Facing losses on bad loans, banks boost credit card rates

By Kathy Chu, USA TODAY

To understand how the collapse of the nation's real estate market is hitting borrowers of all kinds, consider Carson Moore.

Moore, of Elkton, Ky., says he always pays more than the minimum due on his credit cards, and does it on time, every time. But in January, Bank of America told him it was nearly tripling his interest rate, to 22%.

"I don't know why they did it, but I'm not very happy about it," says Moore, 60. "It's not like I miss payments or anything."

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Bank of America (BAC) says it's raising rates on some card accounts based on "periodic" reviews of consumers' risk. The change, it says, isn't directly linked to delinquencies on mortgages and other consumer loans. But as banks' losses mount, they're jacking up fees and rates and tightening rules on all sorts of consumer loans — from credit cards to auto loans — to cushion their losses, some analysts say.

"Banks will want to make up that income somewhere," says William McCracken of Synergistics Research, a research firm. "They're going to be much more aggressive. Everyone is going to see some (price) increase unless they have perfect credit."

By raising rates and fees — but not boosting them so high that they push borrowers into default — lenders are seeking a "delicate financial balance," says Robert Manning, a finance professor at Rochester Institute of Technology. "They can't squeeze too hard that they're going to kill their client. But they have to squeeze more revenue out of their current portfolios."

Even as the Federal Reserve has aggressively slashed short-term interest rates, banks are raising rates on some credit cards. They're also boosting late fees, lifting caps on balance-transfer fees and raising ATM fees for other banks' customers.

Bank fees have been rising for years. But as their loan losses have surged, banks have become quicker to raise certain fees and rates, analysts say. Lenders collected a record $18.1 billion in penalty fees last year just on credit cards — up 69% from 2003 — from such customer missteps as paying late or exceeding a credit limit, according to R.K. Hammer, a consulting firm. The fees are likely to rise an additional 5.5% this year, Hammer says, because of late fees as people struggle to pay bills.

"I would expect banks to raise fees on a variety of services to offset some of the losses," says Richard Bove, a financial services analyst at Punk Ziegel. "They're going to start to nickel-and-dime you to build non-interest revenue."
Escalating fees and rate increases come at a politically explosive time. Congress has held hearings on whether banks need tighter regulation given the increasingly broad range of credit-card fees and policies — such as deadlines in the middle of a day for receiving payments — that have tripped up consumers.

Ahead of those hearings, companies vowed to scale back some of their fees and punitive practices. Chase, for instance, announced then that it'd stop raising card rates on customers whose credit scores had dropped, and Citigroup said it would no longer raise rates if customers paid late to other creditors.

But Bill Hardekopf, CEO of LowCards.com, a card-comparison site, says he fears that "amid Congress' preoccupation with fears about the economy, the ramp-up in fees and punishing practices by consumer lenders will go unchecked."

"Financial institutions have a right to make a profit, but they don't have a right to make an extra profit because they messed up elsewhere," says Maloney, who plans to introduce a bill to combat arbitrary interest rate increases and to ban issuers from applying such increases to existing debt. Sens. Hillary Rodham Clinton and Barack Obama have also made credit card reform an issue in their presidential campaigns.

Read the fine print on rates

Overall, falling interest rates are expected to reduce banks' cost of capital. In theory, that should lead to lower loan rates for consumers. Many credit card rates are pegged to short-term rates that fall when the Fed cuts rates.

But that doesn't stop issuers from changing an interest rate. Their contracts typically say they have the right to change a rate "at any time, for any reason."

A Federal Reserve survey of senior loan officers last month found that 13 of the 53 banks surveyed have widened the spread — which could boost their profits — between what it costs them to borrow and what they charge on certain consumer loans. Four of 39 banks surveyed widened spreads on credit cards.

Loren Cooley, 39, of Toledo, Ohio, saw the rate on her Chase credit card nearly tripled late last year, to about 20%. Why? Her overall debt had swelled, and her credit score had dropped, mainly because of medical bills. Her issuer raised her rate, Cooley complains, even though she usually paid on time and hadn't increased her debt on the card.

After USA TODAY contacted Chase, it offered to cut Cooley's rate on her existing balance to 7.99%. Chase wouldn't discuss the rate increase but says it's working with the consumer to resolve the issue.

Chase has also raised the rate paid by new customers of its popular Chase Freedom card — even as the Fed has cut rates. The card's rate soared as high as 17.2% in December, compared with 14.2% in September, before slipping back to 16% in January.

Card rates exceeding 30%?

Advocates say they fear that as employers shed jobs and housing values sink, more people will see their credit card rates raised to as much as 32%. Such penalty pricing can kick in if consumers pay late by just one minute or exceed their credit limit once.

Consumers can also be slapped with penalty rates if they pay late to some other creditor, because "a lot of issuers are still re-pricing accounts based on credit scores," says Curtis Arnold of CardRatings.com.

The New York State Banking Department says it's fielding more complaints about credit cards, many of them from people who feel their rates have been unfairly jacked up, says spokeswoman Jacqueline McCormack. The state agency refers such calls to federal regulators that oversee card companies, she says.

On a national level, data about card complaints are mixed. Complaints to the Federal Deposit Insurance Corp., which oversees state-chartered banks, rose 53% from 2006 to 2007. Janet Kincaid, head of the FDIC's consumer-response center, says she expects complaints to rise further this year because of the soft economy. Meantime, the Office of the Comptroller of the Currency, which supervises national banks, says it hasn't seen a noticeable rise in such complaints.

Though card defaults are still mild compared with historical levels, Fitch Ratings expects them to rise through 2008 because, "We're not sure the Fed cuts will have an immediate effect" on consumers, says Christopher Wolfe, a managing director at Fitch. The firm expects credit card charge-offs to climb at least 35% and auto-loan losses at least 50% this year.

As defaults rise, auto lenders are becoming stricter about who qualifies for loans. GMAC Financial Services is making fewer loans to consumers with poor credit, says spokeswoman Gina Proia.

Still, those who qualify for auto loans are generally able to stretch their payments over a longer period — meaning lower monthly payments — as cars have become costlier, says John Bella, a managing director at Fitch. But Bella warns that banks could cut back on these longer-term auto loans if their losses on them escalate.
Some student-loan borrowers, meantime, can expect to pay more. Mark Kantrowitz of FinAid.org, a financial aid site, expects interest rates on private loans — which aren’t guaranteed by the government — to rise by between a quarter of a percentage point and 1½ points over the next few months.

As the economy weakens, consumers should look out for such changes in loan terms and rates — especially on credit cards. Banks generally must tell consumers in writing of “material” changes in terms.

Some of the stricter policies banks are imposing:

• In mid-April, Bank of America will start charging 3% for balances transferred to all its credit cards, rather than capping fees at $75 to $100 on some cards. Last year, it also raised, to $3, the fee it charges customers of other banks for withdrawing money from its ATMs.

• Chase has raised ATM fees charged to other banks’ customers for using most of its ATMs. Wachovia says it’s testing the higher fee for withdrawals by other banks’ customers at 4% of its 5,100 ATMs.

Chase spokesman Tom Kelly says it’s “appropriate” to charge other banks’ customers $3 to use Chase ATMs because “it’s continually more expensive to buy and service machines.”

• Citigroup (C) is weighing similar changes to its credit cards. Last month, after the bank announced a large write-down on bad mortgage loans, CFO Gary Crittenden replied to an analyst’s question about whether Citi would “pull back (on offering cards) or increase pricing or neither” by saying it was doing “all of the above.”

A majority of Citi’s recent card losses occurred in five states — California, Florida, Illinois, Arizona and Michigan — where a disproportionate number of customers are defaulting on mortgage bills, it says.

• Discover Financial (DFS) last year raised the top rate charged to risky new card customers and raised late fees for most of its customers. Spokeswoman Laura Gingiss says the company “assess(es) different risk factors on an ongoing basis,” which could result in changes such as higher APRs on credit cards.

• Capital One (COF) made a slew of changes to its credit cards last year. They include shortening the grace period — the time that customers have to pay their bills without incurring interest charges — to 25 days from 30 days and raising the cash-advance fee to 23% from 19%. In 2008, the issuer plans to “assess fewer fees on customers as they continue to adjust to (last year’s) new pricing,” CEO Richard Fairbank said last month.

Nelson Brentlinger of Pueblo West, Colo., says he recently borrowed $5,400 from his Capital One card to pay mortgage bills because he was told he’d pay no interest for 18 months. But when Brentlinger made new purchases on the card and tried to pay them off at the end of the month, the issuer applied his payment to his 0% balance and charged him 17.99% interest on his new purchases.

Brentlinger says he felt misled, because no one told him that payments would be applied to the lower-rate balance first. He complained to state regulators and to Capital One. Eventually, the bank forgave his interest charges. Capital One said it did so as a “goodwill gesture” because a representative might have given him wrong information.

Still, Brentlinger isn’t happy with the way he was treated. He suggests that if he, as someone who always pays on time, is being hit by unexpected new fees, other consumers will also be feeling the pain.

The experience “makes me feel very uncomfortable about credit card companies,” Brentlinger says.

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