

26th August 2015

By email: economics.sen@aph.gov.au

Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Committee Members

Inquiry into matters relating to credit card interest rates

Financial Counselling Australia is pleased to have the opportunity to provide a submission to the inquiry into credit card interest rates.

Credit card debt features in the problems faced in a majority of cases seen by financial counsellors. High credit card interest rates mean that some consumers pay more for credit than is reasonable. For many consumers, high rates also contribute to financial hardship and prevent them from 'escaping' the trap of credit card debt.

Our submission is that competition is not effective in maintaining credit card interest rates at a reasonable level. Changes are needed in the way in which credit cards are marketed and the product itself is designed, to overcome consumer behavioural biases that hamper competition.

We support the joint submission from Consumer Action Law Centre and Financial Rights Legal Centre. In our submission we have provided additional information based on the experience of financial counsellors, as well as sharing some individual case examples from their work.

Yours sincerely



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ABOUT FINANCIAL COUNSELLING

About Financial Counselling Australia (FCA)

FCA is the peak body for financial counsellors in Australia. FCA's member groups are the eight State and Territory financial counselling associations. We support financial counsellors and provide a voice on national issues.

About Financial Counsellors

Financial counsellors assist consumers in financial difficulty. They provide information, support and advocacy to help consumers deal with their immediate financial situation and minimise the risk of future financial problems. The majority of financial counsellors work in community organisations, although some are employed by government. Their services are free, confidential and independent.

How financial counsellors help people in debt

Community based financial counsellors are free services that provide assistance, information and advocacy to people experiencing financial difficulty including problems with debt. Financial counsellors have knowledge of a range of areas of law and policies, including consumer credit law, debt enforcement practices, the bankruptcy regime, industry hardship policies and government concession frameworks. Financial counsellors are required to hold, or to be studying, a Diploma in Community Services (Financial Counselling).

The majority of financial counselling clients have credit card debt that is contributing to their financial difficulties. By the time some clients access financial counselling services they may be close to losing their home, going bankrupt, or experiencing health problems related to financial pressures.

Financial counsellors can help these people in a number of ways, including:

- Accessing formal 'hardship' schemes at banks, finance companies or utility companies;
- Analysing the person's situation and identifying how the person may be able to protect their housing, income or other vital assets;
- Ascertaining whether the client is legally responsible for the debt;

- Helping the person to better understand their financial situation;
- Lodging disputes with industry ombudsman schemes (for example if an unfair contract or obligation arose as a result of abuse or if the company does not respond appropriately to a 'hardship' request);
- Negotiating with creditors and debt collectors over outstanding debts (including consumer credit, mortgages, land rates, child-care, medical);
- Accessing other support services, such as relationship counselling, housing services or emergency relief services;
- Explaining and assisting with options such as bankruptcy if there is no other way to resolve debt issues.

Financial counsellors also feedback their experiences and highlight issues that have a negative impact on their clients. Either individually, or through FCA, they consult with industry, government and other stakeholders and help to encourage practices that prevent financial problems in the first place. For example, through their State and Territory peak bodies, financial counsellors contributed to a public report on the major banks' handling of hardship applications, leading to improvements in bank responses.¹ FCA has also recently released a report on problems associated with the provision of credit in online sports betting.²

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¹ "Rank the Banks" Financial counsellors in Australia rank the financial hardship policies of the 'big four' banks, some of the smaller banks and GE. Financial Counselling Australia, 2015

² 'Duds, Mugs and the A-List: The Impact of Uncontrolled Sports Betting, Financial Counselling Australia, August 2015,
www.financialcounsellingaustralia.org.au/Corporate/Publications/Reports

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1 OVERVIEW

1.1 Submission Focus

Our submission focuses on issues relating to the client group commonly represented in the case work of financial counsellors - those who maintain interest-bearing debt ('revolvers') and who have no ability to repay the debt within a reasonable period. The submission addresses the following issues:

- The impact of high interest rates on these borrowers;
- The impact and risks of credit card marketing, such as balance transfers on these borrowers;
- The need for more behavioural research into credit card use and application of the outcomes of research to regulation.

1.2 Summary

Our submission is that competition is not effective in maintaining credit card interest rates at a reasonable level. This is reflected in the way credit card products are designed and marketed.

The credit card market consists of at least two very different products – a payment facility and a credit facility. The majority of consumers only use their card as a payment facility while a significant minority maintain an ongoing level of debt (while some fluctuate between each group).

A range of factors limit the benefits of competition for all credit card customers, but there are particular problems faced by those who maintain high levels of debt over a period of time and who are more likely to be in a situation where they cannot choose a cheaper product. It is these borrowers who suffer as a result of high interest rates and who can do the least to activate competition. Financial counsellors assist many consumers in this position. Where once we saw people with just one credit card they were struggling to repay, it is common now to see clients with three, four, five or more credit cards.

If competition is to influence interest rates in this market, the Government's response must focus on the impact of consumer behaviour (and the way lenders exploit that behaviour) and legislate around product design and marketing, for example regarding minimum payments and balance transfers. More specifically:

- The level of minimum payments needs to be increased from 2% (this would need to be phased in, given the impact it would have on some borrowers now with credit card debt)
- The appropriate level of a credit card limit should be assessed on the ability of a borrower to repay it as if it were fully drawn, within three years
- Balance transfer offers should be prohibited if the borrower has not actually repaid their credit card debt in full at some point in the previous 12 months, unless the new interest rate at the end of the interest free term is lower than the rate they are currently paying
- Independent research is needed to delve into bank data about the actual use of credit cards by consumers.

2 CREDIT CARD INTEREST RATES: COMPETITION IS NOT WORKING

Summary

- Many consumers do not choose credit cards based on price. This is confirmed by empirical research.
- It can also be inconvenient to switch between credit cards if this means changing a number of direct payments.
- Borrowers with outstanding debt may face additional problems switching to another card.

2.1 Many consumers do not choose credit cards based on price

Consumers do not choose credit cards based on price. Unlike most other forms of credit, whether or not the debt bears interest, and the amount of interest bearing debt, depends on the borrower's future behaviour. If credit card borrowers are too optimistic about their future behaviour and future events, which is often the case,³ they are unlikely to pay attention to the interest rate when applying for a credit card.

It is unlikely that the many borrowers who have high levels of interest bearing credit card debt envisaged those circumstances at the time they obtained the card, and therefore they were unlikely to choose the best card for their situation. By the time a borrower has a high level of debt that cannot be repaid immediately, the ability to change to a cheaper card may be limited.

The lack of attention to credit card interest rates was confirmed in research conducted by Justin Malbon for the Ministerial Council on Consumer Affairs in 1999.⁴ The research assessed the impact of changes to what was then the Uniform Consumer Credit Code⁵ and included a survey of consumers. Malbon found that only 21% of consumers in the survey compared interest rates when choosing a

³ See Yang, Markoczy and Qi, Unrealistic optimism in consumer credit card adoption, *Journal of Economic Psychology*, Volume 28, Issue 2, April 2007, Pages 170–185 and Dr Richard Tooth, 'Behavioural economics and the regulation of consumer credit', August 2012, para. 47, available at: <http://www.srgexpert.com/wp-content/uploads/2015/08/Consumer-Credit-Behavioural-Economics-Case-Study-2012-Final.pdf>

⁴ Malbon, Taking Credit, a Survey of Consumer Behaviour in the Australian Consumer Credit Market, 1999

⁵ The precursor to what became the National Credit Code under the current *National Consumer Credit Protection Act 2009*.

credit card. Consumers were instead more likely to focus on the convenience factor (35%) and incentives such as fly-buys (27%).

Malbon found that clear disclosure has less effect in the credit card market, than in the personal loans or mortgage market, partly because of the underlying market conditions:

“There is less visible price competition, and the lenders are able to discriminate between consumers who are discerning about price and able to repay loans within the interest free period from those who are less discerning or able to repay within the interest free period. Consequently, even if the market was relatively well informed about the credit card products on offer, other factors are at play which reduce the overall competitiveness of the market.”⁶

2.2 Switching credit cards is difficult

The increasing use of automatic/regular payments means that for many consumers, switching credit cards will take considerable effort. The risk of forgetting to change one regular payment to a new card, for example insurance, may dissuade many consumers from making the change in the first place.

For consumers with outstanding debt there are also other impediments to switching products. Even if the borrower is not in default, their payment and spending history may not place them in a position to qualify for a low cost card.

⁶ Ibid, p 13.

3 CREDIT CARDS CAN BE COSTLY DEBT TRAPS

Summary

- Credit card users are often divided into two groups: transactors, who pay the full amount of their credit card debt each month and revolvers, who pay a portion.
- Bank data suggesting that most people repay either all, or well above the minimum balance of their outstanding credit card balance each month, does not provide a complete picture.
- What is more likely is that a large percentage of people may make a relatively large payment each month, but then withdraw a similar amount. The banks do not make these figures available.
- This behavior is consistent with the experience of financial counsellors. We see many clients with persistently high credit card debts.
- High interest rates make this debt difficult to get under control.

3.1 Revolvers and Transactors

Credit card users can be divided into categories depending on how they use their credit cards. For some individuals, depending on their circumstances and behaviour, a credit card can be a convenient payment method, perhaps smoothing out the occasional cash flow issue. This group is called “transactors” and they generally pay their account balance in full each month. There are a range of issues relevant to this group, including transaction costs and the impact of loyalty points, but we do not focus on these issues or this group of consumers in this submission.

For other consumers credit cards are a debt trap. About two-thirds (64%) of outstanding credit card balances is accruing interest – about \$32.6 billion.⁷ Not

⁷ <http://www.rba.gov.au/statistics/tables/index.html#money-credit> Credit and Charge Card Statistics C1

surprisingly, it appears that this 64% of interest-bearing debt is attributable to only about 35% of borrowers⁸, commonly referred to as ‘revolvers’.

There are some consumers who move between both groups (ie who repay in full sometimes), but the banks’ figures⁹ indicate that 29% of credit card users may maintain an ongoing debt, and it is this group that we believe require particular attention. Interest rates have the most impact on borrowers who maintain a level of debt over a long period and we will focus on this group and issues that arise for many of them:

- It is likely that most borrowers who have maintained a high level of outstanding debt over a number of years did not envisage this when they first chose the card and so did not choose the card most suited to their future behaviour;
- Borrowers who cannot repay their balance are likely to find it more difficult than others to impact competition and change to a lower interest product, whereas borrowers who repay their balance in full each month, or who are in a position to repay the balance in a short period of time, can more easily “shop around” for a more suitable card;
- Credit providers have access to data that allow them to determine the likely habits of their credit card customers and can design products, and marketing, to profit from that behaviour;
- It is more difficult for lenders to identify if these borrowers are in financial hardship (than for other forms of credit). The borrower can continue to use the card each month and at the same time pay more than the minimum payment. If the card balance stays at a similar point over many months, the borrower is not, in effect, paying anything off the debt.
- On average, the outstanding debt of revolvers is about four times higher than transactors.

3.2 What the banks say about the data

Lenders’ interpretation on the data provides a false, positive picture. According to one bank,¹⁰ “consolidated data from “the 4 majors (who represent 76% of the

⁸ <http://www.financialliteracy.gov.au/media/558752/research-anz-adultfinancialliteracysurvey2014-fullreport.pdf> p56

⁹ National Australia Bank’s submission to the House of Representatives Standing Committee on Economics on National Consumer Credit Protection Amendment (Credit Cards and Home Loans) Bill 2011 (p12) www.aphref.aph.gov.au_house_committee_economics_nationalprotectionbill_submissions_sub003-nab.pdf

¹⁰ National Australia Bank’s submission to the House of Representatives Standing Committee on Economics on National Consumer Credit Protection Amendment (Credit Cards and Home Loans) Bill 2011 (p12)

market in Australia), indicates that we have 6% of the accounts making a minimum payment in any given month and 1% making a minimum payment for six consecutive months. This means that 94% of our customers pay more than the minimum in any given month, with most customers paying the majority of their balance:

- 6% of customers make the minimum payment in any given month
- 35% of customers always pay in full each month
- 30% of customers move between being paying in full for some months and then paying a large proportion of their balance; and
- the remaining 29% of customers pay on average 18% of their balance (well above the minimum)."

FCA's response

The 94% of borrowers who pay more than the minimum monthly payment includes borrowers (we believe many borrowers), who are unable to significantly reduce their credit card debt, but pay off an amount each month which they simply then spend again to meet their living expenses (for an example see Kylie's case below).

Further data is required, including the percentage of customers whose balance does not change more than 20% over 12 months, if the data is to inform effective policy.

3.3 The impact of high interest rates on revolvers

Many clients that financial counsellors see have maintained high interest credit card debts of \$5,000, \$10,000, \$20,000 or more over some years. These consumers are usually in crisis and the credit card payments are in arrears by the time they seek help.

It is likely that some, perhaps many, consumers who are not falling into arrears, and are able to maintain more than the minimum payment, are similarly trapped in high interest credit card debt.

The low minimum payment and the nature of credit cards means that a borrower can make monthly payments while, at the same time, using the credit card for living expenses. Credit card debtors can therefore hide the fact that they are in financial hardship, and some who are not in hardship may still feel trapped in debt, with few options.

Kylie - Trapped in Debt

Kylie is in her early 30s, and has had a credit card for about ten years. She regrets that she did not pay more attention to her credit card use in her early-mid 20s, and for the last four or five years she has not been able to reduce the outstanding balance of about \$20,000.

Kylie has permanent employment in retail. She believes she can afford to pay \$450 per month on a regular basis, but with an interest rate of 15%, it will take more than 5 years to pay off the debt.

Kylie feels trapped, and unable to move forward with any financial plans until she had repaid this debt. She was not approved for a balance transfer to another card, however even if she had a 21% rate that applies after the '0' balance period, this may have left her in a worse position.

Kylie would not be considered by the lender to be in financial hardship, and she is unlikely to seek help from a financial counsellor however we believe that her case represents the situation in which many credit card customers find themselves.

Hovering around the credit limit

While many clients are in arrears by the time they see a financial counsellor, those who are not have usually maintained a debt that has remained constantly close to their credit limit for some time, like Kylie (above). These borrowers have an outstanding debt close to their credit limit, pay the minimum payment or more each month, but continue to use the card so that their balance does not reduce significantly. For example, take a consumer with a credit limit of \$25,000 and owing \$23,000, the minimum monthly payment is \$460, but the borrower regularly pays \$600 – more than the minimum monthly payment. However, during the month the borrower spends \$500 on the card to buy food, petrol and other living expenses.

In fact, such a borrower cannot really afford to pay the minimum monthly payment unless he or she can re-borrow on the card. Despite this the borrower is making payments that exceed the minimum monthly payment, something a lender may regard as demonstrating the borrower is not in hardship.

This behaviour could actually indicate that the borrower cannot actually afford the minimum monthly payment if they are relying on using credit for necessities in order to make the credit card payment.

Case examples

The following case studies are typical of the types of cases financial counsellors see very day.

Adam

Adam acquired a serious, permanent injury from an accident about five years ago. His situation has been exacerbated by substance abuse issues.

Adam received a lump sum compensation payment for his injuries and he considered using this to purchase a property. However his attempts to gain additional finance to supplement this money were thwarted by his bad credit record.

Adam recently attended his bank to withdraw cash. Upon receiving his money, he was advised by the teller that he was eligible for a credit card. The client was surprised but also thrilled at this news and an application form was sent to his home address. He did not turn his mind to the applicable interest rate at any point. Adam received a \$10,000 credit card, and proceeded to withdraw the entire amount in less than 2 weeks to satisfy his drug habit.

His family soon became aware of what was happening and confiscated the credit card. However, the client now has \$8,000 of debt and limited capacity to repay that debt given that his income consists of the Disability Support Pension and a small income stream related to the compensation payment.

Des

Des is 75 years old and has been on the Age Pension for around 10 years. He struggled to find affordable housing and his only option was to live in a caravan park. He struggled to pay the rent in the park and he used his credit card to supplement his income and to essentially avoid homelessness.

He has been paying \$300 a month towards the credit card for a number of years, which has only ever enabled him to keep on top of the interest; he has never been able to pay down any of the principal. The balance of the credit card has stayed at around \$15,000 for some years.

The client became exasperated at the fact that he was only paying interest and approached a financial counsellor for assistance to file for bankruptcy.

Shane

Shane is in his early twenties and initially obtained a credit card when aged 18 or 19 to pay for an overseas trip. The trip cost around \$2,000, and after his trip, he used the card on occasion to supplement his income. After a couple of years, he felt the debt was out of control and accessed his superannuation (around \$6,000) to repay the debt.

He began using the card again after making the repayment and now has \$10,000 of credit card debt. As many people his age, he has been 'in and out' of casual work. He is currently in receipt of the Newstart Allowance and is at risk of homelessness. He has always had the same credit card from the same bank and never turned his mind to the possibility of getting a better interest rate.

Nisha

Nisha is in her early fifties and runs her own small business, however the business has not been as successful recently, in part due to health issues.

Nisha obtained a credit card to supplement her income. Unfortunately, her health deteriorated to the point that she can now no longer work at all. She is in receipt of the Disability Support Pension and has one credit card with around \$11,000 of debt. She makes the minimum repayment each month but incurs more debt later in the month as she is not left with enough money to cover her basic living expenses. To reduce her expenditure, and put more money towards the credit card, she has started sacrificing medical treatments and supplements suggested by her doctor to assist with her medical condition.

Overall, the debt is increasing rather than decreasing. She does not know what other things she can sacrifice in order to get on top of the debt.

4 STRUCTURAL PROBLEMS IN THE CREDIT CARD MARKETPLACE

Summary

- Balance transfers clearly target people struggling with debt and can leave them worse off.
- Minimum monthly payments of 2% on credit cards are too low.
- Responsible lending guidelines need to be tightened in assessing new or increased credit card limits. A consumer should be able to repay the maximum limit within three years.

4.1 Balance transfers exacerbate problems with debt

Balance transfers are, on the surface, an attractive way for consumers with credit card debt to try and get back on top of their financial situation. These offers are marketed strongly by many financial institutions, with the new provider offering either a no or low interest rate on the outstanding debt. There are a number of dangers with a balance transfer product:

- the standard rate for new purchases on the card may be higher than the borrower's original card;
- the consumer, despite their best intentions, does not in fact repay the transferred debt within the interest free period and so the debt is never reduced;
- the consumer does not actually close the old card and ends up with debts on both the new and the old card (because the old card now has unused credit)

Balance transfers are an effective way for credit card lenders to increase the proportion of revolvers in their credit card portfolio. While some people who may be attracted to balance transfers will be able to pay off their debt during the 'honeymoon' period, many will not. Of course these transfers are designed for, and targeted at, consumers who feel burdened by credit card debt. Without making dramatic changes in spending habits, the consumer is likely to have a high level of debt when the higher interest rate is applied – and then hope to find another transfer balance offer. Rather than provide a solution for consumers who are in trouble, balance transfers can worsen their situation. Again, take up of balance

transfers may rely, in part, in consumers being over optimistic about their ability to pay off their card within the period.

The terms and conditions of offers and marketing strategies involved in balance transfers illustrate how the industry tries to profit from borrowers who feel over indebted. We are not aware of any lenders that offer real solutions - unless the borrower is in arrears and enters a hardship program. A bank may plan for the fact that some of the additional customers accepted during a particular marketing campaign will end up as bad debts, but the overall impact of more customers, with more continuing debt, negates this.

A few examples show the marketing approach for balance transfers and illustrate how borrowers who feel trapped in their current credit card debt may find it difficult to make the best decision based on their circumstances.

“Time to live” is the phrase on Westpac’s¹¹ balance transfer webpage. Unlike some others however, Westpac is clear about the rate that applies at the end of the interest free period. The consumer has a difficult choice though. If the borrower wants to pay 0% interest on the transfer amount for 18 months, the interest rate after that is 21.49%. If the borrower only wants 0% for three months, the rate reverts to 13.49%.

On Citibank’s website¹² Citibank says “save with 0% pa for 18 months on balance transfers”. The actual interest rate that applies at the end of the interest free period (21.74%) is in small text that requires the reader to scroll down in a box. However features clearly emphasised include “1 point for \$1 spend on eligible purchases” and “free wine every time you dine with the Citibank Dining Program”.

4.2 Minimum monthly payments are too low

The difficult situation that many ‘revolvers’ find themselves in is exacerbated by the extremely low minimum monthly payments required.

Low minimum payments (often around 2%) allow lenders to extend a higher amount of credit than they could if minimum monthly payments were at a more reasonable level. Minimum payments at this level contribute to ‘hiding’ financial distress from lenders - and sometimes the borrowers themselves.

¹¹ <http://www.westpac.com.au/personal-banking/credit-cards/balance-transfer/>

¹² https://www.citibank.com.au/aus/credit_cards/cards_classic.htm

While increasing the minimum monthly repayments for all card holders would cause problems for some borrowers, minimum monthly repayments should be increased in a way that will not cause hardship for current borrowers with outstanding debt.

4.3 The ‘substantial hardship’ test for responsible lending is inappropriate

We are concerned that some credit card providers are providing credit cards to consumers that are not suitable, and may be unaffordable.

It is inappropriate for lenders to base an assessment of whether payments can be made without “substantial hardship” on the minimum monthly payment – even if there is a buffer built in.

A borrower who can manage the minimum monthly payment, or slightly more, may not default and may not be considered by the lender to be in “substantial hardship”. In our view, credit card debt should not be extended beyond what the individual could repay in three years.

The longer it will take the borrower to repay, the more vulnerable the borrower is to any change in financial circumstances. In fact if you consider any borrower who maintains outstanding debt for five years or more (and this is common) it is not unlikely that their financial circumstances could change during the period due to unemployment, illness or family circumstances.

5 FINDINGS FROM BEHAVIOURAL RESEARCH

Summary

- Credit card marketing confirms the effort lenders go to in order to distract borrowers from the costs and risks of credit card products.
- We need independent research that assesses how consumers actually use credit cards, rather than relying on bank data.

5.1 Credit card marketing exploits consumer behaviour

In research commissioned by Consumer Action Law Centre,¹³ the authors considered the psychological aspects of credit limit increase offers - referred to in the report as “unsolicited credit card limit increase offers” (UCCLIOs). While these offers are now restricted to consumers who consent to receiving them, the analysis of this marketing illustrates the effort lenders go to in order to distract borrowers from the costs and risks of credit card products.

In relation to UCCLIOs:

- Of 21 letters offering credit limit increases, only five provided information that would alert the customer to the issues around accepting the increase. The warnings were in small print and one of those focused on “flexibility”, a word repeated four times in the warning, “reinforc[ing] the positive heuristic”. (p16)
- The analysis of the written offers found they used at least “six different forms of psychological manipulations to promote and sell an increase in credit amongst their customers” (p17):
- The format of the UCCLIO leads to low-involvement, trust, and the use of a peripheral route to understanding.

¹³ Harrison and Massi, Congratulations, You’re Pre-Approved! - An analysis of credit limit up-selling letters, Consumer Action Law Centre, 2008 <http://consumeraction.org.au/wp-content/uploads/2012/04/Congratulations-Youre-Pre-Approved.pdf>

- Expertise increases trust, in that the UCCLIOs are signed by managers in the banks i.e., financial experts. In the letters, customers are reassured that they can afford the credit increase by a credible source, that is, an expert.
- Consumers of financial products are likely to use heuristic processing, rather than systematic processing when considering a credit limit-increase offer.
- The use of the statement, “pre-approved” implies psychological ownership, and property rights. In addition, consumers who have been told that they have pre-approval will then assume that this is the “status quo”, resulting in a psychological barrier to reject the status quo.
- UCCLIOs are “loss-framed”, in that the letter is structured in a way that suggests the offer is something special and missing acceptance would be detrimental. This approach is consistent with evidence from behavioural economics showing that generally individuals feel losses more strongly than gains and will act to avoid them.

While it is not unusual for businesses, including credit providers, to use various psychological techniques to influence customer choices, these strategies are likely to be particularly effective in relation to credit card borrowers, and increase the danger of consumers falling into unmanageable debt.

5.2 Why consumer behaviour matters

Understanding consumer and psychology behavior in the design and marketing of credit cards is central to credit card interest rates because:

- Consumers who pay interest over a long period of time are unlikely to have predicted their credit card behavior at the time they acquired the card;
- This optimism means that consumers are likely to focus on rewards programs or interest free periods (which usually do not apply at all unless the balance is paid in full), and pay less attention to interest rates;
- Consumers who are looking at ‘balance transfer’ offers for a way out of high credit card debt may pay even less attention to the interest rates that apply at the end of the low or no interest period;
- Choosing a cheaper product once a borrower has outstanding debt is difficult. Even if the borrower is not in default, he/she may fail to qualify for a low rate card due to past spending and payment behavior. Interest on funds to repay the old card is likely to be charged at the higher ‘cash advance’ rate unless the borrower accepts a ‘balance transfer’ offer (which is short-term);

- While ‘balance transfer’ arrangements are likely to appeal to borrowers who are unable to repay their credit card debt in a reasonable time, interest rates at the end of ‘balance transfer’ offers are often higher than average rates (sometimes over 21%) and therefore not suitable for these borrowers.

5.3 The need for further research into consumer behaviour

Disclosure and education are likely to have limited impact on credit card interest rates. If Government and regulators are to respond adequately to the lack of effective competition in relation to credit card interest rates, they need to consider an approach that takes into account consumer behaviour – just as the lenders take this into account in planning product design, marketing and pricing. Lenders should therefore be required to share more details about their credit card data to enable this research to take place. For example, it would be useful to know:

- the number and percentage of customers whose credit card balance does not change more than 20% over 12 months;
- the level of credit card debt for this group in comparison to their incomes;
- the relationship for various customer segments between average debt, average payments and average expenditure;
- what proportion of balance transfer customers pay back the old credit card debt within the no or interest free period;
- what proportion of balance transfer customers continue as “revolvers” and whether their overall debt levels increase after the balance transfer.

6 CONCLUSIONS

There are many consumers with high levels of credit card debt – and this group of consumers is much larger than the group who default on their debt. Even for consumers who are struggling, or juggling their debts, two percent of the outstanding credit card debt each month may not be a large amount. In fact due to the design of credit cards and low minimum monthly payments, those who default are likely to be a small group, at the extreme end of financial hardship.

Credit card interest rates are much higher than they should be and limited competition allows them to remain so. Further, it is the borrowers who are maintaining high levels of debt and have the least ability to “shop around” for a better deal who pay the most interest and have the least consumer choice.

To avoid further detriment from the impact of unrealistic consumer optimism in this market, balance transfer offers should be prohibited for borrowers who have not had a zero balance in the last 12 months, unless the interest rate at the end of the term is less than their current interest rate.

We also support the submission provided separately to the Committee by the Consumer Action Law Centre and the Financial Rights Legal Centre.