THE CREDIT CARD ACT OF 2009 WAS NOT ENOUGH: A NATIONAL USURY RATE WOULD PROVIDE CONSUMERS WITH THE PROTECTION THEY NEED.

I. INTRODUCTION

Ruth Owens, a holder of a credit card with a $1,900 limit issued by Discover, had a balance of $1,460.73 in January of 1996.[1] Ms. Owens did not use her card in the previous month but did incur monthly charges.[2] These charges included a fee for a product called CreditSafe Plus, which was supposed to put payment and finance charges on hold should Ms. Owens become disabled, hospitalized, or unemployed; Ms. Owens was on Social Security Disability and was unemployed when the card was issued.[3] Between January 1996 and February 1997, Ms. Owens did not make any purchases on the card and always made a payment towards her balance—although some payments were made late, which resulted in fees.[4] In February, 1997, Ms. Owens made her first transaction on the card in over a year-and-a-half with a $300 cash advance; at the end of the month the balance stood at $1,895.53.[5]

In May 1997, Ms. Owens made another payment, but because it was under the minimum amount due, she incurred a late fee that increased her balance to $1,962.82.[6] After making only one charge for $300 over the course of one year while making payments toward the balance, Ms. Owens' accrual of monthly charges and fees pushed her over her credit limit resulting in an additional charge.[7] Over the

1. *See* Discover Bank v. Owens, 822 N.E.2d 869, 871 (Ohio Misc. 2004).
2. *Id.*
3. *Id.* at 871–72. Apparently, the only time the credit protection product would provide any benefit was if Ms. Owens were to become hospitalized. *Id.* The product was of little benefit to Ms. Owens, but she was still sold the product and incurred a monthly fee for it. *Id.* at 872.
4. *Id.* at 872. In 2005, the average late payment fee was $33.64. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-06-929, CREDIT CARDS: INCREASED COMPLEXITY IN RATES AND FEES HEIGHTENS NEED FOR MORE EFFECTIVE DISCLOSURES TO CONSUMERS 18 (2006) [hereinafter GAO REPORT], *available at* http://www.gao.gov/new.items/d06929.pdf.
5. *See Owens*, 822 N.E.2d at 872.
6. *Id.* Paying less than the minimum balance on a credit card debt can result in a late fee. *Id.*
7. *Id.*

next six years, Ms. Owens did not use the card and continued to make payments toward her balance; but, because of charges and fees, the balance never fell below her limit of $1,900.[8] Over that six-year period, Ms. Owens made payments totaling $3,492.[9] One would assume those payments would be enough to satisfy the debt, considering that if the same payment were made on a $2,000 loan at a 21% annual percentage rate (APR), the debt would have been paid off.[10] However, when the credit card company filed a collection suit in May 2003, the company claimed Ms. Owens owed $5,564.28.[11]

The case of Ruth Owens is just one example of a consumer not using a credit card recklessly but nevertheless having fees and finance charges inflict financial ruin.[12]

Since the 1970s, consumers have become increasingly saddled with debt, which has led to an increase in bankruptcy filings.[13] During this same period, credit card issuers "began to introduce cards with a greater variety of interest rates and fees" while making card agreements more complex.[14] This combination led to an increase in the cost for a consumer to obtain credit, often unbeknownst to the consumer.[15] The Credit Card Accountability Responsibility and Disclosure Act of 2009 (Credit CARD Act), signed into law on May 22, 2009,[16] "was developed to implement needed reforms and help protect consumers by prohibiting various unfair, misleading and deceptive practices in the credit card market."[17] The reform was needed because situations similar to that of Ms. Owens were becoming common.[18]

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8. *Id.*
9. *Id.*
10. NAT'L CONSUMER LAW CTR., THE COST OF CREDIT: REGULATION, PREEMPTION, AND INDUSTRY ABUSES § 11.8.2.2, at 734 (4th ed. 2009) [hereinafter COST OF CREDIT].
11. *Owens*, 822 N.E.2d at 872.
12. *See, e.g.*, *In re* McCarthy, No. 04-10493-SSM, 2004 Bankr. LEXIS 2584, at *1–6 (Bankr. E.D. Va. July 14, 2004) (discussing a credit card consumer whom made $218.16 in purchases and made $3,058 in payments over a two-year period but saw the account balance increase from $4,888 to $5,357).
13. *See infra* Part III.B.
14. S. REP. NO. 111-16, at 3 (2009).
15. *See id.* at 4.
16. Credit Card Accountability and Disclosure Act of 2009, Pub. L. No. 111-24, 123 Stat. 1734 [hereinafter Credit CARD Act] (codified in scattered sections of 15 U.S.C.).
17. S. REP. NO. 111-16, at 2.
18. *See generally* Donna S. Harkness, *When Over-the-Limit Is over the Top: Addressing the Adverse Impact of Unconscionable Consumer-Credit Practices on the Elderly*, 16 ELDER L.J. 1, 2–4 (2008) (recounting the case of an elderly client who was represented by a student attorney while enrolled in the Elderly Law Clinic at the University of Memphis).

While the Credit CARD Act implemented some much needed regulation to alleviate the consumer debt burden, it did not go far enough. Credit card issuers are still able to exploit consumers' behavioral biases, thereby obscuring the cost of credit;[19] therefore, to effectuate the Act's intended purpose, a national usury[20] rate needs to be implemented. This comment argues that a floating national usury rate tied to the prime rate that would cap the interest rate that credit card issuers can charge consumers is necessary to carry out the Act's policy.

In the early years of credit card transactions, consumers were protected by state usury laws.[21] But the Supreme Court's interpretation of the National Bank Act[22] in *Marquette National Bank of Minneapolis v. First Omaha Service Corp.*[23] essentially preempted a state's power to enforce state usury laws against credit card issuers and deregulated the credit card market.[24] This decision, explored further in Part II,[25] is one of the reasons federal legislation, as opposed to state legislation, is needed to curtail many practices[26] employed by credit card issuers.

Part II of this comment explores the early history of credit cards and how the credit card marketplace has evolved in this country.[27] That part also discusses two Supreme Court decisions[28] that have enabled credit card companies to essentially avoid regulation on the interest and fees that can be charged to consumers.[29]

19. *See infra* Part III.C.

20. Usury is defined by *Black's Law Dictionary* as "the charging of an illegal rate of interest as a condition to lending money" and "[a]n illegally high rate of interest." BLACK'S LAW DICTIONARY 1685 (9th ed. 2009). "Usury laws are among the oldest form of economic and financial regulation." Steven Mercatante, *The Deregulation of Usury Ceilings, Rise of Easy Credit, and Increasing Consumer Debt*, 53 S.D. L. REV. 37, 39 (2008). Essentially, usury laws place a legal limit on the maximum allowable interest a lender can charge, if any at all. *See* Brian M. McCall, *Unprofitable Lending: Modern Credit Regulation and the Lost Theory of Usury*, 30 CARDOZO L. REV. 549, 554–58 (2008).

21. Mark Furletti, Comment, *The Debate over the National Bank Act and the Preemption of State Efforts to Regulate Credit Cards*, 77 TEMP. L. REV. 425, 430–31 (2004).

22. National Bank Act, 12 U.S.C. §§ 21–216d. (2006 & Supp. IV 2011).

23. Marquette Nat'l Bank of Minneapolis v. First Omaha Serv. Corp., 439 U.S. 299, 307–15 (1978).

24. *See id.* at 313, 318–19.

25. *See infra* Part II.B.1.

26. *See infra* Part III.A.

27. *See infra* Part II.

28. *See* Smiley v. Citibank (S.D.), N.A., 517 U.S. 735 (1996); *Marquette*, 439 U.S. 299.

29. *See infra* Part II.B.1–2.

Part III takes a look at the Credit CARD Act and the benefits it will provide consumers.[30] It then looks at the massive debt problem American society is currently facing.[31] Part III then delves into consumers' seemingly irrational behaviors when it comes to credit cards and how that behavior has been exploited by credit card issuers.[32]

Part IV explores legislative options that can be undertaken to help alleviate the consumer debt situation.[33]

II. THE EVOLUTION OF THE CREDIT CARD CULTURE IN AMERICA

The relative abundance of credit cards in the marketplace is a fairly recent development.[34] At the turn of the twentieth century, large scale department stores, such as Sears & Roebuck, introduced the concept of "credit cards."[35] Early cards allowed consumers to make purchases at the issuing store on credit; however, because most merchants demanded consumers pay off the cards by the end of the month, early "credit cards" were not a product that the masses had the ability to use.[36]

The modern credit card (i.e., a non-retail specific card issued by a third-party) was developed in the middle of the twentieth century.[37] The "Diner's Club Card," first issued in 1949, was the first card of its kind, a card that granted consumers "universal purchasing power offered by a third party."[38] With the introduction of the Diner's Club Card, credit cards were no longer retailer specific and consumers had greater purchasing ability.[39] Because of the success of the Diner's Club Card, other companies, such as American Express, entered the credit card market.[40] However, like the earlier retailer specific credit

30. *See infra* Part III.A.
31. *See infra* Part III.B.
32. *See infra* Part III.C.
33. *See infra* Part IV.
34. Kathleen M. Moore, *The Pending Credit Card Debt Meltdown: What's Happening in Your Wallet?*, 21 ST. THOMAS L. REV. 420, 421 (2009).
35. Mercatante, *supra* note 20, at 39–40.
36. *Id.* Early credit cards did not offer revolving debt. *Id.* at 40. Consumers still needed sufficient funds to pay off the entire debt on a monthly basis. *Id.*
37. Christopher L. Peterson, *Truth, Understanding, and High-Cost Consumer Credit: The Historical Context of the Truth in Lending Act*, 55 FLA. L. REV. 807, 865 (2003).
38. Mercatante, *supra* note 20, at 40.
39. *Id.*
40. *Id.*

cards, the balance of these cards had to be paid at the end of each month.[41]

In the late 1960s, the credit card industry experienced a boom with the advent of the Visa and MasterCard systems.[42] While Visa and MasterCard did not issue credit cards (or credit) to consumers, they organized networks of bank-issuers and entered into merchant agreements to facilitate credit card transactions.[43] The network of bank-issuers issued credit to consumers, and Visa and MasterCard handled the management and operation of the payment and card systems.[44] The merchant agreements were made so that a national entity, as opposed to a regional or local bank-issuer, was backing the card transaction.[45] By forming networks of bank-issuers and merchants, Visa and MasterCard provided consumers a card that could truly be used nationally.[46]

A. Development of Usury Laws

Throughout history, usury laws have had a presence in economic and financial regulation.[47] Limits on interest rates can be traced back as early as 2000 B.C. to a Mesopotamian kingdom.[48] Greeks and Romans denounced the practice of usury and implemented laws

41. Oren Bar-Gill, *Seduction by Plastic*, 98 NW. U. L. REV. 1373, 1382 (2004).

42. *Id.*

43. *See* Christopher C. DeMuth, *The Case Against Credit Card Interest Rate Regulation*, 3 YALE J. ON REG. 201, 207 (1986).

44. *Id.* Visa and MasterCard are known as "card associations." *See* GAO REPORT, *supra* note 4, at 73. When a consumer makes a purchase, the transaction is transmitted by the merchant to the card association. *Id.* The card association forwards the merchant request to the card issuer, who then clears the transaction. *Id.* The card association then pays the merchant after taking a fee from both the card issuer and merchant. *Id.*

45. Adam J. Levitin, *Priceless? The Economic Cost of Credit Card Merchant Restraints*, 55 UCLA L. REV. 1321, 1367 (2008). When the credit card market was in its infancy during the 1960s, many merchants were reluctant to take credit cards issued by banks outside of their state. *Id.* During this period, there were no banks with a national presence. *Id.* The formation of the Visa and MasterCard associations guaranteed credit cards would be accepted by their member merchants and gave cards the ability to be used nationally. *Id.* at 1367–68.

46. *Id.* Visa and MasterCard supply settlement, authorization, and other services to their bank-members and settle over a billion transactions annually. DeMuth, *supra* note 43, at 207.

47. Paul G. Hayeck, *An Economic Analysis of the Justifications for Usury Laws*, 15 ANN. REV. BANKING L. 253, 255 (1996). A purpose of usury laws is the protection of the borrower. COST OF CREDIT, *supra* note 10, at 3. Lenders and borrowers are often not on equal footing and the lenders' terms are often offered on a "take it or leave it" basis. *See id.*

48. Hayeck, *supra* note 47, at 255.

against it.[49] Because of this historical foundation, early English common law prohibited the charging of interest.[50]

During the founding of America, the English settlers brought the English common law, and, therefore, the concept of usury, to the American colonies.[51] Prior to America's independence, many colonies adopted usury statutes.[52] Massachusetts, in 1661, was the first colony to enact a usury statute and other colonies soon followed suit.[53] In many states, variations of these original usury laws are still in place today.[54]

In the twentieth century, when the credit card marketplace began to develop, these state usury laws governed credit card transactions.[55] Because each state enacted usury laws that were specific to its state and citizens, credit card issuers were faced with the challenge of dealing with an assortment of regulations.[56] Credit card issuers contended that having to deal with varied state regulations increased the costs of doing business.[57]

The lack of uniformity in state laws led to citizens of different states being treated differently with regard to credit products.[58] For example, American Express would need a different contract with different terms, and would have to charge a different interest rate for extending credit to a citizen of State A than it would for extending credit to a citizen of State B. Credit card issuers alleged that this problem led to an inefficient business model that was costly and not easily managed or operated.[59]

Faced with strict usury laws in each state, credit card companies turned to the federal courts for relief.[60] Two Supreme Court cases[61]

49. Mercatante, *supra* note 20, at 39.
50. Hayeck, *supra* note 47, at 255.
51. Mercatante, *supra* note 20, at 39.
52. *See* COST OF CREDIT, *supra* note 10, § 2.2.2, at 17.
53. Hayeck, *supra* note 47, at 256.
54. *See, e.g.*, MD. CODE ANN., COM. LAW § 12-102 (LEXISNEXIS 2005) (specifying the maximum interest rate to be six percent). *See also* COST OF CREDIT, *supra* note 10, § 2.2.2, at 17.
55. Bar-Gill, *supra* note 41, at 1381–82.
56. Mercatante, *supra* note 20, at 39–40.
57. *Id.* at 40–41.
58. *See id.* at 40.
59. Bar-Gill, *supra* note 41, at 1381, 1381 n.27.
60. *See, e.g.*, Marquette Nat'l Bank of Minneapolis v. First Omaha Serv. Corp., 439 U.S. 299 (1978).
61. *See, e.g.*, Smiley v. Citibank (S.D.), N.A., 517 U.S. 735 (1996); *Marquette*, 439 U.S. 299 (1978).

played a major role in deregulating usury laws and have enabled credit card issuers to reap tremendous profits.[62]

B. *The Supreme Court's Role in "Deregulating" the Credit Card Industry*

With the way the National Bank Act (NBA)[63] was drafted, credit card issuers saw an opportunity that would allow them to operate a more homogenous business practice and circumvent state usury laws.[64]

1. *Marquette National Bank of Minneapolis v. First Omaha Service Corp.*

In *Marquette*, First Omaha National Bank (Omaha Bank), a national banking association[65] with its charter address in Omaha, Nebraska, regularly solicited customers and issued credit cards to consumers in Minnesota as well as in its home state.[66] The two states had different usury limits; Minnesota allowed a maximum interest rate of 12%, while Nebraska allowed a maximum rate of 18%.[67] Omaha Bank charged its Minnesota customers the 18% rate allowed in Nebraska, the state in which it was chartered.[68]

Marquette National Bank of Minneapolis (Marquette) brought suit to enjoin Omaha Bank from soliciting business in Minnesota until it complied with Minnesota law.[69] Omaha Bank argued that because it

62. *See* CONSUMERS UNION, CREDIT CARD FACTS AND STATS 1 (2009) (stating that, in 2006, credit card issuers collected $115 billion in revenue and made $18 billion in profits).

63. National Bank Act, 12 U.S.C. §§ 21–216d (2006 & Supp. IV 2011). The NBA established "a federally chartered banking system" that created a federal banking system separate from and independent of state control. Furletti, *supra* note 21, at 427. The purpose of the NBA was to stabilize the economy during and after the Civil War. *Id.* The NBA allowed banks to establish a federal charter to avoid hostile state interference. *Id.*

64. *See infra* Part II.B.1.a.

65. A national bank is a bank chartered under federal laws as opposed to state laws. *See* Furletti, *supra* note 21, at 427.

66. Marquette Nat'l Bank of Minneapolis v. First Omaha Serv. Corp., 439 U.S. 299, 301–02 (1978).

67. *Id.* at 302.

68. *See id.* at 302–04.

69. *Id.* at 304. Marquette brought the suit because, to make up the profits it was "losing" to Omaha Bank, Marquette was forced to charge an annual fee. *Id.* People are more apt to choose a card with no annual fee and a higher rate rather than a card with any annual fee and a lower interest rate. *See* Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*, 157 U. PA. L. REV. 1, 35–36 (2008).

was a national bank, it was governed by federal law and, thus, the NBA.[70] The NBA stated that a national bank may charge "interest at the rate allowed by the laws of the State . . . where the bank is located."[71]

The issue in the case was the meaning of the term "located."[72] Omaha Bank argued that because it was chartered in Nebraska, it was "located" there for the purpose of the NBA.[73] Marquette, on the other hand, argued that because Omaha Bank continuously and systematically solicited credit card business in the state of Minnesota, Omaha Bank was "located" in Minnesota for the purpose of that particular credit card program.[74] The Court held that a national bank is "located" in the state identified on its organization certificate (i.e., the location of the bank's headquarters).[75] If the term were construed as Marquette contended, "the term 'located' would be so stretched as to throw into confusion the complex system of modern interstate banking."[76]

The Court's decision allowed national banks to "export" the interest rate of the state in which it is chartered to citizens of another state.[77] The Court viewed the exporting of credit card interest rates in the same vein as a citizen of one state crossing state lines to obtain a loan in another state.[78]

With the Court's interpretation of the term "located," the NBA "effectively preempted the interest rate regulations of the forty-nine states in which a card issuer could not actually be organized."[79]

a. The effect of the Marquette *decision*

With the Court ruling that credit card issuers could export the interest rates from their charter state to citizens of foreign states, the *Marquette* decision limited what states could do to protect their own

70. *Id.* at 308.
71. 12 U.S.C. § 85 (2006 & Supp. IV 2011).
72. Marquette Nat'l Bank of Minneapolis v. First Omaha Serv. Corp., 439 U.S. 299, 308 (1978).
73. *See id.* at 308.
74. *See id.* at 309–10.
75. *Id.* at 310.
76. *Id.* at 312. The Court stated that the "minimum contacts" argument could cause difficulties for national banks as to whether contacts with citizens of foreign states would be sufficient to alter the meaning of the term "located." *Id.*
77. *Id.* at, 318.
78. *Id.* However, because of mail and modern technology, the ability to obtain credit from another state is substantially easier than in the past. *Id.* at 318–19.
79. Furletti, *supra* note 21, at 431–32.

citizens from usurious interest rates.[80] States with no usury laws or with laws allowing high interest rates became prime locations for the headquarters of credit card issuers.[81] Within six years of the *Marquette* decision, eighteen states relaxed their usury laws and another sixteen repealed usury laws altogether.[82] Post *Marquette*, credit card issuers moved their operations to states with liberal or no usury laws and began to market cards nationally.[83] Because credit card issuers were able to export the rates of the state in which they were chartered, the "*Marquette* decision produced a functionally deregulated credit card market."[84]

2. *Smiley v. Citibank (South Dakota), N.A.*

In 1996, the Supreme Court issued another ruling that allowed credit card issuers "to increase their income stream even more dramatically."[85] Despite the ruling in *Marquette* that allowed credit card issuers to export the interest rates of their charter states, the foreign states seemingly still had the ability to control the fees that credit card issuers charged to consumers within their states.[86] In *Smiley v. Citibank (South Dakota), N.A.*,[87] a credit card issuer's ability to export fees was challenged.[88]

In *Smiley*, a resident of California had two credit cards that were issued by Citibank, a national bank located in South Dakota.[89] The credit card agreements allowed Citibank to charge for certain late fees that were permissible by South Dakota law but violated California law.[90] After being charged a late fee, Smiley brought suit, alleging the fee violated California state law and was "unconscionable."[91]

80. Bar-Gill, *supra* note 41, at 1382.
81. Vincent D. Rougeau, *Rediscovering Usury: An Argument for Legal Controls on Credit Card Interest Rates*, 67 U. COLO. L. REV. 1, 10 (1996).
82. *See* DeMuth, *supra* note 43, at 213.
83. Rougeau, *supra* note 81, at 10. Citibank, a national bank that was headquartered in New York, relocated its operation to South Dakota where there were no usury laws. DeMuth, *supra* note 43, at 215–16.
84. Bar-Gill, *supra* note 41, at 1382.
85. COST OF CREDIT, *supra* note 10, § 11.8.2.4, at 736.
86. *See* Alan S. Kaplinsky, *Federal Usury Law Developments*, 101 BANKING L.J. 663, 669–70 (1984).
87. Smiley v. Citibank (S.D.), N.A., 517 U.S. 735 (1996).
88. *Id.* at 737.
89. *Id.* at 737–38.
90. *Id.* at 738.
91. *Id.*

In analyzing whether the charging of the fee was permissible, the Court deferred to the Office of the Comptroller of Currency's (OCC)[92] definition of "interest."[93] The OCC stated:

> The term "interest" as used in 12 U.S.C. 85 includes any payment compensating a creditor or prospective creditor for an extension of credit, making available of a line of credit, or any default or breach by a borrower of a condition upon which credit was extended. It includes, among other things, the following fees connected with credit extension or availability: numerical periodic rates, late fees, not sufficient funds (NSF) fees, overlimit fees, annual fees, cash advance fees, and membership fees. It does not ordinarily include appraisal fees, premiums and commissions attributable to insurance guaranteeing repayment of any extension of credit, finders' fees, fees for document preparation or notarization, or fees incurred to obtain credit reports.[94]

In deferring to the OCC's definition, which encompassed a wide variety of fees, the Court looked only at whether the OCC's definition of "interest" was reasonable, not whether the interpretation represented the best possible interpretation.[95] The Court held that because the OCC's interpretation was not unreasonable, the fees stipulated in the definition were "interest" and could be exported.[96]

a. The effect of the Smiley *decision*

Under the Court's holding in *Smiley*, national banks have been able to export fees permitted by their charter states so long as the fees are considered "interest" under the OCC's definition.[97] The OCC's definition of "interest" includes many fees, "such as late payment, over-limit, cash advance, returned check, annual fees, and membership fees."[98] Like *Marquette*, *Smiley* eradicated a state's ability to protect its citizens from charges a credit card issuer can

92. The OCC is the agency granted power to regulate national banks. *See* 12 U.S.C. § 1 (2006 & Supp. IV 2011).
93. *Smiley*, 517 U.S. at 739–40.
94. 61 Fed. Reg. 4849, 4869 (Feb. 9, 1996) (codified at 12 C.F.R. § 7.4001(a) (2012)).
95. *Smiley*, 517 U.S. at 740, 744–45.
96. *Id.* at 746–47.
97. *See* Karen Mower, Note & Comment, Smiley v. Citibank (South Dakota), N.A.: *Banks Find "Interest" in Credit Card Late Payment Fees*, 1 N.C. BANKING INST. 169, 187 (1997).
98. COST OF CREDIT, *supra* note 10, § 11.8.2.4, at 736.

impose.[99] Credit card issuers have reaped huge rewards at the expense of consumers because of this decision.[100] Penalty fee revenue for issuers has increased from $1.7 billion in 1996 to $18 billion in 2007—a nine-fold increase since *Smiley* was decided.[101]

III. THE CURRENT CREDIT SITUATION AND THE IMPACT OF THE CREDIT CARD ACT

As credit cards have become more ubiquitous with minimal regulation,[102] consumers' irrational behavioral tendencies have been exploited by credit card issuers, thereby contributing to the massive consumer debt.[103] Credit card issuers have engaged in deceptive and unfair practices[104] that have led to the consumer debt steadily trending upwards since the *Marquette* decision.[105] As outstanding consumer debt has mounted, bankruptcy filings have increased.[106] And while consumers have been amassing debt in unprecedented amounts,[107] credit card companies are experiencing record profits.[108] The Credit CARD Act was enacted to protect consumers and address the vast consumer debt the American society is faced with.[109]

A. The Credit Card Accountability Responsibility and Disclosure Act of 2009

The Credit CARD Act was passed to "implement needed reforms and help protect consumers by prohibiting various unfair, misleading

99. Mower, *supra* note 97, at 188–89.
100. *See* COST OF CREDIT, *supra* note 10, § 11.8.4.1, at 742.
101. *Id.* After *Smiley*, credit card issuers grew their fee revenue by "making fees higher in amount, imposing them more quickly, and assessing them more often." *Id.*
102. *See supra* Part II.B.
103. *See supra* Part III.B–C.
104. *See Reforming the Practices of Credit Card Companies and Providing New Protections for Consumers: Hearing Before the S. Comm. on Banking, Hous., & Urban Affairs*, 111th Cong. 19–20 (2009) (statement of Travis Plunkett, Legislative Director, Consumer Federation of America).
105. *G-19 Release: Consumer Credit Outstanding*, BOARD GOVERNORS FED. RES. SYS., http://www.federalreserve.gov/releases/g19/HIST/cc_hist_r.html (last updated May. 7, 2012) [hereinafter *Consumer Credit Outstanding*] (providing monthly historical data of revolving consumer credit outstanding).
106. GAO REPORT, *supra* note 4, app. II at 86–87.
107. *See Consumer Credit Outstanding*, *supra* note 105.
108. *The Effect of Current Credit Card Industry Practices on Consumers: Hearing Before the S. Comm. on Banking, Hous. and Urban Affairs*, 110th Cong. (2007) (statement of Travis B. Plunkett, Legislative Director, Consumer Federation of America, Consumer Action and Consumers Union).
109. S. REP. NO. 111-16, at 2–4 (2009).

and deceptive practices in the credit card market."[110] Namely, the Credit CARD Act prohibits raising interest rates without any notice,[111] double-cycle billing,[112] universal defaults,[113] charging a higher rate of interest to an outstanding balance,[114] and raising rates within the one-year period after a card is issued to a consumer.[115] Additionally, the Credit CARD Act stipulates that all fees and penalties a credit card issuer charges must be "reasonable and proportional" to the violation.[116]

The Credit CARD Act has been hailed as the "greatest set of federal legislative enactments in history directed specifically at credit cards and the credit card industry."[117] The Act attempts to regulate the credit card industry through "substantive regulation of credit card terms and behavior, and regulation designed to improve disclosure to consumers."[118]

1. Key Components of the Credit CARD Act

a. Universal default and universal change in terms

Prior to the Act, credit card issuers' agreements with consumers allowed terms, including those relating to interest rates and other fees, to be changed for no reason and with little notice to the user.[119] Universal defaults allowed issuers to change card agreement terms because of circumstances wholly unrelated to the card.[120] Even if the cardholder had acted in accordance with the card agreement, issuers

110. *Id.* at 2.
111. *See* Credit CARD Act, § 101(a), 15 U.S.C. § 1637(i)(1) ("[A] creditor shall provide written notice of an increase in an annual percentage rate . . . not later than 45 days prior to the effective date of the increase.").
112. *Id.* § 102(a), 15 U.S.C. § 1637(j)(1) (prohibiting "double-cycle billing and penalties for on-time payments").
113. *Id.* § 101(b), 15 U.S.C. § 1666i-1(a) ("[N]o creditor may increase any annual percentage rate, fee, or finance charge applicable to any outstanding balance, except as permitted by [the ACT].").
114. *Id.* § 101(b), 15 U.S.C. § 1666i-1(c) ("[A] creditor shall not change the terms governing the repayment of any outstanding balance.").
115. *Id.* § 101(d), 15 U.S.C. § 1666i-2(a) (prohibiting any increase in the "annual percentage rate, fee, or finance charge . . . before the end of the 1-year period beginning on the date on which the account is opened").
116. *See id.* § 1665d(a) ("[A]ny penalty fee or charge that a card issuer may impose . . . [must] be reasonable and proportional to such omission or violation.").
117. Joseph U. Schorer, *The Credit Card Act of 2009: Credit Card Reform and the Uneasy Case for Disclosure*, 127 BANKING L.J. 924, 925 (2010).
118. *Id.* at 942.
119. GAO REPORT, *supra* note 4, at 33–36.
120. S. REP. NO. 111-16, at 4–5 (2009).

were able to increase the interest rates or fees because of a late payment on another account—including accounts for car payments, mortgage payments, or other credit cards.[121]

In addition to universal default clauses, many credit card agreements included an "Any Time, Any Reason" clause where issuers could change the terms of the contract at any time for almost any reason.[122] A 2008 survey indicated that 77% of issuers reserved the right to increase a card holder's interest rate at any time and apply the new rate on subsequent purchases as well the pre-existing balance.[123]

While universal defaults and "Any Time, Any Reason" clauses are not completely barred by the Act, the Act does provide consumers with protection relating to these practices.[124] Credit card issuers must notify card holders forty-five days prior to any change, and issuers must "maintain reasonable methodologies for assessing" whether an interest rate should be increased.[125] The Act also prohibits issuers from imposing a higher interest rate on existing balances.[126]

Consumers benefit because they must receive explicit notice of rate increases forty-five days prior to any change that affects the card's price.[127] Additionally, issuers cannot impose new, higher interest rates on balances from purchases that consumers have already made.[128] This allows consumers to rationally finance purchases through credit cards, because their interest rates cannot increase unpredictably and increase the credit cost and the total cost of the purchase.

b. Limits on interest rate increases

The Act places other restrictions on interest rate increases. Rates on newly issued cards cannot be raised within the first year.[129] However, promotional rates are exempt from this provision and can

121. *See* Jaclyn Rodriguez, *The Credit CARD Act of 2009: An Effective but Incomplete Solution Evidencing the Need for a Federal Regulator*, 14 N.C. BANKING INST. 309, 314–15 (2010).
122. S. REP. NO. 111-16, at 5.
123. *Id.*
124. *Id.*
125. Credit CARD Act, § 148, 123 Stat. 1734, 1737–38; Schorer, *supra* note 117, at 931–32.
126. Credit CARD Act § 171, 123 Stat. at 1736.
127. *See* Schorer, *supra* note 117, at 931–32.
128. *See id.* at 928–29.
129. Credit CARD Act § 101(d).

be increased after six months.[130] Whenever rates are increased, the Act requires issuers to review the rate increase "to assess whether . . . factors have changed" and to determine whether the interest rate should be reduced.[131] The Act states that issuers should consider "the credit risk of the obligor, market conditions, or other factors."[132] No other guidance is given on what an issuer must do in its evaluation, how it should document its evaluation, or that the rate should be lowered if certain criteria are met.[133]

This portion of the Act was likely targeted at curbing many of the prescreened solicitations and "teaser rates"[134] that card issuers advertise.[135] Card issuers would routinely send solicitations[136]—with low introductory rates and high "up to" credit limits[137]—to consumers who likely could not qualify for or receive such a low rate or high credit limit (i.e., individuals with poor or no credit histories).[138] When the consumer actually applied, the credit limit on the card received was lower and the interest rate higher than the applicant expected.[139] And when the consumer received the card with terms that were much worse than expected, that consumer could not decline the card and start searching for a new card because multiple credit requests can lower the consumer's credit score.[140] A lower credit score means the consumer is less likely to get another card.[141]

130. *Id.* The Federal Reserve Board of Governors is tasked with defining "promotional rate." *Id.*

131. Credit CARD Act, § 101(c), 123 Stat. 1734, 1737–38.

132. *Id.*

133. The Act specifically states that "[t]his section shall not be construed to require a reduction in any specific amount." *Id.* § 148(c).

134. Teaser or introductory rates are offers, typically unsolicited, of a low interest rate for an initial period of time. *See* Bar-Gill & Warren, *supra* note 69, at 50–51. After the introductory period, the interest rate increases. *Id.* at 51. Consumers feel they will not need to borrow past or will switch cards after the introductory period ends. *Id.* More than a third of consumers pick a card for the teaser rate but often never switch once the rate increases. *Id.*

135. *See* Schorer, *supra* note 117, at 932.

136. *See* Mechele Dickerson, *Vanishing Financial Freedom*, 61 ALA. L. REV. 1079, 1102 (2010).

137. An "up to" credit limit is the card's maximum credit limit. OFFICE OF THE COMPTROLLER OF THE CURRENCY, U.S. DEP'T OF THE TREASURY, ADVISORY LETTER 2004–10, CREDIT CARD PRACTICES 2 (Sept. 14, 2004).

138. S. REP. NO. 111-16, at 6 (2009).

139. *Id.*

140. *Id.*

141. *Id.*

c. *Fees and double-cycle billing*

Double-cycle billing was a practice employed by about one-third of card issuers that computed finance charges on balances that had already been paid.[142] Under this practice, a consumer who paid only a portion of the outstanding credit balance when it was due would still be charged interest on the entire amount.[143] This practice increased a card holder's cost because interest was being charged and collected on portions of a balance that had already been paid.[144] This fee was hidden from consumers, and it was virtually impossible to determine that a balance was subject to double-cycle billing by simply looking at a statement.[145] With limited exceptions, this practice is now prohibited.[146] Consumers benefit because they can no longer be charged interest on a balance which they have paid.

B. *Increased Debt Load*

Over the last forty years, credit card use and the accumulation of consumer debt has increased rapidly.[147] Credit card agreements have become more complicated[148] and have higher, more complex fees.[149] At the same time, credit cards have grown in popularity.[150] In 1970, only 16% of households had a credit card, while that number stands at nearly 75% today.[151] In December 1978, the year of the *Marquette* decision, outstanding consumer debt stood at $48 billion.[152] In May 2009, when the Credit CARD Act was signed into law, outstanding consumer debt had risen to $910 billion.[153]

The growth in the use of credit cards has primarily been driven by two factors: convenience, cards acting as a substitute for cash and checks in transactions; and credit, cards acting as a substitute to other

142. GAO REPORT, *supra* note 4, at 28.

143. Schorer, *supra* note 117, at 932–33.

144. *See id.* at 933.

145. *See* S. REP. NO. 111-16, at 7 (2009).

146. *See generally* Credit Card Accountability Responsibility and Disclosure Act of 2009, Pub. L. No. 111-24, § 102(a), 123 Stat. 1734 (2009) (exceptions include instances where there is an adjustment to a finance charge as a result of a dispute or because of a return of a payment for insufficient funds).

147. *See Consumer Credit Outstanding*, *supra* note 105; Moore, *supra* note 34, at 241–42.

148. GAO REPORT, *supra* note 4, at 6.

149. *Id.* at 18.

150. *Id.* at 1.

151. S. REP. NO. 111-16, at 3.

152. *Consumer Credit Outstanding*, *supra* note 105.

153. *Id.* Outstanding consumer debt peaked in December 2008 at $989 billion. *Id.* In November 2010, debt stood at $807 billion. *Id.*

short-term loans.[154] In 2007, the average household made monthly charges of $889 on credit cards.[155] Nearly half of all card holders carry some debt over from month to month.[156]

In the 1990s, after the *Smiley* decision, credit card issuers "began to introduce cards with a greater variety of interest rates and fees, and the amounts that cardholders can be charged have been growing."[157] As card fees and rates became more complex, the Government Accountability Office (GAO) found the need for heightened regulation and more effective disclosures to consumers.[158] As credit card agreements, fees, and interest rates have gotten more complex, they have been a major factor in the increase in consumer debt.[159] As debt has steadily accumulated for consumers, bankruptcy filings have increased.[160]

In 1980, the year after the *Marquette* decision, 287,000 consumers filed for bankruptcy.[161] Twenty-five years later, more than two million consumers filed for bankruptcy.[162] While credit card usage cannot be solely responsible for the 600% increase in bankruptcy filings over the twenty-five year period, it has been a factor.[163]

154. Todd J. Zywicki, *The Economics of Credit Cards*, 3 CHAP. L. REV. 79, 83 (2000).
155. KEVIN FOSTER ET AL., FED. RESERVE BANK OF BOS., NO. 09–10, THE 2008 SURVEY OF CONSUMER PAYMENT CHOICE 7 (2008), *available at* http://www.bos.frb.org/economic/ppdp/2009/ppdp0910.pdf.
156. Brian K. Bucks et al., *Changes in U.S. Family Finances from 2004 to 2007: Evidence from the Survey of Consumer Finances*, 95 FED. RES. BULL. (February 2009).
157. S. REP. NO. 111-16, at 3 (2009).
158. *See* GAO REPORT, *supra* note 4, at 77–79.
159. *Id.* at 1–7.
160. *See id.* app. II. at 86–87; *Consumer Credit Outstanding*, *supra* note 105.
161. GAO REPORT, *supra* note 4, at 56.
162. *Id.* at 86.
163. *Id.* at 56–57.

C. Behavioral Analysis of Credit Card Usage and How Consumers Are Impacted[164]

A former general counsel of Citigroup once stated that "[n]o other industry in the world knows consumers and their transaction behavior better than the bank card industry. It has turned the analysis of consumers into a science rivaling the studies of DNA . . . ."[165] The nature of the credit card agreement and the knowledge credit card issuers obtain regarding consumer behavior place issuers in a position where they are able to exploit consumers' irrational tendencies.[166] As highly sophisticated and well-capitalized companies, credit card issuers are in position to exploit consumers' behavioral biases with little resistance.[167]

By analyzing and utilizing virtually all consumer transaction data,[168] credit card issuers are able to closely track consumer behavior and exploit irrational tendencies.[169] This exploitation of consumer behavior is a factor in the ever-increasing consumer debt burden.[170] Because of minimal regulation and oversight of credit cards, issuers have been able to implement practices that hide the true cost of credit from consumers.[171] In a well-functioning market with rational

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164. The behavioral analysis discussed in this section is brief and intended to lay a basic foundation for a behavioral economic analysis of credit cards. For more detail on the behavioral economics, consult the following sources: Bar-Gill, *supra* note 41, at 1395–1402; Susan Block-Lieb & Edward J. Janger, *The Myth of the Rational Borrower: Rationality, Behavioralism, and the Misguided "Reform" of Bankruptcy Law*, 84 TEX. L. REV. 1481 (2006); Christine Jolls, Cass R. Sunstein & Richard Thaler, *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471 (1998); Angela Littwin, *Beyond Usury: A Study of Credit-Card Use and Preference Among Low-Income Consumers*, 86 TEX. L. REV. 451 (2008); Maurice E. Stucke, *Money, Is That What I Want?: Competition Policy and the Role of Behavioral Economics*, 50 SANTA CLARA L. REV. 893 (2010).

165. Duncan A. McDonald, Viewpoint, *Card Industry Questions Congress Needs to Ask*, AM. BANKER, Mar. 23, 2007, at 10.

166. *See* Peter A. Alces & Michael M. Greenfield, *They Can Do What!? Limitations on the Use of Change-of-Terms Clauses*, 26 GA. ST. U. L. REV. 1099, 1099–1106 (2010). Further, twelve credit card issuers control over 80% of the market. *Id.* at 1129 & n.83.

167. *See* Bar-Gill & Warren, *supra* note 69, at 33.

168. *See id.* at 23–24. In May of 2003, there were approximately 2.3 billion credit and debit card transactions. GAO REPORT, *supra* note 4, at 14.

169. Bar-Gill & Warren, *supra* note 69, at 23–24.

170. *See id.*

171. *See id.* at 23–25.

consumers, regulation would not be needed.[172] However, credit card consumers display irrational behavior, which justifies additional regulation.[173]

1. Imperfect Self-Control

Many consumers enter into credit card agreements with the intention not to overspend.[174] However, credit cards separate consumers from their money and minimize the "pain of paying."[175] Without the pain of spending, consumers lose touch with the money they are spending.[176] A credit card separates the decision to obtain a credit card from the decision to spend on credit.[177] Because credit cards are open-ended loans, the only thing stopping consumers from exceeding their own pre-set spending limit is their own self-control.[178]

When consumers enter into credit card agreements with the expectation that they will simply be convenience users and not revolve a debt, they do not pay much attention to interest rates.[179] Consumers who do not plan to carry a balance look almost exclusively at card benefits and the annual fee charged rather than the interest rate and penalty fees.[180] Such incentives are designed to encourage consumers to increase their credit use.[181]

2. Hyperbolic Discounting

The theory of hyperbolic discounting provides an answer to why a consumer would spend more than initially anticipated.[182] A hyperbolic discounter "discounts costs and benefits that will materialize in the near future, . . . but assigns only a smaller additional discount for costs (and benefits) that will materialize in the

172. *See* Zwicki, *supra* note 154, at 110–29 (arguing that the credit card market is competitive, and thus well-functioning).
173. *See* Bar-Gill & Warren, *supra* note 69, at 1–8.
174. Bar-Gill, *supra* note 41, at 1395.
175. *Credit Cards Often Sell Us on Spending*, AM. PUB. RADIO (Feb. 3, 2009), http://www.marketplace.org/topics/business/credit-cards-often-sell-us-spending.
176. *See id.*
177. *See* Bar-Gill & Warren, *supra* note 69, at 33–34.
178. *See* Bar-Gill, *supra* note 41, at 1395.
179. Zywicki, *supra* note 154, at 101.
180. *Id.* at 101–02.
181. *See* Dickerson, *supra* note 136, at 1103.
182. Bar-Gill, *supra* note 41, at 1396.

more distant future."[183] Essentially, what this amounts to is a "present-biased" preference.[184]

Individuals inordinately prefer immediate rewards over greater future rewards or consequences.[185] For instance, a hyperbolic discounter "when offered the choice between $100 today and $110 tomorrow . . . will choose the $100 today because [the individual] discounts tomorrow's reward heavily compared to today's."[186] With credit cards, individuals obtain cards with an intention to use the card only in particular circumstances—for necessities or emergencies, for example.[187] But when the time comes to use the credit card, individuals focus on their immediate gratification and spend rather than consider the future consequences.[188]

3. Imperfect Information

Because consumers are in an unequal position compared to credit card issuers with respect to bargaining power and the ability to collect data, credit card issuers include terms and clauses that consumers do not know of or understand.[189] For example, many credit card issuers do not include the penalty interest rate to which a card can be increased, or what activities warrant a penalty.[190] For these reasons, it is difficult for consumers to effectively price credit cards and thus understand a card's true costs to them.[191] Without an understanding of how credit products work, namely how interest rates are applied and what fees a card has, consumers cannot evaluate the true cost of credit.[192] For example, in a nationwide survey by the Consumer Federation of America, it was found that 63% of respondents did not know that the APR was the primary indicator of a

183. *Id.* (emphasis omitted).
184. Angela Littwin, *Beyond Usury: A Study of Credit-Card Use and Preference Among Low-Income Consumers*, 86 TEX. L. REV. 451, 467 (2008).
185. W. Kip Viscusi, *Rational Discounting for Regulatory Analysis*, 74 U. CHI. L. REV. 209, 238–39 (2007).
186. Littwin, *supra* note 184, at 468.
187. *See* Bar-Gill, *supra* note 41, at 1395–97.
188. *See* Littwin, *supra* note 184, at 468.
189. GAO REPORT, *supra* note 4, at 33–51.
190. PEW HEALTH GRP., TWO STEPS FORWARD: AFTER THE CREDIT CARD ACT, CREDIT CARDS ARE SAFER AND MORE TRANSPARENT — BUT CHALLENGES REMAIN 21 (2010), *available at* http://www.pewtrusts.org/uploadedFiles/wwwpewtrustsorg/Reports/Credit_Cards/PEW-CreditCard%20FINAL.PDF?n=1231.
191. Bar-Gill & Warren, *supra* note 69, at 32.
192. *See id.* at 33–34.

loan's cost and that 30% did not even know what the letters meant.[193] Further, many card holders were not aware that they could exceed their maximum balance thereby resulting in an overage fee.[194]

Also, many consumers do not understand credit card agreements because of confusing and complicated language.[195] While the average adult in the United States reads at or below the eighth-grade level,[196] agreements are written at the tenth- to twelfth-grade level.[197] Additionally, not all fees that are charged by credit card issuers must be disclosed.[198] A failure to understand the credit agreement and the lack of awareness of potential fees creates an uncertainty of how much the credit card could cost the consumer.[199]

4. Discounting the Possibilities of Unforeseen Contingencies

Consumers often underestimate their future borrowing because of optimistic views of their own futures.[200] Credit cards, rather than savings, are being used as safety nets in low- and middle-income families.[201] Credit cards give families the impression of financial security, but, when families are encountered with an unforeseen contingency (e.g., losing a job, medical complication, or loss of a spouse), placing debt on credit cards can start a "downward financial spiral."[202]

D. The Credit CARD Act Does Not Provide Enough Protection

While the Credit CARD Act regulations are a step in the right direction to protecting consumers and easing the burden of debt our society faces, Congress should have taken a closer look at instituting

193. *Id.* at 30–31.

194. Many card holders thought that their card would be turned down if they attempted to make a purchase that exceeded their balance. *See* Rodriguez, *supra* note 121, at 309.

195. GAO REPORT, *supra* note 4, at 33–36.

196. *Id.* at 6.

197. *Id.* For example, the GAO found that one credit card agreement "used the term 'rolling consecutive twelve billing cycle period' instead of saying 'over the next 12 billing statements' or 'next 12 months.'" *Id.* at 46.

198. *Id.* at 35. If a consumer is not aware of a fee, there is no way that fee could be factored into the decision to borrow on a credit card.

199. *See id.* at 41–43, 46.

200. Bar-Gill, *supra* note 41, at 1400.

201. CTR. FOR RESPONSIBLE LENDING, THE PLASTIC SAFETY NET: THE REALITY BEHIND DEBT IN AMERICA 10–11, 16 (2005), *available at* http://www.demos.org/pubs/PSN_low.pdf.

202. *Id*. at 19.

a national usury rate to prevent credit cards from charging a "high"[203] rate of interest to consumers.

While Senator Bernie Sanders (Vermont (Independent)) proposed an amendment to the Credit CARD Act that would have established a national usury rate of 15%,[204] the amendment was handily defeated with little debate.[205] Despite Congress' reluctance to enact a national usury rate, there is ample evidence that consumers need more protection than what is provided in the Credit CARD Act, and a national usury rate would supply that protection.[206]

IV. REGULATION IN THE FORM OF A NATIONAL USURY RATE IS NEEDED

As explained in Part III, "[h]uman life is marked by fits of rational and irrational behavior."[207] This irrational behavior, in addition to credit card issuers' practices and contracts that can be indecipherable to the layperson, justifies additional regulation on credit cards. The Credit CARD Act took a step in the right direction by curbing some of the industry's most egregious practices.[208] But to battle the consumer debt situation, Congress needs to revisit the concept of usury laws that were prevalent in the formation and early era of this country.

In implementing usury laws, there are three logical options that Congress could pursue. First, Congress could amend the loophole in the NBA and give states the ability to regulate the interest rates being extended to their citizens.[209] Second, a national fixed rate could be implemented to apply to all states.[210] Or, third, a floating rate tied to the prime rate could be implemented so that the maximum interest

203. The term "high," when speaking on a rate of interest for a credit card, is relative. *See* Zywicki, *supra* note 154, at 99–100. However, it is hard to argue that a credit card with an interest rate of 79.99% is not "high." *See, e.g.*, Chuck Jaffe, *Credit-Card Issuers Find Creative Ways to Skirt New Law*, MARKETWATCH (Jan. 21, 2010, 12:01 AM), http://www.marketwatch.com/story/credit-card-firms-get-crafty-in-skirting-law-2010-01-21.

204. *See* 155 CONG. REC. S5351-65 (daily ed. May 12, 2009) (Senator Sanders proposing Amendment 1062 to the Credit CARD Act to establish a national usury rate).

205. 155 CONG. REC. S5423 (daily ed. May 13, 2009). The National Usury Rate amendment was defeated by a vote of 33 yeas to 60 nays. *Id.*

206. *See supra* Part III.

207. Rougeau, *supra* note 81, at 40.

208. *See supra* Part III.A.

209. *See, e.g.*, *supra* Part II.A.

210. *See, e.g.*, 155 CONG. REC. S5351-65 (daily ed. May 12, 2009).

rate "incorporates the economic reality of the ever-changing cost of money in the general economy."[211]

A. State Regulation

Amending the NBA so that states retake control of usury rates within their own borders is likely unworkable. Taking this action would be met with great resistance by the credit card and banking industry.[212] The entire industry would have to be reorganized. This would create many of the same problems the credit card industry encountered while it was in its infancy: state-by-state regulation and required compliance with the particular laws of each state.[213]

Additionally, the United States economy has become more national and "[i]n an era of interstate banking, uniform regulation of consumer credit products at the federal level may well be more efficient than a litany of consumer protection rules that vary from state to state."[214] In the current marketplace, state regulation would create a convoluted system in an era where the United States economy is more national than local.[215]

B. Federal Regulation—National Fixed Usury Rate

The second option, establishing a national usury rate, is a model that would provide consumers with needed protection, but it is not the best option. The main problem with this option is that it is not responsive to changing economic conditions.[216] However, if Congress were to go this route, the Credit Union Act provides a ready model that could be followed.[217] National Credit Unions are subject to a national usury rate established by statute[218] and subject to agency governance.[219]

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211. Rougeau, *supra* note 81, at 41.
212. *See, e.g.*, *supra* Part II.A.1. The credit card industry challenged state regulation in the federal courts and likely would oppose any regulation granting power back to the states. *See, e.g.*, *supra* Part II.A.1.
213. *See supra* Part II.
214. Bar-Gill & Warren, *supra* note 69, at 83.
215. *See id.*
216. *See* Zwicki, *supra* note 154, at 150–52.
217. Federal Credit Union Act, 12 U.S.C. § 1751 *et seq.* (2006 & Supp. IV 2011). It should be noted that credit unions are "nonprofit, cooperative financial institution[s] owned and run by [their] members," while credit card issuers and commercial banks are designed to operate in the free market and turn a profit. COST OF CREDIT, *supra* note 10, § 3.6.1, at 113.
218. 12 U.S.C. § 1757(5)(A)(vi).
219. *Id.* § 1757(5)(a)(vi)(I).

The Federal Credit Union Act, originally enacted in 1934, set forth legislation that, among other things, regulated the amount of interest a nationally chartered credit union could charge on a loan.[220] Currently, credit unions are statutorily permitted to charge a maximum interest rate of 15%.[221] However, the statute also grants power to the Federal Reserve Board of Governors (Board) to consult "with the appropriate committees of the Congress" to determine whether the interest ceiling should be raised because of circumstances threatening the "safety and soundness of individual credit unions as evidenced by adverse trends in liquidity, capital, earnings, and growth."[222] Since May 1987, the Board has set the maximum interest rate at 18%.[223]

While this option would provide consumers with protection from exorbitant interest rates, a fixed rate would not allow credit card issuers to adjust interest rates when the market so requires.[224] A problem with this option is that a regulation board would have to be created to monitor economic conditions and substitute a higher rate if the conditions so required.[225] Issuers would not, therefore, be able to quickly adapt to a changing market or economic conditions.[226]

C. Federal Regulation—National Floating Interest Rate

Establishing a national floating interest rate that is tied to the prime rate provides the best option for regulating credit card interest rates.[227] Tying the maximum allowable interest rate to the prime rate would allow an interest rate to adjust with the issuer's cost of doing business, which is somewhat dependent on the prime rate.[228]

220. Federal Credit Union Act, ch. 750, 48 Stat. 1216 (1934).

221. 12 U.S.C. § 1757(5)(A)(vi).

222. *Id.* § 1757(5)(A)(vi)(I).

223. *See* COST OF CREDIT, *supra* note 10, § 3.6.1, at 113 (citing Letter from NCUA to Federal Credit Unions No. 08-FCU-02 (Jan. 2008), http://www.ncua.gov/Resources/Documents/LFCU2008-02.pdf).

224. *See* Zwicki, *supra* note 154, at 150–52.

225. *See, e.g.*, 12 U.S.C. § 1757(5)(A)(vi)(I).

226. *See* Loan Interest Rates, 71 Fed. Reg. 42, 249 (July 26, 2006) (codified at 12 C.F.R. pt. 701); Zywicki, *supra* note 154, at 150–52.

227. ELIZABETH WARREN & AMELIA WARREN TYAGI, THE TWO INCOME TRAP: WHY MIDDLE-CLASS MOTHERS AND FATHERS ARE GOING BROKE 145 (2003).

228. Credit card issuers have three main costs in running their business: marketing costs, collection costs, and the cost to borrow money that is eventually relent to consumers. *Id.* at 148. Credit card lenders borrow from the Federal Reserve at the prime rate. *See id.* Credit card issuers then relend that money they have borrowed to consumers. *Id.*

Additionally, the prime rate is a benchmark rate and is used in other lending activities.[229]

By tying the maximum usury rate to an index, issuers will not suffer when economic conditions worsen and their costs of obtaining money rises.[230] Likewise, when issuers' costs to obtain money drops but the interest rate charged to a consumer does not correspondingly drop, issuers will not receive a windfall.[231] A majority of credit card issuers' profits come from interest charged on accounts.[232] Issuers profit when they loan money at a higher rate than what they obtain it for.[233] Tying a maximum interest rate to the prime rate would ensure that an issuer's cost of doing business—extending credit—did not fall below its cost of operations—obtaining money.[234] More importantly, if consumers are aware that their costs of borrowing on credit are tied to the prime rate, they could judge the costs of borrowing—or at least have a baseline pricing point—more effectively.[235]

To effectively carry out this policy, fees and all other charges must be included in the definition and calculation of interest.[236] Without calculating fees within the definition of interest, credit card issuers could circumvent an interest cap by creating and charging consumers new fees.[237] Including all fees within the definition of interest would also help consumers more effectively price the cost of credit. The OCC has already defined certain fees as interest.[238] By including fees in the calculation of interest, consumers could better assess the cost

229. *See, e.g.*, 15 U.S.C. § 1639c(a)(6)(D)(ii) (2006 & Supp. IV 2011) (tying the standards for a home mortgage loan to the prime rate).

230. *See* WARREN & TYAGI, *supra* note 227, at 148.

231. *Id.* Professor Warren explains just how significant an issuer's windfall can be by using the happenings of 2001, when the Federal Reserve lowered interest rates nine times during the course of the year. *Id.* While the Federal Reserve lowered interest rates, credit card issuers did not return the favor to their consumers. *Id.* The issuers did not change their business strategy: marketing and collection costs stayed the same and their credit products stayed the same. *Id.* at 148–49. Profits rose $10 billion. *Id.* at 149. Card holders received no benefits from the Federal Reserve's lowering of the interest rate; all holders did was transfer $10 billion in net worth to card issuers. *Id.*

232. GAO REPORT, *supra* note 4, at 67. Approximately 70% of credit card revenue comes from interest rates. *Id.* However, what is not clear is whether certain fees, which the OCC defined as interest in *Smiley*, are included in that calculation. *See id.* at 68–71.

233. *See id.* at 96–98, 104.

234. *See* WARREN & TYAGI, *supra* note 227, at 148.

235. This premise is based on the assumption that credit card consumers would be aware of the prime rate and that the maximum interest rate is tied to the prime rate. *See id.*

236. *See id.*

237. *See, e.g*, David Lazarus, *Grateful Citi Hits Us in the Wallet*, L.A. TIMES, March 9, 2010, at B1.

238. 61 Fed. Reg. 4849, 4869 (Feb. 9, 1996) (codified at 12 C.F.R. § 7.4001(a) (2012)).

of credit card borrowing.[239] This would minimize the imperfect information problem because no matter how complicated a credit card agreement is, consumers would know that all potential fees would be included in the calculation of interest.[240]

Many of those against the regulation of interest rates adhere to the free market principle.[241] They believe that people should have the free choice to obtain credit cards and that paternalistic regulation is against the American economic system;[242] that the credit card market is competitive and it will correct itself;[243] that consumers act rationally and regulation would impinge on their choice;[244] and that a deregulated market provides for lower costs and more choices of credit products.[245] However, these arguments assume the existence of a well-functioning credit card marketplace.[246] In an efficient market with rational consumers, regulation would be harmful.[247]

The problem with that argument is that credit card consumers have demonstrated irrational behavior when using credit card products.[248] The free-market detractors' argument against a national usury law is misplaced because of consumers' irrational behavior.[249] Because of the sheer volume of transactions that credit card issuers track, they likely know that consumers do not act rationally.[250] Issuers know that consumers can be exploited—because of either their irrational behavior or imperfect information on the credit products being offered—and the issuers create credit products to exploit the consumers.[251]

Implementing a floating usury rate would force credit card issuers to reevaluate their lending practices.[252] Overaggressive lenders would not be able to rely on the litany of fees and high interest rates

239. *See* WARREN & TYAGI, *supra* note 227, at 145, 148.
240. *See supra* Part III.C.3.
241. *See* DeMuth, *supra* note 43, at 242.
242. Zwicki, *supra* note 154, at 94.
243. *See* Kenneth C. Kettering, *True Sale of Receivables: A Purposive Analysis*, 16 AM. BANKR. INST. L. REV. 511, 544 (2008).
244. *See* Zwicki, *supra* note 154, at 98–99.
245. *See* WARREN & TYAGI, *supra* note 227, at 145.
246. *See* Bar-Gill & Warren, *supra* note 69, at 7.
247. *See* DeMuth, *supra* note 43, at 221.
248. *See supra* Part III.C.
249. *See supra* Part III.C.
250. *See supra* Part III.C.
251. *See supra* Part III.C.
252. *See* WARREN & TYAGI, *supra* note 227, at 145.

to make a profit.[253] Credit card issuers' current lending practices operate in a manner where the issuers know that some consumers will not be able to repay their loans, so a higher interest rate is charged to all card holders.[254] Issuers would have to more closely scrutinize whom they extended credit card products to and the amount of credit extended.[255] Because issuers would not be able to charge a "high" interest rate to individuals with marginal credit records, it would become unprofitable to extend credit to those in financial trouble.[256] When extending credit, issuers would not be able to rely on high interest rates as a safety net for bad loans and would have a greater incentive to determine what the card holders could actually repay.[257]

While a maximum interest rate would likely reduce the access consumers have to credit,[258] "that is not necessarily a negative development."[259] Consumers have been active participants in the credit card market, and their lack of self-control is a reason for the consumer debt burden.[260] However, a primary reason for the Credit CARD Act was to address the billions in outstanding consumer debt.[261] This increase in consumer debt coincided with the expansion of credit cards being offered and used.[262] Consumers have been receiving extensions of credit that they simply cannot afford.[263] A national floating usury rate would limit the amount of total credit being extended to consumers, and consumers' lack of self-control would be minimized because credit lines would not be great.[264] Consumers would not be able to run up as much debt on credit cards if lenders must scrutinize the amount of credit being extended and consumers have lower limits.[265]

253. *See* Dickerson, *supra* note 136, at 1109–10.
254. *Id.* at 1103; *see* Todd M. Finchler, *Capping Credit Card Interest Rates: An Immodest Proposal*, 12 ANN. REV. BANKING L. 493, 503 (1993) .
255. Mercatante, *supra* note 20, at 42, 44, 50–51.
256. *See* WARREN & TYAGI, *supra* note 227, at 147.
257. *See id.* at 148.
258. Rougeau, *supra* note 81, at 43.
259. *See id.*
260. *See* Dickerson, *supra* note 136, at 1103–04.
261. S. REP. NO. 111-16, at 3–4 (2009).
262. GAO REPORT, *supra* note 4, at 86.
263. *See supra* Part III.B.
264. *See* Carolyn Carter et al., *The Credit Card Market and Regulation: In Need of Repair*, 10 N.C. BANKING INST. 23, 46–47 (2006).
265. *See* Mercatante, *supra* note 20, at 50–51.

V. CONCLUSION

While the Credit CARD Act implemented some consumer protections that should benefit credit card users, to effectively carry out the policy, a national usury rate needs to be enacted. Consumers have demonstrated that they act irrationally when using credit cards.[266] Their irrational behavior has been exploited by credit card issuers, which has led to a dramatic increase of consumer debt over the last twenty-five years.[267] A national usury rate tied to the prime rate would provide consumers with much needed protection. Consumers would be able to better price the cost of credit, and issuers would have to engage in more prudent lending.

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266. *See supra* Part III.C.
267. *See* GAO REPORT, *supra* note 4, app. II at 86–87; *Consumer Credit Outstanding*, *supra* note 105.

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