Credit card “bill of rights” puts few restraints on banks

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Last week the US Congress passed and President Obama signed into law the so-called Credit Card Holders’ Bill of Rights, legislation that has been touted by both the Congress and the Obama administration as a major reform of unfair practices by credit card issuers.

This legislation has been pushed through Congress amid growing outrage by middle class card holders over the increasingly arbitrary and usurious methods being used by credit card issuers to extract ever more money from a shrinking pool of card holders who are, at the same time, being battered by the economic crisis. The banks, which have suffered severe losses in other areas, such as the collapse of the mortgage bubble, have turned to their credit card business as a potential source of increased revenue.

For several decades credit cards had indeed been an area of growing profitability. Credit card debt has increased by 25 percent in the last decade. About 90 million households carry credit cards, with an average debt load of more than $10,500, according to CardTrak.com. Penalty fees alone amount to $15 billion per year, representing 10 percent of the credit card industry’s revenues. Recently, however, as unemployment, mortgage foreclosures, and other aspects of the crisis have hit large numbers of people, the income realized by the banks from credit cards has declined, due both to a marked retrenchment in purchases, as well as a growing proportion of late payments and outright defaults.

MasterCard’s Chief Financial Officer Martina Hund-Mejean told Reuters that US purchase volumes are declining in the second quarter at a higher rate than in the first quarter. The AP reports a record drop in borrowing on credit cards, which fell at an annual rate of $7.8 billion in February. It was the sharpest drop in dollar terms since federal records began in 1968, and the steepest percentage decline since 1978.

As the economic crisis deepens, the rate of payment defaults has grown markedly. The Federal Reserve reported that in the first quarter of 2009, credit card delinquencies rose to an all-time high of 6.5 percent. Credit-card defaults reached a near-record 7.5 percent. These defaults are occurring across the board, including both “risky” and “credit worthy” borrowers, reflecting the broad impact of the economic crisis. This has placed banks and other credit card issuers in a precarious position, and they have responded aggressively.

As has been widely reported in the media, some of the tactics employed by the banks in an attempt to increase their rate of return have included: repeated increases in interest rates based on little or no justification even for customers who paid regularly, imposition of increasingly large penalties for late payments often created due to arbitrary and unannounced changes in due dates, shortened periods between statement delivery and payment due date, and double billing during a single payment cycle. The average interest rate charged on credit card balances was 13.5 percent in February, according to a Federal Reserve report in March. Interest rates of more than 20 percent are paid by about a third of card holders, and some are as high as 41 percent.

For several decades the credit card companies had used a range of aggressive and deceptive practices to lure large numbers of people into taking cards, tactics such as low “teaser” rates that would later be raised substantially and lavish campaigns on college campuses to snag financially unsophisticated students. However, now, as growing numbers of people have suffered economic difficulties due to the crisis, the banks have unilaterally reduced credit limits or closed accounts entirely based on “profiling” card holders, using presumed similarities to people who had defaulted on payments, even if the individual in question has given no indication of such difficulties.

The new legislation will, at best, dampen these practices only slightly. The bill’s main provisions include a prohibition on raising interest rates on existing balances unless payments are at least 60 days overdue and a requirement that credit card issuers give 45 days notice of increases in interest rates or other changes in an existing “agreement.” The bottom line is that interest rates and fees can still be raised, only a bit more slowly. For those already paying 20 percent or more such “restraints” will have little significance. Furthermore, as growing numbers of people lose their jobs or are hit in other ways by the economic crisis, the slight delays in the imposition of increasingly usurious terms by the banks will barely be noticeable.

The most significant change that could have been made, the imposition of a cap on interest rates and fees, was briefly floated by some Democrats, but quickly killed.

Senator Christopher Dodd, chairman of the Finance Committee and a major recipient of campaign contributions from the financial sector, is quoted by the *Huffington Post* as saying, "There used to be a time you could go to jail for charging rates like they charge today. Even organized crime would blanch at some of these fees. So there'll be a movement in that regard [capping interest rates and fees—WSWS]. There's [sic] obviously some legitimate arguments about opposing caps, and I'm listening to them, but frankly the overwhelming majority of people I talk to would like to see some limitation put on these rates."

Senator Bernie Sanders of Vermont, who styles himself a “socialist,” proposed a 15 percent cap on credit card interest, the same as is currently in effect for credit unions. “When banks are charging 30 percent interest rates, they are not making credit available,” said Mr. Sanders. “They are engaged in loan sharking.” The amendment was overwhelmingly rejected, drawing only 33 votes of the 60 needed.

In its report on the vote, the *New York Times* noted: “The banking industry, which had some heavyweight representatives monitoring the vote, warned that an interest rate limit could cause a sour reaction in the financial markets.” Presumably, senators who have counted on the financial services industry for a large share of their campaign contributions were conscious of the “heavyweights’” presence.

The grandstanding over the issue of rate and fee caps followed by a quick climb down illustrates the fundamentally fraudulent nature of this legislation and the total subservience of the Democrats to the financial elite. The proposed legislation’s provisions are similar to ones the Federal Reserve was already planning to implement in July of 2010. The politicians, for all of their bombast, are only bringing these regulations forward a few months. In other words, the implementation of these limited restrictions is still nearly a year away, leaving plenty of time for the banks to increase rates at will. They will also find ways of circumventing the bill’s provisions when they do come into effect, such as through the imposition of annual fees.

Top card companies, including JPMorgan Chase & Co., Citigroup, Bank of America, Capital One, and American Express, are already “raising interest rates on a larger portion of customers than usual and increasing the number of fees they impose,” Joshua Frank, a senior researcher at the Center For Responsible Lending, said in a research note. Many cardholders have seen increases of as much as 10 percentage points or more over their existing rate.

The lopsided votes for passage of this bill in both the House and Senate, with many Republicans joining the Democrats, is a sure sign that, the constraints put on the credit card companies by this legislation are minor. The *New York Times* quoted Edward L. Yingling, president and chief executive of the American Bankers Association, as stating that the bill contained provisions that were “tough, but workable.” Warnings by issuers that the legislation will result in a restriction of credit are disingenuous at best, since they are already cutting credit limits and closing accounts.

Despite the claim by Senate Majority Leader Harry Reid that, “We stood up for consumers and stood up to abusive credit card companies,” there is little in the legislation to aid the large numbers of working and middle class people who are being crushed by credit card debt. The bill’s actual purpose was indicated by Reid when he stated that, “Any effort to restore confidence in our economy must start not on Wall Street but on Main Street, and that’s what the credit card situation is all about.” In other words, this is one component of the government’s campaign to try to convince the population that through its efforts the economy is beginning to improve.

Americans are estimated to hold a total of more than $2.5 trillion in personal debt, excluding home mortgages, according to the Federal Reserve. The growth of personal indebtedness over the last several decades is largely the result of two factors. First, the decline of real wages has forced middle and working class people to use credit, not only for “luxuries,” as the right-wing media is fond of repeating, but to deal with unexpected expenses, such as medical bills not covered by insurance, or to pay for “big ticket” items such as large household appliances. For businesses and the wealthy using credit to compensate for variations in “cash flow” is portrayed as a perfectly acceptable practice. However, when people of lesser income do essentially the same thing, they are branded as irresponsible and extravagant, living beyond their means and, by implication, their status.

Over the past decades, credit card defaults have paralleled the unemployment rate fairly closely. This tends to undercut the myth propagated by the media that many people (read: the working class) “irresponsibly” overspend through the use of credit cards getting themselves into unmanageable levels of debt. In fact, it appears that difficulties arise primarily when people lose their jobs. Another frequent factor is huge medical bills due to catastrophic or chronic illness. Therefore, payment defaults by individuals are primarily the result of the capitalist crises and inadequate social programs.

Credit card companies are behaving in accordance with patterns established in recessions of the past. The companies squeeze cardholders in order to maintain their profits during the economic downturn. The expectation is that the increased rate of return will carry them until better times return, despite the fact that this policy will drive a certain percentage of their customers into extreme economic difficulty and raise the rate of payment defaults. In other words, there is a cold calculation that no matter how many people are driven to default, the increased income from those remaining will maintain the revenue balance in the company’s favor until the economy rebounds.

This strategy is based on the assumption that the rebound will occur before the balance tips the other way—when the losses from the ever increasing numbers of defaults overwhelm the company’s ability to squeeze greater income from those credit card holders who have not yet succumbed to economic ruination, which is brought on, in part, by the very policies carried out by the companies. Clearly, this model leads to disaster if the economic crisis continues for longer than expected. However logical it might appear for the banks to reduce the financial stress on borrowers so that they can survive over the long term and continue making payments, the incessant need to maximize profits in the short term in order to maintain investor support makes this latter strategy impossible for capitalists. Thus, the “logic of the market” leads to irrational and destructive results.

The business and financial elites are caught in a contradiction. On the one hand, retailers are desperate to get people spending again, which means a return to the “easy credit” conditions of recent years. On the other hand, the banks, while enjoying a temporary respite due to federal bailout money, but at the same time still acutely aware of their highly precarious financial positions overall, are driven to jettison those card holders they consider risky while squeezing the remainder for all the revenue they can get. The huge amount of outstanding credit card debt—nearly a trillion dollars—poses a major threat to the stability of the banking system. The federal government has reported that 12 of the nation's 19 biggest banks could experience credit card losses of $82.4 billion through the end of next year under a “worse-than-expected” economic scenario. With rising unemployment and other stresses on the economic condition of increasing numbers of middle and working class people, this contradiction will only get deeper.