



# CARD Act Cut Fees \$20 Billion

by

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The Credit CARD Act of 2009 succeeded in cutting fees for cardholders to the tune of about \$20 billion per year -- without boosting interest rates or drying up the availability of credit, according to a new study based on 150 million accounts.

"We find that regulations to limit fees were highly effective," said the authors of the working paper posted online Sept. 26 by the National Bureau of Economic Research.

The paper is the largest study to look at the CARD Act and the first to measure what it saved consumers -- but it is unlikely to put an end to the debate about the consumer protection law.

Industry studies, looking at different data sets and time periods, have found that the CARD Act had significant benefits for consumers, but some tradeoffs as well. Faced with restrictions on fees, banks have reined in card lending and raised rates, pushing some borrowers toward payday lenders.

"They're looking at it from a different angle," said Nessa Feddis, general counsel at the American Bankers Association.

The new paper looks at a data set of 150 million general purpose credit card accounts from eight large banks tracked by the Office of the Comptroller of the Currency, from January 2008 through December 2012. "Regulating Consumer Financial Products: Evidence from Credit Cards," is co-authored by economists Sumit Agarwal at the National University of Singapore, Souphala Chomsisengphet of the OCC, Neale Mahoney at the University of Chicago and Johannes Stroebel at New York University.

Subprime borrowers saw the greatest drop in fees, the study found. Accounts with FICO scores below 620 had paid fees of about 23 percent of their average daily balance, on an annualized basis, before the law took effect. After the law's full implementation in August 2010, total fees had fallen to about 9 percent of the average daily balance, with over-limit fees reaching practically zero. Groups with higher credit scores saw more muted benefits, as they were paying less in fees than subprime borrowers to begin with.

## Regulators gathering

The study gives support for the effectiveness of regulation just as banking regulators are gathering in Chicago to discuss credit cards. The U.S. Consumer Financial Protection Bureau is expected to announce its own study about the effects of the CARD Act at the hearing Oct. 2. (The bureau is funded through the Federal Reserve, not Congress, so it is unaffected by the government shutdown.)

The study "seems to show that people with lower FICO scores are getting credit cards ... and that they are quite profitable for companies," said Ellen Schloemer, executive vice president at the Center for Responsible Lending. The center published its own study in 2011 disputing the notion that the CARD Act led to higher interest rates. It also found that credit card solicitations weren't impacted by the consumer protection law.

Consumer advocates say that upfront interest rate increases are better for cardholders than "gotcha" fees that snag the unwary or hit people who are already struggling financially.

The new paper disputes critics who say that regulators are playing a game of Whac-a-Mole, hitting costs in one area only to have them pop up in another. While rates offered on new cards rose after the law was signed and implemented, the average rates charged at the eight major banks studied were stable, the researchers found.

## Recession muddies the picture

Feddis at the ABA said the analysis fails to correct for effects of the recession. After millions of subprime accounts were written off, the remaining accounts leaned toward high-score "transactors" who mainly pay off their balances before racking up interest charges. For that reason, she said, interest costs based on average balances seem lower after the 2009 downturn.

A February study by the ABA that looked at a broader range of banks found that card rates for existing accounts rose somewhat, going from 13.78 at the third quarter of 2008 to 14.5 percent at the third quarter of 2012. Rates for home mortgages and car loans were going down during this same period.

Another analysis, the Federal Reserve's quarterly survey of bank loan officers, has found that banks cooled sharply toward card lending since 2009. Stroebel, one of the authors of the Sept. 26 study, said the effects of the recession are difficult to separate from the CARD Act.

"There's obviously a lot going on in the economy that might restrict credit," he said.

According to the OCC data, credit card interest rates remained stable for both low- and high-FICO score borrowers. That indicates that the reduced income for late fees and over-limit fees was not a factor in setting cardholders' interest rates, Stroebel said. Since high-FICO borrowers were rarely subject to late fees or over-limit fees, they were relatively unaffected by the CARD Act.

The Credit Card Accountability Responsibility and Disclosure Act was signed on May 22, 2009, and its major provisions took effect over phases in 2009 and 2010. First it required banks to give 45 days' notice before increasing rates. In the second phase, it required banks to let customers opt-in to charges that would cause over-limit fees. It also limited late fees to \$25 under most circumstances, and barred charging more than one penalty fee for a single violation.

### Low FICO scores, high profits

Some of the most eye-opening passages of the recent study have to do with the high profitability of cardholders with low credit scores. Even when looking at the charge-offs linked to these higher risk accounts, they were the most profitable group for card issuers during the pre-CARD Act period of April 2008 to January 2010, the study found. Per dollar of account balance, accounts with a FICO score below 620 generated profits of 7.9 percent, compared to an overall average profit of 1.6 percent, the study found.

Feddis said it is known that high-risk borrowers pay more for credit. As to their profitability, she said the industry association cannot comment because of anti-trust concerns.

Looking at the entire four-year period, the study of OCC data found that total fees per account averaged \$53.60 on an annualized basis while interest charges were \$159, based on an average daily balance of \$1,250. Late fees were the largest fee at \$22.99 annualized, followed by payment protection or "debt suspension" fees at \$7.93. Over-limit fees averaged \$7.48, monthly or annual fees were \$5.87, cash advance fees were \$3.92 and balance transfer fees cost \$3.56.

The study also confirmed that a small number of cardholders are paying down their balances faster post-CARD Act. The law required issuers to show how much you would save by paying off the balance in 36 months, instead of just making the minimum payment. Since this calculation began appearing on bills, the percentage of cardholders making the larger payment increased by 0.5 of a percentage point, resulting in annualized interest savings of \$24.

"We find these disclosure requirements had a small but significant effect on borrowers' repayment behavior," the study said.

**See related:** A guide to the Credit CARD Act of 2009

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