Consumer Federation of America

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BANKING REGULATORS FINALIZE RULES ON CREDIT CARD ABUSES

Rules Would Stop Some Unfair Practices in 2010;
Congress Must Act to Provide Broader Reform More Quickly

The Consumer Federation of America (CFA) today applauded federal banking regulators for finalizing rules to curb some of the most abusive credit card lending practices but expressed concern that the requirements would not take effect for more than a year and a half. CFA also called on Congress to provide additional consumer protections to rein in abuses not addressed by the regulators. The final rule was released today by the Federal Reserve Board, the Office of Thrift Supervision and the National Credit Union Administration. Among other things, the regulators would stop many unjustified interest rate hikes on existing balances, prohibit the charging of interest on debt already paid off and require issuers to allocate cardholder payments more fairly.

"Federal regulators have taken an important first step to stop credit card companies from using hidden traps and tricks to drive up the amount of debt consumers owe," said Travis B. Plunkett, legislative director of the Consumer Federation of America. "However, it is not helpful to consumers struggling to pay off hefty debts in the middle of a recession, to give credit card companies the green light to continue to mislead and overcharge consumers for another year and a half. We urge Congress to provide consumers with immediate relief from abusive credit card practices, including unfair tactics not addressed in these rules."

The new rule would prohibit or restrict a number of abusive credit card practices:

- **Costly and unjustified retroactive interest rate increases**. The proposal would prohibit the widespread practice of charging higher interest rates on balances incurred before a rate increase went into effect, unless the cardholder is more than 30 days late in paying his or her credit card bill. Although the proposal would not prohibit card issuers from raising rates because of a supposed problem with another creditor or a drop in a cardholder's credit scores (a practice often called "universal default"), forbidding issuers from applying higher rates to existing charges should discourage credit card companies from unjustifiably increasing cardholders' interest rates in many cases.

- **Hidden payment allocation methods that cause debts to escalate**. Credit card issuers would be required to more fairly apply the payments that cardholders make to balances with different interest rates. When consumers transfer balances with low, short-term "teaser" rates (that have higher rates for new purchases), or take out high-rate cash advances, issuers would be required to apply payments either to the higher rate debt or to both the higher and lower rate debt proportionately. Currently, credit card issuers apply payments only to the lower rate debt.

- **Interest charges on debts that have already been paid**. The proposal would forbid "double cycle billing," which results in cardholders paying interest on debts paid off the previous month during the grace period.

- **Excessive fees for low-credit cards**. The proposal would forbid credit card companies that target consumers with poor credit histories from requiring consumers to pay fees that amount to more than half of the credit being offered, if those fees are charged to the card that is being issued. If the fees being charged to the card amount to more than one-quarter of the credit line, cardholders would be allowed to pay these fees off over a six-month period.

Congress is considering a number of reforms that would address practices not targeted by these proposed rules:

- **Aggressive lending to young consumers**. Requiring credit card companies to consider the ability of consumers under the age of 21 to repay the loans they are offered and allowing them to affirmatively choose whether to receive credit card solicitations.

- **Excessive and growing penalty fees**. Requiring that penalty fees be reasonably related to the costs that credit card issuers incur because of a late or over-limit transgression.

- **Outrageous interest rate hikes**. Limiting "penalty" interest rate increases to 7 percent above the previous rate if the consumer fails, for instance, to make a payment on time, or requiring that penalty rate increases can only be imposed on future purchases.

- **Repeat over-limit fees**. Allowing over-limit fees to be charged only once, unless additional charges increase balances above the account limit.

- **Fees for paying a bill.** Prohibiting card issuers from charging a fee to consumers who pay a bill by telephone, on the internet, or by mail.

- **Unilateral changes in terms**. Prohibiting card issuers from altering credit card agreements while they are in force without specific written consent from the cardholder.

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Consumer Federation of America (CFA) is a non-profit association of 300 consumer groups, with a combined membership of more than 50 million people. CFA was founded in 1968 to advance the consumer's interest through research, advocacy and education.

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CREDIT CARD FACTS

- **Credit Cards in the U.S.: 1.22 billion.** (663 million bank cards, 555 million retail/gasoline cards.) *Source: CardTrack.com.*

- **Revolving Consumer Credit Outstanding in the U.S.: $969.9 billion**, as of July 2008. *Source: Federal Reserve Statistical Release, Consumer Credit Outstanding, Table G. 19, September 8, 2008.*

- **Credit Card Debt Held by Consumers in the U.S.: about $850 billion**, as of July 2008. *Source: CFA calculation,*[1] *based on the data above reported by the Federal Reserve Board.*

- **Average Credit Card Debt per Household: $7,430.** *Source: 114.4 million households; U.S. Census Bureau, "American Families and Living Arrangements 2006."*

- **Average Credit Card Debt per Card-Holding Household that Carries a Balance: $17,103.** *Source: 74.9 percent of households (about 85.7 million) have a credit card. 58 percent of households with a credit card*[2] *(about 49.7 million) do not pay their balance in full every month; Federal Reserve Board, "2004 Survey of Consumer Finances."*[3]

- **Credit Card Solicitations mailed in 2007: 5.2 billion.** *Source: Synovate Mail Monitor, "US credit card mail volume declined in 4th quarter 2007 as troubled issuers pull back," February 2008.*

- **Credit Card Solicitations per Household: 36**.

- **Credit Card Accounts that Pay a Late Fee: 35 percent**, representing about 242 million cards.[4]

- **Income from Penalty Fees for Six Largest Credit Card Issuers: $7.4 billion.**[5]

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[1] Revolving credit outstanding is often used as a proxy for credit card debt, but most experts believe that outstanding credit card debt is slightly less. Approximately 5 percent of consumer revolving credit is not on credit cards. Between 4 to 9 percent of the debt does not truly revolve. It is repaid to the credit card issuer before the next billing cycle starts. Taking these two factors into account, outstanding credit card debt is likely to be between $834.1 and $882.6 billion.

[2] This means that about 43 percent of all households carry all of the credit card debt that is outstanding.

[3] Bucks, Brian K., Kennickell, Arthur B. Moore, Kevin B., "Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances," p. 31, http://www.federalreserve.gov/PUBS/oss/oss2/2004/bull0206.pdf.

[4] "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, pg. 5. Thirty-five percent of the credit card accounts from the six largest issuers that the GAO examined had at least one late fee in 2005.

[5] "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, pg. 72. This figure is for 2005.