral accounts that provide credit enhancement to the investors in the transactions and cardmember payments allocated to the securitized loans, both of which are held at the trusts. These assets also include the interest-only strip receivable, reflecting the estimated fair value of the excess cash flows allocated to securitized loans and retained certificated beneficial interests. Income derived from these assets representing interest earned on accounts at the trusts, changes in the fair value of the interest-only strip receivable and interest income on investment securities also are not reversed in a managed presentation.

Management believes it is useful for investors to consider the credit performance of the entire managed loan portfolio to understand the quality of loan originations and the related credit risks inherent in the owned portfolio and retained interests in our securitizations. Managed loan data is also relevant because we service the securitized and owned loans, and the related accounts, in the same manner without regard to ownership of the loans.

Financial measures using managed data are non-GAAP financial measures. Whenever managed data is presented in this prospectus, a reconciliation of the managed data to the most directly comparable GAAP-basis financial measure is provided. See GAAP to Managed Data Reconciliations.

Key Developments Impacting Reported Results

In August 2007, management began a strategic review of the International Card segment. This review, which was completed in the fourth quarter, involved a review of U.K. financing options and costs (particularly given market disruptions), consideration of industry trends in the United Kingdom, the various challenges facing credit card issuers in that market, the impact of certain initiatives we have already undertaken to restore profitability to the segment and the expected impact of additional actions planned in light of these circumstances. As a result of the strategic review, management revised its long-range projections for the International Card segment, and revised its estimate of the segment s fair value. The carrying value of the International Card segment at November 30, 2007 was in excess of its revised estimated fair value, and, as such, we recorded a non-cash impairment charge of $391 million ($279 million after tax) to other expense. The total pretax impairment charge included a $291 million write-down of goodwill and $100 million write-down of other intangible assets.

Certain of our interest-earning assets and interest-bearing liabilities have floating rates which are tied to short-term market indices, such as the Federal Funds rate and LIBOR. During the year ended November 30, 2006, the Federal Reserve increased the Federal Funds target rate by 125 bps to 5.25%. As a result, the yields on interest-earning assets and the costs of floating rate interest-bearing liabilities increased during 2006 and remained at these levels for most of 2007. During this period, the relationship between the Federal Funds rate and LIBOR remained stable.

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During the fourth quarter of 2007, in response to worsening credit conditions, the Federal Reserve decreased the Federal Funds target rate by 75 basis points to 4.50%. During this period, tight credit conditions caused the relationship between the Federal Funds rate and LIBOR to change materially, with LIBOR often remaining significantly higher than the Federal Funds rate. Also, asset-backed commercial paper rates rose and credit spreads widened materially.

Market conditions also reduced the availability of new issuance in certain funding markets. In response to various liquidity events, our senior management increased the size of our liquidity reserve.

In the United Kingdom, disruptions in the financial markets as well as a weakened consumer credit environment have impacted asset-backed securitization issuance, leading us to retain on our balance sheet approximately $500 million of receivables from a maturing asset-backed transaction as of November 30, 2007.

On June 30, 2007, our Distribution from Morgan Stanley became effective. Our results of operations for the year ended November 30, 2007 include costs incurred as a result of the Distribution of approximately $34 million.

New U.S. bankruptcy legislation became effective in October 2005, making it more difficult for consumers to declare bankruptcy. We experienced a surge in bankruptcy receipts leading up to the effective date of this legislation. We charge off bankrupt accounts at the end of the month that is 60 days following the receipt of notification of the bankruptcy, so in the second half of calendar 2005 we experienced higher charge-offs as a result of this legislation. October 2005 was the peak month for bankruptcy receipts during this transition to new legislation. October receipts, in accordance with our policy, were charged off in December 2005.

The results of 2005 were adversely impacted by a higher level of bankruptcy charge-offs, a negative revaluation of the interest-only strip receivable reflecting the impact on projected excess spread of elevated charge-offs in December 2005 and additional provisions to the allowance for loans losses for bankrupt accounts in the portfolio at November 30, 2005. We experienced a dramatic decline in bankruptcy receipts following the effective date of the new U.S. bankruptcy legislation. The results of 2006 benefited from a significantly lower level of bankruptcy charge-offs, a favorable revaluation of the interest-only strip receivable reflecting higher excess spread projections and a decrease in the level of allowance for loan losses. We believe the passing of this legislation negatively impacted 2005 and benefited the overall results of 2006, causing year-over-year comparisons to the year ended November 30, 2007 to be impacted as well. During 2007, we experienced a higher level of bankruptcy charge-offs, although still significantly lower than pre-legislation levels.

Separate from the previously described impact of the surge in bankruptcy receipts, the underlying credit quality of the U.S. loan receivables continued to improve in 2006 and 2005 and remained relatively stable throughout most of 2007. In the fourth quarter of 2007, delinquencies began to rise reflecting the downturn in market conditions.

During 2006 and 2005, certain matters caused our use of certain funding sources, including the U.S. credit card securitization market, to vary from our historical use of this market for funding our business. Following Morgan Stanley s announcement in April 2005 to explore a spin-off of Discover, the counter party credit ratings on Discover Bank were lowered to their current levels. As a result of our lower credit ratings, we lost access to Federal Funds as a significant source of short-term financing, but were able to mitigate the impact by increasing short-term borrowings from Morgan Stanley.

In response to the exploration of the spin-off, Moody s placed the asset-backed securities issued domestically by the Discover Card Master Trust I (DCMT) under review for a possible downgrade, which we believe contributed to a temporary disruption in our ability to access the securitization markets. This disruption lasted approximately five months, at which time Moody s re-affirmed the ratings on the asset-backed securities. This deferral of new securitization transactions, as well as a high

level of maturities of existing securitization transactions and the discontinued issuance of new short-term certificates from the DCMT in response to higher projected charge-offs following the October 2005 effective date of the new U.S. bankruptcy legislation, caused the level of securitized loans in 2005 to decrease below prior year levels. These effects lingered into 2006, causing outstanding securitization transactions to remain somewhat lower than historical levels on average. In August 2005, Morgan Stanley announced that it would not pursue a spin-off of Discover.

During the last three years, there have been increasing regulatory initiatives in the United Kingdom with respect to late and overlimit fees, interchange fees and the sale of retail insurance products, and a relaxation of bankruptcy laws that have made it more difficult to collect on delinquent accounts and easier for cardmembers to declare bankruptcy. The changes contributed to increased U.K. bankruptcy charge-offs and lower late fee, overlimit fee and interchange revenues.

In February 2006, we acquired the Goldfish credit card business in the United Kingdom, adding approximately $1.4 billion in receivables. Under the terms of the acquisition, we did not purchase any late stage delinquencies. As such, the year ended November 30, 2006 reflects a lower level of charge-offs than the year ended November 30, 2007, which includes the full impact of the Goldfish acquisition.

Recent Developments

Recent Earnings

On March 19, 2008, we released financial information with respect to the three months ended February 29, 2008. We reported net income from continuing operations for the first quarter of 2008 of $239 million, or $0.50 per share, as compared to $260 million, or $0.54 per share in the first quarter of 2007. Reported net income of $81 million included a $158 million net loss from discontinued operations related to our Goldfish business, previously reported as the International Card segment. Net income from continuing operations was down 8% as higher provision for loan losses and lower net interest income were primarily offset by higher other income. For further information please see our Current Report on Form 8-K filed with the SEC on March 19, 2008.

Sale of the International Card Segment

On February 7, 2008, Discover and Barclays Bank Plc entered into a definitive sale and purchase agreement relating to the sale of £129 million of net assets (equivalent to approximately $258 million) of our U.K. credit card business, which represented substantially all of our International Card segment and included $3.1 billion in owned loan receivables at November 30, 2007. The aggregate sale price under the agreement is £35 million (equivalent to approximately $70 million), payable in cash at closing and subject to a post-closing adjustment. The closing is expected to occur by the end of our second quarter of 2008. The sale is subject to the satisfaction of a number of conditions, including clearance from the U.K. Office of Fair Trading, the transfer of a minimum value of receivables and consents under material contracts. There can be no assurance that the sale will occur by the end of our second quarter of 2008, if at all. As a result, we reclassified the net assets of the business to discontinued operations in the first quarter of 2008, restating prior periods for comparability. We recorded a loss from discontinued operations of $158 million in the first quarter of 2008. This included a loss from the write-down of net assets to fair value of $172 million and net income from operations of $14 million which included gains from the sale of other assets.

Segments

We manage our business activities in three segments: U.S. Card, Third-Party Payments and International Card. In compiling the segment results that follow, the U.S. Card segment bears all overhead costs that are not specifically associated with a particular segment and all costs associated with Discover Network marketing, servicing and infrastructure, with the exception of an allocation of direct and incremental costs driven by the Third-Party Payments segment.

U.S. Card. The U.S. Card segment offers Discover Card-branded credit cards issued to individuals and small businesses over the Discover Network. Also included within the U.S. Card segment are our other consumer

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products and services businesses, including prepaid and other consumer lending and deposit products offered through our subsidiary, Discover Bank.

Third-Party Payments. The Third-Party Payments segment includes PULSE and our third-party payments business.

International Card. The International Card segment offers consumer finance products and services in the United Kingdom, including Morgan Stanley-branded, Goldfish-branded and various affinity-branded credit cards issued on the MasterCard and Visa networks.

The following table presents segment data on a managed basis (dollars in thousands), and a reconciliation to a GAAP presentation.

	Managed Basis					GAAP Basis
	U.S. Card	Third-Party Payments	International Card	Total	Securitization Adjustment(1)	Total
For the Years Ended November 30,						
2007						
Interest income	$ 6,376,298	$ 2,376	$ 481,845	$ 6,860,519	$ (3,972,350)	$ 2,888,169
Interest expense	2,729,065	19	246,704	2,975,788	(1,593,373)	1,382,415
Net interest income	3,647,233	2,357	235,141	3,884,731	(2,378,977)	1,505,754
Provision for loan losses	1,853,396		317,446	2,170,842	(1,220,677)	950,165
Other income	2,101,076	118,700	168,043	2,387,819	1,158,300	3,546,119
Other expense(2)	2,390,463	84,097	681,952	3,156,512		3,156,512
Income (loss) before income tax expense(2)	$ 1,504,450	$ 36,960	$ (596,214)	$ 945,196	$	$ 945,196
2006						
Interest income	$ 5,748,698	$ 1,801	$ 416,986	$ 6,167,485	$ (3,708,959)	$ 2,458,526
Interest expense	2,160,569	23	176,997	2,337,589	(1,397,549)	940,040
Net interest income	3,588,129	1,778	239,989	3,829,896	(2,311,410)	1,518,486
Provision for loan losses	1,663,472		238,172	1,901,644	(1,146,007)	755,637
Other income	2,097,676	110,700	165,160	2,373,536	1,165,403	3,538,939
Other expense	2,381,880	83,529	254,074	2,719,483		2,719,483
Income (loss) before income tax expense	$ 1,640,453	$ 28,949	$ (87,097)	$ 1,582,305	$	$ 1,582,305
2005(3)						
Interest income	$ 5,409,381	$ 673	$ 294,343	$ 5,704,397	$ (3,529,586)	$ 2,174,811
Interest expense	1,671,331	95	129,671	1,801,097	(1,024,618)	776,479
Net interest income	3,738,050	578	164,672	3,903,300	(2,504,968)	1,398,332
Provision for loan losses	2,263,617		126,462	2,390,079	(1,511,593)	878,486
Other income	1,753,828	92,143	97,691	1,943,662	993,375	2,937,037
Other expense	2,272,126	92,866	167,635	2,532,627		2,532,627
Income (loss) before income tax expense	$ 956,135	$ (145)	$ (31,734)	$ 924,256	$	$ 924,256

(1) The Securitization Adjustment column presents the effect of loan securitization by recharacterizing as securitization income the portions of the following items that relate to the securitized loans: interest income, interest expense, provision for loan losses, discount and interchange revenue and loan fee revenues. Securitization income is reported in other income.

(2) 2007 includes a $391 million pretax ($279 million after tax) non-cash impairment charge related to our International Card segment.

(3) PULSE was acquired in January 2005.

The segment discussions that follow for the years ended November 30, 2007, 2006 and 2005 are on a managed basis.

U.S. Card

The U.S. Card segment reported pretax income of $1.5 billion for the year ended November 30, 2007, down 8% as compared to November 30, 2006. The decrease in pretax income was driven by an increase in provision for loan losses partially offset by higher net interest income. Provision for loan losses increased $189.9 million, or 11%, reflecting an increase in bankruptcy charge-offs compared to the unusually low levels in 2006 and a

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higher level of loans retained on our balance sheet. Net interest income increased $59.1 million, or 2%, due to higher interest income, reflecting higher average receivables, partially offset by an increase in interest expense, reflecting increased funding costs and borrowings.

For the year ended November 30, 2007, managed loans grew 5%, to $48.2 billion, driven by record sales volume of $90.3 billion, up 4% over last year. U.S. credit quality remained strong, although delinquency rates increased from last year reflecting weakening in the U.S. economy. The managed net charge-off rate of 3.84% was down 12 basis points from last year and the over 30 day delinquency rate of 3.59% was 20 basis points higher than last year. In 2008 we estimate the full year managed net charge-off rate will be between 4.75% and 5.00%.

A small portion of our newly-originated loans are issued to borrowers with FICO scores below 660 at the time of account origination but who have met our other specific underwriting criteria indicating to us that they have the ability and willingness to pay. We have restricted this initiative to potential customers with FICO scores above 600, and the majority of these new accounts had FICO scores at origination in the 640 to 660 range. At November 30, 2007, less than 3.5% of receivables related to new accounts originated within the year were at FICO scores below 660 at time of origination.

While we seek to carefully control the level of new account originations at FICO scores below 660, over time some accounts that were originated at higher FICO scores will migrate to levels below 660 due to circumstances that affect their credit performance. Consistent with industry standards for reporting securitization U.S. master trust data, we disclosed that as of October 31, 2007, approximately 26% of receivable balances in the domestic trust related to accounts with FICO scores below 660 at that date. While this percentage relates solely to credit card receivables held in the trust, we believe they are representative of our managed loan portfolio.

The U.S. Card segment produced strong results for the year ended November 30, 2006, with pretax income of $1.6 billion, up 72%, as compared to November 30, 2005. These results reflected the strong credit quality of the domestic managed credit card portfolio and the continued favorable impact of the new U.S. bankruptcy legislation on charge-offs, the revaluation of the interest-only strip receivable and the allowance for loan losses. The increase in pretax income was due to higher other income and a lower provision for loan losses partially offset by lower net interest income and higher other expenses. Other income increased $343.8 million, or 20%, due primarily to an increase in the fair value of our interest-only strip receivable as a result of lower bankruptcy receipts and our estimate of its related favorable impact on future charge-offs as well as a higher level of new securitization transactions. Provision for loan losses decreased $600.1 million, or 27%, reflecting strong credit quality and lower bankruptcy charge-offs. Net interest income decreased $149.9 million, or 4%, as higher interest expense was partially offset by higher interest income. The increase in interest expense was primarily due to an increase in the cost of funds driven by the rising interest rate environment. The increase in interest income reflects lower interest charge-offs due to improved credit quality and the effect of a rising interest rate environment on floating rate credit card loan receivables partially offset by higher promotional rate balances. Other expense increased $109.8 million, or 5%, driven by higher compensation and benefits expense and increased legal fees, primarily related to the litigation against Visa and MasterCard, and consulting costs, partially offset by lower cardmember fraud expense.

For the year ended November 30, 2006, managed credit card loans grew 3%, to $45.7 billion, driven by higher transaction volume partially offset by higher cardmember payment rates. Sales volume increased 6%, primarily reflecting increased cardmember usage and higher prices of gasoline (which represents approximately 8% of sales volume). Managed interest spread compressed 50 basis points as increased cost of funds outpaced higher interest yield. The managed net charge-off rate of 3.96% decreased 134 basis points, reflecting strong credit quality and lower bankruptcy charge-offs. Over 30 and over 90 day delinquency rates decreased 59 basis points and 16 basis points to 3.39% and 1.59%, respectively, due to a shift to loans with lower risk profiles and improved collection experience.

Third-Party Payments

The Third-Party Payments segment reported pretax income of $37.0 million for the year ended November 30, 2007, up 28% as compared to November 30, 2006. The increase in pretax income was driven by

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higher revenue from increased volumes that was partially offset by higher marketing and pricing incentives and from higher third-party card issuer fees. Third-Party Payments debit and credit volume was $91.7 billion for the year ended November 30, 2007, up 25% from 2006.

The Third-Party Payments segment reported pretax income of $28.9 million for the year ended November 30, 2006 versus a pretax loss of $0.1 million for the year ended November 30, 2005 driven by increased other income and lower other expense. Other income increased $18.5 million, or 20%, due to higher volume from third-party card issuers signed in mid-2005 and higher transaction processing revenue related to increased volume on the PULSE Network. Other expense decreased $9.3 million, or 10%, as a result of one-time costs incurred in 2005 in connection with third-party issuer signings partially offset by higher transaction processing expense related to increased volumes on the PULSE Network.

Transactions processed on the PULSE Network increased 300 million, or 19%, to 1.9 billion for the year ended November 30, 2006.

International Card

The International Card segment reported a pretax loss of $596.2 million for the year ended November 30, 2007, as compared to a pretax loss of $87.1 million for the year ended November 30, 2006, driven by a non-cash impairment charge of $391 million as well as higher provision for loan losses and other expenses. Continued disruption in the U.K. financial markets, higher interest rates and our decision to reduce our loan exposure to the U.K. market have negatively affected the book value of the Goldfish business, resulting in the impairment charge. The provision for loan losses increased $79.3 million, or 33%, reflecting a full period of charge-offs related to the Goldfish and Liverpool Victoria portfolios, weakening in the consumer credit environment in the United Kingdom, maturing securitizations resulting in an increase in receivables being retained in the portfolio, and an increase in the provision for loan losses related to the implementation of higher minimum payment requirements on certain accounts. Other expenses, excluding the impairment charge, increased $36.9 million, or 15%, primarily due to spin-off related costs and various business initiatives.

The International Card managed credit card receivables decreased 6% from last year to $4.4 billion, reflecting increased payments and lower loan growth as we shifted our focus to reducing unprofitable accounts. This was partially offset by favorable foreign exchange rates. The managed net charge-off rate of 6.54% increased 109 basis points from last year. The managed over 30 days delinquency rate increased 67 basis points from last year to 5.25%.

The International Card segment reported a pretax loss of $87.1 million for the year ended November 30, 2006, an increase of $55.4 million over the pretax loss incurred for the year ended November 30, 2005, primarily as a result of the acquisition of the Goldfish business and the deteriorating consumer credit environment in the United Kingdom. The increase in pretax loss was driven by increases in the provision for loan losses and other expense partially offset by higher net interest income and other income. The provision for loan losses increased $111.7 million, or 88%, as a result of the weakened credit environment in the United Kingdom, the Goldfish acquisition and increased bankruptcy charge-offs. Other expense increased $86.4 million, or 52%, primarily due to incremental costs as a result of the acquisition of the Goldfish business. Net interest income increased $75.3 million, or 46%, and other income increased $67.5 million, or 69%, primarily related to a higher level of managed loan receivables as a result of the acquisition of the Goldfish business. The increase in other income was partially offset by lower levels of late and overlimit fee revenues resulting from regulatory changes which limited the per-incident amount of fees that can be charged.

For the year ended November 30, 2006, managed credit card loans grew $2.0 billion, or 74%, to $4.6 billion primarily due to the addition of the Goldfish business. Managed interest spread was flat compared to the prior year as lower yield was offset by lower cost of funds. Credit quality continued to deteriorate as the managed net charge-off rate rose 135 basis points to 5.45%, and the over 30 and over 90 day delinquency rates increased to 4.58% and 2.22%, respectively.

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GAAP to Managed Data Reconciliations

Securitized loans against which beneficial interests have been issued to third parties are removed from our statements of financial condition. Instances in which we retain certificated beneficial interests in the securitization transactions result in a reduction to loan receivables of the amount of the retained interest and a corresponding increase in investment securities available-for-sale. The portions of interest income, provision for loan losses and certain components of other income related to the securitized loans against which beneficial interests have been issued are no longer recorded in our statements of income; however, they remain significant factors in determining the securitization income we receive on our retained beneficial interests in those transactions. Management believes it is useful for investors to consider the credit performance of the entire managed loan portfolio to understand the quality of loan originations and the related credit risks inherent in the owned portfolio and retained interests in securitization. Loan receivables on a GAAP (or owned) basis and related performance measures, including yield, charge-offs and delinquencies can vary from those presented on a managed basis. Generally, loan receivables included in the securitization trusts are derived from accounts that are more seasoned, while owned loan receivables represent a greater concentration of newer accounts, occurring as a result of the degree to which receivables from newer accounts are added to the trusts. The seasoning of an account is measured by the age of the account relationship. In comparison to more seasoned accounts, loan receivables of newer accounts typically carry lower interest yields resulting from introductory offers to new cardmembers and lower charge-offs and delinquencies.

Beginning with Earnings Summary, the discussion of GAAP results is presented on a consolidated and combined basis with any material differences between segment performance specifically identified. The table that follows provides a GAAP to managed data reconciliation of loan receivables and related statistics that are impacted by asset securitization:

Reconciliation of GAAP to Managed Data

	For the Years Ended November 30,		
	2007	2006	2005
	(dollars in thousands)		
Balance Sheet Statistics			
Loan Receivables			
GAAP Basis	$ 23,954,295	$ 23,742,750	$ 22,803,166
Securitization Adjustment	28,599,309	26,703,427	24,440,063
Managed Basis	$ 52,553,604	$ 50,446,177	$ 47,243,229
Total Assets			
GAAP Basis	$ 37,376,105	$ 29,067,242	$ 26,943,923
Securitization Adjustment	28,375,826	26,444,943	24,370,113
Managed Basis	$ 65,751,931	$ 55,512,185	$ 51,314,036
Total Credit Card Loans			
Credit Card Loans			
GAAP Basis	$ 23,703,101	$ 23,646,901	$ 22,496,211
Securitization Adjustment	28,599,309	26,703,427	24,440,063
Managed Basis	$ 52,302,410	$ 50,350,328	$ 46,936,274
Average Credit Card Loans			
GAAP Basis	$ 22,814,043	$ 21,656,295	$ 19,931,636
Securitization Adjustment	28,524,092	26,560,251	27,398,507
Managed Basis	$ 51,338,135	$ 48,216,546	$ 47,330,143

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	For the Years Ended November 30,		
	2007	2006 (dollars in thousands)	2005
Interest Yield			
GAAP Basis	10.58%	10.38%	10.12%
Securitization Adjustment	13.93%	13.96%	12.88%
Managed Basis	12.44%	12.36%	11.72%
Net Principal Charge-off Rate			
GAAP Basis	3.82%	3.79%	4.84%
Securitization Adjustment	4.28%	4.31%	5.52%
Managed Basis	4.08%	4.08%	5.23%
Delinquency Rate (over 30 days)			
GAAP Basis	3.50%	3.22%	3.69%
Securitization Adjustment	3.92%	3.76%	4.24%
Managed Basis	3.73%	3.50%	3.98%
Delinquency Rate (over 90 days)			
GAAP Basis	1.63%	1.53%	1.62%
Securitization Adjustment	1.84%	1.75%	1.87%
Managed Basis	1.74%	1.65%	1.75%
U.S. CARD			
Loan Receivables			
GAAP Basis	$ 20,831,117	$ 20,790,244	$ 20,611,306
Securitization Adjustment	27,349,319	25,011,827	23,826,144
Managed Basis	$ 48,180,436	$ 45,802,071	$ 44,437,450
Domestic Credit Card Loans			
Credit Card Loans			
GAAP Basis	$ 20,579,923	$ 20,694,395	$ 20,434,977
Securitization Adjustment	27,349,319	25,011,827	23,826,144
Managed Basis	$ 47,929,242	$ 45,706,222	$ 44,261,121
Average Credit Card Loans			
GAAP Basis	$ 19,845,880	$ 19,120,946	$ 18,644,660
Securitization Adjustment	26,965,690	25,156,303	26,092,042
Managed Basis	$ 46,811,570	$ 44,277,249	$ 44,736,702
Interest Yield			
GAAP Basis	10.75%	10.50%	10.16%
Securitization Adjustment	14.07%	14.08%	12.93%
Managed Basis	12.66%	12.53%	11.78%
Net Principal Charge-off Rate			
GAAP Basis	3.41%	3.64%	4.95%
Securitization Adjustment	4.15%	4.20%	5.55%
Managed Basis	3.84%	3.96%	5.30%
Delinquency Rate (over 30 days)			
GAAP Basis	3.28%	3.05%	3.69%
Securitization Adjustment	3.82%	3.67%	4.23%
Managed Basis	3.59%	3.39%	3.98%

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	For the Years Ended November 30,		
	2007	2006	2005
		(dollars in thousands)	
Delinquency Rate (over 90 days)			
GAAP Basis	1.53%	1.44%	1.61%
Securitization Adjustment	1.79%	1.72%	1.86%
Managed Basis	1.68%	1.59%	1.75%
INTERNATIONAL CARD			
Credit Card Loans			
GAAP Basis	$ 3,123,178	$ 2,952,506	$ 2,061,234
Securitization Adjustment	1,249,990	1,691,600	613,919
Managed Basis	$ 4,373,168	$ 4,644,106	$ 2,675,153
Average Credit Card Loans			
GAAP Basis	$ 2,968,163	$ 2,535,349	$ 1,286,976
Securitization Adjustment	1,558,402	1,403,948	1,306,465
Managed Basis	$ 4,526,565	$ 3,939,297	$ 2,593,441
Interest Yield			
GAAP Basis	9.42%	9.51%	9.63%
Securitization Adjustment	11.43%	11.94%	11.80%
Managed Basis	10.11%	10.38%	10.72%
Net Principal Charge-off Rate			
GAAP Basis	6.56%	4.94%	3.28%
Securitization Adjustment	6.49%	6.36%	4.91%
Managed Basis	6.54%	5.45%	4.10%
Delinquency Rate (over 30 days)			
GAAP Basis	4.91%	4.36%	3.78%
Securitization Adjustment	6.09%	4.96%	4.53%
Managed Basis	5.25%	4.58%	3.95%
Delinquency Rate (over 90 days)			
GAAP Basis	2.27%	2.16%	1.73%
Securitization Adjustment	2.83%	2.32%	2.09%
Managed Basis	2.43%	2.22%	1.81%

Critical Accounting Policies

In preparing our consolidated and combined financial statements in conformity with GAAP, management must make judgments and use estimates and assumptions about the effects of matters that are uncertain. For estimates that involve a high degree of judgment and subjectivity, it is possible that different estimates could reasonably be derived for the same period. For estimates that are particularly sensitive to changes in economic or market conditions, significant changes to the estimated amount from period to period are also possible. Management believes the current assumptions and other considerations used to estimate amounts reflected in our consolidated and combined financial statements are appropriate. However, if actual experience differs from the assumptions and other considerations used in estimating amounts in our consolidated and combined financial statements, the resulting changes could have a material adverse effect on our consolidated and combined results of operations and, in certain cases, could have a material adverse effect on our consolidated and combined financial condition. Management has identified the policies related to the estimation of the allowance for loan losses, the accounting for asset securitization transactions, interest income recognition, the accrual of cardmember rewards cost, the evaluation of goodwill for potential impairment and accrual of income taxes as critical accounting policies.

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Allowance for Loan Losses

The allowance for loan losses represents management s estimate of probable net loan losses inherent in the loan portfolio. Management evaluates the allowance quarterly for adequacy. The allowance is established through a charge to the provision for loan losses. In estimating losses inherent in the credit card loan portfolio, we use an approach that utilizes a migration analysis of delinquent and current credit card receivables. A migration analysis is a technique used to estimate the likelihood that a loan receivable will progress through the various stages of delinquency and to charge-off. The migration analysis considers uncollectible principal, interest and fees reflected in loan receivables. In determining the proper level of the allowance for loan losses, management also considers factors that may impact loan loss experience, including current economic conditions, recent trends in delinquencies and bankruptcy receipts, account collection management, policy changes, account seasoning, loan volume and amounts, payment rates and forecasting uncertainties.

If management used different assumptions in estimating probable losses, the impact to the allowance for loan losses could have a material effect on our consolidated and combined financial condition and results of operations. For example, a 10% change in management s estimate of probable net loan losses could have resulted in a change of approximately $92 million in the allowance for loan losses at November 30, 2007, with a corresponding change in the provision for loan losses. See Note 5: Loan Receivables to the audited consolidated and combined financial statements contained in this prospectus for further details about the allowance for loan losses.

Accounting for Asset Securitization Transactions

We account for our securitization transactions in accordance with Statement No. 140. The gain on the securitization transaction depends in part on the previous carrying amount of the assets involved in the transfer, allocated between the assets transferred and the retained interests based upon their respective fair values at the date of the transfer. The interest-only strip receivable represents the contractual right to receive interest and certain loan fee revenues less certain costs, including loan losses on securitized loans and the contractual rate of interest paid to third-party investors in the securitization as well as a servicing fee from the trust over the life of the asset sold. In the absence of observable market prices, the fair value of the interest-only strip receivable is estimated based on the present value of expected future cash flows using management s best estimate of the key assumptions, including forecasted interest yield, loan losses and payment rates, the interest paid to investors and a discount rate commensurate with the risks involved. Changes in the estimated fair value of the interest-only strip receivable, as well as certain other retained interests, are recorded in securitization income. The use of different estimates or assumptions could produce materially different financial results. In addition, estimates are likely to change in the future as components of the interest-only strip receivable valuation are sensitive to market and economic conditions.

If management used different assumptions in estimating the value of the interest-only strip receivable, the impact could have a material effect on our consolidated and combined financial condition and results of operations. For example, a 20% change in the excess spread assumption for all securitized loans could have resulted in a change of approximately $80 million in the value of the interest-only strip receivable as of November 30, 2007. See Note 6: Credit Card Securitization Activities to the audited consolidated and combined financial statements contained in this prospectus for further information about the accounting for securitizations.

Interest Income Recognition

Interest income earned through finance charges on credit card loans is calculated based on the amount of loans outstanding and the contractual interest rates on such loans. Accrued interest is included in credit card loan receivables when billed to the cardmember. We accrue unbilled interest revenue on a monthly basis from a cardmember s billing cycle date to the end of the month. The unbilled interest accrual is recorded on the consolidated and combined statements of financial condition in accrued interest receivable for owned loans and in amounts due from asset securitization for securitized loans. We make certain assumptions and estimates in the determination of unbilled accrued interest, including a projection of the percentage of loan balances that will revolve. We apply the same methodology in the determination of unbilled accrued interest for both owned loans and securitized loans.

If management used different assumptions in the determination of the unbilled portion of accrued interest income and the valuation of accrued interest on securitized loans, our financial condition and results of operations could have been materially different. For example, a 10% change in management s projection of the percentage of loans that will revolve in the next cycle could have resulted in a combined change in accrued interest receivable and amounts due from asset securitization of approximately $31 million at November 30, 2007, with a corresponding change in interest income. See Net Interest Income for additional details concerning interest earned through finance charges on credit card loans.

Cardmember Rewards Cost

We offer our cardmembers various reward programs, including the Cashback Bonus reward program, pursuant to which we offer certain cardmembers a reward equal to a percentage of their purchase amounts based on the type and volume of the cardmember s purchases. The liability for cardmember rewards is included in accrued expenses and other liabilities on our consolidated and combined statements of financial condition. We compute rewards liability on an individual cardmember basis and it is accumulated as qualified cardmembers make progress toward earning a reward through their ongoing purchase activity. The liability is adjusted for expected forfeitures of accumulated rewards. We estimate forfeitures based on historical account closure and charge-off experience and actual cardmember purchase activity. We recognize Cashback Bonus reward cost for both owned loans and securitized loans as a reduction of discount and interchange revenue in the consolidated and combined statements of income.

If management used a different estimate of forfeitures, our consolidated and combined financial condition and results of operations could have differed significantly. For example, a 100 basis point decrease in the estimated forfeiture rate as of November 30, 2007, could have resulted in an increase in accrued expenses and other liabilities of approximately $9 million. The corresponding increase in rewards cost would have been reflected as a decrease in discount and interchange revenue. See Other Income and Note 2: Summary of Significant Accounting Policies to the audited consolidated and combined financial statements contained in this prospectus for further details about cardmember rewards cost.

Goodwill

We recognize goodwill when the purchase price of an acquired business exceeds the fair values of the acquired net assets. As required by GAAP, we test goodwill for impairment annually, or more often if indicators of impairment exist. In evaluating goodwill for impairment, management must estimate the fair value of the business unit(s) to which the goodwill relates. Because market data concerning acquisitions of comparable businesses typically are not readily obtainable, other valuation techniques such as earnings multiples and cash flow models are used in estimating the fair values of these businesses. In applying these techniques, management considers historical results, business forecasts, market and industry conditions and other factors. We may also consult independent valuation experts where needed in applying these valuation techniques. The valuation methodologies we use involve assumptions about business performance, revenue and expense growth, discount rates and other assumptions that are judgmental in nature.

If the assumptions used by management in valuing its acquired businesses are inappropriate, we may be exposed to an impairment loss that, when realized, could have a material impact on our consolidated and combined financial condition and results of operations.

Following a strategic review of the International Card segment that began in the third quarter of 2007 and was completed in the fourth quarter, management determined that an interim test for impairment was needed on the goodwill associated with that segment. The impairment test resulted in the recognition of an impairment

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charge impacting goodwill and other intangible assets. See Note 9: Goodwill to the audited consolidated and combined financial statements contained in this prospectus for further details concerning the fourth quarter goodwill impairment charge.

Income Taxes

We are subject to the income tax laws of the jurisdictions where we have business operations, primarily the United States, its states and municipalities, and the United Kingdom. We must make judgments and interpretations about the application of these inherently complex tax laws when determining the provision for income taxes and must also make estimates about when in the future certain items will affect taxable income in the various taxing jurisdictions. Disputes over interpretations of the tax laws may be settled with the taxing authority upon examination or audit. We regularly evaluate the likelihood of assessments in each of the taxing jurisdictions resulting from current and subsequent years examinations, and tax reserves are established as appropriate.

Changes in the estimate of income taxes can occur due to tax rate changes, interpretations of tax laws, the status and resolution of examinations by the taxing authorities, and newly enacted laws and regulations that impact the relative merits of tax positions taken. When such changes occur, the effect on our consolidated and combined financial condition and results of operations can be significant. See Note 17: Income Taxes to the audited consolidated and combined financial statements contained in this prospectus for additional information about income taxes.

Earnings Summary

The following table outlines changes in our consolidated and combined statement of income for the periods presented (dollars in thousands):

	For the Years Ended November 30,			2007 vs. 2006 increase (decrease)		2006 vs. 2005 increase (decrease)	
	2007	2006	2005	$	%	$	%
Interest income	$ 2,888,169	$ 2,458,526	$ 2,174,811	$ 429,643	17%	$ 283,715	13%
Interest expense	1,382,415	940,040	776,479	442,375	47%	163,561	21%
Net interest income	1,505,754	1,518,486	1,398,332	(12,732)	(1%)	120,154	9%
Provision for loan losses	950,165	755,637	878,486	194,528	26%	(122,849)	(14%)
Net interest income after provision for loan losses	555,589	762,849	519,846	(207,260)	(27%)	243,003	47%
Other income	3,546,119	3,538,939	2,937,037	7,180	0%	601,902	20%
Other expense	3,156,512	2,719,483	2,532,627	437,029	16%	186,856	7%
Pretax income	945,196	1,582,305	924,256	(637,109)	(40%)	658,049	71%
Income tax expense	356,566	505,689	346,341	(149,123)	(29%)	159,348	46%
Net income	$ 588,630	$ 1,076,616	$ 577,915	$ (487,986)	(45%)	$ 498,701	86%

Net income for the year ended November 30, 2007 was $588.6 million, down 45% compared to the year ended November 30, 2006, driven by a non-cash impairment charge of $391 million, as well as higher provision for loan losses and other expense. The U.S. provision for loan losses increased, reflecting a trend toward higher levels of delinquencies as well as a higher level of loans retained on the company s balance sheet. The international provision for loan losses increased due to a full period of charge-offs related to the Goldfish and Liverpool Victoria portfolios, weakening in the consumer credit environment in the United Kingdom, certain maturing securitized receivables being retained in the portfolio, and an increase in reserves related to the implementation of higher minimum payment requirements on certain accounts. Other expense excluding the impairment charge, increased due to spin-off related costs and various business initiatives. The year ended November 30, 2007 also included a higher effective tax rate.

Net income for 2006 and 2005 was influenced by consumer behavior in anticipation of the October 2005 effective date of the new U.S. bankruptcy legislation. We believe 2005 results were adversely affected as

consumers filed for bankruptcy before the new U.S. bankruptcy legislation. This legislation resulted in an acceleration of charge-offs in 2005 and first quarter 2006, a negative revaluation of the interest-only strip receivable in 2005 and additional provisions to the allowance for loan losses in 2005. In contrast, full year 2006 results were positively affected by a sharp decline in consumer bankruptcy receipts, resulting in lower charge-offs. Full year 2006 also benefited from a favorable revaluation of the interest-only strip receivable and a decrease in the level of allowance for loan losses.

Net income for the year ended November 30, 2006 was a record $1.1 billion, up 86% compared to the year ended November 30, 2005, driven by higher other income and net interest income and lower provision for loan losses, as well as a lower effective tax rate, partially offset by higher other expenses. Other income increased due to higher securitization income resulting from lower credit losses on securitized loans attributable to strong credit quality and the continued lower level of charge-offs following the October 2005 effective date of the new U.S. bankruptcy legislation, resulting in a higher excess spread and a favorable revaluation of the interest-only strip receivable. Increases in other expenses were driven by costs related to the Goldfish acquisition, higher compensation and benefit costs and increased legal and consulting costs. Also, the year ended November 30, 2006 included a lower effective tax rate due to tax benefits related to the favorable resolution of various tax matters.

Net Interest Income

Net interest income represents the difference between interest income earned on interest-earning assets which we own and the interest expense incurred to finance those assets. Net interest margin states the interest income, net of interest expense, as a percentage of total interest-earning assets. Our interest-earning assets consist of loan receivables, certain retained interests in securitization transactions included in amounts due from asset securitization, certain cash and cash equivalents, including Federal Funds sold, and investment securities. Because the third-party investor interests in securitization transactions are not assets owned by us, they are not included in interest-earning assets nor is the interest yield on the related loans included in interest income. See Note 4: Investment Securities to the consolidated and combined financial statements contained in this prospectus for further disclosure regarding investment securities.

Net interest income for the year ended November 30, 2007 decreased $12.7 million, or 1%, and net interest margin decreased 118 basis points to 4.76% as compared to the year ended November 30, 2006. The modest decrease in net interest income was due to higher average interest-bearing liabilities and a higher cost of funds on interest-bearing liabilities largely offset by higher average interest-earning assets. In 2007, the establishment of the liquidity reserve, which earns a lower interest rate, adversely impacted the net interest margin for the year ended November 30, 2007. Net interest income for the year ended November 30, 2006 increased $120.2 million, or 9%, and net interest margin increased 6 basis points to 5.94% as compared to the year ended November 30, 2005. The increase in net interest income is due to higher average interest-earning assets and a higher interest yield offset by an increase in the cost of funds. The favorable impact of the higher interest yield on net interest margin was offset in part by the higher average interest-earning assets and the higher cost of funds.

Interest income is influenced by the level of interest-earning assets, the most significant of which is our loan receivables. The level of loan receivables can be influenced by portfolio growth strategies, including portfolio acquisition, cardmember spending and payment behavior and changes in the level of securitized loans. Typically, new securitization transactions have the effect of decreasing loan receivables, whereas maturities of existing securitization transactions increase loan receivables. For the years ended November 30, 2007 and 2006, there were higher levels of average securitized loans than their respective prior year comparisons. However, these higher levels were more than offset by overall growth in average loans, resulting in higher average loan receivables, contributing favorably to interest income in 2007 and 2006.

Other interest-earning assets that can influence interest income are certain amounts due from asset securitization included in other interest-earning assets on the average balance sheet, certain cash and cash equivalents, including Federal Funds sold, and investment securities. Amounts due from asset securitization

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relate to certain assets retained by us in securitization transactions. The levels of these assets are impacted by securitization maturities and can vary in relation to the level of securitized loans. Federal Funds sold represent amounts maintained for liquidity purposes. For the year ended November 30, 2007, the interest income was favorably impacted by a higher level of Federal Funds sold, which was significantly greater in comparison to that of prior years as a result of the establishment of our liquidity reserve in the first half of 2007. See Liquidity and Capital Resources for further discussion of our liquidity reserve.

Interest income is also influenced by the interest rate on interest-earning assets. Credit card loan receivables earn interest at fixed rates as well as floating rates that are aligned with the prime rate. Amounts due from asset securitization and Federal Funds sold earn interest at floating rates tied to short-term rates aligned with market indices. Accordingly, interest income earned on floating rate interest-earning assets is influenced by changes in the interest rate environment. Loan receivables are our largest asset. During the years ended November 30, 2007, 2006 and 2005, average credit card loan receivables earning interest at floating rates represented 45%, 52% and 50%, respectively, of total average loan receivables. The prime rate decreased 0.75% during the fourth quarter of 2007. The impact of this decline on interest income in 2007 was lessened due to the timing of the decrease in the prime rate and a shift to a higher percentage of fixed rate average loan receivables. Conversely, during 2006 and 2005, the prime rate increased 1.25% and 2.00%, respectively, which contributed favorably to interest income earned on the owned loan receivables, amounts due from asset securitizations and Federal Funds sold. Additionally, interest income in 2006 was further impacted by a higher percentage of loan receivables earning interest at floating rates.

Credit performance is another factor which influences interest income. As a result of the improved credit environment following the October 2005 effective date of the new U.S. bankruptcy legislation and our risk management practices, the number of cardmembers having lower risk profiles has increased. Generally, cardmembers with a lower risk profile have higher payment rates, resulting in a lower percentage of loan receivables on which interest is accrued. Although interest income is lower as a result, interest-related charge-offs, which are recorded as a reduction to interest income, are also lower. This was particularly evident following the October 2005 effective date of the new U.S. bankruptcy legislation. The differences in year-over-year comparisons have narrowed as charge-offs have increased from the levels seen at the initial time period following the legislation s effective date. The interest billed and subsequently charged-off, net of recoveries, was 0.90% for both years ended November 30, 2007 and 2006 and 1.14% for the year ended November 30, 2005.

Interest-bearing liabilities reflect our funding requirements and consist of deposits and short- and long-term borrowings. Prior to the Distribution, interest-bearing liabilities also included borrowings from Morgan Stanley. We incur interest expense on our interest-bearing liabilities at fixed and floating rates. Accordingly, changes in the interest rate environment, changes in the percentage of floating rate interest-bearing liabilities and the replacement of maturing debt can impact interest expense. The floating rate average interest-bearing liabilities as a percentage of total average interest-bearing liabilities was approximately 48% during both years ended November 30, 2007 and 2006 and 41% during the year ended November 30, 2005. The level of average interest-bearing liabilities during 2007 was higher than prior year, reflecting the establishment of a liquidity reserve and growth in loan receivables. Accordingly, the level of floating rate average interest-bearing liabilities, specifically money market accounts, was higher as well. The increased levels of floating rate interest-bearing liabilities coupled with the higher interest rate environment in 2007 as compared to 2006, adversely impacted interest expense. In addition, the higher interest rate environment in 2007 also had a negative effect on the cost of issuing new fixed rate certificates of deposit to replace maturing certificates of deposit issued at lower, historical rates. Similarly, the increase in the percentage of floating rate average interest-bearing liabilities during the year ended November 30, 2006, as compared to 2005, adversely impacted interest expense due to a rising interest rate environment.