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Representing Older Adults

National Consumer Law Center®

Advice for Seniors About Credit Cards

Credit card debt can cause tremendous financial problems for seniors. Credit card problems are a leading cause of consumer bankruptcy filings. Contrary to popular myth, huge credit card bills are not mostly due to irresponsible overspending. Many consumers resort to credit cards to meet pressing financial needs or due to an emergency. Others find themselves hopelessly in credit card debt due to snowballing finance charges, late fees, and other high fees.

This publication is designed to help elder advocates educate their clients on how to use credit cards wisely.

Credit Card Offers: Things to Consider

Credit card marketers mail consumers billions of offers annually. These offers can be very enticing. Some promise special terms, such as a low rate or no annual fee. Some lure consumers with offers of frequent flyer miles, cash back, freebies such as T-shirts and mugs or contributions to schools or favorite charities.

While credit card offers present pitfalls, just saying no may not be a practical solution. It is difficult to get by in our society without a credit card. A credit card may be necessary for travel, for transacting business over the Internet or to place orders by telephone.

But shopping around among competing credit cards can also be tough. Lenders may highlight low teaser rates, but bury in the fine print descriptions of expensive fees, high rates that take effect when teaser rates expire and other traps.

Because of abuses by credit card companies, Congress passed a new law in May 2009 called the Credit Card Accountability, Responsibility, and Disclosures Act or the "Credit CARD Act." The Credit CARD Act bans some, but not all, of the worst abuses by credit card companies.

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Suggestions to Keep in Mind When Reviewing Credit Card Offers

1. **Avoid accepting too many offers.** There is rarely a good reason to carry more than one or two credit cards. Consumers should be very selective. Too much credit can lead to bad decisions and unmanageable debts. Opening too many new credit card accounts can also lower credit scores.

2. **Beware subprime credit cards.** Instead of turning down consumers with bad credit, some lenders will offer them subprime credit cards. But cards offered to consumers with poor credit scores or without credit records generally come with very high interest rates, other expensive fees or low credit limits, and often include charges for unnecessary products such as "credit protection."

Avoid credit cards advertised as helping with bad credit. They are likely to be expensive, and often end up worsening the recipient's credit record.

Some lenders actually seek out stressed consumers with offers for "fee-harvester" cards that are so laden with front-end fees that a holder has almost no credit left to use to charge purchases. The Credit CARD Act passed in 2009 sought to stamp out fee harvesting by restricting fees to 25 percent of the credit extended, but that is still very pricey.

Sometimes lenders offer subprime credit cards as a trick to revive old debts from other credit card companies. Lenders buy up old debts, then offer debtors new credit cards and, when a new account is opened, slap an old debt on the new credit card account.

3. **Look carefully at the interest rate, but remember that it can change.** You should always know the interest rate on your cards and try to find the lowest rate possible. Credit card lenders usually have several interest rates for a credit card. They also constantly change their rates, although the Credit CARD Act bans some types of rate changes. Some important terms to understand are:

- APR** This is the interest rate expressed as an annual figure. Most cards have different APRs for purchases versus cash advances versus balance transfers and other types of transactions.
- Variable rates.** Most credit cards use variable rates, which change with the rise or fall of a common index rate (an example of a variable rate might be "U.S. Prime Rate plus 5%"). While variable interest rates can be very confusing, it is important to understand when and how rates change.
- "Teaser" rates.** A teaser rate is an artificially low initial rate that lasts only for a limited time. The Credit CARD Act requires that a teaser rate last at least six months. After that, the rate automatically goes up. A balance built up while a teaser rate is in effect will then grow at a much higher permanent rate.
- Penalty rates.** Many credit card contracts, including those that advertise low permanent rates, provide in the small print for an interest rate increase if the holder makes even a single late payment. The Credit CARD Act prohibits lend-

ers from imposing the higher rate on the holder's existing balance unless payment is more than 60 days late. But the new, higher rate will apply to future purchases and cash advances. Penalty rates may be added on top of late charges or other fees. For a consumer having financial problems, late charges and penalty interest rates increase the debt burden. Even in the absence of financial problems, avoiding missing payment dates by more than 60 days is important in order to avoid imposition of penalty rates.

4. **Fees, fees, fees.** Other terms of credit may be just as important as interest rates. Credit card companies now impose a myriad of fees – late fees, fees for exceeding a credit limit, annual fees, membership fees, cash advance fees, balance transfer fees, even fees for buying lottery tickets with a card – and keep raising these fees every year. These fees all add to the cost of a credit card, so that a card that appears cheaper with a low APR could end up being much more expensive.

5. **Look for the grace period.** Most credit cards offer a “grace period,” or period of time during which the amount of the purchase is not added to the credit card balance that incurs finance charges (cash advances usually don't have a grace period). Without a grace period, finance charges begin accruing immediately, and a low rate may actually be higher than it looks.

The grace period is critical if you intend to pay off the balance in full each month. Under the Credit CARD Act, lenders must mail monthly credit card statements at least 21 days before the end of the grace period. Longer grace periods benefit consumers. To avoid missing a deadline and incurring finance charges, a consumer should consider paying on-line or over the phone. The Credit CARD Act prohibits imposing a fee for paying over the phone except in cases where a consumer requires the help of a live customer service representative.

6. **Watch out for bait & switch offers.** Some credit card lenders advertise attractive, low-interest credit cards with high limits, but in the fine print reserve the right to substitute a less attractive, more expensive card if the applicant fails to meet certain conditions. The substituted card often has a higher interest rate, more expensive fees, and/or a lower credit limit.

7. **Always carefully review the disclosure box in the credit card offer, and compare it to the disclosure box received when the account is opened.** Lenders must make important disclosures about the terms of a credit card offer in a box, usually on the reverse side of or accompanying the credit card application. Review these carefully. If the disclosure box is on the reverse side of the application, make a copy.

When the credit card is sent out, it will come with another disclosure box. It is important to review this box, and compare it to the original disclosures. Make sure the terms of the offer – especially the APR – haven't changed.

It is also important to read the credit contract, which also comes with the card. If any terms are unclear, call the lender for an explanation. A cardholder who does not receive a satisfactory explanation should cancel the card.

8. **If a credit card has terms you do not like: Cancel!** There is no reason to keep a credit card if you don't like the terms. The Credit CARD Act gives a cardholder the right to reject changes in terms and instead close an account. Of course, if the card has been used, the holder will still need to pay off the balance.

How the New Credit Card Law Protects Consumers

As discussed above, the Credit CARD Act protects consumers against some of the worst abuses by credit card lenders. Significant protections include:

1. **Protections against rate increases for existing balances.** The Credit CARD Act prohibits credit card lenders from increasing the interest rate that applies to an existing balance on a credit card, a practice known as a "retroactive rate increase." Some exceptions to this rule are discussed below.

2. **Protections against rate increases for future transactions.** Lenders can raise interest rates for future purchases or transactions, but there are certain limitations:

Notice. Lenders must give written notice before increasing a rate. The increased rate will apply to any purchases or transactions that are made 14 days after the notice is sent. In addition, lenders must wait 45 days from sending the notice before it takes effect. However, no notice is required for increases due to one of the exceptions discussed below.

First-year ban. Lenders cannot raise any interest rates, including on future purchases and transactions, during the first year of an account unless one of the exceptions discussed below applies.

Review of rate increases. A lender that increases the interest rate on an account must review the account every six months and should decrease the rate if indicated by the review.

3. **Exceptions.** The Credit CARD Act has several exceptions to its rules prohibiting retroactive rate increases, rate increases during the first year of an account, and notice requirements. These exceptions include:

Variable rates. If a card carries a variable interest rate, the lender may raise the rate if the increase is solely due to an increase in the "index" rate, e.g., the prime rate.

Teaser rates. A lender may raise the rate after the expiration of a teaser rate, but only to the post-teaser rate previously disclosed. Also, teaser rates must last a minimum of six months.

Sixty days late. A lender may raise a rate if the card holder fails to make a required minimum payment within 60 days after the due date. Even then, the holder may get the old rate reinstated by making minimum payments on time for the next six months.

4. **Minimum payment protections.** When the prohibition against a retroactive rate increase applies, the Credit CARD Act limits how much the lender can increase the required minimum payment. The lender may either use the existing minimum payment terms, give the holder five years to pay off the outstanding balance at the old rate or increase the minimum payment to no more than twice as much of a contribution to paying down the balance as the old minimum payment.

5. **Limits on penalty fees.** The Credit CARD Act imposes new limits on penalty fees, such as late payment and over-the-limit fees.

Reasonable and proportional penalty fees. A penalty fee must be “reasonable and proportional” under rules issued by the Federal Reserve Board.

Over-the-limit opt-in. No over-the-limit fees may be charged unless the consumer has agreed that the lender may approve transactions that will exceed the credit limit.

Limitations on number of over-the-limit fees. Lenders may charge only one over-the-limit fee per billing cycle (usually one month). In addition, lenders may only charge the fee in the next two billing cycles unless the consumer uses the card again, or goes below the limit and then exceeds it again.

6. **Payment allocation.** Any amount paid above the minimum payment must be applied to the balance with the highest interest rate, except in the last two months before a deferred interest plan expires. (Deferred interest plans are discussed below).

7. **Prohibits unreasonable due date practices.** In the past, lenders often used tactics to trip consumers into paying late, so that the lender could impose a late payment fee or penalty rate. The Credit CARD Act prohibits these tactics by:

- Prohibiting credit card lenders from setting payment cutoff times earlier than 5:00 pm.
- Requiring payments due dates to be on the same day each month.
- If the due date falls on a weekend or holiday, requiring a payment received on the next business day to be considered timely.
- Requiring lenders to mail credit card statements at least twenty-one days before the due date or the end of the grace period.

Understanding Alternative Types of Credit Cards

Secured vs. Unsecured Credit Cards. All other things being equal, an unsecured card is preferable to a secured card. Since interest rates on secured cards are typically just as high as those on unsecured cards, the choice in favor of an unsecured card should be clear. Although most credit cards are unsecured, the discussion below lists different types of secured cards to watch out for.

Credit Cards Secured By Purchases. Some credit card lenders claim to take collateral in items purchased with their card. If a holder has problems making payments, those lenders may threaten to repossess property bought with the card. In addition, this collateral may affect a consumer's rights if he or she later needs to file bankruptcy. Most threats to repossess such personal property are not carried out because the expense of repossession outweighs the value of used property. Nevertheless, it is a good idea to use an unsecured card instead of a secured card whenever possible.

Credit Cards Secured By a Bank Account. Another type of secured credit card extends credit up to a limit equal to the amount the holder has on deposit in a particular bank account. If the holder fails to make the payments, he or she loses the money in the account. These cards are usually marketed as a way to establish a good credit record by allowing the holder to demonstrate the ability to make regular monthly payments.

Some secured credit cards may be useful for some who lacks any credit history at all - for example, a recent immigrant. However, someone with bad credit should carefully consider whether to choose a secured credit card. The secured card may be a subprime card with very high rates or fees, or other abusive features. These cards are often marketed to consumers with poor credit records as a way to "fix" their problems.

Credit Cards Secured By A Home. Some lenders offer credit cards in connection with a home equity line of credit. Each time the card is used, the balance is secured by the holder's home. In many cases, home improvement contractors offer these cards as a way to pay for home improvements. Sometimes the initial amount advanced is as much as the holder's credit limit.

Home secured credit cards are almost always a bad idea. Nonpayment may result in the loss of a family's home. Always beware of home improvement contractors offering credit. Borrower are likely to find more favorable terms by seeking a traditional home equity credit line from a bank at a lower interest rate.

Cashed Check Loans. Another credit offer to avoid takes the form of a check mailed by a credit card company. By cashing the check, a borrower not only accepts a high interest rate credit, but also gets stuck with a big balance on a new account right from the start. It is better to find a reasonable credit card offer and use the new card carefully. To borrow a large lump sum, try to get a bank loan instead.

Credit Cards vs. Debit Cards. Debit card transactions take money directly from the holder's bank account. Merchants accept debit cards, like credit cards, to pay for goods or services.

Although they often look the same, there are important differences between credit and debit cards. Use of a debit card results in the immediate withdrawal of money from a bank account. By comparison, use of a credit card, in effect, takes out a loan that must be repaid only when the credit card bill is due for payment.

Some debit cards with a VISA or MasterCard logo, when swiped at a point-of-sale device (e.g., a card reader at a grocery store or gas station), give the option of using the card as "credit" or "debit." But even if the credit option is selected, the card remains a debit card. By choosing "debit," the holder opts to provide a PIN (Personal Identification Number) to complete a transaction. By choosing "credit," the holder completes the transaction by signing his or her name on a receipt for identification. In both cases, money is immediately withdrawn from the holder's bank account.

There are advantages and disadvantages to using a credit card versus a debit card. Using a debit card reduces the risk of running up a big unpaid balance on a credit card. On the other hand, a credit card permits slower repayment – but with interest. That may provide useful flexibility to a cardholder on a tight budget who wants to make sure that the most pressing debts are paid first.

A holder's right to dispute charges are more limited with a debit card than with a credit card. For example, a charge for a vacuum cleaner that breaks within a week after being purchased from a nearby store may be disputed with the issuer of a credit card when a credit card was used in the transaction. (See the Consumer Facts publication "Your Credit Card Rights" for more information.) There are no similar rights when a debit card is used. A holder's responsibility for losses from a lost or stolen card can be much greater for a debit card than for a credit card.

Avoiding Problems: Things to Think About When You Use A Card

1. **Don't use credit cards to finance an unaffordable lifestyle.**
2. **In a financial bind, do not make it worse by using credit cards to make ends meet.** Finance charges and others fees will add to a debt burden. However, using a credit card in a period of financial difficulty is preferable to putting a home on the line by taking out a home equity loan.
3. **Don't get hooked on minimum payments.** Many credit card lenders have dropped their minimum payments to as low as 2% of the outstanding balance. Others have raised their minimum payments, sometimes to 4% of the balance, due to pressure from federal banking agencies. But making only the minimum payment will pay off a debt very slowly, if at all. For example, a \$1,000 credit card balance with an 18% interest rate will take nearly 8 years to pay off by making minimum payments of \$20 per month (and that's without making any more purchases with the card). It will take a little over four years to pay off that same debt by paying \$50 per month. The longer it takes to pay off the debt, the more interest the holder ends up paying.
4. **Don't run up the balance in reliance on a temporary "teaser" interest rate.**

5. **When it is affordable to do so, make credit card payments on time.** Avoid late fees and penalty rates.
6. **Avoid the special services, programs and goods that credit card lenders offer to bill to their cards.** Most of these special services – credit card fraud protection plans, credit record protection, travel clubs, life insurance and other similar offers – are bad deals.
7. **Don't Max Out.** Charging a credit card up to its limit is very risky. It's easy to get socked with high over-limit fees. Plus, a credit card account close to its limit will cause a big drop in the holder's credit score. This may even cause the lender to impose a penalty rate.

Advice When Behind On Credit Card Payments

1. **When in financial trouble, pay higher priority debts first.** Consumers should resist pressures to make credit card payments ahead of payments on a home or car that could be lost.
2. **Do not move credit card debt up in priority because the creditor threatens suit.** Credit card lenders are notorious for using aggressive debt collection agencies to collect from consumers. Resist their urgings to make credit card payments by using money set aside or in a budget for payments on a mortgage or car loan.¹
3. **If you can afford to pay something less than the full amount of your credit card debts, contact each credit card lender and try to make a payment arrangement which fits your budget.** The lender might also agree to waive fees, lower interest rates or otherwise change the terms to make payments more affordable.
4. **Never (or almost never) refinance credit card debt with a home loan.** Don't do it even for a lower interest rate or lower payments. Trading in credit card debt for a mortgage loan risks loss of a home if financial problems continue.
5. **Consider going to a credit counseling agency.** A reputable agency can help, but a choice must be made wisely. See the Consumer Facts publication "Tips on Choosing A Reputable Credit Counseling Agency" for advice on picking a credit counseling agency.
6. **Be wary of "Debt Settlement" and similar offers.** While it may make sense to approach a lender to seek relief or arrange more favorable terms for a credit card account, unscrupulous debt settlement services advertise aggressively and charge big fees to act as intermediaries between debtors and credit card lenders. Don't fall for empty promises! Remember that there are bad actors out there who only want debtors' money. Some get paid by creditors for help in locating debtors and sizing up their ability to pay.

1. For more information on budgeting and prioritizing debt, see National Consumer Law Center, Guide to Surviving Debt (2010 ed).



Additional Resources

National Consumer Law Center, *Truth in Lending* (7th Edition 2010).

National Consumer Law Center, *Guide to Surviving Debt* (2010 ed).

Consumer Action, Annual Credit Card Survey, available at www.consumer-action.org/news/articles/2010_-_2011_credit_card_survey/.

U.S. Public Interest Research Groups, "Truth About Credit" website, www.truthaboutcredit.org.

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