Senator Dianne Feinstein
Statement on Credit Card Minimum Payment Notification
Before the Banking Committee
May 17, 2005

Thank you, Chairman Shelby and Ranking Member Sarbanes for scheduling this hearing. I believe that it is important that we explore the issue of consumer credit card debt.

Today, 144 million Americans utilize credit cards and charge more debt on those cards than ever before. (*Frontline*, "The Secret History of the Credit Card", November 2004.) In 1990, Americans charged $338 billion on credit cards. By 2003, that number had risen to $1.5 trillion. (Carddata.com.)

Many Americans now own multiple credit cards. In 2003, 841 million bank-issued credit cards were in circulation in the U.S. (CardWeb.com.) That number becomes nearly 1.4 billion credit cards, when cards issued by stores and oil companies are factored in. (HSN Consultants.) That's an average of 5 credit cards per person.

The proliferation of credit cards can be traced, in part, to a dramatic increase in credit card solicitation. In 1993, credit card companies sent 1.52 billion solicitations to American homes; in 2001, they sent over 5 billion. (*Mail Monitor*, a service of BAIGlobal, Inc. See also Consumer Federation of America, Press Release, "Credit Card Issuers Aggressively Expand Marketing and Lines Of Credit On Eve Of New Bankruptcy Restrictions, February 27, 2001.)

As one would expect, the increase in credit cards has also yielded an increase in credit card debt. Individuals get six, seven, or eight different credit cards, pay only the minimum payment required, and many end up drowning in debt. That happens in case after case.

Since 1990, the debt that Americans carry on credit cards has more than tripled, going from about $238 billion in 1990 to $755 billion in 2004. (Testimony of Tamara Draut, Director of the Economic Opportunity Program, Demos, Before The Subcommittee on Financial Institutions and Consumer Credit Regarding Financial Services Issues: A Consumer's Perspective, September 15, 2004.)

As a result, the average American household now has about $7,300 of credit card debt. (Federal Reserve, Release G. 19, "Consumer Credit.")

As has been discussed much in this Congress, the number of personal bankruptcies has doubled since 1990. (Testimony of Tamara Draut, Director of the Economic Opportunity Program, Demos, Before The Subcommittee on Financial Institutions and Consumer Credit Regarding Financial Services Issues: A Consumer's Perspective, September 15, 2004) Many of these personal bankruptcies are people who utilize credit cards. These cards are enormously attractive. However, these individual credit card holders receive no information on the impact of compounding interest. They pay just the minimum payment. They pay it for 1 year, 2 years -- they make additional purchases, they get another card, and another, and another.

Unfortunately, these individuals making the minimum payment are witnessing the ugly side of the "Miracle of Compound Interest." After two or three years, many find that the interest on the debt is such that they can never repay these cards, and do not know what to do about it.

Statistics vary about the number of individuals who make only the minimum payments. One study determined that 35 million pay only the minimum on their credit cards. (Frontline, "The Secret History of the Credit Card", November 2004.) In a recent poll, 40% of respondents said that they pay the minimum or slightly more. (Cambridge Consumer

Credit Index Poll, 3/05.) What is certain is that many Americans pay only the minimum, and that paying only the minimum has harsh financial consequences.

I suspect that most people would be surprised to know how much interest can pile up when paying the minimum. Take the average household, with $7,300 of credit card debt, and the average credit card interest rate, which in April, before the most recent Federal Reserve Board increase of the prime rate, was 16.75%. (Carddata.com.) If only the 2% minimum payment is made, it will take them 44 years and $23,373.90 to pay off the card. (All calculations from CardTrak at Cardweb.com.) And that is if the family doesn't spend another cent on their credit cards – an unlikely assumption. In other words, the family will need to pay over $16,000 in interest to repay just $7,300 of principal.

For individuals or families with more than average debt, the pitfalls are even greater. $20,000 of credit card debt at the average 16.75% interest rate will take an 58 years and $65,415.28 to pay off if only the minimum payments are made.

And 16.25% is only the average interest rate. The prime rate, despite recent increases, remains relatively low – at 6%. However, interest rates around 20% are not uncommon. In fact, among the 10 banks that are the largest issuers of credit cards, the top interest rates on credit cards are between 23 and 31 percent – and that does not factor in various penalties and fees. (Cardweb.com.) When penalty interest rates are factored in, the highest rates are 41%. (Carddata.com.) In 1990, the highest interest rate – even with penalties, was 22%, a little more than half of what they are today. (Carddata.com.)

Even if we assume only a 20% interest rate, a family that has the average debt of $7,300 at a 20% interest rate and makes the minimum payments will need an incredible 76 years and $41,884 to pay off that initial $7,300 of debt. That's $34,584 in interest payments – more than 4 times the original debt. And these examples are far from extreme.

Moreover, these are not merely statistics, but are reflective of very real situations for many people. On March 6, the Washington Post ran a headline story on its front page, entitled "Credit Card Penalties, Fees Bury Debtors." I would recommend this article to my colleagues, because it illustrates part of the problem – that credit card companies, aggressively marketing their products, end up charging outrageous interest and fees to their customers. I ask that the article be included in the record. The article highlighted the following stories:

- Ohio resident, Ruth Owens tried for six years to pay off a $1,900 balance on her Discover card, sending the credit company a total of $3,492 in monthly payments from 1997 to 2003. Yet her balance grew to $5,564.28,
- Virginia resident Josephine McCarthy's Providian Visa bill increased to $5,357 in two years, even though McCarthy has used the card for only $218.16 in purchases and has made monthly payments totaling $3,058.
- Special-education teacher Fatemeh Hosseini, from my state of California, worked a second job to keep up with the $2,000 in monthly payments she collectively sent to five banks to try to pay $25,000 in credit card debt.   Even though she had not used the cards to buy anything more, her debt had nearly doubled to $49,574 by the time she filed for bankruptcy last June.

Unfortunately, these stories are not unique.

Part of the problem goes back to changes made in the credit card industry. For a long time, most banks required their customers to pay 5 percent of their credit card balance every month. That was before Andrew Kahr, a credit card industry consultant, got involved. Mr. Kahr realized that if customers were able to pay less, they would borrow more, and he convinced his clients that they should reduce the minimum payment to just 2 percent. (*Frontline*, "The Secret History of the Credit Card", November 2004.)

The PBS program "Frontline", ran a program in November of last year titled "The Secret History of the Credit Card" that examined the rapid growth of the credit card industry and included an interview with Mr. Kahr.

Mr. Kahr's innovation has been a windfall for the credit card industry. If consumers are paying a lower percentage of their balance as the minimum payment, the credit card companies will make more money over time. In fact, many in the industry refer to individuals who pay their credit card bills in full as "deadbeats", because they are less profitable than individuals who carry large balances, who are known as “revolvers.” (*Frontline*, “The Secret History of the Credit Card”, November 2004.)

And Mr. Kahr’s own research showed that just making the minimum payment eased consumers' anxiety about carrying large amounts of credit card debt -- they believe they are still being financially prudent. (*Frontline*, “The Secret History of the Credit Card”, November 2004.)

The bill I am proposing speaks directly to those types of consumers. There will always be people who cannot afford to pay more than their minimum payments. But, there are also a large number of consumers who can afford to pay more but feel comfortable paying the minimum payment because they don’t realize the consequences of doing so.

Now I am certainly not trying to demonize credit cards or the credit card industry. Credit cards are an important part of everyday life. However, I do think that people should understand the dangers of paying only their monthly minimums. In this way individuals will be able to act responsibly.

Mr. Chairman, it’s not necessarily that people don’t understand the basics of interest. Most of us just don’t realize how fast it compounds or how important it is to do the math to find out what it means to pay a minimum requirement.

The bottom line is that for many consumers, the two percent minimum payment is a financial trap.

The Credit Card Minimum Payment Notification Act is designed to ensure that people are not caught in this trap through lack of information. The bill tracks the language of the amendment originally proposed to the Bankruptcy bill that was co-sponsored by Senator Kyl, Senator Brownback, and myself.

Let me tell you exactly what this bill would do. It would require credit card companies to add two items to each consumer's monthly credit card statement:

1) A notice warning credit card holders that making only the minimum payment each month will increase the interest they pay and the amount of time it takes to repay their debt; and

2) Examples of the amount of time and money required to repay a credit card debt if only minimum payments are made;

<u>OR</u>

If the consumer makes only minimum payments for six-consecutive months, the amount of time and money required to repay the individual's specific credit card debt, under the terms of their credit card agreement.

The bill would also require that a toll free number be included on statements that consumers can call to get an estimate of the time and money required to repay their balance, if only minimum payments are made.

And, if the consumer makes only minimum payments for six-consecutive months, they will receive a toll free number to an accredited credit counseling service.

The disclosure requirements in this bill would only apply if the consumer has a minimum payment that is less than 10% of the debt on the credit card, or if their balance is greater than $500. Otherwise, none of these disclosures would be required on their statement.

The language of this bill comes from a California law, the "California Credit Card Payment Warning Act," passed in 2001. Unfortunately, in 2002, this California law was struck down in U.S. District Court as being preempted by the 1968 Truth in Lending Act. The Truth in Lending Act was enacted in part because Congress found that, "The informed use of credit results from an awareness of the cost of thereof by consumers." Consequently, this bill would amend the Truth in Lending Act, and would also further its core purpose.

These disclosures allow consumers to know exactly what it means for them to carry a balance and only make minimum payments, so they can make informed decisions on credit card use and repayment.

The disclosure required by this bill is straightforward – how much it will cost to pay off the debt if only minimum payments are made, and how long it will take do it. As for expense, my staff tells me that on the website Cardweb.com, there is a free interest calculator that does these calculations in under a second. Moreover, I am told that banks make these calculations internally to determine credit risk. The expense would be minimal.

Percentage rates and balances are constantly changing and each month, the credit card companies are able to assess the minimum payment, late fees, over-the-limit fees and finance charges for millions of accounts.

If the credit card companies can put in their bills what the minimum monthly payment is, they can certainly figure out how to disclose to their customers how much it might cost them if they stick to that minimum payment.

The credit card industry is the most profitable sector of banking, and last year it made $30 billion in profits. (Carddata.com.) MBNA's profits alone last year were one-and-a-half times that of McDonald's. Citibank was more profitable than Microsoft and Wal-mart. (Frontline, "The Secret History of the Credit Card", November 2004.) I don't think they should have any trouble implementing the requirements of this bill.

I believe that this is extraordinarily important and that it will minimize bankruptcies. With companies charging very substantial interest rates, they have an obligation to let the credit card holder know what those minimum payments really mean. I have people close to me I have watched, with six or seven credit cards, and it is impossible for them, over the next 10 or 15 years, to pay off the debt if they continue making just minimum payments.

We now have a bankruptcy bill that has passed into law. I continue to believe that a bill requiring a limited but meaningful disclosure by credit cards companies is a necessary accompaniment. I think you will have people who are more cautious, which I believe is good for the bankruptcy courts in terms of reducing their caseloads, and also good for American consumers.

The credit card debt problem facing our nation is significant. I believe that this bill is an important step in providing individuals with the information needed to act responsibly, and it does so with a minimal burden on the industry.