

## SOME INCONVENIENT TRUTHS ABOUT THE IMPACT OF THE CREDIT CARD ACT

Assessing rates, fees, and credit availability after the Credit CARD Act

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UNconventional Wisdom is a periodic guest blog, where authors hold up the so-called common wisdom to a fresh perspective. To propose a guest blog, email either William Streeter, editor in chief, or Steve Cocheo, executive editor

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"Practical politics consists of ignoring the facts."

—Henry Adams

There is little doubt that the Credit CARD Act would, and in fact did, provide valuable protections to consumers, primarily through the elimination of surprise interest rate increases, especially on existing balances. However, there were tradeoffs, not all necessarily positive for consumers, that have been ignored or distorted.

Various reports focusing on the impact of the Credit CARD Act have sent a common message: "The Credit CARD Act that eliminated certain practices has had the impact of eliminating those practices."

In other words, credit card companies are complying with the law.

That's almost circular reasoning. No one expected card companies to ignore the law. However, many of the reports do not seem to stretch much beyond this rather obvious conclusion.

In particular, they fail to describe what has really happened to credit card interest rates and fees, and the availability of credit card credit, since it became clear that prohibitions against certain practices were coming quickly. (See timeline in chart at the end of this article.)

The "accepted wisdom" on CARD Act

Frequently cited in recent articles about the impact of the CREDIT Card Act is a Pew study released May 2011: A New Equilibrium: After Passage of Landmark Credit Card Reform, Interest Rates and Fees Have Stabilized.

In that report, the charitable trust stated:

"As the two-year anniversary of the Credit Card Accountability, Responsibility, and Disclosure (Credit CARD) Act approaches, new research from Pew confirms that consumer credit cards have become safer and more transparent while interest rates and fees have stabilized since the Act's new reforms have taken effect."

That Pew study compared credit card solicitations from March 2010 and January 2011. Pew reported that it found that, "Interest rates have stabilized. Median advertised interest rates for purchases on bank-issued credit cards--12.99% to 20.99 % depending on a consumer's credit history--remained unchanged from 2010."

Some interpreted this research to mean that interest rates had not changed due to the Credit CARD Act. On the strength of that interpretation, they declared the Credit CARD Act an unmitigated success with no impact on interest rates and no negative impact on consumers.

Curiously, they were ignoring or disowning earlier Pew studies. Those reports had shown that interest rates and some fees, such as charges for balance transfers, had increased after the Federal Reserve Board's adoption of its regulation in December 2008 and prior to March 2010--the period after which rates stabilized, but almost a year after the Credit CARD Act was signed.

### A closer look at impact

More interesting than the level of advertised credit card interest rates today--the focus of the May 2011 Pew study--is its comparison of today's rates with reported advertised rates at the time the Federal Reserve Board's adoption of the regulations which became the Credit CARD Act's core provisions.

Those provisions would have the greatest potential for increasing interest rates and fees. Looking at previous Pew studies, one draws this key conclusion:

Since the Board's adoption of the rule that was ultimately incorporated into the Credit CARD Act, advertised interest rates increased about 3 percentage points for the lowest advertised rate and about 4 percentage points for the highest advertised rate.

According to Pew, advertised interest rates (lowest and highest) went up from 9.99% to 15.99% to 12.99% to 20.99%.

### Pew Studies

December 2008

July 2009

March 2010

January 2011

Purchase APR

9.99% to 15.99%

(page 3, October 2009)

12.24%-17.99%

(page 3, October 2009)

12.99% to 20.99%

(page 3, July 2010)

12.99% to 20.99%

(page 2, May 2011)

In other words, according to the combined Pew studies, advertised credit card interest rates went up after adoption of the Board's final rule and have recently stabilized.

This is a slightly more informative description of the comprehensive Pew data. And it is a better summarization of what has happened to credit card interest rates since proposal of and adoption of new rules than the conclusion that credit card interest rates have recently stabilized.

Let's dig deeper

There's a more valuable and accurate set of data than advertised rates for measuring what interest and fees cardholder actually pay. This has been ignored by many reporters. The information is found in data that nine of the largest credit card companies provided to the Consumer Financial Protection Bureau at its request. The data were compiled by Argus Information & Advisory Services.

A key point: Based on what the big banks' customers actually pay, retail APRs have increased, especially among low-risk accounts--the accounts held by the most creditworthy customers.

The prime rate-adjusted retail APR increased about 2.4 percentage points, from 10.9% to 13.3%, from the third quarter of 2008 (after the Board's proposed regulation but before final adoption) and the third quarter 2010, after the August 2009 and February 2010 implementation of the core provisions of the CARD Act. 5

In addition, the Argus data found that about twice as many cardholders are paying annual fees.

The percentage of people paying an annual fee doubled from 12.7% in the third quarter of 2008 (after the Board's proposed regulation but before its final adoption) to 25.5% in the third quarter of 2010.

As of the third quarter of 2008, one in four rather than one in eight is paying an annual fee.

This contrasts with the May 2011 Pew study, which found only 14% of offers (not actual accounts) included an annual fee.

Yet, rather than relying on the Argus data showing what cardholders actually pay, many reporters instead cited the Pew study. Apparently, for some, in determining whether people pay annual fees, data showing whether they actually pay annual fees is less relevant than data derived from solicitations of whether people may have to pay an annual fee.

#### Odd omissions from Pew analysis

Similarly, coverage of this issue has strangely overlooked changes to other fees since the proposal and adoption of the Board rule and subsequent passage of the Credit CARD Act.

In May 2011, Pew reported that annual fees and other charges have changed little. Yet its July 2010 report found that fees for cash advances and balance transfer fees had already risen significantly--by one-third--between July 2009 and March 2010. The Argus data found that balance transfer fees, as a percentage of the transfer, increased from 1.8% to 3.2% from the third quarter of 2008 to the third quarter of 2010.

Also missing from the discussion about the impact of the Credit CARD Act is the impact on the availability of credit cards and the amount of credit card lines.

Pew did not report on availability of credit.

However, the Argus data show a drop in new account volumes and lower credit lines. (See page 4 of the PowerPoint.) It might be reasonable to opine that credit card credit should not have been so easily accessible. (Easily suggested by those who have it, rather than those who need it, but can't get it.) But why ignore the facts?

An inescapable conclusion from all the data

None of this is to say that the increase in interest rates and other fees or the reduction in credit card availability is completely attributable to the Credit CARD Act. Clearly, there is no question that the economy had a significant impact.

However, equally clear is that the Credit CARD Act has contributed to the changed credit card landscape--and will continue to be a factor. How much is attributable is difficult to tease out, but that the Credit CARD Act had an impact is undeniable.

The question is, why are some so eager to deny it?

Why not simply acknowledge that, while there were many positive aspects for consumers, there were trade-offs?

Share your viewpoints on the research and Nessa Feddis's column in the comment section at the end of this page

#### Footnotes:

1 See for example, "Two Steps Forward: After the Credit CARD Act, Credit Cards Are Safer and More Transparent—But Challenges Remain." The Pew Health Group LINK: [www.pewtrusts.org/creditcards](http://www.pewtrusts.org/creditcards) July 2010; and "Credit Card Reform Act Working, Report Finds," [www.ConsumerAffairs.com](http://www.ConsumerAffairs.com), July 2010: "Many of the most troublesome practices of the credit card industry have been eliminated."

2 In July 2008, the Federal Reserve Board proposed regulations significantly limiting the ability of credit card issuers to increase interest rates on existing balances and requiring advance notice of interest rate increases on new balances. These were among other provisions ultimately incorporated into the Credit CARD Act. The Board adopted its final regulation in substantially the same form in December 2008.

3 Pew did not have data for advertised rates prior to the adoption of the final regulation adopted in December 2008 so a comparison of advertised rates at the time of the proposal is unavailable.

4 Each cell contains a link to a PDF of the Pew report the data is taken from. You can find the data using the page number reference.

5 It is safe to assume that credit card issuers began to consider adjustments to their business models and pricing for new accounts immediately after the Board's July 2008 proposal and continued to make adjustments after its adoption in December 2008 and before the Credit CARD Act was adopted in May 2009.

Timeline for card regulation and legislation

July 2008

Board proposes regulation prohibiting certain practices, including restrictions on rate increases on existing balances. Advance notice of increases on new balances required.

December 2008

Board adopts final regulation, to be effective July 2010.

Pew surveys advertised credit rates and terms.

May 2009

President signs Credit CARD Act.

July 2009

Pew surveys advertised credit rates and terms. Report released October 2009 shows advertised interest rates increased 2.15 percentage points (lowest) to 2.00 percentage points (highest) between December 2008 and July 2009.

August 2009

Critical Credit CARD Act provisions go into effect:

- Card issuers must provide 45- day advance notice of rate increases or other significant changes.
- Cardholders must have opportunity to opt out of certain changes, including rate changes, and pay existing balance off at original rate.

February 2010

Bulk of remaining provisions go into effect, including further restrictions on rate increases; opt in requirements for over-the-limit fees; and payment applications to balances.

March 2010

Pew surveys advertised credit rates and terms. Report released July 2010 show advertised interest rates increased 0.75 percentage point (lowest) to 3 percentage points (highest) between July 2009 and March 2010.

Combined with earlier Pew study, advertised interest rates in July 2010 were 3 percentage points higher for the lowest advertised rate and about 4 percentage points for the highest advertised rates than in December 2008 when the Board adopted its final rule.

January 2011

Pew surveys advertised credit rates and terms. Report released May 2011 show advertised rates remained the same between March 2010 and January 2011.