

A NATIONAL CONSUMER LAW CENTER REPORT

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FEE-HARVESTERS:  
LOW-CREDIT, HIGH-COST  
CARDS BLEED CONSUMERS

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November 2007

NATIONAL  
CONSUMER LAW  
CENTER



# FEE-HARVESTERS: LOW-CREDIT, HIGH-COST CARDS BLEED CONSUMERS

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A Report by the National Consumer Law Center  
Rick Jurgens, Consumer Advocate  
Chi Chi Wu, Staff Attorney

November 2007

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National Consumer Law Center, 77 Summer St., 10<sup>th</sup> Floor, Boston, MA 02110  
[www.consumerlaw.org](http://www.consumerlaw.org)

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## EXECUTIVE SUMMARY

Millions of consumers are being victimized by “credit” card offers that charge hundreds of dollars in fees and extend minimal available credit – sometimes as little as \$50. These cards, which we call “fee-harvester” cards, share a common thread: high fees that eat up most of an already low credit limit, leaving the consumer with little real, useable credit and at a high price.

For example, one of the fee-harvester cards featured in this report comes with a credit limit of \$250. However, the consumer who signs up for this card will automatically incur a \$95 program fee, a \$29 account set-up fee, a \$6 monthly participation fee, and a \$48 annual fee – an instant debt of \$178 and buying power of only \$72.

While high fees, high interest rates, and other abuses pose a threat to consumers of prime credit cards as well as to those with bad and no credit histories, fee-harvester cards are designed to maximize profits by targeting the most vulnerable consumers. Fee-harvester cards are part of the subprime strata of credit cards, and represent an extreme version of the abuses by the card industry.

Fee-harvesting is very profitable. In 2006, one company – CompuCredit – collected \$400 million in fees from a portfolio of fee-harvester cards that by mid-2007 had saddled cardholders with nearly \$1 billion in debt.

The business models of CompuCredit and others that issue and market fee-harvester cards depend upon federal banking laws and regulations that preempt state interest rate caps and consumer protection laws. Preemption also benefits the mainstream credit card industry, which makes enormous profits by charging interest rates and fees that could otherwise be limited by the states. Weak enforcement actions and guidelines issued by federal banking regulators have done little to contain the harm.

Preemption makes bank charters an invitation to extract high fees. For example, CompuCredit, frustrated in efforts to get its own bank charter, has marketed fee-harvester cards in partnerships with compliant banks that act as issuers.

Recently, CompuCredit partnered with Urban Trust Bank, which says its “mission” is to bring affordable banking services to minority communities. CompuCredit has other powerful partners, including a unit of Synovus, a large Georgia bank holding company that is also a major service provider to mainstream credit card companies. CompuCredit also has ties to some of Wall Street’s largest and most prestigious banks.

Several small banks specialize in the issuance of fee-harvester cards, including South Dakota-based First Premier; First National of Pierre; Delaware-based First Bank of Delaware; and Applied Bank, formerly known as Cross Country Bank. Some big banks also have big stakes in the subprime market, including Capital One, which has sometimes used the fee-harvesting model, and HSBC.

Congress should act to end preemption and to close the legal loopholes that now enable banks to attach high fees to nearly meaningless offers of credit that are at the heart of fee-harvesting. In addition, Congress should regulate interest rates, fees, and unilateral contract changes throughout the credit card industry, and permit individual consumers to seek recourse when creditors violate their rights under the Federal Trade Commission Act.

# PART I. FEE-HARVESTERS: SUBPRIME CARDS WITH LITTLE CREDIT AND HIGH FEES

## A. Introduction

“You don’t need a good credit score to get a great credit card!” That’s the too-good-to-be-true promise on a web site advertising the “Imagine Gold MasterCard,” a plastic offering by the tiny First Bank of Delaware.<sup>1</sup>

Each day, on the Internet and through mass mailings, First Delaware and other banks pitch similar “great” cards. They seek to lure consumers who can be pressured to pay high prices for cards because they lack a borrowing history or have a spotty credit record.

In fact, these cards work very well – for the banks. Each year they rake in hundreds of millions of dollars from the so-called “subprime” market by issuing cards that come with enormous fees and tiny credit lines – “fee-harvester” cards.

But fee-harvester cards pose a threat to the financial well-being of consumers, especially those with low credit scores, who are likely to end up holding nearly worthless pieces of plastic and paying hundreds of dollars in fees.

That’s what happened to Thelma Perry, a Chicago woman who in the winter of 2005 received a letter from the tiny First National Bank of Pierre, S.D., offering her a “pre-approved Visa account.” The bank – one of several issuers of fee-harvester cards based in South Dakota – had obtained a report on Perry from a credit bureau.<sup>2</sup>

Apparently, something the bank saw in Perry’s file marked her as a target for a classic “fee-harvester” card offer. This one had a “credit limit up to \$1,500.” But as is typical, that offer came with a qualifier, under an asterisk: “most customers receive an initial credit limit of \$250.” And from that \$250, the bank would immediately deduct a \$50 annual “membership” fee, a \$119 “acceptance” fee and a \$6 monthly “participation” fee, leaving Perry and other lucky new cardholders with the princely sum of \$75 to spend. Those who got carried away and spent more than that \$75 also incurred a \$29 over-limit fee.<sup>3</sup>

Perry sued, alleging that the bank violated the Fair Credit Reporting Act by failing to properly disclose the offer’s terms and by illegally looking at her credit report without actually committing to offer any substantial amount of credit. The bank responded with a filing describing in detail the layout and paper size of the contents of its mailing and noting that the disclosures required by the FCRA had been made in eight point type.<sup>4</sup>

After Perry lost in federal district court, she appealed to the U.S. 7<sup>th</sup> Circuit Court of Appeals. While the appeals panel, in a 2-1 vote, sided with the bank, a dissenting opinion by Judge Terence Evans observed that First National’s solicitation appeared to be a fee-harvesting scheme dressed up as a credit card offer.

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<sup>1</sup> First Bank of Delaware web advertisement viewed Aug. 14, 2007 at [app50.imaginegoldcard.com/signup.form;jsessionid=a4MJ9jvS4D74mfOSKr](http://app50.imaginegoldcard.com/signup.form;jsessionid=a4MJ9jvS4D74mfOSKr).

<sup>2</sup> Perry v. First National Bank, 459 F.3d 816 (7th Cir. 2006).

<sup>3</sup> Exhibit A to Complaint, Perry v. First National Bank (N.D. Ill. Mar. 11, 2005).

<sup>4</sup> First National Bank’s Brief in Support of Motion for Summary Judgment, Perry v. First National Bank (N.D. Ill. April 29, 2005), at 3.

First National's offer was "not a 'legitimate credit product'" but "an unconscionably one-sided financial deal that defies a reasonable concept of sufficient value," he wrote.<sup>5</sup>

First National's aim was to tap legally protected credit information it uses to find targets, according to Evans, who wrote: "For anyone who understands credit card marketing schemes, it is difficult not to conclude that First National is using its privileged access to financial data simply to extract one creative fee on top of another from consumers who are either naive, desperate or both."<sup>6</sup>

Evans went on to describe a dark corner of the subprime card market where "credit card companies employ savvy marketing analysts and sophisticated algorithms to target their offers toward particular niches of consumers."<sup>7</sup> But that reasoning failed to persuade the other two members of the appeals panel, so First National – and a host of competitors – remain free to continue marketing their fee-harvester cards.

## **B. "Dream" Card, Fee Nightmare**

Judged by the marketing pitches, a fee-harvester card seems like a ticket for a fast escape from financial troubles. Issuers beckon consumers to apply for cards with uplifting names like "Aspire" or "Premier." They promise easy access to the credit and convenience that comes with holding a Visa or MasterCard. They entice with the status of carrying a "gold" or "platinum" card.

But while the labels may sound like the stuff of dreams, an application for one of these plastic fee-harvesters can plunge a vulnerable consumer into a nightmare world of high fees and other costly provisions. A description of one such offer prompted one of the judges during the oral argument in *Perry v. First National Bank*, to exclaim: "Who in their right mind would ever agree to accept these terms?"<sup>8</sup>

But many consumers do. Some may be desperate and fail to notice that a deal sounds too good to be true. Others may not care, or may be confused by the terms of a complex credit offer. And some may have other worries or responsibilities – like serving their country.

Perhaps that's what was on the mind of the sailor who in February 2007 walked in the door at the Navy-Marine Corps Relief Society office in Bremerton, Wash. She had with her a statement for a "credit" card she had gotten three months earlier from another South Dakota bank: First Premier of Sioux Falls.

The sailor had only used her card during one four-day period in early December. And, judging by the charges on her statement, her spending "binge" had hardly been excessive: \$18 at the post exchange, \$8 for gas, \$40 at Kay-Bee Toys and \$20 at a Chuck E Cheese pizzeria.<sup>9</sup>

Yet that \$85 "spending spree" had pushed her over the credit limit on a card which – as it said right on the top of her bill – was \$250. How could that have happened?

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<sup>5</sup> *Perry v. First National Bank*, 459 F.3d 816, 827 (7th Cir. 2006) (Judge Evans' dissenting).

<sup>6</sup> *Id.* at 826-27.

<sup>7</sup> *Id.* at 826.

<sup>8</sup> Recording of oral argument in *Perry v. First National Bank* posted at web site of U.S. 7<sup>th</sup> Circuit Court of Appeals at <http://www.ca7.uscourts.gov/tmp/7C1FF23J.mp3>.

<sup>9</sup> Credit card statement copies and information from correspondence and interviews with Liz Kosse, director of the Navy-Marine Corps Society in Bremerton, Wash. (on file with authors)

The fees did it. In terms typical of fee-harvester cards issued by First Premier and others, the unwary sailor had, without a single swipe of her card, incurred a \$95 program fee, a \$29 account set-up fee, a \$6 monthly participation fee, and a \$48 annual fee – an instant debt of \$178 and buying power of only \$72. So the sailor got an unexpected bon voyage from landlocked First Premier: a balance of \$320.81 to pay off while she served her country.<sup>10</sup>

### **C. A (Nearly) Perfect Engine**

Millions of Americans have held a fee-harvester card at one time or another. For some, carrying that card has been a brief – if expensive – interlude that resulted from a limited or poor credit history, or maybe just a bad choice of plastic. For others, living with high-priced plastic is a symptom of chronic financial ills.

But for a portion of the credit card industry, the business of issuing cards that harvest fees but deliver little credit has become a gold mine – a rich lode of revenue and profits.

In the 1975 movie “Jaws,” a marine biologist played by Richard Dreyfuss makes this observation about the great white shark: “What we are dealing with is a perfect engine, an eating machine. It’s really a miracle of evolution.”

Subprime card issuers sometimes claim to have developed a similarly ingenious engine that ensures profits and eliminates risks. Drawing upon expertise in credit data analysis, mass marketing and debt collection, predators have built specialized business models that enable them to prosper by “serving” poor and disadvantaged consumers.

#### *A Progenitor: BestBank*

The model dates back at least to the early 1990s. One early adopter of the fee-harvesting model was a tiny Colorado lender named BestBank which, in 1994, began issuing credit cards in a deal with a professional marketing firm. The cards had a \$250 credit limit and required a cardholder to make a no-interest \$250 deposit with the bank and pay a \$129 annual fee.<sup>11</sup>

Soon, Colorado officials began receiving complaints about “high pressure marketing tactics involving young unsophisticated consumers and the elderly.”<sup>12</sup> Eventually, BestBank sold its small portfolio of secured credit card accounts and began issuing unsecured Visa cards with a \$600 credit limit. However, to get these cards consumers had to pay \$498 to join a travel club and a \$45 annual fee.<sup>13</sup>

The scam eventually fell under its own weight. In 1998, Colorado and federal regulators shut down BestBank after examining its books and finding that it had included among its assets millions of dollars of credit card accounts that the “holders” had never applied or paid for.<sup>14</sup> In February 2007, Judge Richard Matsch of the U.S. District Court for Colorado found three officers of the bank guilty of conspiracy, bank fraud, filing false reports and wire fraud.<sup>15</sup>

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<sup>10</sup> *Id.*

<sup>11</sup> Findings Pursuant to Rule 23(c), United States v. Edward P. Mattar III, No. 03-cr-00232 (D. Colo. Feb. 12, 2007) at 3-4.

<sup>12</sup> *Id.* at 5.

<sup>13</sup> *Id.* at 8.

<sup>14</sup> *Id.* at 23-25, 27.

<sup>15</sup> *Id.* at 30-40.

Matsch's judgment included this cogent summary of fee-harvester cards: "The profit in sub-prime lending is made by charging front-end fees to obtain the cards rather than in generating interest income on the balances in accounts because many cardholders will be unwilling or unable to make their payments on time or at all."<sup>16</sup>

### *Evolution*

While BestBank toppled, other predators survived or emerged, and proved more adept at harvesting fees without attracting unwanted attention from law enforcement or regulators. A current generation of predators has learned a very effective way to protect themselves against risk: impose an extremely low limit on a card's purchasing power, or credit line. Limits of a few hundred dollars – sometimes lower – make it nearly impossible for cardholders to buy very much of anything. When issuers write off balances, they consist mostly of unpaid fees – to themselves.

These are the fee-harvester cards.

## **D. The Fee-Harvester Squeeze**

The credit card market is full of abuses - high interest rates; exorbitant charges; hair trigger contract provisions that slap consumers with penalties and junk fees; and surprise changes in terms imposed without the consumer's agreement. In an industry known for bleeding consumers, fee-harvester cards represent the ultimate in money suckers - cards that from the outset squeeze consumers for enormous fees but provide only a trickle of credit in return.

The terms of the fee-harvester cards are carefully set to maximize the profits of issuers. Credit limits are set so low that fees almost immediately eat up all or most of the available credit. The consumer is left with little useable credit - at a very expensive price.

Issuers of fee-harvester cards spend hundreds of millions of dollars to find customers who will buy into their predatory deals. Each marketing drive aims to generate a quick crop of cash and a secondary crop of IOUs, some of which card issuers will cash in, some of which they will sell to debt collectors. Even as the cash flow from one sales push subsides, a new mass mailing or TV commercial campaign seeks the next batch of victims.

Left behind in the wake of each marketing blitz are thousands of unfortunate cardholders who find they have paid costs comparable to a payday loan in exchange for few dollars of "credit." And many will face a painful choice: pay these junk fees or fall deeper in debt and do additional damage to their credit scores.

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<sup>16</sup> *Id.*



**Sample Terms from Fee-Harvester Cards<sup>17</sup>**

<b>First Premier Bank<sup>18</sup></b>	
Credit Limit	\$250
Program Fee	-\$95
Account Set-Up Fee	-\$29
Participation Fee	-\$6 (per month)
Annual Fee	-\$48
Total Usable Credit	\$72

<b>Aspire Card (CompuCredit)<sup>19</sup></b>	
Credit Limit	\$300
Account Opening	-\$29
Annual fee	-\$150
Total Usable Credit	\$121

<b>Capital One<sup>20</sup></b>	
Credit Limit	\$200
Annual Fee	-\$50
Diner Club Membership	-\$99
Total Usable Credit	\$51

<b>Legacy Visa<sup>21</sup></b>	
Credit Limit	\$250
Acceptance Fee	-\$119
Annual Fee	-\$50
Participation Fee	-\$6 (per month)
Total Usable Credit	\$75

<b>Continental Finance<sup>22</sup></b>	
Credit Limit	\$300
Account Set-Up Fee	-\$99
Participation Fee	-\$89
Annual Fee	-\$49
Account Maintenance Fee	-\$10 (per month)
Total Usable Credit	\$53

<b>CorTrust MasterCard<sup>23</sup></b>	
Credit Limit	\$250
Acceptance Fee	-\$119
Annual Fee	-\$50
Participation Fee	-\$6 (per month)
Total Usable Credit	\$75

<sup>17</sup> In the charts that follow, Total Usable Credit represents the available credit line after imposition of initial fees. If the consumer is able to pay off the initial fees, most of the credit line should become available. However, many of the financially struggling consumers who receive these offers may not be able to immediately pay off hundreds of dollars in fees.

<sup>18</sup> From facts in case described in Section I.B. above. See also *Examining the Billing, Marketing, and Disclosure Practices of the Credit Card Industry, and Their Impact on Consumers: Hearing Before the Senate Cmte on Banking, Housing, and Urban Affairs*, 110th Cong. (2007) (statement of Dr. Robert Manning, Director, Center for Consumer Financial Services, Rochester Institute of Technology).

<sup>19</sup> Assurance of Discontinuance, *In the Matter of Columbus Bank and Trust Co. and CompuCredit Corp.*, New York Attorney General's Office, June 30, 2006, available at [www.oag.state.ny.us/press/2006/jul/Aspire%20Visa%20Assurance.pdf](http://www.oag.state.ny.us/press/2006/jul/Aspire%20Visa%20Assurance.pdf).

<sup>20</sup> From facts in case described in Section III.D. above. Press Release, *Attorney General Darrell McGraw Sues Capital One Bank and Capital One Services, Inc.* U.S. State News (July 2005), available from *Westlaw* at 2005 WLNR 10881649.

<sup>21</sup> *Perry v. First National Bank*, 459 F.3d 816 (7th Cir. 2006).

<sup>22</sup> First Bank of Delaware, Continental Finance Terms & Conditions, <https://www.cfcapply.com/gold1mc/fbd-terms.htm> (last viewed October 18, 2007).

<sup>23</sup> *Bonner v. CorTrust, N.A.*, 2006 WL 1980183 (N.D. Ind. 2006).

Fee-harvesters and other aggressive subprime creditors depend on fees but also boost profits by using an extensive arsenal of abusive tactics to collect cash from vulnerable consumers, including:

- **Downselling.** Card marketers frequently lure consumers by advertising cards with substantial credit limits and attractive terms, but issuing cards with lower credit limits and less favorable terms. Providian Financial, a card issuer now owned by Washington Mutual, was an early practitioner of this form of bait-and-switch marketing. Providian enticed consumers to transfer balances to Providian cards from competing credit cards by promising lower interest rates, then imposed rates that were about the same or even higher than consumer's original rate.<sup>24</sup> Delaware-based Applied Bank (formerly known as Cross Country Bank) told consumers that they had been approved for a credit limit of up to \$2,500 but often issued cards with nominal credit limits below \$400 – and available credit was even lower after these \$400 limits were eaten up by fees.<sup>25</sup>
- **Deceptive add on products.** Issuers of high-fee, low-credit fee-harvester cards frequently bill customers for expensive and useless products, including “credit protection” and memberships in diner’s and travel clubs. Providian advertised a “no annual fee” card that required the purchase of a \$156 per year credit protection policy.<sup>26</sup> Capital One added a “diner’s club membership” despite the fact that the consumer declined the product.<sup>27</sup> Applied Bank, then operating as Cross Country Bank, misled consumers into enrolling in products such as “Credit Account Protection” or “Applied Advantage” Program. BestBank added \$498 ‘travel club memberships’ to the accounts of cardholders who had only \$600 in available credit on their cards. According to federal prosecutors, fewer than half of the borrowers who were charged for these memberships even received membership materials.<sup>28</sup>
- **Slice and dice:** Rather than increasing the credit available on an existing card with a low limit, a bank will sometimes issue an additional card that also has a low limit. That increases the odds that a cardholder will incur penalty fees or rates by exceeding the limits or missing payment deadlines on one of multiple cards. A 2006 report in Business Week magazine identified five consumers who ended up mired in debt after they were issued multiple credit cards by Capital One Bank. A Capital One spokeswoman told the magazine that the “vast majority” of Capital One cardholders had only one account, but that “a very small percentage” had three or more cards.<sup>29</sup>
- **“Deposits” charged to cards.** Secured cards, in which the consumer makes a cash deposit as collateral for purchases and costs incurred on a card, offer an expensive but sometimes useful option to consumers with bad or limited credit histories. However, some card issuers, instead of requiring a cash deposit, charged a bogus “deposit” to the holder’s balance. The problem was that these cards were advertised as no deposit accounts. In addition, the “deposit” and fees ate up most or all of the credit extended to the cardholder.<sup>30</sup>

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<sup>24</sup> *In re Providian Nat'l Bank*, No. 2000-53 (Dept. of the Treasury, Office of the Comptroller of the Currency June 28, 2000), available at [www.occ.treas.gov/FTP/EAs/ea2000-53.pdf](http://www.occ.treas.gov/FTP/EAs/ea2000-53.pdf).

<sup>25</sup> *People v. Applied Card Sys., Inc.*, No. 2073-03 (N.Y. Sup. Ct. May 28, 2004) (transcript of proceedings), available at <http://www.oag.state.ny.us/press/2004/jul/6a.pdf>.

<sup>26</sup> *In re Providian Nat'l Bank*, No. 2000-53 (Dept. of the Treasury, Office of the Comptroller of the Currency June 28, 2000), available at [www.occ.treas.gov/FTP/EAs/ea2000-53.pdf](http://www.occ.treas.gov/FTP/EAs/ea2000-53.pdf).

<sup>27</sup> See Section III-D, below.

<sup>28</sup> *Three Individuals Found Guilty of Conspiracy, Fraud Related to Boulder Based BestBank Failure*, U.S. Federal News, February 12, 2007.

<sup>29</sup> Robert Berner, *Cap One's Credit Trap*, Business Week, November 6, 2006.

<sup>30</sup> See, e.g., *In re First Nat'l Bank of Marin*, No. 2001-97 (Dept. of the Treasury, Office of the Comptroller of the Currency December 3, 2001), available at [www.occ.treas.gov/ftp/eas/ea2001-97.pdf](http://www.occ.treas.gov/ftp/eas/ea2001-97.pdf).

- **Abusive debt collection.** Issuers of fee-harvester cards frequently employ abusive debt collection tactics. According to the Minnesota Attorney General’s Office, employees of Applied Bank (formerly Cross Country) withdrew electronic payments from cardholders’ bank accounts without permission, called holders at their homes on holidays, at dawn or late at night, threatened to foreclose on homes or repossess property, threatened to call immigration authorities and intimidated debtors by using bogus titles or profanity or racial slurs.<sup>31</sup> CompuCredit, a fee-harvester card issuer, says that its collectors aim “to collect as much of the money that is owed to us in the most cost effective and customer friendly manner possible;”<sup>32</sup> however, CompuCredit recently settled an investigation by New York regulators who alleged that the company exploited customers’ fear of getting yet another blemish on an already poor credit history.<sup>33</sup>
- **Reverse redlining.** Lenders have historically denied residents of minority communities equal access to credit, a form of discrimination known as redlining. Some issuers, seeking to exploit that history, have launched “affinity” campaigns that market high cost products, including fee-harvester cards, to minority communities. For example, a marketing company called Urban Television Network distributed the Freedom Card, a fee-harvester card that often had a credit limit of only \$300. Promotional efforts for the Freedom Card included a contract with musician Queen Latifah.<sup>34</sup>

In addition, the tactics used by issuers of fee-harvester cards mirror abusive practices found throughout the credit card industry, which are discussed in more detail in Part II. One tactic commonly used by issuers of mainstream cards is the imposition of onerous penalties for late payments or charges that exceed credit limits, including fees as high as \$40 and immediate hikes in interest rates on outstanding balances to annual percentage rates (APRs) as high as 40%. Such penalties can be triggered for every month the consumer is over the limit or when a deadline is missed by not days, but hours. Fee-harvester cards are especially vulnerable to over limit fees because the low credit limits increase the odds that consumers will exceed those limits.

Indeed, fee-harvesters depend on these penalty fees. For example, according to the American Banker, Atlanta-based card marketer CompuCredit, which issues fee-harvester cards, posted a surprise loss in the second quarter of 2007, in part because late and over-limit fees were \$22 million lower than expected.<sup>35</sup>

## **E. Growth of Subprime**

Fee-harvester cards belong to the class of credit cards known as “subprime” cards, mostly targeted at consumers with credit scores under 660. Until the end of the 20th century, consumers generally had to

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<sup>31</sup> State v. Cross Country Bank, 703 N.W.2d 562 (Minn. Ct. App. 2005). See also Cross Country Bank v. McGraw, No. 04-C-464 (Cir. Ct. Kanawa County W. Va. Dec. 9, 2004), available at [www.wvs.state.wv.us/wvag/press/2004/dec/CrossCountryorder.htm](http://www.wvs.state.wv.us/wvag/press/2004/dec/CrossCountryorder.htm); People v. Applied Card Sys., Inc., No. 2073-03 (N.Y. Sup. Ct. May 28, 2004) (transcript of proceedings), available at <http://www.oag.state.ny.us/press/2004/jul/6a.pdf>. See also Lautenschlager Suing Delaware Credit Card Issuer, Greater Milwaukee Business Journal, Nov. 21, 2003, available at <http://www.bizjournals.com/milwaukee/stories/2003/11/17/daily40.html>

<sup>32</sup>CompuCredit Corp., Form 10-K for the Fiscal Year Ended December 31, 2006, Feb. 28, 2007, at 10 [hereinafter “CompuCredit 2006 Form 10-K”]

<sup>33</sup> Assurance of Discontinuance, *In the Matter of Columbus Bank and Trust Co. and CompuCredit Corp.*, New York Attorney General’s Office, June 30, 2006, at 4, available at [www.oag.state.ny.us/press/2006/jul/Aspire%20Visa%20Assurance.pdf](http://www.oag.state.ny.us/press/2006/jul/Aspire%20Visa%20Assurance.pdf).

<sup>34</sup> Freedom Card, Inc. v. JP Morgan Chase & Co., 432 F.3d 463 (3rd Cir. 2005).

<sup>35</sup> Harry Terris, *New Card Mix, New Issues at CompuCredit*, American Banker, Thursday, May 10, 2007.

have good credit histories in order to qualify for credit cards. Other consumers usually were forced to look elsewhere for loans and were denied the convenience of using plastic to pay for things.

But that changed as credit card issuers seeking to grow began to find plastic already in the hands of most “prime” consumers that wanted to have a card. Credit card issuers large and small began putting cards in the hands of consumers whose low credit scores had previously kept them locked out of the credit card market. Other cards went to consumers who, because they had previously not borrowed, had no credit scores.<sup>36</sup>

### **A Quick Primer On Credit Scores**

Credit scores usually are generated from consumer credit histories compiled by the nation’s three large credit bureaus: Experian, Equifax, and Transunion. Each history contains information about a consumer’s record of paying bills on time, bills sent to debt collection agencies, outstanding debt amounts, and number, types and age of credit accounts. Lenders use credit scores to set the price and terms of credit offers, based on the assumption that the score will predict the likelihood that the borrower will repay the loan on time. The most widely used credit score – often called a ‘FICO score’—is calculated using proprietary formulas from Fair Isaac & Co. Scores range from 300 and 850. Credit card issuers typically define a consumer with a score of 660 or lower as a subprime borrower.

Banks found some lucrative opportunities in the subprime market, where disadvantaged or unsophisticated borrowers could be made to pay premium prices for sub-par services. As one observer noted, “The higher rates and fees associated with riskier credit sectors have become an irresistible lure for many prime issuers hungry to boost profits in the oversaturated credit card marketplace.”<sup>37</sup>

Fee harvesting represents an extreme in the premiums charged for subprime cards, going from merely expensive to offering little useable credit at an extravagant price.

The subprime credit card market also provided rich hunting grounds for predators. Some boiler room operations used telemarketing and other high-pressure tactics to persuade consumers seeking credit cards to send in cash. Often, the boiler room operators packed up and moved on without sending any credit cards at all to their victims.<sup>38</sup>

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<sup>36</sup> “Historically, we would not accept a single bankrupt client ever,” Sandra Derickson, then a top executive at HSBC, a large British bank that issues prime and subprime credit cards in the U.S. market, told financial analysts in 2004. “We now allow people (to get cards) who’ve had bankruptcies more than five years in the past, and we’re finding they’re performing very effectively.” See HSBC Holdings “Global Cards” Investor Event and Conference Call, FD (Fair Disclosure) Wire, May 19, 2004.

<sup>37</sup> Kate Fitzgerald, *Prime Issuers Tiptoe into Riskier Waters*, Cards & Payments, April 2007.

<sup>38</sup> In September 2002, the FTC and 15 other federal and state agencies conducted “Operation No Credit,” a law enforcement sweep targeting enterprises that offered consumers “major credit cards such as a MasterCard or Visa, or a loan, for a one-time advance fee, that never produce the promised credit cards or loans.” See Press Release, “FTC, States Give ‘No Credit’ to Finance-Related Scams in Latest Joint Law Enforcement Sweep,” Federal Trade Commission, Sept. 5, 2002.

## **F. CompuCredit: Secrets of a Fee-Harvester Revealed**

Not surprisingly, most issuers of fee-harvester cards don't say much publicly about how they profit from down-on-their-luck and disadvantaged cardholders. One issuer that does is a low-profile Atlanta company called CompuCredit.

CompuCredit is listed on the NASDAQ, a national stock market. In exchange for this listing, which makes it relatively cheap for the company to raise capital, CompuCredit is required by securities laws to disclose information about its businesses and properties. Because credit cards generate most of CompuCredit's profits and revenue, the company's financial reports provide a unique public look – albeit in stilted language and sometimes numbing detail – at how a company makes money issuing fee-harvester cards.<sup>39</sup>

At first glance, CompuCredit's core business – issuing cards to consumers viewed as unlikely to pay their bills – sounds risky. So a company financial filing offers this lengthy reassurance to investors: “We believe that we have priced our products and acquisitions such that over time the income we earn from receivables that are not charged off is sufficient to cover our marketing expenses, our servicing expenses, overhead expenses, our costs of funds and our losses from cardholders who fail to make their payments and are charged off.”<sup>40</sup>

In plain English, the company collects enough money from its cardholders to cover the cost of finding customers, handling their accounts, paying other corporate expenses and getting money from investors, lenders or depositors.

Amazingly, CompuCredit's operation is so lucrative that the company comes out ahead even as many cardholders – perhaps angered by high fees and lack of credit – prove unwilling or unable to pay their bills. The numbers are staggering. CompuCredit charged off \$728 million owed by its cardholders in 2006, yet raked in enough fees and interest to post a \$107 million profit.<sup>41</sup>

Fee-harvester cards provided a windfall to the company. Fees collected on those cards soared to \$444 million in 2006, a five-fold increase since 2004.<sup>42</sup> Although CompuCredit did not disclose just how many fee-harvester cards it issued, it did reveal the jump in the money owed it by holders of those cards: from \$327 million at the end of 2005 to \$732 million a year later and on up to \$972 million at the midpoint of 2007.<sup>43</sup>

Of course, finding customers for fee-harvester cards can be expensive – especially since not many stick around. As T. Denny Sanford, founder of First Premier Bank, a CompuCredit competitor, put it in a recent interview: “We seldom keep anyone beyond an 18- to 24-month period of time.”<sup>44</sup> CompuCredit, which spent \$106 million on marketing in 2006 and has told analysts it expects to boost that spending to

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<sup>39</sup> CompuCredit's filings stretch out that three-word description into a 16-word mantra that only a lawyer could love: “largely fee-based credit card offerings to consumers at the lower end of the FICO scoring range.” This gem of a phrase appears 78 times in CompuCredit's Form 10-K for 2006.

<sup>40</sup> CompuCredit 2006 Form 10-K at 7.

<sup>41</sup> *Id.* at 34, 52.

<sup>42</sup> *Id.* at 38.

<sup>43</sup> CompuCredit Corp., Form 10-K for the Fiscal Year Ended December 31, 2005, March 1, 2006, at 32; CompuCredit 2006 Form 10-K at 36; and CompuCredit, Form 10-Q, Aug. 1, 2007, at 24.

<sup>44</sup> Kelly Hildebrandt, *Predatory? Not in the Least*, Sioux Falls Argus Leader, Aug. 14, 2007, at 1A.

\$160 million in 2007, has noted “the shorter life cycle of many of the accounts” associated with its fee-harvester cards.<sup>45</sup>

Fee-harvester cards are often marketed as tools for consumers to use to repair or improve damaged credit. However, fee-harvester card issuers have so far failed to back those claims with evidence. When asked during a conference call with analysts whether CompuCredit had any statistics on the percentage of customers who got a lower tier card that “graduated” to an “up market card,” David Hanna, CompuCredit’s chief executive, responded: “We do not have that data right here. Perhaps we’ll share it in a future all (sic), because it is one of our strategies is to take customers from the intro offer, if you will, and move them into higher credit lines and products that offer more to that customer base.”<sup>46</sup> Sanford, the head of competitor First Premier Bank, also declined to quantify the number of cardholders who “graduated” to better cards.<sup>47</sup>

In the meantime, CompuCredit’s fee-harvester cards have very little purchasing power. Balance growth is driven mainly by fees, so that in cases where consumers walk away from or give up trying to pay their credit card bills, much of the unpaid balances represent fees rather than payments for purchases to third-party merchants. In other words, much of the money charged off by CompuCredit was never spent on anything but its own fees.

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<sup>45</sup> CompuCredit 2006 Form 10-K at 51.

<sup>46</sup> CompuCredit Earnings Conference Call Q1 2007– Final, FD (Fair Disclosure) Wire, May 8, 2007.

<sup>47</sup> Kelly Hildebrandt, *Predatory? Not in the Least*, Sioux Falls Argus Leader, Aug. 14, 2007, at. 1A.

## PART II: THE ENABLERS: HOW FEDERAL LAW AND REGULATORS PERMIT FEE HARVESTING

### A. Preemption: The Answer to “Can This Be Legal?”

Consumers, shocked by the high costs and abusive practices of credit card issuers, frequently ask: “Can this be legal?”

Too often, it is. The legality of many credit card practices that outrage consumers results from a federal law passed during the Civil War era, 1980s deregulation, and a pair of 20<sup>th</sup> century Supreme Court decisions. Adding to this consumer-unfriendly mix are the actions of federal banking agencies that have aggressively muscled out state regulators from helping consumers abused by credit cards.

The origins of this phenomenon can be traced back to 1863, when the National Bank Act became law. In a 1978 case, the Supreme Court interpreted this Act to “preempt” or overrule state usury laws by permitting national banks to follow the usury law (or lack thereof) of their home state. In effect, that Supreme Court decision allowed banks to “export” ultra-high interest rates from states without usury laws to states with more restrictive laws.<sup>48</sup>

Soon after that decision, big credit card issuers including Citibank and JPMorgan Chase moved their bases to states such as South Dakota and Delaware, states without usury caps. After 1978, the credit card industry grew rapidly. From 1978 to 1995, total credit card debt increased six-fold to \$378 billion.<sup>49</sup>

Congress, in the wake of the Supreme Court’s decision and the high interest rate environment of the 1980s, added more fuel to the boom with a series of laws that allowed other banks to skirt state interest rate caps.<sup>50</sup> In 1996, the Supreme Court gave credit card issuers another boost by ruling that the national banks’ exemption from restrictive state laws also applied to fees, such as late fees or over-limit fees.<sup>51</sup>

Meanwhile, federal banking agencies added further momentum to preemption by issuing regulations that preempted state laws regulating credit card disclosures, specific practices and other terms.<sup>52</sup> The Office of Comptroller of Currency even prohibited state regulators from pursuing banks for violations of federal laws.<sup>53</sup>

Thus, banks are free to ignore state laws that would otherwise limit interest rates, finance charges and other credit terms. Preemption has transformed the business models of credit card issuers. Banks rushed to increase late charges, over-limit fees, and other charges. The average late payment fee soared from under \$13 in 1995 to over \$33 in 2005, an increase of 115% adjusted for inflation, according to the

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<sup>48</sup> *Marquette Nat’l Bank of Minn. v. First of Omaha Serv. Corp.*, 439 U.S. 299, 99 S. Ct. 540, 58 L. Ed. 2d 534 (1978).

<sup>49</sup> See, Fed. Res. Bull., available at [http://www.federalreserve.gov/releases/g19/hist/cc\\_hist\\_mt.txt](http://www.federalreserve.gov/releases/g19/hist/cc_hist_mt.txt).

<sup>50</sup> See National Consumer Law Center, *The Cost of Credit: Regulation, Preemption, and Industry Abuses* § 3.1.1 (3d ed. 2005 and Supp.).

<sup>51</sup> *Smiley v. Citibank (S.D.)*, Nat’l Assn., 517 U.S. 735, 116 S. Ct. 1730, 135 L. Ed. 2d 25 (1996).

<sup>52</sup> See, e.g., 12 C.F.R. §§ 7.4007 and 7.4008 (OCC); 12 C.F.R. § 560.2 (OTS).

<sup>53</sup> See 12 C.F.R. § 7.4000(a), which provides: “Only the OCC or an authorized representative of the OCC may exercise visitatorial powers with respect to national banks, ...

(2) For purposes of this section, visitatorial powers include:

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(iv) Enforcing compliance with any applicable federal or state laws...”

Government Accountability Office.<sup>54</sup> Average over-limit fees also jumped, from under \$13 in 1995 to over \$30 in 2005, an increase of 95% adjusted for inflation, the GAO found.<sup>55</sup>

The result has been a fee-based revenue bonanza for the banks. Total penalty fee revenue in the credit card industry increased nearly nine-fold, from \$1.7 billion in 1996 when the Supreme Court extended preemption to card fees, to \$14.8 billion in 2004.<sup>56</sup>

While federal regulators have repeatedly given banks a green light to squeeze more and more out of cardholders, state regulators have been stripped of most of their weapons for fighting abuses. At best, state regulators can pursue state-chartered banks for abuses other than exceeding interest rate or fee caps, such as violation of state laws prohibiting unfair or deceptive practices.

### Who Governs Whom?

Banks are regulated by federal or state agencies, depending on what type of bank they are and the type of charter they have.<sup>57</sup> Federally chartered banks are regulated by the Office of the Comptroller of Currency (OCC) or the Office of Thrift Supervision (OTS).<sup>58</sup> State-chartered banks are regulated by banking regulators in their home states but also by either the Federal Reserve Board (Fed)<sup>59</sup> or the Federal Deposit Insurance Corporation (FDIC).

## **B. The Beast Spawned by Preemption**

Credit cards promise consumers readily available credit and convenient transactions. Moreover, a piece of plastic is needed for many everyday transactions: buying a plane ticket, reserving a hotel room, renting a car or shopping on-line. But lack of regulation has raised the price of admission to the world of plastic.

While the squeeze is hardest on consumers with bad credit or limited borrowing histories, even holders of mainstream cards find themselves subject to abusive practices by issuers and marketers. Preemption is the catalyst responsible for the general lack of real, meaningful regulation that permits credit card abuses in all segments of the market. The link between fee-harvester cards and the rest of the credit card market is that absence of regulation, which allows the bad practices including:

- Generally high interest rates charged for credit card borrowing;

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<sup>54</sup> Government Accountability Office, *Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers*, GAO-06-929, September 2006, at 20, available at [www.gao.gov/new.items/d06929.pdf](http://www.gao.gov/new.items/d06929.pdf). [hereinafter “GAO Credit Card Report”].

<sup>55</sup> *Id.* at 21.

<sup>56</sup> Cardweb.com, *Fee Party* (Jan. 13, 2005), available at <http://www.cardweb.com/cardtrak/news/2005/january/13a.html>.

<sup>57</sup> See National Consumer Law Center, *The Cost of Credit: Regulation, Preemption, and Industry Abuses* § 3.3.1 (3rd ed. 2005 and Supp.)

<sup>58</sup> Federal credit unions are regulated by the National Credit Union Administration (NCUA).

<sup>59</sup> The Fed is also in charge of writing the regulations for several federal consumer protection laws, such as the Truth in Lending Act, the Electronic Funds Transfer Act, and the Truth in Savings Act.



- Penalty increases in interest rates triggered by events in the cardholder’s account, including late payments or charges made above an account’s credit limit.
- Universal default policies that trigger penalty interest rates because of events not involving the same credit card account, including a drop in credit score, a late payment on a different account or even making an inquiry about a mortgage or car loan.
- Penalty fees for being a day late or going over limit (with the creditor’s approval) that are unrelated to actual costs and assessed as means to boost revenue and profits
- Additional arbitrarily high fees for cash advances, balance transfers, wire transfers, currency conversions and other transactions.
- Allocation of payments within an account in a way that increases a consumer’s exposure to higher rates and fees.
- Hair trigger tactics that impose late fees and penalty rates, including counting payments as “late” if received after noon (or even 10 AM) on the due date.
- Unilateral changes in terms that give the lie to any offer of a “fixed” rate and tilt the whole framework of the contract in favor of the bank.
- Mandatory arbitration clauses that deny cardholders legal relief from abusive practices by issuers.
- Contracts spelled out in tiny print, with terms that even industry insiders find nearly incomprehensible.

Fee-harvesting cards are an extreme version of the abuses of mainstream cards. They are on one end of the spectrum of credit card abuses, but they nonetheless share certain characteristics with their mainstream cousins. And the enabler that has made all of this possible is preemption - preemption of state laws that protect consumers, leaving a huge gaping regulatory hole in its wake.

### **C. Regulators’ Fingers in the Dike**

Federal banking regulators have generally adopted a hands-off approach to credit card fees and interest rates, but they have occasionally intervened to rein in some of the most egregious practices of the fee-harvesters and other issuers of subprime cards. The majority of the enforcement actions have been taken by the OCC, which regulates most of credit card lending. These actions, taken prior to 2004, include:

**Providian (2000).**<sup>60</sup> Providian settled an investigation with the OCC in which it was alleged that the company had engaged in downselling and deceptive marketing of credit insurance add-ons. At that time, Providian was the largest issuer of cards in the subprime market. Providian agreed to pay \$300 million in restitution to consumers. Providian was acquired by Washington Mutual in 2005.<sup>61</sup>

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<sup>60</sup> *In re Providian Nat'l Bank*, No. 2000-53 (Dept. of the Treasury, Office of the Comptroller of the Currency June 28, 2000), available at [www.occ.treas.gov/FTP/EAs/ea2000-53.pdf](http://www.occ.treas.gov/FTP/EAs/ea2000-53.pdf).

<sup>61</sup> *Washington Mutual to Buy Providian for \$6.45B*, San Francisco Business Times, June 6, 2005.

**Direct Merchants Bank, N.A. (2001).**<sup>62</sup> Direct Merchants, a subsidiary of Metris, agreed to pay restitution of approximately \$3.2 million after an investigation by the OCC, in which it was alleged that the bank engaged in deceptive practices, including charging \$79 processing fees to consumers who were promised unsecured cards with no processing fees.<sup>63</sup> Metris was acquired by HSBC in 2005.<sup>64</sup>

**First National Bank of Marin (2001 and 2004).**<sup>65</sup> The OCC required the bank to pay \$4 million in restitution for bogus security deposits. Despite being slapped once, the bank continued using these fake security deposits, forcing the OCC to take a second enforcement action against this bank in 2004 to the tune of \$10 million. Marin's bogus security deposits left the consumer with only \$2.50 in available credit.

**First National Bank in Brookings (2003).**<sup>66</sup> The OCC required the bank to provide \$6 million in restitution for using bogus security deposits and high fees that often left consumers with only \$50 or with no available credit. In addition, the bank charged consumers upfront application fees to receive these useless cards, sometimes tricking consumers into revealing bank account information and then debiting the fees from the consumer's bank account.

**First Consumers National Bank, Beaverton, Oregon (2003).**<sup>67</sup> The OCC required the bank to make restitution of approximately \$1.9 million for unspecified deceptive credit card practices.

The Fed has taken a handful of actions against subprime card issuers based on safety & soundness considerations, including:

**BANKFIRST Corp. (2003).**<sup>68</sup> The Fed required this bank to stop opening new accounts for customers with credit scores less than 660. The agreement did not provide restitution for consumers or address any abusive practices against consumers.

**First Premier Bank and Premier Bankcard, Inc. (2003).**<sup>69</sup> The Fed required First Premier to stop increasing its credit card business to borrowers with credit scores under 660 until the bank implemented a better risk management plan. Unfortunately, the agreement did not spell out or put an end to practices abusive to consumers, nor did it order restitution to injured consumers.

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<sup>62</sup> Consent Order, *In re* Direct Merchants Credit Card Bank, No. 2001-24 (Dept. of Treasury, Office of the Comptroller of Currency, May 3, 2001), available at [www.occ.treas.gov/ftp/eas/ea2001-24.pdf](http://www.occ.treas.gov/ftp/eas/ea2001-24.pdf).

<sup>63</sup> "Fact Sheet Regarding Settlement Between the OCC and Direct Merchants Bank"

<sup>64</sup> Press Release, *HSBC Finance Corporation to Acquire Metris Companies, Inc.*, August 4, 2005.

<sup>65</sup> *In re* First Nat'l Bank of Marin, No. 2001-97 (Dept. of the Treasury, Office of the Comptroller of the Currency December 3, 2001), available at [www.occ.treas.gov/ftp/eas/ea2001-97.pdf](http://www.occ.treas.gov/ftp/eas/ea2001-97.pdf).

<sup>66</sup> *In re* First Nat'l Bank in Brookings, No. 2003-1 (Dept. of the Treasury, Office of the Comptroller of the Currency January 17, 2003), available at [www.occ.treas.gov/ftp/eas/ea2003-1.pdf](http://www.occ.treas.gov/ftp/eas/ea2003-1.pdf)

<sup>67</sup> Press Release, *OCC Requires First Consumers National Bank to Refund Customer Fees* (Dept. of the Treasury, Office of the Comptroller of the Currency August 1, 2003), available at <http://www.occ.treas.gov/toolkit/newsrelease.aspx?Doc=CR79N6BX.xml>

<sup>68</sup> *Written Agreement by and among BANKFIRST Corporation, Sioux Falls, South Dakota, a registered bank holding company, and its subsidiary bank, BANKFIRST, also of Sioux Falls, South Dakota, and the Federal Reserve Bank of Minneapolis*, Federal Reserve Board, April 29, 2003, available at <http://www.federalreserve.gov/boarddocs/press/Enforcement/2003/20030429/attachment.pdf>

<sup>69</sup> *Written Agreement by and among United National Corporation, Sioux Falls, South Dakota; First PREMIER Bank, Sioux Falls, South Dakota; PREMIER Bankcard, Inc., Sioux Falls, South Dakota; and the Federal Reserve Bank of Minneapolis*, Federal Reserve Board, September 25, 2003, available at <http://www.federalreserve.gov/Boarddocs/Press/enforcement/2003/20030925/attachment.pdf>

The Federal Trade Commission (FTC), which does not have authority over banks for the most part, has stepped in to stop fraud and deception by aggressive non-bank marketers. For example, in September 2002, the FTC and other federal and state agencies conducted “Operation No Credit,” a law enforcement sweep that targeted enterprises which offered consumers “major credit cards such as a MasterCard or Visa, or a loan, for a one-time advance fee, that never produce the promised credit cards or loans.”<sup>70</sup>

## **D. Regulatory Guidance**

In addition to the handful of enforcement actions, federal banking regulators have issued a few guidance documents on subprime cards. The Federal Financial Institutions Examination Council (FFIEC)<sup>71</sup> issued a guidance document in 2003 on risk management of credit card loans, which specifically disapproved of such practices as:<sup>72</sup>

- Offering additional credit cards or increases in credit limits to already overextended borrowers;
- Tolerating slow repayment of over-limit accounts and inadequately managing risk of these accounts;
- Setting minimum payments so low as to create negative amortization, i.e., when payments do not fully pay off the interest and fees that have accrued since the last payment, thereby increasing the balance instead of paying it off;
- Offering workout agreements that last over 60 months.

The FFIEC guidance primarily addressed issues with the potential to affect the safety and soundness of regulated banks, mainly by attempting to force banks to better account for risks assumed by extending credit to cardholders. The guidance provided few protections for consumers, and in at least one instance – the guidance regarding workout agreements – mandated harsher treatment of consumers by banks. Originally aimed at subprime card issuers, the FFIEC guidance was extended to all credit card issuers after regulators observed that some of the practices “first noticed in the subprime lending shops were also occurring in the prime shops.”<sup>73</sup>

In 2004, the OCC issued an advisory letter identifying a number of unfair and deceptive acts and practices in the marketing of credit cards,<sup>74</sup> including:

- Promoting credit cards with credit limits “up to” a specified dollar amount if the “up to” amount is essentially illusory because most applicants do not receive this amount of credit.
- Offering promotional rates without disclosing material terms and limitations, such as time limits on the promotional rate, circumstances that could shorten the period the rate is in

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<sup>70</sup> “FTC, States Give ‘No Credit’ to Finance-Related Scams in Latest Joint Law Enforcement Sweep,” release from the Federal Trade Commission, Sept. 5, 2002. One scam charged a fee of as much as \$499, and delivered dummy cards with non-magnetic stripes. Others charged upfront fees ranging from \$79 to \$219, then sent customers applications for bank credit cards. One marketer promised a “platinum” card to those who paid an advance fee of \$189, then delivered a card good only to buy merchandise from its own catalog. A Canadian telemarketer charged \$199, then never sent consumers any cards at all.

<sup>71</sup> The Federal Financial Institutions Examination Council (FFIEC) is a joint body composed of the federal banking agencies.

<sup>72</sup> Federal Financial Institutions Examination Council, Credit Card Lending Account Management and Loss Allowance Guidance, (Jan. 2003), *available at* [www.federalreserve.gov/BoardDocs/press/bcreg/2003/20030108/attachment.pdf](http://www.federalreserve.gov/BoardDocs/press/bcreg/2003/20030108/attachment.pdf).

<sup>73</sup> Rob Garver, Card Crackdown Goes Beyond Subprime, *American Banker*, January 6, 2003.

<sup>74</sup> OCC Advisory Letter AL 2004-10 (Sept. 14, 2004), *available at* [www.occ.treas.gov/Advlst04.htm](http://www.occ.treas.gov/Advlst04.htm).

effect or cause the rate to increase and limits on the types of charges or balances to which the rate will apply. The OCC also warned against failing to disclose potential balance transfer fees or other fees, or failing to disclose a policy of applying payments to promotional balances first.

- Failing to disclose in promotional materials when the bank can increase a consumer's interest rate or fees, or take other action to increase the cost of credit.

A second OCC advisory letter issued later that year addressed potentially unfair or deceptive practices in the marketing of secured credit cards. The letter especially disapproved of banks allowing fake security deposits to be "charged" to the credit card.<sup>75</sup>

The Fed has proposed, as part of its overhaul of credit card disclosures, to require special disclosures for subprime credit cards. The Fed has proposed that, if the initial fees on a card eat up more than 25% of a credit limit, then the creditor must disclose that fact in the table required for disclosures, often called the "Schumer box."<sup>76</sup> While this specialized disclosure is a positive proposal, it is but a small component in any set of protections that would be necessary to help consumers avoid the abuses of fee-harvesters.

While these guidance documents spotlight some practices that harm consumers, abuses continue. Substantive protection for consumers will require tougher laws, stronger rules and much more extensive enforcement resources at the state and federal level.

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<sup>75</sup> OCC Advisory Letter AL 2004-4 (April 28, 2004), *available at* [www.occ.treas.gov/Advslt04.htm](http://www.occ.treas.gov/Advslt04.htm).

<sup>76</sup> 72 Fed. Reg. 32, 948, 32,954 (June 14, 2007).

## PART III: THE PLAYERS

### A. CompuCredit: The Soul of a New (Fee-Harvesting) Machine

#### *CompuCredit's Rise*

CompuCredit rose quickly to establish itself as a leading marketer of subprime credit cards and assemble a billion-dollar portfolio of fee-harvester cards. The company was formed in 1997 in Atlanta by two brothers who had worked in the debt collection industry – including at a leading debt collection firm that had been founded by their father. Several of the top executives at CompuCredit previously worked at Equifax, another Atlanta firm that is one of the big three credit bureaus.<sup>77</sup>

CompuCredit is one of several companies that have claimed to have found the key to taking much of the risk out of making high-cost loans to “subprime” consumers. Unlike many of its counterparts – including some much larger – CompuCredit managed to survive the shakeout of the subprime lending industry that followed the 2001 recession.

In fact, CompuCredit took advantage of the downturn to snap up portfolios of subprime credit card accounts from several distressed competitors buffeted by rising charge-offs, falling stock prices and impatient creditors. Other CompuCredit units collect debts, finance automobiles and make payday loans.<sup>78</sup>

But cards remain the main source of profits at CompuCredit which, with \$2.5 billion in receivables, ranked 17<sup>th</sup> among all issuers of Visa and MasterCard in terms of money owed it by cardholders. Reflecting the limited buying power of its cards, CompuCredit ranked only 34<sup>th</sup> in transaction volume.<sup>79</sup>

CompuCredit's expansion has been bankrolled by Wall Street. In 2002, for example, two leading investment banks – Goldman Sachs and Citigroup's Salomon Smith Barney unit – formed a joint venture with CompuCredit that bought at a discount a \$1.5 billion portfolio of accounts for cards originally issued by Providian. The next year, Merrill Lynch joined with CompuCredit to buy another portfolio of Providian accounts, this with a face value of \$824 million. In 2005, Merrill Lynch and CompuCredit partnered again to buy a \$376 million portfolio of receivables on credit cards issued by BANKFIRST Corp., a South Dakota bank.<sup>80</sup>

In March 2006, several hedge funds and big private investors ponied up \$300 million to back CompuCredit's fee-harvester card business. In that deal, put together by Bear Stearns & Co., CompuCredit issued convertible notes secured by its portfolio of fee-harvester card receivables.<sup>81</sup>

Earlier, another Wall Street giant provided crucial backing to CompuCredit. In 2001, an investment fund controlled by JPMorgan Chase, the nation's third largest bank, ponied up \$25 million to help CompuCredit ride out the recession.<sup>82</sup> That investment fund, Corsair Capital, was later spun off by the

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<sup>77</sup> CompuCredit, Form 424B4, April 23, 1999, at 32, 43-44.

<sup>78</sup> CompuCredit 2006 Form 10-K at 1-5.

<sup>79</sup> The Nilson Report, August 2007, Issue 886, p. 10-11.

<sup>80</sup> CompuCredit 2006 Form 10-K at 1-2.

<sup>81</sup> CompuCredit, Form S-3, March 10, 2006, at 1-2.

<sup>82</sup> “CompuCredit Completes Private Equity Placement,” Business Wire, Dec. 27, 2001; CompuCredit Form S-3A, filed Nov. 3, 2003, p. 2.

bank but still holds 2.9 million shares, or a 5.5 percent ownership interest, in CompuCredit. Corsair's chairman, a former J.P. Morgan Chase executive, has a seat on CompuCredit's board.<sup>83</sup>

In recent months, uncertainty in the credit markets has helped sour investors on CompuCredit's stock. In late September, CompuCredit's stock price of just over \$20 was down nearly 50 percent from its 52-week high, although that still gave the company a market value of \$1.1 billion.

### *CompuCredit Wants a Bank*

Throughout its short history and rapid growth in the subprime card market, CompuCredit has lacked one powerful tool: a bank. In order to take advantage of bank preemption and impose the high charges that make fee-harvester cards profitable, CompuCredit has needed to find banks that would "issue" the cards.

Although some marketers of fee-harvester cards own or are affiliated with banks, CompuCredit has been rebuffed in three separate attempts to get its own bank. In May 1999, the Georgia Department of Banking and Finance approved CompuCredit's application for a new bank charter, but rescinded that action in December 2001.<sup>84</sup>

Then, in 2003, citing worries about CompuCredit's financial condition and the competence and experience of its management, the Office of the Comptroller of the Currency rejected CompuCredit's application to buy Sioux Falls, S.D., based Axsys National Bank from Federated Department Stores.<sup>85</sup>

And in 2006, CompuCredit dropped its bid to acquire rival card issuer CardWorks Inc. and its Utah-based Merrick Bank, an industrial loan bank, after the FDIC announced a moratorium on such acquisitions.<sup>86</sup> CompuCredit had the backing of Merrill Lynch in that aborted \$302-million deal.<sup>87</sup> Frustrated in its attempts to get its own bank charter, CompuCredit has been forced to rely on partnerships with existing banks to keep its credit card rates and terms beyond the reach of state regulators.<sup>88</sup>

### *Enter Urban Trust*

Last year, CompuCredit found what at first glance appeared to be an unlikely partner: Urban Trust Bank, a small savings institution with branches in the District of Columbia and Florida. CompuCredit and Urban Trust signed a contract in December 2006, under which the bank would issue, and CompuCredit would market and administer, the accounts of a new credit card.<sup>89</sup>

Urban Trust's owner is billionaire Robert L. Johnson, the founder of the cable-based Black Entertainment Television network. Johnson, who in 2001 sold his majority interest in BET in a \$3

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<sup>83</sup> CompuCredit Corp. Form DEF 14A, filed April 10, 2007, p. 25.

<sup>84</sup> Georgia Department of Banking Finance, 2001 Annual Report, p. 17.

<sup>85</sup> Comptroller of the Currency, Administrator of National Banks, Corporate Decision #2003-11, October 2003, p. 2-3.

<sup>86</sup> David Breikopf, *CompuCredit Needs a Plan B*, *The American Banker*, Aug. 4, 2006, at 1.

<sup>87</sup> CompuCredit 2006 Form 10-K at 5.

<sup>88</sup> These arrangements resemble "rent-a-bank" deals in which payday lenders partnered with banks in order to make ultra-high-cost loans in states with restrictive usury laws. Federal regulators have recently forced banks to end these arrangements with payday lenders.

<sup>89</sup> CompuCredit Corp. Form DEF 14A, filed April 10, 2007, p. 23. Under the arrangement, Urban Trust will receive 5 percent of the payments and cover 5 percent of the net purchasing, marketing, servicing and collection costs of the joint venture. Urban Trust advanced CompuCredit \$750,000 to cover future expenses and CompuCredit deposited \$300,000 with Urban Trust to cover purchases by cardholders.

billion deal, characterizes his bank as one that will benefit disadvantaged consumers and communities. Urban Trust is a “well-capitalized, well-managed black-owned financial institution,” he told the Washington Post in 2006. He added that Urban Trust would “bring more access to capital to individuals and families who need it, especially those that need help managing their assets and their wealth in a better way.”<sup>90</sup>

Urban Trust has found a powerful ally in that “mission”: Wal-Mart Inc., the world’s largest retailer. Wal-Mart has been angling to expand its financial services offerings, forming multiple partnerships with banks and attempting to create its own bank. In January 2007, Wal-Mart struck a deal with Urban Trust to lease space and open retail bank branches inside some Wal-Mart stores. “Urban Trust Bank brings banking services to Wal-Mart customers in underserved urban and minority communities,” said Wal-Mart Chief Executive Lee Scott. “I’m proud to embark upon a strategic alliance with Bob Johnson and Urban Trust Bank to bring affordable financial services to these communities.”<sup>91</sup>

Urban Trust’s deal with CompuCredit – announced in December 2006, just a month before Urban Trust signed its deal with Wal-Mart to bring “affordable” banking services to minority communities – came with less fanfare. And some of the financial services offered through Urban Trust’s credit card alliance with CompuCredit are hardly “affordable.” Consider this solicitation, posted on the Internet on July 1 by Urban Trust and CompuCredit for a Salute Visa credit card with a \$70 credit line. After paying, in cash, a \$20 account opening fee and deducting a \$19 monthly participation fee, a cardholder will receive the privilege to charge goods and services up to ..... \$51!

Worse still, that \$51 of buying power will come at a cost that will approach or exceed the cost of getting the same cash for the same period through a payday loan.

Lender/creditor	Available Credit	Initial Fee	Recurring Fee	cost for one year	APR (if all fees included)
MySaluteCard.com from Urban Trust Bank and CompuCredit	\$51	\$20	\$19 per month	\$248	486%
ACE Cash Express, Fla	\$50	n/a	\$7 per 14 days	\$182	364%

Over a year, a cardholder who pays in full each monthly balance would still pay as much for the \$51 credit line as a borrower who took out and rolled over a payday loan for \$50 at an annual percentage rate of 364%. The cost of the Salute card would be even higher if the customer incurred any over-limit fees.

That fee-harvester cards marketed by CompuCredit saddle customers with costs comparable to a payday loan is no shock considering that CompuCredit also owns and operates a chain of 475 payday loan stores in 17 states and the United Kingdom.

While a partnership with a payday lender may seem at odds with Johnson’s pronouncements about Urban Trust’s mission, in reality the apple has not fallen far from the tree. Johnson bought Urban Trust from Frank Hanna Jr., who is the father of CompuCredit Chief Executive David Hanna, made a fortune

<sup>90</sup> Terence O’Hara, *Johnson Buys Bank to Build Black-Focused Financial Firm*, Washington Post, March 15, 2006, at A1.

<sup>91</sup> *Urban Trust Bank to Open Bank Branches Inside Select Wal-Mart Supercenters*, PR Newswire, Jan. 24, 2007.

in the debt collection industry, retains a “substantial minority interest in Urban Trust” and has a seat on its board.<sup>92</sup>

By June 2007, holders of the new cards owed \$4.5 million in fees and other charges to CompuCredit and Urban Trust.<sup>93</sup> But in October, Urban Trust’s web site no longer linked to the Salute card site and instead directed visitors to check back later because the bank was “working to improve the information currently available on our credit card products.”<sup>94</sup>

## **B. CompuCredit Crosses the Line**

CompuCredit has other bank allies that enable it take advantage of preemption, including a long-standing relationship with a little known Georgia institution called Columbus Bank & Trust Company. Columbus Bank is a subsidiary of Synovus, the nation’s 35th-largest bank holding company. Columbus Bank issues CompuCredit’s trademarked Aspire Visa card.<sup>95</sup>

Synovus, which is chartered in Georgia, is a big player in the credit card industry through its Total System Services subsidiary. Total System Services, which recently took over processing transactions for Capital One, accounted for a third of Synovus profits in the second quarter of 2007.<sup>96</sup>

While CompuCredit’s alliance with Synovus’ Columbus Bank unit has shielded the high costs and fees of the Aspire card from scrutiny by state regulators, Columbus’s status as a state-chartered bank means that its marketing and collection abuses can be challenged. And when New York’s Attorney General recently did just that, CompuCredit and Columbus Bank took an \$11 million hit.

The New York AG alleged that CompuCredit and the Synovus unit used misleading disclosures in a marketing campaign that sold New York consumers two versions of the Aspire card, including one for consumers with “extremely low credit scores” that delivered a \$300 credit line – consumed by \$179 of initial fees!<sup>97</sup> Consumers with “slightly better credit scores” got cards with lower fees but higher interest rates and a \$1,800 line of credit but only \$900 available during the first four months they held the card.<sup>98</sup>

The Attorney General also accused CompuCredit and Columbus Bank of violating New York law by pressuring cardholders to pay the fees even before they had used their cards, and to pay for memberships in “buyers programs” which the cardholders had not joined.<sup>99</sup> Cardholders who failed to pay were yelled at, hung up on, called repeatedly at work and had messages left with their neighbors, according to the Attorney General.<sup>100</sup>

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<sup>92</sup> CompuCredit Corp. Form DEF 14A, filed April 10, 2007, p. 23.

<sup>93</sup> CompuCredit Form 10Q filed Aug. 1, 2007, p. 46.

<sup>94</sup> Urban Trust Bank web site, <http://www.urbantrustbank.com/pers%20credit%20card.cfm>, visited Oct. 18, 2007. An Urban Trust spokeswoman said the link was taken down as Urban Trust prepares to issue its own branded credit cards and that it continues to partner with CompuCredit and to issue Salute cards. Email from Urban Trust spokeswoman Xina Eiland, Oct. 19, 2007, on file with authors.

<sup>95</sup> CompuCredit, Form 10-K for the Fiscal Year Ended December 31, 2004, at 6. In addition to the term Aspire, CompuCredit has also trademarked the terms “Emerge,” “Imagine,” “Majestic,” “Purpose” and “Tribute.” CompuCredit 2006 Form 10-K at i.

<sup>96</sup> Synovus Financial Corp., Form 10Q for the period ended June 30, 2007, at 19-20.

<sup>97</sup> Assurance of Discontinuance, *In the Matter of Columbus Bank and Trust Co. and CompuCredit Corp.*, New York Attorney General’s Office, June 30, 2006, at 2-4, available at [www.oag.state.ny.us/press/2006/jul/Aspire%20Visa%20Assurance.pdf](http://www.oag.state.ny.us/press/2006/jul/Aspire%20Visa%20Assurance.pdf).

<sup>98</sup> *Id.* at 2.

<sup>99</sup> *Id.* at 4.

<sup>100</sup> *Id.* at 5.



CompuCredit and Columbus Bank, without admitting or denying the findings, agreed to pay \$500,000 in civil penalties, \$25,000 in costs and \$11 million in restitution to customers, and to refrain from engaging in those illegal practices in the future.<sup>101</sup>

CompuCredit recently warned investors that more trouble may be on the way. Investigations begun by the FDIC in June 2006 and the FTC six months later have focused upon “whether marketing and other materials contained misrepresentations regarding, among other things, fees and credit limits” and the company’s “servicing and collection practices.” Both agencies have sought to limit some marketing, servicing and collection practices and make CompuCredit reimburse customers and pay fines. CompuCredit says the investigation touches upon “a significant amount of fees and a substantial number of accounts” and that it is “vigorously contesting the proposed reimbursement of fees and payment of fines.”<sup>102</sup>

#### A DYNASTY OF DEBT

At CompuCredit, profiting from debt runs in the family. For example, one of its early investors was Frank Hanna Jr., founder of Nationwide Credit, one of the country’s largest debt collection firms, which he sold in 1990 in a \$65 million deal.<sup>103</sup>

Hanna’s two sons – Frank III and David – followed in their father’s footsteps at Nationwide Credit. In 1989, Frank Hanna III founded another debt management firm, Account Portfolios and, after his brother joined the company, it was sold in an \$80-million deal in 1995.<sup>104</sup>

An ensuing venture into the health insurance industry sparked opposition from consumer advocates. Taking advantage of legal and corporate changes at Blue Cross, in 1995 the two brothers ponied up \$40 million to acquire a controlling interest in Georgia’s largest health insurance provider.<sup>105</sup> While the initial deal’s failure to set aside money to extend coverage to low-income patients triggered lawsuits, it worked out well for the Hannas, who pocketed a pre-tax profit of \$86 million when they eventually sold Georgia Blue Cross.<sup>106</sup>

Even before their Blue Cross adventure ended, the Hanna brothers launched CompuCredit. Although the stock is publicly traded, a majority of the company – 52.8 percent – remains in the brothers’ hands. At the stock’s recent trading price around \$24, their stake – which is evenly divided between them – is worth well over \$600 million.

### **C. Warning: These Banks May Be Dangerous To Your Financial Health**

The growth of subprime credit cards, coupled with the regulatory void created by preemption and inadequate enforcement, mean that consumers must look skeptically through any door that opens to invite them to an offer of credit that seems surprisingly attractive. A recent report by the Government

<sup>101</sup> *Id.*; Press Release, “Sub-Prime Credit Card Issuer To Provide \$11 Million in Restitution, Companies Agree to Halt Deceptive Practices,” New York Attorney General’s Office, July 3, 2006.

<sup>102</sup> CompuCredit Corp. Form 10-Q, filed Aug. 1, 2007, p. 19.

<sup>103</sup> *First Financial Management Corp. Announces Nationwide Credit Acquisition Agreement*, Business Wire, May 29, 1990.

<sup>104</sup> Form S-4 filed by Outsourcing Solutions, Nov. 26, 1996, at 65, F-8.

<sup>105</sup> Andy Miller, *Blue Cross Near End of Its Tale of Turmoil; Six-year saga*, Atlanta Journal and Constitution, Feb. 11, 2001, at 1P.

<sup>106</sup> Andy Miller, *Blue Cross Near End of Its Tale of Turmoil; Six-year saga*, Atlanta Journal and Constitution, Feb. 11, 2001, at 1P.

Accountability Office argued that big banks' concerns about their brands and reputations might make them reluctant to gouge cardholders.<sup>107</sup>

But for consumers, more than a "brand name" is needed to ensure that an advertised card is not a fee-harvester. Only a close look at the terms and conditions of an offered card can explain whether it is a cost-effective source of credit and convenience.

Comparison shopping can be difficult. An August Internet search for credit cards for consumers with bad credit showed a confusing array of cards available, and no clear, reliable road map for avoiding predators.

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<sup>107</sup> The Government Accountability Office noted "Federal Reserve representatives told us that major card issuers with long-term franchise value are concerned that their banks not be perceived as engaging in predatory lending because this could pose a serious risk to their brand reputation. As a result, they explained that issuers may be wary of charging fees that could be considered excessive or imposing interest rates that might be viewed as potentially abusive." *See* GAO Credit Card Report at 30.

A Sampling of Cards Offered to Consumers with "Bad Credit"

Brand	Bank issuer	Marketing for Trademark Partner	Federal Regulator	Credit Limit	Disclosed Opening Available Credit	Mandatory Opening Fees	Mandatory Annual Fees	Late Payment Fee	Overlimit Fee	Initial APR	Misc
Imagine Gold MasterCard \$300 card	First Bank of Delaware	CompuCredit	FDIC, state-chartered by Delaware	\$300	\$150	\$154.95 (\$150 annual fee, \$4.95 opening fee)	\$78 (\$6.50/mo account maint fee)	\$35	\$35	19.75%	unspecified credit limit increase after 6 months, add credit limit if used for car rental, hotel
Imagine Gold MasterCard \$70 card	First Bank of Delaware	CompuCredit	FDIC, state-chartered by Delaware	\$70	\$55	\$19.95 (\$15 annual fee, 4.95 opening fee)	\$228 (\$19/mo account maintenance fee)	\$5 to \$35	\$25	19.50%	monthly unspecified credit limit increase over first year, add credit limit if used for car rental, hotel
Continental Finance MasterCard	First Bank of Delaware		FDIC, state-chartered by Delaware	\$300	\$63	\$188 (\$98 set up, \$89 participation)	\$189 (\$49 annual, \$10/mo account maint)	\$30		19.92%	
Centennial Gold MasterCard	First Premier Bank		FDIC, state-chartered by South Dakota	\$250	\$72	\$244 (\$29 setup fee, \$95 program, \$48 annual, \$6 mo participation)		\$25	\$25	9.90%	
Orchard Bank Platinum MasterCard	HSBC Bank Nevada National Assn		Office of the Comptroller of the Currency	not disclosed on web site		0-\$29	\$39-\$89			8.9-14.9%, then 19.5%, then adjustable to prime plus 1.25%	requires \$20 initial payment in cash
Salute Visa Gold \$300	Urban Trust Bank	CompuCredit	Office of Thrift Supervision	\$300	\$170	\$222 (\$150 annual, \$6/mo acct maint)		\$35	\$35	14.99%, then adjustable to prime plus 6.74%	
Salute Visa Gold \$70	Urban Trust Bank		Office of Thrift Supervision	\$70	\$70	\$248 (\$19/mo acct maint fee, \$20 account opening fee paid in cash)		\$5 to \$35	\$25		
Capital One Classic Platinum	Capital One Bank		Federal Reserve Bd, state-chartered by Virginia	\$300 to \$3,000			\$19 membership	\$19-\$39	\$19-\$39	0 initially, then on 2/2/08 goes to 14.9%	
Capital One Platinum Max	Capital One Bank		Federal Reserve Bd, state-chartered by Virginia	\$300 to \$2,500			\$19 membership	\$19-\$39	\$19-\$39	16.9%, advertised as fixed, "won't increase for 3 years - no matter what"	
Capital One Platinum	Capital One Bank		Federal Reserve Bd, state-chartered by Virginia	\$300 to \$3,000			\$39 membership	\$19-\$39	\$19-\$39	0% thru 2/08, then 8.9%, adjusted quarterly to prime plus 0.65%	
Capital One Standard Platinum	Capital One Bank		Federal Reserve Bd, state-chartered by Virginia	\$300 to \$3,000			none	\$19-\$39	\$19-\$39	0% thru 2/08, then 19.8%, adjusted quarterly to prime plus 11.55%	

Some of the banks that use the fee-harvester model to a significant degree include:

*First Premier*

The Hannas aren't the only folks who have gotten rich marketing cards and collecting fees from society's poorest and most disadvantaged consumers. In fact, they aren't even the richest. That distinction belongs to T. Denny Sanford, who has amassed a \$2.8 billion fortune as the founder and owner of First Premier Bank of Sioux Falls, S.D.<sup>108</sup>

South Dakota became a mecca of the credit card industry, after the state rewrote its banking laws in 1981 in a successful bid to lure banks to relocate onto the prairie. Taking advantage of the looser laws, Sanford, who became wealthy selling construction materials, bought a South Dakota bank in 1986, renamed it First Premier and hired a former Citigroup executive to run it.<sup>109</sup>

Sanford has done very well for himself. He estimated his net worth at \$55 million in a 1995 divorce, so using that as a benchmark his fortune has increased more than 50-fold in only a dozen years.<sup>110</sup> The main source of that wealth has been the bank, with a current market value that Forbes magazine put in a range from \$2 billion to \$3 billion. This year First Premier expects to post total revenue of \$810 million (including fee revenue of more than \$600 million), enough to charge off \$400 million in uncollectibles and still post \$310 million in pretax profits.<sup>111</sup>

These tremendous profits are generated in part from First Premier's fee-harvesting cards (like the one that snagged the sailor in Bremerton, Washington). According to its website, First Premier's credit card arm is among the top 11 VISA and MasterCard issuers, with over 3.7 million customers.<sup>112</sup>

Sanford casts a long shadow in Sioux Falls, where his bank's work force of 1,100 makes it South Dakota's ninth largest employer.<sup>113</sup> His profile rose dramatically last year when he pledged \$400 million over eight years to a local hospital that immediately changed its name to Sanford Health.<sup>114</sup>

First Premier's nationwide credit card marketing eventually drew the attention of regulators outside South Dakota. In 2003, the Federal Reserve intervened to require First Premier to boost reserves in order to protect depositors from possible losses in the bank's rapidly growing subprime credit card business. That action did nothing to protect consumers of First Premier's fee-harvester cards.<sup>115</sup>

The fee harvesting continued, and in August 2007, First Premier was the subject of enforcement action by the Attorney General of New York, where the bank had marketed unsecured cards for 18 years. The Attorney General alleged that that the bank had advertised cards "with no processing fee" but charged \$178 in initial fees to open an account with a \$300 credit limit. He also alleged that the bank violated

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<sup>108</sup> David Whelan, *Dying Broke*, Forbes Magazine, Oct. 8, 2007, at 232.

<sup>109</sup> David Whelan, *Dying Broke*, Forbes Magazine, Oct. 8, 2007, at 232.

<sup>110</sup> Maura Lerner, *Billionaire has healthy goal for his wealth; Saying he wants to die broke, St. Paul native T. Denny Sanford is giving millions to Midwest medical groups?* The Minneapolis Star Tribune, Feb. 18, 2007, at 1B.

<sup>111</sup> David Whelan, *Dying Broke*, Forbes Magazine, Oct. 8, 2007, at 232.

<sup>112</sup> <http://www.firstpremier.com/bankcard/acquainted/acquainted.html> (viewed April 13, 2007).

<sup>113</sup> Peter Harriman, *Credit Limits Could Rattle Sioux Falls*, The Sioux Falls Argus Leader, Aug. 13, 2007, at 1A. Other big credit card employers in Sioux Falls include Citi, with 3,200, Wells Fargo, with 3,050 and HSBC with 875.

<sup>114</sup> Ben Gose, *Great Plains Generosity*, Chronicle of Philanthropy, Feb. 8, 2007, at 7.

<sup>115</sup> *Written Agreement by and among United National Corporation, Sioux Falls, South Dakota; First PREMIER Bank, Sioux Falls, South Dakota; PREMIER Bankcard, Inc., Sioux Falls, South Dakota; and the Federal Reserve Bank of Minneapolis*, Federal Reserve Board, September 25, 2003, available at <http://www.federalreserve.gov/Boarddocs/Press/enforcement/2003/20030925/attachment.pdf>.

New York law by billing cardholders for the initial fees before they had even used their cards, deceiving consumers by offering them credit limits “up to \$2,000,” and labeling cards gold or platinum to give them “the cache (sic) traditionally associated with elite credit cards.”<sup>116</sup>

First Premier Bank neither admitted nor denied wrongdoing but agreed to pay \$100,000 in civil penalties and \$5,000 in costs and refund \$4.5 million to its New York customers. The Attorney General noted that First Premier had stopped some of the challenged practices on its own initiative and the bank agreed to refrain from illegal billing and deceptive marketing practices in the future.<sup>117</sup>

*Applied Bank, or the Subprime Lending Artist formerly known as Cross Country*

Privately owned Applied Bank gained notoriety as a subprime credit card pioneer after it was chartered in 1996 as Cross Country Bank in banker-friendly Delaware. Two name changes later, Applied has shown a penchant for getting tough with cardholders, former employees and elected officials who challenge it.<sup>118</sup>

News coverage at the time of the bank’s creation focused upon its plans to issue secured credit cards. However, the bank soon gravitated toward fee-harvester cards, advertising credit limits of up to \$2,500 but issuing cards with limits of \$400 or less and origination and annual fees of \$150.<sup>119</sup>

Applied’s lending practices prompted a series of lawsuits by attorneys general from New York, Wisconsin, Texas, Pennsylvania, Minnesota and West Virginia. In May 2004, a New York judge found that the bank had engaged in “repeated and persistent fraudulent, illegal and deceptive practices.”<sup>120</sup>

Three months later, the FTC announced that Applied’s debt collection affiliate had entered into a consent order to settle a complaint that it had illegally called cardholders’ relatives, neighbors and employers, as well as used obscene and abusive language in its collection calls.<sup>121</sup> Without admitting to any violations, Applied agreed to refrain from illegal collection practices in the future.<sup>122</sup>

*First Bank of Delaware*

Tiny First Bank of Delaware, which specializes in lending to disadvantaged or vulnerable consumers, has partnered with CompuCredit to issue fee-harvester and prepaid cards.<sup>123</sup> In November 2005, First Delaware agreed to issue Discover cards that would be marketed by CompuCredit’s Purpose Solutions

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<sup>116</sup> Assurance of Discontinuance, *In the Matter of First Premier Bank*, New York Attorney General’s Office, July 23, 2007, at 1-3, available at <http://www.oag.state.ny.us/press/2007/aug/First%20Premier%20Bank%20Settlement.pdf>.

<sup>117</sup> *Id.* at 4, 6. See also Press Release, *Attorney General Cuomo Announces \$4.5 Million Settlement in Sub-Prime Credit Card Probe*, New York Attorney General’s Office, Aug. 15, 2007.

<sup>118</sup> Mitchell Pacelle, *Pushing Plastic: Combative Banker Faces State Suits Over Credit Cards*, Wall Street Journal, Nov. 5, 2004, at 1.

<sup>119</sup> Affirmation, *People of the State of New York v. Applied Card Systems Inc and Cross Country Bank*, March 28, 2003, at 4-5. See also Jonathan D. Epstein, *Consumers Sue Cross Country Bank*, Wilmington News Journal, April 20, 2003, at 17F; Mitchell Pacelle, *Pushing Plastic: Combative Banker Faces State Suits Over Credit Cards*, Wall Street Journal, Nov. 5, 2004, at 1.

<sup>120</sup> *People v. Applied Card Sys., Inc.*, No. 2073-03 (N.Y. Sup. Ct. May 28, 2004) (transcript of proceedings), available at <http://www.oag.state.ny.us/press/2004/jul/6a.pdf>.

<sup>121</sup> “Two Companies Settle Harassment Charges Relating to Debt Collection,” Federal Trade Commission, release of Aug. 25, 2004; also Complaint in the Matter of Applied Card Systems Inc, et al, Federal Trade Commission, 2004.

<sup>122</sup> Agreement Containing Consent Order, *In the Matter of Applied Card Systems Inc*, Federal Trade Commission, Oct. 6, 2004.

<sup>123</sup> First Bank of Delaware, Form 10-KSB for the Fiscal Year Ended December 31, 2006, at 48.

unit.<sup>124</sup> First Delaware also issues cards that use CompuCredit's Imagine and Tribute trademarks, including a TributeGold MasterCard that comes with a \$70 credit limit that is quickly consumed by a \$20 opening fee and a \$19 per month (or \$228 per year) maintenance fee.

First Delaware recently disclosed it was in talks “regarding concerns raised by the FDIC in connection with certain of the Bank’s credit card and lending programs” and that “the FDIC may pursue an informal or formal regulatory action.”<sup>125</sup>

Earlier, prodding from the FDIC prompted First Delaware to break its ties with payday lenders, who partnered with the bank in a “rent-a-bank” arrangement. The FDIC warned First Delaware that it should stop partnering with third parties to make payday loans because of “perceived reputational, compliance and legal risks,” and the bank shut down that operation.<sup>126</sup> First Delaware also made pricey refund anticipation loans until 2006.<sup>127</sup>

Controversy about First Delaware’s ties to payday lenders and refund anticipation loans prompted its 2005 spin-off by its former parent, Republic First Bancorp.<sup>128</sup> In reporting the separation, the Philadelphia Inquirer quoted a financial analyst who said that the spin-off would “remove the ‘blemish’ of ‘predatory lending’” from Republic First and make it ‘a far more attractive acquisition candidate.’<sup>129</sup> Yet First Delaware and Republic First remain closely tied with common ownership and top executives.<sup>130</sup> They also share data-processing, accounting, personnel and regulatory compliance operations.<sup>131</sup>

#### *First National Bank of Pierre, S.D.*

There are plenty of banks around the country with the words “First National” in their moniker. When the “First National” you’re hearing from hails from Pierre, the state capital of banker-friendly South Dakota, or from nearby Fort Pierre, beware.

Thelma Perry’s case, discussed at the beginning of this report, wasn’t First National of Pierre’s first accusation of abusive credit card lending. In a regulatory action initiated against First National of Pierre after an examination in 2001, the OCC reached a settlement prohibiting the bank from misleading and deceptive advertising of its credit cards. The OCC directed First National of Pierre to take steps to prevent future deceptive advertising concerning credit lines and the amount of initial available credit.<sup>132</sup>

Recently, First National of Pierre opened a new frontier in the subprime card market. In conjunction with a Southern California marketing company called Green Dot Corp., the bank launched a pilot project in which Visa Gold cards with a \$200 credit limit are sold for \$89.95 at checkout counters of

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<sup>124</sup> *Purpose Solutions LLC to Launch New Credit Card on Discover Network*, Business Wire, Nov. 1, 2005. See also First Bank of Delaware, Form 10-KSB for the Fiscal Year Ended December 31, 2006, at 42.

<sup>125</sup> *First Bank of Delaware Reports 342% Increase in Second Quarter Earnings and 75% Increase in Year-To-Date Earnings*, PRNewswire, July 17, 2007.

<sup>126</sup> First Bank of Delaware, Form 10-KSB for the Fiscal Year Ended December 31, 2006, at 18.

<sup>127</sup> Benjamin Lowe, *Bank Says It Will End Tax-Refund Lending*, Philadelphia Inquirer, July 27, 2006 at C1.

<sup>128</sup> First Bank of Delaware, Form 10-KSB for the Fiscal Year Ended December 31, 2006, at 3.

<sup>129</sup> *Business News in Brief*, Philadelphia Inquirer, Nov. 2, 2004, p. D3.

<sup>130</sup> Harry Madonna is the chief executive of both banks, and Madonna and investor Harris Wildstein are two the largest shareholders in each bank. See First Bank of Delaware, Notice of Annual Meeting of Shareholders to be Held on April 17, 2007, at 4, 18; Republic First Bancorp, Schedule 14A, March 23, 2007, at 22.

<sup>131</sup> First Bank of Delaware, Notice of Annual Meeting of Shareholders to be Held on April 17, 2007, p. 19.

<sup>132</sup> See Agreement By And Between First National Bank, Ft. Pierre, South Dakota and the Office of the Comptroller of the Currency, No. 2002-61 (Dept. of Treasury, Office of the Comptroller of Currency July 18, 2002), available at <http://www.occ.gov/FTP/EAs/ea2002-61.pdf>.

Rite Aid drug stores. An executive of Green Dot defended the cards because “the fees are lower than what subprime consumers would pay at payday lenders.”<sup>133</sup>

## **D. Big Banks That Cross the Line in Subprime**

Extracting fees from consumers trapped in the high-cost world of subprime borrowing isn't just for piranhas. Some big fish swim in that pond as well, including two banks – Capital One and HSBC – that rank among the five largest MasterCard and Visa issuers. Both have high-profile brands in the subprime credit card market that have been cited by regulators for using abusive marketing and collection practices.

### *Capital One*

In the subprime card industry, no machine is better oiled than that of Capital One. A key lubricant: the \$1.4 billion a year that the bank spends on marketing efforts ranging from direct mailings, ubiquitous television commercials and sponsorship of a college football bowl game.<sup>134</sup>

Heavy investment in its brand has helped Capital One climb to the number four position among Visa and MasterCard issuers, with cards for prime as well as subprime consumers. In 2006, its domestic credit card business posted net income of \$1.8 billion on revenue of \$8 billion.<sup>135</sup>

In 2002 Capital One disclosed that about 40 percent of its credit card assets were in subprime accounts.<sup>136</sup> Three years later, according to the bank, it deemphasized squeezing short-term profits out of subprime customers.<sup>137</sup>

While there is no ready measure of how well the bank has implemented that shift, the experiences of some consumers show that at the least it had plenty of work to do. And while the bank does not disclose how many of its subprime cards are fee-harvesters, whether it is a large or small percentage doesn't matter for people like Gabor Marsi, a 39-year-old Akron, Ohio, air conditioner repairman.

Marsi applied for and got a Capital One MasterCard after he emerged from a bankruptcy caused by the family's unexpected medical expenses. Capital One made Marsi pay a \$50 application fee and gave him a card with a \$200 credit limit. Capital One also sought to get Marsi to sign up for a “diner's club” membership. “We are not interested,” Marsi recalls telling the marketer. “We are just trying to get back on our feet.”

But Capital One didn't take no for an answer. After Marsi and his wife used the card to charge a \$130 baby crib, they were shocked to discover that the card had been charged \$99 for the diner's club membership, and that the card's credit limit had been exceeded. The Marsis ended up paying \$700 to

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<sup>133</sup> H. Michael Jalili, *Green Dot's Test of Store-Sold Product Extended*, February 23, 2007, at 5; H. Michael Jalili, *Green Dot Credit Program Coming to More Sites*, August 10, 2007, at 6.

<sup>134</sup> Capital One Financial Corp., Form 10-K Annual Report Pursuant to Section 13 Or 15(d) of the Securities Exchange Act of 1934 for the Fiscal Year Ended December 31, 2006, at 42. [hereinafter “Capital One 2006 Form 10-K”]

<sup>135</sup> Capital One 2006 Form 10-K at 48.

<sup>136</sup> Capital One Financial Corp., Form 8-K, July 16, 2002, at 4.

<sup>137</sup> The bank said it would change its business so as “not to engage in certain repricing practices prevalent in the industry that focus on short-term growth at the expense of customer loyalty and generating long-term profitability.” See Capital One 2006 Form 10-K at 49.

finance their \$130 baby crib and are now fighting a lawsuit by Capital One, which claims Marsi still owes \$3500.<sup>138</sup>

Another Capital One customer who found she had a problem in her wallet was Maryann Strouse, a partially disabled woman in Sunbury, Pa., to whom the bank issued a card in August 1999. Strouse, who is now 73 years old and living on social security payments, had used the card which had an initial credit limit of \$200 “extremely sparingly,” according to her lawyer. Between February of 2000 and June 2005, Strouse made only four purchases for a total of \$430 and paid \$1,190 to Capital One.<sup>139</sup>

That \$1,190 wasn’t enough to satisfy Capital One’s appetite for fees, which had included \$295 for “membership” and \$300 for a “privacy guard” as well as penalties of \$495 for late payments and \$130 for exceeding her credit limit. So in 2006, with the balance on the account accruing interest at an annual rate of 26.9 percent, Capital One sued Strouse for \$1,466.15.<sup>140</sup>

Strouse fought back, and in court filings termed the contract Capital One used to run up her fees as “unconscionable.” The bank rejected Strouse’s offer to settle the debt for \$300<sup>141</sup> and so far the case remains unresolved.

Capital One, which once ran commercials contrasting its lending practices to those of barbarian competitors, has at times flexed its own muscles against debtors. In 2003, it paid \$160,000 to settle a class action lawsuit challenging its debt collection and credit card marketing practices. The lawsuit alleged that Capital One violated the Fair Debt Collection Practices Act by sending out misleading collection letters with improper notices<sup>142</sup> and tried to trick some debtors to forfeit their rights and charge their debts to new “zombie” credit cards issued by the bank.

Capital One has also been accused of violations by state attorneys general in Minnesota and West Virginia. They alleged that Capital One:<sup>143</sup>

- heavily promoted low “fixed APRs,” (including the well known “No Hassle” television advertisements) that implied the interest rates for Capital One cards would never increase, then frequently increased rates for late payments or over-limit transactions and also reserved the right to increase rates for no reason at all.
- sent solicitations to consumers stating they were pre-approved for credit cards with limits “up to” \$5,000, but issued many of the recipients cards with limits as low as \$200.
- refused to cancel cards when requested by consumers and told them the cards could not be canceled so long as there was an outstanding balance.

The Minnesota Attorney General’s lawsuit resulted in a \$1.25 million settlement.<sup>144</sup>

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<sup>138</sup> Interview with Gabor Marsi, July 25, 2007.

<sup>139</sup> Interview Joe DeCristopher, North Penn. Legal Services; Answer, Capital One Bank v. Strouse, Civ. No. CV-07-64 (Pa. Ct. of Common Pleas of Northumberland Cty, July 30, 2007).

<sup>140</sup> Interview Joe DeCristopher, North Penn. Legal Services; Answer, Capital One Bank v. Strouse, Civ. No. CV-07-64 (Pa. Ct. of Common Pleas of Northumberland Cty, July 30, 2007).

<sup>141</sup> Interview Joe DeCristopher, North Penn. Legal Services.

<sup>142</sup> Carbajal v. Capital One, F.S.B., 2003 WL 22595265 (N.D. Ill. Nov. 10, 2003).

<sup>143</sup> See Complaint, State of Minnesota v. Capital One Bank, (Minn. Dist. Ct. – 2nd Jud. Dist. Dec. 30, 2004) available at <http://www.ag.state.mn.us/consumer/PDF/PR/CapitalOneComplaint.pdf>; Press Release, *Attorney General Darrell McGraw Sues Capital One Bank and Capital One Services, Inc.* U.S. State News (July 2005), available from Westlaw at 2005 WLNR 10881649.



In May 2007, President Bush nominated Capital One executive Larry Klane to become one of the seven Governors of the Federal Reserve Board.<sup>145</sup> The Fed, among its many other critical roles, is the agency that writes the rules for credit card disclosures under the Truth in Lending Act.

### HSBC

HSBC, a giant London-based bank with assets of \$1.9 trillion, muscled its way into the American subprime card market by buying up a pair of subprime pioneers that had fallen on hard times themselves. In a \$14-billion deal in 2003, HSBC bought Household International, a well-known subprime lender with 1,300 storefronts and a history of controversy over its subprime mortgage practices. In 2002, Household agreed to pay \$484 million in a settlement with attorneys general of all 50 states over these practices.<sup>146</sup>

In Household, HSBC also got \$18 billion in managed credit card receivables<sup>147</sup> and a history of aggressive card marketing practices. In fact, the deal closed only after Household was required by the OCC to provide over \$6 million in restitution for deceptive practices regarding private label subprime credit cards and to make improvements to their compliance program.<sup>148</sup>

In 2005, HSBC – still hungry for more high-return subprime lending business – paid \$1.6 billion to buy Metris Cos., a direct mail card marketer with a \$6 billion managed portfolio of subprime accounts.<sup>149</sup> Metris had its own brush with the regulators in 2001, discussed in Section II.C above, when its Direct Merchants Bank unit paid \$3.2 million in restitution to consumers under a consent order with the OCC. The OCC had accused Direct Merchants of “downselling,” by charging \$79 processing fees to consumers who were deceived by marketing materials that promised unsecured cards with no processing fees.<sup>150</sup>

HSBC’s deals helped it grow to become one of the top five Visa and MasterCard issuers, with \$28 billion in receivables at the end of 2006.<sup>151</sup> In a 2004 presentation to analysts, former HSBC Vice Chairman Bobby Mehta said that the bank managed 22 million credit card accounts with \$20 billion of receivables, and that about 25 percent of the bank’s receivables were on cards held by subprime customers.<sup>152</sup>

In an unusually revealing discussion of the subprime lending business, Mehta told the analysts how HSBC uses its Household and Orchard brands to offer cards to “people with blemished credit” and to young people and immigrants without credit histories. Then, he said, “based on payment behavior you graduate these customers to larger (credit) lines and greater utility and greater value propositions.”<sup>153</sup>

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<sup>144</sup> Consent Judgment, *State of Minnesota v. Capital One Bank*, (Minn. Dist. Ct. – 2nd Jud. Dist. Dec. 30, 2004), on file with authors.

<sup>145</sup> Jeannine Aversa, *Bush Nominates Two to Federal Reserve*, USA Today, May 15, 2007.

<sup>146</sup> Reuters, *Household International, Inc. Agreement Paves Way for Restitution*, Chicago Tribune, December 17, 2002.

<sup>147</sup> *Order Instituting Cease-and-Desist Proceedings, Making Findings, and Imposing Cease-and-Desist Order*, In the Matter of Household International Inc., Administrative Proceeding File No. 3-11072, Securities and Exchange Commission, March 18, 2003.

<sup>148</sup> *Formal Agreement by and between Household Bank (SB), N.A., Las Vegas, Nevada and the Office of the Comptroller of the Currency*, No. 2003-17 (Dept. of Treasury, Office of the Comptroller of Currency March 18, 2003), available at <http://www.occ.gov/FTP/EAs/ea2003-17.pdf>.

<sup>149</sup> Press Release, *HSBC Finance Corporation to Acquire Metris Companies, Inc.*, August 4, 2005.

<sup>150</sup> “Fact Sheet Regarding Settlement Between the OCC and Direct Merchants Bank”

<sup>151</sup> The Nilson Report, January 2007, Issue 872.

<sup>152</sup> HSBC Holdings, “*Global Cards*” Investor Event and Conference Call, FD (Fair Disclosure) Wire, May 19, 2004.

<sup>153</sup> HSBC Holdings “*Global Cards*” Investor Event and Conference Call, FD (Fair Disclosure) Wire, May 19, 2004.

## PART IV: STOPPING THE BLEED

Regulators and lawmakers must act to protect the most vulnerable among us. Predators that mass market fee-harvester cards must be exposed and their anti-consumer business model unplugged. While no clear boundary separates predatory deals from those that are “merely” high-priced, this report shows the sharp teeth of some of the worst “fee-harvester” card issuers.

The problem extends beyond a handful of bad actors. All credit card issuers and marketers should stop seeking to boost profits by squeezing their most vulnerable customers. Those credit card issuers and marketers who wish to be viewed as responsible businesses should end their ties to predators; avoid unfair charges and fees; and fully disclose the terms, revenue and profits of the subprime portions of their businesses.

Of course, the pressure and thirst for profit is too strong to make industry self-policing an effective defense against abuse of consumers. So Congress and regulators must act to prevent these abuses. And consumers must be alerted to the fact that in the current barely-regulated credit card market the first and only ethical rule that can be relied upon is “let the buyer beware.”

### **A. Reforms Specific to Fee-Harvesters**

Throwing a monkey wrench into the predatory business model of fee-harvesters requires that lawmakers and regulators recognize that much of that business has little or nothing to do with issuing credit. Fees eat up most of the offered “credit” on a newly issued card, which is designed to maximize revenue by preying upon consumers.

Fair and honest marketing of credit cards to consumers with bad repayment histories or low incomes requires – at a minimum – a genuine extension of credit.

Thus, Congress should:

- Require that credit card issuers extend a minimum amount of credit. Even the OCC has recognized that sometimes too little credit is not real credit, defining in a consent order “‘little or no available credit’ as meaning available credit of \$50 or less.<sup>154</sup> Issuers should be required to extend at least \$300 of available credit. In addition, initial upfront fees cannot consume more than 10% of the overall credit line.
- Amend the definition of a “firm offer of credit” under the Fair Credit Reporting Act to prevent fee harvesting marketers from using near useless extensions of credit as a pretext to obtain credit report information that identifies likely targets for predatory offers.

### **B. A Return to Credit Card Regulation**

Many abuses by fee-harvesters are similar and sometimes identical to heavy-handed tactics used throughout the credit card industry. Restoring state protections for credit card consumers would undo the beast spawned by preemption, returning us to when credit was meaningfully and substantively regulated.

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<sup>154</sup> *In re First Nat'l Bank in Brookings*, No. 2003-1 (Dept. of the Treasury, Office of the Comptroller of the Currency January 17, 2003), available at [www.occ.treas.gov/ftp/eas/ea2003-1.pdf](http://www.occ.treas.gov/ftp/eas/ea2003-1.pdf)

If Congress is unwilling to restore state law safeguards against credit card abuse, protection of consumers targeted by fee-harvesters would be strengthened by reforms that consumer groups have advocated for credit cards in general.<sup>155</sup> Addressing these flaws in the legal and regulatory framework of our financial system would also help protect the financial health of the 80 million American households that hold at least one credit card. These include:

- **A cap on credit card fees to an amount the card issuer can show is reasonably related to reflect the actual costs of providing credit card products and services and the actual risks taken on by card issuers and the investors who finance card lending.** This would limit issuers from packing junk charges onto both prime and fee-harvester cards.
- **No unsound loans.** Issuers should offer credit the old fashioned way, using sound underwriting principles based on the ability of consumers to pay and that ensure the cardholder is not overextending financially by taking on more debt.
- **A cap on credit card interest rates.** Rates should be limited to a standard benchmark, plus a margin to provide for a reasonable profit. For example, the rate cap for credit cards could be set at the prime rate, plus a margin of 10 percent. The rate cap should be calculated on the basis of an APR calculated to include all card fees plus the periodic rate (called an “effective” or “fee-inclusive” APR). This would limit the incentive for bait and switch tactics.
- **A private right of action to enforce Section 5 of the Federal Trade Commission Act.** The FTC Act bans deceptive and unfair acts, which could characterize most abusive card marketing practices. However, the FTC Act doesn’t permit consumers who have been harmed by these practices to seek relief under that law. Injured consumers should be allowed to pursue justice under the FTC Act when victimized, and not rely on federal and state authorities who may lack the resources or political will to challenge abuses by deep-pocketed card issuers and marketers.
- **A prohibition on the ability of credit card issuers to change the terms of a credit card contract, without the consumer’s active consent.** These “unilateral changes in terms” permit bait and switch tactics.
- **Ban pre-dispute binding mandatory arbitration.** No consumer should be forced to waive his or her right to a court trial as a condition of using a credit card. Prohibit binding mandatory arbitration for consumers' claims and for collection actions against consumers.

## C. Consumer Tips

1. If you have bad credit, an offer of a credit card may seem very tempting, but watch out. If a credit card offer seems too good to be true, it may turn out to be a very bad deal.

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<sup>155</sup> See, e.g., *Joint Recommendations of Consumer Groups on Unfair Credit Card Practices: Eliminate Reckless and Abusive Lending by Credit Card Companies*, January 25, 2007, available at [www.consumerlaw.org/action\\_agenda/credit\\_cards/content/CC\\_Platform2007.pdf](http://www.consumerlaw.org/action_agenda/credit_cards/content/CC_Platform2007.pdf); National Consumer Law Center, et al, *Comments to the Federal Reserve Board’s Advance Notice of Proposed Rulemaking - Review of the Open-End (Revolving) Credit Rules of Regulation Z*, Docket No. R-1217, March 28, 2005, available at [http://www.consumerlaw.org/action\\_agenda/credit\\_cards/content/open\\_end\\_final.pdf](http://www.consumerlaw.org/action_agenda/credit_cards/content/open_end_final.pdf).

2. First determine why – and if – you need a credit card. Then shop around for others forms of credit or payment. Consider whether a debit card or some other form of doing transactions might meet your needs adequately – and much more cheaply! (But watch out for expensive “overdraft protection.”)
3. Don’t fall for marketers’ promises of “glamour” or easy loans. If you have bad credit, you will almost certainly pay a high price for any unsecured loan. Look carefully at the interest rates, fees and penalty provisions of an offered card, and if you don’t understand them, walk away. Also, remember that the issuer can change any of the terms with only a short notice. There is no free lunch!
4. If your goal is to repair your credit, you must be patient. Look for loans – secured or unsecured – that carry a reasonable interest rate, aren’t loaded with fees and offer you a chance to build a repayment history without paying steak prices for hamburger helper credit.
5. Be wary of offers that come to you in bulk mailings, from a telemarketer, through broadcast advertisements or over the Internet. Many marketers who use these channels expect to issue high volumes of credit cards that will generate lots of fees – for them – and extend little or no credit to you. Don’t play their game.