Testimony of the

U.S. Public Interest Research Group

Edmund Mierzwinski
Consumer Program Director

Oversight Hearing On
Abusive Credit Card Industry Practices

Before the U.S. Senate Banking Committee

The Honorable Richard Shelby, Chairman

17 May 2005

Chairman Shelby, Senator Sarbanes, members of the committee:

Thank you for the opportunity to offer U.S. PIRG's views on abusive credit card industry practices. We commend you for having this timely hearing. I am Edmund Mierzwinski, Consumer Program Director of U.S. PIRG. As you know, U.S. PIRG serves as the national lobbying office for state Public Interest Research Groups. PIRGs are non-profit, non-partisan public interest advocacy organizations with offices around the country.

(1) INTRODUCTION AND SUMMARY:

The extremely concentrated credit card industry, in efforts to increase profitability above already substantial levels, continues to engage in a growing and wide number of unfair, anti-consumer practices. These practices are enabled by a pliant federal bank regulatory apparatus, which has generally ignored the growing problem while relying on an unfortunate series of court decisions to expand federal preemption and narrow the authority of state enforcers to better protect their own citizens.

The most common unfair credit card company practices include the following:

- Unfair and deceptive telephone and direct mail solicitation to existing credit card customers – ranging from misleading teaser rates to add-ons such as debt cancellation and debt suspension products, sometimes called "freeze protection," which are merely the old predatory credit life, health, disability insurance products wrapped in a new weak regulatory structure to avoid pesky state insurance regulators[1];
- increased use of unfair penalty interest rates ranging as high as 30% APR or more, including, under the widespread practice of "universal default," the practice of imposing such rates on consumers who allegedly miss even one payment to <u>any</u> other creditor, despite a perfect payment history to that credit card company;
- imposing those punitive penalty interest rates retroactively, that is, on prior or existing balances as well as on future purchases, further exacerbating the worsening levels of high-cost credit card debt;
- higher late payment fees, now generally $30-40, which are often levied in dubious circumstances, even when consumers mail payments 10-14 days in advance;
- aggressive and deceptive marketing to new customer segments, such as college students with neither a credit history nor an ability to repay, as well as marketing to persons with previous poor credit history;
- partnerships with telemarketers making deceptive pitches for over-priced freeze protection and credit life insurance, roadside assistance, book or travel clubs and other unnecessary card add-ons;
- the increased use of unfair, pre-dispute mandatory arbitration as a term in credit card contracts to prevent consumers from exercising their full rights in court; and the concomitant growing use of these arbitration clauses in unfair debt collection schemes;
- the failure of the industry to pass along the benefits of what, until recently, were several years of unprecedented Federal Reserve Board interest rate cuts intended to provide economic stimulus, through the use of unfair floors in variable credit card contracts. The Fed kept dropping rates, but the card companies did not, once these floors were reached.

There are two engines that drive this train of unfair practices. First, the companies include a contract clause that states: Any term can be changed at any time for any reason, including no reason. Second, the aforementioned use of one-sided pre-dispute binding mandatory arbitration clauses[2] prevents consumers from challenging these practices in court.

The practices described above can be illustrated with the following examples:

- Banks entice consumers to open or continue credit card accounts with promises of a fixed interest rate on unpaid balances on purchases. Thereafter, they unilaterally increase the so-called fixed rate, and may change it to a variable rate[3].
- Banks bait credit card consumers with teaser offers promising a low introductory interest rate on additional credit card debt and the consumer's pre-existing (regular) interest rate thereafter. But after individual consumers accept the offer and increase their debt, banks unilaterally and without notice raise the consumer's regular interest rates because now, the individual consumer's debt is allegedly "too high." Banks also reserve the right to take regular credit card payments and apply them to the lowest interest rate debt instead of the highest, in a circumstance where a consumer has transferred zero percent debt to a card with an existing balance.
- Banks ignore consumers' disputes to charges, which, according to banks themselves, need not be paid pending resolution. Instead, banks unilaterally use such non-payment to charge late fees and raise interest rates.
- Banks reduce credit limits of consumers on their credit card accounts unilaterally and without advance notice, and do so in such manner and to such an extent as to intimidate consumers into abandoning their legitimate objection to charges.
- Banks fail to adequately inform consumers in advance of a proposed increase in interest rate based on the individual consumer's purportedly high debt or other information in such consumer's credit report. Thereby, consumers have no opportunity to avoid the increased interest rate, and are saddled with significant additional interest payments without advance notice.
- Credit card companies use low, short-term "teaser rate" introductory APRs to mask higher regular APRs. The introductory APR is one of the primary tools used to market a card, and it usually appears in large print on the offer and envelope. In a recent PIRG study discussed below, of 100 card offers surveyed, 57 advertised a low average introductory APR of 4.13%. Within an average of 6.8 months, the regular APR shot up 264% to an average regular APR of 15.04%. The post-introductory APR, as well as the length of the introductory period, were not prominently disclosed.
- Important information is disclosed only in the fine print of the offer. For example, the fine print of most offers states that if an applicant does not qualify for the offered card, s/he will receive a lower-grade card, which usually has a higher APR and punitive fees. The fine print is easy to overlook, and as a result, a consumer may receive a card that s/he did not want.
- Free does not mean free. The "free" offers that are advertised with many cards are not usually as impressive as they appear. Most are "free-to-pay" schemes, where the failure to cancel within 30 days imposes hefty annual fees for tawdry products. Others include significant restrictions or hidden costs.
- Companies are failing to disclose the actual APRs of cards. Increasingly, credit card companies are quoting a range of APRs in offers rather than a specific APR, a practice called "tiered" or "risk-based" pricing. These ranges are frequently so wide as to be utterly useless

to consumers. Even recent directives of the Office of the Comptroller of the Currency (OCC) have begun to recognizes some of these practices as unfair.

- Fine print fees for cash advances, balance transfers, and quasi–cash transactions such as the purchase of lottery tickets significantly raise the cost of these transactions. But the terms governing these transactions are buried in the fine print, where consumers can easily miss them. Minimum fees, also stated only in the fine print, allow credit card companies to guarantee themselves high fee income regardless of the transaction amount.

Another way to look at these problems is to look at an example: In a recent court complaint against a credit card company, a consumer attorney pleaded the following facts:

> On June 17, 2002 the balance owed on the consumer's account was $702.00. On June 18, 2002, the bank added a $59 club membership fee that caused the consumer's account to exceed his credit limit by $11 (the balance owed was $761 and the credit limit was $750). From June 2002 until August 2004, even though the consumer made timely monthly payments each month, the bank added $435 in over-limit fees to this account and $495 in late charges on this account.

This consumer responded to some bank-initiated telemarketing pitch or bill insert to join some sort of a membership club, then the bank allowed him to go over his limit to complete the transaction for a purchase it itself had initiated, then that triggered an ongoing cascade of repeated late and over-the-limit fees that have caused the consumer to end up in a cycle of rising debt even though he no longer uses the card. This example, multiplied by millions of consumers, gives you an idea of how credit card debts have piled up in this country.

(2) REGULATORY ACTIONS AND COURT ACTIONS AGAINST CREDIT CARD COMPANIES

These views are not merely our own nor merely those of consumer attorneys. The very worst of the industry's excesses have resulted in increased regulatory, legislative and legal scrutiny. Even the Treasury's Office of the Comptroller of the Currency (OCC), no consumer protector, has begun to escalate its efforts against unfair credit card company practices. Although it has not yet taken any public actions against any well-known major institutions, it has gone after a number of unknown fringe institutions and one albeit large, but relatively upstart mono-line credit card bank, Providian. More recently, the OCC has issued a series of regulatory guidances admonishing banks against certain common unfair practices and even consolidated these actions onto one website to make their efforts appear more comprehensive[4]. Unfortunately, the OCC has not imposed public penalties or sanctions on any of the current "Top Ten" banks, even though most advocates believe the practices are endemic to the industry.

Meanwhile, State Attorneys General Enforce the Law

Of course, state Attorneys General, always the top consumer cops on the beat, have long been aggressively pursuing crime and other anti-consumer practices in the credit card suites. Some recent actions by state Attorneys General and federal regulators include the following.

- In January 2005, Minnesota Attorney General Mike Hatch filed an unfair practices suit against Capital One Bank and Capital One F.S.B. for using false, deceptive and misleading television advertisements, direct-mail solicitations, and customer service telephone scripts to market credit cards with allegedly "low" and "fixed" interest rates that, unlike its competitors' rates, supposedly will never increase. Capital One, of course, is one of the nation's largest credit card companies, with an aggressive advertising campaign urging consumers to put a Capital One card in their wallet and avoid the other companies, generally portrayed by Capital One as Vikings, Visigoths or other sorts of plundering barbarians. Other states, including West Virginia, have since announced parallel investigations of Capital One. West Virginia, this month, had to file suit to enforce its subpoenas against the bank.[5]

- In the last several years, numerous state Attorneys General, including Minnesota, Texas, West Virginia, New York and others have filed actions against the large sub-prime credit card company Cross Country Bank for its deceptive and predatory practices when marketing to consumers with impaired credit histories. The Attorney General of Minnesota's complaint alleges the bank uses racial, derogatory and abusive epithets in the bank's threatening phone contacts with customers[6]. The Attorney General of Pennsylvania had this to say in 2004: "Instead of helping consumers as promised, the defendants actually pushed cardholders further into debt when they used the credit cards. Those who failed to make the payments, were subjected to a barrage of abusive, harassing collection practices that included the use of profanity and multiple calls to consumers' homes or offices."[7]
- In December, 2002, 28 states and Puerto Rico settled a case with First USA (a unit of Bank One, which is now part of JP Morgan Chase after its acquisition of Bank One) "that will provide new protections against misleading telemarketing campaigns for more than 53 million credit card holders. First USA Bank N.A. - the largest issuer of Visa credit cards - and also known as Bank One Delaware NA, has agreed to implement broad reforms in its relationships with third-party vendors to ensure that non-deceptive marketing campaigns are used in soliciting the bank's credit card holders. Specifically, under the agreement, First USA must prohibit vendors from engaging in deceptive solicitations."[8]
- In February 2002, 27 states negotiated an agreement for Citibank, then the nation's largest credit card issuer, to stop deceptive practices in the marketing of similar tawdry add-on products. "The states raised concerns that the marketing practices of Citibank's business partners were deceptive and often resulted in consumers being charged for products and services - such as discount buying clubs, roadside assistance, credit card loss protection and dental plans - that they had no idea they agreed to purchase."[9]
- In 2001, the OCC imposed multi-million dollar penalties and a restitution order against Direct Merchants' Bank for its practice of "'downselling' consumers by prominently marketing to consumers one package of credit card terms, but then approving those consumers only for accounts with less favorable terms, and touting the approved account in a fashion designed to mislead the customer about the fact he or she had been 'downsold'[10]."
- In 2000, the tiny San Francisco District Attorney and the California Attorney General[11] began an investigation later joined by what many claim was an embarrassed and late to the party OCC, which resulted in imposition of a minimum of $300 million in civil penalties and a restitution order against Providian for deceptive marketing of mandatory credit life insurance, known as freeze protection, and other violations. The OCC, not generally known for hyperbole in defense of the consumer, said the following: "We found that Providian engaged in a variety of unfair and deceptive practices that enriched the bank while harming literally hundreds of thousands of its customers[12]."
- Since 1999, the Minnesota Attorney General and other states have settled multi-million dollar claims against U.S. Bank for its practice of allowing telemarketers access to its credit

card customer records for the purpose of deceptively marketing add-on products including credit life insurance, roadside assistance packages, and other gimmickry billed to consumers who did not even give their credit card numbers and had no knowledge that they had allegedly placed orders or would be billed for any product.

- Several private class action lawsuits have been settled recently against other large banks for abusive practices, such as charging consumers late fees, even when they pay on time.
- The federal courts have also acted in favor of consumers in several important cases. In 2003, the 3rd Circuit found that Fleet Bank had violated the Truth In Lending Act (TILA) when it promised Paula Rossman a no-annual-fee credit card and changed the terms immediately, less than a year after she'd obtained the card, even though Rossman had not violated any of the contract's terms by paying late, going over her limit, or anything else. The court described the essential problem this way:

> A statement, therefore, that a card has "no annual fee" made by a creditor that intends to impose such a fee shortly thereafter, is misleading. It is an accurate statement only in the narrowest of senses--and not in a sense appropriate to consumer protection disclosure statute such as the TILA. Fleet's proposed approach would permit the use of required disclosures--intended to protect consumers from hidden costs--to intentionally deceive customers as to the costs of credit.[13]

Of course, Rossman highlights one of the critical hypocrisies and significant flaws in the federal un-regulation of the credit card marketplace, where credit card contracts are take-it-or-leave contracts of adhesion imposed on consumers that supposedly allow the bank to make any changes at any time for any reason. As the court quotes Fleet's contract in Rossman:

> We have the right to change any of the terms of this Agreement at any time. You will be given notice of a change as required by applicable law. Any change in terms governs your Account as of the effective date, and will, as permitted by law and at our option, apply both to transactions made on or after such date and to any outstanding Account balance.[14]

- Numerous colleges and universities, as we illustrate below and as Doctor Manning will indicate in his testimony, have banned or strictly regulated the marketing of credit cards on campuses, to address widespread complaints about tawdry practices.

(3) POLICY RECOMMENDATIONS OF U.S. PIRG TO ADDRESS ABUSIVE CREDIT CARD PRACTICES:

Prohibit Deceptive and Unilaterally Unfair Practices, Including Retroactive Interest Rate Increases: Enact legislation such as the omnibus proposal by Senator Dodd, S 499, a member of this committee, to prohibit a number of unfair practices, starting with the notorious retroactive interest increase. When banks impose universal default, or otherwise increase interest rates, they do not merely increase rates on interest accruing on future purchases, but also on prior balances. This has the effect of saddling the consumer with massive debt.

Require Real Disclosure of Minimum Payment Warnings: Senator Akaka of this committee has proposed legislation, S. 393, (a similar provision is also included in S. 499) that would require every consumer's credit card billing statement to include a new disclosure. The Akaka

Minimum Payment Warning is one of the few disclosures that rises above the clutter and will make a difference, and that's the reason banks vehemently oppose this proposal. The minimum payment warning would tell consumers how many actual years it would take to pay off their specific credit card, at their current balance and interest rate, if they only made the minimum requested payment and never used the card again. Each consumer would receive a different, dynamic disclosure, which would change monthly. We were disappointed when the Senate rejected the similar Akaka amendment during floor consideration of the draconian bankruptcy bill, S. 256, successfully and aggressively sought by the credit card industry and enacted into law at lightning speed this Congress, despite no evidence of bankruptcy abuse. Instead, that new bankruptcy act includes yet another virtually worthless generic disclosure. That disclosure was approved and signed off on by the industry simply because it will not work to reduce the credit card debts that cripple many American consumers. In a speech to bankers last week, Acting OCC Comptroller Julie Williams said "in order for the free market to work, consumers need to have the means to make informed decisions."[15] We urge the OCC to back the Akaka bill. It will work.

Ban on Late Fee Penalties When Payments Postmarked Before Due Date and Require a Minimum 30 Days To Pay Bill: In response to uncertainty over mail delivery following events related to the 9/11 terrorist attacks, the OCC issued a 12 September 2001 "encouragement" that banks voluntarily work with debtors who may pay bills late, especially if due to mail disruption.[16] A better solution in 2005, after four years of ever escalating complaints about ever-escalating late fees, would be to establish a hard date rule for all consumers. If the bill is postmarked by the due date, it is considered on time and no penalties can be imposed. Such a bill would address numerous problems faced by consumers.

First, with the endorsement of the OCC, bills are no longer on time unless received by a certain time during the due date. Second, attempts to make overnight deliveries when you don't remember to send your bill at least two weeks in advance result in late payments anyway, because overnight deliveries are not accepted at the same address. Finally, some banks have begun using confusing 3 week payment cycles which have made it harder to make payments on time.

In the past, numerous House members have proposed hard due date legislation, where a bill postmarked by the due date would be considered on time. Others have proposed legislation requiring a minimum 30 days for bills to be considered on time for the purpose of avoiding late payment penalties.[17]

Ban the Universal Default "Bait-and-Switch:" We have received numerous complaints that more and more banks are reviewing credit reports of existing customers and raising rates due to a decline in credit score or an alleged one or two late payments to any other creditor, even if the consumer's payments to the credit card issuer are timely and the account is in good standing. While we do not disagree that banks should be able generally to risk-price their products, we do not believe that universal default is being used as a proportional response but merely as a tool to increase revenue. We believe the regulators should be required to come forward with an analysis of the growing problem. After all, if the banks can offer dozens of different products to new customers based on their risk, why don't they have dozens of proportional responses for consumers when their risk increases?

As Representative Sanders has proposed, in the Credit Card Bait and Switch Act of 2003, HR 2724, the use of universal default should at least be strictly regulated, and as Senator Dodd has proposed in S. 499 this year, retroactive rate increases should be banned.

Give College Students And Other Young People Only The Credit They Deserve: Credit card companies issue credit to students without looking at credit reports (they don't have any) and without regard to ability to repay. Other Americans must have a good credit report or a co-signer to obtain credit. College students merely apply. College students and other young people should be protected from credit card debt hassles by having to meet similar standards, as S. 499 (Dodd) would provide. The proposed bill offers several ways for young consumers to qualify to obtain credit cards.

Further Restrict Pre-Acquired Account Telemarketing: Many of the deceptive practices described in the state actions above involve banks sharing customer information with tawdry third-party telemarketers selling even tawdrier products characterized by over-priced travel clubs and mediocre health insurance plans. In addition, many institutions have seized on the identity theft epidemic fueled by their own sloppy credit granting practices to pitch over-priced credit monitoring add-ons. In our view, neither the provisions of Gramm-Leach-Bliley dealing with encrypted credit card numbers nor changes to The Telemarketing Sales Rule have adequately stopped banks from treating their customers unfairly due to the lure of massive commissions from their telemarketing partners.

Cap Interest Rates: Reinstate federal usury ceiling for credit cards to prohibit the use of unconscionable penalty interest rates. Prime plus ten per cent seems like a reasonable profit.

Ban Mandatory Pre-Dispute Arbitration: The Congress has enacted legislation protecting car dealers from unfair arbitration clauses in their contracts with car manufacturers. The Senate has passed legislation similarly protecting farmers from arbitration in their contracts with powerful agribusiness concerns. It is time to enact similar legislation to protect consumers. Bills to ban pre-dispute mandatory arbitration in consumer credit card contracts have been proposed in 1999 by Rep. Gutierrez (HR 2258) and in 2000 by Rep. Schakowsky (HR 4332).

Ban The Use of Arbitration in Debt Collection Schemes: Arbitration agreements are not only being used in attempts to prevent consumers victimized by deceptive advertising and interest rate practices to have their day in court. Increasingly, according to a major new report by the National Consumer Law Center, major credit card companies, including First USA and MBNA, are partnering with arbitration firms to establish debt collection mills that force consumers into paying debts, including debts they may not even owe:

> Now, at least two giant credit-card issuers and one of the nation's largest firms arbitrating their consumer disputes have combined these practices in a disturbing new way: They're using binding, mandatory arbitration primarily as an offensive weapon, by fast-tracking disputes over credit-card debt into rapid arbitration. A number of consumers charge that the banks often do this with little notice, after long periods of dormancy for the alleged debt or over consumers' specific objections -- then force those who don't respond swiftly or adequately into default. The arbitrator often forces the consumer to also pay for the hefty arbitration costs and the card issuer's attorney, making the total tab for consumers several times the original amount owed and many times what it would have been in more traditional debt settlements. So it's a neat pathway to turbo-charged profits for both the card issuer and the arbitrator.[18]

We were disappointed that the Congress recently enacted a one-sided bankruptcy bill, absent proof of abuse. The bill failed to rein in these practices. We respectfully urge you to consider our proposals to rein in the unfair credit card company practices described above that have exacerbated the growth of credit card debt, which is the real problem we face, not abuse of the bankruptcy laws. In addition to the bankruptcy law's general manifest harshness and its intended elimination of a critical safety net during uncertain economic times, the bill's nominal credit card disclosures are deficient and unacceptable, as we pointed out above.

In addition to banning certain practices as above, U.S. PIRG, the Consumer Federation of America and others recently joined the National Consumer Law Center in detailed and comprehensive comments to the Federal Reserve Board on ways to improve the Truth In Lending Act's disclosures and other regulations. The comments provide a window on the way that the industry exploits loopholes and inconsistencies in the act to hurt and exploit consumers.[19] The TILA was supposed to be a remedial act, a law written to prevent unfair practices, and has often been correctly interpreted that way in the courts, yet the regulators have insisted on allowing the industry to carve out nooks and crannies that allow banks to avoid the spirit of the law. The proposals below augment and update the disclosures in the important 1988 disclosure legislation that established what is known as the "Schumer" box, which requires credit card company solicitations to clearly and prominently disclose all fee and interest related "trigger terms."[20]

Additional key statutory changes recommended in those comments include the following:

• A cap on all other charges, whether considered a finance charge or not, to an amount the card issuer can show is reasonably related to cost.
• No unilateral change-in-terms allowed.
• No retroactive interest rate increases allowed.
• No penalties allowed for behavior not directly linked to the specific card account at issue.
• No over limit fees allowed if issuer permits credit limit to be exceeded.
• No improvident extensions of credit –require real underwriting of the consumer's ability to pay.
• Meaningful penalties for violating any substantive or disclosure that provide real incentives to obey the rules.
• A private right of action to enforce section 5 of the Federal Trade Commission Act, which prohibits unfair or deceptive practices by businesses, including banks.

(4) ABUSIVE CREDIT CARD INDUSTRY PRACTICES ON CAMPUS

Having saturated the working adult population with credit card offers, credit card companies are now banking on a new market: college students. Under regular credit criteria, many students would not be able to get a card because they have no credit history and little or no income. But the market for young people is valuable, as industry research shows that young consumers remain loyal to their first cards as they grow older. Nellie Mae, the student loan agency, found that 78% of undergraduate students had credit cards in 2000. Credit card companies have moved on campus to lure college students into obtaining cards. Their aggressive marketing, coupled with students' lack of financial experience or education, leads many students into serious debt. According to a recent PIRG study, the Burden of Borrowing, credit card debt exacerbates skyrocketing student loan debts. That 2002 study found that thirty-nine percent (39%) of student borrowers now graduate with unmanageable levels of debt, meaning that their monthly payments are more than 8% of their monthly incomes. The study also found that student borrowers were student borrowers were even more likely to carry credit card debt, with 48% of borrowers carrying an average credit card balance of $3,176.[21]

Campus Marketing: In 2004, Maryland PIRG and the Maryland Consumer Rights Coalition releasing a shocking study of credit card marketing practices on the state's college campuses. Among the highlights of Graduating Into Debt[22] were the following:

• Credit card vendors are setting up tables on some campuses in violation of university policies prohibiting or limiting tabling.
• At least two schools currently sell their student lists (names, addresses and telephone numbers) to credit card issuers.
• Several schools have exclusive marketing agreements with one credit card issuer for which they receive financial compensation.
• Only one school that allows on-campus marketing has a comprehensive written policy specifically governing credit card marketing.

Previously, a PIRG study, the **Credit Card Trap,** released in April 2001, included a detailed study of the worst credit card practices. The report was released at the same time as we announced a detailed fact sheet available at a new website truthaboutcredit.org.[23] Because Linda Sherry of Consumer Action is releasing more recent survey data, I will not go into details on the report's survey results. The key findings of a year 2000 survey of 100 credit card offers included in "The Credit Card Trap" are available online.[24] The report also included a survey of college student marketing, which we summarize here.

Marketing to College Students Is Aggressive

The State PIRGs surveyed 460 college students within the first month of either the fall or spring semester of 2000–2001. The key findings include:

- Two-thirds of college students surveyed had at least one credit card. The average college student had 1.67 credit cards.
- 50% of students obtained their cards through the mail, 15% at an on-campus table, and 10% over the phone.
- 50% of students with cards always pay their balances in full, 36% sometimes do, and 14% never do.
- 48% of students with one or more cards have paid a late fee, and 7% have had a card cancelled due to missed or late payments.
- 58% of students report seeing on-campus credit card marketing tables for a total of two or more days within the first two months of the semester. Twenty–five percent report seeing on-campus tables more than five days.
- One-third have applied for a credit card at an on-campus table. Of these, 80% cite free gifts as a reason for applying.
- Only 19% of students are certain that their schools have resources on the responsible use of credit. Three out of four of these students (76%) have never used these resources.

The state PIRGs have run counter-education campaigns against credit card marketing on campus. The industry and its vendors set up tables where hawkers distribute "free" t-shirts, Frisbees and candy to students who apply for cards. They also aggressively post so-called "take-one" flyers on bulletin boards in every classroom. PIRG chapters have set up tables where we distribute credit card education literature. We also have created our own "think twice" take-one flyers and posted them on campuses. The brochures link to our website, truthaboutcredit.org.

We believe it is appropriate and proper for colleges and universities to regulate credit card marketing on campuses, including consideration of restrictions or bans on credit card tabling and other marketing. In addition, colleges should improve generally weak financial literacy, credit card and debt training programs for students, as should high schools. However, we believe that these responses are best made by student governments, college administrators or state legislatures, not the Congress, so we make no specific recommendations here.

(5) BRIEF PROFILE OF THE CREDIT CARD INDUSTRY:

Our policy changes can be made without hurting the credit card companies, who have enjoyed a lucrative ten year run at the expense of consumers. Credit card lending is the most profitable form of banking, according to the Federal Reserve's most recent report to Congress in 2004: "Although profitability for the large credit card banks has risen and fallen over the years, credit card earnings have been consistently higher than returns on all commercial bank activities."[25] In recent years, those profits have hovered at or near record levels. Profits in 2003 were $30 billion according to various sources, with late and over-the-limit fees adding dramatically to the total.

There may be, as the industry witnesses will trumpet, some 6,000 credit card issuers. But there are only ten that matter. The actual marketplace is highly concentrated. The nation's top ten bank credit card issuers grew an average of 6.5% during 2003, holding aggregate card loans of $538.9 billion, approximately 77% of the total U.S. market.

Since 1980, revolving debt, which is largely credit card debt, increased from just $56 billion to $800 billion, according to the most recent Federal Reserve postings of May 2005.[26] Approximately 55% of consumers carry balances (the rest are convenience users) meaning consumers with credit card balances average $10-12,000 each in total credit card and revolving debt.[27]

Credit card companies have increased profit by increasing the amount of credit outstanding by decreasing cardholders' minimum monthly payments, increasing interest rates, and piling on enormous fees. Until very recently, credit card companies engaged in a practice of decreasing the minimum percentage of the balance that cardholders must pay in order to remain in good standing. Today, most companies still require a minimum monthly payment of only 2% or 3% of the outstanding balance. As a result, cardholders who choose to pay only the minimum each month take longer to pay off their balances, paying more interest in the process. In its recent guidances, the OCC has admonished banks to raise these minimum payment levels. "The required minimum payment should be sufficient to cover finance charges and recurring fees and to amortize the principal balance over a reasonable period of time."[28]

According to a U.S. PIRG analysis, a consumer carrying just $5,000 of debt at 16% APR would take 26 years to pay off the balance if she only made the 2% requested minimum payment, even if she cut the card up and never used it again.

An industry source indicates that in 2003, 69 percent of US households received an average of 4.8 offers per month, or 58 offers/year. The Federal Reserve also estimates that this has resulted in American consumers now carrying an average of 4.8 credit cards each[29]. During 2004, US households received estimated 5.23 billion credit card offers, up 22% compared to 2003 and exceeding the previous record of 5.01 billion offers set in 2001.[30]

(6) STATE PREEMPTION: ANOTHER PART OF THE PROBLEM

Although states have recently aggressively sought to enforce unfair and deceptive practices laws against credit card companies, the states have been limited in their enforcement by the growing use of preemption theory to restrict their regulation of the industry. In 1978, in Marquette,[31] the Supreme Court held that states could export nationally the interest rates of the bank's home state, prompting a concentration of the industry in a few bank-friendly states, including Delaware and South Dakota. In 1996, the court in Smiley[32] extended the Marquette holding by defining late fees as "interest," allowing a bank's home state late fee rules to similarly be exported nationally.

These onerous decisions applied only to the regulation of interest and fees, not to disclosures. In 2002, a U.S. District Court used National Bank Act preemption theory, backed by the OCC, to overturn an important new California law requiring a monthly minimum payment warning, further restricting state authority to protect consumers.[33] Then, of course, in 2004, the OCC imposed two onerous administrative rules restricting states from enactment or enforcement against national banks and their state-licensed operating subsidiaries[34].

These decisions and actions have aided and abetted the anti-consumer practices of this industry and deserve careful scrutiny by the committee. We remain disappointed that the committee has not reined in the over-reaching OCC rules, although it did hold an important oversight hearing in the last Congress.[35]

(7) CONCLUSION

We thank you for holding this important oversight hearing. We urge the committee to go further and enact legislation protecting consumers from unfair credit card company practices. We hope that we have provided you with adequate information to support the need for action by the Congress to rein in the credit card industry's most unfair and abusive practices and would be happy to work with your staffs on proposed legislation.

ENDNOTES

[1] See an Office of the Comptroller of the Currency (OCC) regulatory interpretative letter endorsing debt cancellation and debt suspension products as part of the business of banking (and exempt from stricter state insurance regulation) at http://www.occ.treas.gov/interp/jan01/int903.doc

[2] The consumer organizations testifying today, U.S. PIRG, the Consumer Federation of America and Consumer Action, are all founding members of a broad new campaign to educate the public and the Congress about the need to eliminate one-sided binding mandatory arbitration (BMA) clauses imposed as contracts of adhesion in consumer contracts, sometimes merely with a notice of change of terms inserted in a consumer's bill. See http://www.stopbma.org/

[3] It is the bank position that the Truth In Lending Act allows them to change fixed rates with as little as fifteen days notice and that a fixed rate is merely a rate that is not variable. A variable rate is defined as one tied to an index, such as the Wall Street Journal prime rate as disclosed on a certain date.

[4] Obtain these guidances and copies of recent regulatory actions at the OCC credit card practices website available at http://www.occ.treas.gov/Consumer/creditcard.htm

[5] 9 May 2005, See news release "ATTORNEY GENERAL DARRELL McGRAW SUES TO ENFORCE SUBPOENAS INVESTIGATING CAPITAL ONE BANK AND CAPITAL ONE SERVICES," available at http://www.wvs.state.wv.us/wvag/

[6] See "State Sues Cross Country Bank over Harassing Debt Collection Practices," 3 April 2003, available at the Minnesota Attorney General's website http://www.ag.state.mn.us/consumer/PR/pr_CrossC_40303.htm In November, 2004 the state obtained a temporary injunction barring the bank's abusive practices. See http://www.ag.state.mn.us/consumer/PDF/CrossCountryBank.pdf

[7] 24 June 2004, Press release of Pennsylvania Attorney General's Office "AG Pappert takes action against bank and its collection company in alleged predatory lending/credit card scheme," available at http://www.attorneygeneral.gov/press/pr.cfm

[8] 31 December 2002, FIRST USA TO HALT VENDORS' DECEPTIVE SOLICITATIONS, Press Release of New York Attorney General Eliot Spitzer, available at http://www.oag.state.ny.us/press/2002/dec/dec31a_02.html

[9] 27 Feb 2002, AGREEMENT CURBS TELEMARKETING APPEALS TO BANK CUSTOMERS, Press Release of New York Attorney General Eliot Spitzer, available at http://www.oag.state.ny.us/press/2002/feb/feb27b_02.html

[10] Fact Sheet Regarding Settlement Between the OCC and Direct Merchants Bank, 3 May 2001

[11] See "Providian to Refund $300 Million to Consumers Over Alleged Abusive Credit Card Practices," 28 June 2000 available at California Attorney General page http://caag.state.ca.us/newsalerts/2000/00-098.htm

[12] June 28, 2000, Statement of Comptroller of the Currency John D. Hawke, Jr.

[13] See Rossman v. Fleet Bank (RI) Nat'l Ass'n, 280 F.3d 384, 390-91 (3d Cir. 2002) available at http://laws.lp.findlaw.com/3rd/011094.html

[14] See Rossman v. Fleet Bank (RI) Nat'l Ass'n, 280 F.3d 384, 390-91 (3d Cir. 2002) available at http://laws.lp.findlaw.com/3rd/011094.html

[15] See OCC news release, "Acting Comptroller Williams Tells Bankers Disclosures not Working for Consumers," 12 May 2005 available http://www.occ.treas.gov/scripts/newsrelease.aspx?Doc=Z1J2IZ9.xml

[16] See OCC Press release NR- 2001-79.

[17] See, eg, bills previously filed by Representatives including Darlene Hooley, (HR 3477, 1999) and Andy Jacobs, (HR 1537, 1995) and John McHugh, (HR 1963, also in 1995).

[18] See 17 February 2005, "New Trap Door for Consumers: Card Issuers Use Rubber-Stamp Arbitration to Rush Debts Into Default Judgments," National Consumer Law Center, available at http://www.consumerlaw.org/initiatives/model/content/ArbitrationNAF.pdf

[19] See Comments of National Consumer Law Center, U.S. PIRG, Consumer Federation of America et al "Regarding Advance Notice of Proposed Rulemaking: Review of the Open-End (Revolving) Credit Rules of Regulation Z," Federal Reserve System, 12 CFR Part 226, Docket No. R-1217 available at http://www.consumerlaw.org/initiatives/test_and_comm/content/open_end_final.pdf

[20] The Fair Credit and Charge Card Act of 1988's disclosures were championed by Representative Chuck Schumer, now a Senator and a member of this committee.

[21] See "The Burden of Borrowing," the State PIRGs' Higher Education Project, March 2002, available at http://www.pirg.org/highered/highered.asp?id2=7972

[22] See "Graduating Into Debt: Credit Card Marketing on Maryland College Campuses," February 19, 2004, Maryland Consumer Rights Coalition and Maryland Public Interest Research Group, available at http://marypirg.org/MD.asp?id2=12264&id3=MD&

[23] "The Roadmap To Avoid Credit Hazards" is downloadable at http://www.truthaboutcredit.org/roadmap.pdf. Numerous other materials and reports are available at http://www.truthaboutcredit.org .

[24] See the state PIRG credit card education website http://www.truthaboutcredit.org

[25] "The Profitability of Credit Card Operations of Depository Institutions: An Annual Report by the Board of Governors of the Federal Reserve System, submitted to the Congress pursuant to Section 8 of the Fair Credit and Charge Card Disclosure Act of 1988," June 2004, available at http://www.federalreserve.gov/boarddocs/rptcongress/creditcard/2004/ccprofit.pdf

[26] See http://www.federalreserve.gov/releases/g19/Current/

[27] The banks frequently cite a Federal Reserve analysis of University of Michigan Survey of Consumer Finances polling data to allege that only 45% of consumers carry a balance. Consumer group contacts with industry sources indicate that these numbers are low. If true, of course, average balances would be even higher. Consumer groups use a conservative figure of 55% carrying balances, with some sources putting the number as high as high as 60% or more. For a discussion of our analysis of credit card debt calculations, see the state PIRG report "Deflate Your Rate," March 2002, available at http://www.truthaboutcredit.org

[28] OCC Advisory Letter AL 2004-4, April 28, 2004, available at http://www.occ.treas.gov/ftp/advisory/2004-4.txt

[29] "The Profitability of Credit Card Operations of Depository Institutions: An Annual Report by the Board of Governors of the Federal Reserve System, submitted to the Congress pursuant to Section 8 of the Fair Credit and Charge Card Disclosure Act of 1988," June 2004, available at http://www.federalreserve.gov/boarddocs/rptcongress/creditcard/2004/ccprofit.pdf

[30] According to Mail Monitor, the direct mail tracking service from Synovate.

[31] In 1978, the Supreme Court in Marquette vs. First Omaha Service Corp invalidated state usury laws as they apply to national banks. Marquette held that under Section 85 of the National Bank Act (NBA) of 1863 national banks could export to any of their customers, no matter where they lived, the highest interest rate allowed in the bank's home state, now usually Delaware, Virginia, Nevada or South Dakota. See Marquette Nat. Bank. V. First of Omaha Services, 439 US 299 (1978).

[32] In Smiley, the Supreme Court extended Marquette to allow exportation of a home state's fees. The court paid deference to a new OCC rule that added a wide range of fees to the definition of interest under Section 85 of the National Bank Act, including late fees, over limit fees, annual fees, and cash advance fees. See Smiley v. Citibank (South Dakota). 517 US 735 (1996)

[33] Since the federal Truth In Lending Act was non-preemptive with respect to certain account statement disclosures, California enacted legislation (Civil Code Section 1748.13) requiring that monthly credit card statements disclose information about how long it would take to pay off a card if you only made the minimum requested monthly payment. Federal law did not then require this, although a similar, weaker provision is included in the bankruptcy law recently signed (Public Law 109-8). The law was overturned on summary judgment in American Bankers Association v. Lockyer, 239 F. Supp. 2d 1000, 1009 (E.D. Cal. 2002).

[34] See the PIRG OCCWatch website for detailed information on the OCC's anti-consumer actions, including links to its rules, http://www.pirg.org/occwatch Also see "Preemption Of State Consumer Laws: Federal Interference Is A Market Failure," by U.S. PIRG's Edmund Mierzwinski, which appeared in the Spring 2004 (Vol. 6, No. 1, pgs. 6-12) issue of the Government, Law and Policy Journal of the New York State Bar Association. The article includes a major section on the OCC rules, available at http://www.pirg.org/consumer/pdfs/mierzwinskiarticlefinalnysba.pdf

[35] 7 April 2004, Review of the National Bank Preemption Rules, Oversight Hearing of the U.S. Senate Banking Committee, available at http://banking.senate.gov