

The Credit C.A.R.D. Act: Opportunities and Challenges for Credit Unions

Adam J. Levitin

Associate Professor of Law

Georgetown University Law Center

filene
RESEARCH INSTITUTE



About Us

Deeply embedded in the credit union tradition is an ongoing search for better ways to understand and serve credit union members. Open inquiry, the free flow of ideas, and debate are essential parts of the true democratic process.

The Filene Research Institute is a 501(c)(3) not-for-profit research organization dedicated to scientific and thoughtful analysis about issues affecting the future of consumer finance. Through independent research and innovation programs, the Institute examines issues vital to the future of credit unions.

Ideas grow through thoughtful and scientific analysis of top-priority consumer, public policy, and credit union competitive issues. Researchers are given considerable latitude in their exploration and studies of these high-priority issues.

Traditionally, the Filene Research Institute focuses on long-term research questions that can take months or years to research and publish. Occasionally Filene also publishes Research or Innovation briefs. These briefs allow Filene to present important, time-sensitive, notorious, and unbiased topics to the credit union system. Oftentimes these briefs present an opportunity to distribute original research or innovation findings from Filene researchers or Fellows. We hope the “brief” format meets your need to obtain actionable and objective information in a timely manner.

By George A. Hofheimer,
Chief Research Officer

In September 2009, Bank of America inspired a YouTube video that quickly became a viral hit, earning more than 400,000 views and mentions at ABC News, the *Baltimore Sun*, CNN, and CBS News. Unfortunately for Bank of America, the video's subject, California resident Ann Minch, spends nearly five minutes lambasting the bank. Minch, a 14-year Bank of America customer, claims the bank jacked her annual percentage rate (APR) from 12.99% to 30% even though she was not late on payments and had not exceeded her credit line. When she called to inquire, Minch says the bank didn't budge, but instead referred her to a debt consolidation service. The video both protests her treatment and goes on to call for a debtors revolt.

Minch's video illuminates the thinking behind the 2009 C.A.R.D. Act: that consumers will be better served if undeserved interest rate hikes are outlawed, card issuer options are constricted, and fees are minimized. Perhaps more clearly, though, the video puts a convenient wrap around grassroots consumer sentiment and the opportunity for credit unions and other financial institutions that craft demonstrably responsible and consumer-friendly credit card programs.

The industry-wide return on assets of credit cards plunged from 3.3% in 2006 to 1.4% in 2008, according to Filene Fellow Robert Manning, and huge issuers will need to recoup those profits in the new environment. In the face of that turmoil, two Harvard researchers suggested in June 2009 that the credit union card model of plain-vanilla rules and low-interest rates disprove industry claims that issuers cannot afford to offer cards without the traditional fees. Not only does Professor Adam Levitin use this business brief to agree with those researchers, he argues that the C.A.R.D. Act widens the credit union niche for consumers like Ann Minch.

Key Findings

Levitin calls the act "the most significant piece of credit card legislation in a generation" and highlights some of the early ramifications along with intriguing credit union data:

- By constraining introductory credit terms and making it difficult for issuers to change borrowing terms, the Credit C.A.R.D. Act scrambles the credit card industry's backloaded pricing model, which depends on quick repricing and penalties for consumers who demonstrate risky behavior.

- Issuers are reconsidering the standard underwriting scheme that considers just FICO, stated income, and credit reports. Already many issuers are homing in on existing depository customers rather than broadcasting cheap credit promotions in the mail.
- At just 5% of overall credit union lending, credit cards are not core to most credit unions' lending. However, members who use a credit union credit card carry higher balances on average than users of bank cards, and credit union issuers have fewer dormant accounts.

The implications for credit unions are exciting. Large-scale issuers may retain the competitive advantages of sophisticated automated underwriting and efficient back-office operations. The C.A.R.D. Act now limits many fees and penalties that are unfriendly to consumers, so large issuers will likely develop new ones to reenergize their profits.

The right strategic place for credit unions, says Prof. Levitin, is to focus efforts on simplicity and transparency while doubling down on collaborative credit card efforts to improve efficiencies. Doing so will allow credit unions to pick off the current and future malcontents fleeing boorish bank behavior.

Credit card growth will not automatically accrue to credit unions. Large issuers will use their scale and their marketing power to assert their dominance despite the new restrictions. The opportunity for credit unions lies in banding together, cutting complexity, and offering members a clearly transparent option. Ann Minch would be proud.



Adam J. Levitin

Adam J. Levitin is an associate professor of law at Georgetown University Law Center in Washington, DC, where he teaches courses in bankruptcy, commercial law, contracts, and structured finance. He is also the Robert Zinman Resident Scholar at the American Bankruptcy Institute. Before joining the Georgetown faculty, Professor Levitin practiced in the Business Finance & Restructuring Department of Weil, Gotshal & Manges LLP in New York. He has also served as special counsel for mortgage affairs for the Congressional Oversight Panel supervising the Troubled Asset Relief Program and as law clerk to the Honorable Jane Richards Roth on the United States Court of Appeals for the Third Circuit. Professor Levitin's research focuses on financial institutions and their role in the consumer and business credit economy. He holds a JD from Harvard Law School, an MPhil and an AM from Columbia University, and an AB from Harvard College, all with honors.

Introduction

On May 22, 2009, President Obama signed into law the Credit Card Accountability, Responsibility, and Disclosure Act of 2009 (the “Credit C.A.R.D. Act”), P.L. 111-24, the most significant piece of credit card legislation in a generation. The Credit C.A.R.D. Act mandates major changes in credit card underwriting and the resultant business model. These changes both pose challenges and offer opportunities for credit union card operations in particular.

This research brief first reviews the major provisions of the Credit C.A.R.D. Act. It then considers how these changes affect card issuers’ underwriting and marketing in general. Next it surveys the relative position of credit unions in the card industry and cards in credit unions’ business, after which it turns to an analysis of how the Credit C.A.R.D. Act is likely to affect credit unions. It concludes with some suggestions of how credit unions can position their card operations to take advantage of the market changes wrought by the act.

The Credit C.A.R.D. Act: A Summary of Key Legislative Provisions

Limitations on Changes to Account Terms

The Credit C.A.R.D. Act places a number of restrictions on issuers’ ability to change the terms of existing accounts. First, issuers are prohibited from increasing rates, fees, or finance charges either retroactively on an existing balance or prospectively on an account in its first year of existence, except in specific circumstances:¹

- Upon the expiration of a promotional rate.
- Upon the expiration of a workout agreement.
- If the rate is a variable rate tied to an index.
- If the cardholder is 60+ days delinquent.

Promotional rates are required to last at least six months,² and if a delinquent cardholder whose rates have been raised makes timely payment for six months, the issuer must restore the original rate.³ If an issuer wishes to raise rates, fees, or finance charges or otherwise change significant account terms prospectively for reasons other than a change in a variable rate’s index or the expiration of a promotional rate or workout agreement, the issuer must provide notice of the change at least 45 days before it goes into effect, along with notice to the cardholder of the right to cancel the account before the term change.⁴

Limitations on Specific Types of Fees and Charges

The Credit C.A.R.D. Act also limits specific types of fees and charges. It requires cardholders opt-in to overlimit fees⁵ and restricts

the number of overlimit fees in a billing cycle.⁶ It limits the level of fees that can be applied to an account opening,⁷ a provision aimed at so-called subprime “fee-harvester” cards. The act further mandates that penalty fees be reasonable (as to be defined by the Federal Reserve through rule-making).⁸ Moreover, it prohibits the application of finance charges to any amount repaid on time, regardless of whether the full balance was repaid on time or the minimum payment was made.⁹

Other Provisions

The Credit C.A.R.D. Act also standardizes minimum payment requirements¹⁰ and requires that payments be first credited to the highest APR balance.¹¹ The act increases the mandatory minimum grace period for receiving payments from 15 to 21 days from the date of mailing of the billing statement.¹² Finally, the act imposes additional disclosure requirements relating to balance payoff timing¹³ and restricts marketing to college students.¹⁴

Effective Dates

Most provisions in the Credit C.A.R.D. Act go into effect February 22, 2010, but the 45-day notice of term-change provisions, the limitations on repricing existing balances, the requirements of payment application to highest interest rate balances first, and the 21-day minimum grace period already went into effect on August 22, 2009. Additionally, as of August 22, 2010, card issuers that raised cardholders’ rates after January 1, 2009, must review the reason for rate changes every six months and restore the old rate if the reason for the rate hike no longer exists.¹⁵ It is important to note that the Credit C.A.R.D. Act applies only to consumer cards and does not affect small-business cards.

Implications of the Credit C.A.R.D. Act for the Card Issuance Business

The Credit C.A.R.D. Act has several implications for the card issuance business. The predominant card issuance business model in recent years has involved card products with low up-front costs (no annual fees, low promotional rates) but high contingent back-end costs (penalty interest rates and late and overlimit fees). The back-end costs could be triggered by particular consumer behavior that might relate to the card account (late payment), to other on-us accounts, to off-us accounts (universal default), or simply any-time/any-reason repricing. These products were marketed on the basis of low promotional rates and rewards programs rather than on lowest total costs or greatest aggregate benefits.

This business model made credit very cheap for consumers to obtain initially, but it backloaded the costs. Backloaded, contingent costs are much less salient to consumers than up-front, noncontingent costs because of a well-documented cognitive phenomenon known as hyperbolic discounting. Thus, if two cards have the same net cost for the same transaction pattern, consumers are likely to select the card with the backloaded, contingent costs because they perceive it as cheaper.

For the backloaded cost model to work, however, the card issuer needs to be able to reprice the cardholder when various risk indicators are triggered, not just prospectively but also for existing balances. The ability to reprice balances retroactively, combined with the lock-in effect created by the costs of switching cards, made this business model very profitable; card industry pretax profits were \$39.60 billion (B) in 2008.¹⁶

The Credit C.A.R.D. Act places major limitations on the backloaded card business model. First, promotional rates must now be locked in for six months. This means issuers will be much more cautious in offering promotional rates. Second, retroactive repricing can no longer be triggered by consumer behavior, excluding serious delinquency. Retrospective universal default is no longer legal, so a card issuer cannot reprice a balance on the basis of the consumer's behavior with other accounts. The only credit-risk-based reason an existing balance can be repriced is if it is 60+ days delinquent, which means there is already a good chance that it will eventually be charged off.¹⁷ Prospectively, repricing is not possible in the account's first year unless it becomes 60+ days delinquent. After the first year, prospective repricing is possible only upon 45 days' notice, and with mandatory periodic reviews and resets if the risk condition has dissipated.

These restrictions on repricing will force more careful initial underwriting. Because issuers will not be able to reprice immediately according to perceived changes in consumer risk, it is particularly important that issuers underwrite correctly when the account is opened. This might require a more robust informational basis for underwriting than the standard basis of stated income, FICO scores, and credit reports.

The need for better initial underwriting, combined with concerns about declining consumer creditworthiness overall, has manifested itself in a sharp pullback of direct-mail offers in the card industry.¹⁸ Instead, marketing is now focusing on in-branch and Web site efforts with the goal of cross-selling to existing depositary customers. This has a double benefit of providing a more robust information basis for underwriting and increasing cardholder and depositor loyalty. The

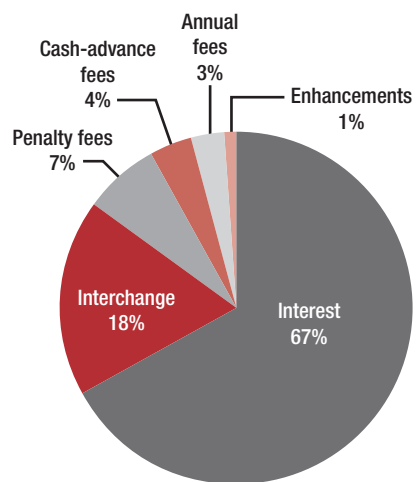
emphasis on initial underwriting will also likely mean that below-market promotional rates will become rarer and less generous.

Restrictions on the ability to reprice also mean that most issuers are likely to switch to variable-rate cards in order to avoid interest rate risk. Because rates on performing cards are locked in for the first year of the account's life and for at least 45 days thereafter, card issuers that continue with fixed-rate cards are exposed to short-term interest rate risk. While this risk can be hedged, it is likely cheaper to transfer it to consumers, even though that might elevate default risk.

The Credit C.A.R.D. Act's restrictions on back-end, behaviorally contingent fees will also make initial underwriting more important. Fees are economically interchangeable with interest, even if they are distinct in their behavioral impact. Consumers must affirmatively opt-in to over-limit, and the number of overlimit fees is limited. Likewise, penalty fees must be reasonable according to yet-to-be-written Federal Reserve regulations. These changes mean that card issuers will not be able to rely as much on fee income. To be sure, as Figure 1 shows, penalty fees, such as late and overlimit fees, make up only 7% of bankcard issuer revenue on average, and total penalty fee revenue has been significantly less than industry profits historically. For issuers seeking to maintain profit margins, however, the Credit C.A.R.D. Act will require better initial underwriting to compensate for reduced ability to levy back-end fees.

In addition to increasing the importance of initial underwriting, the Credit C.A.R.D. Act will likely result in a reconfiguration of credit card fees and rates. The act's limitations on certain fees and billing practices will encourage card issuers to reexamine the cost-benefit of existing fees as well as to look for additional sources of revenue to compensate for those diminished by the act. This means that there will likely be increases in existing fees that have limited price salience to consumers, such as interchange, foreign transaction fees, cash advance fees, and penalty interest rates, even as some issuers have eliminated overlimit fees because compliance costs of opt-ins outweigh revenues.¹⁹ The next few years will also see issuers testing new fee types in the market: paper-statement fees, high-risk transaction fees (for transactions with high chargeback risks), inactivity fees, monthly availability fees, etc. Some issuers are also likely to reexamine annual fees, which have generally been eschewed by the industry because of their high salience to consumers due to their up-front,

Figure 1: Sources of Bankcard Issuer Revenue, 2008



Source: Kate Fitzgerald, 2009 Bankcard Profitability Study, CARDS&PAYMENTS, May 2009, at 23.

sunk costs.²⁰ Issuers have also begun to experiment with monthly minimum payment increases as a risk-control method; the Credit C.A.R.D. Act allows for retroactive repricing as part of a workout agreement, but the term “workout” is undefined in the act. It is possible that a consumer could consent to retroactive repricing in exchange for an unwinding of an increased monthly minimum payment that the consumer cannot afford, and that such a deal would be considered a workout agreement, making the retroactive price increase permissible. Similarly, rewards programs, the value of which is extremely difficult for consumers to gauge, are likely to be scaled back.

Stated interest rates are likely to rise as a result of the act’s prohibition on finance charges on balances repaid on time. This prohibition not only means that double-cycle billing—a relatively rare practice of applying a finance charge to the average daily balance of the past two billing cycles—is no longer possible, but also ends the standard practice of applying finance charges to the average daily balances, including daily balances during the grace period. The result is that the average daily balance to which finance charges may be applied will, all things being equal, now be smaller for the same transaction pattern. Therefore, the only way to generate the same revenue as before from that transaction pattern is to apply a higher stated interest rate to the account. The Credit C.A.R.D. Act is thus likely to result in higher *stated* rates, even if the *effective* rate stays constant.

The pressure on stated rates will have a unique impact for federal credit unions (FCUs). FCUs are already limited to an 18% maximum APR on finance charges.²¹ The National Credit Union Administration (NCUA) interprets the finance charge cap on FCUs as applying to the effective rather than the stated rate.²² Therefore, FCUs have had to charge stated rates that are sufficiently below 18% so as to avoid crossing the threshold based on the effective rate. As this restriction remains in place for FCUs, the Credit C.A.R.D. Act is thus likely to result in an increased stated rate disparity between FCU card products and non-FCU cards. To the extent that consumers are choosing cards on the basis of stated purchase rates, this change should accrue to the benefit of FCUs.

While the Credit C.A.R.D. Act limits the backloaded pricing model, it does so by prohibiting or restricting specific fees and repricing. This leaves open the possibility of new, creative fees and price structures that get to the same result, and the competitive dynamics in the card marketplace will encourage issuers to continue to pursue backloaded pricing models. Because backloaded prices appear cheaper to consumers, an issuer that backloads prices has a competitive advantage over one with up-front pricing.

Credit Union Card Operations

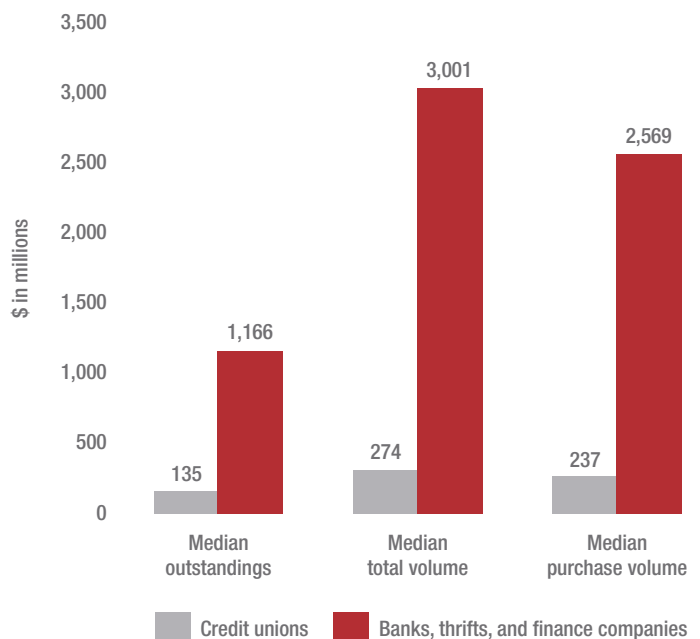
Card issuance is highly concentrated among a handful of large banks. Ten large bank issuers make up almost 90% of the market in terms of dollars transacted and outstandings, with the top five alone providing nearly three-quarters of the total.²³ Although 47 of the 100 largest card issuers in the United States are credit unions, they accounted for only 1.76% of outstandings at the end of 2008 and 1.25% of dollars transacted in 2008.²⁴ Only two credit unions (Navy FCU and Pentagon FCU) had more than a billion dollars in credit card outstandings at the end of 2008.²⁵

The dominance of large institutions in the card issuance market is a function of the economies of scale in the card business. State-of-the-art dynamic underwriting, fraud detection, rewards programs, national direct-mail advertising, and processing can all be highly automated, which involves substantial fixed costs that are feasible only when defrayed over large account and transaction volumes. Dynamic underwriting capability and fraud detection are essential for a backloaded, behaviorally triggered pricing model. Moreover, economies of scale also benefit issuers in terms of funding and liquidity. Larger depository issuers have deep pools of low-cost funds in the form of deposits and are also able to support off-balance-sheet securitization facilities that provide ongoing liquidity.

Most credit unions cannot compete successfully against large commercial banks and finance companies on the business model of backloaded pricing and economies of scale. By and large, credit union credit card operations are relatively small operations. Median outstandings, dollar amount transacted, and purchases are far smaller than for non-credit union card issuers (banks, thrifts, finance companies; see Figure 2). Credit unions lack the economies of scale for card processing and the resources to invest, at least individually, in the most sophisticated risk-management technology.

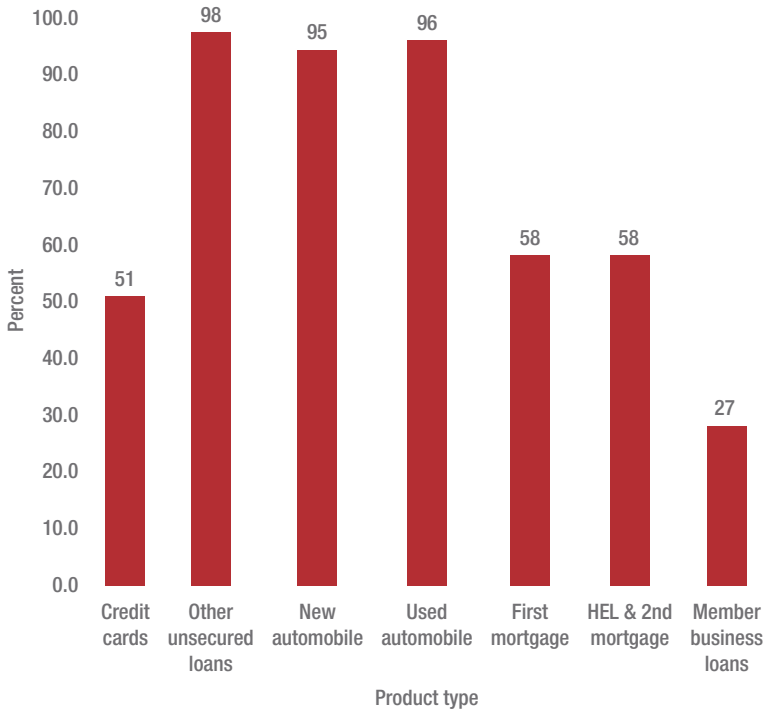
Although 47 of the 100 largest card issuers in the United States are credit unions, they accounted for only 1.76% of outstandings at the end of 2008 and 1.25% of dollars transacted in 2008.

Figure 2: Comparison of Credit Union and Bank Card Activity in 2008



Source: Nilson Reports, Issues 917, 918, and 919, 2009; author's calculations.

Figure 3: Percentage of Credit Unions Offering Product Type, Q1 2009

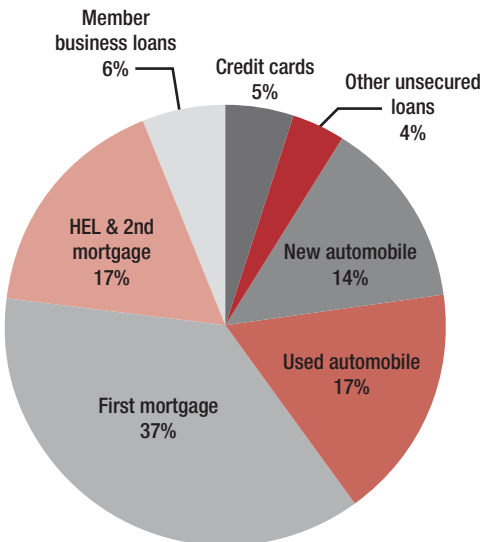


Source: CUNA, U.S. Credit Union Profile, May 28, 2009.

Credit cards are also not a core credit union product. For most credit unions, cards are not a profit center as much as a product offered as a service to members with the goal of retaining member loyalty to retain a deposit base for other types of lending. This allows credit unions some flexibility in their card business model that is not available to other financial institutions.

Only around half of credit unions offer credit cards, and credit cards make up only 5% of credit union lending, approximately \$32.72B outstanding on 12.6 million accounts as of the end of 2008, for an average balance of \$2,596²⁶ (see Figures 3 and 4). Credit unions that do offer cards tend to be larger, and credit cards make up a slightly larger percentage of their loan portfolio (see Figures 5 and 6).

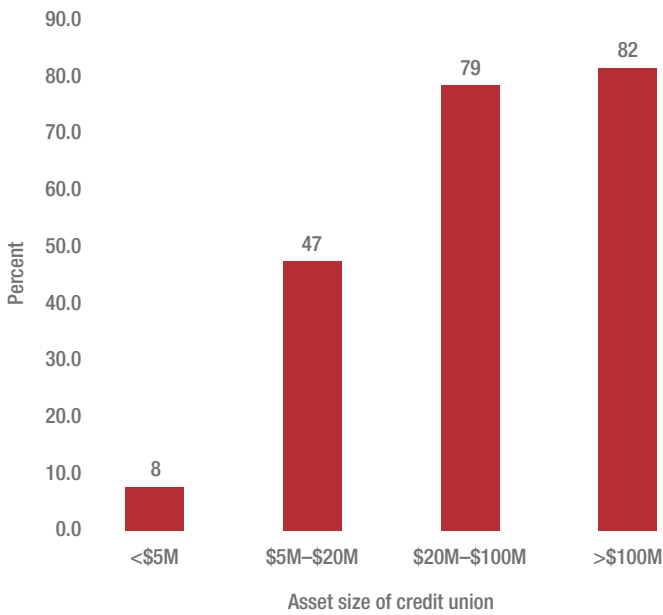
Figure 4: Credit Union Loan Portfolio Distribution, March 2009



Source: CUNA, U.S. Credit Union Profile, May 28, 2009.

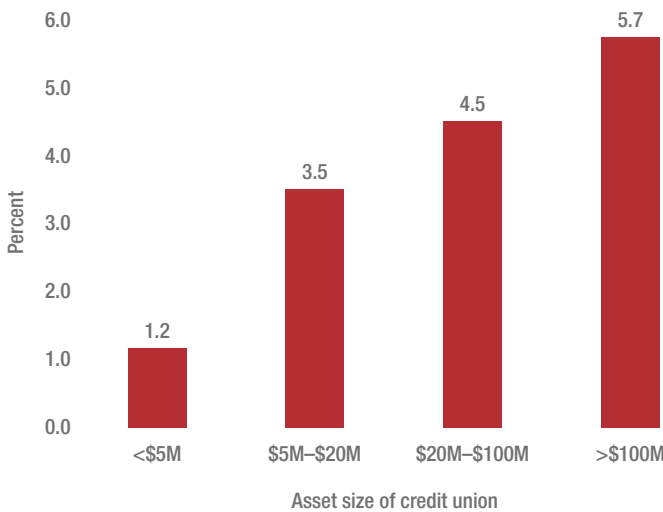
While credit unions have lower delinquency rates for their cards than bank issuers do, cards have the highest delinquency and net charge-off rates of any type of credit union loan product (see Figure 7). Nonetheless, credit cards remain an attractive product for many credit unions to offer because they are a loyalty device. A higher percentage of members have their credit union's credit card than any other credit union loan product (see Figures 8 and 9). The card is also the only credit union product that the member is likely to use on a daily basis; once a mortgage loan or auto loan is closed, the member merely makes payments. With a credit card, however, the member will keep making transactions on the account, cementing an ongoing lending relationship. Credit unions tend to have fewer dormant accounts than non-credit union issuers, indicating greater product loyalty among credit union cardholders²⁷ (see Figure 10).

Figure 5: Percentage of Credit Unions Offering Credit Cards by Asset Size, Q1 2009



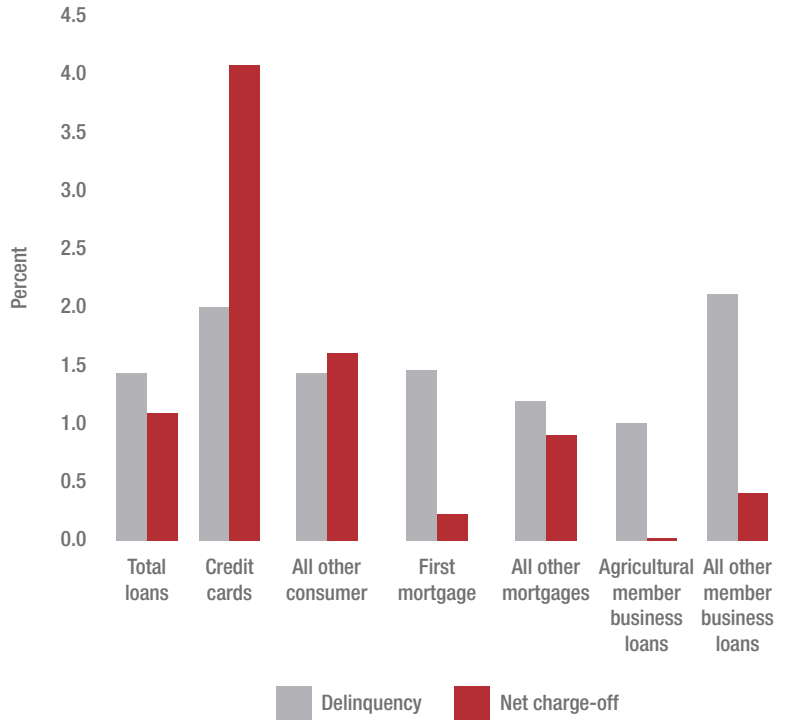
Source: CUNA, U.S. Credit Union Profile, May 28, 2009.

Figure 6: Credit Card Percentage of Loan Portfolio by Credit Union Size, March 2009



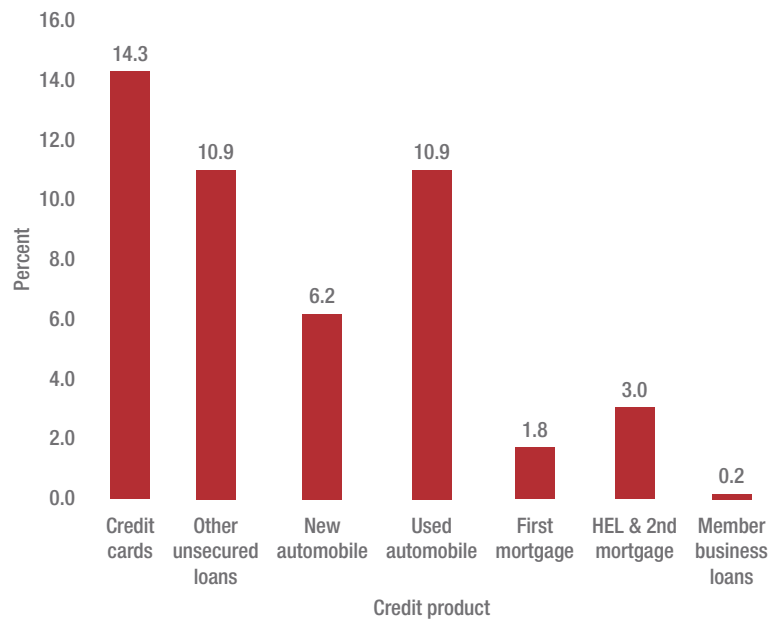
Source: CUNA, U.S. Credit Union Profile, May 28, 2009.

Figure 7: Delinquency and Net Charge-Off Rates, Q1 2009



Source: CUNA, U.S. Credit Union Profile, May 28, 2009.

Figure 8: Credit Product Penetration of Members, Q1 2009



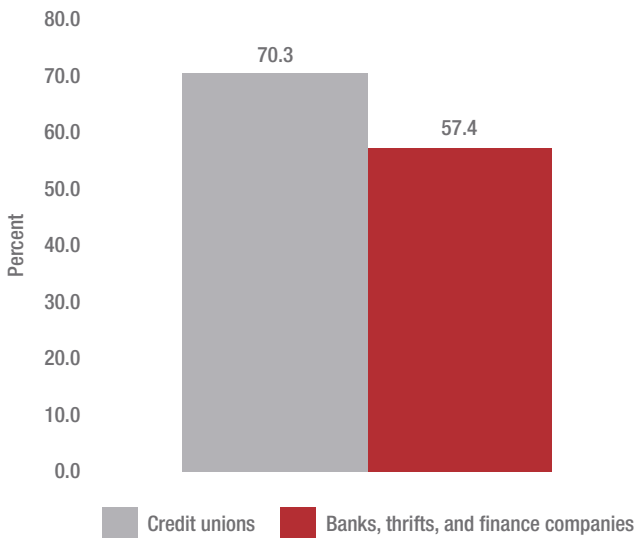
Source: CUNA, U.S. Credit Union Profile, May 28, 2009.

Figure 9: Credit Card Penetration of Members by Credit Union Size, Q1 2009



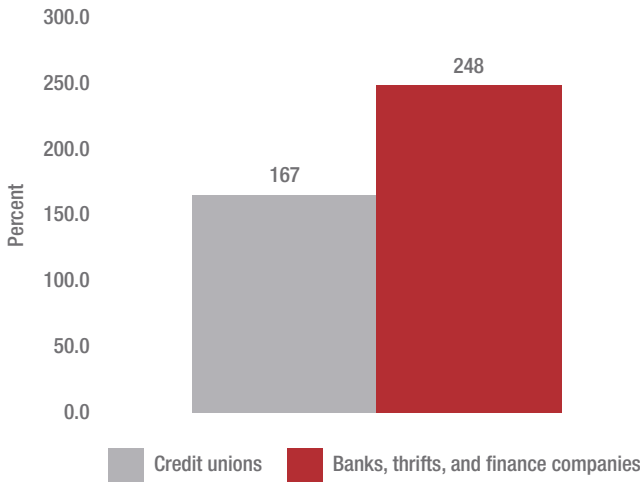
Source: CUNA, U.S. Credit Union Profile, May 28, 2009.

Figure 10: Median Percentage of Card Accounts Active in 2008



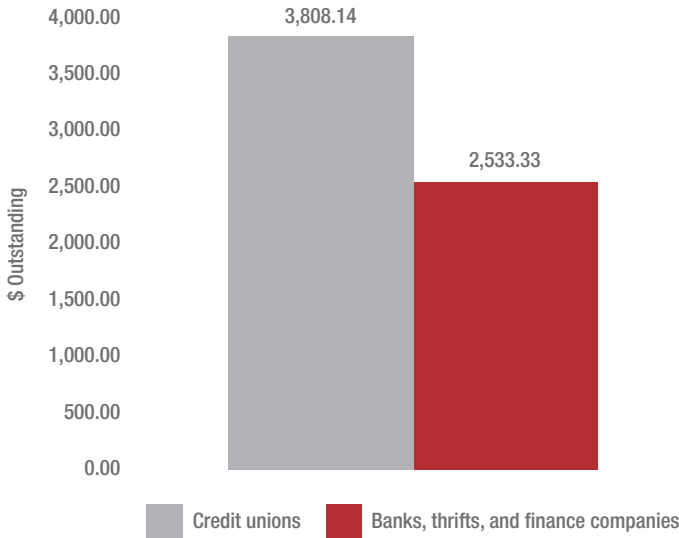
Source: Nilson Reports, Issues 917, 918, and 919, 2009; author's calculations.

Figure 11: Median Turn Rates (Purchase Volume to Outstandings), 2008



Source: Nilson Reports, Issues 917, 918, and 919, 2009; author's calculations.

Figure 12: Median Outstandings per Active Account, 2008



Source: Nilson Reports, Issues 917, 918, and 919, 2009; author's calculations.

Card usage by credit union members also appears to have patterns different from those of cardholders of other institutions. Median turn rates—a measure of purchase volume to outstandings—are significantly lower for credit union card issuers than for other issuers (see Figure 11). This indicates that all else being equal, interchange income is a less central revenue source for credit unions than interest revenue. Not surprisingly, the median balance outstanding for credit unions at the end of 2008 was \$3,808.14, whereas for non-credit union issuers it was \$2,533.33 (see Figure 12). Credit union cardholders carry larger balances on average than bank cardholders. Default rates on credit union card accounts, however, are substantially lower. This suggests that credit union cardholders are more reliable revolvers who are therefore more likely to be price sensitive than sporadically revolving cardholders. This could indicate that credit union membership reflects a self-sorting of consumers based on credit price sensitivity.

Challenges and Opportunities for Credit Unions

Many card industry observers believe that “size will become a more pronounced advantage for credit card issuers, and not just from a branding perspective . . . [but also because] large issuers’ sophisticated systems for determining creditworthiness and more-efficient back-office operations will

become crucial in eking out profit in the increasingly constrained credit card industry. . . .”²⁸ Credit unions are at a disadvantage when they attempt to compete with large banks and finance companies on business models that require economies of scale and are centered around backloaded, behaviorally contingent pricing.

For credit unions to compete successfully in the card space, a two-part strategy is needed. First, credit unions would do well to focus on their traditional strengths and concentrate on developing a niche in straightforward, accessible, plain-vanilla card products. For most credit unions, credit cards are not a profit center as much as a service offered to members in order to retain deposit loyalty. This creates economic room for credit unions to stand behind simple, no-hidden-fees cards that strive for customer satisfaction not through rewards programs and credit insurance products with added on bells and whistles, but through transparent and fair costs and terms. As Mark Meyer and Luis Dopico have noted, “The key credit union attraction for many customers will likely remain their offering relatively simpler products with fewer fees.”²⁹ A user-friendly card business model that emphasizes simplicity and transparency is a way for credit unions to establish a market share among consumers frustrated with large bank issuers’ billing tricks and traps.

While the Credit C.A.R.D. Act will limit some of those tricks and traps, it will also incentivize large issuers to come up with new ones. Indeed, a central goal of major card issuers is to maintain product complexity in order to frustrate comparison shopping among cards on the basis of net cost. At their core, credit cards are a commodity product, and transparent, simple price structures would result in greatly reduced profit margins. Complexity is essential for maintaining product profitability, but it also has the effect of alienating a substantial number of consumers who want a simple, transparent product. This is the demographic that credit unions should target for their card products, and cards may provide an entry point for developing a broader financial services relationship.

Credit unions would do well to focus on their traditional strengths and concentrate on developing a niche in straightforward, accessible, plain-vanilla card products.

The moment is ripe for such a move. The credit crisis has led to a retrenchment in the card industry, particularly from large issuers. This retrenchment is likely to be exacerbated by the Credit C.A.R.D. Act as issuers respond to limitations on risk-based repricing by limiting lines and raising rates preemptively. Smaller issuers like credit unions have generally been more careful with their underwriting because they have expanded their portfolios less aggressively. Accordingly, they are not overly exposed on credit card risk. Moreover, smaller issuers have largely operated within the C.A.R.D. Act’s constraints for years;³⁰ the Credit C.A.R.D. Act does not provide nearly as much of a shock to credit unions’ card operations as it does to banks’. Therefore, as the large issuers that dominate the card market

cut customers' lines and raise rates and fees, smaller issuers have an opportunity to pick up the large issuers' disgruntled customers.

To be sure, small issuers like credit unions will need to be careful about the potential adverse selection issues in picking up cardholders who are unhappy with their existing issuer because of reduced lines or increased rates. Credit unions also face a difficulty in that card issuance is available only for members, so in order to issue a card, a share purchase must also be made. The share purchase, however, may well serve as a type of screening; the self-selection bias in credit union membership may well reduce their card portfolio risk. It also means that credit unions cannot engage in expensive direct-mail campaigns to solicit card accounts. Moreover, as credit unions frequently have multiple-product relationships with their members, they have a more robust basis for underwriting.

The second part of the credit union card strategy should be to focus on developing economies of scale through cooperative ventures

within the industry. Credit unions do not necessarily compete with other credit unions for members; instead, competition is typically with other types of financial service providers. This means there is room for credit

The second part of the credit union card strategy should be to focus on developing economies of scale through cooperative ventures within the industry.

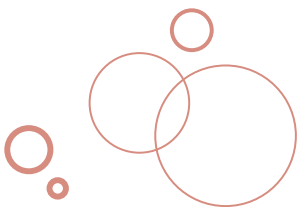
unions to invest in joint ventures and cooperatives for card processing and even underwriting operations that can provide them with economies of scale that defray technology costs.

Credit unions' ability to compete in the card space depends on recognizing that they can offer a different business model than that of the large bankcard issuers. Product differentiation is key. Rather than offering complex, multifunctional products with opaque pricing, designed to generate profits based on a requisite level of late payments by consumers, credit unions can stake out a solid part of the market by emphasizing simple, transparent card products that offer credit at a reasonable, clearly presented price, and by developing economies of scale through cooperative ventures that allow efficiencies to be passed along to members in the form of lower prices.

1. Credit Card Accountability, Responsibility, and Disclosure Act, §§ 101(b), (d) (2009).
2. *Id.* § 101(b).
3. *Id.* § 101(b).
4. *Id.* § 101(a)(1).
5. *Id.* § 102.
6. *Id.* § 102.
7. *Id.* § 105.
8. *Id.* § 102(b).
9. *Id.* § 102(b).
10. *Id.* § 104.
11. *Id.* § 104.
12. *Id.* § 106(b).
13. *Id.* §§ 201–205.
14. *Id.* §§ 301–305.
15. *Id.* § 101(c).
16. Cardweb.com (Bank Credit Card Annual Pre-Tax Profits).
17. Robin Sidel, *Charge-Offs Start to Shred Card Issuers*, WALL ST. J., December 11, 2008, at online.wsj.com/article/SB122895752803296651.html. Historically, around 20% of 60–89-day delinquent debt is charged off. Recently, roll rates have been higher. *Id.*
18. Kate Fitzgerald, *Small Issuers' Last Stand?* CARDS&PAYMENTS, August 2009, at 19.
19. Maria Aspan, *Law Hits Home as Cards Opt Out of Overlimit Fees*, AM. BANKER, August 10, 2009, at 1.
20. Maria Aspan, *Annual Fees: Citi Takes Leap*, AM. BANKER, August 14, 2009, at 1; Maria Aspan, *Beyond Rate Hikes: How New Law Reshuffles Cards*, AM. BANKER, May 26, 2009, at 1.
21. 12 U.S.C. § 1757(5)(A)(vi) (15% limit, with permission for the NCUA to raise temporarily). The NCUA has raised the limit to 18% continuously since 1987. Statement of The Honorable Joann M. Johnson, Chairman, National Credit Union Administration, “Regulation Z and Credit Card Disclosure Revisions” before the Subcommittee on Financial Institutions and Consumer Credit, U.S. House of Representatives, June 7, 2007, at 14.
22. *Id.* at 14; 12 C.F.R. § 701.21(b)(7); NCUA Letter 09-FCU-05 (July 2009); NCUA OCG Opinion Letter 00-1217, January 25, 2001 (noting that “NCUA has generally looked to the

Federal Reserve System's Regulation Z, implementing the Truth in Lending Act, for guidance on what constitutes a finance charge. 12 C.F.R. 226; 15 U.S.C. §1605. Transaction fees are specifically included among the examples of finance charges in Regulation Z. 12 C.F.R. §226.4(b)(2)."); NCUA OGC Opinion Letter Nos. 91-0412 (late charges are not considered a finance charge by the NCUA for usury cap purposes; it is unclear if this opinion letter would still hold after the Supreme Court's ruling in *Smiley v. Citibank*, 517 U.S. 735 (1996), which held that late fees were reasonably included in the definition of interest in the regulations of the Office of the Comptroller of the Currency), www.ncua.gov/Resources/RegulationsOpinionsLaws/OpinionLetters/2000/00-1217.html.

23. Nilson Reports, Issues 917, 918, and 919, 2009; author's calculations.
24. *Id.*
25. Nilson Reports, Issue 917, 2009.
26. NCUA, 2008 Yearend Statistics for Federally Insured Credit Unions, www.ncua.gov/Resources/Reports/statistics/Yearend2008.pdf.
27. Lower dormancy rates might be a function of the requirement that accounts be closed when credit union membership lapses. See NCUA OGC Opinion Letter 00-0133, March 1, 2000.
28. Fitzgerald, *supra*, note 18, at 22.
29. Mark C. Meyer & Luis G. Dopico, *Credit Card Availability, Interest Rates, and Usage in 2005–2009, Consumer Finance Monthly Research Brief #4*, at 38.
30. Fitzgerald, *supra*, note 18, at 26.



ideas grow here

PO Box 2998
Madison, WI 53701-2998
Phone (608) 231-8550

www.filene.org

PUBLICATION #202 (11/09)

ISBN 978-1-932795-81-3

filene
RESEARCH INSTITUTE

