

THE CREDIT CARD TRAP: How to Spot It, How to Avoid It

TABLE OF CONTENTS

Executive Summary	1
Key Findings	2
I. Terms and Conditions Are Worsening	2
II. Marketing Practices Are Misleading and Deceptive	2
III. Marketing to College Students is Too Aggressive.....	3
Introduction: The High Cost of Credit	5
Students And Credit Cards	6
Credit Card Fees and Terms Are Worsening: Findings of the State PIRGs’ National Credit Card Survey	7
Graph 1: Penalty APRs: One Late Payment Can Cost You.....	12
Table 1—Fleet Mastercard Penalty Rate Can Cost You	12
Findings: Student Credit Card Usage And On-Campus Marketing	13
Additional Costly Credit Card Company Tactics	14
Table 2: Low Monthly Minimum Payments Are Profitable.....	14
Manipulative Marketing Practices	16
Credit Card Companies: Anti-Consumer Practices and Legal Action	20
Where To Find Disclosures About The Terms And Conditions Of A Credit Card Offer	23
Front	23
Back.....	23
TERMS TO UNDERSTAND	23
Table 3: HOW APR AFFECTS THE COST OF CREDIT	25
Recommendations	29
PIRG Credit Card Consumer Checklist	30
Table 4: To Obtain Credit Reports:.....	31
Recommendations For College Administrators	31
Law and Policy Recommendations	32
Survey Methodologies	33
Additional Resources	34
Endnotes	35

ATTACHMENTS:

Appendix A: 1 page

Results from the State PIRGs’ Survey of 100 Credit Card Offers

Appendix B: 4 pages

**Results from the State PIRGs’ Survey of Students’ Credit Card Usage and
On-Campus Marketing**

Appendix C: 3 pages

Selected Offer Data for Fixed and Variable Rate Cards

THE CREDIT CARD TRAP: How to Spot It, How to Avoid It

EXECUTIVE SUMMARY

Credit card companies are flooding us with card solicitations, deceiving us with misleading offer terms, and gouging us with higher-than-ever fees. As a result, consumers are sinking further into high-cost credit card debt.

As credit card companies intensify their marketing campaigns to boost profits, consumers are being flooded with more flashy credit card offers than ever before. In the second quarter of 2000, credit card companies sent a combined total of 992 million solicitations, a record high. The average household receives eight credit card offers each month, and students, who often have no regular income, are encouraged several times a week by posters, fliers, and on-campus marketers to apply for credit cards.

At the same time, credit card companies are charging outrageous interest rates as high as 30% per year. Consumers, students, and others are subject to a host of unfair and deceptive terms and conditions, saddled with enormous fees, and encouraged by credit card companies to make low minimum payments so that the companies can earn more in interest. As a result, the average credit card debt for Americans who carry balances reached \$5610 in 2000, an increase of nearly one-third since 1995.

As consumers struggle, credit card companies are making bigger profits than ever. Between 1995 and 1999, thanks in part to aggressive marketing and misleading practices, companies' profits skyrocketed from \$7.3 billion to \$20 billion.

In order to reduce their own debt losses and increase profits, the credit card industry is spending millions—more than \$6 million in the first half of 2000—to pass further bankruptcy restrictions and to defeat pro-consumer bankruptcy legislation. The credit card industry is seeking to make it more difficult for consumers to declare bankruptcy and to increase the amount of debt for which consumers will be liable after declaring bankruptcy. Economic experts have pointed out that by making it more difficult for cardholders to default through bankruptcy, these industry-sponsored, anti-consumer bankruptcy restrictions will encourage credit card companies to be more predatory in lending, because the risk of issuing cards to higher-risk consumers such as students and those with low incomes will decline.

An additional measure of the problem with credit card marketing is increased attention by regulators. In June 2000, the Treasury Department's Office of the Comptroller of the Currency (OCC) imposed a civil penalty and restitution order totaling over \$300 million against the sixth largest credit card bank, Provident. In September 2000, the Federal Reserve Board issued new regulations requiring improved disclosures in credit card solicitations.

The State PIRGs conducted two surveys for this report. In a survey of 100 credit card offers during the summer of 2000, the State PIRGs found two major themes: (1) credit card terms and conditions are becoming less favorable to consumers; and (2) credit card marketing practices are misleading and deceptive. In an on-campus survey of college students, conducted during the current school year, the State PIRGs found that the marketing of credit cards to college students is too aggressive. The State PIRGs compared these results to those of a 1998 PIRG survey and found that the situation has not improved.

KEY FINDINGS

I. Terms and Conditions Are Worsening

In a survey of 100 credit card offers, the State PIRGs found that:

- **The average penalty annual percentage rate (APR) was 22.84%, eight points higher than the average APR for purchases, and is triggered by as little as one late payment or a late payment to another creditor.**

The average penalty APR (the APR for accounts that are delinquent) was 22.84%, nearly eight percentage points higher than the average APR for purchases.

That increase is especially concerning because credit card companies may charge the penalty APR if a single payment is even one day late or arrives later than a specified time on the due date. Credit card companies may also charge a penalty APR if the creditor finds that there is a problem with a cardholder's payment pattern on other debts. Once a penalty APR is assessed, it may remain in place permanently or for a particular amount of time.

- **The average late payment fee was \$27.61, and fees ranged from \$15–\$35.**

All cards surveyed assessed late payment fees, which ranged from \$15 to \$35 and averaged \$27.61.

Consumers are paying more and credit card companies are reaping more profit from late fee income than ever before. Income from late fees has risen for three reasons:

- (1) the average late fee has more than doubled since 1992, when the average was \$12.53, and fee amounts continue to grow;
- (2) companies have decreased the amount of time between when a bill is mailed and payment is due; and
- (3) nearly two-thirds of companies have eliminated leniency periods, the time after a payment's due date before a late fee is assessed.

- **The average grace period was 22.6 days. Five cards had no grace period at all.**

The average grace period was 22.6 days. Only one card surveyed had a grace period of 30 days, and five (all from the same company) had no grace period at all. Grace periods are rapidly decreasing in length as credit card companies realize that shorter grace periods bring in more profit. In addition, a grace period usually does not apply if a balance is carried from month to month.

- **The average over-the-limit fee was \$27.61, and fees ranged from \$15–\$35.**

All 100 cards surveyed charged over-the-limit fees to cardholders who exceeded their credit limits by as little as one dollar. Those fees ranged from \$15 to \$35, and averaged \$27.61. The State PIRGs' survey found only one company that charged a fee of less than \$20. In addition, a punitive APR increase often accompanies the assessment of an over-the-limit fee, worsening the financial impact on consumers.

- **Minimum payments are decreasing, bringing in more money for credit card companies.**

Credit card companies are raising profits by lowering minimum payments from the former industry standard of 5% of the unpaid balance to as low as 2%. As a result, consumers who pay only the minimum each billing cycle stay in debt longer and pay more interest.

II. Marketing Practices Are Misleading and Deceptive

- **Credit card companies use low, short-term “teaser rate” introductory APRs to mask higher regular APRs. The average introductory APR was 4.13%, which jumped 264% to an average regular APR of 15.04%.**

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. Of the 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 (a practice called “bait and switch”). 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 have significant restrictions or hidden costs, such as enrollment fees or expiration dates.

- **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. For example, Provident National Bank’s Aria card has a range of 7.99% (for “preferred” customers) to 20.24%. As a result, applicants don’t know what APRs they will get until they receive their cards.

- **“Fixed” rates may not be fixed at all.**

Credit card companies play on consumers’ common misconception of the term “fixed rate.” Though companies imply that a fixed rate will not increase for the life of the card, companies actually may increase fixed rates with as little as 15 days notice to cardholders.

- **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.

III. Marketing to College Students is Too Aggressive

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.

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.**

Congress has failed to enact any meaningful reform. In the meantime, the credit card industry is seeking not only to make it more difficult for consumers to declare bankruptcy, but also to increase the amount of debt for which consumers will be liable after declaring bankruptcy. Economic experts have pointed out that by making it more difficult for cardholders to default through bankruptcy, these industry-sponsored, anti-consumer bankruptcy restrictions will encourage credit card companies to be more predatory in lending, because the risk of issuing cards to higher-risk consumers such as students and those with low incomes will decline. The State PIRGs oppose the industry-supported bankruptcy bills and amendments that seek to punish, rather than assist, consumers in debt.

The State PIRGs urge state and federal lawmakers to:

- (1) strengthen consumer protection laws by outlawing such deceptive practices as failing to prominently disclose non-introductory and penalty APRs; making minimum monthly payment requirements too low; and using “bait and switch” marketing; and
- (2) empower consumers by improving meaningful disclosures. For instance:
 - The actual, non-introductory APR should be displayed as prominently as the introductory APR throughout the offer.
 - The amount of time and interest required to pay off a balance at the minimum payment rate should be included on every periodic statement and customized to each cardholder.
 - All offers should state the penalty APR and the conditions under which it will go into effect.

The State PIRGs also commend the San Francisco District Attorney, the Attorney General of Minnesota, and other states’ Attorneys General for taking action against illegal or deceptive credit card marketing. For example, in the summer of 2000, the San Francisco District Attorney and the OCC imposed a \$300 million civil penalty and restitution order against Provident. The suit had alleged multiple anti-consumer practices, including a charge that Provident billed cardholders for services the cardholders had not agreed to, and that the company intentionally posted payments late in order to receive more late fee income. Minnesota Attorney General Mike Hatch has filed important lawsuits against financial institutions including U.S. Bank and Fleet Mortgage, and the telemarketer Memberworks, over the sharing by banks of confidential credit card and other non-public personal information with telemarketers¹.

THE CREDIT CARD TRAP: How to Spot It, How to Avoid It

INTRODUCTION: THE HIGH COST OF CREDIT

Though interest rates fell sharply in the early 1990s after twenty years of relative stability, the cost of credit has risen dramatically since then.²

In its 1999 *Annual Report to Congress* on credit card pricing, the Federal Reserve Board acknowledged that “credit card pricing . . . involves other elements, including annual fees, fees for cash advances, rebates, minimum finance charges, over-the-limit fees, and late payment charges.”³ The report also notes that, in the past, card issuers offered one interest rate for all customers. In recent years, however, issuers have begun to offer a range of interest rates, with the specific rate offered to a consumer dependent on that consumer’s particular credit risk and usage patterns. Finally, the report notes that issuers have tried to make their cards more attractive by offering low introductory rates, especially on balance transfers, and by offering affinity cards, such as cards with airline mileage programs or cash rebates.⁴

Credit card companies have increased the cost of credit by decreasing cardholders’ minimum monthly payments, increasing interest rates, and piling on enormous fees. In recent years, credit card companies have decreased the minimum percentage of the balance that cardholders must pay in order to remain in good standing. Today, most companies 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.

Credit card companies’ profits nearly tripled from 1995 to 1999, jumping from \$7.3 billion to \$20 billion. The industry’s widespread adoption of costly terms and conditions helped lead to this massive increase in profits. Some of the newest conditions companies have imposed on consumers include:

- increased late payment fees,
- significant annual percentage rate (APR) increases after only one or two late payments,
- increases in a consumer’s APR when her standing with other creditors declines,
- increased APRs for cash advances, decreased grace periods, and
- decreased minimum monthly payments.

In 2000, fee income accounted for 25% of credit card companies’ total income, and between 1995 and 1999, total fee income increased by 158%, from \$8.3 billion to \$21.4 billion.⁵

The rising cost of credit is contributing to an increase in average personal debt. In 2000, the average credit card debt for Americans who carry a balance reached \$5610, and increase of nearly one-third since 1995.⁶

Consumers file for bankruptcy to bring enormous debts under control. The typical Chapter 7 bankruptcy filer has high credit card debts—in 1996, \$17,544 in credit card debt and an annual after-tax income of \$19,800.⁷ From 1996-2000, revolving debt, such as that incurred by the use of credit cards, accounted for about 20% of total household debt, according to the Federal Reserve.

Students And Credit Cards

During his first semester of college, Jeff applied and was approved for two credit cards. Jeff planned to use his card only if he knew he could pay off the balance right away, but the temptation to spend money for things he couldn't afford proved to be too great. Within the next year Jeff received eight new credit cards. Soon Jeff had exhausted all his financial resources.

Jeff continued to receive credit card offers from new companies, and his current companies increased the credit limits on his cards. Letters notifying him of increases in his limits told him that he had "earned" the increases, giving Jeff the impression that the credit card companies didn't consider his debts to be too significant. Therefore, Jeff continued to tell himself that his financial situation wasn't a serious problem, even though he was unable to pay even the minimum on his balances each month.

By the end of his junior year, Jeff had 11 bank cards and 5 retail credit cards. In addition to being a residence hall advisor, which paid very little, Jeff started working at least 30 hours per week at two part-time jobs so that he would be able to make the minimum payments on his cards each month. After only three years in college, Jeff faced \$20,000 in credit card debt.

Jeff believes that the "credit card industry knows exactly what it is doing [by encouraging debt] while taking advantage of students. . . . How can these banks justify giving me 11 credit cards on an annual income of only \$9,000?" Jeff's school offered no financial education information or counseling for credit problems. Says Jeff, "Everything is discussed in freshman orientation or residence hall programs: AIDS, suicide, eating disorders, alcohol, depression, peer pressure, sex ed, academic pressures—all but financial crisis management."

—Excerpted from *"The Power of Plastic: The Costs and Consequences of Student Credit Card Debt."* Robert Manning, *Georgetown University, 1998.*

Faced with stockholder pressure to maintain astronomical growth rates and a saturated market of working adults, credit card companies are seeking out new populations to which they can market cards. Despite the fact that most students have little or no income, college students have become a lucrative market for credit card companies in recent years. Research conducted by the credit card industry has found that young adults tend to remain extremely loyal to their first card as they grow older. Thus, credit card companies want to secure that loyalty early in order to increase profits once the student becomes a salaried adult.⁸ Maria Mendler, vice president of public affairs for Citibank, has said, "If you look at the college market, this could potentially be our best long-term customer."⁹

The college student market has turned out to be a wild success for credit card companies. A 2000 survey by Nellie Mae, the student loan agency, found that three out of five college students carry at least one credit card. The study also found that the average balance on undergraduates' credit cards was \$2748.¹⁰

Credit card companies that market on college campuses frequently offer free gifts to students for filling out card applications. Some companies also offer money to campus groups based on the number of applications that are filled out. These marketing practices encourage students to apply for credit cards merely for the sake of obtaining the free gifts or in order to help school groups obtain the financial rewards offered by credit card companies. Because more students apply for cards as a result of these

marketing tactics, credit card companies are encouraged to use even more aggressive tactics when marketing to college students.

In addition, credit card companies give large sums of money to colleges for the privilege of marketing on campus and to alumni. Georgetown University, for example, accepted \$2.3 million from a credit card company for an exclusive marketing agreement. Not a penny of this money was spent on financial education for students.¹¹ In January 2001, *60 Minutes II* reported on a typical large university contract between First USA and the University of Oklahoma:

“First USA pays \$13 million to get on campus and issue a credit card with the University of Oklahoma’s name on it. Hundreds of colleges are cutting similar deals. The ten year contract between First USA and the University of Oklahoma gives the bank the exclusive right to market its MasterCard or Visa to the [school’s] alumni, employees, and students. First USA guarantees the university a minimum payment of \$13 million and the school gets 0.4% of every purchase students charge. On demand, the university agrees to provide the bank with the names, addresses, and phone numbers of its 21,000 students.”¹²

Numerous studies by independent consumer groups have found that young adults lack the knowledge necessary to successfully manage their own finances. For example, Jump Start, an organization devoted to educating children and teens about financial matters, administered a test of personal finance skills to 1500 high school seniors.¹³ The average score was 57%, an F on any grading scale. Only 5% of the seniors scored a C or better. Few school systems incorporate financial education into their basic curriculums, and as a result students enter the real world with little knowledge of personal finance.

CREDIT CARD FEES AND TERMS ARE WORSENING: FINDINGS OF THE STATE PIRGS’ NATIONAL CREDIT CARD SURVEY

The State PIRGs reviewed 100 credit card offers in June 2000 and found disturbing trends within the credit card industry to boost profits at consumers’ expense. Credit card companies have increased profits by raising existing fees, inventing fees, and making payment conditions more stringent (for example, by shortening grace periods) so that cardholders are less able to avoid penalty fees. Credit card companies’ anti-consumer practices also include increasing annual percentage rates, lowering minimum payments, and including automatic arbitration clauses in credit card application contracts.¹⁴ Some of the most prevalent practices are described below:

LATE FEES

- **100% of cards surveyed charged late fees. The average late fee was \$27.61, and fees ranged from \$15 to \$35.**
- **Fees have increased 10% from a 1999 survey average of \$25.20.¹⁵**
- **Five cards charged the highest fee of \$35.**

Credit card companies continue to increase their profits by increasing their fees. Late fees, in particular, have skyrocketed in the last four years. In a 2000 survey, Consumer Action (CA) found that the average late fee increased 112% from 1992 to 2000.¹⁶ Credit card companies have escalated the number of late penalty fees they assess in three ways:

1. Less Time to Pay the Bill

Companies have shortened the length of time between the arrival of the monthly statement and the payment due date. The interval between receiving a bill in the mail and sending in a

payment may be less than two weeks.¹⁷ As a result, there is a higher chance of a late payment charge being assessed.

2. Early Posting Deadlines

Companies have moved payment posting deadlines to earlier times of day, such as 8:00 a.m., which effectively means that a payment must be received the day before it is due to be posted on the due date.¹⁸ Citibank and MBNA, for example, consider a payment late if it is not received by 10 a.m. on the due date.¹⁹ Posting times are generally found only in the fine print of a credit card agreement. As mail is rarely delivered before 9 or 10 a.m., early posting times have the net effect of requiring a payment to arrive the day before the stated due date, a practice which misleads consumers and results in a higher rate of late fee assessment. (On November 16, 2000, two consumers in Miami filed a suit against MBNA for its practice of considering payments to be late if not received by 10 a.m. The plaintiffs' lawyers are seeking class action status.²⁰)

3. Elimination of Leniency Periods

Companies have decreased or eliminated leniency periods. (The leniency period is the amount of time after the due date that a payment can arrive before the company assesses a late fee.) In the past, credit card companies had leniency periods of 5-15 days; today, nearly two-thirds of all companies impose late fees immediately.

Automatic payment programs are advertised as a way for consumers to avoid the worries of remembering to pay their credit card bills on time each month. However, consumers might not escape late fees by enrolling in their credit card companies' automatic payment programs. Enrollment in an automatic payment program authorizes a credit card company to deduct payments directly from a cardholder's bank account each month. However, First USA Bank charges late fees to cardholders enrolled in its automatic payment program if the program withdraws payments late.²¹

Of course, late fees are only part of the penalty for paying late. Often, late payments also trigger penalty APRs and negative credit reports.

OVER-THE-LIMIT FEES

- **100% of cards surveyed assessed an average over-the-limit fee of \$27.61.**
- **Fees ranged from \$15 to \$35 per offense, with 5 cards charging the highest fee, \$35.**

Credit card companies charge over-the-limit fees to any cardholder whose outstanding balance exceeds his or her credit limit. The number of banks charging a penalty of \$20 or more to cardholders who exceeded their credit limits has exploded. According to one 1995 survey, only one bank charged an over-the-limit fee of \$20 or more.²² Today, the State PIRGs found only one card (the FirstStar Bank College Card) out of 100 surveyed that charged a penalty of less than \$20.

Over-the-limit fees are charged at the slightest overextension. Citibank, for example, charges the fee when a cardholder exceeds his or her limit by as little as one dollar.²³

In addition to charging over-the-limit fees, credit card companies will often also increase the APRs of cardholders who exceed their limits, effectively penalizing consumers twice for one infraction. (For more information, see the section in this report on penalty APRs, page 15.)

CASH ADVANCE RATES AND TRANSACTION FEES

- **70% of offers stated the APR for cash advances. The average APR was 19.03%, and the highest was 27.50%.**

- **70% of cards (49 of 70) that disclosed the APR for cash advances charged a higher APR for cash advances than for purchases.**
- **APRs for cash advances were, on average, 3.99 percentage points higher than APRs for purchases.**
- **98% of cards charged a cash advance transaction fee averaging 4.31%. Fees ranged from 1–5%.**
- **97% of offers stated a minimum dollar amount for cash advance transaction fees. The average minimum was \$4.95. The highest minimum fee was \$20, found on three offers: two from Bank of America, and the Household Bank Gold MasterCard.**
- **81% of offers did not cap cash advance transaction fees. The 19 offers that did set a maximum cash advance transaction fees had an average maximum of \$21.07. Maximums ranged from \$10–25.**

The APR for cash advances is often higher than the APR for purchases, a fact that is usually buried in the fine print of a credit card offer. For example, Capital One’s Platinum Visa has an APR of 10.9% for purchases; the APR for cash advances, however, is 19.8%, nearly double the interest rate for purchases. To make matters worse, the APR for cash advances does not appear in the “Annual Percentage Rate” section of the disclosure chart; rather, it is often referenced by an asterisk that appears after the words “for purchases” in the chart, or it may appear next to the chart.

To add insult to injury, companies may use a different method to calculate interest on cash advances than the method used for purchases, a fact that frequently escapes consumers’ notice. Grace periods may also not apply to cash advances. As a result, interest may begin to accrue immediately on cash advances, even if it does not on purchases.

In addition to charging a higher interest rate on cash advances, credit card companies charge transaction fees for this service. For example, the Associates National Bank Student MasterCard charges 4% of the transaction, and has no maximum; also, the APR for cash advances is four percentage points higher than that for purchases. Thus, if a consumer carrying this card requests a cash advance of \$500, her card will be charged a transaction fee of \$20 in addition to the higher APR of 21.49%.

Many credit cards surveyed have minimum cash advance transaction fees. Thus, no matter how small the cash advance, the companies can guarantee themselves higher fees. For example, the AT&T Universal Platinum Card has a transaction fee of 3%, but a minimum of \$10. Thus, a cardholder who receives a \$50 cash advance will actually be charged a transaction fee of 20%.

BALANCE TRANSFER TRANSACTION FEES

- **The average APR for balance transfers was 6.62%. 48% of card offers surveyed gave applicants the option to transfer balances from other cards.**
- **The highest balance transfer APR was 19.80%, for the People’s Bank Premier Platinum; the lowest rate, 1.9%, was a promotional rate for the Citibank Platinum Select MasterCard.**
- **25% of offers charged an average transaction fee of 2.46% for balance transfers. Transaction fees ranged from 0–3%.**
- **21 offers stated a minimum transaction fee for balance transfers. Minimum fees ranged from \$2–10, with an average of \$4.22.**
- **84% of offers had no cap on balance transfer transaction fees. Sixteen offers stated an average maximum transaction fee for balance transfers of \$23.19. Maximums ranged from \$10–40.**

As with cash advances, transaction fees usually accompany balance transfers. Credit card companies may assess a fee as a percent of the transaction, with or without minimum and maximum amounts. In addition, balance transfers carry an APR, and this rate is often different than the APR for purchases. Interest on transferred balances may begin to accrue immediately, and low introductory APRs often do not apply to balance transfers.

In addition, the APR on transferred balances may vary depending on the amount a consumer transfers. For example, the AT&T Universal Platinum MasterCard advertises a 1.9% APR on transferred balances. However, the fine print of the offer states that this rate only applies if more than \$3500 is transferred at the time the account is opened. If a consumer transfers balances totaling \$3500 or less, a higher APR applies.

INTRODUCTORY OR PROMOTIONAL APR

- **57% of card offers surveyed advertised an average short-term introductory APR of 4.13%, ranging from 0–9.99%.**
- **Introductory APRs were an average of 73% lower than regular APRs.**
- **The average short-term introductory APR lasted for 6.8 months. Introductory period lengths ranged from 3–12 months.**
- **33 of the offers (58% of those advertising introductory APRs) had introductory period lengths of 6 months or less.**

Introductory APRs are usually much lower than regular rates. For this reason, and because an exceptionally low promotional APR may mask an exceptionally high actual APR, credit card companies advertise these APRs in prominent places on the envelope and offer. Frequently, the limiting terms of a low advertised APR are embedded deep in the text of the offer. For example, the front of a brochure for American Express's Optima Platinum card has a yellow text balloon advertising a 0% APR. This claim is neither qualified with the words "introductory", nor does an asterisk appear next to the rate to indicate that there may be qualifications. The fact that this APR is introductory does not become apparent until the consumer reads the text of the offer. Such marketing tactics are misleading and deceptive.

Introductory APRs last for only a short time (usually 6 months), a fact that is difficult to find in the text of the offer, if it is stated in the offer at all. It is even harder to find the much higher actual (that is, non-promotional) APR that will go into effect once the introductory term is over.

The touted introductory APR often carries many restrictions. Sometimes the introductory APR applies only to balance transfers and not to purchases. Other times the introductory APR applies only if a balance transfer is made. Rarely does the promotional APR apply to all of the services the card offers.

PENALTY APR

- **60% of cards surveyed charged a penalty APR on accounts in default or bad financial standing.**
- **The average penalty rate was 22.84%, about 52% higher than the average regular (non-penalty, non-introductory) APR of 15.04%.**
- **Penalty rates ranged from 13.99–36.25%.**

A penalty rate, which is intended to be punitive, is generally much higher than the regular APR. While the State PIRGs' survey found that the average penalty rate was eight percentage points

higher than the average regular APR, we also found 6 cards that had penalty rates twelve or more percentage points higher than regular rates. By contrast, a 1998 survey found that penalty rates were, on average, 4.5 percentage points higher than regular rates.²⁴

Credit card companies offer many reasons for raising a cardholder's APR to a penalty, or default, rate. Reasons vary among companies and include:

- the minimum payment is at least one day past due;
- any two consecutive payments are missed;
- the account balance is over the limit;
- payment is not honored by the cardholder's bank for any reason;
- there is an adverse change in the cardholder's financial condition (including job loss, demotion, or divorce);
- the cardholder is delinquent with another creditor;
- any two payments are late in any rolling 6-month period; and/or
- any one payment is past due for two billing cycles.

A 2000 survey found that 69% of credit cards issuers will raise a cardholder's interest rate as a result of at least one late payment, a 50% increase since 1998.²⁵

In addition to the assessment of a penalty APR on the account to which a late payment was made, one or more late payments usually result in a negative credit report item, raising interest rates even more for future credit. Particularly outrageous is when a credit card company raises a cardholder's APR if the cardholder is in "bad standing" with any other creditor. So, to raise their own fee income, banks check credit reports for minor delinquencies to other banks or card companies. For example, Citibank notified its cardholders in 1999 that it would increase a cardholder's interest rate to 23.9% "if payment is not received by us or any other creditor within 30 days of the due date."²⁶ This practice is especially concerning because the average cardholder today carries 4.2 credit cards.²⁷ Thus, if an average cardholder makes a single late payment to Company A, s/he may see increases in the APRs of the credit cards s/he has with Companies B, C, and D, even if Companies B, C, and D never once receive a late payment from this cardholder and even if the one late payment does not reflect a pattern of delinquency that indicates that the consumer presents a higher risk.

Punitive APR increases are another tactic by which credit card companies make it difficult for consumers to get out from under the high-cost credit card trap. On a \$2000 balance, an APR increase of twelve percentage points would cause a cardholder to pay nearly twice as much in interest than before.²⁸ Yet banks argue that it is consumers' irresponsible spending, rather than the banks' deceptive and unfair practices, that cause the "need" for bankruptcy law "reform".

The following bar graph shows the differences between the regular interest rate and penalty interest rate of five cards included in the survey. These five cards all had penalty rates that were at least 13 percentage points higher than the regular rate.

The Fleet Platinum MasterCard had the largest difference, of nearly 17 percentage points. A consumer carrying a balance of \$2000 on this card and making payments of \$60 per month would pay \$1167.89 more in interest and would take 20 months longer to pay if assessed the penalty rate of 24.90% instead of the regular rate of 7.99%. A consumer making only a relatively high minimum percentage payment of 3% of the outstanding balance would take even longer to pay. (See table below bar graph.)

Graph 1: Penalty APRs: One Late Payment Can Cost You

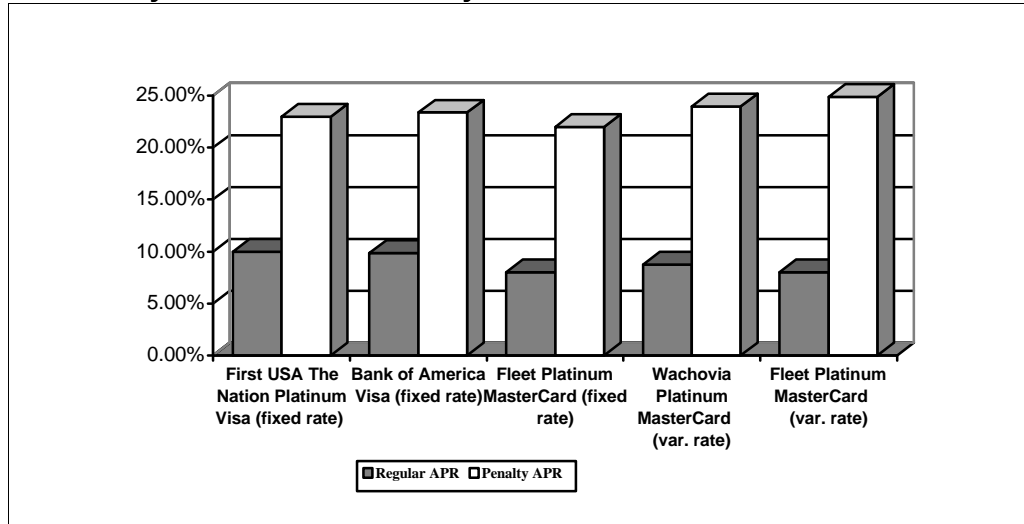


Table 1—Fleet Mastercard Penalty Rate Can Cost You
FLEET PLATINUM MASTERCARD (var. rate)* Starting Unpaid Balance = \$2000

	Regular 7.99% APR		Penalty Rate 24.90% APR For Paying Late*	
	Pay \$60 each month	Pay 3% of outstanding balance each month	Pay \$60 each month	Pay 3% of outstanding balance each month
Total Interest Paid	\$269.48	\$466.73	\$1437.37	\$3314.87
Time To Pay off Balance	38 Months	84 Months	58 months	169 Months

* Presumes consumer stays at penalty rate of 24.90%. Some cards allow consumer to be reinstated at regular rate following period of on-time payments.

GRACE PERIODS

- 99% of cards had grace periods of 25 days or less; the average length was 22.62 days.
- 31% of cards had grace periods of 20 days.
- Five cards—all from Providian—had no grace period.
- Only one card, the American Express Optima Gold (Delta Air Sky Miles), had a grace period of 30 days.

Over time, credit card companies have decreased their grace periods. Historically, grace periods were a full month (31 days); in recent years, however, grace periods have become as short as 20 days or less.²⁹ The grace period is the time after any new transactions are made during which interest does not accrue on those transactions. The due date of the minimum payment is generally the end of the grace period. Most credit card companies assess interest on a daily basis, beginning once the grace period has ended. Grace periods usually do not apply to cards on which balances are carried over from the previous billing cycle.

The length and terms of the grace period make a significant difference in how much consumers pay to use credit. Not all grace periods are alike, and consumers must read the fine print carefully. Some credit card companies offer no grace period at all, many offer a grace period only to cardholders who have paid their balances in full the previous month, and a few offer a grace period regardless of whether or not a cardholder pays his or her balance in full each month. These

conditions can generally be found in the disclosure chart. The disclosure chart is a boxed area, which usually appears on the back of an offer, containing the terms of the offer that must be disclosed under the Truth in Lending Act. (For more information on disclosure charts, see “How to Read a Credit Card Offer,” included in this report on page 31.)

In the disclosure chart for Household Bank’s Gold MasterCard, the section entitled “Grace Period for Purchases” states that the card has a grace period of “at least 20 days after the close of the previous billing cycle when you pay your balance in full.” This statement, while true, does not tell the consumer what happens if the previous month’s balance is not paid in full. A more accurate statement would include this information; for example, an offer might state, “If your balance from the previous month was not paid in full, the grace period described above does not apply, and interest, therefore, will begin to accrue immediately upon purchase.”

Even if a grace period does apply, many banks now backdate interest charges, meaning that once the grace period ends, the amount of interest assessed is calculated from the date of purchase rather than from the posting date. If a consumer carries a balance of \$2000 from month to month on a card with a 15.04% APR, and interest charges are backdated an average of five days each month, the consumer will pay nearly \$50 per year in extra interest.

ANNUAL FEES

- **15% of cards surveyed charged an average annual fee of \$31.76. Fees ranged from \$25–155.40.**

In order to make advertised cards sound more enticing, many credit card offers emphasize that the advertised cards don’t have annual fees. For example, a direct mail offer for the Travelers Group Platinum MasterCard states, “With so much purchasing power, you’d expect to pay a sizable annual fee. . . Our Platinum card offers you a high credit line, substantial savings in interest, and no annual fee!” Consumers should not be too impressed, however, as most cards do not carry annual fees: the State PIRGs’ survey found that 85% of cards surveyed do not have annual fees.

The decrease in the number of cards charging an annual fee has been more than offset by the increase in interest rates and existing fees, as well as by the invention of new fees. As a result, credit card offers sound more appealing than ever before, even though the actual cost of credit for consumers is higher than ever.

Findings: Student Credit Card Usage And On-Campus Marketing

- Two-thirds of college students have at least one credit card. The average college student has 1.67 credit cards.
- 85% of students with cards had their primary cards in their own names. Only 16% had co-signed primary cards. By comparison, 1998 survey by the State PIRGs, “The Campus Credit Card Trap,” found that 69% of students had obtained credit cards in their own names.³⁰
- 50% 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. In the PIRGs’ 1998 survey, 28% of students reported paying late at least once in the last two years.

- 58% reported seeing on-campus credit card marketing tables for a total of two or more days within the first two months of the semester. 25% 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.
- 73% reported receiving at least two credit card offers by mail within the last month, and more than a quarter reported receiving more than five offers by mail in the last month. 41% had received at least two credit card offers by phone in the last month.
- 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.
- Students reported that the most common credit education resource available to them on their campuses was pamphlets/booklets/other literature (85%). Also available were advisers (26%), campus intranet resources (17%), and classes/seminars (13%).

ADDITIONAL COSTLY CREDIT CARD COMPANY TACTICS

UNEXPECTED APR INCREASES: Reasons Not Disclosed in the Offer

Credit card companies may raise the APR on a customer's card for reasons other than the ones stated in the offer. For example:

- **Mergers.** Interest rates may increase as a result of corporate mergers or buyouts.³¹ One consumer, for example, held a Huntington Bank credit card for its low interest rate of 8.5%. When the card was sold to Direct Merchants Bank, the consumer's interest rate jumped to 17.4%.³²
- **"Fixed" Rates.** Surprisingly, so-called fixed rates can also be raised at any time, with as little as 15 days notice, even if the consumer hasn't committed any alleged infraction.

LOWERED MINIMUM PAYMENTS: Cost Consumers More

The minimum monthly payment is the portion of a cardholder's outstanding balance that s/he must pay in any one billing cycle in order to avoid penalty fees. In the past, most banks required a minimum monthly payment of 4%. In 1998, however, almost half of the banks surveyed by the non-profit group Consumer Action required a minimum monthly payment of 2%.³³

Low minimum payments may sound good—they allow consumers to buy expensive products and services while only paying a fraction of the cost up front. However, if a cardholder makes only the minimum payment on his or her balance each period, it will likely take years to pay off, even for a balance of only a few hundred dollars. Most importantly, paying only the minimum each period increases the amount of time it takes to pay off a balance and the amount of interest that must be paid. By lowering minimum monthly payments, credit card companies ensure that cardholders pay much more in interest over time. The next chart demonstrates the high cost of paying only the minimum.

Beginning Balance	APR	Monthly Payment	Total Interest Paid	Months To Pay (Years)
\$2000	15.04%	2% unpaid balance	\$2205.63	169 (14)
		5% unpaid balance	\$589.74	65 (5.5)
		10% unpaid balance	\$269.31	36 (3)
		\$40/month	\$1164.23	80 (6.7)
		\$100/month	\$316.99	24 (2)
		\$200/month	\$151.11	11 (1)

As the chart above shows, a cardholder who makes the 2% minimum payment each month on a \$2000 balance will pay \$1936.32 more in interest and will take 133 more months to pay off his or her balance than a cardholder who makes 10% payments each month. By paying only the 2% minimum, this cardholder will pay nearly twice the original balance! However, if this cardholder makes payments of just three percentage points more than the minimum each month (5% payments), s/he will save \$1616 in interest payments.

INACTIVITY FEES: Fee Charged for Good Credit Behavior

Some credit card companies are now penalizing good credit behavior with such fees as the “inactive user” fee. The definition of an inactive user varies: some companies assess inactivity fees on cardholders who do not use their cards at all within a specified time period, while other companies consider a cardholder inactive if he or she uses a card fewer than a specified number of times within a specified time period, or if the cardholder’s purchases total less than a specific dollar amount. For example, in 1998:

- Advanta charged a \$15 fee to its cardholders for every six-month period in which they did not use their cards;
- Chase Manhattan Bank raised the APR of its Gold Card holders by 2% if they carried a balance of less than \$2500;
- the GE Rewards card charged a \$25 annual fee to each of its cardholders who paid less than \$25 in interest each year; and
- Republic National Bank and Union Bank of California charged annual fees of \$18 and \$24 respectively to cardholders whose yearly purchases totaled less than \$3,000.³⁴

APPLICATION OF PAYMENTS: Consumers Pay More Interest

When a cardholder makes a payment of less than the full balance, the credit card company chooses where to apply the payment. Most companies will apply the cardholder’s payment to the balance carrying the lowest APR. Because the APR for cash advances is usually higher than the APR for purchases, if a cardholder has both made purchases and received cash advances, the credit card company will likely apply his or her payment to the purchase balance rather than the cash advance balance in order to maximize profits. Thus, cardholders who engage in multiple types of transactions and do not pay their balances in full may end up paying more in interest than they expect.

ARBITRATION CLAUSES: Consumers Lose Right to Sue

Many credit card offers bind the cardholder to arbitration. Arbitration is a legal process by which disputing parties settle the matter outside of a court of law, using a mediator rather than a judge or jury to come to a decision. Binding arbitration, which is a condition of most credit card agreements, contractually obligates both parties in a dispute to accept the decision of the mediator. Thus, by requiring consumers to agree to binding arbitration as a condition of issuing a credit card, credit card companies effectively deny consumers their right to have their days in court.

Arbitration clauses are buried in the fine print of credit card agreements. The organization Trial Lawyers for Public Justice found that not one person of 136 interviewed knew their cards had mandatory arbitration clauses.³⁵

By requiring that consumers agree to binding arbitration as a condition of carrying a credit card, credit card companies ensure that consumers will have a hard time winning disputes. Arbitrator lists are frequently drawn from lists of industry defenders, denying consumers the right to an unbiased

mediator. The rules governing arbitration are different and less favorable to consumers than rules governing court cases; for example, the statute of limitations for arbitration may be as short as 90 days, whereas consumers bringing a case in court have several years. Fewer remedies are available in arbitration; arbitrators cannot, for example, award punitive damages. Finally, mandatory arbitration eliminates the possibility of class-action suits being filed against a credit card company.

MANIPULATIVE MARKETING PRACTICES

In an effort to boost profits, credit card companies are using more aggressive and manipulative marketing schemes to lure consumers into the high cost credit card trap. Credit card offers often begin introductory letters by telling consumers that they are special. For example, Citibank tells consumers, “Your excellent credit has earned you the best card we’ve ever offered: the *new* AT&T Universal Platinum MasterCard.” Credit card offers also make consumers feel like they are part of an elite group of people. For example, American Express tells consumers, “As the membership criteria at American Express are becoming increasingly stringent, the Gold Card is becoming even more difficult to acquire. You, however, have demonstrated exceptional financial responsibility. For this reason, you have been selected for Approved Membership for the Gold Card.”

Such marketing tactics are used to flatter consumers and make them feel as if they can be part of a prestigious group of successful people who, because of their “good credit,” now have an opportunity to acquire additional credit (and to potentially ruin their good credit). The following are marketing tactics frequently used by credit card companies to entice and exploit consumers:

BAIT AND SWITCH

Credit card offers that arrive by mail frequently advertise high-grade (or prime risk) cards, such as Gold or Platinum, which generally have lower APRs and lower fees. Consumers, enticed by the idea of obtaining a high-grade card, often apply under the assumption that the advertised card is the only card they are applying for. However, most credit card companies reserve the right to send the consumer a lower-grade card with a higher APR and higher fees, a fact that consumers may miss as it is usually stated in fine print on the back of the offer.

For example, an insert included with an offer for an Aspire Diamond Visa card states,

If we determine at the time you respond to the offer that you no longer satisfy the credit eligibility requirements that we previously established and you previously met, we may . . . consider you for an alternative Aspire Classic [card].
--

Appearing below this paragraph is a box summarizing the alternative finance charge rates, which states that the alternative APR is 5.25 percentage points higher than the APR for the offered Diamond card.

Surprisingly, it is rare for an offer to disclose the finance charge rates for alternative cards. Most offers simply state that the company reserves the right to consider you for a lower-grade card without disclosing the terms of that card.

TIERED PRICING: Prevent Consumers from Comparison Shopping

A new anti-consumer practice is catching on quickly with credit card companies: tiered, or risk-based, pricing.³⁶ In offers, credit card companies who have adopted this practice will quote a

range of possible APRs rather than giving a firm quote to an applicant. A 2000 survey found that one-third of card issuers quote a range of APRs on card offers.³⁷ For example, Provident National Bank's Aria card has a meaninglessly wide range of 7.99%–20.24%, and the WalMart Card issued by Chase Manhattan Bank has a “non-preferred” APR that is nearly nine percentage points higher than the standard APR. Once the company receives an application, they assess the applicant's credit history and score before assigning an APR. Applicants with the best credit scores get the best rates, while applicants with lower credit scores get higher rates. Since few consumers know or have access to their credit scores, applicants don't know what APR they will get until they receive their cards. Consumers are thus denied the right to comparison shop and make educated decisions before applying for a credit card.

Additionally, when consumers don't know ahead of time what the APRs will be on cards they apply for, and then receive cards with unfavorable APRs, they have to cancel accounts that have already been established rather than being able to decide not to apply for the cards in the first place. Furthermore, one of the many factors that creditors look at when considering the credit-worthiness of a potential customer is the number of credit accounts that applicant currently has or has had in the past, resulting in a negative effect on consumers' credit ratings.

“FIXED” RATES: Not Fixed at All

The term “fixed rate” refers to a specific type of APR. As it is legally defined, a fixed rate is any rate that is not tied to an economic index such as the prime rate. Credit card companies can raise fixed rates as often as they like, with as little as fifteen days' notice to cardholders. Thus, the term “fixed rate” misleads consumers, who may assume that “fixed” means the rate will not change.

In advertising their cards, credit card companies play on consumers' lack of knowledge about the technical meaning of “fixed”. For example, the text of a direct mail offer for the Bank of America Platinum Visa states,

<p style="text-align: center;">Your fixed APR is only 9.9% (this rate does not expire) Unlike an 'introductory' rate, this one won't jump up after a few months. In fact, as long as your account is not in default, your fixed rate will remain at 9.9%. . . . Again—this 9.9% APR lasts for years . . .</p>
--

This fixed rate will remain fixed only if Bank of America decides not to raise it! It may last “for years,” or it may rise at any time with only 15 days notice to cardholders. Consumers receiving this offer may easily be misled.

“AS LOW AS” OR “UP TO”: Small but Significant Words

It is easy to overlook these words because they are usually written in smaller type than the attractive APR rates that accompany them. For example, an offer that states “APR as low as 2.9%” or “Credit Line up to \$50,000” means just that—the actual APR a consumer receives with his or her card will likely be much higher, and the credit line much lower. Consumers should be aware of these small but significant words.

As a result of these and similar deceptive practices, often only clarified in the small print or “mice type,” the Federal Reserve Board in September ordered banks to make offers clearer, with important disclosures in the same size type as the “come-on,” or teaser, disclosures. The Board also increased the number of disclosures that must be included within the table of fees in an

application generally known as the Schumer box: Credit card companies must comply with these rules by October 1, 2001.

“Under the final rule, disclosures must be in a readily-understandable form and readily noticeable to consumers. The APR for purchase transactions must be in 18-point type. Cash advance and balance transfer APRs must be included in the table. Balance transfer fees must be disclosed either in or outside of the table.”³⁸

“YOU CAN ALWAYS CARRY MORE THAN ONE CARD”: Convincing Consumers to Apply for More High-Cost Credit

Some companies include notes along with their offers announcing, for example, that, “You can always carry more than one MasterCard credit card. So do not delay in accepting your new Platinum Plus card. With it, you will enjoy a separate line of credit as well as superior benefits and services. Reply today-with no annual fee, it costs you nothing to respond.”

That it “costs you nothing to respond” is not entirely true. When the consumer applies for a card, the credit process begins and just the fact that the consumer has applied for a card shows up on his or her credit report as an “inquiry.” Even if a consumer doesn’t plan to use the entire credit limit on all of his or her cards, anyone—lenders, creditors, landlords, employers—who checks that consumer’s credit report will see how much potential debt s/he could have, and may not want to do business with that person. Consumers lose points off their credit scores for every inquiry on their credit reports.³⁹

“YOU’RE PRE-APPROVED!”: Approval Is *Not* Guaranteed

“Pre-approved” usually means that the consumer was selected to receive the application because s/he met some certain credit criteria. It does *not* mean that the consumer will definitely receive the advertised card, or any card at all. Consumers applying for “pre-approved” cards are still subject to review of their financial situation by the credit card company, and receipt of a card is contingent on a satisfactory review.

“URGENT!”: Deceptive Offer Appearances

Credit card companies realize that they have saturated the adult population with direct mail offers, and that as a result an increasing number of consumers are refusing to open the offers they receive. To counteract this trend, credit card companies are disguising direct-mail credit card offers to look like everything from IRS forms to rebate checks.

For example, one of the authors of this study received an offer from Capital One that arrived in an 8”x11” envelope made to look like a Federal Express or U.S. Postal Service mailer. The front stated “Express Priority” in large letters, with a picture of an eagle’s head. The back stated “Urgent” repeatedly across the flap, and boxes for “Time Sensitive,” “Materials Inspected,” and “Urgent” were marked. It even had a “Package Tracking Number” and bar code. Inside the envelope was a “Priority Notification” Gold MasterCard offer. This same author received another offer in an envelope marked “Important Documents Enclosed.” A box on the front of the envelope stated:

U.S. Mail: The enclosed documents are intended solely for the addressee listed and should be opened by the aforementioned only. Do not bend, fold, tear, or mutilate.

A return address was stated, but the sender was not. Inside the envelope was an offer for the Capital One Visa Platinum card.

MATERIAL INCENTIVES: Enticing Consumers to Incur Greater Debt

- **“Free” Money**
Some companies offer “free” money, in the form of cash rebates, or points redeemable for cash, gifts, or discounts for every dollar the consumer spends using the credit card. However, these incentives programs are not truly “free”: some carry a participation cost. Unless the cardholder makes frequent large purchases with his or her card, the rebates, gifts, and discounts may add up to less than the cardholder paid to join the program.
- **Donations**
Some credit card companies donate money to the consumer’s favorite charity or alma mater. Companies that donate money to non-profit organizations appeal to consumers by letting them know that they will be helping their favorite organizations with every purchase they make with these particular credit cards. Rarely, however, do these cards advertise just how much cardholders will actually be donating to their favorite organizations through the use of these cards. The actual contribution is usually very little. In fact, it is common for credit card companies to give the organizations they sponsor only 0.5% of all purchases—just 50 cents for every \$100 charged.⁴⁰ Most organizations sign a contract with the company issuing the card stating that the actual amount the company donates will not be disclosed, and, unfortunately, there is no law requiring the disclosure of this information.⁴¹
- **Trial Offers**
Some companies automatically sign up their cardholders for free trial offers. For example, Direct Merchants’ Bank signs up their cardholders for an extra product warranty called PurchaseShield. If a cardholder fails to cancel the service before the trial offer ends, his or her card is automatically charged for continuation of the service. Sadly, this practice is legal as long as the terms and conditions of the trial offer(s) are stated in the card application.

Cardholders agree (knowingly or not) to the terms of the trial offers when they sign the application. For example, the application for the Direct Merchants’ Bank card states, “I accept the Direct Merchants’ Bank MasterCard. . . and agree to the enclosed Terms and Conditions and acceptance of PurchaseShield benefits and the Terms and Conditions of the Cardmember Agreement, which will be sent to me when my account is opened.” Nowhere is it explicitly stated that consumers are automatically signed up for this service when they apply for the card and that their cards will be automatically charged if they don’t cancel the service before the 60-day free trial period ends.

An increasing number of credit card companies sign up their cardholders for free trial services, such as magazine subscriptions and credit protection. However, if the cardholder forgets to cancel the service before the trial period ends, his or her card will be automatically charged for continuation of the service. Although companies cannot sign up a cardholder for a trial service without his or her consent, companies often employ misleading or deceptive marketing practices to obtain consent. For example, a telephone representative may call a cardholder and tell her that she “will receive” a free magazine subscription, without ever asking the cardholder if she wants to take part in

the offer. If the cardholder doesn't explicitly say no and confirms her information when prompted by the representative, the credit card company will likely interpret her responses as consent.

- **Other Incentives**

A growing number of credit card companies offer incentives such as free or discounted airline tickets or long distance calling. These so-called deals usually come with expiration dates and significant restrictions.

USE OF SYMBOLS: Further Complicating Hard-to-Read Disclosures

Many offers include an asterisk (*) or other symbols (such as † or ^{1, 2, 3}) to refer consumers to further information relating to a particular phrase or concept on the credit card offer or agreement. When a consumer sees an asterisk or other symbol, s/he generally expects the corresponding information to appear at the bottom of the page. However, many symbols are often accompanied only by phrases such as "see reverse for details." On some offers, symbol-referenced information does not appear on the same page as the phrase with the symbol; rather, it appears on the back of the page or on another piece of paper altogether, usually in fine print. Consumers often miss important information because they must search for and sift through numerous amounts of symbol-referenced information scattered throughout the credit card agreement or offer.

For example, in the body of a direct mail offer letter for the People's Bank Visa card, the term "Pre-Approved" is followed by an asterisk. The corresponding information does not appear on the same page as the letter, but on the back of the offer. It is not set apart for easy location, but buried within numerous paragraphs of fine print under the heading "Conditions of Offer."

CREDIT CARD COMPANIES: ANTI-CONSUMER PRACTICES AND LEGAL ACTION

On September 30, 1998, Darrell and Elizabeth Essary combined both of their old First USA credit card accounts to a new First USA account because the company offered a low introductory APR of 3.9% on this new account. Their first monthly payment after this consolidation was due on October 19, 1998, according to the monthly statement. Darrell and Elizabeth mailed their payment nine days before the due date.

On their November statement, however, the Essarys discovered that First USA did not post this payment until October 25. Because their payment was posted after the due date, the Essarys were charged a late fee of \$20.00, and their introductory APR of 3.9% skyrocketed to 22.99%.

To avoid future late postings and fees, the Essarys decided to enroll in First USA's automatic payment program, which authorized First USA to take payments directly from their checking account each month. First USA, however, failed to process the paperwork necessary to enroll the Essarys in the program. On November 13, 1998—four days before their monthly payment was due—First USA informed the Essarys that their payment could not be made through the automatic payment program. As a result, the Essarys mailed their November payment on November

13. The payment was posted after the due date, and the Essarys were charged another late fee.

Following the November payment, First USA assured the Essarys that their monthly payments would be drawn automatically from their checking account beginning with the next statement. However, on their January 1999 statement, the Essarys discovered that First USA had charged them a late fee for their December 1998 payment. Despite the fact that the Essarys were enrolled in the automatic payment program, First USA posted their December payment a week late. The Essarys contacted First USA and explained that they should not be held responsible if the automatic payment program failed to draw the payment on time. First USA agreed drop the December late fee; however, the company did not lower the 22.99% penalty APR to the original introductory APR of 3.9%.

—From *Marsh v. First USA Bank*, Second Amended Complaint, US District Court for the Northern District of Texas, Dallas Division.

The deceptive and unfair marketing practices credit card companies use lure some consumers into debt. In 1998, the average debtor filing a Chapter 7 bankruptcy had an after-tax annual income of \$19,620, with \$17,544 in credit card debt.⁴²

Credit counseling services have traditionally been helpful for consumers who are in debt but wish to avoid bankruptcy. The average credit counseling client has about \$19,000 in unsecured (credit) debt, according to the Consumer Counseling Service of Greater Chicago. As credit card companies increase their profits, however, they have decreased their support for and participation in non-profit debt counseling and debt reduction plans. In particular:

1. Fewer and fewer credit card companies are reducing interest rates for consumers who have entered into debt management programs.

Consumers who face difficulty in paying back their debts may enroll in debt management programs, which were designed with the intent of facilitating debt repayment. Recently, however, banks have refused to lower interest rates for consumers in these programs; even worse, some banks are *raising* rates for enrollees. In fact, four of the ten largest credit card companies have raised interest rates for consumers in debt management programs. One of these four, MBNA, raised its rate from 10% to 15.9%, an increase of over 50%.⁴³ If a consumer has \$10,000 in debt, a rate increase this severe will cost the consumer an additional \$1,022 over three years. Thus, as debt management programs become less favorable, more consumers may be forced to declare bankruptcy.

2. Funding for Credit Counseling Has Been Reduced.

Credit card companies, which are the major source of funding for credit counseling agencies, are reducing by at least one third the amount they contribute to counseling agencies.⁴⁴ As a result, counseling agencies are raising costs for their indebted clients, putting help out of reach for those who need it.

Thankfully, government agencies and individual consumers are calling the companies' deceptive practices into question in courts of law. Several of the nation's largest credit card companies have been investigated by local, state, and federal agencies for anti-consumer business practices within the past two years.⁴⁵ First USA, Provident, Chase, MBNA, and Citibank have all recently settled lawsuits over unfair late fees, deceptive teaser rates, and misleading use of the term "fixed" rate, for amounts ranging from \$7.8–105 million.⁴⁶ Alleged practices include purposely posting monthly payments late in order to

increase cardholders' APRs and to gain more late fee income.⁴⁷ Providian was found to have charged its cardholders over \$20 million in undeserved penalties in this way,⁴⁸ and a private suit was filed against MBNA on November 16, 2000 alleging that the company charged late fees and extra interest to cardholders whose payments were not late, and that cardholders "have sustained economic damages" as a result.⁴⁹ In October 2000, the Office of the Comptroller of the Currency (the chief national bank regulator) and the San Francisco District Attorney, which had been investigating Providian for numerous deceptive and anti-consumer practices, announced a settlement with the company that included penalties and a minimum of \$300 million in restitution to consumers. In addition to assessing undeserved penalties on cardholders, Providian was accused by the government of deceptively advertising accounts as free of annual fees, even though a mandatory annual payment was masked as a monthly payment for a credit life insurance variant Providian called "freeze protection."

Incredibly, a Providian spokesman, Alan Elias, told Consumer Reports magazine, "The fine print is concise, clear, and easy to understand."⁵⁰ Conversely, here is what the U.S. Office of the Comptroller of the Currency (OCC), not generally noted for protecting consumers, said in its release announcing both civil penalties and restitution:

"In reaching the settlement, which culminates year-long investigations by two agencies [the OCC and the San Francisco District Attorney], the OCC concluded that the bank [Providian] engaged in a pattern of misconduct in which it misled and deceived consumers in order to increase profits. The OCC believes hundreds of thousands of consumers were harmed by Providian's activities, and that the bank profited as a result."⁵¹

Worse, a senior Providian official even tried to tell U.S. PIRG's Consumer Program Director that the \$150/year "freeze protection is a value proposition for some consumers." For once, U.S. PIRG and the OCC agree.

Increasingly, credit card banks have also come under fire for sharing confidential consumer information with telemarketers, which then use deceptive scripts to seduce consumers into placing trial orders. In a well-publicized case, Minnesota Attorney General Mike Hatch charged U.S. Bank with sharing customer information with the telemarketer Memberworks, which then called the consumers and asked them to accept a trial offer. Since the consumers didn't give out their credit card or checking account numbers, they didn't think they'd ordered anything, but it turned out the bank had given Memberworks their account numbers, resulting in the consumers being billed \$70-100 or more for generally over-priced add-on products such as credit card protection, credit life insurance, and roadside assistance. Minnesota (and other states) have now settled with both U.S. Bank, which paid a multi-million dollar penalty, and Memberworks. According to 1998 documents it filed with the Securities and Exchange Commission, Memberworks had or has contracts with at least 19 of the nation's 25 largest banks. Minnesota has now filed against Fleet Mortgage for similar practices.⁵²

How to Read a Credit Card Offer

Credit card companies and banks mail approximately three billion pre-approved credit card solicitations every year.⁵³ Credit card companies try to make these offers so enticing that consumers will want to open the envelope, read the material, and reply to the offer. But for many consumers, reading a credit card offer or agreement is like driving a car late at night, in an unfamiliar neighborhood, without a map. When it comes to credit card offers and agreements, the missing map and unfamiliar roads are replaced by constantly changing terms and conditions coupled with misleading advertising pitches. Here is a road map to the average direct-mail credit card offer:

Where To Find Disclosures About The Terms And Conditions Of A Credit Card Offer

Front

The front of a credit card offer is meant to entice the consumer who receives it to apply for the card. The offer nearly always takes the form of an introductory letter, which rarely contains the whole story. Consumers are forced to become detectives in order to discover the significant information that is omitted from the introductory letter. The front of most credit card offers includes:

1. the introductory or promotional APR;
2. the advertised credit line (usually prefaced by the language “credit line up to”);
3. advertisement of special offers and privileges that the card offers its cardholders; and
4. the date by which the offer must be returned.

In addition, the front of the offer will feature enticements such as “free gift” or “cash back,” as well as information to make the consumer feel good, such as “pre-approved” or “you’ve been selected from thousands to receive this offer.” Consumers should remember, however, that these are marketing gimmicks designed to encourage them to apply for the card.

Back

The back of the credit card offer contains the most important information, compiled into a disclosure chart. (Note: credit card companies will sometimes place the disclosure chart and related information on a separate insert instead of on the back of the offer.) The disclosure chart is required by law and must state:

1. the actual APR (that is, what the APR will be once the introductory period ends);
2. the formula for the APR, if the rate is variable;
3. the length of the grace period;
4. the amount of the annual fee, if any;
5. the minimum finance charge;
6. any transaction fees (for example, fees for cash advances);
7. the method of computing the purchase balance for each billing period;
8. late payment fees, and default or delinquency fees; and
9. over-the-limit fees.

The back of the offer also includes the conditional terms of the offer, which may have been referenced by symbols in the introductory letter. In addition, consumers will find different notices based upon state law on the back of the offer, usually below the disclosure chart. Finally, the back of the offer describes the terms and conditions of any insurance products offered.

TERMS TO UNDERSTAND

- **Annual Percentage Rate (APR)**

The APR is the annual interest rate that credit card companies assess on a cardholder’s monthly purchase balance. The amount of interest cardholders pay each billing period is determined by the APR, which is broken down into periodic increments. That is, if a cardholder has an APR of

12% and is billed monthly, s/he pays a monthly interest rate of 1%. There are two types of APRs: variable rate and fixed rate.

A **variable rate** is usually based upon the Prime Rate, which is an interest rate determined by the United States Government. *The Wall Street Journal* publishes this rate on the third Tuesdays of March, June, September, and December. Credit card companies that use variable APRs take the Prime Rate, often referred to as the “prime” or the “index”, and add an additional percentage. This additional percentage is determined by each company, and is referred to as the “margin” or “spread”. Alternatively, companies may base variable rates on the London Interbank Offered Rate (“LIBOR”), which is also published in *The Wall Street Journal*.

Consumers should remember: (1) that the rate will change on a quarterly basis as the economic index changes, and (2) that the rate current at the time of the offer may have changed by the time the account is opened.

A **fixed rate**, by contrast, is not based on any fluctuating market index. If a credit card company chooses to use a fixed rate, this will be stated in the body of the introductory letter. A fixed rate can change at any time, even mid-cycle, as long as a credit card company gives its cardholders fifteen days notice.⁵⁴

Consumers need to remember that “fixed” does not mean the rate will remain the same until the card expires. In addition, a card that offers a fixed introductory APR may not have a fixed non-introductory rate.

Different transactions carry different APRs. For example, cash advances generally have higher APRs than balance transfers and purchases. These other APRs can be found above or below the disclosure chart, and they are usually highlighted by a symbol or footnote number.

If an APR is described as “introductory,” consumers should look through the offer to determine the length of the introductory period, and what the APR will be once the introductory period is over; this information can be found in the disclosure chart. Upon closer inspection, consumers may discover that advertised low rates only apply to balance transfers. And the consumer must keep in mind that if s/he defaults on one or more payments or exceeds the card’s credit limit, most companies will raise the low introductory APR to a higher, punitive rate, regardless of whether or not the introductory period has ended.

Consumers should remember: (1) if an account does not remain in good standing during the introductory period, most credit card companies will curtail the introductory period and impose a higher APR, and (2) an introductory rate most likely does not apply to all transactions.

The cost of credit can vary significantly depending on a card’s APR. Using the lowest, average, and highest non-introductory APR rates found in the State PIRGs’ survey, the following chart shows the effect APR has on the cost of credit if minimum payments of 3% are made every month until the balance is paid off:

Table 3: HOW APR AFFECTS THE COST OF CREDIT				
Starting Unpaid Balance	APR:	Total Paid:	Total Interest Paid:	Length of Time to Pay:
\$2000	7.99%	\$2269.48	\$269.48	38 months
	15.04%	\$2605.82	\$605.82	44 months
	30.25%	\$4420.61	\$2420.61	74 months

As the chart shows, a cardholder with an APR of 30.25% (the highest APR found in the State PIRGs' survey) will pay more in interest than s/he spent on purchases! This cardholder will also pay nearly ten times as much interest as a cardholder with the lowest APR. Thus, APR has a significant influence on the cost of credit.

Consumers should look for cards that have APRs near or below 15.04% (the average in the State PIRG's survey). If a card offers a variable rate, the margin should be less than 8.5 percentage points. Default APRs (if unavoidable) should be less than 20%, or if variable, a margin of less than 15.5 percentage points. Consumers should also look for cards that apply default rates only for a limited amount of time and that require more than three payments to be late before an account is labeled "in default." The actual APR for which a consumer qualifies will vary based on that consumer's credit history; thus, it is important to compare multiple credit card offers to ensure that the APR of any particular offer is the best deal.

- **Credit Limit**

The credit limit (or line) is the maximum cumulative amount of money the consumer is allowed to borrow from the credit card company. The amount of available credit is equivalent to the limit minus the total charges. Thus, if a cardholder has a \$5000 limit and makes \$5000 in purchases, s/he will not be able to make any more purchases with that card until a portion of the balance is paid off. Once the cardholder pays off, for example, \$200, then s/he will have an available credit line of \$200. The credit limit and the available line of credit appear on the periodic statement cardholders receive from their credit card companies.

Credit card offers usually advertise the highest possible credit limit that a consumer could receive; however, the actual limit is not determined until the company reviews the applicant's credit report.

- **"Pre-Approved"**

The term "pre-approved" usually appears on the offer envelope and in the body of the introductory letter, and means that a consumer is approved to apply for the credit card because he or she met some initial credit or income criteria. Every applicant for a credit card is still subject to a credit check, regardless of whether or not the application said "pre-approved". By signing the offer, a consumer authorizes the credit card company to review his or her credit report, upon which actual approval for the card is contingent.

The appearance of the term "pre-approved" on a credit card offer does *not* mean that a consumer will automatically receive a card by accepting the offer. If an applicant's financial situation has changed since the offering company first screened him or her for the offer, or if the company

finds, upon closer screening, that the applicant doesn't qualify for the credit line, s/he may receive a lower-grade card, or no card at all.⁵⁵

- **Annual Fee**

Some credit card companies charge consumers an annual fee for the privilege of using a credit card. Annual fees do not replace other fees, such as late fees or cash advance fees. If a credit card has an annual fee, this will be stated in the disclosure chart. Most credit cards that have annual fees are affinity cards, which give some kind of perquisite to cardholders (such as those that earn airline miles).

Because so few non-affinity cards today have annual fees, the State PIRGs recommend that consumers look for a card with no annual fee. If a consumer is considering an affinity card with an annual fee, s/he should determine whether the benefits offered outweigh the cost of the annual fee.

- **Grace Period**

A grace period is the time during which a purchase made with a credit card does not accrue interest. Some credit card companies do not have grace periods at all. Thus, cardholders are charged interest from the moment of purchase, or as of the time the charge is posted. Most companies, however, have grace periods of 20–25 days. Grace periods usually apply only to new purchases, not outstanding balances. In addition, grace periods may not apply to certain transactions, such as cash advances.

Consumers should look for cards with grace periods of at least 25 days. (Two-thirds of the cards in the State PIRGs' survey had grace periods of at least 25 days.) Consumers must remember that the length of the grace period determines when interest will begin to accrue. If a card has no grace period, interest will begin to accrue immediately.

- **Late Payment Fee**

By paying a late fee, a consumer is not protected from additional repercussions. As mentioned previously, a late payment may cause a cardholder's APR to rise; multiple late payments may affect a consumer's credit rating and standing with other credit companies.

Consumers should look for cards with late payment fees of \$20 or less. However, these are becoming rarer because the current industry trend is to increase late payment fees. Consumers should examine an offer carefully to ensure that a low late payment fee is not masking other unfavorable terms and conditions.

- **Methods of Computing Purchase Balances**

The method a card issuer uses to compute purchase balances significantly affects how much consumers pay to use credit. Some credit card companies include a consumer's current purchases (that is, those purchases made within the current billing period) when figuring out the amount of interest to be paid, while other companies exclude those purchases.

While the method for computing the average daily balance can be found in the disclosure chart, the particular consequences of the chosen method of computation are not explained in the offer.

A good explanation of the different methods used to calculate balance can be found at www.creditalk.com. A simplified summary of the three most common methods follows:

- 1. Average Daily Balance.** This is the most common computation method. The outstanding balances for each day in the billing cycle are added, and this total is divided by the number of days in the billing cycle. New purchases may or may not be added, depending on the terms of the card. If the terms state that new purchases are included, purchases made during the billing cycle will raise a cardholder's balance and may increase the finance charge.
- 2. Adjusted Balance.** Payments or credits that are received during the current billing period are subtracted from the balance at the beginning of the billing cycle. New purchases are not included in the calculations. For example, if a cardholder's beginning balance was \$2000, and s/he made a payment of \$500 during the billing period, s/he would only be charged interest on the remaining \$1500. This is generally the most consumer-friendly computation method.
- 3. Two-Cycle Balance.** To obtain this balance, credit card companies add together the average daily balances for the current and the previous billing cycles. The average daily balances for the current billing period may or may not include new purchases. The two-cycle balance method is the least consumer-friendly method of balance computation.

- **Transaction Fee**

A substantial portion of the growth in credit card companies' profits can be attributed to transaction fees. Credit card companies now charge cardholders fees for various types of transactions, including cash advances, balance transfers, and quasi-cash transactions (see below).

- **Cash Advances**

Cash advances are immediate cash loans from a credit card company. Fees for cash advances vary, but typically run from 3% to 4% of the transaction and include a minimum fee, and may or may not include a cap, or maximum fee. Information about cash advances is usually contained within or just outside of the disclosure chart. In addition to any transaction fees, cash advances may carry an APR higher than for purchases, and grace periods may not apply.

Information about cash advances is not required to be included in the disclosure chart. It is often found below or next to the disclosure chart, sometimes in a section headed "More Rate and Fee Information."

Consumers should look for transaction fees of 2% or less with no minimum charge and a cap on the maximum charge. In addition, consumers should look for cards that have the same (or lower) APR and grace period for cash advances as for purchases.
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- **Balance Transfers**

Balance transfers allow cardholders to transfer the balance on one credit card to another. Most consumers transfer balances to take advantage of a lower APR. It is important, however, to make sure that the transfer cost is calculated into all transfer transactions. Balance transfers typically cost about 3% of the transaction, but fees can be as low as 1%. As with cash advances, balance transfer APRs may differ from purchase APRs, and balance transfers usually

incur transaction fees; this information can be found in the “Terms and Conditions” section of the offer. In addition, credit card companies that offer balance transfers may allow only a small window of time in which the transfer must be requested.

Most credit card companies will only transfer balances that together total no more than the new card’s credit line. Once a balance is transferred to another credit card company, the consumer loses the right to dispute with vendors any charges that have been transferred.

Balance transfers sometimes require four to six weeks to complete. The cardholder continues to pay the former credit card company, both on the balance and any interest that has accrued, until the balance has been paid in full by the company to which the balance has been transferred. After a balance transfer, cardholders must notify their former credit card company if they intend to cancel the card; otherwise, they may be charged inactive user fees. The new credit card company does not close the old account for the cardholder, even if the remaining balance is fully transferred. Therefore, consumers should continue to make payments to the old credit card company on all transferred accounts until they are sure that the transfers have been completed.

Consumers should look for transaction fees of 2% or less with no minimum fee and a cap on the maximum fee. In addition, consumers should look for cards that have the same (or lower) APR and grace period for balance transfers as for purchases.

- **Quasi-Cash Transactions**

Quasi-cash transactions, also called cash equivalents, are defined as transactions that are similar to cash. The purchase of lottery tickets, wire transfers, casino betting chips, travelers checks, and money orders, as well as off-track betting, are all categorized as quasi-cash transactions. The fee for these transactions is usually a percentage of the transaction and may or may not include a cap. In addition, the APR for quasi-cash transactions may be higher than the APR for purchases, and quasi-cash transactions may have a shorter grace period, or no grace period at all.

As with cash advances and balance transfers, consumers should look for cards that have transaction fees of 2% or less for quasi-cash transactions, no minimum fee and a cap on the maximum, and grace periods and APRs similar to those for purchases.

- **Credit Card Insurance/Credit Protection/Credit Life Insurance**

Most credit card companies (67% of cards in the State PIRGs’ survey) offer **credit insurance**, which may be called a “payment protection plan.” This insurance covers the cardholder’s balance if there is death, disability, or the cardholder becomes involuntarily unemployed.

Credit card companies promote “payment protection plans” as a way for cardholders to protect their credit ratings. Coverage, however, is limited and expensive. The cost of coverage is usually a flat rate per \$100 of balance. For example, in Indiana, the insurance is \$0.60 for every \$100. Thus, if there is a \$200 balance, the insurance costs \$1.20, and if there is a \$5,000 balance, the insurance costs \$30. The rate varies from state to state. The cost of coverage in Louisiana is nearly four times the cost of coverage in New York.⁵⁶ The cost of insurance is automatically deducted from the cardholder’s account if s/he agrees to coverage. Credit insurance is profitable for credit card companies, accounting for up to 40% of their income from fees.⁵⁷

Credit insurance pays less per dollar on each claim than most other types of insurance. In addition, consumers who enroll in credit protection plans pay interest on the cost of their insurance because the cost of the insurance is included in the total amount owed. For these reasons, the Consumer Federation of America has called credit insurance “the nation’s worst insurance rip-off.”

Debt suspension, sold in the same way as credit insurance, freezes an enrollee’s debts upon illness or unemployment until the enrollee is able to pay or the deferral period ends. Because they are not insurance plans, debt suspension plans are not bound by cost and marketing restrictions. One consumer paid \$149 per year for a debt suspension plan on a Provident card with a \$500 limit.⁵⁸ Rarely, if ever, will a consumer benefit from a debt suspension plan. Credit card companies, however, will continue to benefit financially from these plans until pro-consumer curbs are enacted.

Unfortunately, it is common for credit card applicants to unintentionally sign up for credit card insurance. While credit insurance is optional under the Truth in Lending Act, credit card offers often make enrollment seem mandatory.⁵⁹ Similar language is used for both the card agreement and the insurance agreement, and the two agreements are often placed next to each other. Consumers applying for credit cards should always read carefully the text preceding all signature lines on the application

The State PIRGs recommend that consumers avoid credit protection/insurance or debt suspension, which most consumer groups agree are rip-offs. In addition, consumers should keep in mind that many people need not pay their debts once they are deceased!

- **Secured Credit Card**

Some credit card companies offer “secured” credit cards to consumers with bad credit ratings. A secured credit card is linked to a bank account held by the cardholder. The cardholder makes a deposit into this account, and the credit line of the card is equivalent to, or sometimes slightly higher than, the amount of the deposit.

Consumers usually earn interest on the amount of money they deposit into a secured card account. Based on this fact, some companies entice consumers by telling them that they are making an investment. These accounts, however, have low interest rates, and the amount a consumer earns in interest is significantly reduced or eliminated by fees associated with the card.

The State PIRGs urge consumers considering a secured credit card to check the terms of the offer closely—some secured credit cards from reputable financial institutions can help consumers improve bad credit ratings, while other cards may be rip-offs.

RECOMMENDATIONS

CONSUMER TIPS

As credit card companies continue to use deceptive marketing practices and lobby for anti-consumer national bankruptcy “reform,” consumers must be vigilant in order to avoid high-cost debt and excessive fees. If, after obtaining a card, the credit card company imposes new terms that a

cardholder doesn't agree with or finds unfavorable, s/he should cancel the card immediately to avoid being bound by these terms.

PIRG CREDIT CARD CONSUMER CHECKLIST

- ✓ Read disclosure charts carefully and thoroughly
- ✓ Carry only one or two major credit cards
- ✓ Pay by cash, check, or debit card when feasible
- ✓ Avoid using the full available credit line
- ✓ Pay off all balances in full every billing period, or pay as large a portion of the remaining balance as possible, making the largest payments toward the card with the highest interest rate
- ✓ Seek credit counseling as soon as financial problems arise

Look for a card with:

- ✓ a regular (non-introductory) APR near or below 15.04%;
- ✓ a grace period of at least 25 days;
- ✓ late payment fees no higher than \$20;
- ✓ no penalty APR for late payments or relationships with other creditors, or if unavoidable, a penalty rate no higher than 20% and applicable only for a specified period of time;
- ✓ and no annual fee.

The State PIRGs also offer the following recommendations that consumers should keep in mind when applying for or carrying a credit card:

- **Privacy**

To avoid receiving direct mail credit card solicitations, take advantage of the right to opt out by calling 1-888-5-OPTOUT, which will block a consumer's credit file from being pre-screened for "pre-approved" offers at the three major credit bureaus (Experian, TransUnion, and Equifax). To prevent your credit card company (or bank or other financial institution) from sharing information with telemarketers, take advantage of your new (limited) right to opt-out of the sharing of your confidential financial information with telemarketers and other "unaffiliated third parties"⁶⁰ at the Privacyrights.org website. For more information on how to opt-out of other types of marketing offers and solicitations, see the website Junkbusters.Com.

- **Complaints**

The State PIRGs urge consumers to file complaints with their state Attorney General and the national Office of the Comptroller of the Currency (www.occ.treas.gov or 713-336-4301) if they believe they are the victims of unfair bank marketing, late fee penalties, or interest rate charges.

Check for Credit Report Errors

Consumers should check their credit reports at least once a year for errors. Errors are common—a 1998 PIRG survey found that 70% of credit reports contained errors of some kind—and may cause creditors to deny credit or issue it at high interest rates.⁶¹ Correct any errors immediately. Consumers in CO, GA, MA, MD, NJ, and VT are entitled to one free report per bureau per year; consumers in other states may have to pay up to \$8 per report.

Table 4: To Obtain Credit Reports:

Equifax 1-800-685-1111 Experian 1-888-397-3742 TransUnion 1-800-888-4213
Consumers in CO, GA, MA, MD, NJ, and VT are entitled to one free report per bureau per year. [Consumers in other states may have to pay up to \$8.50 per report unless they have recently been denied credit, or are unemployed, or may be a victim of identity theft.]

Recommendations For College Administrators

College administrators are starting to show concern about credit card marketing on campus and rising levels of student credit card debt. Recently, at least one college, Indiana University, has made a seminar on credit card debt part of orientation for new students and parents. “This is a terrible thing,” said administrator John Simpson. “We lose more students to credit card debt than academic failure.”⁶² The State PIRGs have the following recommendations for colleges:

- **Prohibit high-pressure marketing tactics:** Colleges should curtail the practice of allowing credit card companies to pay student groups a fee based on the number of applications completed at on-campus tables, since this practice leads to overly-aggressive marketing by the companies. One student, who testified before Congress about her credit card debts, said she signed up for the credit card that got her in trouble because a friend told her that his fraternity was planning a party with the \$1 per application that the fraternity received from a credit card company. A preferable business practice would be for credit card companies to pay a flat fee to schools or student groups for the tabling privilege, rather than a fee based on the total number of applications filled out.
- **Restrict Free Gifts:** Colleges should prohibit credit card companies from offering free gifts to students for filling out applications, unless the student has first read a credit card education brochure prepared by the college or by a non-profit credit education organization.
- **Credit/Debt Education Materials:** Colleges should include credit card and debt education materials adjacent to credit card solicitations in campus centers and on tables and posters, etc. In addition, credit card and debt education materials should be included in bookstore shopping bags, preferably in place of the credit card applications that are generally found in these bags.
- **Limit Marketing:** Colleges should review and consider limiting the total number of credit card tables allowed on campus each quarter or semester.
- **Offer Credit/Debt Education Programs:** Credit card and debt education and counseling sessions should be made a regular part of campus programming. In particular, colleges should include in freshman orientation an independently prepared, mandatory information session regarding the responsible use of credit cards.

- **Offer Low Interest Loans and Credit Counseling:** Low-interest loans should be available to severely indebted students so that these students are not forced to drop out of school to work off their debts.

LAW AND POLICY RECOMMENDATIONS

- **Require Minimum Payment Disclosure**

The Truth in Lending Act (TILA) requires creditors to disclose information that consumers need to know before entering into a credit contract. For example, the disclosure chart found on all credit card offers is required by TILA.

The State PIRGs support an amendment to TILA that would require credit card companies to disclose to every cardholder the total amount of interest that a cardholder would pay over time on his or her outstanding balance, as well as how long it would take that cardholder to repay the outstanding balance if s/he makes only the minimum payment each billing period. As mentioned above, by lowering minimum payments, credit card companies increase profits and cardholders pay more and are in debt longer. An amendment would reveal the truth, and give consumers the information they need to make educated financial and budgetary decisions. A 1999 survey by the Opinion Research Corporation International found that 85% of the public supported this disclosure requirement.⁶³

- **Require Credit Card Companies to Raise Minimum Payments**

The industry standard for minimum payments used to be 5% of the balance. In recent years, however, the industry standard has declined to 2% to 3%. According to Stephen Brobeck of the Consumer Federation of America, this decline “is responsible for much of the rise in consumer bankruptcies [in] the past decade.”⁶⁴ Low minimum payments give cardholders with large balances a false sense of financial security, especially if credit card companies do not disclose the time and cost of paying only the minimum each period. As a result, consumers may not realize how deeply in debt they are until bankruptcy is the only option. Therefore, the State PIRGs support any legislation that requires credit card companies to raise minimum payment standards.

- **Defeat Anti-Consumer Bankruptcy “Reform”**

In order to reduce their own debt losses and increase profits, the credit card industry is spending millions—more than \$6 million in the first half of 2000—to pass further bankruptcy restrictions and to defeat pro-consumer amendments to their wish-list bankruptcy legislation.⁶⁵ The bill now in conference committee in the U.S. Congress includes no significant provisions reining in unfair credit card practices. In 1999, for example, the Senate-passed bill at least included an amendment to require the disclosure of minimum payment facts (as discussed above). Making this information available would lead to less over-priced credit card debt and fewer personal bankruptcies, but reduce credit card profits.

The onerous bankruptcy bill being pushed by the credit card industry would also make it more difficult for consumers to obtain a fresh start in bankruptcy and would increase the amount of debt for which consumers will be liable after declaring bankruptcy. Economic experts have pointed out that by making it more difficult for cardholders to default through bankruptcy, these industry-sponsored, anti-consumer bankruptcy restrictions will encourage credit card companies to be more predatory in lending, because the risk of issuing cards to higher-risk consumers such as students and those with low incomes will decline.⁶⁶ The State PIRGs oppose the industry-supported bankruptcy bills and amendments that seek to punish, rather than assist, consumers in

debt. No evidence exists that average consumers are abusing the bankruptcy laws; yet, plenty of evidence of credit card company malfeasance is available.

- **Enact Curbs on Deceptive Credit Card Marketing and Irresponsible Lending**
The State PIRGs particularly oppose any legislation that reduces consumer bankruptcy protection without simultaneously imposing restrictions on deceptive credit card marketing practices and irresponsible lending. Credit card companies routinely blame consumers' irresponsible spending for the high number of personal bankruptcies, and refuse to acknowledge their own share of the blame. In a 1998 report by the Consumer Federation of America, Stephen Brobeck called banks "hypocritical" for seeking bankruptcy restrictions "when their irresponsible marketing and extension of credit card debt has been an important cause of rising personal bankruptcies."⁶⁷

The State PIRGs support a requirement that offered credit lines be reasonable in relation to the actual income of the consumer receiving the offer. Credit card companies encourage debt by extending high credit limits to students and lower-income consumers, who do not have sufficient income to pay high balances. In particular, when marketing to students, credit card companies often offer a credit line based on the student's earning potential rather than on his or her current actual income. As a result, students are misled by the idea that they will "get a good job" after graduation and therefore do not need to worry about paying off their mounting debts. Such misconceptions lead consumers to debt and credit card companies to higher profits.

- **Additional Policy Recommendations**
 1. Require disclosure charts to include the fees and interest rates for cash advances and balance transfers, as well as any other penalties that credit card companies may impose, such as penalty APRs.
 2. Require that the disclosure chart appear prominently on the offer, and that it be in a font size at least as large as the font size of the body of the offer.
 3. Require that introductory rates quoted in an offer be followed by the actual (post-introductory) rate.
 4. Prohibit blanket disclosures such as "except where prohibited by state law" or "as allowed under state law." All disclosures should be state-specific.
 5. Require clear and unequivocal alerts to consumers if an alternate card with different terms and conditions may be or has been sent.
 6. Require offers to include a postcard that consumers may mail to the company to remove their names from all credit card mailing lists.
 7. Require that an independent body publish a semi-annual report comparing credit card terms and conditions, and giving averages for all fees and rates. This report should be made available to the public on the Internet, and all credit card offers must include the address of this website.
 8. Require credit card companies to pay for all educational material, but the materials must be prepared by a body not affiliated with the industry, such as a college or a consumer advocacy group.
 9. Prohibit the marketing of credit and debit cards to minors.

SURVEY METHODOLOGIES

Data from 100 credit card offers, reviewed in the summer of 2000, appear in Appendix A. The majority were direct mail offers; a few were brochures obtained at retail establishments and on college campuses. When the offer stated a numerical range, the highest number in the range appears on the chart, with the

exception of grace periods, for which the lowest number in the given range was used. Results from the survey appear in Appendix C. Rate information and fees for quasi-cash transactions are not included in the chart.

- **APRs**
The APRs that appear on the chart are the APRs stated in the disclosure charts of the offers. If the offer stated a variable APR, the APR current at the time of the offer appears in the chart.
- **Advertised Introductory APRs**
The rate appearing in the chart is the rate that was most heavily advertised and appeared most often in the body of the offer. The introductory rate included in the chart may be for purchases only, for balance transfers only, or for both purchases and balance transfers (as stated in the offer).
- **Grace Periods**
The grace periods that appear in the chart only apply if the previous statement's balance was paid in full and on time.
- **Balance Transfer APRs**
If a promotional APR applies to balance transfers, that rate appears in the chart. If not, the regular rate for balance transfers appears.
- **Cash Advance APRs**
If a promotional APR applies to cash advances (most do not), the promotional rate appears in the chart.

CAMPUS CREDIT CARD USAGE AND MARKETING SURVEY

In October and November of 2000 and February of 2001, 460 credit card surveys were completed by current college students at 40 campuses across the United States. The results of the survey appear in Appendix B.

ADDITIONAL RESOURCES

- The State PIRGs' new credit card education website, www.truthaboutcredit.org, has consumer recommendations, advice for students, a balance payment calculator, links to other on-line resources, and more.
- www.creditalk.com has understandable information on credit card terms and conditions, as well as other useful consumer resources.
- Surviving Debt: A Guide for Consumers, published by the National Consumer Law Center, has a chapter on "What You Need to Know About Your Credit Rating" and offers helpful advice debt management. To order directly from NCLC, call (617) 523-8089, or write to them at 18 Tremont St. Suite 400, Boston, MA, 02108.
- MyVesta.org is a non-profit, Internet-based debt counseling service. Assistance is available at www.myvesta.org or by calling 1-800-680-DEBT.
- The 2001 Consumer Action Handbook, published by the U.S. Government, has information on personal finance and credit use, as well as numerous other consumer topics. It also has an extensive index of corporate contacts and consumer protection offices organized by state, and it provides information on how consumers can remove themselves from mail and telephone marketing lists. It is available for free by writing to: Handbook, Federal Consumer Information Center, Pueblo, CO, 81009; by calling 1-800-688-9889 or online at www.pueblo.gsa.gov.

Endnotes

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- ²⁸ 1999 Credit Card Survey, Consumer Action.
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- ⁶⁰ Consumers should be receiving "Privacy Policy Disclosures from all financial institutions where they have an account, over the next few months. If you opt-out, you can slow the number of marketing pitches your bank makes through third parties. See new fact sheets from the Privacy Rights Clearinghouse on the Financial Services Modernization Act <<http://www.privacyrights.org/fs/fs24-finpriv.htm>> and its limited opt-out rights: <<http://www.privacyrights.org/fs/fs24a-optout.htm>> For more information about how to protect your privacy, see the Junkbusters.Com website.
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