Testimony Of

Edmund Mierzwinski,
Consumer Program Director,
U.S. Public Interest Research Group

Before The
Subcommittee on Commercial and Administrative Law
of the United States House of Representatives
The Committee on the Judiciary
The Honorable Steve Cohen, Chair

At A Hearing Regarding The Question:

Are Credit Cards Bankrupting Americans?

2 April 2009

Testimony of Edmund Mierzwinski of U.S. PIRG

Chairman Cohen, Ranking Member Franks and members of the Subcommittee, I am Edmund Mierzwinski, Consumer Program Director and Senior Fellow of the non-profit, non-partisan U.S. Public Interest Research Group (U.S. PIRG).[1] We are pleased to offer our testimony today regarding credit card practices and consumer bankruptcy, specifically, on the question: "Are Credit Cards Bankrupting Americans?"

SUMMARY

Your hearing comes at an opportune time. Over the last several years, even after enactment of the draconian 2005 bankruptcy amendments[2] insisted upon by an eight-year credit card industry campaign, the credit card companies have continued to engage in arbitrary, abusive, and unfair credit card lending practices that trap consumers in a cycle of costly debt, such as sharply escalating "universal default" interest rates that can double some cardholders monthly payments overnight. Put simply, owning a credit company is a license to steal. You can change the rules at any time for any reason, including no reason. Pernicious mandatory arbitration clauses prevent consumers from private enforcement against unfair practices. State attorneys general have been preempted by federal regulators from enforcing laws against national banks and thrifts—nearly every large credit card company is a national bank. Those federal regulators, until a recent burst of consumer protection activity by the Federal Reserve, have encouraged the increasing use of unfair practices through lax oversight. Since 2000, the Office of the Comptroller of the Currency (OCC), chief regulator of national banks, has not imposed one public civil penalty or other sanction against a large credit card company.

Considerable evidence links the rise in bankruptcy in recent years to the increase in consumer credit outstanding, and, in particular, to credit card debt. The problem has been exacerbated by the 2005 bankruptcy amendments, which have made it harder and more expensive to file for bankruptcy, leaving many consumers in the credit card company "sweat box," despite no evidence that consumers are abusing the bankruptcy system. Consumers are hurt by credit card practices, but no longer have adequate relief. Congress should immediately reform credit card company practices and make changes to the bankruptcy code to provide relief to aggrieved consumers.

RECOMMENDATIONS TO THE COMMITTEE

Congress should take immediate action to restrict unfair credit card tricks and traps and increase enforcement of credit card laws. Congress should reform the bankruptcy laws so that the victims of these tricks and traps are not prevented from obtaining relief.

1. Congress should immediately enact the strongest possible credit card reforms. S. 414, the Credit CARD Act (Dodd), was approved Tuesday by the Senate Banking Committee. HR 627, the Credit Cardholders' Bill of Rights (Maloney), which passed the House in 2008, was

[1] The **U.S. Public Interest Research Group** serves as the federation of and federal advocacy office for the state PIRGs, which are non-profit, non-partisan public interest advocacy groups that take on powerful interests on behalf of their members. Main website is uspirg.org. Special credit card reform site is truthaboutcredit.org.
[2] Bankruptcy Abuse Prevention and Consumer Protection Act Of 2005, Public Law 109-8.

considered in a House Financial Services subcommittee yesterday. Both bills are more comprehensive than the proposed Federal Reserve rules.

a. Final reform should ban a variety of unfair tricks, including universal default clauses, where consumers in good standing are dinged with penalty interest rates for alleged late payments to others, or for no reason at all.
b. Final reform should ban "any time, any reason" changes to credit card contracts.
c. Final reform should prevent credit card companies from treating student consumers as special class, by issuing credit cards without regard for ability to repay.

2. Congress should enact the Arbitration Fairness Act, HR 1020 (Johnson), to eliminate mandatory arbitration clauses in credit card (and other consumer) contracts. Congress should take additional steps to reform consumer private rights of action against wrongdoers.
3. Congress should reinstate the rights of state legislatures to enact stronger laws against unfair practices of national banks and reinstate the rights of state attorneys general to enforce laws against national banks.[3] Congress should broaden state attorney general enforcement of federal laws, since federal regulators lack the resources and the will to defend consumers.
4. In 2006, Congress prohibited loans to military families at rates higher than 36% APR. Congress should reinstate usury ceilings for all Americans at the same rate, as proposed in HR 1608 (Speier).
5. Congress should enact a variety of changes to the bankruptcy code to restore its balance and protect Americans from the consequences of these and other unfair practices.
    a. Congress should immediately complete overdue action on the strongest possible version of legislation allowing bankruptcy judges to make loan modifications to prevent foreclosures (HR 200, Conyers). A broad variety of consumer, civil rights, labor and community groups continues to express disappointment to this simple reform to slow the 6,600 foreclosures occurring weekly, which also hurt neighborhoods and the taxpayers paying for the Wall Street bailout.
    b. Congress should take a variety of actions to amend the so-called Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. Among the simple actions it could take would be to lower the cost of filing for bankruptcy, subordinate high cost credit transactions to the claims of other claims in bankruptcy, make specific exemptions to means-testing requirements, and repeal pre-bankruptcy counseling requirements.[4]
6. Congress should require that any bank receiving taxpayer-backed infusions of TARP/TALF funds should immediately comply with the credit card rules finalized by the Federal Reserve in December but stayed for compliance until July 2010.

---

[3] In 2006, the Supreme Court decision in *Wachovia v. Watters* upheld the bulk of the OCC rules in a statutory interpretation. Before the court for oral argument this term is *Cuomo v. Clearinghouse and OCC*, which may reinstate a narrow portion of attorney general authority—to enforce remaining state consumer protection laws against national banks. The OCC holds that while some fair lending and other laws still apply, it is the only allowable enforcer.

[4] For a detailed analysis of these reforms, see testimony of John Rao, National Consumer Law Center, before the Senate Committee on the Judiciary, 4 December 2008. We concur with Mr. Rao's recommendations in their entirety. Hearing available at http://judiciary.senate.gov/hearings/hearing.cfm?id=3606

DISCUSSION

The Fed's change in regulatory approach is instructive of the worsening situation. The agency, which had relied largely on disclosures as protection, issued its first-ever regulation making certain credit card company practices illegal, using its unfair and deceptive acts and practices authority under Section 5 of the Federal Trade Commission Act.[5] The actions by the Fed, although they will not take effect until July 2010, came none too soon. However, action in both the House and Senate may result in passage of an even stronger law.[6]

Moderate-income families with little flexibility in their budgets are particularly hard hit if they have to pay more in unjustifiable fees and credit card interest. Signs that credit card delinquencies and defaults are rising sharply should be a further warning that these practices have helped make credit card loans unsustainable for many Americans. The meltdown of the subprime mortgage market demonstrates the importance of ending abusive lending practices when warning signs arise. Congress should take steps now to rein in these practices to forestall an even greater economic crisis.

There is considerable evidence linking the rise in bankruptcy in recent years to the increase in consumer credit outstanding, and, in particular, to credit card debt. The remainder of this testimony explains how the growth in the use of credit card tricks and traps occurred and its impact on consumers.

A. DID THE BANKRUPTCY LAW FAIL?

Yes, according to U.S. PIRG analysis of research by leading independent academics. "Did the Bankruptcy Law Fail" is the title of a recent article by some of the nation's leading bankruptcy specialists, including Professors Bob Lawless, Katherine Porter and Elizabeth Warren. Here is what they say, including their views on the role played by credit card companies, the leading proponents of that supposed reform enacted in 2005.

> These findings thus cast doubt on the suggestion that those purged from the bankruptcy courts - approximately 800,000 in 2007 alone based on trend extrapolation - were high-income deadbeats; they instead appear to have been ordinary American families in serious financial distress. The data also show that debtors filing for bankruptcy in 2007 have even greater debt loads than their counterparts from 2001, a development that seems to track a national trend of increasing consumer debt. The findings thus align with at least two predictions of some legal scholars. The first is that the bankruptcy reform bill was not aimed at high-income abusers but was instead a general assault on all debtors, regardless of their financial circumstances. **The second is that debtors are waiting longer - and incurring more debt - before ultimately**

[5] Federal Reserve, Office of Thrift Supervision and National Credit Union Administration rules amending Regulation AA and prohibiting certain credit card practices under authority to enforce Section 5 of the FTC Act were issued December 18, 2008 and take full effect in July 2010. The rules apply to all institutions, including those regulated by the OCC. http://www.federalreserve.gov/newsevents/press/bcreg/20081218a.htm

[6] S. 414, the Credit CARD Act (Dodd), was approved Tuesday by the Senate Banking Committee. HR 627, the Credit Cardholders' Bill of Rights (Maloney), which passed the House in 2008, was considered in a House Financial Services subcommittee yesterday. Both bills are more comprehensive than the rules and would take effect earlier.

seeking bankruptcy relief, consistent with the so-called "sweat box" theory of credit card lending [emphasis added]. [7]

These experts go on to explain that since 2005 nothing has really changed in the demographics of people who file for bankruptcy and why they file. Over 90% of filings are still because people get sick, or get divorced or lose their job or a substantial part of their income. Things have just gotten worse for them in the period before they file, if they file:

> The debtors who filed for bankruptcy in 2007 also looked worse than their 2001 counterparts in another respect: they had much more credit card, medical, utility, and other unsecured debt—debt that is either due immediately (utility) or very expensive when financed long-term (credit card).[8]

That sweat box theory is a term coined by another expert, Ronald Mann, who explains it thus:

> In my view, the most important aspect of the new [2005 bankruptcy] law is not the increased payouts associated with means testing, but the way in which the law encourages debtors to defer bankruptcy filings. […] Another key part of the business model, related to the high switching costs for distressed borrowers, is the increasing ability of the leading issuers to collect substantial revenues in the form of late and over-limit fees. […] the interest rates that borrowers pay while they are in the sweat box greatly exceed the cost of the lender's funds. Thus, if the borrower resides in the sweat box for very long—making substantial interest payments at a high rate—the lender with a lower cost of funds in effect receives a return of the funds that it has lent each month. If we imagine borrowers who limp along, carrying those balances for decades—neither discharging them in bankruptcy, nor ever paying them off entirely, perhaps making an occasional minor purchase—we can see how profitable this business model [the sweat box] can be.[9]

Mann goes on to explain that with these very high interest rates, and low monthly payments at high interest rates and more than occasional penalty fees paid by the consumers in the sweat box, that a consumer account might prove economically profitable after just 30-34 months, but that the affected consumer would have many years more to go to pay off his or her balance. Mann: "this is just about long enough for the lender to recover its investment, but not nearly long enough for the cardholder to repay its debt."[10]

---

[7] Quotation is from authors' abstract. Lawless, Robert M., Littwin, Angela K., Porter, Katherine M., Pottow, John, Thorne, Deborah and Warren, Elizabeth, Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors (October 17, 2008). American Bankruptcy Law Journal, Vol. 82, pp. 349-406, 2008; U of Michigan Law & Economics, Olin Working Paper No. 08-023; U of Michigan Public Law Working Paper No. 133; U Illinois Law & Economics Research Paper No. LE08-034; U of Texas Law, Law and Econ Research Paper No. 136; Harvard Law and Economics Discussion Paper; U Iowa Legal Studies Research Paper No. 08-50. Available at SSRN: http://ssrn.com/abstract=1286284

[8] *Ibid.*

[9] Mann, Ronald J., Bankruptcy Reform and The 'Sweat Box' of Credit Card Debt. University of Illinois Law Review, 2006; U of Texas Law, Law and Econ Research Paper No. 75. Available at SSRN: http://ssrn.com/abstract=895408

[10] *Ibid.*

So, it is very clear to bankruptcy experts that the 2005 reforms may have reduced the number of bankruptcy filings, but at a high cost. By making it both harder and more expensive to file for bankruptcy, and then to avoid paying off unsecured debt if you do manage to file, the bankruptcy bill has allowed credit card companies to keep consumers in the "sweat box."

So, to answer the committee's question posited in this hearing, yes, credit cards are bankrupting Americans. While some consumers bearing the brunt of unfair credit card practices may not ever file for bankruptcy, those that do end up filing are worse off than previously because they have been paying more and more credit card penalty fees and penalty interest for a longer period before they file. Of course, once they do go through the new hoops and pay the higher fees required to finally file, they then face the difficulties of the new bankruptcy law itself, which has a tough means test that requires more of them to enter Chapter 13 repayment plans that then require continued payment of those unsecured debts to credit card companies. As Mann points out, the credit card company has probably already found that consumer profitable. It then uses the bankruptcy law to squeeze more from him or her and delay their re-entry into the full economic system.

B. CARDHOLDERS ARE SHOWING SERIOUS SIGNS OF ECONOMIC STRESS

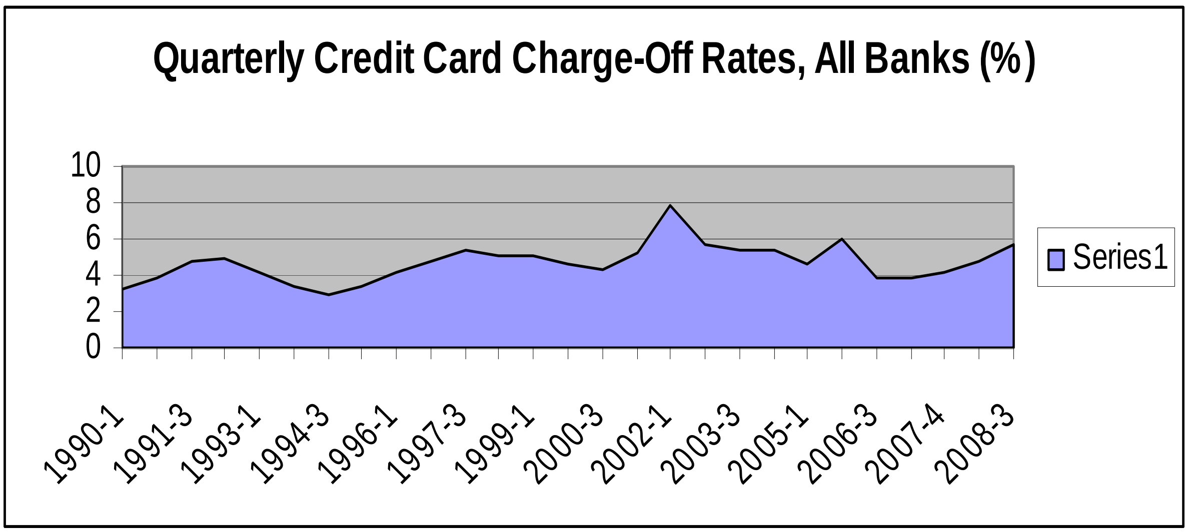
Credit card debt now held by Americans is approaching one trillion dollars,[11] up 20% since 2003.[12] Lower income and minority Americans face a higher burden of debt as a percentage of income than more affluent Americans, placing greater stress on them.[13]

As the economy has worsened and home foreclosures have increased to record levels, consumers are increasingly having serious difficulty paying their credit card bills. One widely watched measure of financial health, the amount of credit card debt paid off by Americans monthly, is now at one of the lowest levels ever recorded.[14] Credit card charge-offs, the percentage of the value of credit card loans removed from the books (net of recoveries), or "written off," have been persistently high for most of the last thirteen years and are now approaching the highest levels on record. During the decade between the end of 1995 and the start of 2006, credit card charge-offs were not below 4 percent in a single quarter.[15] They increased to more than 4 percent in the fourth quarter of 2006 and broke 4 percent again during the later half of 2007. Since then, charge-offs have escalated sharply to 5.62 percent in the third quarter of 2008. There is a very good chance that charge-offs will keep rising because the number of delinquent credit card payments – an early sign of payment difficulty – are also approaching historically high levels. Thirty-day credit card

[11] According to Federal Reserve statistical release G-19 for March, revolving debt (nearly all is credit card debt) was $961 billion dollars in January 2009.
[12] Garcia, Jose, "The New Squeeze: How A Perfect Storm of Bad Mortgages and Credit Card Debt Could Paralyze the Recovery," Demos, 2008. Available at http://www.demos.org
[13] Garcia, Jose, :Borrowing To Make Ends Meet," Demos, 2007, available at http://www.demos.org
[14] Chu, Kathy, "November Credit-Card Payoff Rate Fell Sharply," *USA Today*, February 8, 2009. The monthly payment rate fell by 2.5 percentage points to 16.1 percent in November 2008, according to CardTrak.com.
[15] Federal Reserve Board, "Charge-Off and Delinquency Rates on Loans and Leases at All Commercial Banks," available at www.federalreserve.gov/release/chargeoff. Most experts attribute lower charge-offs in 2006 to the surge of bankruptcy filings (and corresponding increase in charge-offs) that occurred in the third and fourth quarters of 2005.

delinquencies are now at their highest point in six years, since the last economic recession ended.[16] Moreover, a number of major issuers have reported fourth quarter charge-offs that indicate that borrower defaults and issuer losses will exceed those of the last two recessions.[17] The difficulty that many families are having affording their credit card bills has been exacerbated by the mortgage crisis. As home values have dropped sharply, Americans have been unable to use home equity loans and home refinancing to pay off their credit card debts.[18] Moreover, despite rising credit card delinquencies, there is evidence that some families are attempting to stay current on their credit card loans but not their mortgage payments, a shift in behavior from past economic crises.[19]

Quarterly Credit Card Charge-Off Rates, All Banks (%)[20]



Source: Federal Reserve.

Although some issuers have suffered losses in the last year, over time the credit card industry has been the most profitable in the banking sector, earning a return on assets (ROA) from 1995 to 2008 that was more than three times greater than that for commercial banks overall.[21] Because of the

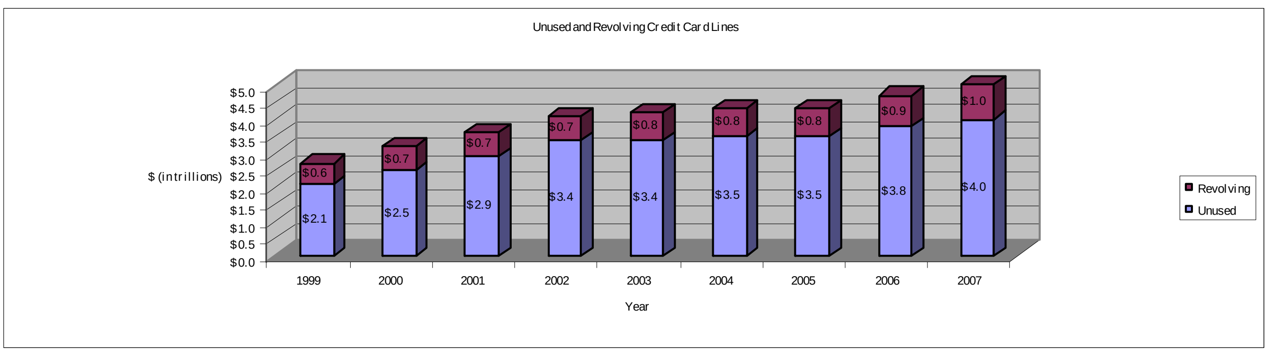
[16] 30-day credit card delinquencies during first three quarters of 2008 were between 4.79 and 4.88 percent, the highest levels since 2002. Federal Reserve Board, "Charge-Off and Delinquency Rates on Loans and Leases at 100 Largest Commercial Banks" "U.S. Credit Card Delinquencies at Record Highs – Fitch," *Reuters*, February 4, 2009.
[17] Terris, Harry, "Credit Card Losses Seen Surpassing Levels of Last Two Recessions," *American Banker*, January 28, 2009.
[18] Westrich, Tim and Weller, Christian E., "House of Cards, Consumers Turn to Credit Cards Amid the Mortgage Crisis, Delaying Inevitable Defaults," Center for American Progress, February 2008.
[19] Chu, Kathy, "More Americans Using Credit Cards to Stay Afloat," *USA Today*, February 28, 2008.
[20] Federal Reserve Board, "Charge-Off and Delinquency Rates on Loans and Leases at All Commercial Banks," available at www.federalreserve.gov/releases/chargeoff/chgallsa.htm , accessed April 14, 2008.
[21] "Card Profits 04," *CardTrak*, January 24, 2005; "Banner Year," *CardTrak*, February 2004; FDIC, *FDIC Quarterly Banking Profile*, Third Quarter 2006 at 5, Table I-A; FDIC, *FDIC Quarterly Banking Profile*, Fourth Quarter 2000 at 4, Table I-A. Commercial banks' average return on assets between 1995 and 2004 was 1.23 percent, less than one third the size of the credit card industry average return on assets of 3.73 percent over the same period, according to R.K. Hammer and Associates.

high mortgage losses that many large banks experienced in 2007, there was more than a five-fold difference between bank and credit card profits.[22]

C. CONSUMERS HAVE SHOWN FAR MORE CAUTION IN TAKING ON CREDIT CARD DEBT THAN ISSUERS USED IN MARKETING AND EXTENDING CREDIT

It is conventional wisdom that consumer demand fueled the growth of revolving debt to about $961 billion.[23] However, a careful analysis of lending patterns by credit card companies shows that aggressive and even reckless lending by issuers played a huge role in pushing credit card debt to record levels. From 1999 through 2007, creditor marketing and credit extension increased about twice as fast as credit card debt taken on by consumers,[24] even though the rate of growth in credit card debt in 2007 was the highest it had been since 2000.[25]

The debt growth rate started slowing in the second quarter of 2008 and then experienced a rare decline in the fourth quarter.[26] This most significant reason for this drop was probably the decline in consumer spending brought on by the recession. Additionally, issuers significantly reduced their marketing of new credit and started reducing some existing credit lines in the latter half of 2008.[27]



Source: VERIBANC, Federal Reserve.

---

[22] ROA for credit card issuers in 2007 was 4.65%, R.K. Hammer and Associates, January 2008. ROA for commercial banks in 2007 was .86%, FDIC, "Banks and Thrifts Earned $105.5 billion in 2007," February 26, 2008.
[23] As of January 2009, the amount of revolving debt held by Americans was $961billion. Although this figure is often used as a proxy for credit card debt, most experts believe that outstanding credit card debt is slightly lower. First, approximately 5 percent of consumer revolving credit is not on credit cards. Second, 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 $829 and $877 billion.
[24] VERIBANC, Inc. (www.VERIBANC.com) and Federal Reserve Consumer Credit Outstanding. According to Federal Reserve figures, consumer revolving debt grew by 50 percent from $627.5 billion in December 1999 to $941.4 billion in December 2007. According to VERIBANC, unused lines of credit grew at almost double the rate (90.5 percent) that consumers increased their use of credit card lines, increasing from $2.1 trillion in 1999 to just under $4.0 trillion ($3,983,200,614) at the end of 2007.
[25] The amount of revolving debt increased by 7.8 percent in 2007, which was the sharpest increase since revolving debt grew by 11.6 percent in 2000. Federal Reserve, Statistical Release, "Consumer Credit Outstanding," Table G.19.
[26] The amount of credit card debt in the fourth quarter of 2008 dropped by 5.4 percent, from $976.7 billion to $963.5 billion. Federal Reserve, Statistical Release, "Consumer Credit Outstanding," Table G.19.
[27] Wolfe, Daniel, "Top Issuers, with Less Appetite for Risk, Slashing Credit Lines, *American Banker*, December 2, 2008. Banjo, Shelly, "Credit Card Companies Slash Credit Limits," *The Wall Street Journal*, January 5, 2009.

A similar trend is evident when examining the consumer response to massive increases in marketing by creditors that started in 1990. The most significant form of marketing for creditors remains solicitation by mail. Over half of credit cards held by consumers are the result of mail solicitation.[28]

Issuers increased the number of mailed credit card offerings six-fold from 1990 to 2005, from just over 1.1 billion to a record 6.06 billion.[29] Since then, solicitations dropped to 5.8 billion in 2006, 5.2 billion in 2007, and 3.8 billion in 2008.[30] Wealthier families receive the highest number of credit card mailings, but low-income families are more likely to open the solicitations they receive.[31] The table at right indicates that issuer interest in marketing credit cards grew much faster than consumer interest in accepting new cards. The consumer response rate to mail solicitations declined seven-fold from 2.1 percent in 1990 to 0.3 percent in 2005, picking up slightly to 0.5 percent in 2006 and 2007. This means that for every 250 solicitations consumers receive, they reject more than 249. The tiny response rate demonstrates that the vast majority of consumers are being responsible when offered unsolicited credit.

	Solicitations (billions)[32]	Response Rate
1990	1.1	2.1%
1991	0.99	2.4%
1992	0.92	2.8%
1993	1.5	2.2%
1994	2.5	1.6%
1995	2.7	1.4%
1996	2.38	1.4%
1997	3.01	1.3%
1998	3.44	1.2%
1999	2.54	1.0%
2000	3.54	0.6%
2001	5.01	0.6%
2002	4.89	0.5%
2003	4.29	0.6%
2004	5.23	0.4%
2005	6.06	0.3%
2006	5.8	0.5%
2007	5.2	0.5%

D. ISSUERS ENCOURAGE THE LEAST SOPHISTICATED AND RISKIEST HOUSEHOLDS TO RUN UP UNSUSTAINABLE LEVELS OF DEBT

The growth of revolving debt in this country to $964 billion has obviously not affected all Americans equally. The extraordinary expansion of the credit card industry in the 1990s was fueled by the marketing of credit cards to populations that had not had widespread access to mainstream credit, including lower- and moderate-income households, consumers with seriously blemished credit histories, college students, older Americans and minorities.

In a practice widely known as risk-based pricing, creditors charged riskier consumers more to cover potential losses, usually in the form of higher interest rates. To make the assumption of debt more attractive to these households – and to entice them into carrying debt for longer periods – creditors lowered minimum payment balances from around five percent of principal to just over two percent. As a result, an estimated eighty percent of all households now have at least one card.[33] According to

[28] Vertis Inc., press release, "Financial Direct Mail Readers Interested in Credit Card Offers," January 25, 2005; "Card Marketing 101," *CardTrack*, September 2002.
[29] Synovate Mail Monitor, press release, "Mail Monitor Reports Record Six Billion Credit Card Offers Mailed in U.S. during 2005," April 27, 2006.
[30] Synovate Mail Monitor, press release, "U.S. Credit Card Mail Volume Declined to 3.8 billion in 2008," January 30, 2009.
[31] Kidane, Amdetsion and Sandip Mukerji, Howard University School of Business, "Characteristics of Consumers Targeted and Neglected by Credit Card Companies," *Financial Services Review*, Vol. 13, No. 3, 2004 at 186.
[32] Synovate Mail Monitor
[33] Cardweb.com

the Federal Reserve Board, about 42 percent of cardholding households pay their credit card bill in full every month,[34] which means that the remaining 50 million or so families that carry debt owe an average of about $17,000.[35]

Moderate and lower income households that are more financially vulnerable shoulder a significantly higher level of debt relative to their incomes. In the current economic climate, these households are also under financial pressure from many external factors, such as flat wages, rising unemployment, skyrocketing home foreclosures and increasingly unaffordable health insurance. In other words, the "democratization of credit" has had serious negative consequences for many Americans, putting them one unexpected financial emergency away from bankruptcy.

Lower-Income and Minority Households

Close to half of all minority families in the U.S. carry credit card debt.[36] Although lower and moderate-income households are less likely to have bank credit cards than more affluent families, they are more likely to carry over debt from month-to-month. Sixty one percent of the lowest income households with a card carry balances, compared to 45 percent of higher income families.[37] Credit card debt also represents a significant portion of lower-income families' income. A 2004 Gallup poll found that families with credit card debt earning under $20,000 a year owed 14.3 percent of their income in credit card debts, those earning between $20,000 and $29,999 owed 13.3 percent and those earning between $30,000 and $39,999 owed 11.0 percent. Compare this to the 2.3 percent of their income owed by families earning over $100,000.[38] The increase in credit card debt has contributed to alarmingly high overall levels of debt for many of these lower and moderate-income families. More than one-quarter of the lowest income families spent over 40 percent of their income on debt repayment in 2001.[39]

---

[34] Bucks, Brian K., Arthur B. Kennickell and Kevin B. Moore, "Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances," Federal Reserve Bulletin, vol. 92, February 2006, pg. 31.
[35] CFA calculation based on estimated credit card (as opposed to revolving) debt of $850 billion. If a conservative estimate of 75 percent of 114.4 million households have credit cards, and only 58 percent of these households carry debt, then the remaining 49.7 million households have an average of $17,103 in debt.
[36] Bucks, Brian K., Arthur B. Kennickell and Kevin B. Moore, "Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances," *Federal Reserve Bulletin*, vol. 92, February 2006, pg. 24.
[37] Board of Governors of the Federal Reserve System, "Report to the Congress on Practices of the Consumer Credit Industry in Soliciting and Extending Credit and their Effects on Consumer Debt and Insolvency," submitted to the Congress pursuant to section 1229 of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, June 2006 at 9 Table 6.
[38] Gallup Poll News Service, "Average American Owes $2,900 in Credit Card Debt," April 16, 2004.
[39] Aizcorbe, Kennickell and Moore 2003 at 29, Table 14. In 2001, more than one in four (27.0%) families in the lowest income quintile spent more than 40% of their income on debt payments, compared to less than one in six (16.0%) of families in the second lowest income quintile and one in nine (11.0%) of all families who spent 40% or more of their income on debt payments.

Younger and Older Americans

Starting in the early 1990's, credit card issuers targeted massive marketing efforts at college campuses throughout the country, resulting in a sharp growth of credit card debt among college-age and younger Americans. The Consumer Federation of America (CFA) [40] with Dr. Robert Manning, and U.S. PIRG[41] were among the first to document the serious consequences of this trend. Since U.S. PIRG's 1998 Campus Credit Card Trap report and Dr. Manning's report for CFA in 1999, this issue has been the subject of much public and media scrutiny. And yet, Americans under 35 years-of-age continue to show more signs of trouble managing credit card debt than any other age group. The amount of credit card debt held by students graduating from college more than doubled to $3,262 between the mid-1990s and 2004.[42] Americans under 35 are less likely to pay off their credit card balances every month than average Americans,[43] are paying more for debt obligations than in the past and are increasingly likely to pay more than 40 percent of their incomes on credit card debt.[44] Moreover, there is increasing evidence that issuers are now targeting high school students with credit card offers.[45] They are also marketing branded debit cards to adolescents, in part to encourage these young consumers to use similarly branded credit cards when they are older.[46] U.S. PIRG's most recent report also documented intense marketing of credit cards on college campuses and the growing use of contracts between colleges (sometimes through their alumni associations) and credit card companies for exclusive marketing of both credit and debit cards to college students.[47]

The growth of credit card debt among older households is also troubling. Although these households were long thought to be the most frugal and resistant to consumer debt, changing economic conditions – especially declining pension and investment income coupled with rising health care and prescription costs – have made credit card debt a more serious financial issue for older Americans. Between 1992 and 2001, Americans over age 65 saw their credit card debt nearly double from $2,143 to more than $4,000.[48] The number of seniors filing for bankruptcy more than

[40] Manning, Robert, "Credit Cards on Campus: Costs and Consequences of Student Debt," June 8, 1999. CFA Press Release available at: http://www.consumerfed.org/ccstudent.pdf

[41] Mierzwinski, Edmund, "The Campus Credit Card Trap," April 1998, U.S. PIRG Education Fund; Mierzwinski, Edmund and Lindstrom, Christine, "The Campus Credit Card Trap: A Survey of College Students and Credit Card Marketing," March 2008, U.S. PIRG Education Fund; Mierzwinski, Edmund and Lindstrom, Christine, "Characteristics of a Fair Campus Credit Card," U.S. PIRG Education Fund, April 2008. Both of the 2008 reports are available at http://www.truthaboutcredit.org.

[42] Trigaux, Robert, "Generation Broke: New Grads Bear Heavy Load," *St. Petersburg Times*, November 22, 2004.

[43] Draut, Tamara, Director of Demos Economic Opportunity Program, Testimony Before the House Banking Committee Subcommittee on Financial Institutions and Consumer Credit, September 15, 2004, at 8. More than half (55%) of Americans carry revolving balances compared to 71% of borrowers aged 25-34.

[44] *Ibid*. at 4-5. In 1992, about one in thirteen (7.9%) Americans aged 25-34 had debt greater than 40% of their income; by 2001, about one in eight (13.3%) had these high debt burdens.

[45] Mayer, Caroline E., "Girls Go From Hello Kitty To Hello Debit Card; Brand's Power Tapped to Reach Youth," *The Washington Post*, October 3, 2004.

[46] Ludden, Jennifer, "Credit Card Companies Target Kids," *All Things Considered*, National Public Radio, February 6, 2005.

[47] Testimony of Christine Lindstrom, Director U.S. PIRG Higher Education Program, at a hearing on "Problem Credit Card Practices Affecting Students: The Need for Legislative Action," before the Subcommittee on Financial Institutions, June 26, 2008 available at http://financialservices.house.gov/hearing110/hr0626084.shtml.

[48] Demos, "Retiring in the Red," January 19, 2004 at 3.

tripled from 1991 to 2001.[49] More recent data from a 2008 AARP report[50] show that "Americans 55 and older have experienced the sharpest increase in bankruptcy filings."

Seniors have fewer credit cards than other age groups and are more likely to pay their credit cards in full every month, but a greater proportion of older Americans also have lower incomes.[51] This means that credit card debt has a more severe impact on this age group. For example, credit card debt can threaten older homeowners, who stand to lose their home – and their most significant hedge against poverty – if they use home equity to pay off credit card debt.

The Downsizing of Minimum Payments

As credit card issuers dramatically expanded their marketing and extension of credit in the 1990s, they lowered monthly minimum payment amounts. By reducing the minimum payment, issuers could offer more credit, encourage consumers to take on more debt, and ensure that consumers would take far longer to pay off their debts, thus making them more profitable for the industry.[52] Monthly minimum payment rates were reduced from around 5 percent of principal owed in the 1970s to just over 2 percent by the turn of the century.[53] In 2005, 19 million credit card borrowers make only the minimum payments.[54]

The number of consumers paying just above the minimum rate is even larger. In a representative survey conducted for the Consumer Federation of America by Opinion Research Corporation in November of 2005, 34 percent of those questioned said that they usually pay the minimum rate or somewhat more. More than 40 percent of respondents earning less than $50,000 a year said they paid the minimum rate or somewhat more, while 45 percent of African Americans and 51 percent of Hispanics did so.[55] An examination by the Credit Research Center of 310,000 active credit card accounts over 12 consecutive months in 2000 and 2001 found similar results. Just under one-third of the accounts paid 5 percent or less per month of the total amount due.[56] Moreover, payment habits for many cardholders are not static over time. Depending on the economic circumstances of the cardholder involved, he or she could shift from fully paying outstanding balances every month to paying at or near the minimum rate.

However, paying only the minimum on credit cards can increase the length of time the debt is carried and significantly add to the interest cost of the credit card loan. Julie Williams, the First

---

[49] Sullivan, Theresa A., Deborah Thorne and Elizabeth Warren, "Young, Old, and In Between: Who Files for Bankruptcy?" *Norton Bankruptcy Law Advisor*, Iss. No. 9A, September 2001, at 5. The number of older Americans declaring bankruptcy during this period rose from 23,890 to 82,207.

[50] Generations of Struggle, Research Report, AARP Research Institute, Deborah Thorne, Ohio University, Elizabeth Warren, Harvard Law School, Teresa A. Sullivan, University of Michigan, June 2008, available at http://www.aarp.org/research/credit-debt/debt/2008_11_debt.html

[51] Hanway, Steve, "Do Credit Card Habits Improve with Age?" Gallup News Organization, May 18, 2004. Nearly half (48%) of households over 65 years old have incomes below $30,000, compared to 16% of those aged 30-49 and 18% of those aged 50-64.

[52] Interview with Andrew Kahr, credit card industry consultant, "The Secret History of the Credit Card," *Frontline*, November 2004.

[53] Kim, Jane J., "Minimums Due on Credit Cards are on the Increase," *Wall Street Journal*, March 24, 2005.

[54] Der Hovanesian, Mara "Tough Love for Debtors," *Business Week*, April 25, 2005.

[55] Opinion Research Corporation, "Consumer Financial Services Survey," November 3-7, 2005.

[56] Credit Research Center, McDonough School of Business, Georgetown University.

Senior Deputy Comptroller and Chief Counsel of the Office of the Comptroller of the Currency (OCC) has noted that reduced minimum payments "dig borrowers into an ever deeper hole, requiring increasingly more difficult measures" for consumers to get out of debt.[57] CFA has concluded that reduced minimum payments were a significant cause of increasing bankruptcies in the last decade.[58]

One way to alert consumers to the consequences of paying off credit card balances at the minimum rate is to offer each consumer a personalized notice on the billing statement about how long it would take to pay off the balance at the minimum rate, and what would be the total costs in interest and principal.[59] Such a personalized disclosure is, unfortunately, not included in the recent bankruptcy law, which requires consumers to call a toll-free number to get information about how long it would take to pay off their balances.[60] No specific information would be offered on the total cost of paying at the minimum rate. This bankruptcy law requirement will likely have no impact on the millions of consumers paying at or near the minimum rate who will not call a toll-free phone number.

One positive development regarding credit card minimum payments is that regulatory guidance issued by federal banking regulators in January 2003 directed credit card lenders to set minimum payments that "amortize the current balance over a reasonable period of time" and noted that prolonged negative amortization would be subject to bank examiner criticism.[61] Many major credit cards began increasing their minimum payments requirements in 2005, including Bank of America, Citibank, Discover and JP Morgan Chase,[62] in some cases to as high as 4 percent.[63] All issuers were required to fully phase in the changes by the end of 2006.[64]

The Office of the Comptroller of the Currency (OCC) has warned banks that increasing minimum payments may need to be accompanied by a reduction in Annual Percentage Rates (APRs) or eliminating fees to ensure that cardholders can actually reduce their balances and not just tread water with higher minimum bills.[65] Since the increases took effect, consumers with interest rates

[57] OCC, Remarks by Julie L. Williams, First Senior Deputy Comptroller and Chief Counsel before the Risk Management Association's Retail Risk Management Conference on Regulatory Concerns about Certain Retail Banking Practices, Chicago, June 3, 2003, in "Speeches and Congressional Testimony," *OCC Quarterly Journal*, Vol. 22, No. 3, September 2003 at 107.
[58] Consumer Federation of America, "Consumer Restraint Pressures Lenders to Reduce Credit Card Marketing and Credit Extension," January 18, 2000.
[59] Proposed in S. 1176 by Senators Akaka, Durbin, Leahy and Schumer.
[60] Public Law 109-8. This weaker provision has been implemented as part of the Regulation Z disclosure rules approved by the Federal Reserve and other regulators on 18 December 2008 but compliance is not required until July 2010.
[61] Joint press release of Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency and Office of Thrift Supervision, "FFIEC Agencies Issue Guidance on Credit Card Account Management and Loss Allowance Practices," January 8, 2003, see attached "Account Management and Loss Allowance Guidance" at 3.
[62] American Financial Services Association, "Credit Card Minimum Payments Going Up," *Spotlight on Financial Services*, April 2005.
[63] Warnick, Melody, "Credit Card Minimum Payments Doubling," *Bankrate.com*, May 3, 2005. Citibank and Bank of America have announced they are doubling their minimum payment requirements from 2% to 4% of the balance.
[64] Day, Kathleen and Caroline E. Mayer, "Credit Card Penalties, Fees Bury Debtors," *Washington Post*, March 6, 2005.
[65] Der Hovanesian, Mara "Tough Love for Debtors," *Business Week*, April 25, 2005.

above 20 percent have had to cope with payments that have roughly doubled.[66] Consumer groups are unaware of banks that have reduced interest rates.

Targeting Consumers on the Brink of Financial Distress

Nothing illustrates the perverse incentives (and dangers) of the credit card market better than the marketing of cards to consumers with tarnished credit histories, or even worse, to those who are literally on their way to or just coming out of bankruptcy. For example, in the first half of 2007, as home mortgage foreclosures shot up and signs of a serious economic slowdown started to appear, some of the nation's largest credit card issuers increased the number of solicitations they mailed to sub-prime consumers by 41 percent compared to the first half of 2006.[67]

Other major issuers and many smaller companies market high-cost, sub-prime cards to those with blemished credit histories. This population of cardholders can be profitable for the industry. Credit card industry consultant Andrew Kahr estimates that average sub-prime consumers will make two or three late payments a year, from which the industry can generate a separate fee, and that these fees can greatly exceed the interest payments on the small lines of credit themselves.[68]

Sub-prime consumers haven't just encountered high-cost offers of credit, but deceptive marketing practices. In 2000, Providian was required to pay more than $300 million in restitution to its sub-prime cardholders for unfair and deceptive practices.[69] Cross Country Bank, the sub-prime and secured credit card issuer that has been investigated by state and federal regulators for misleading consumers about the terms of its sub-prime credit card accounts and engaging in abusive collection practices, has advertised on late-night and daytime television when more unemployed potential sub-prime customers are more likely to be watching television.[70]

In December of 2008, sub-prime card marketer Compucredit reached a settlement with federal regulators to provide at least $114 million in consumer redress and pay a $2.4 million fine for deceptive marketing of high-fee, low-limit credit cards. Among other allegations, Compucredit was accused of marketing cards with a $300 limit, but failing to adequately disclose the $185 in fees that would be immediately charged to the card.[71]

Consumers exiting bankruptcy are often swamped with offers at prime terms – low interest rates and without annual fees.[72] Many bankruptcy attorneys believe these offers are being made because consumers leaving bankruptcy court cannot erase their debts for another six years. Under the new bankruptcy legislation consumers will not be able to wipe away any credit card debts for eight

[66] "Minimum Payments," *CardTrack*, September 6, 2006.
[67] Gavin, Robert, "Credit Card Companies Pursue Subprime Borrowers," *Boston Globe*, September 5, 2007.
[68] Interview with Andrew Kahr, credit card industry consultant, "The Secret History of the Credit Card," *Frontline*, November 2004.
[69] OCC, Statement of Comptroller of the Currency John D. Hawke J., June 28, 2000.
[70] Pacelle, Mitchell, "Pushing Plastic," *Wall Street Journal*, November 5, 2004.
[71] "Subprime Credit Card Marketer to Provide At Least $114 Million in Consumer Redress to Settle FTC Charges of Deceptive Conduct," Federal Trade Commission, Dec. 19, 2008, http://www.ftc.gov/opa/2008/12/compucredit.shtm.
[72] Mayer, Caroline E., "Bankrupt and Swamped with Credit Offers," *Washington Post*, April 15, 2005.

years. Some categories of credit card debt will not be "dischargeable" at all, no matter how long the consumer waits.[73]

E. ISSUERS HAVE PURSUED ABUSIVE INTEREST RATE, FEE AND RISK MANAGEMENT POLICIES THAT HAVE A HARMFUL IMPACT ON MANY HOUSEHOLDS, AFFECTING BANKRUPTCY RATES

There is considerable evidence linking the rise in bankruptcy in recent years to the increase in consumer credit outstanding, and, in particular, to credit card debt. For example, research by the previously referenced Professor Ronald Mann of Columbia University has found that an increase in credit card spending in the U.S. and four other countries has resulted in higher credit card debt, which is strongly associated with an increase in bankruptcy filings.[74] To make matters worse, credit card companies have become far more aggressive in implementing questionable fees and interest rate practices in recent years. The upshot of these practices is that penalty interest rates, high and accumulating fees and interest on fees can push consumers with high debts over the financial brink into bankruptcy.[75] In fact, consumers in debt trouble sometimes owe as much or more in fees and penalty interest charges, as in principal.

High fees and interest rates can often result in negative amortization, where the principal owed on credit card debt continues to rise despite making payments. Negative amortization in effect traps credit card borrowers on a debt treadmill that keeps moving faster. Although they are making regular payments, their debts continue to mount. In 2004, a Cleveland judge ruled against Discover Card's efforts to collect debts from a cardholder whose balance nearly tripled from $1,900 to $5,564 without making additional purchases because of fees and penalties, including $1,158 in over-limit fees alone. The judge ruled that Discover's practices were unconscionable under state law.[76]

In another case, a bankruptcy court in North Carolina ordered a credit card company to itemize the claims it files in chapter 13 bankruptcy cases.[77] In its findings in support of the Order, the bankruptcy judge listed claims filed in eighteen separate cases broken down between principal and interest and fees. On average, interest and fees consisted of more than half (57 percent) of the total amounts listed in the claims. In one case, the card company filed a claim in the amount of $943.58, of which $199.63 was listed as principal and $743.95 was listed as interest and fees. In another case, a claim of $1,011.97 consisted of $273.33 in principal and $738.64 in interest and fees. It is almost certain that pre-bankruptcy payments in these cases had more than paid off the real charges made by the consumers.[78]

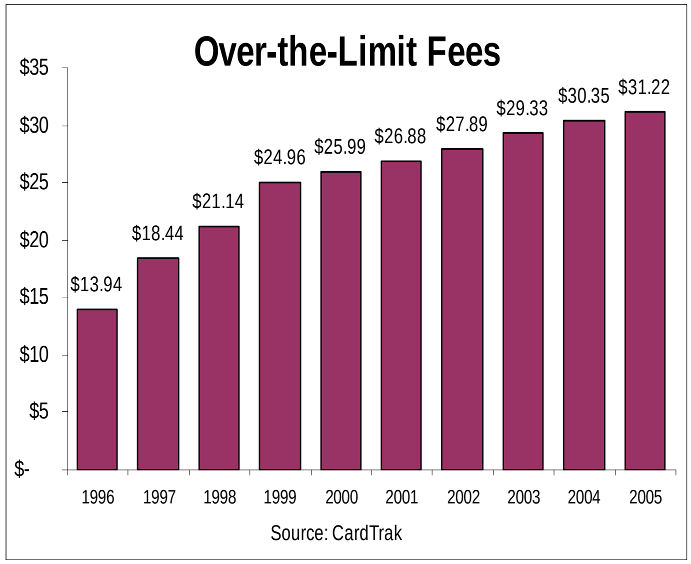
While the 2005 changes may have reduced overall filings, at least in the short run, the changes have not reduced unfair practices by credit card companies.

---

[73] *Ibid*.
[74] Mann, Ronald J., "Credit Cards, Consumer Credit and Bankruptcy," Law and Economics Research Paper No. 44, The University of Texas School of Law, March 2006.
[75] Day, Kathleen and Caroline E. Mayer, "Credit Card Penalties, Fees Bury Debtors," *Washington Post*, March 6, 2005.
[76] National Consumer Law Center, "Responsible Consumers Driven into Default," February 22, 2005.
[77] *In re* Blair, No. 02-1140 (Bankrate. W.D.N.C. filed Feb. 10, 2004)
[78] National Consumer Law Center, "Responsible Consumers Driven into Default," February 22, 2005.

Penalty Fees

Traditionally, penalty fees were designed to deter irresponsible cardholder behavior, but in recent years these fees have become primarily a revenue enhancer for credit card issuers. An analysis by the United States Government Accountability Office (GAO) found that, "…typical cards today now include higher and more complex fees than they did in the past for making late payments, exceeding credit limits, and processing returned payments."[79] The GAO also identified several new fees that issuers have begun using in recent years, some of which they are not required to disclose to consumers in advance. One example of such a fee is the so-called "pay-to-pay" fee for the payment of bills by telephone, which can range from 5 to 15 dollars.[80]



A substantial number of Americans are paying these fees. 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,[81] representing about 242 million credit cards. [82] Thirteen percent of all accounts – or about 90 million cards – were assessed over-limit fees in 2005.

Late fees have been steadily rising over the past decade and can easily exceed monthly payments for consumers paying low minimum balances.[83] In 1996, a Supreme Court decision prohibited states from setting limits on the fees credit card companies could charge their cardholders. Prior to this court ruling, credit card late fees were commonly around five to ten dollars, but have risen sharply since the decision.[84] The GAO analysis found that late fees jumped sharply after the court ruling. The GAO examined fee data collected by CardWeb.com and found that late fees jumped by 160 percent from $12.83 in 1995 to $33.64 in 2005. The GAO also found a sharp fee increase from data collected by Consumer Action, which showed a 119 percent increase from $12.53 in 1995 to $27.46 in 2005.[85] Even more striking, the GAO found that late fees paid by borrowers with typical balances were an average of $37 in 2005.[86] This is important to note as credit card issuers are increasingly assessing "tiered" fees based on the borrower's balance.

---

[79] "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, p. 18.
[80] *Ibid*, p. 23.
[81] *Ibid*, p. 1.
[82] CFA calculation based on 691 million credit cards, *Ibid*, p. 9.
[83] "The Ugly Issuer," *Credit Card Management*, September 2004.
[84] Bergman, Lowell and David Rummel, "Secret History of the Credit Card," *Frontline*, November 2004.
[85] "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, p. 18.
[86] *Ibid*, p. 20.

Credit card issuers used to reject transactions that exceeded a cardholder's credit limit, but it has become common for issuers to accept the transaction and then apply an over-limit fee on cardholders who exceed their credit limits.[87] These fees are often applied by issuers in addition to a higher "penalty" interest rate charge for exceeding the credit limit or carrying a high balance.[88] These monthly fees are charged every month a consumer carries a credit balance higher than their credit limit. According to the GAO report, data collected by Consumer Action shows a 114 percent increase in over-limit fees between 1995 and 2005.[89] Critics of this practice argue that issuers should not assess a penalty fee when they can simply enforce the credit limit if they wish to prevent consumers from exceeding it.

<u>Penalty Interest Rates Are Imposed On Top Of Penalty Fees: The Double Ding</u>

Payment of a late fee no longer serves as a form of liquidated damages. The vast majority of credit card issuers also impose a double ding: they increase interest rates for credit card account holders who pay their bills late, even by a few hours. In 2005, Consumer Action found that 78.7 percent of issuers charged penalty rates for late payments on their cards.[90] For example, representatives for one large issuer told the GAO that they <u>automatically</u> increase a customer's interest rate if this person pays late or exceeds the credit limit. The GAO found that all but one of the 28 cards from the six largest issuers they reviewed charged default rates in 2005. By 2008, 94% of new credit card solicitations included a penalty rate.[91] The average default rate in 2008 is 28.6 percent, up from 23.7 percent in 2003.[92] Even more striking, the spread between the penalty rate and the standard purchase rate more than doubled between 2000 (8.1%) and 2008 (16.9%).[93]

Some consumers with low-rate cards could have their interest rates double overnight for being late on one payment to their credit card.[94] Some issuers also say that they will charge default interest rates for exceeding the credit limit on the card or for returned payments, or that they will increase interest rates for cash advances and balance transfers for violations of card terms.[95]

There is increasing evidence that those who can least afford these higher interest rates – financially vulnerable families – are most likely to be paying them. A study by the research organization Demos found that cardholders that carry debt who earn less than $50,000 a year are more than twice

---

87 "The Ugly Issuer," *Credit Card Management*, September 2004.
88 Bergman, Lowell and David Rummel, "Secret History of the Credit Card," *Frontline*, November 2004.
89 "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, p. 20.
90 Consumer Action, 2005 Credit Card Survey, "Card Companies Use Common 'Risk Factors' to Impose Unfair Rate Hikes, Finds CA," *Consumer Action News*, Summer 2005.
91 Frank, Joshua M., *Priceless or Just Expensive? The Use of Penalty Rates in the Credit Card Industry*, p. 10, Center for Responsible Lending (December 16, 2008), hereafter Frank, *Priceless or Just Expensive*., available at http://www.responsiblelending.org/pdfs/priceless-or-just-expensive.pdf.
92 Id at 9. (The 2006 GAO report did find that some issuers do not assess default rates unless there are multiple violations of card terms. "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, pgs. 24, 25.)
93 Frank, *Priceless or Just Expensive*, at 9-10.
94 Bergman, Lowell and David Rummel, "Secret History of the Credit Card," *Frontline*, November 2004.
95 "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, p. 25.

as likely to pay interest rates above 20 percent as the highest income Americans who carry debt. African-American and Latino credit card holders with balances are more likely than whites to pay interest rates higher than 20 percent.[96]

One recent study estimated that the cost of the penalty rate shock cost a revolver carrying the average $10,678 balance $1800 a year.[97] At a time when we are looking for ways to put money back in the hands of families, reducing this $150 a month surtax could have a real stimulative effect.

Retroactive Application of Penalty Rates

All issuers also apply penalty interest rates retroactively to prior purchases. This has the effect of increasing the price on purchases already made but not paid off.[98] Some cards even apply penalty rates to debts that were already paid at a lower rate.[99] There is simply no legal or economic justification for assessing a penalty interest rate to an existing balance. There is no other industry in the country that is allowed to increase the price of a product once it is purchased. Issuers have already assessed a consumer's risk of not repaying the loan and presumably offered an interest rate based on that risk. Issuers should be required to allow a consumer to pay off his or her existing balance at that interest rate.

Even for consumers who clearly are becoming higher risk, such as those who are a full thirty days late in paying a credit card bill, it is harmful to cardholders and, ultimately, lenders to impose a retroactive rate increase on the existing balance. These families are struggling and need help getting out of debt; they should not be shoved deeper underground. Retroactive penalty interest rate hikes for these cardholders only increases the likelihood that they will completely default, which is in no one's interest. The primary effect of a punitive retroactive rate increase appears to be to escalate the proportion of the consumer's debt owed to the card issuer and to put the card issuer at an advantage over the consumer's other creditors. This practice is unfair to creditors who do not escalate the debt owed by families having difficulty making ends meet.

Universal Default

Universal default clauses in credit card contracts allow credit card companies to raise interest rates on debtors who have problems with other creditors or whose credit scores decline. The increases are triggered not just by a late mortgage or credit card payment to other lenders but also to payment disputes with other types of creditors, like utilities or book clubs.[100] A review of credit card disclosures issued in October 2006 by Consumer Action found five major issuers that said they reserved the right to assess universal default interest rates. Since that time, Citigroup and JP Morgan Chase have said that they will not use the practice, although Citigroup changed this policy

---

[96] Wheary, Jennifer, and Tamara Draut, "Who Pays? The Winners and Losers of Credit Card Deregulation," Demos, August 1, 2007.
[97] Frank, *Priceless or Just Expensive*, at 1.
[98] Draut, Tamara, Director of the Economic Opportunity Program at Demos, Testimony Before the House Banking Committee Subcommittee on Financial Institutions and Consumer Credit, September 15, 2004, at 16-17.
[99] McGeehan, Patrick, "The Plastic Trap," *New York Times*, November 21, 2004. Discover disclosed to its customers that it had changed the terms of its interest rates from a low of zero to 19.99% for a single late payment, but it applied that rate increase for late payments from 11 months prior to the disclosure of the changing interest rate terms.
[100] Burt, Bill, "Pay One Bill Late, Get Punished by Many," *Bankrate.com*, January 20, 2004.

in the fall of 2008.[101] On the other hand, representatives for Bank of America and Discover testified before the Senate late last year that they still use consumer credit scores, at least in part, to trigger higher default interest rates.[102]

It is fundamentally unfair to impose a penalty interest rate on a consumer who has not made a late payment or defaulted on an obligation, especially when this rate increase is applied retroactively. Another concern with using credit reports to trigger a penalty rate is the problems with inaccuracies in credit scoring and credit reporting that CFA and other organizations have documented.[103] Moreover, issuers who impose sharp interest rate increases on consumers who are meeting their obligations often fail to provide any rationale – much less a legitimate one -- for the increase. In January, Bank of America began increasing interest rates on some cardholders to as high as 28 percent but did not inform consumers the reason for the increase in the notification they mailed.[104]

Although credit card issuers contend that interest rate penalties that increase because of universal default are related to the credit risk of the borrower, the application by some issuers of these punitive rate hikes seems to belie that contention. One late payment can result in significant increases in interest rates in some cases, even though there is little evidence that a single late payment to one creditor increases the likelihood of default to all creditors. Moreover, increased fee and interest rate payments may have a similar or greater impact on the borrower's ability to repay than modest problems with another creditor.

Indiscriminate, Undisclosed Changes in Rates and Fees

Many credit card companies reserve the right to change the terms of their credit card contract at any time and for any, *or no*, reason. This allows credit card companies to arbitrarily raise interest rates even for cardholders in good standing and with perfect credit histories. Media reports of recent rate hikes by Bank of America demonstrate the unfairness of any-time/any-reason changes: some consumers saw their interest rates triple without explanation.[105] The result of these unfair clauses is that consumers can't depend on the interest rate promised to them.

In the last few months, JP Morgan Chase has begun charging approximately 400,000 cardholders a $10 a month fee. It is also increasing the minimum payment amount for these consumers from 2 to 5 percent, a substantial amount. Many of these cardholders appear to have been promised a fixed interest rate for the life of the balance.[106]

---

[101] Dash, Eric, "Despite Pledge, Citigroup to Raise Credit Card Rates, Blaming 'Difficult' Environment," *New York Times*, November 15, 2008.
[102] Credit Card Practices: Unfair Interest Rate Increases, U.S. Senate Permanent Subcommittee on Investigation, December 4, 2007.
[103] Consumer Federation of America and National Credit Reporting Association, "Credit Score Accuracy and Implications for Consumers," December 17, 2002. CFA and NCRA reviewed over 500,000 credit files and found that 29 percent of consumers have credit scores that differ by at least 50 points between the credit bureaus.
[104] "A Credit Card You Want to Toss," *Business Week,* February 7, 2008.
[105] Ibid.
[106] Chu, Kathy, "Chase Adds Fee for Low-Rate Credit Cards," *USA Today*, February 9, 2009.

Pricing Tricks: Double Cycle Billing and Manipulation of Payment Allocation

The GAO found that two of six major creditors are using a practice called double-cycle billing, which results in illegitimate interest charges on balances that have already been paid on time.[107] Since then, one of these issuers, JP Morgan Chase, has announced that it will no longer use double-cycle billing. With this practice, issuers consider two billing cycles in assessing interest. A consumer who begins with no balance and pays off most but not all of the purchases he or she makes in the first month would still be charged interest for the entire amount of the balance in the second month. A fair billing process would only result in an interest charge on the amount of the unpaid balance.

The GAO also determined that for 23 of the 28 large issuer cards they reviewed, cardholder payments were first allocated to the balance assessed at a lower rate of interest.[108] The actual proportion of large issuers who in effect use this policy is likely closer to 100 percent since the remaining five issuers applied payments "subject to their discretion". This practice is problematic for the many cardholders who now carry balances at different rates of interest, such as introductory "teaser" rates, cash advance rates, and balance transfer rates. The lower interest rate balances must first be paid off before the issuer will allocate payments to higher rate balances. Allocating payments to lower interest rate balances first unfairly extends the length of time it takes consumers to pay down their balances while increasing the finance charges that issuers earn. Furthermore, a recent study has shown this payment allocation policy and its impact to be very poorly understood by consumers.[109] The study also showed this issuer policy causes pricing to be less related to risk, the opposite of what issuers claim they wish to achieve.

Increases in Credit Card Fees and Interest Rates Significantly Affect Consumer Debt

Penalty fees and interest made up more than three-quarters of credit card issuers revenues throughout 2002 and 2003. Credit card issuers earned $65.4 billion in interest and $7.7 billion in penalty fees in 2003 or 75.7 percent of the total $96.5 billion in revenue.[110] In 2002, penalty fees and interest made up 76.8 percent of the industry's $97.1 billion in revenues. For the approximately 88 million credit cardholding households, penalty fees and interest on their credit card debt cost an average of $830 in 2003.[111]

Unsavory Credit Limit Practices

In its 2008 survey of credit card terms and conditions, Consumer Action identified some unsavory credit limit practices used by major credit card issuers. While reducing credit availability can be a responsible way for credit card issuers to manage growing financial risk during difficult economic times, these aggressive credit line policies can harm consumers.

---

[107] "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, p. 27.
[108] *Ibid*.
[109] Frank, Joshua M., *What's Draining Your Wallet? The Real Cost of Credit Card Cash Advances*, Center for Responsible Lending (December 16, 2008), available at http://www.responsiblelending.org/pdfs/whats-draining-your-wallet.pdf.
[110] Daly, James J., "Smooth Sailing," *Credit Card Management*, May 2004 at 31.
[111] Consumer Federation of America calculation from Daly, James J. 2004 and Census Bureau figures.

Each in its own way puts consumers at greater risk of being charged higher interest rates, falling deeper in debt, and causing a ripple effect among issuers. Consumers reported some credit limit practices to Consumer Action that are patently unfair.

- Following you down. As consumers pay off large balances, the credit limit is reduced so that the balance is always close to the credit limit.
- Sorry, you're over limit. Credit limits are reduced to levels lower than the current balance, triggering over limit fees and requiring a large "balloon" payment of the over-due amount. This practice also puts the consumer at risk of being hit with a penalty interest rate.
- Where's my credit limit? Cards are declined at the point of purchase, and only then do cardholders find out that their limits have been reduced with no warning.
- Ganging up on consumers. One credit card issuer lowers your credit limit, which lowers your credit score, which causes another of your cards to lower your credit limit.

The Combined Effect of Abusive Practices during the Recession

Although credit card issuers have curbed aggressive marketing and cut back on credit extension in the last year, they appear to be accelerating the use of many of the irresponsible and harmful practices detailed above to cut or mitigate their losses. For example, card issuers have used their ability to unilaterally change the terms of credit card contracts by raising interest rates even as the Federal Reserve has sharply reduced the federal funds rate.[112] They have also added new fees,[113] increased the amount of fees,[114] and, as detailed above, used harmful rather than responsible methods to lower credit lines. Citigroup back-peddled last fall on its promises not to increase interest rates "at any time for any reason."[115] As mentioned above, Chase has suddenly started charging hundreds of thousands of cardholders fees of $120 a year, while sharply increasing the monthly amount that these cardholders owe each month. Bank of America and Capital One have used vague clauses in cardholder agreements to raise interest rates on cardholders because of "market conditions."[116] Issuers have every right to try and limit their losses during the current economic crisis if they act responsibly, but the use of these harmful, unjustified and sometimes arbitrary practices is contributing to the economic insecurity of millions of families who thought they were complying with their obligations.

---

[112] Trejos, Nancy, "Less Power to Purchase, Consumers' Credit Card Limits Slashed as Companies Try to Reduce Risk," *Washington Post*, November 16, 2008.
[113] Lieber, Ron, "Credit Card Companies Go to War Against Losses," *New York Times*, January 31, 2008.
[114] Trejos, Nancy, "Less Power to Purchase, Consumers' Credit Card Limits Slashed as Companies Try to Reduce Risk," *Washington Post*, November 16, 2008.
[115] Dash, Eric, "Despite Pledge, Citigroup to Raise Credit Card Rates, Blaming 'Difficult' Environment," *New York Times*, November 15, 2008.
[116] "Card Rates Rise 'Out of the Blue,'" *The Oregonian*, January 25, 2008. Kimes, Mina, "Card Companies Jacking Up Rates," *Cable News Network*, http://money.cnn.com/2008/09/26/news/economy/creditcards_kimes.fortune/.

When "Risk-Based" Pricing is Predatory

Credit card issuers often claim that their interest rate and fee policies are justifiable because they are necessary to compensate for the increased financial risk of lending to borrowers with blemished or limited credit histories. It is true that borrowers who pay their balance every month are receiving a valuable service at no cost in many cases. It is quite possible, in fact, that riskier borrowers who revolve their debt and pay higher interest rates and fees are subsidizing in-part the cost of services that these non-revolvers receive. It is important to note, though, that issuers still receive substantial fee income from merchant "interchange" fees and, in some cases, from annual fees.

The key question is whether interest rates and fees charged to riskier consumers are fair and can be legitimately related to the actual financial risk incurred by creditors. There is increasing evidence that the answer to this question is "no."[117] It is becoming more apparent that many of the most abusive fees and interest rates are assessed simply because it is what the market will bear.

The amount of fees and penalty interest rates do not appear to be proportional to the risk or cost incurred by issuers. For many years, issuers have justified "sticky" interest rates that rise faster than they decline by stating that these higher interest rates were necessary to compensate for increased risk. As issuers have increased the number and amount of fees and penalty interest rates they charge, it seems that higher baseline interest rates alone are not sufficient anymore to compensate for risk. There is very little evidence that relatively modest problems, like one or two late payments of a short duration – significantly increase a consumer's chances of default. It would appear to be impossible to justify charging a consumer with a reasonably good credit history with a late payment fee of $35 and a default interest rate of 29 percent on prior purchases, in addition to the finance charge the consumer would already pay on a fairly high interest rate, such as 17 percent. One sign that default rates may not be truly reflective of costs or risk incurred by issuers is that the "fixed amount" that issuers add to the index rate in setting default rates rises when the cost of funds declines. The GAO found that this fixed amount increased from about 19 percent in 2003 to 22 percent in 2005 on the 28 large issuer cards they evaluated.[118]

In response to these "tell-tale" signs of price gouging, it is time for issuers to provide more information to lawmakers and to the public about their real costs to demonstrate that their pricing practices are truly fair.

F. FEDERAL RULE ON UNFAIR AND DECEPTIVE CREDIT CARD PRACTICES

On December 18, 2008, the Federal Reserve Board, the Office of Thrift Supervision and the National Credit Union Administration issued a final rule to curb unfair and deceptive practices by credit card issuers. The rules do not take effect until July 1, 2010.[119]

[117] Testimony of Adam J. Levitin, Associate Professor of Law, Georgetown University Law Center, before the Subcommittee on Financial Institutions and Consumer Credit of the Financial Services Committee of the United States House of Representatives, March 13, 2008.
[118] "Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers," U.S. Government Accountability Office, September 2006, p. 24.
[119] Federal Reserve System, 12 CFR Part 227 [Regulation AA; Docket No. R-1314]; Department of the Treasury, Office of Thrift Supervision, 12 CFR Part 535 [Docket ID. OTS-2008-0027] RIN 1550-AC17; National Credit Union

The new rules prohibits or restricts a number of abusive practices, including:

- **Interest rate increases on existing balances, unless the cardholder is more than 30 days delinquent.** The rule does not prohibit prospective "universal default" rate increases because of a supposed problem that the cardholder has with another creditor. It does eliminate the practice as applied retroactively, which has provided a major financial incentive for issuers to use it, though consumers struggling with their debt, who have missed a payment, could still be hit with large retroactive rate increases. The rule prohibits issuers from increasing interest rates on existing balances because a cardholder has made a minor mistake, such as paying late by a few days.

- **Payment allocation methods that cause debts to escalate**. The rule takes steps to require credit card issuers 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 will 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. Though the rule improves current payment allocation practices significantly, consumers would still be unable to completely pay off costly high rate balances by making extra payments unless the consumer pays off the lower rate balances at the same time.

- **Interest charges on debts that have already been paid**. The rule forbids "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 rule forbids 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 will be allowed to pay these fees off over a six-month period.

The rule is an important first step in stopping issuers from using some unfair and deceptive practices to increase the amount of debt consumers owe. However, it is not helpful to consumers struggling to pay off hefty debts in the middle of a recession to allow issuers to continue to use for another year and a half practices that federal regulators have deemed to be abusive. The Credit Cardholders' Bill of Rights Act under consideration the Financial Services Committee achieves both of these goals. (See below for discussion of this bill and how it compares to the regulators' rule.)

Administration, 12 CFR Part 706, RIN 3133-AD47; Unfair or Deceptive Acts or Practices. http://www.federalreserve.gov/newsevents/press/bcreg/20081218a.htm

G. ENSURING THAT CREDIT CARD ISSUERS RECEIVING GOVERNMENT ASSISTANCE OFFER LOANS THAT ARE FAIR AND SUSTAINABLE

As part of the federal government's efforts to rescue the financial sector, credit card banks are receiving taxpayer assistance in several forms, including through the direct infusion of funds and the Troubled Assets Relief Program (TARP). On February 10th, Treasury Secretary Geithner announced that he would expand an additional program designed to make consumer credit more widely available. The Term Asset Backed Securities Loan Facility (TALF) would use the Federal Reserve Board's credit facility power, be operated by the Federal Reserve Bank of New York, and include a special purpose vehicle capitalized from TARP funds. Initially, the program was to use $20 billion to support a program for up to $200 billion in non-recourse loans to buyers of securities backed by non-mortgage debt, including consumer credit card debt. In other words, buyers of credit card securitizations would be able to borrow funds from the Federal Reserve Bank of New York to purchase these securitizations, with repayment from revenues from the securitized credit card debts. Secretary Geithner said he wants to expand the program to support between $500 billion and $1 trillion in lending.

A diverse coalition of more than twenty organizations led by Consumers Union has called on Secretary Geithner to require that any securitized debt whose purchase is financed through this program meet standards for fairness and truthfulness, including those standards were finalized in December 2008 by the Federal Reserve Board.[120] The groups sought this change to ensure that any consumer credit card debt facilitated through this taxpayer-backed program will promote, rather than damage, household economic stability.

Specifically, the organizations called on Secretary Geithner to impose two minimal eligibility conditions on all financing by the TALF for credit card securitization pools:

1. Immediate compliance with details of the rule against unfair or deceptive acts or practices for all consumer credit card debt in the pool; and

2. A specific program for cardholders to earn a reduction in penalty interest rates back to a lower standard rate after no more than six months of on-time payments for all consumer credit card debt in the pool.

Any government backed program to make capital available for credit card debt must be limited to that credit card debt which is not associated with practices that federal regulators have determined to be unfair or deceptive. Federal backing of credit card securitizations must also be limited to credit card debt with a clear "road map" to non-penalty rates for households who pay on time while under a penalty rate.

A stated purpose for the Troubled Assets Relief Program (TARP) is to restore stability to the financial system. However, the first installment of TARP money did not even begin to promote financial stability for borrowers, homeowners, and communities in the face of the tide of foreclosures, onerous credit card practices, and the crying need for affordable, sustainable,

[120] https://mail.consumerfed.org/exchweb/bin/redir.asp?URL=http://www.consumersunion.org/pdf/TALF.pdf.

systematic loan modifications. The new TALF program for non-mortgage debt should limit its offer of liquidity to avoid the type of credit card debt that detracts from sustainable lending and household financial stability.

Providing more capital for credit card lending will not meet the national need for enhanced financial stability for households if the credit card debt that is facilitated under the TALF can continue until July 1, 2010 to contain the harmful terms and practices that the Federal Reserve Board and two other federal regulators have identified as unfair or deceptive. The challenges for the U.S. economy are great. Consumers cannot be the engine of economic recovery if they are burdened with high interest rate credit card debt that federal regulators have determined is not justified. Any further taxpayer assistance to credit card issuers must include conditions that will ensure that the credit provided will promote, or at least not be detrimental to, family economic stability.

H. H.R. 627—Credit Cardholders Bill of Rights

The "Credit Cardholders' Bill of Rights Act" (Maloney) helps restore fairness to the credit card marketplace. (Note: The bill was considered yesterday in a House Financial Services subcommittee so it may been have changed,)

The bill would require credit card issuers to take a number of steps to treat consumers more fairly, including:

1. **Ending Bait and Switch Contract Clauses.** H.R. 627 invokes the basic tenet of fair dealing by prohibiting credit card companies from changing contract rules in the middle of the game through "any time, any reason" interest rate and fee hikes. Instead, they must disclose, up front, the specific, material reasons for which they will unilaterally change contract terms.

2. **Limiting Retroactive Application of Rate Hikes for Consumers in Good Standing.** H.R. 627 prohibits card issuers from applying "universal default" interest rate hikes retroactively to balances borrowed at a lower rate. As cited above, some issuers still use credit information not related to the account a consumer has with that company, such as a drop in a consumer's credit score, to raise interest rates. While consumers with a perfect payment history with their credit card company are understandably outraged when their interest rate rises for these reasons, the devastating consequences of retroactive application of these increases is equally egregious. Minimum monthly payments rise, sometimes dramatically. The time to pay-off the balance increases, sometimes by many years, while the total cost of the debt skyrockets. H.R. 627 limits these destabilizing impacts by prohibiting the retroactive application of rate hikes not related to the cardholder's credit card account.

3. **Preventing Credit Card Companies from Gaming Consumer Payments.** H.R. 627 reduces the ability of card companies to play costly games with consumer payments by requiring them to apply payments proportionately to card balances with different interest rates. As stated above, when consumers accept card offers for short-term teaser rates for balance transfers and cash advances and higher rates for other balances, credit card companies apply payments *first* to the lower-rate balance, preventing consumers from

paying off higher interest balances and imposing unwarranted and costly finance charges. Issuers refuse to apply *any* portion of a consumer's payment to the higher interest rate balance, preventing consumers from paying down *any* portion of the high-cost balance until the lower interest rate balance is repaid. As a result, balances build up at the much costlier rate and finance charges accrue.

4. **Prohibiting Unfair and Hidden Interest Rate Charges on Balances Repaid During the Grace Period.** H.R. 627 prohibits credit card companies from using "double-cycle billing" to charge interest on balances repaid during the grace period. As mentioned above, this practice allows credit card issuers to sap unwarranted finance charges from the wallets of consumers who usually do not carry balances. Although some credit card issuers have disavowed this practice, some still engage in it. This legislation makes clear that a grace period is a grace period.

5. **Ending Unfair Late Fees for On-Time Payments**. H.R. 627 ends the classic late-fee gotcha. Consumers who mail their payments well in advance are often socked with a late fee of up to $40 because of card companies' own processing delays or arbitrary deadlines. The abuse has been exacerbated as credit card companies have shortened the time period in which consumers can make an on-time payment. Other consumers make electronic payments on the due-date, only to be hit with a late fee because they posted their payment five minutes after the issuer's arbitrary deadline on that day. The legislation provides that consumers demonstrating that they have paid their bill at least seven days before the due date are presumed to have paid on time and cannot be charged a late fee. It also sets a single uniform time of no earlier than 5 p.m. local time by which payments must be received on the due date to prevent companies from setting earlier and arbitrary deadlines that result in late fees. Issuers must also mail credit card bills 25 days before the bill is due, instead of the current rule requiring only 14 days, to help ensure that consumers will have enough time to pay.

These provisions largely track those required in the credit card rule finalized by federal regulators. There are a few significant differences, however. Most important is that H.R. 627 will take effect three months after enactment, while the regulators' rule does not take effect until July of 2010. Protections that are in H.R. 627 that are not included in the regulators' rule include:

- Consumers will be able to choose not to be allowed to exceed their credit limit
- Credit card companies will not be able to extend credit to borrowers younger than 18.
- Consumers who receive extraordinarily high-cost "subprime" cards would be better protected under H.R. 627. The Board rule permits fees to consume 50 percent of the consumer's credit line, whereas under H.R. 627 fees cannot be charged to more than 25 percent of the credit line.

Protections that are included in the regulators' rule that are not in H.R. 627 include:

- Prohibiting the practice of deferring interest rate payments. Deferred interest usually involves an advertised promise such as "no interest for one year," but the fine print calls for interest to be charged retroactively if the consumer does not fulfill a condition of the deferral agreement, such as paying in full before the end of the deferral period.

- Banning the hair-trigger loss of promotional interest rates. Issuers would not be able to use any reason they wanted to raise a promotional rate during the promotional period, but could only do so of a cardholder was thirty days or more late in paying a bill.
- Prohibiting "universal default" rate increases on future purchases for the year a card is issued. The rule primarily restricts interest rate increases on <u>existing</u> balances, but in this case the rule would prohibit interest rate increases <u>prospectively</u> for the first year a card is issued, because of a supposed problem the cardholder has with another creditor or a drop in the cardholder's credit score.

We recommend that the Congress conform H.R. 627 to the additional requirements in the rule. We also recommend that the Congress include in H.R. 627 several additional provisions that would enhance consumer protection not yet addressed by the bill, including: a ban on all universal default rate hikes, including prospective rate hikes before the card expires; a prohibition on retroactive application of *any* rate hike to prior balances; a requirement that the size of penalties charged by issuers be directly related to actual costs incurred; and a requirement that credit card issuers ensure that young consumers have the ability to repay the loans they are offered.

We also recommend that the Congress eliminate a provision in H.R. 627 allowing issuers to charge over-limit fees for three consecutive months, even if the cardholder only exceeds the credit limit with a single transaction. Instead, H.R. 627 should prohibit issuers from charging over-limit fees if they choose to allow a cardholder to exceed the credit limit.

Taken together, the reforms offered in H.R. 627 would be an important first step in making the credit card marketplace fairer and more transparent. By prohibiting issuers from using questionable methods to sharply increase some "back end" interest charges, this bill would start to shift pricing in the industry to the "front end," especially the initial interest rate. It would encourage issuers to compete to attract consumers based on those initial charges, and to use responsible risk-management techniques to manage their financial exposure if the risk profile of the borrower declines over time. The bill would not stop issuers from using responsible risk-based pricing methods to establish initial interest rates or to change them prospectively if the borrower's credit worthiness declines.

Conclusion

We appreciate the opportunity to provide our views to the Subcommittee today. We hope our testimony has illustrated that at the intersection of many consumer problems in today's world you can find both credit card company practices and the bankruptcy changes of 2005 demanded by those firms. Both need reform. We look forward to working with you on changes to laws that will better protect American families from unnecessary economic stress brought on by harsh credit card practices and unwarranted restricted access to a bankruptcy fresh start.