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CHARGE IT

CREDIT CARDS AND THE CANADIAN CONSUMER

REPORT OF THE STANDING COMMITTEE ON CONSUMER AND CORPORATE AFFAIRS AND GOVERNMENT OPERATIONS

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Minutes of Proceedings and Evidence of the Standing Committee on

Consumer and Corporate Affairs and Government Operations

Procès-verbaux et témoignages du Comité permanent de la

Consommation et des Corporations et de l'Administration Gouvernementale

RESPECTING:

An examination of the evolving role of credit cards in the Canadian economy pursuant to Standing Order 108(2)

INCLUDING:

The First Report to the House

CONCERNANT:

Étude de l'évolution du rôle des cartes de crédit dans l'économie canadienne conformément à l'article 108(2) du Règlement

Y COMPRIS:

Le Premier Rapport à la Chambre

Second Session of the Thirty-fourth Parliament, 1989

Deuxième session de la trente-quatrième législature, 1989

STANDING COMMITTEE ON CONSUMER AND CORPORATE AFFAIRS AND GOVERNMENT OPERATIONS

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The Standing Committee on Consumer and Corporate Affairs and Government Operations has the honour to present its

FIRST REPORT

In accordance with its mandate under Standing Order 108(2), your Committee has examined the evolving role of credit cards in the Canadian economy and has agreed to present this report.

Fewer than three years have passed since the last parliamentary Committee reported on credit cards in Canada. The first question to be addressed in this report, therefore, is why the issue is being reexamined. There are several answers.

The best is that the public once again perceives a problem with credit cards. Former MPs, the constituents of current MPs and newspaper columnists have noted the high level and stickiness of credit card rates. These observers and others have watched with concern the growing importance of credit cards in the economy and the many innovations in the credit card market. Everyone is concerned with how difficult it is to understand the pricing of the various types of cards—difficulties that were not solved by the previous parliamentary report.

The members of this Committee share these concerns and, of course, have a duty to examine publicly perceived problems.

In addition, the members of this Committee take a wide view of consumer affairs, a view that includes possible future developments. There seems little doubt that electronic funds transfers (EFT) will be at the centre of consumers' future financial transactions. We cannot claim to know the exact nature of the future EFT system, but we can say that the credit card is an important bridge to it.

If there are problems with credit cards today, will these problems be magnified in the future? Again, we cannot say for sure. But we do feel confident that if we address any problems with today's credit cards, we will be setting the stage for a more efficient and equitable EFT system tomorrow.

This report is meant to accomplish three tasks. The first is to examine the perceived problems. An important finding in this report is that there is not a structural flaw in the market for credit cards, structural in the sense that immediate legislation (or action by the Bureau of Competition Policy) is warranted. The workings of the market can be improved, however, by providing the consumer with better information about the true relative price of various cards.

The need for better information is the basis for the second and third tasks of this report. The second is to show the consumer how to use the information that is currently available to make wise choices about credit cards (or even about whether to use a credit card). The third task is to signal to the card issuers how they should improve the information they provide consumers.

Under Standing Order 108(2), the House of Commons Standing Committee on Consumer and Corporate Affairs and Government Operations decided in mid-1989 to examine the evolving role of credit cards in the Canadian economy. The Committee held hearings in June with Mr. Don Blenkarn, M.P., Chairman of the Finance Committee; Mr. Reginald Stackhouse, former M.P. who first raised the issue in the House in mid-1986; Ms. Linda Leatherdale, business editor of the Ottawa *Sun*; and officials with the Consumers Association of Canada, the Canadian Bankers' Association, the Retail Council of Canada, and the Trust Companies' Association of Canada.

During the summer recess, the Committee directed one of its researchers to examine several remaining issues, including methods of calculating interest charges for different types of credit cards and the current practices of Canadian card issuers with respect to the disclosure of cost information to consumers. Members held several *in camera* meetings in October to draft the report.

BACKGROUND

The Finance Committee tabled its report *Credit Cards in Canada* in March 1987. This report and the Background Paper "Interest Rates and Credit Cards" appended to it provide useful information about the workings of the credit card market in Canada.

That report noted the importance of credit cards in the Canadian economy, the increasing versatility of cards and the substantial growth in the use of cards from the late 1970s to the mid-1980s. Since that time, the growth has been even more impressive.

Appendix 1 contains a table from the earlier report and adds three years of data for the use of MasterCard and Visa. These are often called bank cards, although they are issued by trust companies, credit unions and other financial institutions in addition to banks. The latest data available are for 31 October 1988, the end of the banks' 1988 fiscal year. Credit card sales grew by 56.7% between the end of fiscal years 1985 and 1988. To provide a frame of reference, nominal GNP grew 25.3% over the same period.

MasterCard and Visa are now used for about 9% of all consumption, up from about 7% at the end of 1985. Half a billion transactions each year are now made with these cards. Retail card use would increase these figures. In some department stores, over half the purchases are on credit. Even these facts understate the importance of credit cards. During the hearings, Committee members brought out the fact that credit cards are now an importance piece of identification. You may need one to cash a cheque or register at a hotel, and you will almost certainly need one to rent a car.

On the back of many credit cards, a magnetic strip gives access to a worldwide network of automated teller machines (ATMs). Growth in the use of ATMs has also been spectacular, and this growth adds to the convenience of many credit cards. Some retailers whose cards do not have access to the ATM network have set up procedures for using their cards to obtain cash.

It is obvious that the financial system is changing. A retailer who provides a cash advance now competes not just with other retailers selling similar products but with financial institutions. Several parliamentary committees are concerned with these trends. Right now, this Committee notes the pivotal role of credit cards in these trends.

But it is not the growing importance of credit cards that has attracted most public comment. Instead, it is the cost of using these cards, especially the high interest rates and the method of calculating interest charges. Appendix 2 contains a figure showing representative credit card rates (for MasterCard, Visa and a typical retailer) and the Bank Rate, all from the late 1970s. Note that the MasterCard rate shown is the rate for a card with no fees. The Visa rate is for a card with a $6 annual fee or 15 cents per transaction. (This is down from the $12 fee or 15 cents per transaction that was introduced in the third quarter of 1983 and lowered in the third quarter of 1987.)

As can be seen from the figure, credit card rates are sticky in the sense that they change less frequently than other short-term rates such as the Bank Rate. In part this is due to legal requirements that make card issuers notify their customers at least 30 days before a rate change. Since mid-1987, the rates on the so-called bank cards have changed more often than in the previous decade. There has not been a complete interest rate cycle since that time, however, so it is not possible to say whether future changes will be more frequent with a general fall in interest rates.

Of note in the Figure in Appendix 2 is the spread between card rates and short-term rates, represented here by the Bank Rate. With sticky card rates, this spread fluctuates over a wide range. In August 1981, for example, the Visa-Bank Rate spread was actually slightly negative; in May 1983, this spread had reached 14.62 percentage points.

The Visa-Bank Rate spread was 11.46 percentage points in February 1987 while the Finance Committee was drafting its report. With the drop in bank card rates following the report, the spread fell to 7.31 percentage points. The Finance Committee did not frame its recommendation for bank card rates in terms of a desired spread between card rates and a reference short-term rate. Given the pattern of interest rates that prevailed while the Committee was examining credit cards and recommendation 6 concluding the section "The Special Position of the Large Banks," it is possible to say that the Committee would have accepted a Visa-Bank Rate spread of 7 to 7.5 percentage points.

The spread at the end of September 1989 was 7.52 percentage points. In other words, the recent movements of the bank card rates have been in line with the general movement of rates in Canada.

This spread may strike some observers as still excessive, but it can be explained by the high non-interest costs of running a credit card operation. Research undertaken by the Finance Committee and information from U.S. studies support this explanation of a high spread.

Appendices 3 and 4 contain figures that show that spreads between bank card rates and short-term rates are actually lower in Canada than in the United States and the United Kingdom. Since the mid-1980s, moreover, the general pattern of bank card rates in Canada and the U.K. has been similar, with decreases in 1987 and increases in the past year.

MasterCard and Visa are not, of course, the only credit cards in Canada. Outstanding balances on cards issued by the major department stores now run at about a third of the outstanding balances for the so-called bank cards. There are scores of other retailers who offer credit cards; many oil companies offer cards, though some of these are like American Express, Diner's Club, and other travel and entertainment cards in that they are charge cards.

Appendix 5 contains an exhibit showing the costs and terms of 14 bank cards and 19 other cards. This exhibit is from "Credit Card Costs—September 1989" put out by Consumer and Corporate Affairs. The data are for September 1st and generally show the costs and terms set out in the cardholder's agreement.

In some cases, however, the data on grace periods are for standard practices; the standard practice for The Bay, for example, is to allow 30 days for a grace period, although officially the term is 25 days. Whether the official or standard practice is shown depends on the card issuer. Some have standard practices that are more lenient than their official or posted practices but do not want this publicized.

The tables in the Consumer and Corporate Affairs publication show the wide array of terms available on credit cards in Canada—and these tables do not include the premium or gold cards available. The text with the tables highlights additional complications.

Over the summer recess, the Committee had one of its researchers prepare a Background Paper on credit cards (T.J. Thomas, "Interest Charges and Other Costs of Credit Cards," forthcoming). This paper examines the pricing of bank cards and retail cards, and shows, going step by step, how various transactions (purchases, cash advances, partial payments and full payments) would affect interest charges.

The paper clears up some misconceptions about credit cards, but also shows that the comparison of nominal rates for different cards may not indicate the best deal for consumers. The following are the major findings for the so-called bank cards and retail cards.

1. **Bank Cards**

a. In general, a credit card loan is priced the same as a small daily loan: interest is charged at a daily rate from the day the loan is made until the day the loan is repaid.

b. Interest is charged (i) from the posting (roughly the purchase) date to the statement date, (ii) for the month from statement date to statement date, and (iii) from the statement date to the payment date (the so-called residual interest). This is the same as saying, as above, that interest is charged from the purchase date to the payment date. The component (ii) above may cover several months between the first statement date after purchase to the statement date before the final payment.

c. Multiple purchases, partial payments, full payments and the timing of these transactions make the calculation of interest charges complicated. Cash advances and use of a card outside Canada also add complications. But the general view of credit card lending as the same as a series of small daily loans stays true. Even in complicated cases, total interest charges can be divided into the three components.

d. The effective rate of interest for cards issued by financial institutions is never above the posted rate. The effective rate can, however, be below the posted rate if the consumer pays off in full before the end of the grace period and is charged no interest on new purchases. Two institutions do not charge residual interest; this also lowers the effective rate. If the consumer always pays in full by the end of the grace period, of course, the effective rate will be zero.

e. From the day a partial payment is made, interest accrues on the remaining balance, not on the previous outstanding balance.

f. Interest on bank cards is not compounded.

2. **Retail Cards**

a. Unlike bank cards, retail cards generally charge interest on a monthly basis with interest accruing from the statement date and not the purchase date. Retailers do not charge residual interest. In terms of the components of interest given above, retailers charge only component (ii).

b. Retailers also offer a grace period, and it is usually longer than that for bank cards (30 days versus 21 days for typical cards). If a partial payment is 50% or more of the outstanding balance, retailers calculate interest charges on the remaining balance; if the payment is less than 50%, interest is calculated on the previous outstanding balance.

c. Because interest charges are calculated on a monthly basis, it is fairly easy to figure out the dollar amount of charges. (This is true even after a partial payment has been made.) It is, however, extraordinarily complicated to figure out the effective rate of interest on a retail card.

d. It is reasonable to say that the range for the effective rate on a retail card is about 6% to 28.8% (assumed here to be the nominal or posted rate). If the consumer pays a purchase off in three or four months with roughly equal payments, the effective rate is around 20%, which is about what bank cards charge. The longer it takes to pay off a purchase, the closer is the effective rate to the nominal rate. It is theoretically possible to have the effective rate exceed the nominal rate, but the assumptions needed for this to be true are decidedly unrealistic.

The two most important findings in the paper are:

a. In no case examined was the effective rate on a bank card above the posted rate. Some observers have said otherwise and have suggested that the effective rate might be very high—even 1000 per cent. This is a mistake, probably one based on a faulty calculation.

(An example may clear up some confusion. Suppose you make a purchase for \$1000 on July 10th. The next statement, assumed to fall on the 25th of each month, shows a balance of \$1000. You make a partial payment of \$975 on August 5th, so the remaining balance is \$25. With no new transactions, the statement on August 25h will show a new balance of \$39.54, which is the sum of the previous remaining balance of \$25 and interest charges of \$14.54 based on a posted rate of 20 per cent per year.

There are two incorrect calculations that would produce large ostensible rates of interest. The first simply divides total interest charges (\$14.54) by the remaining balance (\$25): this gives an apparent rate of interest of 58.2 per cent. The other, more sophisticated, calculation adjusts for the length of the loan—\$25 for 21 days. This calculation takes the previously calculated rate of interest (58.2 per cent) and multiplies by 17.38 (which equals 365 days divided by 21 days) to give another apparent rate of interest of 1012 per cent. Both calculations are incorrect.

The reason the calculations are incorrect is that each ignores the implicit loan of $1000 from the purchase date to the payment date. The $14.54 in interest charges can correctly be considered the sum of interest charges on two implicit loans. The first is an implicit loan for $1000 running for 26 days from July 10th (the purchase date) to August 4th (the day before the partial payment was made). The second implicit loan is for $25 running 21 days from August 5th (the day of the partial payment) to August 25th (the statement date). The interest charge on the first implicit loan is $14.25; the interest charge on the second implicit loan is $0.29. In each case, the interest rate used was the daily rate corresponding to a 20 per cent annual rate—that is, 20 per cent divided by 365 or 0.05479 per cent per day.

The effective rate is 20 per cent per year, the same as the posted rate.)

b. It is reasonable to say that the range for the effective rate on a retail card is 6% per year to 28.8% per year. What the effective rate is depends on the timing of purchases and payments, the amount of any partial payment and the number of months it takes to pay the full balance.

Because the effective rate on a retail card can vary so widely, the spread between the effective retail card rate and the Bank Rate may be much smaller than the spread between the nominal rates shown in Appendix 2. The difference between the nominal and effective rate for a retail card depends on behaviour by the card user, behaviour that may not be consciously aimed at lowering the effective rate. With better information, a consumer might alter behaviour with respect to purchases and payments.

WORK OF THE FINANCE COMMITTEE, 1986-1987

The hearings, background research and report of the Finance Committee are readily available, so no detailed account of that Committee's work is needed. As noted, the Finance Committee was struck by the impressive growth of credit card use and concerned that rates might be at unwarranted levels. What led to this concern was the continued high level of rates in the face of a general downward movement in Canadian rates. (The Consumer and Corporate Affairs Committee also is concerned by high rates, but this concern was sparked by the recent increase in some credit card rates to their current high levels.)

The Finance Committee found that competition was fierce among card issuers and that there did exist lower cost alternatives to the credit cards issued by the large banks. The puzzle to the Finance Committee—and one that remains for this Committee—was "Why don't Canadians switch their Visa and MasterCard accounts from the large banks to other financial institutions?"

The Finance Committee offered three possible answers. The first, and most important, was a lack of information about the credit card market. The second was the uncertainty that a prospective card issuer might increase its rates and fees to match those of the large banks. The third reason was that Canadians were insensitive to the high rates on credit cards—the costs of finding and obtaining a lower cost card were greater than the expected savings on interest costs.

An important finding of the Finance Committee was that credit card debt rose with the income of the card user. Over half of those with 1983 incomes below $25,000 had no instalment debt, either because they had no credit cards or because they had paid off all their instalment debt. (These findings were based on a 1984 Statistics Canada survey that is still the source of the most recent data on the distribution of instalment debt.)

The Finance Committee made a number of recommendations in its March 1987 report. Some were aimed at having card issuers lower their rates. Others were aimed at improving the understanding by consumers of credit card pricing. The recommendations acknowledged the overlapping jurisdiction by the federal and provincial governments with respect to credit cards.

Soon after the report was tabled, the major issuers of bank cards lowered rates and fees by the equivalent of about 3 percentage points. Some rates, most notably the rates charged on retail credit cards, did not change.

WORK OF MINISTERS RESPONSIBLE FOR CONSUMER ISSUES

The work of the Finance Committee on credit cards and its recognition of overlapping jurisdiction stimulated the federal, provincial and territorial ministers responsible for consumer and corporate affairs to pursue the issue. In June 1987, the Ministers struck a working group to "propose a consistent standard for the disclosure of the rates, terms and conditions of the cost of credit."

The federal minister through the Department of Consumer and Corporate Affairs initiated a regular publication on the cost of credit cards in Canada. This began in December 1987 and gave fees, interest rates, grace periods and the starting point for calculations of interest charges for 35 credit cards.

In April 1988, the Federal-Provincial-Territorial Working Group on Cost of Credit Disclosure published the "Discussion Paper on Credit Card Interest Charges." This paper provided background information on credit cards in Canada and pointed to several alternatives for increasing the awareness and understanding of credit card interest charges.

Since the publication of the discussion paper, the Working Group has met with several card issuers, associations representing their issuers, and consumer groups. At the most recent annual Conference of Federal, Provincial and Territorial Ministers responsible for consumer issues, the Ministers again examined credit card interest charges.

The following is the relevant paragraph from the Conference News Release (NR-25308, 12 September 1989):

> Credit card interest charges continue to be a concern of consumers and governments. The Ministers warned the credit card industry that it must take further action to disclose the components of total interest charges on credit cards in a clear manner. The Ministers acknowledged the credit and industry's efforts to improve consumer understanding of credit card costs, but indicated they were not satisfied with the steps taken to date.

As was the case with recent legislation in the U.S. and, to some extent, with the 1987 Finance Committee report on credit cards in Canada, the emphasis of the Ministers is on disclosure and not the regulation of rates. At this time, moreover, the Ministers appear to be looking for voluntary disclosure by card issuers. The following shows a possible breakdown of interest charges that would meet the type of voluntary disclosure sought:

(a) interest from the purchase date to the next statement date,

(b) interest accruing during the month covered by the statement, and

(c) interest from the payment date to the statement date (the so-called residual interest).

The interest on cash advances might also be shown as a separate component.

Further breakdowns are possible—for example, (b) could be divided into interest that accrued before a payment was made (that is, interest based on the total balance) and interest that accrued after a payment (that is, on the remaining balance). Dividing total interest charges into too many components, of course, leads to confusion and defeats the purpose of the breakdown.

Retailers would be little affected by such a disclosure requirement: most retailers calculate interest on a monthly basis from the statement date, so their interest charges would fall only into category (b) above. Financial institutions would face large programming costs with such a requirement.

Interest charges in categories (a) and (c) above often surprise consumers and lead them to think that the pricing of credit cards is unfair (one can, for example, pay off a card balance in full and still have interest charges accrue in category (c)). If consumers saw the components of total interest—and understood the rationale for each component—there might be fewer complaints about credit cards. But such disclosure would not help a consumer choose the card that would offer the lowest effective rate of interest.

As an example, consider the case where you make a purchase for $1000 on July 10th. The statement on July 25th shows an outstanding balance of $1000 (no interest charges are shown for a new purchase). On August 5th you make a partial payment of $400. The statement on August 25th shows a new balance of $621.15, the sum of the remaining balance of $600 and interest charges of $21.15.

These interest charges may be broken down into the components (a) and (b) above. Component (a) is $8.77 and represents the interest charges on $1000 for the 16 days between July 10th (the purchase date) and July 25th (the statement date after the purchase). Component (b) is $12.38 and represents the sum of charges on two implicit loans, one for $1000 for the 10 days running from July 26th (the first day of the new statement, or billing, period) to August 4th (the day before the partial payment was made) and the second implicit loan for $600 from August 5th (the payment date) to August 25th (the next statement date).

Assume you pay the entire balance of $621.15 on September 7th and have no new transactions during the September billing period. The statement on September 25th will show a new balance of $3.95. This is the residual interest, or component (c) above, on the implicit loan of $600 from August

26th (the first day of the new statement period) to September 6th (the day before the payment was made).

The work of this Committee builds on previous work of the Finance Committee and, to some extent, parallels the work of the Ministers responsible for consumer issues. Doing similar work to these Ministers is not necessarily a bad thing, as more publicity should be given to information about credit cards. In his appearance before this Committee, Mr. Don Blenkarn, M.P., commented on the "Credit Card Costs" paper put out regularly by the Department of Consumer and Corporate Affairs:

> I think the government has gone some way in terms of its disclosure paper that it brings out every quarter, but not nearly far enough. I think the paper is excellent, the study is excellent, but it is kept under a bushel so nobody sees it.

Information is the key issue in the credit card market, as it is in the market for other financial services and, indeed, for most consumer products. Good information on the costs and other terms of credit cards is becoming available, and this Committee (and the Ministers responsible for consumer issues) want to make sure that that information is of use to the average consumer.

EXTENT OF COMPETITION IN THE CREDIT CARD MARKET

Whether a spread between a card rate and the Bank Rate of 7 or 10 percentage points (or any other figure) is "too high" depends in large measure on the extent of competition in the credit card market. The Finance Committee found evidence of a highly competitive market in Canada, with a large number of card issuers competing on the basis of the price and non-price elements of their cards. In addition, there are alternatives to credit card borrowing such as personal lines of credit or specific consumer loans.

Since the time of the Finance Committee Report competition in the credit card market in Canada has, if anything, increased. The number of issuing institutions for MasterCard or Visa has increased from 10 to 13, and there are scores of affiliated institutions offering these cards under their name and independently setting the interest rate and other terms for the card.

More stores now accept the so-called bank cards. By the end of the 1988 bank fiscal year, almost 650,000 merchants accepted these cards—up by over 100,000 from the time the Finance Committee began its study of credit cards. More large retailers now accept bank cards, so the direct competition between bank cards and retail cards has intensified. American Express has introduced a general purpose credit card, Optima, that will compete with the premium or gold cards issued by financial institutions. Royal Bank has taken over the Diner's Club card and is marketing it more aggressively.

Non-price competition has also intensified, especially for the premium cards. Different cards offer different packages of insurance, discounts on hotels and car rentals, rebates and various other attractions. The so-called affinity cards are another new development used by card issuers to increase market share. A graduate of, say, Queen's University may agree to use a certain credit card, and the card issuer will give some money (often a percentage of the purchases made with the card) to Queen's.

Still, some Members of this Committee—and, indeed, Members of the Finance Committee—thought that the similarity of rates among some card issuers indicated ani-competitive behaviour, behaviour that should be investigated by the Bureau of Competition Policy.

There are three sections of the new *Competition Act* would apply to credit card issuers—Section 45 dealing with general conspiracies that would lessen competition, section 49 dealing with agreements among banks and Section 61 dealing with price maintenance.

Section 61 prohibits card issuers from making any agreement, threat or promise that would prevent a merchant from offering a discount for the use of cash. Sections 41 and 49 cover agreements that would keep the terms of cards offered by different issuers at the same level (or at some specified relationship).

To prove conspiracy under the *Competition Act* one needs evidence of an agreement. The Act requires more than price leadership or parallel pricing to constitute an offence. As several witnesses before this Committee pointed out similar prices can also be an indication of competition.

Determining the extent of competition is tricky. There is evidence, however, that the market for credit cards in Canada is highly competitive in terms of the push for market share. There is certainly no evidence that card issuers have agreed among themselves on the interest rates and other terms of credit cards.

DISCLOSURE AND INFORMATION

Pivotal to the credit card issue is the question of information. Is there enough information, available at the right time, for a prospective card holder to choose a card wisely? Many of the recommendations of the Finance

Committee and subsequent work by the Ministers responsible for consumer issues and the Department of Consumer and Corporate Affairs have been aimed at improving the availability, timing and usefulness of information about credit cards.

More can be done. Consumers may be badly informed about products, prices and the existence of lower cost alternatives to what they buy. If consumers are badly informed, they do not put pressure on a market to become more competitive. In some cases, good information may exist but it moves slowly to consumers. Here, too, the market will not be as competitive as it could be.

Similar reasoning in the United States led Congress there to pass legislation that requires better disclosure of credit card costs. It is useful to look at that legislation and then at current practices of Canadian card issuers, using the U.S. law as a frame of reference.

1. Recent U.S. Legislation on Credit Cards

On 3 November 1988, the U.S. Congress passed the *Fair Credit and Charge Card Disclosure Act of 1988* (Public Law 100-583 [H.R. 515] Hereafter FCCCD Act). The law provides detailed and uniform disclosure of rates and other costs of credit cards in applications and solicitations to open credit and charge card accounts. This law gives consumers basic cost information on cards at an earlier time than under the current *Truth in Lending Act* which provides only that consumers receive credit disclosure statements before the first transaction. The FCCCD Act took effect 3 April 1989, but compliance is optional until 31 August 1989 (and 29 November 1989 for one section of the Act). Because of the late compliance dates, there is no useful experience of this law.

Under the new law, card issuers must provide information in three situations:

a. direct mail applications and solicitations,

b. telephone solicitations, and

c. applications and solicitations that are made available to the general public (such as those contained in catalogues, magazines, generally available publications or in applications commonly referred to as "take ones").

Disclosure is also required in two other circumstances:

a. when a renewal notice is sent for those cards that have a renewal fee,

b. when credit insurance is offered by the card issuer and the issuer decides to change insurers.

Most of the information that must be disclosed under this law must be in the form of a table prescribed by the Board of Governors of the Federal Reserve System (see Appendix 6). Note that the Board has regulatory authority with respect to this Act.

The Act requires the disclosure of four cost elements associated with credit cards:

a. annual percentage rate (APR),

b. annual or periodic fees and transaction fees,

c. grace period, and

d. name of the balance calculation method.

The Board of Governors of the Federal Reserve System has identified several methods of calculating the balance as common. A card issuer who uses one of these methods may meet the disclosure requirements by giving the name of the method used; card issuers who use another method not included on the Board's list must provide an explanation of the method used. The following methods have been identified by the Board:

a. Average daily balance
   — including new purchases or
   — excluding new purchases,

b. Two-cycle average daily balance
   — including new purchases or
   — excluding new purchases,

c. Adjusted balance, and

d. Previous balance.

The new law preempts state credit and charge card disclosure laws. As the Board's Press Release with the amendments to Regulation Z (Truth in

Lending) stated: "The preemption of such provisions of state law is total, and differs from other provisions of the TILA [Truth in Lending Act] which generally preempt only inconsistent state laws."

The *Fair Credit and Charge Card Disclosure Act of 1988* is the result of several years of congressional work on the issue of credit cards, work that has in many respects paralleled work done by parliamentary committees in Canada. Congress rejected proposed legislation that would have put a cap on credit card rates and instead worked to improve the disclosure that consumers would receive about the costs associated with credit cards, although some states do have interest rate ceilings. As can be seen from the above sections, the new credit card law does not mandate common methods for pricing by card issuers. Instead, the law attempts to insure that consumers have information at a time that will be useful as they shop for a credit card.

The tables in Appendix 6 are from the Federal Reserve Press Release on Regulation Z (Truth in Lending) which implements the *Fair Credit and Charge Card Disclosure Act of 1988.* Note that the tables designed by card issuers need not be identical to the following, but must be substantially similar.

The standardized table, available with promotional material, gives prospective card holders an excellent way of comparing the terms of various credit cards. There are still problems with the approach, the biggest problem having to do with the naming of the method of calculating interest charges. Here, for example, is the name and description of one method.

> *Two-cycle average daily balance (including new purchases).* This balance is the sum of the average daily balances for two billing cycles. The first balance is for the current billing cycle, and is figured by adding the outstanding balance (including new purchases and deducting payments and credits) for each day in the billing cycle, and then dividing by the number of days in the billing cycle. The second balance is for the preceding billing cycle and is figured in the same way as the first balance.

Keep in mind that for this method, only the name must be given in the standardized table. Whether anyone would understand how interest is calculated from the name alone is a moot point. What research for this Committee has demonstrated is that information about relative nominal rates does not necessarily provide information about relative effective rates.

2. Current Disclosure Practices in Canada

Not surprisingly, perhaps, Canadian card issuers do not use a standardized table to present the costs of using their credit cards. Practices vary widely with respect to what cost information is presented and how it is presented. Of special concern to the Committee was disclosure in applications and promotional material. In other words, the Committee shares the same concerns that led to legislation in the United States.

Because practices vary widely and because there are so many card issuers in Canada, it is probably most useful to highlight the best and the worst practices.

The worst is the stand-alone application that gives no information about the costs of using the card. Some contain such phrases as "the applicant agrees to abide by the terms and conditions of the XYZ Card Agreement accompanying the XYZ Credit Card." Comparison shopping for a credit card is not helped by giving a consumer the terms of a card after he or she has applied for a card and received it.

This worst practice seems to hold for the smaller card issuers, although this generallization does not hold for all the small issuers examined by this Committee. Many large isssuers also have applications without specific cost information on them, but these issuers often have supporting material that explains the use of the card and provides detail on the costs.

The large retailers were quite good about providing information on the costs of their cards, which means the interest rate used and the manner of calculating interest charges. In many cases, the application was part of a promotional brochure. This often contained, in addition to the interest rate used in the calculations, examples of interest charges (and minimum payment requirements) for different levels of purchases.

The large financial institutions also have widely varying practices. The best among them are models of what can be done. The National Bank, for example, has recently included the interest rate on its credit card with the promotional material and application form that it now uses. The Royal Bank does not include the rate with its application, but offers supporting material that gives a phone number for information about its financial services. It also provides an excellent pamphlet—"Straight Talk about Visa"—that now includes sample calculations and an explanation of how interest charges are calculated.

In terms of the U.S. disclosure model, the best example in Canada is the flyer "About Our Credit Cards" that Canada Trust has available with its application forms. On the back of this flyer is a table "About Our

MasterCards'' that provides in large print the terms of the four cards it offers (Appendix 7).

Dr. John Evans, President of the Trust Companies Association of Canada, appeared before the Committee, stressed the importance of information and pointed out that providing good information can give a card issuer a competitive advantage. The work of the Royal Bank and Canada Trust to provide better disclosure is part of an effort by these institutions to increase market share. Nonetheless, the result is better information for the consumer—and a model for other card issuers.

3. Other Sources of Information

It is not only the card issuers, of course, who can provide information about the relative costs of different credit cards. The Finance Committee report and the Background Paper appended to it provided information that was picked up and brought up to date by many commentators.

As mentioned above, the Department of Consumer and Corporate Affairs puts out a regular publication on the costs of credit cards. Recently, that department has also put out a flyer "Choosing a Credit Card—Tips to Remember.'' The Canadian Bankers' Association is also developing a flyer explaining the interest costs of the different types of cards.

The Consumers' Association of Canada has also taken up the issue of credit cards on occasion and has included information on the wise selection and use of cards in its publications. Consumer-oriented columns in newspapers and magazines will at times take up the issue, as will consumer shows on radio or television.

If the card issuers, for some reason, were to try intentionally to keep information about cards unavailable or cloudy, there are other sources. In this case, critics could do more than criticize: they could help solve a perceived problem. Of course, the best solution is for everyone involved to try to provide accurate, timely and useful information for consumers.

PROPOSED LEGISLATION IN CANADA

The concerns expressed in the introduction to this report led two Members of Parliament to table private bills dealing with credit cards. The bills call for a floating cap on credit card rates and for a standardized method of calculating interest charges.

1. Private Member's Bill C-214 on Limitation of Interest Rates and Fees in Relation to Credit Card Accounts

On 10 April 1989, Mr. John Rodriguez, M.P., presented a bill that would provide for a floating cap on credit card rates and a ceiling on any fees associated with credit cards.

According to the bill, the ceiling on rates would float with the average of the weekly Bank Rates from the previous month. The spread between the card rate ceiling and the average Bank Rate will depend on the type of credit card:

(a) Financial card with fees—6.5 percentage points,

(b) Financial card without fees—8.5 percentage points,

(c) Petroleum company card—9.5 percentage points,

(d) Retail company card—11.5 percentage points.

The ceiling for (d) is on unpaid monthly balances exceeding $400. In its brief to this Committee, the Retail Council of Canada pointed out that "it is, in fact, those who are most affluent who tend to maintain higher account balances.'' This is in line with a finding of the Finance Committee:

> A mixture of evidence from the U.S. and Canada suggests that ceilings on credit card rates in Canada would, in the main, benefit well-educated, upper-income card users between 35 and 44 years old with above-average card balances who, for unknown reasons, do not now take advantage of lower-cost alternatives to regular credit card borrowing.

The Finance Committee Report also included a section on the possible effects of interest rate ceilings on credit cards. Three types of ceiling were considered—an absolute limit on the rate, a floating limit and a tiered system of limits. The second and third types are found in Bill C-214. The following are the relevant paragraphs from the Finance Committee Report:

> The suggestion for a floating limit seems more sophisticated and more practical. If the credit card rate were tied to an interest rate that followed the general cycle of interest rates, the limit would appear to be reasonable throughout the interest rate cycle. However, the proposal also has problems.
>
> The most significant problem is in choosing the margin that should be fixed between the reference interest rate and the credit card rate. Choosing the reference rate is also a problem. A witness with the Consumers' Association of Canada suggested that credit card rates be linked to the prime rate, but would not be

pinned down to specifying the margin over prime for card rates. This witness did say that the appropriate level for the credit card rate in early December 1986 would be about equal to the consumer loan rate.

It is far easier to say that credit card rates should float with short-term interest rates than it is to specify the margin that would link the credit card rate to the chosen reference rate. The argument for legislating a floating ceiling on credit card rates presumes that credit card operations produce excess profits—that current interest rates on credit cards are too high. The floating ceiling, according to this view, merely eliminates the excess profits. Again, this seems simple, but the problem comes in trying to determine the precise amount of the excess profits so that the precise margin for the floating ceiling can be set.

Because of the variance in interest rates on credit cards, a floating ceiling would not affect all card issuers equally. A truly equitable policy would control not only interest rates but also any fees and the length of the grace period. Although superficially equitable, such policy could destroy much of the choice consumers now enjoy with respect to differently priced credit cards.

Another reason for not restricting the rate on credit cards to some margin above a reference short-term interest rate is that profits on credit card operations are cyclical. If the configuration of rate, fees and grace period were chosen to eliminate excess profits in one year, the card issuers might still suffer losses in other years. As seen above, the relatively high returns on card operations in 1985 offset to some extent the losses in 1981. In other words, one needs to know how interest rates, other operating costs and credit card use vary over the cycle to choose the correct margin.

The third type of restriction on credit card rates is a tiered system of rates with those with larger outstanding balances paying a lower rate of interest than those with lower outstanding balances. The rationale for this system is the nature of the fixed costs per account. Interest charges (and fees, if any) cover these fixed costs and the cost of funds. Those with large outstanding balances pay high interest charges that should easily cover the fixed costs for the account and probably cover the fixed costs for those with low (or zero) outstanding balances. It might seem fair, therefore, to have those with high balances pay lower interest charges, so they are not subsidizing other card users.

One of the witnesses before the Committee said that it had experimented with a tiered system of rates, but its customers objected to the system, claiming that the issuer was trying to tempt its card holders into running up larger bills. The experiment was discontinued because of the bad public relations involved. On the other hand, Canada Trust offers tiered rates on one of its premium cards—16.5% on balances below $2,500 and 13.5% on balances above $2,500. Several card issuers in the U.S. also offer tiered rates. There are, however, problems with tiering interest rates for different categories of card user. The main problem is the same as for the other restrictions on rates, namely that the information needed to set the tiers is difficult to determine. One would need to know the fixed costs per account and this is difficult to calculate as it involves allocating overhead to credit card operations and then to separate accounts. Different card issuers will have different accounting procedures; a tiered system that seems fair for the holders of one card may seem unfair to the holders of other cards.

How Canadians would be affected by rate ceilings would depend on how card issuers react to the ceilings and on the characteristics of card users. Those who do not now have a credit card and those who will never have a credit card could also be affected by interest rate ceilings.

All card issuers would probably react to ceilings with measures aimed at maintaining profits. Such measures would include:

(1) introducing or increasing annual or transaction fees;

(2) shortening or eliminating the grace period;

(3) using a new method for calculating the interest-bearing balance;

(4) improving the quality of credit card loans by

(a) ending the issue of new cards,

(b) taking back some cards (for example, those with delinquent accounts),

(c) lowering credit limits;

(5) linking credit card use to other services and increasing the price of these services;

(6) increasing merchant discounts; and

(7) (for those issuers selling goods and services) raising other prices.

This list is based on the background paper by Desbois and Thomas [appended to the Finance Committee Report] and a recent study by the Board of Governors of the Federal Reserve System in the U.S. (G.B. Canner and J.T. Fergus, "The Economic Effects of Proposed Ceilings on Credit Card Interest Rates", /Federal Reserve Bulletin/, January 1987).

The Federal Reserve paper examined relevant studies on consumer credit restrictions in the U.S. and consumer surveys carried out during the past two decades by researchers at the University of Michigan. The Federal Reserve study concluded that reactions to ceilings would erode the benefits of ceilings to credit card borrowers and impose costs on other consumers. Among the other consumers, those with lower incomes would be most affected.

The extent of the reaction to a rate ceiling, of course, depends on the level of the ceiling or, with a floating ceiling, on the spread between a reference rate and the card rate. Unfortunately, there is no accurate guide for determining the ideal ceiling or spread.

When the business editor of the Ottawa *Sun* appeared before the Committee, she left five binders with 458 responses to a *Sun* write-in campaign on credit cards. Fifty-four responses, or almost 12%, wanted government regulation. Eleven wanted controls or regulations, but did not specify them. Of the rest, 15 wanted rates fixed at a particular level, and 28 wanted a floating cap on rates. There was no agreement, however, on what the fixed rate should be—suggested rates of 10, 13, 15 and 18% were given.

There was also no agreement on a floating cap. Some wanted credit card rates limited to the level of the Bank Rate, the personal lending rate, an unspecified bank loan rate or the prime rate. Others wanted a margin over prime of 1 1/2, 2, 3, 4 or 5 percentage points; still others wanted a margin over the Bank Rate of 2, 3 or 5 percentage points.

2. Private Member's Bill C-238 on Calculation of Credit Card Interest Charges

On 8 May 1989, Mr. Don Blenkarn, M.P., presented a bill that would amend the *Interest Act* and regulate the calculation of interest charges on credit cards.

The bill would make all card issuers use the same method for calculating interest charges—interest charges would be calculated monthly, unpaid interest would be subject to interest itself and all interest calculations would be made from the statement date. (The bill refers to interest calculations being made from the due date, but the context suggests that this means the statement date.) The mandated method would be similar to the method now used by retailers; the method is quite different from that used by financial institutions, namely the calculation of credit card interest charges on the basis of daily balances.

The bill would provide a grace period during which no interest is charged for all purchases. The minimum grace period would be from the date of purchase to the statement date. If purchases are distributed evenly through the month, the average additional grace period is 15 days for those with outstanding balances. Currently, those with outstanding balances on bank cards who do not pay their account in full by the end of the grace period are charged interest from the date of purchase.

The bill is consistent with a recommendation in the 1987 report by the Finance Committee on credit cards in Canada:

> That the Minister of Finance work with the relevant provincial ministers to put into force legislation requiring all credit card issuers to calculate interest-bearing balances by a common method. The method should be uniform, allow a grace period for new purchases (to ensure that payments are credited first to any interest-bearing balance), recognize the timing of payments (so being late a day on a payment does not lead to interest charges for an entire month) and allow that any partial payment lower the interest-bearing balance.

The argument for mandating a common method of interest calculation for all credit card issuers is that a common method would enable consumers to compare the effective interest rate on different cards. As the News Release issued on the day Mr. Blenkarn presented his bill put it: "Thus one bank's 15% may be another bank's 20%." The intent of Bill C-238 is to ensure that the apparent difference between posted interest rates is not simply an artifact of the way interest balances are calculated. According to the News Release: "Mr. Blenkarn's amendment to the *Interest Act* sets the measuring stick by which Canadians may compare interest rates. The amendment creates one standard making interest rate calculation understandable to all, and thus giving financial institutions an incentive to have competitive rates."

There are several possible problems with Mr. Blenkarn's private bill. Among the problems are:

(a) The effective price of a credit card includes several elements in addition to the rate of interest. These other elements include annual (or monthly) fees and transaction fees. Cards with different interest rates (but the same method of calculating the interest-bearing balance) could have the same effective price, while cards with the same rates could have different effective prices.

(b) Within card-issuing groups—for example, financial institutions as a group or retailers as a group—the method of calculating the interest-bearing balance tends to be uniform.

(c) By restricting card issuers to one method of calculating interest balances, the bill removes some consumer choice. Consumers may now recognize the differences between cards issued by different types of card issuers and choose their cards accordingly.

(d) Restricting the way card issuers can price their cards could arrest the evolution of credit cards—for example, the move towards a debit card. Some groups may, of course, now oppose any move towards replacing charge cards with debit cards, but this is something the market (meaning all potential users of the cards) should decide. Rigid legislation would affect all future innovations, including innovations that are not now foreseen.

(e) The restrictions in the bill would be extremely costly to financial institutions that now use a daily balance method for calculating interest charges. The response of the affected institutions would probably be to increase interest rates, shorten grace periods, add or increase fees and eliminate the marginal card user (the one whose current expected revenue just matches the cost to the institution of that individual's card). It should be noted that the marginal user is often the consumer with low income.

(f) Treating financial institutions the same as retailers neglects the fact that retailers can adjust the price of their products to counter any changes in the return on their credit card operations, while financial institutions cannot.

(g) Many consumers now have daily interest deposit accounts. The extension of the grace period would enable some wise consumers to collect interest from a financial institution while that institution finances a purchase made by the consumer.

(h) There are possible federal/provincial conflicts.

IS THERE TOO MUCH CREDIT CARD LENDING?

During the hearings in June several Members of the Committee noted that they were swamped with applications for credit cards, especially when they visited major retailers. They wondered whether such marketing practices led to too much credit card lending and, eventually, to financial problems and possible bankruptcy for their constituents.

Bankruptcy is a tricky issue, one that the Committee may examine in more detail in the future. It is, of course, impossible to provide a precise figure for the acceptable level of bankruptcies. For now, it is enough to point out that in an economy where credit is readily available and where future trends of income and employment are not known with certainty, bankruptcies will occur.

This Report addresses two related questions. What is the link between credit card borrowing and bankruptcy? Do credit card issuers lend money too easily?

For the first question, the Superintendent of Bankruptcy has produced some relevant data from a random sample of personal bankruptcies in a six month period over 1988-89. Surprisingly, as the table in Appendix 8 shows, over 40% of bankruptcies did not involve credit card lending.

Those with cards owed, on average, $4,588 on the general purpose cards and $1,965 on the specific purpose cards. There is probably considerable overlap among the two groups of cardholders. If the overlap were as extensive as it could be the average card debt for a bankrupt would be about $6,400. Based on some rough adjustments to data provided in the Finance Committee Report we can say that this is about four times the level of debt of the average card user with debt.

We must be cautious, however, when interpreting this finding. The average card-using bankrupt has a relatively large amount of credit card debt. But at the time of bankruptcy credit card lending may have been the only type of lending available to the individual—credit card debt ballooned near the time of the bankruptcy, but this was a result, not necessarily a cause, of financial distress.

The second caution is that there may have been some intentional misuse of credit card borrowing by persons who were going bankrupt. Again, this would inflate the figure for credit card borrowing but would not mean that such borrowing was the cause of bankruptcy. In this case, it is the option of bankruptcy—an option eventually taken—that led to the borrowing.

The third caution is that credit card borrowing was not the major type of borrowing by those who went bankrupt. Total liabilities of those with general purpose cards was $31,984; total liabilities of those with the specific use cards was $29,987. Credit card liabilities are thus about a fifth of total liabilities. (The random sample included one unusual personal bankruptcy—total liabilities of $703,132—that increased the average total liabilities by 4 to 5% but does not affect the general conclusion that credit card borrowing was about a fifth of total liabilities.)

One might argue that credit card borrowing was the straw that broke the camel's back. But it seems more likely that the figures show a general problem with all types of credit—or an unexpected fall in income.

The second question is related. Do credit card issuers lend money too readily? Evidence presented to the Committee suggests that the answer is no. The first piece of evidence concerns the credit requirements of those issuing cards. Retailers appearing before the Committee stated that they reject 40% of all card applications and try to keep bad debt below 2% of outstanding balances.

The Canadian Banker's Association did not present evidence on the proportion of applications rejected, but the table of statistics on MasterCard and Visa they included in their brief showed delinquent accounts at 0.7% of outstanding balances. Fraud pushes the bad debt proportion up slightly, but it is still below 1%. This is about half the typical bad debt ratio found on bank cards in the U.S. There is some anecdotal evidence that U.S. banks that mail out cards indiscriminately have loan losses in the order of 5%.

Canadian card issuers appear reasonably prudent in managing credit risk. If there is too much credit card lending, therefore, it would be because interest rates on credit cards are too low—an argument never raised before a Parliamentary Committee.

The tentative finding of this Committee is that credit card lending is not a major cause of bankruptcy. However, unwise credit card borrowing, together with the unwise use of credit in general, can lead to financial hardship. Consumers would obviously be better off with more education about the wise use of all credit.

WHAT SHOULD THE CONSUMER DO?

Up to this point, the emphasis has been on finding a way to improve the information provided by card issuers (or third parties such as the Department of Consumer and Corporate Affairs). This emphasis is probably reasonable. After all, if the consumer is to make a wise choice of a credit card or use cards wisely, the consumer must have information about the relative costs of different cards.

The information must be available, timely and in a form that is useful to the average consumer. Previous recommendations have in the main been directed at improving the disclosure of information and thus the competitiveness of the credit card market.

Consumers also have a role to play in improving the competitiveness of this market. If consumers complain about the high cost of credit cards—and they do—they must be willing to act on information that would show them the relative costs of using different cards.

Even now, when information is far from ideal, some consumers do respond to relative costs. Almost 10% of the respondents to the Ottawa *Sun*'s write-in campaign, for example, said that they were cutting up some of their cards or not using them (and relying on cash, credit cards with lower rates or substitutes for credit card lending). Most saw their action as a protest against high rates and not as a simple choice among alternative ways of paying for a purchase.

Consumers really face two choices. Should they use any source of credit? If they rely on credit cards as a source of credit, what is the best card to use?

There is, unfortunately, no single answer to the question of which is the best card. The flyer "Choosing a Credit Card—Tips to Remember" put out by the Department of Consumer and Corporate Affairs offers some excellent advice:

> Identifying the lowest cost credit card is not easy. It is not enough just to compare interest rates. How interest charges are calculated can be as important as the interest rate itself.
>
> The following tips may save you money:
>
> Compare
>
> - Interest rates
> - Number of days given to pay in full before interest is charged (grace period)
> - How interest charges are calculated (from date of purchase or date of statement)
> - Non-interest charges such as transaction charges or annual fees
> - Other benefits such as convenience or discounts
>
> Consider
>
> - If you regularly pay your balance in full before the due date, consider all non-interest charges.
> - If you regularly pay your balance within a few months, find out how the interest is calculated. A credit card that calculates interest from the statement date may cost you less than one that calculates it from the date of purchase—regardless of the interest rate.
> - If you take a long time to pay your balance, use a card with a low interest rate.
>
> Remember
>
> The four major groups of cards offer different features ... Check with card issuers directly for the details respecting any particular card.

This is obviously good advice and it would be easier to take if all the costs of using a credit card were readily available.

Before deciding which credit card to use, however, the wise consumer will question the credit choice. The Canadian Bankers' Association puts out a useful pamphlet, "Credit Wise: A Guide to Consumer Credit." This guide discusses the pros and cons of using credit and provides some excellent advice:

> ... you should also take into account that using credit to obtain immediate use of goods and services for which you do not have the cash may result in your having trouble keeping up with credit payments later. Using credit may make it easier for you to buy on impulse, which can play havoc with your finances. Taking advantage of special sales and bargains may end up costing you more in interest charges later than you saved by buying at the reduced price. The convenience of credit may lead you to forget to keep track of what you owe until the monthly statement arrives. If you do not stick to your budget, keeping track of your credit purchases will not be of much help.

The overriding goal of this Committee is to improve the well-being of Canadian consumers. A wiser use of credit would certainly be a step towards improved well-being or, from another viewpoint, towards reduced financial hardship.

The wise use of credit depends on the use of information. Some of this information is personal, dealing, for example, with expected wages and salaries in the near future. Some information is objective such as the relative costs of different credit cards. This report has by necessity focused on the objective information and sought ways to improve it.

But information is costly to produce. If it is not used, or if it is presented in ways that are not useful, the costs will exceed the benefits. The finding that more information is needed cannot go unqualified. Along with being available, information must be timely and understandable.

Consumers, and any groups or individuals representing them, must take an active part in the process. Information on credit cards is part of a large set of information on credit and other economic variables. All such information fits in with the continuing education of consumers and, with this, their improved well-being.

RECOMMENDATIONS

The following recommendations are meant to refer to all cards issued in Canada, both charge cards and credit cards. An example of the range of cards considered can be found in the publication "Credit Card Costs" put out on a regular basis by the Department of Consumer and Corporate Affairs.

The recommendations, of course, are not limited to the cards specified in that publication.

1. **That the Department of Consumer and Corporate Affairs commission follow-up studies to determine the extent of the circulation of material they produce on credit cards and the effectiveness of this material, and that the results of these studies be made available to this Committee.**

2. **That credit card issuers provide full disclosure with applications and any promotional material of the specific costs of using their cards before cards are issued.**

   The information shall include, but shall not be limited to, the annual interest rate, any relevant component of this rate (such as daily or monthly rate), the length of the grace period, any fees, the point at which interest charges begin (purchase date, statement date or other), any specific treatment of partial payments and any special treatment of certain transactions (for example, cash advances). This material shall be put in a standardized table, perhaps similar to the one now used by Canada Trust (see Appendix 7).

3. **That all card issuers be required to provide to all card holders a copy of this table annually.**

4. **That the card issuer be required to provide to any consumer who applies for a credit card the standardized table set out in recommendation 2 no later than with the issuance of the card.**

5. **That card issuers give card holders at least 30 days notice of renewal, disclosing the costs and the card holder's right to cancel.**

6. **That credit card issuers be compelled to calculate interest charges in a manner which fully credits any partial payment by the credit card holder.**

7. **That card issuers should prominently display on applications, promotional material and statements a toll-free telephone number for further information about the terms of their cards.**

8. **That the Department of Consumer and Corporate Affairs add to its regular publication "Credit Card Costs" a chart showing consumers, in an historical context, the spread between representative credit card rates (MasterCard, Visa and a retail rate) and the Bank rate (see Appendix 2 in this report for an example).**

9. That in no instance should the spread between card rates and the Bank Rate exceed 8% for financial cards and 16 ½% for retail cards.

10. That the Department of Consumer and Corporate Affairs, with related departments at the provincial and territorial levels and with organizations such as the Consumers' Association of Canada and the Canadian Bankers' Association, increase their efforts to educate consumers about the effective costs of using different types of credit cards.

11. That the Department of Consumer and Corporate Affairs work with the provincial and territorial departments responsible for consumer issues to ensure the widest circulation possible of information on the costs and wise use of credit cards.

12. That the Department of Consumer and Corporate Affairs work with the provincial and territorial departments responsible for consumer issues to prohibit retailers from requiring customers to present a valid credit card as a form of identification or as a prerequisite to obtaining a good or service.

13. That a signature of a card holder or his or her delegate be required to validate a transaction.

APPENDIX 1

MASTERCARD AND VISA STATISTICS, 1977-88

Source: Canadian Bankers' Association

Date Year end:	Number of Cards in Circulation (Millions) (2)	Dollar Sales (Billions)	Outstanding Dollars (Billions) (1)	Gross Dollar Volume (Billions) (2)(4)	Sales Slips Processed (Millions) (2)	Average Sale	Delinquency 90 days & over (3)	# of Cards Reported Lost or Stolen (2)	# of Cards Fraudulently used (2)	$ Amount of Fraudulent Accts.Written off (Millions) (2)	Merchant Outlets (5)	Visa/MC issuing Institutions Represented (6)
77/09/31	8.18	3.61	1.38	4.04	118.82	30.46	1.3	-	-	-	271,150	-
78/09/31	8.99	4.90	1.84	5.44	150.76	32.50	1.3	-	_	_	290,692	_
79/09/31	9.85	6.64	2.35	7.32	185.83	35.72	1.2	-	-	-	322,115	-
80/09/31	10.76	8.82	2.87	9.44	218.42	39.47	1.3	-	-	-	347,845	-
81/09/31	11.98	10.59	3.40	11.51	249.64	42.43	1.0	-	-	-	371,831	-
82/10/31	11.58	13.83	3.72	13.38	274.90	50.30	1.7	259,028	-	15.88	382,206	-
83/10/31	12.13	14.84	3.73	14.85	297.55	49.88	0.9	275,754	19,200	17.39	419,610	10
84/10/31	13.05	16.92	4.42	17.10	325.16	52.05	0.7	299,152	21,332	16.79	442,928	10
85/10/31	13.97	19.35	5.06	20.42	372.91	51.90	0.7	330,380	21,026	17.54	527,042	10
86/10/31	15.50	23.01	5.76	23.57	417.21	55.15	0.8	378,239	22,326	18.61	571,771	10
87/10/31	17.62	26.37	6.76	26.90	450.65	56.79	0.7	408,571	23,913	15.78	642,429	12
88/10/31	19.40	30.33	7.84	31.20	489.96	60.21	0.7	460,348	25,773	15.63	646,844	13

SOURCE: THE CANADIAN BANKERS' ASSOCIATION 02-Oct-89

(1) As at last day of year end. Not necessarily interest bearing.

(2) Reported total to year end.

(3) Percentage of outstandings as at year end.

(4) Equals total of dollar (retail) sales volume and cash advance volume.

(5) Merchants accepting VISA and/or MasterCard. Duplication may occur as merchants accepting both cards have been reported by each plan.

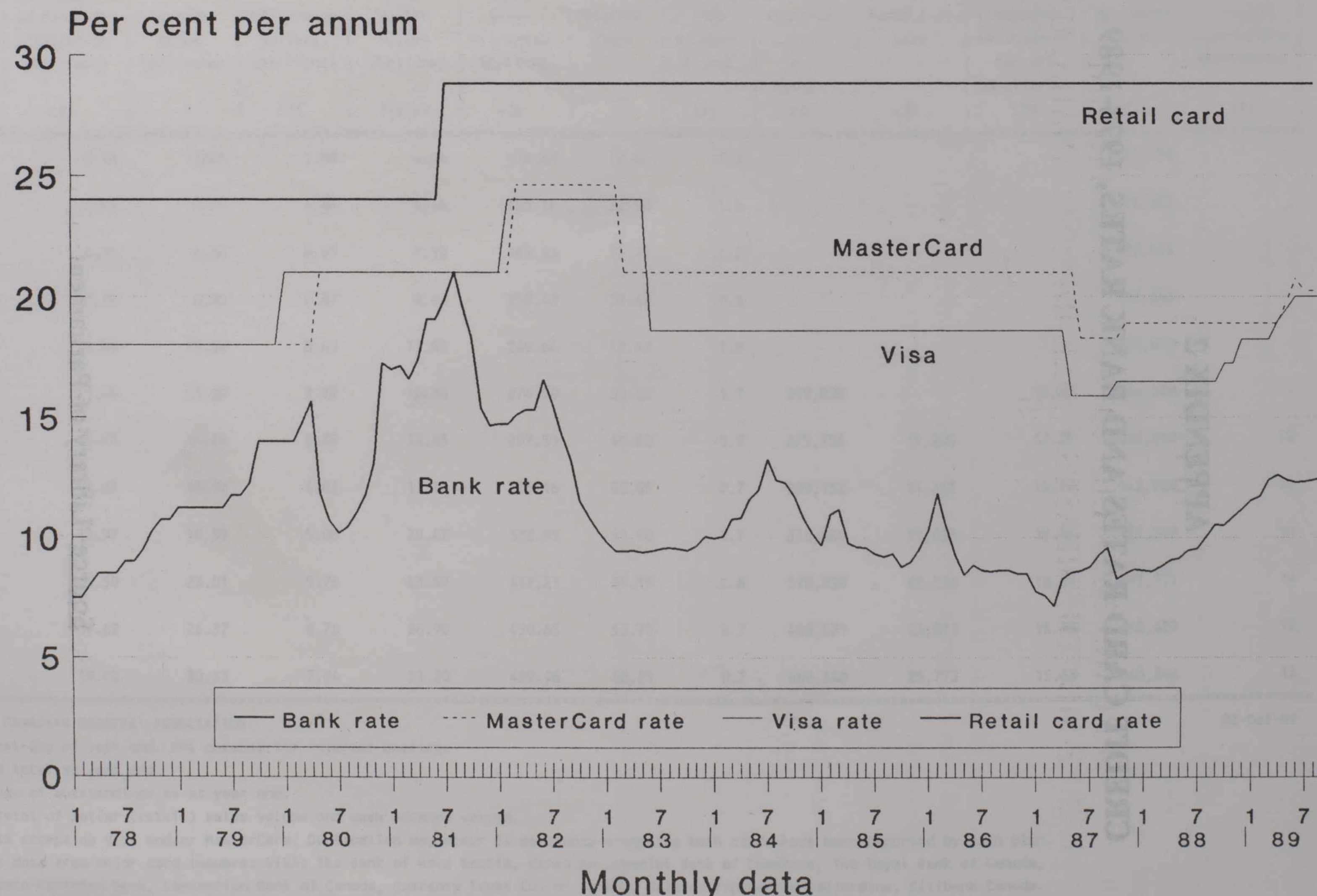
(6) Includes data from major card issuers: VISA: The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, The Royal Bank of Canada, The Toronto-Dominion Bank, Laurentian Bank of Canada, Guaranty Trust Co. of Canada, Caisses Populaires Desjardins, Citibank Canada. MASTERCARD: Bank of Montreal, National Bank of Canada, The Canada Trust [illegible]. Credit Union Electronic Services Inc. (CUETS), Royal Trust Corp.

APPENDIX 2

CREDIT CARD RATES AND BANK RATES, 1978-1989

Source: Library of Parliament

Representative Credit Card Rates
versus the Bank Rate



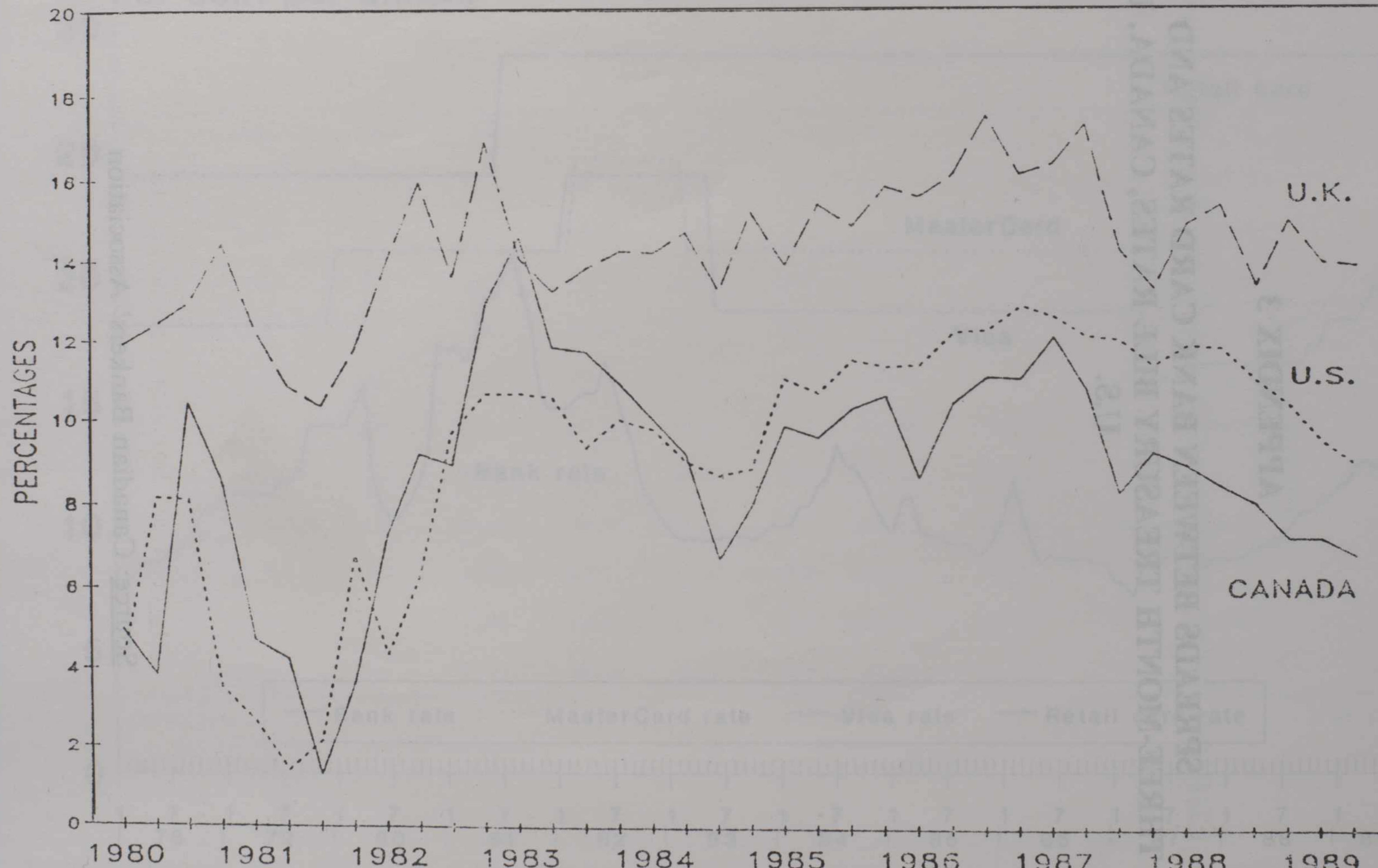
Source: Library of Parliament (Research Branch).

APPENDIX 3

SPREADS BETWEEN BANK CARD RATES AND THREE-MONTH TREASURY BILL RATES, CANADA, U.K., U.S.

Source: Canadian Bankers' Association

SPREAD - BANK CARDS VS THREE-MONTH T-BILLS
CANADA, U. K. & U. S.



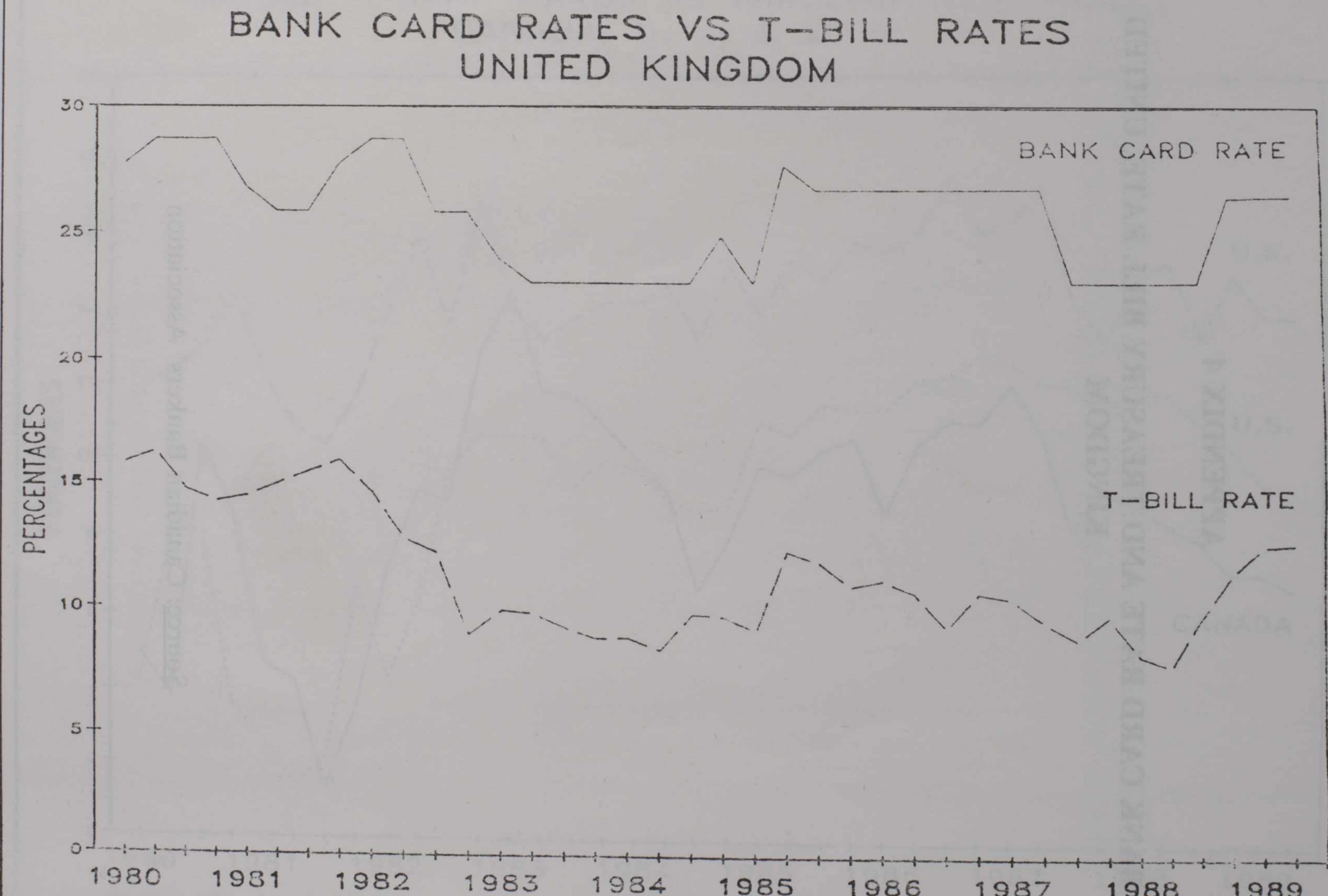
Source: Canadian Bankers' Association.

Source: CBA & FRB

APPENDIX 4

BANK CARD RATE AND TREASURY BILL RATE, UNITED KINGDOM

Source: Canadian Bankers' Association



Source: Canadian Bankers' Association.

DB238

APPENDIX 5

INTEREST RATES, COSTS AND OTHER TERMS OF CREDIT CARDS IN CANADA

Source: Consumer and Corporate Affairs, "Credit Card Costs—September 1989."

CREDIT CARDS -- BANKS, TRUST COMPANIES, CREDIT UNIONS

Interest is calculated on a daily interest basis and payments immediately reduce the daily balance that is subject to interest. Interest is payable on the full daily balances up to the date of payment in full. Exceptions are the Bank of Nova Scotia and the Toronto-Dominion Bank which charge interest only up to the date of the most recent statement - when the balance is paid in full.

For the amounts of merchandise purchases included for the first time in the monthly statement balance, no interest is charged if the full balance is paid within the grace period. There is no grace period on cash advances.

September 1989	Fees ($ annual)	Interest Rates (% annual)	Grace Period (days)	Interest Calculated from	
				Date of Purchase	Date of Statement
MasterCard					
Bank of Montreal	--	20.25	21	X	
Canada Trust	12*	19.75	15		X
Canada Trust Supercharge	--	16.4	0		X
CS CO-OP	--	20.25	21	X	
National Bank	--	20.25	21	X	
National Trust	--	18.9	21	X	
VISA					
Bank of Nova Scotia	12*	20.0	21	X	
Can. Imp. Bank of Commerce	6*	20.0	21	X	
Central Guaranty	--	20.25	21	X	
Centre Desjardins	12	20.25	21	X	
Laurentian Bank	12	18.9	21	X	
Royal Bank	12*	20.0	21	X	
Toronto Dominion Bank	6	20.0	21	X	
Vancouver City Savings	6*	20.0	21	X	

* Lower fees may apply.

OTHER CREDIT CARDS

September 1989	Fees ($ annual)	Interest Rates (% annual)	Grace Period (days)	Interest Calculated from: Date of Purchase	Date of Statement
Canadian Tire	-	28.8	30		X
Eaton's	-	28.8	30		X
en Route	30	22.0	30		X
Home Hardware	-	28.8	30		X
Hudson's Bay	-	28.8	30		X
Petro Canada	-	21	25		X
Sears	-	28.8	30		X
Simpsons	-	28.8	30		X
Sunoco	-	24	25	X	
Ultramar	-	24	21		X
Woodward's	-	26.4	30		X
Zellers	-	28.8	30		X

Except for Canadian Tire and Home Hardware, retail stores subtract payments equal to or exceeding 50 percent of the monthly statement balance before calculating interest charges. Home Hardware calculates interest charges on either the month-end statement balance (minus any payments) or on a daily basis depending on whether purchases are paid off within the first month or over a longer period.

In Quebec, interest is calculated on a daily basis, which means that all payments reduce, as of the date of payment, the balance that is subject to interest.

CHARGE CARDS

September 1989	Fees ($ annual)	Late Penalty Rates (% annual)	Grace Period (days)	Late Penalty Calculated from: Date of Purchase	Date of Statement
American Express	55	30	45		N.A.
Diner's Club	55	24	30		N.A.
Esso Petroleum of Canada	-	24	30		X
Husky Oil Ltd.	-	18	25		X
Irving Oil	-	24	25		X
Shell Can. Products Ltd.	-	24	25		X
Texaco Canada Inc.	-	24	25		X

Husky Oil calculates late penalties on the month-end balance, while Irving, Shell and Texaco calculate penalties on a daily basis. American Express and Diner's Club levy penalties on past due balances at intervals beginning a specified number of days after the statement date.

APPENDIX 6

POSSIBLE STANDARDIZED TABLES FOR THE DISCLOSURE OF CREDIT CARD COSTS UNDER U.S. LAW

Source: Board of Governors, Federal Reserve System. Press Release (Final amendments to Regulation Z implementing the Fair Credit and Charge Card Disclosure Act), 4 April 1989.

G-10(A) -- Applications and Solicitations Model Form (Credit Cards)

Annual percentage rate for purchases	______%
Variable rate information	Your annual percentage rate may vary. The rate is determined by (*explanation*).
Grace period for repayment of balances for purchases	You have [__ days] [until _____] [not less than __ days] [between __ and __ days] [__ days on average] to repay your balance [for purchases] before a finance charge on purchases will be imposed. [You have no grace period in which to repay your balance for purchases before a finance charge will be imposed.]
Method of computing the balance for purchases	
Annual fees	[[Annual] [Membership] fee: $_____ per year] [(*type of fee*): $_ ___ per year] [(*type of fee*): $_________]
Minimum finance charge	$_____
Transaction fee for purchases	[$_____] [__% of _____]
Transaction fee for cash advances, and fees for paying late or exceeding the credit limit	Transaction fee for cash advances: [$_____] [__% of _____] Late payment fee: [$_____] [__% of _____] Over-the-credit-limit fee: $_____

G-10(B) -- Applications and Solicitations Model Form (Credit Cards)

Annual percentage rate for purchases	Variable rate information	Grace period for repayment of the balance for purchases	Method of computing the balance for purchases	Annual fees	Minimum finance charge	Transaction fee for purchases
____%	Your annual percentage rate may vary. The rate is determined by (*explanation*).	[__ days] [Until ______] [Not less than __ days] [Between __ and __ days] [__ days on average] [None]		[Annual fee: $____ per year] [Membership fee: $____ per year] [(*type of fee*): $____ per year] [(*type of fee*): $_____]	$____	[$____] [__% of ____]

Transaction fee for cash advances: [$_____] [__% of ____] Late payment fee: [$_____] [__% of ____]

Over-the-credit-limit fee: $_____

G-10(C) -- Applications and Solicitations Model Form (Charge Cards)

Annual fees	Transaction fee for purchases	Transaction fee for cash advances, and fees for paying late or exceeding the credit limit
[Annual fee: $____ per year] [Membership fee: $____ per year] [(*type of fee*): $____ per year] [(*type of fee*): $____]	[$____] [__% of ____]	Transaction fee for cash advances: [$____] [__% of ____] Late payment fee: [$____] [__% of ____] Over-the-credit-limit fee: $____
All charges made on this charge card are due and payable when you receive your periodic statement.		

APPENDIX 7

CANADA TRUST PROMOTIONAL SHEET: "ABOUT OUR MASTERCARDS"

Source: Canada Trust

ABOUT OUR MASTERCARDS

FEATURES	SuperCard MasterCard	SuperCharge MasterCard*	SuperGold MasterCard	U.S. Dollar MasterCard
Cash advances at over 31,000 money machines	✓	✓	✓	
Money machine access to selected CT accounts	✓	✓	✓	
Overdraft protection for CT chequing accounts	✓	✓	✓	
Guaranteed cheque cashing	✓	✓	✓	
Tilden car rental discount	✓	✓	✓	
50% off room rates at participating hotels**	✓	✓	✓	
Travel accident insurance coverage	up to $100,000	up to $100,000	up to $400,000	up to $100,000
5% discount on vacation packages			✓	
Toll-free travel arrangements			✓	
Guaranteed lowest airfare			✓	
Best airline route search			✓	
1/2 price trip cancellation insurance			✓	
Emergency cash/ ticket replacement			✓	
Exotic excursion offers			✓	
Villas of the World vacation option			✓	
Wine Club option			✓	
Toll-free customer hotline			✓	
Fees	$1/month reduced by any interest charges	none	$60 annual	$1 U.S./month reduced by any interest charges
Minimum credit line	$1,000	$1,000	$5,000	$1,000
Annual interest rate	19.75%	16.4%	16.5% ***	19.75%
Interest on special cheques/cash advances	Special cheques: From date transaction is recorded on your MasterCard account; Cash advances: From date obtained			
Interest on merchandise purchases	From date statement issued, if balance not paid in full by due date	From date statement issued	From date statement issued, if balance not paid in full by due date	From date statement issued, if balance not paid in full by due date
Payment due (after statement issue)	15 days	25 days	22 days	15 days

*Not available in Quebec
**With Tilden Car Rental, Oct. 15 to April 30, annually
***19.75% on balances less than $2500; effective June 1989

Canada Trust

09-258 (0589)

APPENDIX 8

CREDIT CARDS AND BANKRUPTCY

Source: Superintendent of Bankruptcy

Percentage of Bankrupts Holding Credit Cards

	General Use	Specific Use
no card	42%	46%
1 card	33	23
2 cards	16	16
3 or more cards	9	15

Source: Superintendent of Bankruptcy. The sample consisted of 856 non-business files. The General Use category includes bank cards and travel and entertainment cards; the Specific Use category includes the retail and oil company card.

REQUEST FOR GOVERNMENT RESPONSE

Your Committee requests that the Government table a comprehensive response to this Report in accordance with the provisions of Standing Order 109.

A copy of the relevant Minutes of Proceedings and Evidence (*Issues Nos. 12, 13, 14, 15, 19, 20, 23 and 24 which includes this Report*) is tabled.

Respectfully submitted,

GARTH TURNER,
Chairman

MINUTES OF PROCEEDINGS

WEDNESDAY, OCTOBER 25, 1989
(26)

[*Text*]

The Standing Committee on Consumer and Corporate Affairs and Government Operations met *in camera* at 4:11 o'clock p.m. this day, in Room 306 West Block, the Chairman, Garth Turner, presiding.

Members of the Committee present: Don Boudria, Gilbert Chartrand, John Cole, Louise Feltham, Jean-Marc Robitaille, John Rodriguez, Len Taylor, Garth Turner and Brian White.

Acting Members present: Nic Leblanc for Gabriel Larrivée; Darryl Gray for Peter L. McCreath.

In attendance: *From the Research Branch of the Library of Parliament*: Terrence J. Thomas, Economics Division, Research Officer.

It was agreed,—That the Chairman undertake the usual consultations to seek an order of the House authorizing the Committee to hold meetings throughout Canada in relation to its review of Canada's postal service for three weeks during the period of January 29 to March 9, 1990.

The Committee resumed its examination of the evolving role of credit cards in the Canadian economy. (*See Minutes of Proceedings, Monday, June 12, 1989, Issue No. 12*).

The Committee resumed consideration of the Draft Report to the House.

At 5:46 o'clock p.m., the Committee adjourned to the call of the Chair.

THURSDAY, OCTOBER 26, 1989
(27)

The Standing Committee on Consumer and Corporate Affairs and Government Operations met *in camera* at 11:08 o'clock a.m. this day, in Room 306 West Block, the Chairman, Garth Turner, presiding.

Members of the Committee present: Don Boudria, Gilbert Chartrand, John Cole, Louise Feltham, Gabriel Larrivée, Jean-Marc Robitaille, John Rodriguez, Roger Simmons, Len Taylor, Garth Turner.

Acting Member present: Mark Assad for Jean-Robert Gauthier.

In attendance: *From the Research Branch of the Library of Parliament*: Terrence J. Thomas, Economics Division, Research Officer.

The Committee resumed its examination of the evolving role of credit cards in the Canadian economy. (*See Minutes of Proceedings, Monday, June 12, 1989, Issue No. 12*).

The Committee resumed consideration of the Draft Report to the House.

At 11:55 o'clock a.m., the Committee adjourned until 3:30 o'clock p.m. this day.

AFTERNOON SITTING
(28)

The Standing Committee on Consumer and Corporate Affairs and Government Operations met *in camera* at 3.37 o'clock p.m. this day, in Room 701, 151 Sparks Street, the Chairman, Garth Turner, presiding.

Members of the Committee present: Don Boudria, Gilbert Chartrand, John Cole, Louise Feltham, Gabriel Larrivée, Jean-Marc Robitaille, John Rodriguez, Roger Simmons, Len Taylor, Garth Turner.

Acting Member present: Mark Assad for Jean-Robert Gauthier.

In attendance: *From the Research Branch of the Library of Parliament*: Terrence J. Thomas, Economics Division, Research Officer.

*The Committee resumed its examination of the evolving role of credit cards in the Canadian economy. (*See Minutes of Proceedings , Monday, June 12, 1989, Issue No. 12*).*

The Committee resumed consideration of the Draft Report to the House.

It is agreed,—That the Committee request a comprehensive response from the Government.

It is agreed,—That the Draft Report, as amended, be concurred in.

It is agreed,—That the Draft Report, as amended, be the Committee's Report to the House.

It is ordered,—That the Chairman present the Report to the House.

At 6:58 o'clock p.m., the Committee adjourned to the call of the Chair.

Bernard Fournier
Clerk of the Committee

Membres du Comité présents: Don Boudria, Gilbert Chartrand, John Cole, Louise Feltham, Gabriel Larrivée, Jean-Marc Robitaille, John Rodriguez, Roger Simmons, Len Taylor et Garth Turner.

Membre suppléant présent: Mark Assad remplace Jean-Robert Gauthier.

Aussi présent: Du Service de recherche de la Bibliothèque du Parlement: Terrence J. Thomas, attaché de recherche.

Le Comité poursuit l'étude de l'évolution du rôle des cartes de crédit dans l'économie canadienne. (*Voir Procès-verbaux du lundi 12 juin 1989, fascicule no 12*).

Le Comité poursuit l'étude du projet de rapport à la Chambre.

À 11 h 55, le Comité s'ajourne jusqu'à 15 h 30 cet après-midi.

SÉANCE DE L'APRÈS-MIDI
(28)

Le Comité permanent de la consommation et des corporations et de l'administration gouvernementale se réunit, à huis clos, ce jour à 15 h 37, dans la pièce 306 de l'édifice de l'ouest, sous la présidence de Garth Turner (*président*).

Membres du Comité présents: Don Boudria, Gilbert Chartrand, John Cole, Louise Feltham, Gabriel Larrivée, Jean-Marc Robitaille, John Rodriguez, Roger Simmons, Len Taylor et Garth Turner.

Membre suppléant présent: Mark Assad remplace Jean-Robert Gauthier.

Aussi présent: Du Service de recherche de la Bibliothèque du Parlement: Terrence J. Thomas, attaché de recherche.

Le Comité poursuit l'étude de l'évolution du rôle des cartes de crédit dans l'économie canadienne. (*Voir Procès-verbaux du lundi 12 juin 1989, fascicule no 12*).

Le Comité poursuit l'étude du projet de rapport à la Chambre.

Il est convenu,—Que le Comité demande une réponse globale du gouvernement.