

# CREDIT CARD ACT OF 2009: IMPLICATIONS FOR BALANCE TRANSFER PRODUCT

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## Summary

The Credit Card Act of 2009 (“Act”) imposes several limitations on what issuers can or cannot do in their credit card portfolios with respect to fees, APRs, penalty APRs, disclosures, etc. A cursory analysis of profitability and viability of the Balance Transfer product under the pretext of the Act would lead one to believe that the Act will kill the Balance Transfer product. A deeper analysis though, reveals that the Act provides significant opportunity for issuers to reinvent the product and find new population segments that were unattractive earlier. Profit Technologies (“PTC”) has done extensive analysis of the Act and its impact on the credit card industry.

The “consumer friendly” payment allocation imposition, combined with an anticipated widespread increase in the Purchase APR

1. will make the Balance Transfer product attractive to certain segments of the population that found the product unattractive prior to the Act, and
2. will increase risk within certain segments.

## Items Of Interest In The Act

There are a few items in this Act that are of particular interest in relation to the Balance Transfer product.

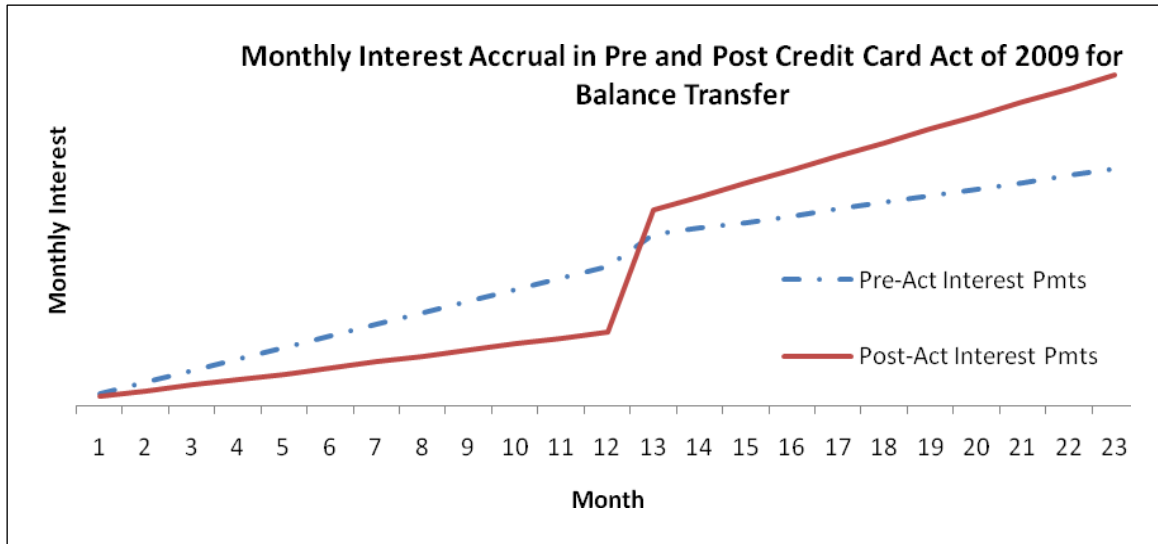
1. **Payment Allocation:** Upon receipt of a payment from a cardholder, the card issuer shall apply amounts in excess of the minimum payment amount first to the card balance bearing the highest rate of interest, and then to each successive balance bearing the next highest rate of interest, until the payment is exhausted.
2. **Promotional Rate Minimum Term:** The promotional APR must be effective for *at least* a 6 month period.
3. **Go To APR (APR upon Promotional APR expiration):** The issuer is permitted to have a higher APR in effect (usually the Purchase APR), as long as the issuer discloses to the consumer, in a clear and conspicuous manner, the APR that would apply after expiration of the promotional period.
4. **Balance Transfer Fee:** The Act does not stipulate any limitations or restrictions on Balance Transfer fee.

## Balance Transfer Economics

There are four components to Balance Transfer revenue:

1. **Balance Transfer Fee:** In the U.S., most Balance Transfer offers carry at least a 3% fee; 4% and 5% fees have been observed as well.

2. **Interest Trapping:** Due to payment allocation, the interest trapping is one way to generate additional revenue prior to the Act going into effect (“Pre-Act”). This is mostly applicable to the Revolver population segment since Transactors have largely shied away from this product due to interest carry.
3. **Universal APR Increases:** There is a widespread belief that the APRs will increase across the portfolios because of the restrictions the Act imposes on the issuers. This means that Post-Act, when promotional rates expire, the outstanding balances in those promotional buckets will reset to a relatively higher APR as compared to in a Pre-Act situation.



## Conclusion

The Credit Card Act of 2009 does impose severe restrictions and causes business disruption. No fee product, which is already retreating, will become obsolete. PTC can help issuers find ways to continue generating earnings and profitable balances through Balance Transfer products with the *right mix of targeting and risk management*. Without this new approach to managing Balance Transfers, this product would definitely become obsolete, at least in its current form.