Statement of Linda Sherry, Director of National Priorities, Consumer Action

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Hello, my name is Linda Sherry, Director of National Priorities at Consumer Action. Consumer Action is a national non-profit consumer education and advocacy organization headquartered in San Francisco with offices in Los Angeles and Washington, DC. Our web site address is CONSUMER [DASH] ACTION [DOT] ORG.

Today, I want to outline the impact that predatory practices can have on low- to moderate-income communities and how changing terms on revolving credit accounts weaken the fabric of America's consumer economy. The interest-rate games that issuers play unfairly grab money out of consumers' pockets—income that could be saved, invested or spent on necessities.

It is not just the declining economy and mortgage crisis that are affecting the ability of credit cardholders to pay off their bills. Credit card issuers have caused a good deal of this economic distress all by themselves through reckless lending – especially to financially vulnerable consumers.

Some lenders have shown little empathy for families who end up coping with balances that shoot up overnight, interest rates and minimum payments that double, and large penalty fees. Unexpectedly doubling or tripling a cardholder's interest rate can seriously destabilize a family's finances, as the family suddenly must make substantially higher minimum payments. Sharp increases in interest rates on existing balances can push a family that is getting by into default and possibly even bankruptcy.

Consider some of these common credit card practices:

- **Penalty interest rates of up to 32%.** These extraordinarily high interest rates are applied to the entire balance, after a consumer's payment is even one day late, or worse, because of account status with other lenders. The defense by the industry is that consumers bring these rates on themselves by mismanaging their accounts.

- **Late fees as high as $39.** In a 2006 study, the GAO found that the six largest credit card issuers had charged <u>35 percent</u> of their cardholders late fees. If a cardholder misses a minimum payment by even one day, these fees are applied in the next billing cycle. Some issuers have a cut-off time <u>on</u> the due date that allows them to charge fees for on-time payments. Due dates that fall on Sundays or holidays have become a very common occurrence requiring consumers to get their payments in before the due date or risk a late fee.

- **Over limit fees of up to $39.** Contrary to what many people believe, a purchase that takes you over your credit limit will not necessarily be denied. Instead, you'll be stuck with an over limit fee, which can be assessed every month until your balance is under the limit. Approving over-limit purchases adds a hidden line of credit the consumer has no control over. We believe such penalty fees should be permissible only if they bear a legitimate relationship to the costs of the violation, not if their sole purpose is to provide a windfall to one party.

- **Retroactive interest rates.** The credit card industry is the only business in which the cost of the transaction can be increased after the transaction has been completed. Higher interest rates are not limited only to subsequent (future) purchases and charges but are figured <u>on the existing balance</u>. This can cause the minimum payment to double or even triple, depending on the cardholder's balance.

- **Unilateral changes in terms.** Fundamentally unfair "change of terms provisions" hide in the fine print of solicitations and cardholder agreements. This legal boilerplate gives issuers the right to change APRs and other key terms at will—<u>at any time, for any reason.</u>

- **No advance notice of penalties.** When you're turned down for credit, the law requires that you receive a letter explaining why. But if you are hit with a penalty rate hike or other punitive adverse change in terms on your credit card, you don't have to be told until your next statement.

Peter and Jodie: Victims of unfair credit card practices

Peter* is a small businessperson who got his first credit card years ago. The card company gave Peter automatic increases in his credit limit until his line of credit reached $25,000. Now he is paying $725 in interest on the card each month. After Peter made several late payments, the company increased his APR to 38.66%. When Peter complained, the issuer said his interest rate could not be reduced and suggested Peter join a debt management program. Peter, who runs his small business using a gold charge card, fears that if he joins a debt management program he will lose access to credit for his business. Peter feels helpless that his debt "has gotten out of control" and he is considering bankruptcy.

This story illustrates how automatic credit line increases (that they didn't ask for) are used to reel cardholders into more and more debt, making them vulnerable to bankruptcy when unreasonably high penalty interest rates are applied indefinitely, with no reduction in rates in sight.

Jodie* and her spouse are a young couple who had good credit, but found themselves facing financial hardship when Jodie had pregnancy complications and had to be hospitalized several times. The couple was able to pay off and settle many of their debts, but missed payments on their credit card resulted in a 33% APR. While upset by the added costs, Jodie was told the rate would be reduced after six months of on-time payments. During that time, the couple paid on time and reduced their balance by 40%, but Jodie was told that the policy had changed, and rate reductions would not be considered until after 12 months of on-time payments.

This illustrates how a responsible young family's finances continue to be unfairly impacted by changes in terms and policies on their credit card, just when they are struggling to put a medical catastrophe behind them.

** Names changed to protect privacy. These are real stories submitted to Consumer Action in late 2008 and early 2009.*

Since 1999 the marketing and extension of credit by card issuers has increased about twice as fast as consumers have taken on debt. These means that aggressive marketing and lending by creditors, not insatiable consumer demand, has been the driving factor in pushing credit card debt.

Hitting cardholders with costly and unjustified interest rates and fees can destabilize a family's finances quickly and trap them in an un-ending cycle of costly debt.

These tricks and traps have always been unfair, but in times of economic difficulty they produce devastating financial repercussions. Working families are hardest hit as they pay more of their incomes for credit card interest and fees.

Unemployed persons, who may rely on established credit to pay for living expenses, are particularly vulnerable to interest rate hikes and other unilateral account changes, such as the unreasonably deep cuts in credit limits by many issuers this year.

We call on issuers to manage risk more appropriately: (1) up front during the application process and before credit is extended, and (2) by monitoring credit limits and adjusting rates only on a forward-going basis.

If the industry does not heed the calls to police itself and reform its practices, we fear the anti-consumer terms outlined today will backfire on the industry and on our wider economy. A tipping point will surely occur. Companies will face greater defaults, negative public relations and increased legislation, and the economy will suffer further because family finances will be pushed to the limit, bankruptcies will increase, and jobs will be lost, increasing the burden on our public assistance system.

This concludes my prepared comments. I'll be happy to take any questions at the end of this call. I'd now like to re-introduce Mark A. Regier, Stewardship Investing Services Manager, MMA, who will conclude our formal comments.

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