Out of Reach: Regressive Trends in Credit Card Access

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Abstract

Despite the ubiquity of credit cards, it was not until the mid-1990s that a large share of lower-income Americans gained access to these useful financial products, which enable cost-saving consumer purchases, small business financing, and economic inclusion. High credit card debt, of course, can cause individual harm, and on the aggregate, booming household debt levels are a serious policy concern. Yet credit card balances account for just 6 percent of U.S. household debt levels, and as a share of disposable personal income fell from nearly 8 percent in the mid-2000s to 5.3 percent in 2015. We identify regressive trends driving decreased card usage, including that between 2007 and 2015, originations to lower-score accounts (generally lower-income consumers) fell 50 percent, and average credit card lines for these accounts shrunk 31 percent, likely forcing down card utilization. Lower-income Americans increasingly lack credit cards.

Consumer credit demand, however, remains high, particularly among lower-income Americans. Supply-side factors – including (1) a 250 percent rise in credit card regulatory restrictions by financial regulators; (2) bans on risk-based pricing; (3) a rising share of unbanked Americans; and (4) unpredictable Consumer Financial Protection Bureau (CFPB) actions – are likely constraining lower-score Americans’ access to credit cards, revealing a tension between consumer financial protection and financial product access. Yet recent regulatory activity has at best only modestly improved customer experiences with credit cards, likely because Americans have historically used cards quite reasonably and expressed satisfaction with these products. We examine how regressive trends in credit card access will likely force consumers into more expensive credit products, hurt small business financing, and impede economic mobility, while also cautioning against high consumer debt levels. We conclude by recommending that policymakers act to curtail unintended regulatory impacts on credit card access by (1) repealing some unnecessary restrictions on risk-based credit card pricing brought about by the CARD Act; (2) reforming the CFPB to better balance consumer protection with consumer financial product access; and (3) streamlining banking regulations to decrease the number of unbanked Americans.

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I. Introduction

Access to consumer credit products is essential to the economic livelihood of American families. These products come in various forms of loans or revolving lines of credit that are unsecured by real estate, the most ubiquitous examples being credit cards, automobile loans, and student loans. Credit cards are important given that they are mostly not secured and are broadly accepted; these financial tools enable individuals to purchase on credit almost any household product imaginable. This working paper aims to understand recent trends in Americans’ usage of and access to credit cards, particularly amongst lower-credit/risk score (measures of a borrower’s creditworthiness)\(^1\) and lower-income Americans. In doing so, it also examines inevitable tensions between consumer financial protection regulation and consumer credit product access.

Many Americans only use credit cards as payment mechanisms, meaning that each billing cycle they pay off balances generated by goods or services purchased on credit (these users are known as “transactors”). Over 40 percent of accounts, however, retain debt balances across billing cycles (holders of these accounts are known as “revolvers”), a strategy that can be an essential ingredient to financial health but, of course, can also lead to financial distress. The use of credit cards to temporarily access debt financing for consumer purchases allows users to make more optimal, long-term wealth-enhancing decisions than they would without cards. Payments on items can be deferred, providing borrowers with more time to generate the income to pay for critical expenditures.

Using a credit card, for example, may enable a family to make a bulk food purchase at a significantly lower per-unit cost than on a one-off basis, or to buy a more expensive, but more efficient, kitchen appliance with lower future utility costs. Despite higher upfront expenses (which are made by taking on credit card debt across a billing cycle while waiting for additional income to accumulate), these purchasing decisions actually can decrease long-term expenditures for consumers relative to paying for one-off food items or less expensive but less efficient kitchen appliances. Credit cards foster long-term savings by facilitating purchases like these, resulting in substantial savings for American families over time.

Credit cards also provide essential, reliable emergency access to liquidity. For example, credit card debt can be used for a critical auto repair when a family does not have sufficient liquid savings. This in turn can enable the family’s primary wage earner to travel to work without having to sell belongings or use more expensive forms of credit like pawnshops. Credit cards also offer users the opportunity to accumulate or preserve balances of liquid assets by deferring expenses on smaller-dollar items – of course, at a cost.\(^2\) Those savings can be used in the event of emergencies for goods or services that may exceed a credit card’s borrowing limit. Additionally, credit cards are essential in education financing: a 2014 survey of U.S. households found that 14 percent use a credit card to finance some educational expenses.\(^3\) Also,

\(^{1}\) For an explanation of how the terms “credit score” and “risk score” are defined and used throughout this research, see infra note 26-28 and accompanying text.


other recent survey data indicates that half of consumers prefer credit cards for online payments (credit cards enable consumers to dispute payments without worrying about getting funds credited back to their account). Credit cards are essential to enabling online commerce.

Despite the ubiquity of credit cards, however, many Americans have enjoyed the numerous benefits of widespread credit card access for only about two decades. Not until the mid-1990s did the majority of Americans in the three lowest income quintiles gain access to credit cards. Yet by the early 2000s, a record 73 percent of Americans had a credit card, including 61 percent of the three lowest quintiles and 38 percent of the lowest. Perhaps contrary to popular perception, the share of total U.S. revolving credit card balances held by low-income users did not change dramatically in the years after the product’s widespread adoption.

Credit cards, of course, are not for everyone, and accumulating excessive credit card debt can cause serious financial harm. A Google search for “credit card debt trap” reveals numerous, well-understood consequences of irresponsible credit card usage and poorly designed products. Yet many of the negative sentiments toward credit products held by policymakers and consumers likely stem in part from what some fittingly call the “other guy” effect. Almost 90 percent of card users reported that the product makes personal financial management easier or makes no difference at all (73 and 16 percent, respectively), yet only half said that they make other people’s – the “other guy’s” – personal financial management easier; in fact, 40 percent of those surveyed replied that credit cards make others’ financial management more difficult. Americans appear to understand the risks of credit cards but likely overestimate the extent to which their neighbors succumb to these risks.

Certainly, the unsustainable accumulation of household debt – housing-related (mostly mortgages) and consumer credit debt – is a legitimate concern that merits the attention of policymakers; leverage build-ups often precede financial downturns. The recent surge in student loan debt, briefly discussed in Section II, absolutely merits policymakers’ attention. Notably, however, while in late 2015 total U.S. household debt was near 2007 levels at $12.1 trillion, we find that as a share of national income, U.S. credit card debt fell from a 2000 through 2008 range of 7.1 to 8.4 percent to just 5.3 percent in the third quarter of 2015; outstanding credit card balances decreased from highs of over $860 billion in 2008 to mid-2004 levels of just over $700 billion. Pre-2007 growth in outstanding U.S. credit card balances was only modest, and in recent years, it has just tepidly increased.

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7 Ibid., 302.
8 Ibid., 311 & 316-318.
9 Ibid., 316-318 (citing Thompson Reuters/University of Michigan Surveys of Consumers).
10 See, for example, Daniel Leigh et al., "Dealing with Household Debt," World Economic Outlook: Growth Resuming, Dangers Remain (International Monetary Fund, 2012).
This working paper explores regressive trends fueling the relative decline in credit card access and usage. We find that a drop in lower-risk-score revolver card accounts – disproportionately lower-income and younger – exerts a strong downward pressure on U.S. credit card balances, which fell for much of 2008 through 2014.\(^\text{12}\) Also, relative to 2007, the number of accounts originated annually to lower-score borrowers – who on average maintain higher balances than higher-score accounts – has dropped 50 percent (yet openings by higher-score borrowers have grown above 2007 levels); thus in recent years, lower-score Americans’ rate of credit card ownership declined substantially.\(^\text{13}\) We also examine how credit card account closures and declining credit lines have driven down credit card usage.

American households’ borrowing patterns and attitudes toward saving have certainly shifted in recent years in the aftermath of the Great Recession. Yet numerous findings suggest consumer credit demand is high, particularly amongst low-income Americans.\(^\text{14}\) We find that supply-side constraints brought about by 2008 Federal Reserve Board (Fed) rulemakings and the 2009 Credit Card Accountability Responsibility and Disclosure Act (CARD Act), as well as quasi-regulatory actions by Dodd-Frank’s Consumer Financial Protection Bureau (CFPB), are likely more significant drivers behind the regressive trends in credit card usage and access we identify, relative to demand factors. We also highlight other policy factors that may be driving lower-score and lower-income Americans out of credit cards, and stress the unfair and unfortunate implications of policy-driven declines in credit card availability, noting that mitigating these regressive trends will likely not result in a substantial impact on growing U.S. household debt levels. In conclusion we urge U.S. policymakers to avoid the “other-guy” effect, and adapt structural and regulatory reforms that will remove unnecessary barriers to credit card access for some on the margins of approval.

II. Understanding U.S. Consumer Credit Growth

Balances of U.S. consumer credit – credit extended to individuals other than loans secured by real estate – recently reached record-levels in both real dollars (reaching an all-time high of about $3.3 trillion in Q3 2015, up 58 percent from over $2.1 trillion in Q3 2003) and as a percentage of national disposable personal income (as illustrated in Figure 1).\(^\text{15}\) This trend, however, is heavily skewed by a recent surge in student loan debt balances. According to Federal Reserve Bank of New York (New York Fed) data, student loans made up over 36 percent of consumer credit balances outstanding in Q3 2015, versus just 26 percent in Q3 2009 and 12 percent in Q3 2003.\(^\text{16}\) In raw dollars, student loan debt skyrocketed over 380 percent from $249 billion in Q3 2003 to over $1.2 trillion in Q3 2015.\(^\text{17}\) Economists note that major drivers of the surge in student debt levels include: (1) a weak labor market for younger Americans, making debt repayment more difficult; (2) household earnings and savings reduced by the Great Recession; (3) massive tuition growth due to increased subsidization by federal loan programs.

\(^\text{12}\) See infra note 21-22, 31-32 & Figures 4-6 and accompanying text.

\(^\text{13}\) See infra Figure 7-8 & notes 37-41 and accompanying text.

\(^\text{14}\) See infra note 58-63 and accompanying text.

\(^\text{15}\) Federal Reserve Bank of New York, supra note 11. We define consumer credit as total household debt minus housing-related debt balances – this definition mirrors that used by the Federal Reserve Board. See Board of Governors of the Federal Reserve System, January 2016 Statistical Release, Consumer Credit (Mar. 7, 2016).

\(^\text{16}\) Federal Reserve Bank of New York, supra note 11; authors’ calculations.

\(^\text{17}\) Ibid.
and decreased state higher education funding; and (4) a large uptick in enrollment.\textsuperscript{18} Consumer credit levels excluding government-owned non-revolving consumer loans (a debt balance that includes government-owned student loans) as a percentage of national disposable personal income have, in fact, fallen since 2008, remaining near 1989 and 1995 levels at 19 percent of national personal disposable income throughout 2014 and 2015, as Figure 1 shows.\textsuperscript{19}

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{figure1}
\caption{Total U.S. Consumer Credit Balances Outstanding as a Percentage of National Disposable Personal Income (Q1 1980-Q2 2015)}
\end{figure}

According to the New York Fed, credit cards accounted for 34 percent of non-student loan consumer credit balances in the third quarter of 2015; auto loans accounted for almost half, and 17 percent was “other” consumer finance products, such as sales financing or personal loans, and retail loans, such as department store charge cards.\textsuperscript{20} Unlike student and auto loans, credit card debt levels declined in dollar volume after 2008, as Figure 2 shows. In fact, according to

\textsuperscript{18} See David O. Lucca et al., “Credit Supply and the Rise in College Tuition: Evidence from the Expansion in Federal Student Aid Programs” (Federal Reserve Bank of New York Staff Report No. 733, Jul. 2015); Susan M. Dynarski, “A crisis in student loans? How changes in the characteristics of borrowers and in the institutions they attended contributed to rising loan defaults” (The Brookings Institution, Evidence Speaks No. 19, Jan. 2016); Adam Looney & Constantine Yannelis, “A crisis in student loans? How changes in the characteristics of borrowers and in the institutions they attended contributed to rising loan defaults” (Brookings Papers on Economic Activity Conference Draft, The Brookings Institution, Sep. 2015).

\textsuperscript{19} Board of Governors of the Federal Reserve System, \textit{supra} note 15. The Bureau of Economic Analysis defines disposable personal income as income received by “persons” (defined as “individuals, nonprofit institutions that primarily serve households, private noninsured welfare funds, and private trust funds”) minus taxes, and notes “it is the income available to persons for spending or saving.” Bureau of Economic Analysis, “NIPA Handbook: Concepts and Methods of the U.S. National Income and Product Accounts” (Dec. 2015).

\textsuperscript{20} These figures were 41 percent, 38 percent, and 21 percent (auto loans, credit cards, and other, respectively) in Q3 2005 and 41 percent, 40 percent, and 19 percent in Q3 2010. Federal Reserve Bank of New York, \textit{supra} note 11; authors’ calculations.
New York Fed data, credit card debt outstanding fell from a high of $866 billion in Q4 2008 to $704 billion in Q4 2011 before reaching a 12-year low of $659 billion in Q1 2014.\(^{21}\) It has since recovered tepidly, reaching $714 billion in Q3 2015 (around 2004 levels).\(^{22}\) Experian data reveals a more rapid increase, finding that outstanding credit card debt reached near-2009 levels in Q3 2015.\(^{23}\)

**Figure 2**

![Graph showing U.S. credit card debt decline](image)

Figure 3 shows that U.S. credit card debt relative to national disposable income remained fairly level – between 7.1 and 8.4 percent – in the eight years prior to Q4 2007, but since then has been declining significantly. As of Q3 2015, national credit card debt outstanding was 5.3 percent of national disposable personal income (a record low since the product gained widespread use).\(^{24}\) Figure 3 also indicates that this sudden drop and subsequent plateau is not a pattern across all consumer credit products: auto loan balances relative to national disposable personal income have grown steadily in recent years, and the shift from other consumer credit products (“other” consumer finance products and retail loans) appears to be a more persistent market trend.

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\(^{21}\) Ibid.

\(^{22}\) Ibid.


\(^{24}\) Federal Reserve Bank of New York, *supra* note 11; Federal Reserve Bank of St. Louis, *supra* note 11; authors’ calculations. Credit cards only achieved widespread use across income quintiles in the early 2000s. See Durkin et al., *supra* note 5, at 303-4.
III. Recent Shifts and Regressive Trends in Credit Card Access and Usage

To understand what factors drove U.S. credit card debt balances to decline so sharply both in absolute and relative terms after 2007, and why balances have stayed at fairly low levels in both relative and absolute terms in recent years, we examined existing research and analyzed publicly available data, as well as information reports and analysis provided to us by Argus Information & Advisory Services, a business unit of Verisk Analytics (Argus-Verisk).25

Argus-Verisk reports risk scores that are generally mapped to most standard industry credit scores. Generic credit scoring takes into account “(1) payment history, (2) indebtedness, (3) length of credit history, (4) types of credit used, and (5) acquisition of new credit” to rank “consumers by the likelihood that they will become seriously delinquent on any of their credit accounts in the near future.”26 Credit scores are calculated by national credit-reporting agencies, and commonly range from 300 to 850 (although some score bands reported are narrower or larger).27 Argus-Verisk risk scores are referenced in Figures 4, 5, 7, 8, and 10, and are bucketed into three score ranges: below 680, between 680 and 759, and above 759.28

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25 Information reports by Argus-Verisk provide an overview of general-purpose cards issued by companies representative of 90 percent of the general-purpose credit card market and are based on a nationally representative dataset of consumer general-purpose credit card information. No individual account holder’s information or specific financial institution’s data can be identified from the dataset. For more on the Argus dataset used in this research, see American Bankers Association, “American Bankers Association Credit Card Industry Monitor: Answers to Frequently Asked Questions” (updated Jun. 25, 2014).
27 Ibid. at 24 & 27 note 35.
28 American Bankers Association, supra note 25.
many others may refer to accounts with a score of less than 680 as subprime, but because of some disagreement between academics and industry actors as to what constitutes subprime, this working paper simply refers to accounts with scores less than 680 as “lower-score.”

Two factors inherently affect outstanding credit card debt levels: credit destruction (the repayment of debts or defaults by customers) and credit creation (the issuance of new levels of credit). Notably, however, the number of credit card users and share of card debt balances in default have declined in recent years. Instead, we find that the post-2007 downturn in credit card debt relative to disposable personal income and recent shifts in credit card debt balances are mainly driven by three trends: (1) revolvers, particularly lower-score revolvers, both declining as a share of a smaller U.S. credit card market and also borrowing less; (2) the share of Americans with card accounts decreasing, in part due to large-scale credit card account closures between 2008 and 2011; and (3) falling credit card origination to lower-score borrowers.

These trends – profiled below – are regressive in their impact. Lower-score Americans are generally less affluent and younger. In fact, survey data published in a recent Federal Reserve Bank of Kansas City working paper indicates that the average score of persons earning less than $49,000 is below 680 (our definition of “lower-score”) while the average score for Americans earning more than $100,000 is 752 (above our 749 threshold of “higher-score”).

(A) Low-score revolvers make up a smaller share of a smaller card market

Figures 4 and 5 show that between Q2 2007 and Q2 2015, revolvers as a share of total credit card accounts held steady, while lower-score revolvers as a share of all accounts declined somewhat and dropped as a share of total revolver accounts. Figures 4 through 6 suggest that the number of lower-score revolver accounts has significantly dropped relative to 2007 levels.

Figure 4

Figure 5

Source: Argus-Verisk

Source: Argus-Verisk (due to rounding, and the absence of a missing score group, percentages tallied for each score group do not always add up to 100)

This drop is a major factor behind the relatively downward credit card debt balance trends illustrated in Figures 2 and 3 because, as Figure 7 reveals, the average revolving balance for lower-score accounts is $1,949 – significantly higher than that for higher-score accounts. Also, the average revolving balance for lower-score borrowers has declined $459 (19 percent) since 2007 (driven in part by the fact that fewer lower-score accounts now exist), which is another factor behind the relative decline in credit card debt levels highlighted in Figures 2 and 3.

Again, these findings suggest regressive trends. Not only are lower-score Americans generally less affluent and younger, as explained above, but also low- to moderate-income credit
Card users generally revolve 80 percent of outstanding balances, while upper-middle-income users revolve just 40 percent. According to one study, the average income of transactors is over $82,000, versus about $51,000 for revolvers, and recent analyses of CFPB and Fed data similarly find that lower-income households generally pay balances in full less frequently than those with higher incomes.

(B) Fewer Americans (particularly lower-income Americans) have cards

As these patterns would suggest, an increasingly large percentage of lower-score and lower-income Americans have no credit card accounts at all. Surely, among credit card holders, over 70 percent have two or more cards, and over 40 percent have three or more. Yet it does not appear that consumers modestly reducing their number of card accounts are driving the downward trend in the number of accounts highlighted above.

A 2014 Gallup survey reported that 29 percent of Americans lack any credit cards, compared to a range of 22 percent and 17 percent between 2001 and 2008. Fed research shows that this trend is particularly pronounced for lower-score borrowers – between 2004 and 2007, 65 to 67 percent of Americans in the lowest-score quartile had a credit card while in 2011, just 53 percent did. Similarly, while 76 percent of individuals in the second lowest credit score quartile had a credit card between 2003 and 2008, by 2011 that share had fallen to just 65 percent. A 2015 study estimated, using public and private data, that low- to moderate-income consumers are 35 percentage points less likely to have a credit card than upper-middle-income Americans (94 percent versus 59 percent), and 2015 Fed research found that 39 percent of households making less than $40,000 annually have no credit card, versus just 12 percent of those making over $100,000. Low card utilization is particularly glaring for Millennials, who, given their age, generally have lower credit scores and incomes. An April 2015 survey found that over one-third of 18- to 29-year-olds have never owned a credit card.

Certainly, changes in consumer preferences stemming from the Great Recession have driven some Americans to close credit card accounts. Between 2009 and 2010, accounts were

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33 Nicki Cohen et al., “Reimagining Financial Inclusion” (Oliver Wyman, 2015), at 56.
36 See Art Swift, “Americans Rely Less on Credit Cards Than in Previous Years,” Gallup (Apr. 15, 2014) (reporting that the average number of credit cards owned by Americans card owners has remained relatively constant since 2004).
37 Ibid.
38 Canner & Elliehausen, supra note 35, at 10.
39 Ibid.
40 Cohen et al., supra note 33, at 56; Board of Governors of the Federal Reserve System, supra note 3, at 28.
significantly more likely to be closed by card users than by card issuers. During this period, however, credit card account closures overall declined significantly, after spiking between mid-2008 and mid-2009, when there was a sharp uptick in the share of card accounts being closed. That surge in closures was likely driven in part by regulatory pressures explored in Section III, and since 2011, quarterly credit account closures have remained much lower than in the mid-2000s, while credit card debt levels relative to personal disposable income have shrunk. Patterns in account closures are only one secondary factor behind decreasing credit card usage.

(C) Credit card originations to lower-score Americans are down

A primary factor behind regressive trends in credit card usage is a drop-off in credit card originations to lower-score borrowers. Figure 8 shows that while overall account originations have recovered to near 2008 levels (which makes sense given the rising number of households and a recovering, albeit tepidly, labor force), the steady rebound in credit card originations after the post-2007 fall is likely not benefiting many lower-score Americans. While 28 percent of originations in 2007 were to consumers with a risk score below 680, in Q2 2015 these consumers accounted for just 20 percent of new accounts originated. Similarly, the share of annual originations to consumers with a score between 680 and 759 has fallen from 44 percent to 39 percent. On the other hand, the share of annual originations to high-risk-score consumers has grown from 28 to 41 percent.

Figure 8

![New General Purpose Credit Card Accounts Originated Annually by Risk Score Group (Millions of Accounts, 2007-15)](#)

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43 See ibid.; Federal Reserve Bank of New York, supra note 11.
44 Jambulapati & Stavins, supra note 42; Federal Reserve Bank of New York, supra note 11; authors’ calculations, supra note 24 and accompanying text.
The sharp decline in originations to lower-score borrowers highlights difficulties facing many Americans seeking access to the credit card market: Figure 8 shows that in 2015 the number of credit cards issued to lower-score consumers was half the number issued in 2007. This downward shift in issuances is not in response to a shift in the credit profile breakdown of prospective American borrowers; the overall score distribution of Americans remained relatively constant over the last decade (since 2005, the share of scored Americans with credit scores below 660 has remained between 34 and 37 percent, according to the New York Fed).\(^{45}\) Notably, the average risk score of new card users (accounts opened within the last 24 months) has grown from 700 in mid-2008 to roughly 727 in Q2 2015 while the average score of new lower-score card users (those with a score of less than 680) has remained relatively constant since mid-2008 (623 in Q2 2008 versus 625 in Q2 2015, and ranging between 613 and 627 during this time).\(^{46}\)

While data on the credit card industry can be somewhat inconsistent and sometimes imprecise, Argus-Verisk, Equifax, and Experian analyses indicate that the overall volume of credit card originations is either still down or has just barely recovered relative to 2007 levels. Argus-Verisk, Fair Isaac Corporation (FICO), Goldman Sachs, and New York Fed Consumer Credit Panel (CCP)-based data/analyses suggest that credit cards are increasingly much less accessible to lower-score Americans relative to 2007 levels.

Issuance patterns highlighted in Figure 8 mirror patterns in card origination reported using Equifax data, which shows that the share of annual credit card originations to Americans with credit scores below 660 was just over 30 percent in Q1 2014, significantly down from over 40 percent in Q1 2007.\(^{47}\) Other research using a smaller sample highlights a sizable decline in the number of accounts originated to consumers with FICO scores below 660 between mid-2008 and late 2011.\(^{48}\) One recent CFPB analysis suggests that subprime, prime, and superprime card originations, relative to 2007 levels, all more than fully rebounded by 2014.\(^{49}\) The accompanying 2015 CFPB report on credit cards also acknowledges, however, that “data sources that cover more of the market” – referencing Experian data – show that overall originations did not recover to “pre-recession” levels until 2015.\(^{50}\) Goldman Sachs research using FICO data found that the share of total credit extended via credit cards received by below 660 FICO score borrowers declined from 26 percent in 2007 to 11 percent in 2013.\(^{51}\)

The CFPB’s 2015 report on credit cards uses CFPB CCP data to show that the share of annual card originations to “subprime” borrowers grew modestly from 2012 to 2014, but does not provide CCP data from before 2012.\(^{52}\) Notably, a Minneapolis Fed-published analysis of

\(^{46}\) Argus-Verisk. See supra note 25 and accompanying text.
\(^{48}\) Sumit Agarwal et al., “Regulating Consumer Financial Products: Evidence from Credit Cards,” The Quarterly Journal of Economics (Nov. 2014), Figure 7(C), at 155. For more information on FICO scores, see Board of Governors of the Federal Reserve System, supra note 26.
\(^{50}\) Ibid., 88-89. See also Tatham, supra note 23.
\(^{52}\) Consumer Financial Protection Bureau, supra note 49, at 90.
New York Fed/Equifax CCP data (which the CFPB has told Congress is “similar” to the CFPB’s CCP data\footnote{Subcommittee on Financial Institutions and Consumer Credit, Committee on Financial Services, U.S. House of Representatives, “Examining the Consumer Financial Protection Bureau’s Collection and Use of Consumer Data: Questions from Chairman Shelley Moore Capito and Vice Chairman Sean Duffy” (Jul. 9, 2013).}) finds that the share of subprime borrowers (defined by the author as credit scores of less than 660) with bank credit card debt held steady between 60 to 70 percent from 2000 to 2007, but between 2008 and 2010 fell to nearly 50 percent, and remained near that level from 2012 through 2014.\footnote{Michael Grover, “Is subprime lending making a comeback?” Community Divided (Federal Reserve Bank of Minneapolis, Oct. 2014).} Meanwhile, the share of prime borrowers (defined by the author as credit scores of 660 or more) with bank credit card debt has remained roughly stable at around 75 percent since 2000.\footnote{Ibid.}

**IV. Examining Possible Drivers of Recent Credit Card Usage and Access Patterns**

This section explains why, although consumer reactions to and economic trends resulting from the 2008 financial crisis and subsequent Great Recession are certainly a factor behind declines in credit card usage by and originations to lower-score and lower-income Americans, demand for consumer credit, in fact, likely remains high. Instead, voluminous and substantial supply-side regulatory constraints introduced since 2008 have likely had a greater impact on credit card usage and access, along with a rise in the unbanked (in part a result of regulatory pressures) as well as unpredictable CFPB quasi-regulatory and enforcement actions.

(A) Understanding trends in credit demand and the impact of consumer sentiment

Shifts in consumer sentiment and economic conditions have certainly shaped credit card utilization patterns both positively and negatively in recent years. Figures 4 and 5 clearly show that for lower-score Americans, the percentage of subprime revolvers grew in the immediate aftermath of the Great Recession. Some lower-score transactors likely became revolvers in response to economic stress prompting demand for credit.

On the other hand, shifts in consumer sentiment have also likely had a downward pressure on credit card balances. Compared to before the crisis, survey data suggests Americans are now more likely to save than to spend.\footnote{See Brendan Moore, “Americans Continue to Enjoy Saving More Than Spending,” Gallup (Apr. 21, 2014).} U.S. labor force participation, despite recent improvements, is still significantly less than before the crisis; this inherently contributes to a weaker economic climate, which in turn reduces consumer propensity to borrow. Furthermore, during recessions borrowers tend to pay down debt,\footnote{See Canner & Elliehausen, supra note 35, at 10.} so the post-2008 decline in lower-score revolvers as a share of a shrinking number of card accounts is undoubtedly fueled in part by lower-score users choosing to borrow less and paying down balances.

Yet demand for credit certainly persists. Consumer credit account inquiries grew 13 percent between Q3 2010 and Q3 2015,\footnote{Federal Reserve Bank of New York, supra note 11.} and a 2014 Fed survey of U.S. households reports that 37 percent of respondents applied for credit within the last year (up from 31 percent the previous
year); its findings also indicate that 24 percent of respondents applied for a credit card.\(^{59}\) Bank senior loan officers surveyed by the Fed reported net increases in credit card loan demand in all but two quarters between Q2 2011 and Q4 2015.\(^{60}\)

Lower-income Americans have a particularly strong need for consumer credit. The U.S. cost of living has outpaced the growth of personal income in recent years; this inherently generates credit demand as families and individuals try to close the gap, which is particularly difficult for Americans with lower incomes.\(^{61}\) Fed research finds that just three in 10 Americans making less than $40,000 could cover a $400 emergency expense without borrowing or selling something that they own.\(^{62}\) To come up with a $2,000 payment in 30 days, over 40 percent of Americans would utilize credit products, according to a recent working paper published by the National Bureau of Economic Research.\(^{63}\) These statistics are concerning from a policy perspective, and show that many Americans are just one emergency away from a deep need for consumer credit.

**(B) Examining regulator-driven supply-side constraints to credit card availability**

Constraints on the ability of lenders to provide credit – in other words, supply-side constraints – appear to play a larger role in the regressive trends explored in Section III than do shifts in Americans’ demand for consumer credit, which, as explained above, appears to have remained strong in recent years. Findings by St. Louis Fed and San Francisco Fed economists suggest that recent declines in credit creation are more attributable to supply-side pressures than to demand-side shifts.\(^{64}\) The scope and impacts of the massive surge in post-2007 regulator-driven supply-side constraints on credit card access are explored in greater detail below.

**(1) 2008 Fed regulations and CARD Act restrictions on borrowing terms**

Figure 9, which was produced using data obtained from RegData, a regulatory text analytics program developed by Omar Al-Ubaydli and Patrick McLaughlin of the Mercatus Center at George Mason University,\(^{65}\) shows that between the publication of the 2007 Code of Federal Regulations (CFR) and the 2014 CFR, federal regulatory restrictions in Title 12 of the CFR related to credit cards grew over 250 percent. Title 12 includes regulations promulgated by all major U.S. financial regulators except for the Securities and Exchange Commission and the Commodity Futures Trading Commission, neither of which directly regulates credit cards.

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Each year in Figure 9 above marks when regulations were published in Title 12 of the CFR, which takes place in the year following publication of the rule in the Federal Register. Thus the uptick between 2009 and 2010 is attributable to December 2008 Fed rulemakings on credit cards that were published in the Federal Register in early 2009 (and were thus published in the 2010 CFR). The immediate post-2011 uptick in Figure 9 is largely attributable to CARD Act rules (Dodd-Frank transferred authority to enforce these rules to the CFPB, which did not gain a section in the CFR until the 2012 edition) as well as the transfer of some existing credit card regulatory powers from non-financial regulators to the CFPB (thus moving existing rules from other parts of the CFR to Title 12 once the Bureau gained a section in this Title in 2012), also as a result of Dodd-Frank.

The December 2008 Fed regulations were first proposed in May 2008 and limited the ability of credit card issuers to modify terms of card agreements to price for changes in borrower risk. Designed with the goal of protecting consumers, the rules changed the credit card market by prohibiting card companies from raising rates on existing debt balances even if a customer’s risk profile changes, requiring that rate increases allowed to occur be reevaluated within six months, limiting the size of penalty fees, and restricting the ability of issuers to determine what balances consumer payments will be counted toward.66 New limits were also put in place on over-the-limit fees, and a 45-day notice was required for changes in terms.

The CARD Act superseded many of these regulatory restrictions before they were actually finalized. The legislation closely mirrored the Fed’s regulations, tightened many of those rules’ provisions, and also added new restrictions, such as a prohibition on fees charged on outstanding balances of interest accrued on previously-repaid credit, as well as stringent limitations on card issuances to those under 21 years old. The CFPB reports that the average retail annual percentage rate (APR) for open credit card accounts increased only modestly after CARD Act rules were implemented, and not surprisingly, finds that CARD Act-related regulations have had the consequence of lowering default rates and fees charged to card consumers, of course, this is what the rules were intended to do. But restricting the variability of conditions under which a lender may lend intuitively constrains credit access.

Several studies suggest that 2008 Fed rule and 2009 CARD Act provisions can be linked to negative pressures on credit card access. Anecdotally, banks reacted to these restrictions by shrinking credit lines to lower-score borrowers or closing accounts entirely. Yet as recent Federal Reserve Bank of Boston research noted, while there “is evidence that a higher fraction of credit card accounts were closed and credit card lending was tightened right after the Federal Reserve Board adopted its rules pertaining to credit cards,” because these closures occurred during the financial crisis, determining precise causal effects is admittedly difficult. We share this skepticism, but note trends profiled in Figures 3 through 8 suggest that dramatic and regressive shifts in credit card usage and access occurred in the immediate anticipation and aftermath of 2008 Fed rulemakings and the CARD Act. Figure 10 below illustrates the drastic drop in credit lines that took place after the Fed’s 2008 rulemakings were proposed and in the lead-up to the CARD Act’s passage.

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67 For useful summaries of key CARD Act rule provisions, see ibid.; Kenneth J. Benton et al., “An Overview of the Regulation Z Rules Implementing the CARD Act,” Consumer Compliance Outlook (Federal Reserve System, Q1 2010); Getter, supra note 66. For a helpful overview of differences and similarities between the CARD Act and 2008 Fed rules, see ibid., at 18-23.


69 See, for example, Larry Santucci, “A Tale of Two Vintages: Credit Limit Management Before and After the CARD Act and Great Recession” (Federal Reserve Bank of Philadelphia, Payment Cards Center Discussion Paper, Feb. 2015); Joshua Ronen & Tiago da Silva Pinheiro, “Unintended Consequences of the Credit Card Act” (Working Paper, Aug. 2014). For an overview of these and other similar studies, see Durkin et al., supra note 66, at 47-52.

70 Jambulapati & Stavins, supra note 42.

71 Ibid.
This reduction in credit card lines has coincided with sizable declines in revolving balances maintained on credit cards in recent years (shown in Figure 7). Some research suggests that the size of borrowers’ revolving balances is generally quite sensitive to the size of the credit line extended.\(^{72}\) Thus the extent to which 2008 Fed rulemakings and the CARD Act lowered the size of credit lines extended to borrowers is perhaps another notable downward pressure on credit card usage. The CFPB found that in the two years after most CARD Act-related rules were finalized, a $200 billion drop in credit lines took place, and subprime consumers largely felt the decline.\(^{73}\)

Some research claims that CARD Act rules had no impact on credit line amounts or credit card originations, but as Professor Todd Zywicki of George Mason University’s School of Law recently noted, these studies often fail to consider that firms anticipated and then reacted to the Fed’s 2008 rulemakings as early as 2007 (in fact, some studies fail to mention the 2008 rulemakings altogether); this methodological issue is also highlighted by the CFPB in its 2013 CARD Act Report.\(^{74}\) Any analysis of shifts in credit card account terms and account origination patterns using the period of time just prior to the Act’s passage as a baseline, as Zywicki explains, fails to appropriately detect firms’ reactions to 2008 regulations. That said, determining the precise extent to which 2008 Fed and CARD Act restrictions on credit card lending have impacted lower-score Americans’ access to cards is outside the scope of this research, and perhaps irresolvable given that the financial crisis occurred simultaneously.

\(^{72}\) See Durkin et al., supra note 5, at 163 (explaining how research suggests that consumers may have “target utilization rates”).


\(^{74}\) See Todd Zywicki, “No, the credit Card Act is not a free lunch,” The Washington Post (The Volokh Conspiracy, Jan. 2016) (noting flaws in the methodology of Agarwal et al., supra note 48); Consumer Financial Protection Bureau, supra note 73, at 27 (noting two “limitations” to using 2008 as a baseline: [1] changes in credit card repricing activity resulting from the CARD Act may “reflect an already elevated amount of repricing activity in the baseline” resulting from credit card rulemakings proposed by the Fed (along with other agencies) in May 2008, which “may have led some issuers to reprice accounts while it was still lawful to do so,” and [2] “the effect of the financial crisis [] affected issuer behavior” during 2008). See also Durkin et al., supra note 66, at 46-49.
(2) Basel III and Dodd-Frank bank regulatory shifts

Figure 9 also illustrates sizable increases in Fed and FDIC credit card-related regulations from 2011 through 2013. One driver was new Basel III capital rules, which increased the amount of capital banks must hold against credit card asset-backed securities.\textsuperscript{75} Another factor is new capital stress tests required by Basel III and Dodd-Frank rulemakings, which may be pressuring banks to shed lower-score borrowers from credit card portfolios. Research from the Federal Reserve Bank of Philadelphia finds that under a variety of adverse economic conditions taken into account by stress tests, low credit-score issuers face the highest loss rate\textsuperscript{76} (stress tests aim to project how banks would perform in such scenarios). According to the Fed’s reported Dodd-Frank Act stress test methodology and results, the tests used loan-level data and considered “characteristics of the account and borrower” for particular credit card loans.\textsuperscript{77}

A more important driver of regressive credit card issuance and usage trends, however, is bank regulations that drive increases in the cost of banking, which in turn contribute to lower-income consumers being priced out of the traditional banking system. Without a basic banking relationship, approval for and utilization of an unsecured credit card are much more difficult. The proliferation of credit cards in the mid-2000s to lower-income borrowers coincided with, and was enabled by, the proliferation of free checking accounts.\textsuperscript{78}

Yet Dodd-Frank’s Durbin Amendment, which caps debit card interchange fees for banks with more than $10 billion in assets, increases the cost of basic banking services by pushing banks to recover lost earnings through increases in fees and the minimum monthly holding balance necessary to enjoy a fee-free account.\textsuperscript{79} Figure 11 reveals the extent to which the cost of basic banking services has increased since Dodd-Frank was passed.

\textsuperscript{75} For an overview of the impact of Basel III capital rules on credit card issuing banks, see Carl Mosesson, “Basel III Challenges for the Cards Business” (MasterCard Worldwide, Global Insights, Jan. 2013).


\textsuperscript{79} See \textit{ibid}. 


Again, these upticks are pricing an increasing number of Americans – particularly low-income Americans – out of the traditional banking system, thus also making credit card access more difficult. In 2013, there were 9.6 million unbanked U.S. households, up from 9.1 million in 2009 before Dodd-Frank passed in 2010.80 A 2015 Fed report found that 16.7 percent of Americans from households earning less than $40,000 are unbanked, compared to 7.6 percent overall.81 The impact of minimum balance and fee increases is likely sizable: in a 2013 FDIC survey, 57.5 percent of unbanked Americans listed “not having enough money to keep in an account or meet a minimum balance” as a reason for not having an account.82 In 2009, before the Durbin Amendment, just roughly 34 percent of unbanked respondents (who had been previously banked) reported that “not [having] enough money to need” an account was a reason for being unbanked, while 11 percent reported that the minimum balance requirement being “too high” was a factor.83 In the 2013 FDIC survey, 31 percent of unbanked Americans reported “high or unpredictable” account fees as a reason for not having accounts; in 2009, just 12 percent of previously banked households listed service charges as a reason for not having an account.84

The Durbin Amendment is hardly, of course, the only culprit behind the rise in bank fees and minimum balances. Low interest rates are certainly also a factor as is the over 100 percent

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80 See Joe Valenti, “Millions of Americans are Outside the Financial System” (Center for American Progress, Oct. 2014) (citing FDIC data).
81 Board of Governors of the Federal Reserve System, supra note 3, at 25.
83 Federal Deposit Insurance Corporation, National Survey of Unbanked and Underbanked Households (Dec. 2009), at 27.
84 Ibid.; Federal Deposit Insurance Corporation, supra note 82.
increase in bank regulatory restrictions between the 2010 CFR and the 2014 CFR.85 Notably, banks with less than $10 billion in assets are formally exempted from the Durbin price caps. Yet in a recent survey of banks with asset sizes under this threshold, half reported being affected by the Durbin Amendment.86 A separate survey of community banks found that 61 percent would ultimately set a minimum balance requirement in response to the Durbin Amendment.87 Competition between large and small banks forces community banks to face the impacts of Durbin’s price cap,88 pricing lower-income Americans out of the basic banking relationships that enable credit card access.

(3) CFPB “regulation by enforcement” and “backdoor rulemaking”

Unpredictable CFPB enforcement actions against credit card companies also likely exert downward supply-side pressure on the provision of credit cards to lower-score, lower-income Americans. Dodd-Frank grants the CFPB authority to investigate, prevent, and prosecute prohibited “Unfair, Deceptive, or Abusive Acts and Practices” (UDAAP) by firms providing various consumer financial products.89 Clear standards for “abusive” practices are essentially nonexistent; even CFPB Director Richard Cordray has referred to the term “abusive” as “a little bit of a puzzle.”90 What constitutes “unfair” or “deceptive” is also only broadly defined.91 Despite rulemaking authority to define UDAAP, the CFPB has chosen not to do so.92

As a March 2016 Promontory Financial Group publication explains, the CFPB “continues to shape” how it defines UDAAP through non-rulemaking actions (such as guidance bulletins and supervisory findings).93 It also notes that “UDAAP’s expanding scope still leaves room for interpretation” by firms and regulators alike.94 Some refer to the CFPB’s use of bulletins, notices, and other non-rulemaking actions to pursue policy objectives as “backdoor rulemaking” given that this process enables the CFPB to avoid formal, transparent regulatory procedures while still augmenting lender behavior.95 One example of “backdoor rulemaking,” notes Senior

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85 RegData 2.2 (using four-digit industry code 5221 – Depository Credit Intermediation), The Mercatus Center at George Mason University. For more on RegData, see Al-Ubaydli & McLaughlin, supra note 59.
87 Letter from Karen M. Thomas, Senior Executive Vice President, Independent Community Bankers of America, to the Board of Governors of the Federal Reserve System (Feb. 22, 2011), at 23.
88 Peirce et al., supra note 86, at 64.
89 Dodd-Frank Wall Street Reform and Consumer Protection Act § 1036 (2010).
92 See ibid.
94 Ibid.
95 See Hester Peirce, Senior Research Fellow, The Mercatus Center at George Mason University, testimony on May 21, 2014, before the Financial Institutions and Consumer Credit Subcommittee, House Committee on Financial Services, 113th Congress, 2nd sess., at 4 (suggesting that the CFPB’s avoidance of regulatory requirements through
Research Fellow Hester Peirce of the Mercatus Center at George Mason University, is CFPB Director Cordray’s suggestion that firms reference an examination manual to determine what constitutes a UDAAP violation.96 Similarly, a five-page CFPB bulletin warning that certain APR promotions and grace periods might constitute UDAAP violations was recently used in lieu of a formal regulatory process to discourage certain product features.97

A lack of clarity as to what constitutes improper lender behavior has certainly not stopped aggressive CFPB enforcement actions against credit card issuing firms. As of December 2015, card-related cases were the most frequent CFPB UDAAP enforcement actions other than mortgage-related cases, and in July 2015, the CFPB noted that it “has secured billions of dollars of relief to millions of consumers” through credit card-related enforcement actions.98 These actions and “backdoor rulemakings” have contributed to what many call a “regulation by enforcement” regulatory environment for UDAAP violations – also characterized as a regulatory “guessing game”99 – in which enforcement actions, consent orders, and exam notices, as well as guidance bulletins, set “guideposts” as to what constitutes acceptable lending behavior.100

Reliance by the CFPB on “backdoor rulemaking” and “regulation by enforcement” allows it to leverage legal ambiguity in order to maximize enforcement effectiveness. A troubling side effect, of course, is that these strategies drive firms to simply stop offering products subject to potential enforcement actions,101 or instead, to only offer “plain-vanilla” products in order “to avoid scrutiny by the Bureau.”102 These products may be suitable for “plain vanilla” consumers, but these individuals hardly exist.103

The effects of the CFPB’s enforcement culture on credit card add-on products (such as credit insurance, which enables a consumer’s credit card bill to be paid in the event of unemployment or another negative income shock) illustrate the consequences of the existing

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96 Ibid. at 4 note 27 (explaining that “using enforcement manuals to proscribe conduct is another form of backdoor rulemaking. Institutions should not be forced to read examination manuals to determine what their legal obligations are.”).
101 See Hester Peirce, “CFPB Knows Abuse When It Sees It” (Expert Commentary, The Mercatus Center at George Mason University, Mar. 29, 2012) (explaining how the CFPB’s flexible enforcement of “abusive acts and practices” drives “businesses simply to avoid offering products to consumers”).
regulated approach.104 Add-on products – which if properly structured may help households more effectively use credit cards by ensuring that at-risk borrowers have the ability to pay in adverse scenarios – have nearly disappeared from the market.105 This makes credit card access more difficult for some consumers who may have demanded add-on products. Similarly, concerns over “regulation by enforcement” and UDAAP ambiguity may drive credit card companies to cut back on the range of cards with rewards programs – which are highly valued, and as of 2012, were provided to three-quarters of card users106 – offered to some consumers. Although rewards account for just 2.7 percent of card-related CFPB complaints,107 the CFPB’s 2015 credit card report and recent remarks by Director Cordray indicate that the CFPB is “concerned” about “confusing” elements of rewards programs.108 Yet avoiding offer-fulfillment failures (differences between rewards offered and rewards delivered), which bring about a high risk of a UDAAP violation, can be very challenging for issuers due to the frequency of card transactions and the high rate of rewards offers extended.109

Banks are understandably eager to avoid product offerings that bring about sizable compliance concerns and/or substantial risk of CFPB examinations, which many companies report to be “confusing, unnecessarily duplicative, inconsistent, and open-ended.”110 Thus it is easy to see how UDAAP-related enforcement actions and “backdoor rulemaking” will result in fewer product varieties being offered to lower-income, lower-score Americans if the CFPB’s enforcement and regulatory culture continues unchanged. While the CFPB examination manual notes that potential UDAAP violations can be outweighed by offsetting benefits to consumers and competition, because no implementing regulations have defined UDAAP, understanding what constitutes a UDAAP violation still necessitates “learning through the mistakes of others,” as Eliott C. Ponte of the National Association of Federal Credit Unions recently warned.111 That lenders must learn from each other’s “mistakes” to remain compliant is indicative of an unnecessarily unpredictable and expensive regulatory climate, the costs of which are likely in large part ultimately felt by American consumers.

V. Policy Implications

Regulatory activities that risk substantially reducing consumer financial product access should come with meaningful benefits to consumer financial protection. Certainly, many of the supply-side regulatory constraints discussed in Section IV aim to achieve objectives deemed desirable by policymakers, such as lower card default rates, reduced card fees, and increased

105 See ibid.
106 Richard Cordray, “Prepared Remarks of CFPB Director Cordray at the Consumer Federation of America” (Dec. 3, 2015) (noting that according to CFPB research, “over half of all consumers say they select credit cards based on the rewards they provide”); Canner & Elliehausen, supra note 35, at 18 (Table 4).
108 See Cordray, supra note 106; Consumer Financial Protection Bureau, supra note 49, at 229-236.
110 Letter from David Hirschmann, Center for Capital Markets Competiveness, to Director Cordray, Consumer Financial Protection Bureau (Feb. 14, 2013), at 2.
111 Ponte, supra note 91, at 3.
enforcement actions against “unfair,” “deceptive,” or “abusive” activities. Also, as explained above, the CFPB finds that the CARD Act has resulted in its intended impacts of reducing credit card fee types and sizes.112

Yet the post-2007 surge in credit card-related regulatory activity does not appear to have significantly altered overall consumer satisfaction with credit cards. The share of U.S. households dissatisfied with their credit cards remained relatively constant between 2001 and 2012 (6 percent versus 8 percent, respectively), as did the share of households saying that credit cards made managing finances more difficult (10 percent versus 8 percent).113 J.D. Power consumer ratings in 2008 – prior to the CARD Act, 2008 Fed rulemakings and the CFPB’s creation – illustrated widespread consumer satisfaction with credit cards and accompanying fees and rates.114 The recent J.D. Power credit card customer satisfaction survey, while reporting record highs in customer credit card satisfaction, shows largely modest gains over customer satisfaction levels reported in 2008.115 Notably, rewards were a major driver behind the uptick in customer satisfaction, and impressions regarding the security of personal information also had a positive impact on consumer sentiments.116 Yet in 2008, rates and fees had “little impact” on customer ratings – as the executive director of financial services at J.D. Power noted at the time: “You’re not seeing some whopping number that people are really ticked off with the fees in their credit cards.”117

In crafting the existing regulatory paradigm, legislators and regulators likely succumbed somewhat to the “other-guy” effect outlined in the introduction – overestimating Americans’ propensity for suboptimal credit card usage decisions. Surely Americans do not fully consider every single cost and risk associated with their credit card, but there are costs to seeking out information, and empirical evidence suggests that consumers swiftly learn from oversights, mistakes, and borrowing experiences, and more generally, for the most part use credit cards in ways consistent with consumer rationality.118 Many studies and surveys (some of which are presented in this working paper) similarly suggest that most Americans who have credit cards generally understand the risks of the product, frequently use them to achieve intended outcomes, and gain substantial financial management benefits from doing so.119 Yet because post-2007 regulatory actions likely do not appropriately reflect these findings, credit cards may now be unnecessarily out of reach for many households once on the margins of approval who would have responsibly used this product.

Not only does this impede these households’ ability to enjoy the transactional benefits of credit cards (such as engaging in online commerce made less risky by credit cards), but also, with credit cards out of reach, increasingly more Americans appear to be “paying” for lacking a

112 Consumer Financial Protection Bureau, supra note 73.
113 See Canner & Elliehausen, supra note 35, at 18 (Table 4).
116 Ibid.
117 Ibid, supra note 114.
118 See generally Durkin et al., supra note 5, at 124-172; Durkin et al., supra note 66.
119 For a comprehensive overview of studies and surveys that illustrate consumers’ propensity to use credit cards in beneficial and reasonable ways, see generally ibid.
credit card by using more expensive alternatives. In fact, in one survey, 55 percent of payday loan users reported being denied or limited credit in the past five years;\textsuperscript{120} in another, 23 percent report being turned down (or anticipated being turned down) for a credit card within the last year.\textsuperscript{121} A recent Fed survey reports 4.2 percent of American households took out a payday loan at some point in 2013, compared to 2.4 percent in 2007 (before the recent increase in credit card-related regulations).\textsuperscript{122} Due to the intended short-term nature of payday loans, their APRs can easily exceed 300 percent, while the average APR across all commercial bank credit card accounts was 12.66 percent in Q4 2015.\textsuperscript{123} Borrowers, of course, are generally very well aware of these costs, and choose to use payday loans because other options (like overdraft protection or pawnshops) are even costlier.\textsuperscript{124} Credit cards are essential sources of emergency funds (and especially were during the last financial crisis\textsuperscript{125}), so decreased availability can simply drive financially stressed consumers to more expensive, readily accessible alternatives (in 2012 there were more payday loan storefronts than McDonald’s in the U.S.\textsuperscript{126}). Now even middle-income Americans appear to be turning to alternative financial services, and as of 2011, 25 percent of Americans had used an alternative financial product or service.\textsuperscript{127}

The regressive trends profiled throughout this working paper also impede the ability of low-income Americans to start businesses. Small business growth – and thus U.S. job creation, as small businesses account for approximately one-third of enterprise employment\textsuperscript{128} – relies heavily on personal credit card availability. According to survey data reported by the National Federation of Independent Businesses, nearly one in five owners of a very small business (those with one to nine employees) revolve balances on their personal credit card to finance their company’s operations.\textsuperscript{129} Overall, half of small business owners report using a personal credit card or cards to pay for business expenses.\textsuperscript{130} Large firms, of course, have also felt the cost of the post-2007 regulatory surge: 2011 Boston Consulting Group research estimated that regulations stemming from 2008 Fed rulemakings, the CARD Act, and Dodd-Frank’s Durbin Amendment will ultimately result in “as much as $25 billion in annual retail-transaction revenues – about 29

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\textsuperscript{124} See ibid.


\textsuperscript{130} Ibid.
percent of total retail-transaction revenues – [being] ‘regulated away’ from financial institutions.”

Furthermore, supply-side regulatory constraints may be increasing the number of Americans without a credit score – CFPB researchers report that 19 million Americans have an unscorable credit file and 26 million have no file at all. The problem is especially severe in low-income neighborhoods, where their analysis finds that half of consumers lack credit scores, compared to 9 percent in high-income neighborhoods. Without credit scores, consumers have a difficult time purchasing homes and starting businesses. This harms economic growth and mobility. The trend is particularly concerning for young Americans for whom CARD Act regulations have made credit card access difficult. The Act bans companies from issuing credit cards to borrowers under 21 unless (1) a parent co-signed (a disproportionate burden on lower-income households) or (2) income documentation was provided (harder to supply for many odd jobs and some starter jobs). In 2006, 80 percent of 19-year-olds had established credit, versus less than half in 2014, with a similar pattern holding true for 20- and 21-year-olds.

Younger Americans also disproportionately face the burdens of the recent 380 percent increase in U.S. student loan debt, which, as explained in Section II, is a major driver behind record-high consumer credit levels in the U.S. Policymakers should, of course, be weary of recent increases in U.S. household debt caused in large part by a surge in consumer credit levels; high national balances of household debt can impede economic growth and increase the likelihood of financial downturns. Thus the appropriate policy focus is not to pressure lenders to extend credit when doing so is an uneconomical decision – this would almost certainly be harmful to the broader economy. Instead policymakers should work to alleviate policies that unintentionally and unnecessarily increase the cost of issuing credit. Granted credit cards are certainly not appropriate for all consumers, but given (1) most consumers’ propensity to understand the risks of credit cards, (2) the various economic benefits of credit cards illustrated above, and (3) that credit card debt remains a relatively small portion of overall U.S. household debt levels (roughly 6 percent), mitigating regressive trends that impede many low-income Americans’ access to these useful financial tools would likely not result in a concerning impact on household debt levels. In fact, because doing so would likely improve many Americans’ economic livelihood and the broader economy, we set forth the following policy recommendations below.

VI. Rethinking Credit Card Regulation and Rule Enforcement

In order to address the troubling policy implications brought about by regressive trends in credit card access, we recommend that U.S. policymakers pursue three broad areas of reform. First, Congress should consider legislative fixes to some of the clear unintended consequences

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133 Ibid.
135 See, for example, Leigh et al., supra note 10.
136 Federal Reserve Bank of New York, supra note 11; authors’ calculations. Credit card debt as a share of total U.S. household debt has remained below 8 percent since Q3 2003.
outlined above. This begins with repealing some provisions of the CARD Act to allow issuers greater latitude in structuring the cost of credit, thus enabling more Americans to develop credit histories and access credit products that – despite exceptions and risks – generally provide a positive contribution to personal financial health. While a full discussion of tradeoffs associated with eliminating specific restrictions is outside the scope of this paper, one critical step to reversing regressive trends in credit card access is to enable issuers to adjust fees and rates to more adequately account for borrower risk. The status quo regulatory arrangement necessitates that lenders originate cards with unnecessarily high rates to “compensate for the potential risk that a borrower might miss a payment at some time in the future.”\textsuperscript{137} The Fed’s approach to stress testing should also be reevaluated to ensure it does not unnecessarily contribute to regressive card-issuance patterns that harm growth and mobility.

Regulatory and legislative fixes such as these, however, will only go so far. Broader, institutional remedies are needed, particularly in the wake of the CFPB’s plan to restrict credit card issuers’ ability to use arbitration clauses (which could massively alter the industry)\textsuperscript{138} and systematically insufficient cost-benefit analysis of CFPB and Federal Reserve rulemakings.\textsuperscript{139} We maintain that many unintended regulatory consequences could be avoided were federal financial regulators required to conduct cost-benefit analyses for major proposed regulations, as we advocated in a separate working paper, “The State and Fate of Community Banking.”\textsuperscript{140} These analyses should be subject to review by the Office of Information and Regulatory Affairs, a process that would result in better-designed regulations with fewer unintended consequences.\textsuperscript{141} Intended consumer financial product safety benefits can and should be achieved at a lower cost to consumers.

Yet reforms of the regulatory process are also not enough; the CFPB’s enforcement actions are unpredictable and the Bureau frequently leverages quasi-regulatory processes that are unaccountable – this may ultimately be quite costly to American consumers. Its current design – a single-director (which enables “backdoor rulemaking” because any statement by the director can appear to be the CFPB’s official position\textsuperscript{142}), the absence of a Congressional appropriations process, and an enforcement approach that fails to adequately take into account economic considerations – makes it ill suited to appropriately weigh consumer protection (of course, an extremely important objective) against other important policy goals such as credit product availability and its important role in economic growth; this in turn results in inadequate improvements to consumer products and services.

\textsuperscript{137} Strongin et al., \emph{supra} note 51.


\textsuperscript{139} See Committee on Capital Markets Regulation, \emph{A Balanced Approach to Cost-Benefit Analysis Reform} (2013).


\textsuperscript{141} \emph{Ibid}.

deliberation of regulatory costs and consequences. Regulatory and enforcement approaches at the Bureau should shift away from the notion that restrictions on back-end risk-based penalty pricing via fees (such as late fees, over-the-limit fees, and cash advance fees) and adjusting rates on existing balances are inherently desirable, and more adequately and transparently consider the costs to consumer choice and innovation of its current approach to consumer financial protection regulation.

Thus the CFPB’s mission should be reformed to better balance consumer financial product access and choice with consumer financial product safety, thus mirroring the Federal Trade Commission’s (FTC) multifunction mission, which has been a critical “source of strength” in policy formation. Furthermore, the Bureau should be transformed into a multi-member commission in order to (1) check against the propensity for bureaucratic “tunnel vision” when promulgating and enforcing rules, (2) avoid unintentionally regressive rulemakings by ensuring that balanced considerations of varying viewpoints on consumer rationality take place, and (3) mitigate the propensity for “backdoor rulemaking” brought about by a single-director structure. Subjecting the CFPB to a Congressional appropriations process is also critical; doing so would further serve as a check against unaccountable “backdoor rulemaking.”

Finally, policymakers should reduce regulatory burdens that unnecessarily increase the cost of banking. As mentioned earlier, the proliferation of inexpensive checking accounts enabled lower-income Americans to gain credit cards. Bipartisan legislation that would have repealed the Durbin Amendment, introduced in 2011, should be reintroduced and passed.

More broadly – and as we propose in “The State and Fate of Community Banking” – a bipartisan commission should be established (based on the Base Realignment and Closure Commission) to merge, streamline, and consolidate banking and consumer finance regulations, including those brought about by the recent 250 percent surge in credit card regulatory restrictions implemented by U.S. federal financial regulators.

VII. Conclusion

In general, credit cards enable Americans to make more optimal purchasing decisions, facilitate access to liquidity, drive economic mobility, and finance small business growth. While excessive household debt is seriously problematic from a policy perspective, we find that credit card balances make up just a small fraction of total household debt, increased only modestly in the lead-up to the crisis, and are now far below highs of the 2000s, particularly when taken as a share of disposable personal income. Despite demand for consumer credit by lower-score and

143 See generally Zywicki, supra note 103.
144 See Smith & Zywicki, supra note 104.
145 See Zywicki, supra note 103, at 894.
146 See ibid., at 877-878; Lux & Greene supra note 140.
147 See Smith & Zywicki, supra note 103; Peirce, supra note 140, at 5-6.
148 See ibid.
lower-income Americans being quite high, and the many practical benefits of these products, access to and usage of credit cards has diminished in recent years for many lower-score and lower-income Americans.

We find that CARD Act-related restrictions on risk-based penalty pricing via fees and the adjustment of rates on outstanding balances, as well as other supply-side constraints, are likely major factors behind credit cards increasingly being out of reach for many lower-score and lower-income households. Other important factors include: (1) shifts in consumer behavior, (2) a growth in the number of unbanked Americans (in part driven by regulatory factors), and (3) a CFPB that engages in unpredictable enforcement and opaque quasi-regulatory activity.

Surely, there is a tension between consumer financial product safety and financial product access. To improve consumer financial protection, regulators may deem it necessary to heavily regulate certain products. Yet in the wake of a 250 percent surge in credit card regulatory restrictions established by U.S. financial regulators since 2007, Americans’ experience with credit cards has at best only modestly improved. This is unsurprising, given that Americans not only largely demonstrate informed utilization of credit cards and responsiveness to their features, but also have overwhelmingly expressed satisfaction with credit cards for quite some time. It appears likely, however, that a narrowly focused pursuit of consumer financial protection – guided by fundamental misjudgments about Americans’ propensity for suboptimal borrowing decisions – has contributed to shrinking credit card access for Americans on the margins of approval, hurting those who could benefit most from access to this useful financial product.

The extent to which this is the case can, of course, be debated, and we certainly acknowledge the financial harm that the accumulation of excessive credit card debt poses. By no means should the findings of this working paper be interpreted as support for high U.S. consumer debt levels. Instead, this research aims to highlight regressive trends in credit card usage and access, likely causes, and why these trends are financially harmful to many households. With credit cards out of reach, American consumers are increasingly turning to more expensive credit products, or finding themselves without access to suitable credit markets altogether. To remedy unnecessarily regressive trends in credit card access, U.S. policymakers should (1) remove some CARD Act restrictions on lenders; (2) reform the CFPB into a dual-mission, multi-member commission accountable to Congress; (3) repeal the Durbin Amendment; and (4) establish a bipartisan commission to assess how to streamline banking regulations to ensure basic banking services are more accessible to American households.