Deceptive Tactics of Credit Card Companies

By: Aaron J. Byrd

Table of Contents

I. Introduction ……..1

II. The Problem: Deceptive Tactics of Credit Card Companies ...…………………………....2

III. The Initial Solution: The Credit CARD Act of 2009 …..3

IV. Drawbacks to the Credit CARD Act of 2009 …………………………………………....5

V. The Proposed Solution: Amend the Credit CARD Act of 2009 ………………….............6

VI. Conclusion ………………………………………………………………………………8

I. Introduction

For decades, American consumers have relied on the availability and accessibility of credit and debit cards to purchase consumer products and services on the assumption that they were fully and fairly aware of the consequences of their purchases. Most consumers were under the mistaken belief that credit card companies accurately depicted and truthfully represented credit terms, interest rates, fees, and costs. However, 800 billion dollars of credit card debt later, Americans are realizing that credit card companies have sneakily and deceptively turned consumers' naivety into a "cash cow" of profit.[i] Accompanying the companies' misleading tactics was an industry void of regulation, allowing these companies to wage a large assault on consumers' gullibility without the fear of being punished or prosecuted.[ii]

In May 2009, Congress introduced the Credit Card Accountability and Responsibility and Disclosure Act of 2009 (the "Credit CARD Act") to regulate the timing and manner of collecting credit card fees as an initial solution.[iii] However, this original solution was attacked by credit industry leaders, as well as criticized by consumer rights advocates for still allowing credit card companies and banks to engage in deceptive and misleading tactics.[iv] This article highlights a number of traditional deceptive tactics that credit card companies routinely employed before the passage of the Credit CARD Act of

2009, as well as reveals the impact of the Credit CARD Act on the credit debt crisis. Finally, this article offers proposed solutions to reduce the risk of unfair and misleading tactics by credit card companies.

II. The Problem: Deceptive Tactics of Credit Card Companies

Credit card companies have traditionally employed a variety of deceptive or misleading tactics against consumers to maximize their profit and revenue from cardholders. These companies would routinely charge costs and fees for opening a credit card account directly to the credit card, thereby deceptively reflecting the amount of credit actually available to the consumer.[v] Credit card companies would also immediately raise interest rates on credit cards once a monthly payment became overdue – even if payments were made one day late.[vi] Many credit card lenders would engage in a tactic known as "slamming" or "loan packing," in which the lenders would sign consumers up for "protective measures," such as credit insurance, without ever disclosing this fact to the consumers or without the consumers ever agreeing to it.[vii] Banks historically have used a tactic called "universal default," in which credit card agreements included a provision that the bank could raise interest rates on a consumer's credit card even if the consumer was late on other payments due, such as utility bills, cable bills, or car payments.[viii]

A common tactic that credit card companies employed is to receive a consumer's payment and apply it to the loan with the lowest interest rate, so that the company can keep charging the higher interest rate from the other loans.[ix] Lenders also allowed purchases over the credit limit, and then raised interest rates and placed the negative information on the consumer's credit report, even if the purchase had only gone over the credit limit by one dollar.[x] Banks also routinely changed due dates so people would pay late, and the banks simply hid the disclosure of the new due date somewhere in the plethora of pages of the credit cardholders' agreements.[xi]

Credit card companies and banks developed a new tactic in which consumers were charged fees for having a $0.00 balance or for "inactivity."[xii] Consumers are actually charged fees for paying off the entire balance of their credit card and for not making any purchases on the credit card for a certain period of time. Furthermore, credit card lenders would solicit consumers with attractive low introductory interest rates and Annual Percentage Rates that eventually ballooned to very high rates early in the term.[xiii] Exhaustive research reveals courts have consistently held that credit card companies can unilaterally change or modify the terms of the credit card agreements, as long as companies provide some form of notice to the consumers.[xiv]

Most noticeably, credit card companies targeted low-income consumers and collected fees based upon a “minimum payment calculation”, in which companies would disclose a “minimum payment” due, but did not disclose related penalty fees. This forced low-income consumers continually into default and unable to remain current on their credit card payments.[xv] Using a number of these tactics, credit card companies and banks would further target consumers who were clearly unable to make payments, and therefore collect fees and raise interest rates on these “subprime” consumers.[xvi] Considering the long history of deceptive tactics employed by credit card companies, consumers demanded that Congress improve the regulation of credit card tactics and restrictions on credit card disclosures.

III. The Initial Solution: The Credit CARD Act of 2009

In May 2009, Congress enacted the Credit CARD Act of 2009 to regulate the timing and manner of collecting credit card fees. [xvii] The Credit CARD Act amended the Truth in Lending Act (TILA).[xviii] TILA's primary purpose was to ensure "meaningful disclosure of credit terms" so consumers could compare available credit terms, "avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices."[xix] Under the Credit CARD Act, credit card companies are required to comply with new restrictions and regulations, and are prohibited from engaging in the deceptive tactics mentioned above.

Specifically, the Credit CARD Act prohibits retroactive rate increases and declares that a “universal default” provision is now illegal.[xx] The Credit CARD Act also requires credit card companies to no longer increase interest rates on existing balances, except when an account is 60 days past due or if it already carries a variable interest rate and the accompanying index rate changes.[xxi] Credit card companies may no longer allocate a consumer's payment above the minimum payment in a manner that maximizes interest rates.[xxii] Additionally, the Credit CARD Act must give 21 days between the date a bill is mailed and the payment due date.[xxiii] Credit card companies and banks must abide by the limits within the Act on how large a penalty fee can be, and credit card companies are prohibited from charging fees that are more than 25 percent of a subprime credit card's line of credit.[xxiv] Finally, the Credit CARD Act contains other prohibitions and restrictions against credit card solicitations and marketing credit cards to college students.[xxv]

Early research revealed that the Act has reversed much of the unclear pricing on credit cards that for years misled consumers into believing they paid less for credit card debt than was actually true.[xxvi] The CARD Act also revealed that interest rates paid on credit cards have fallen in the last year.[xxvii] In fact, the Credit CARD Act shows that not only did interest rates decline between 2009 and 2010, but also that the credit card fee income was flat.[xxviii]

Opponents offer the strong argument that implementation of the Credit CARD Act will lead to higher rates imposed by banks and more difficulty for consumers to obtain credit. However, a counterargument shows that this is because people mistakenly view higher rates on mail solicitations and other offers as a price increase. In reality, though, the credit card offers now just more closely match actual costs. Prices remain relatively level, but consumers now have a better understanding of the price differences and the costs associated with obtaining a credit card. The Credit CARD Act had initial success in reducing the disparity between *actual* costs and the card companies' *stated* costs to consumers, although the Credit CARD Act still suffers from a number of drawbacks and loopholes that benefit the credit card companies.[xxix]

IV. Drawbacks to the Credit CARD Act of 2009

Opponents of the Credit CARD Act have a much stronger argument that the Act is riddled with flaws and drawbacks that allow credit card companies to take advantage of unwary consumers. For example, the Credit CARD Act still allows credit card companies to impose many charges, such as fees for international purchases and for having a zero balance or "inactivity."[xxx] Credit card companies can also close accounts or reduce lines of credit without notice for any reason, although they must wait 45 days before they can impose an over-the-limit fee or a penalty rate on a newly lowered credit limit.[xxxi] Companies can also raise interest rates without limit on future purchases if they give 45 days' notice. If consumers do not accept the higher rate, they may close the account and pay it off over five years.[xxxii]

Furthermore, the Credit CARD Act of 2009 still allows for the "exportation of fees" under federal law.[xxxiii] Under 12 U.S.C. § 1831d, banks are allowed to export the interest rates and fees permissible in the bank's home state.[xxxiv] Therefore, any credit card company whose home state is South Dakota or Delaware will not be subject to a "ceiling" on interest rates and are allowed to charge any rate to consumers while still complying with federal law.[xxxv] Opponents to the Credit CARD Act have convincing arguments that courts have been reluctant to rule against credit card companies and banks in regards to violations of the Credit CARD Act.[xxxvi]

One final major drawback to the Credit CARD Act is that the provisions do not apply to small businesses. Therefore, credit card companies are able to engage in any traditional and conceivable tactic that they want against the holder of a *business* credit card, such as arbitrarily changing any or all terms for credit cards held by small business owners.[xxxvii] Merchants and small business owners receive no protection from the Credit CARD Act and are constantly being deceived by credit card companies. In conclusion, although the Credit CARD Act of 2009 has triggered an early assault on the deceptive and unfair tactics of credit card companies, it has still allowed credit card companies to engage in some practices that are unfair, deceptive, and overly aggressive.[xxxviii]

V. The Proposed Solution: Amend the Credit CARD Act of 2009

A number of proposed amendments to the Credit CARD Act would eliminate deceptive credit card tactics, provide additional protection for consumers, and offer harsher punishments for violators. First, although the Credit CARD Act simply amended the Truth in Lending Act (TILA), the Credit CARD Act should incorporate the entire subsections of TILA and Regulation Z regarding open-end credit disclosures.[xxxix] Incorporating both TILA and Regulation Z also requires credit card companies to provide proper notice requirements for changing the terms of agreements, reducing lines of credit, and closing consumer's accounts. If the Credit CARD Act were to incorporate these provisions, instead of simply amending certain portions of TILA, the Act would carry the weight of both TILA and Regulation Z as the ultimate regulation on the credit card market.

Following the proposed solution of incorporating both TILA and Regulation Z's regulation on open-end credit, the Credit CARD Act should also seek to incorporate the entire Fair Credit Billing Act (FCBA).[xl] The FCBA is an amendment to TILA, and its purpose is to protect consumers from unfair billing practices and to provide a mechanism for addressing billing errors in open-end credit accounts.[xli] With the incorporation of TILA, Regulation Z, and the FCBA, the Credit CARD Act would provide the most comprehensive regulations and prohibitions of credit cards in the financial industry. Opponents to the Credit CARD Act argue that the disclosure requirements fail to protect consumers from inflating prices and do not help consumers obtain credit.[xlii] However, by having one overall act that substantively governs the entire credit card industry, both lenders and consumers become more knowledgeable of the procedures and requirements of credit card transactions. Incorporating these provisions eliminates the need for multiple acts to govern the credit card industry and thus makes it simpler for consumers to understand the industry's regulations, price differences, and interest rate variations.

The Credit CARD Act should also be amended to incorporate the Federal Trade Commission Act's (FTC Act) punishments for credit card companies that still engage in deceptive and unfair practices. Under the FTC Act, the Federal Trade Commission enforces federal violations that are deceptive or unfair business practices.[xliii] By adding the FTC Act's punishments, the Credit CARD Act becomes enforceable by the Federal Trade Commission and United States Attorney General, and by retaining its private right of action under TILA, also is enforceable by state attorneys general and individual consumers. Therefore, the Credit CARD Act becomes enforceable by both federal and state authorities, thus acting as a major deterrent for potential violations by companies and banks.

The actual substantive regulations of the Credit CARD Act need to be amended to restrict the deceptive and unfair tactics credit card companies are still allowed to engage in. For instance, the Credit CARD Act should be amended to prohibit credit card companies from charging "inactivity" fees and zero balance fees. It is contrary to public policy to punish consumers for properly paying down their debt. By eliminating "inactivity" fees and zero balance fees, credit card companies can no longer scam consumers for unmerited profits that plague this industry. Therefore, the Credit CARD Act of 2009 needs to be amended to include these proposed solutions in order to prevent credit card companies from dishonestly exploiting the innocent consumers being preyed on for so many years in this industry.

VI. Conclusion

By enacting these proposed solutions into an amendment to the Credit CARD Act of 2009, Congress will create what consumers, interest groups, and lobbyists have called for over the last decade: an effective, substantive regulation on the credit card industry. The Credit CARD Act of 2009 was the first major step in grappling the predatory tactics of credit card companies, but it is losing its chokehold on the industry as companies develop new tactics to exploit the drawbacks to the Credit CARD Act. Only by amending the Credit CARD Act of 2009 will Congress accomplish the true goals of the credit card regulation, and the American consumer can again safely engage in the credit transactions that remain the lifeblood of the American economy.

Endnotes

[i] *Credit Cards: What You Need to Know*, Center for Responsible Lending, http://www.responsiblelending.org/credit-cards. (last visited May 7, 2012)

[ii] *Finally-Congress Investigates Credit Card Industry*, The Agonist, http://agonist.org/finally_congress_investigates_credit_card_industry (last visited May 7, 2012).

[iii] H.R. 627, 111th Cong. (2009); Southern Div. First Premier Bank v. United States Consumer Fin. Prot. Bureau, 819 F. Supp. 2d 906 (D.S.D. 2011).

[iv] Kerry Tomlinson, Credit Card Tricks Under the New Laws, KATU News, February 17, 2010.

[v] Ben Popkin, How Predatory Lending Works, The Consumerist, May 12, 2010. http://consumerist.com/2010/05/rent-to-own-is-loansharking.html (last visited May 5, 2012).

[vi] Kerry Tomlinson, Credit Card Tricks Under the New Laws, KATU News, February 17, 2010; *Tactics Credit Card Issuers Use to Get You to Pay More*, The Hinsley Law Firm, http://www.consumersdefense.com/cc-company-tricks.html. (last visited May 5, 2012).

[vii] Spears v. Colonial Bank of Alabama, 514 So. 2d 814 (Ala. 1987) (finding that state law did not prohibit car dealers or other companies making loans from receiving commissions on the sale of various types of insurance, so long as all other provisions of those sections were met). The credit card lenders would then charge the consumers for being enrolled in these services and “protective measures,” all the while the consumer has no idea what they are paying for. Lemelledo v. Benefit Mgmt. Corp., 150 N.J. 255 (N.J. 1997) (holding that Beneficial was subject to Consumer Fraud Act and was liable because it routinely engaged in “loan packing” where it forced consumers to pay for credit insurance in the loan without disclosing that fact or by not allowing consumers to obtain the loan if they did not pay for the credit insurance). Consumer victims have been unknowingly billed an average of $150 in the scam. Jill Kuramoto, Lawsuit Aims to Stop Predatory Tactics on Credit Card Holders, KITV News, http://www.kitv.com/news/hawaii/Lawsuit-aims-to-stop-predatory-tactics-on-credit-card-holders. (last visited May 4, 2012).

[viii] Thomas v. Universal Guardian Corp., 144 Ga. App. 869 (Ga. Ct. App. 1978) (holding that agreement provided that if the buyer failed to pay *any* scheduled payment, the seller could collect a default charge); *Tactics Credit Card Issuers Use to Get You to Pay More*, The Hinsley Law Firm, http://www.consumersdefense.com/cc-company-tricks.html. (last visited May 5, 2012).

[ix] *How Credit Card Companies Allocate Your Payments*, Finance for a Freelance Life, http://financefreelancelife.com/2008/07/28/how-credit-card-companies-apply-your-payments/. (last visited May 7, 2012). As a result, consumers likely did not realize that a payment they had sent was being applied to the lower interest rate credit card, and therefore, consumers would default on the higher interest rate loan. This in turn would trigger a default, and then the bank would raise the interest rate even higher, as the consumer had now become a “credit risk” under the “universal default” provision, or would simply require the consumer to keep paying at the higher interest rate. *New Law Bans Payment Allocation Trickery*, CreditCards.com, http://www.creditcards.com/credit-card-news/law-bans-credit-card-payment-allocation-trickery-1282.php. (last visited May 7, 2012

[x] Kerry Tomlinson, Credit Card Tricks Under the New Laws, KATU News, February 17, 2010.

[xi] Id.

[xii] Id.

[xiii] Id.; Rossman v. Fleet Bank Nat'l Ass'n, 280 F.3d 384 (3d Cir. Pa. 2002) (finding that the statement that the card had "no annual fee" made by the bank, if it intended to impose such a fee shortly thereafter, was misleading).

[xiv] Samuels v. Old Kent Bank, 1997 U.S. Dist. LEXIS 11485 (D. Ill. 1997) (rejecting plaintiff cardholders’ claims because agreement expressly provided bank could cancel program at any time for any reason); Garber v. Harris Trust & Savings Bank, 104 Ill. App. 3d 675 (Ill. App. Ct. 1st Dist. 1982) (ruling that either cardholder agreements constituted offers to extend

credit which could be withdrawn at any time, or if they constituted contracts, those contracts were terminable at will); Gray v. American Express Co., 743 F.2d 10 (D.C. Cir. 1984) (holding that although appellee could cancel appellant's card at anytime without notice, the provision did not apply to irreversible transactions completed prior to cancellation, such as appellee's dinner bill); Peterson v. Wells Fargo Bank, 556 F. Supp. 1100 (D. Cal. 1981) (finding that the warning contained in the notice the bank sent to its credit card customers was clear, unambiguous, and adequate).

[xv] Van Slyke v. Capital One Bank, 2007 U.S. Dist. LEXIS 82690, 12-13 (N.D. Cal. Nov. 7, 2007) ("Most customers in the sub-prime market targeted by Capital One make the "minimum payment" reflected on their bills. But where penalty fees have been assessed for a given month, customers who pay only the minimum payment amount represented as the customers' "minimum payment amount" did not include amounts incurred that month for penalty fees, including late, over-the-limit and returned payment fees. As a result, customers find themselves continually in "default" and cannot "catch up" because the monthly statements fail to include these fees as part of the "minimum payment" for that particular month."); See 15 U.S.C. § 1637(b) (2012); 15 U.S.C. § 1637(b)(8) (2012); 15 U.S.C. § 1637(b)(4) (2012); see also Household Credit Servs. v. Pfennig, 541 U.S. 232, 235-236 (U.S. 2004) ("When a creditor and a consumer enter into an open-end consumer credit plan, the creditor is required to provide to the consumer a statement for each billing cycle for which there is an outstanding balance due).

[xvi] Center for Responsible Lending, Comments of the Center for Responsible Lending Regarding Unfair or Deceptive Practices with Respect to Credit Cards, Federal Reserve Board: Reg. AA, Docket R-1314, OTS: Docket ID. OTS-2008-0004, NCUA: RIN 3133-AD47, 73 Fed. Reg. 28904 (May 19, 2008)

[xvii] H.R. 627, 111th Cong. (2009).

[xviii] 15 U.S.C. § 1601 (1968).

[xix] Id. at § 1601(a); Southern Div. First Premier Bank, 819 F. Supp. 2d at 909.

[xx] H.R. 627, 111th Cong. § 101(b) (2009).

[xxi] Id. (and companies must still provide proper notice of the changes to the consumer).

[xxii] Id. at § 104(b)(1).

[xxiii] Id. at § 106.

[xxiv] Id. at § 102.

[xxv] Id. at §§ 301 – 305.

[xxvi] Joshua M. Frank, Credit Card Clarity: CARD Act Reform Works, Center for Responsible Lending, (February 16, 2011), http://www.responsiblelending.org/credit-cards/research-analysis/FinalCRL-CARD-Clarity-Report2-16-11.pdf.

[xxvii] Id.

[xxviii] Id.

[xxix] *Highlights of the New Credit Card Rules: What They Do and Don't Do*, Center for Responsible Lending, http://www.responsiblelending.org/credit-cards/policy-legislation/congress/Highlights-of-the-New-Credit-Card-Rules-What-They-Do-and-Don-t-Do.html. (last visited May 7, 2012).

[xxx] Kerry Tomlinson, Credit Card Tricks Under the New Laws, KATU News, February 17, 2010.
[xxxi] *Highlights of the New Credit Card Rules: What They Do and Don't Do*, Center for Responsible Lending, http://www.responsiblelending.org/credit-cards/policy-legislation/congress/Highlights-of-the-New-Credit-Card-Rules-What-They-Do-and-Don-t-Do.html. (last visited May 7, 2012).

[xxxii] H.R. 627, 111th Cong. § 101 (2009).

[xxxiii] 12 U.S.C. § 1831d (2011).

[xxxiv] Id. Most banks make their home state either South Dakota or Delaware, because these states have no usury "ceiling" rates or penalties for high interest rates. Smiley v. Citibank (South Dakota) N.A., 517 U.S. 735 (1996) (holding that power of "exportation" extends not only to interest rates but also to other charges, including late fees).

[xxxv] Id.

[xxxvi] Chase Bank v. Yance, 2010 Pa. Dist. & Cnty. Dec. LEXIS 123 (Pa. C.P. 2010) (entering judgment for card issuer and awarded it the unpaid balance, attorney's fees, and court costs); Citibank, N.A. v. Mazzarella, 2010 Conn. Super. LEXIS 3285 (Conn. Super. Ct. 2010) (holding that Citibank did not violate the CARD Act and did not engage in any deceptive practices as a creditor).

[xxxvii] *Highlights of the New Credit Card Rules: What They Do and Don't Do*, Center for Responsible Lending, http://www.responsiblelending.org/credit-cards/policy-legislation/congress/Highlights-of-the-New-Credit-Card-Rules-What-They-Do-and-Don-t-Do.html. (last visited May 7, 2012).

[xxxviii] Joshua M. Frank, Predatory Credit Card Lending: Unsafe, Unsound for Consumers and Companies, May 8, 2012, http://www.responsiblelending.org/credit-cards/research-analysis/Unsafe-Unsound-Report-May-2012.pdf.

[xxxix] 15 U.S.C. § 1637 (2011); 12 C.F.R. § 226 (2011); For open-end revolving credit lines, TILA requires creditors to disclose clearly and conspicuously the cost of credit, including all finance charges, annual percentage rates, and total charges. 15 U.S.C. § 1637 (2011); Clark v. Pinnacle Credit Servs., LLC, 697 F. Supp. 2d 995, 1000 (D. Ill. 2010); Rubio v. Capital One Bank, 613 F.3d 1195, 1200 (9th Cir. Cal. 2010). Regulation Z is a specific Federal Reserve Board regulation requiring debt lenders to disclose all the specifics of a given loan, and is used synonymously with TILA. 12 C.F.R. § 226 (2011).

[xl] 15 U.S.C. 1643 (2011).

[xli] Id.

[xlii] Joshua M. Frank, Credit Card Clarity: CARD Act Reform Works, Center for Responsible Lending, (February 16, 2011), http://www.responsiblelending.org/credit-cards/research-analysis/FinalCRL-CARD-Clarity-Report2-16-11.pdf.

[xliii] 15 U.S.C. §§ 41-58 (2011).