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Credit Card Ills: Reducing Racial Disparities in Debt

Andrea Freeman

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CREDIT CARD ILLS: REDUCING RACIAL DISPARITIES IN DEBT

ANDREA FREEMAN*

ABSTRACT

Credit card debt, particularly in conjunction with the subprime lending crisis and severe economic recession, jeopardizes the ability of many African American and Latino households to maintain financial viability. The credit card industry’s business model relies on the payment of fees and high interest rates by the poorest consumers to generate profits and subsidize credit card use by the richest. Documented racial disparities in credit card debt represent and perpetuate structural inequities that require regulatory intervention. Both increased consumer protection and structural reform are necessary to reduce credit card debt disparities arising from present and past discrimination and subordination.

The evolution of credit cards into the primary conduit of consumer debt has dramatically reshaped the relationship between banks and consumers, creating the potential for large-scale exploitation along race and class lines by major financial institutions. This Article builds on legal scholarship on racial disparities by analyzing the problem in the context of credit card debt, explains why

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both law and economics and behavioral economics fail to account for these disparities, and applies a critical race and class analysis to develop proposals that would alleviate in part the structural inequities that lie at the core of the problem. The Article identifies two types of credit card consumers who carry balances, ‘subsistence users,’ who rely on credit to provide for their basic needs, and ‘lifestyle users,’ who maintain a lifestyle above their income through credit. To create transparency that will facilitate regulatory intervention, it calls for full disclosure of industry practices, including targeted marketing and solicitation, and racial discrimination. It then explores two regulatory options for ameliorating the conditions and changing the practices that lead to racial debt disparities: ‘subsistence amnesty’, in the form of the temporary elimination of fees and interest rates on the subsistence purchases of consumers living under the poverty line, and the addition of substantive requirements to the Community Reinvestment Act that would compel credit card companies to help equalize the financial status of low-income communities of color through individual savings accounts, domestic micro-lending, and community-based financial counseling. This Article seeks primarily to contribute to a dialogue about racial debt disparities, in numbers and treatment, among politicians, activists, and economics theorists that will lead to creative strategies to reduce or eliminate these disparities.

INTRODUCTION

The credit card industry has grown from its humble origins as a method for wealthy business travelers to defer payment of their restaurant meals until the end of the month into a global financial industry that reaps billions of dollars in profits from the inability of its lowest-income consumers to match their monthly incomes with their expenses.1 Two major changes to the industry facilitated this expansion. First, deregulation, resulting from two Supreme Court decisions, allowed the banks to avoid limits on interest rates and fees, thereby dramatically increasing their ability to profit from their customers’ dependence on credit cards and shifting the banks’

perception of the model credit card user from one who would pay off her bills at the end of every month to one who could not. Second, securitization, the practice of selling parcels of credit card debt to investors, freed the banks from reliance on their deposit pools to replenish their capital available for lending to credit card consumers and led to global expansion. Also, a class action imposing restrictions on merchant fees limited the potential for profit from the cards’ transacting function and refocused the credit card companies on lending to customers with revolving balances who would consistently pay high interest rates and late fees.

As multiple writers have demonstrated, there is market failure in the credit card industry. This Article builds on that insight by applying an analysis of that failure to racial debt disparities. In a properly functioning market, the consumer, presented with a range of available products, will select the product that best suits her needs. In the process of vying for the consumer’s business, each seller will adjust its product to the consumer’s need, as demonstrated by her choice. The result of this interaction between rational consumers and competing sellers is consumer choice, or the availability of products that provide the consumer with the good or service she requires at the price she is willing or able to pay.

In the credit card industry, behaviors on the part of the consumer and the seller prevent the efficient functioning of this model, leading to market failure and a consequent lack of true consumer choice. Instead of seeking to create a product that matches the consumer’s needs, credit card companies attempt to sell the consumer something


3. Montgomerie, supra note 1, at 302-03.


she does not want: increased and often unmanageable debt. The seller engages in a number of deceptive practices to convince the consumer to purchase this debt against her better instincts. One way sellers do this is by offering very low introductory interest rates (often zero), called teasers, which lure consumers into acquiring a card. The interest rate quickly jumps to one that significantly exceeds lending rates on regular bank loans or mortgages, and most consumers fail to switch to a new card before these rates kick in. Another industry trick is the mass mailing of pre-approved cards, frequently to people in low-income areas who may believe they are not eligible for credit cards. These pre-approved cards are hard to resist, especially for people with heavy financial burdens, and come with very high interest rates and fees for default and late payments. Also, credit card agreements have a provision that allows the companies to change interest rates at any time for any reason without providing advance warnings or recourse to the consumer.

All of these practices are examples of ways in which sellers do not conform to the pressures that would exist in an efficiently functioning market. Additionally, a few major banks and issuers dominate the industry, and their policies and practices do not vary significantly. This market concentration also limits consumer choice.

On the consumer side, various cognitive weaknesses associated with credit card use prevent individuals from acting rationally when acquiring and using credit cards. These include hyperbolic discounting, or a preference for present over future gains, dissociation from the pain of spending that often accompanies cash purchases due to the convenience and simplicity of card use, and the effects of incremental borrowing, which can lead the consumer to amass large amounts of debt through a series of minor purchases. Sellers exploit

10. See infra Part I.A.
these cognitive deficiencies, which lead to non-rational behavior, to increase their profits by attracting customers who will incur the maximum amount of late and over-the-limit fees and pay the highest interest rates. Further evidence of the resulting market failure is the widespread consumer dissatisfaction with credit cards, particularly in low-income users.\footnote{Littwin, supra note 9, at 431-32.} In a properly functioning market, consumers will generally express satisfaction with a product, and sellers’ profits will reflect a reasonable margin. In the credit card industry, profits generated from high interest rates and fees are completely disproportionate to the companies’ costs and consumer dissatisfaction with the product.

Exploration of the credit card market’s failure in scholarly writing presently focuses on two areas: cognitive disabilities and contract deficiencies. Attempting to correct for these two problems alone ignores the need for legislation based on social welfare principles. “Consumer credit is the lever that transforms consumer assets into corporate profits.”\footnote{John P. Watkins, Corporate Profits and Personal Misery: Credit, Gender, and the Distribution of Income, 43 J. ECON. ISSUES 413, 414 (2009).} By inducing consumers to take on debt, often beyond their needs, then charging consumers who cannot immediately pay off this debt fees and interest rates that often exceed the initial loan multiple times, credit card companies engage in upward redistribution of income and wealth on a massive scale.\footnote{The credit card companies’ ability to induce this type of dependence is a testament in part to phenomenal advertising and marketing. “Selling consumer credit is, of course, selling debt—a commodity that would generally be an undesirable one as far as the buyer is concerned. The techniques of selling debt today, however, are such that the nature of the commodity for sale is concealed from the buyer.” Arch W. Troelstrup, The Influence of Moral and Social Responsibility on Selling Consumer Credit, 51 AM. ECON. REV. 550 (1961), quoted in Watkins, supra note 6, at 921.} This redistribution also occurs between poor and wealthy credit card consumers, making credit free for the most sophisticated and high-income users and unconscionably expensive for those who can afford it least.

Class difference, moreover, does not tell the whole story. Statistics published in 2007 demonstrate that the consumers who represent the greatest source of industry profits derived from high
interest rates and fees are disproportionately comprised of low-income African Americans, Latinos, and single women. Legal and economic scholars have, up to this point, largely ignored these racial disparities in debt, focusing on welfare maximization and creative solutions to ‘the credit card problem’ that do not acknowledge the compounded challenges of race and class for consumers in the credit card market.

Debt disparities between African Americans, Latinos, and whites are attributable at least in part to racial discrimination by credit card issuers in the form of ‘redlining,’ the practice of varying credit card contract terms based on the applicant’s zip code and other signifiers of race such as names and appearance. Some of this discrimination likely results from the creditors’ use of race as a proxy for higher default risk. These disparities result for the greater part, however, from the subordination experienced by both African Americans and Latinos in the United States. Due to historical restrictions on black participation in business and access to credit, along with cultural stereotypes that justify and reinforce these restrictions, African Americans generally receive poor treatment from the credit industry.

Alternatives to formal credit such as payday loans and pawn shops,


17. *Id.* at 53. Cohen-Cole’s study does not investigate the motivation behind redlining.

18. See, e.g., Martha L. Olney, *When your Word Is Not Enough: Race, Collateral, and Household Credit*, 58 J. ECON. HIST. 408 (1998) (describing the difference between merchant credit and installment credit and how African Americans experienced financial setbacks due to merchants’ general refusal to extend them merchant credit); Sheila D. Ards & Samuel L. Myers, Jr., *The Color of Money: Bad Credit, Wealth and Race*, 45 AM. BEHAV. SCIENTIST 223, 225 (2001) (exploring the origins of the myths that African Americans have bad credit and explaining that bad credit “serves as a false explanation for the wide racial gaps in loan outcomes”).
prevalent in many low-income African American communities, provide substantially inferior services and therefore do not represent a reasonable substitute.  

Latinos, especially those who are recent immigrants or lack proficiency in English, also face discrimination and inadequate service from the industry, and serve as targets for fraud and unfair contracts. The credit card industry’s structure, which is highly concentrated, and the lack of differentiation between the companies on major terms leave credit card consumers generally without substantial choice in the terms that have the greatest impact on low-income consumers, such as interest rates and fees.

African Americans and Latinos also carry the greater part of credit card debt due to significant wealth gaps in the United States. Particularly for African Americans, this gap has increased dramatically in wake of the 2008 real estate and foreclosure crisis. Even where income and education levels are identical, whites possess exponentially greater levels of assets, or wealth, reducing their dependence on credit cards and providing them with a safety net in times of crisis. The origin of this gap is in government policies, such as the Social Security and Federal Housing Acts, enacted following World War II. The Social Security Act discriminated along employment lines, resulting in the exclusion of most blacks from


21. Cards tend to show variation only on terms that might matter to wealthier consumers, such as with which companies they can accumulate rewards points, or what picture will appear on their card.

22. Devona Walker, How Ruthless Banks Gutted the Black Middle Class and Got Away With It, ALTERNET (Sept. 4, 2010), http://www.alternet.org/economy/148068/how_ruthless_banks_gutted_the_black_middle_class_and_got_away_with_it/ (reporting that black and Latino families owned more than half of California’s foreclosed homes).

23. MELVIN OLIVER & THOMAS SHAPIRO, BLACK WEALTH/WHITE WEALTH: A NEW PERSPECTIVE ON RACIAL INEQUALITY 214 (2d ed. 2006); see generally DALTON CONLEY, BEING BLACK, LIVING IN THE RED: RACE, WEALTH, AND SOCIAL POLICY IN AMERICA (2d ed. 2009).
eligibility for benefits.\textsuperscript{24} The Federal Housing Act channeled home loans away from areas of cities where blacks lived and into white suburbs.\textsuperscript{25} This long history of unequal treatment under the law that began with slavery led to the entrenchment of inequities that society can only eradicate through countermanding laws and policies that strive to achieve racial equality in the financial and all related spheres.

Technological advances in the payment industry indicate that credit card companies will become even more inclined to target low-income African American and Latino consumers. Payment systems such as Paypal\textsuperscript{26} and mobile payments through cellphones\textsuperscript{27} represent emerging threats to credit cards because these new methods are easier and cheaper to use. The transaction costs involved in these systems are minimal and consumers with a cellphone soon may not need to carry a wallet at all. These types of payments also leave consumers less vulnerable to theft. As sophisticated consumers increasingly adopt these payment methods, credit card companies will necessarily turn to their less technologically advanced consumers, many of whom will be African American and Latino, to make up for lost profits through new accounts and additional fees. It is therefore important to

\begin{itemize}
  \item \textsuperscript{24} OLIVER & SHAPIRO, supra note 23, at 40-42. This racial distinction was not facial. Southern legislators deliberately structured benefits policies to leave out domestic and agricultural workers but the Social Security Act itself was colorblind. See id. at 40-41.
  \item \textsuperscript{25} Id. at 41-43. To facilitate racial segregation, the Federal Housing Act handbook provided a model restrictive covenant to white homebuyers.
  \item \textsuperscript{26} For an explanation of how Paypal operates and some of the legal issues surrounding it, see Andrés Guadamuz González, \textit{PayPal: The Legal Status of C2C Payment Systems}, 20 COMPUTER L. & SECURITY REP. 294 (2004).
\end{itemize}
act quickly to push for regulation that will prevent credit card companies from increasing and exploiting existing debt disparities.

Legal scholars, economists, and psychologists have probed the minds of credit card users and analyzed the structure and marketing strategies of the industry to understand why credit card use leads to overborrowing and financial distress. They have also proposed numerous solutions to these problems, ranging from standardization of contract terms to the unbundling of credit cards’ lending and transacting functions to the introduction of a variety of credit cards suited to individual needs. Although industry regulation inevitably meets with great resistance from well-funded lobbyists, it appears to be the only viable method of transforming the structure of the credit card market. This is due to both the market’s failure and the credit card issuers’ willingness to exploit cognitive and psychological mechanisms, such as hyperbolic discounting, over-optimism, and imperfect self-control, that lead consumers to agree to grossly unfair terms.

To date, behavioral economics literature has treated consumers as an undifferentiated group. This is problematic because, although all consumers may be prone to the same cognitive weaknesses, consumers are not identically situated with respect to financial and cultural capital. Analyzing credit card use from a race and class


29. Mann, supra note 5, at 927-32.
32. Explanations of these concepts appear in Part I.A.
perspective reveals important differences between consumers, some of which the industry has exploited and intensified. I identify one type of credit card consumer as a subsistence user. A subsistence user relies on credit cards to pay her electricity and gas bills and to purchase necessities such as groceries and diapers. Without a credit card, she lacks the means to support herself and her family, because of stagnant real wages. The other major type of credit card user, the lifestyle user, can purchase basic necessities without borrowing, but uses credit cards to enhance her lifestyle, whether that means purchasing movie tickets, birthday gifts, or work clothing. All subsistence users and most lifestyle users need a credit card to pay for emergencies such as unforeseen medical expenses or car repairs.

Both traditional law and economics and behavioral economics fail to account for the needs and behavior of subsistence users. Neoclassical law and economics assumes that every consumer makes rational choices based on complete information about products that, through the process of competition, conform to the consumer’s needs or desires. This model makes no distinction between a lifestyle user, who chooses to use a credit card based on her perceptions of how the card will improve her quality of life in some way, and the subsistence user, who must borrow to avoid eviction, hunger, or the loss of vital services such as gas, telephone, or electricity. The demand curve of a subsistence user is predictable and inelastic; it responds to the user’s basic needs, not fluctuations in the credit card market or products.

Behavioral economics seeks to compensate for flaws in the traditional model by examining how cognitive limitations impede rational decision-making. By focusing on purportedly universal human cognitive patterns, however, it does not account for the subsistence user’s unique needs. Basic needs and a dependence created by the credit card industry itself define and explain the subsistence user’s behavior.

Credit cards began as a tool of convenience for the middle class and many people continue to view that service as their proper function. The government provides some support for low-income people through food stamps and other social assistance programs but the amount provided is insufficient in most cases to support a family. Credit card companies zeroed in on this struggling population because it contains the people most likely to revolve balances for the longest periods of time, representing that sweet spot of the market, below the
convenience user but above the individual in bankruptcy proceedings.  

This Article analyzes the problem of racial disparities in credit card debt for the first time in legal scholarship, explains why both law and economics and behavioral economics fail to account for these disparities, and applies a critical race and class analysis to develop proposals that would alleviate in part the structural inequities that lie at the core of the problem. Racial debt disparities include both numbers (dollar amounts of debts, interest rates, and fees) and processes (the targeting of low-income blacks and Latinos and the differential impact of interest rate and fee provisions). Strengthened consumer protection through usury laws, the requirement of full disclosure of industry practices, and mandated community investment designed to alleviate poverty would reduce racial debt disparities significantly.

This Article begins, in Part One, by briefly describing the history and structure of the credit card industry. It presents some of the more salient statistics regarding race and credit card debt and puts forth some historical, political, social, and economic explanations for racial debt disparities. It ends with a review of theoretical perspectives on the relationship between the credit card companies and their customers, primarily from psychological and behavioral perspectives. In Part Two, I evaluate the potential for existing modes of consumer protection to reduce or eliminate racial debt disparities. I examine the contract doctrines of unconscionability, good faith, and penalty; the prohibition of racial discrimination in credit by the Equal Credit Opportunity Act (“ECOA”); and the amendments to the Truth in Lending Act embodied in the 2009 Credit Card Accountability, Responsibility and Disclosure Act (“the CARD Act”). I conclude that these protections are inadequate.

Part Three calls for the Consumer Financial Protection Agency to require full disclosure of credit card practices, including predatory lending and racial discrimination. It describes and analogizes to slavery disclosure laws’ successes in raising public awareness and

34. See Ronald J. Mann, Bankruptcy Reform and the “Sweat Box” of Credit Card Debt, 2007 U. Ill. L. Rev. 375, 385-91.
increasing community investment by financial institutions. This part then offers two proposals to reduce racial disparities in credit card debt. The first is the elimination of interest rates and fees on subsistence purchases by consumers living under the poverty line, a proposal I call ‘subsistence amnesty’. The second proposal invigorates the Community Reinvestment Act of 1977 (“CRA”) by adding requirements compelling financial institutions that engage in racial discrimination to invest in low-income African American and Latino communities with the goal of effecting long-term, structural improvements. I conclude by encouraging individuals to take action to reduce racial debt disparities and calling for further investigation into and discussion of these issues by economists and other scholars, activists, politicians, and journalists.

I. THE CREDIT CARD INDUSTRY

The credit card industry is the most profitable financial service in the United States. Although the use of store charge cards began in the early twentieth century, Diners Club introduced the first universal credit card in 1949. The card had limited use, allowing traveling businessmen to charge meals, and required payment in full each month. Other cards soon appeared, despite doubts that a credit card system could be profitable. From the 1960s to the 1980s, buoyed by congressional and judicial support of deregulation, Bank of America and a rival network, the Interbank Card Association, became the two major credit card players, offering cards that would eventually be branded Visa and Mastercard. The credit card game changed radically in 1978 when, in Marquette National Bank of Minneapolis v. First Omaha Service Corp., the Supreme Court ruled that banks could charge interest rates according to the usury ceilings in the state where their headquarters were located, instead of their customers’ home states. This decision led banks to relocate to states with the

38. Montgomerie, supra note 1.
39. Id. at 310.
40. See MANNING, supra note 28, at 85.
41. Id. The original cards were called Master Charge and BankAmericard. Id.
43. Id. at 308-12.
least restrictive usury laws, and states to repeal restrictive laws to discourage the exodus of major financial institutions. A second Supreme Court decision, *Smiley v. Citibank*, extended this rule to fees in 1996, thereby completing the process of deregulation.

Technology pundits predict that consumer-to-consumer (“C2C”) and mobile payments are the way of the future of payment methods. In November 2010, three of the four top mobile phone providers, AT&T, Verizon, and T-mobile announced that they had established a joint venture for mobile payments that will allow consumers to pay for items by waving their phone near a machine. This innovation will eventually lead to the elimination of the need for a wallet and further consolidation of multiple functions in a handheld phone. The joint venture, Isis, will use Discover financial services and compete directly with Visa and Mastercard. Iphones in Europe have partnered with Visa for contactless payments. If mobile payments are in fact the future of payment systems, the current business model of the credit card industry that relies on less sophisticated consumers for its profits may prove obsolete.

In the meantime, credit card companies continue to wield extensive economic power. Despite recognition by academics, media, Congress, and the courts that credit card companies exploit low-income users and create high social costs by encouraging financial distress, these companies succeeded in strengthening their position through the Bankruptcy Abuse Prevention and Consumer Protection Act (“BAPCA”) and ensuring that the CARD Act would

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44. Bar-Gill, supra note 7, at 1381.
46. *Id.* at 744-47.
47. Aspan & Carew, supra note 27.
50. In spite of its deceptive name, the BAPCA likely served to increase credit card companies’ profits by slowing down the inevitable filings by deeply distressed consumers, allowing the companies to earn greater pre-filing revenues from those
contain enough loopholes to allow them to compensate for lost profits through unregulated fees and terms. It is therefore essential to develop an immediate response to the credit card industry’s exploitation of vulnerable populations.

Today, the four leading brands of credit cards are Visa, Mastercard, American Express, and Discover. The first two operate through a network of banks, which act as the actual issuers of the cards and funds. Issuing banks set individual contract terms with consumers, while Visa and Mastercard set interchange fees with merchants that intermediaries, called acquirers, collect for a small percentage of the interchange fee. Other issuers, such as Capital One, known as monolines, perform no functions other than issuing credit cards. Credit cards compete with other forms of payment, including cash, checks, debit cards, C2C payments such as Paypal, and mobile payments. Cash, which once represented the most honest and ethical form of payment, now carries a stigma of association with criminality and poverty. Although credit cards have long surpassed checks in volume of transaction, the use of checks in the United States is still quite high, despite the associated expenses and inconvenience.

individuals. Mann, supra note 34, at 392.


52. See Ronald J. Mann, Credit Cards and Debit Cards in the United States and Japan, 55 VAND. L. REV. 1055, 1068 (2002).

53. In terms of social value, cash is the least sophisticated, least efficient, and least productive form of money. When we think of cash, we envision small amounts of money that will fit into a wallet, a cookie jar, the opening in a mattress, or a passbook savings account. When we think of cash in large amounts, we envision stacks of bills that have been illegally obtained or accumulated in the criminal or underground economies and that must be laundered or destigmatized. Cash is meant to be spent or saved; it is largely a tool of consumption, not an instrument of investment. Austin, supra note 19, at 1245.

Debit cards are more popular than credit cards in many countries because of their low transaction costs (the money transfers directly from the customer’s account to the merchant) and due to their social benefit.\textsuperscript{55} Debit cards do not perform the function of lending, and consequently do not involve fees or interest rates. For that reason, although ease of use may lead a consumer to spend more using a debit card than she would making a cash or check purchase, debit cards are less likely to lead to financial distress than credit cards.\textsuperscript{56} Debit cards offer slightly less consumer protection than credit cards, however, because there is no delay between point of sale and payment during which a consumer could object to a fraudulent charge. In the United States, Visa and Mastercard also dominate the debit card market, and these companies have deliberately created consumer confusion between debit and credit cards.\textsuperscript{57} Most plastic cards function as either debit or credit cards but, because of the higher profits associated with credit card use, the companies encourage use of the credit card through rewards programs and similar perks.

Credit cards perform two separate functions, transacting and lending. Although there are costs associated with transacting, merchants presently bear these costs. At the point of sale, a consumer pays nothing additional to the purchase price of the item, but the merchant receives from the credit card company only ninety-seven to ninety-nine percent of the amount charged, depending on the type of card or the particular agreement between the individual merchant and company.\textsuperscript{58} It is unclear whether merchants make or lose money from credit card use because no accurate statistics reflect the amount of

\textsuperscript{55} MANN, supra note 28, at 106. For example, the card markets of Australia, Canada, and the United Kingdom are dominated by the use of payment cards but with substantially lower use of credit cards and credit card borrowing than the United States, likely due to increased segmentation between debit and credit card products.

\textsuperscript{56} MANN, supra note 28, at 29, 120.

\textsuperscript{57} See MANN, supra note 28, at 32-33; MANNING, supra note 28, at 115 (explaining how the banking industry has attached automatic lines of credit to debit cards to erode “the traditional ‘cognitive connect’” between debit cards and bank accounts).

\textsuperscript{58} Rewards cards cost merchants more than regular cards, but merchants do not pass these costs back to the individual consumer.
increased business generated by credit card use as offset by merchant fees. Although discounts for the use of cash were once common, regulation abolished these discounts. Congress subsequently repealed the ban, but most merchants have not reinstated discounts, nor do they charge more for credit card use.

Studies have revealed that credit card use increases overall consumer spending and consumer debt. It is also correlated with increasing personal bankruptcies. Credit card issuers have fought hard to prevent debtors from discharging their credit card debt in bankruptcy and made some gains in this regard with the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act. Courts have recognized, however, that the credit card companies deliberately prey on consumers who cannot repay their loans, and have resisted compelling debtors to pay the companies on these grounds.


60. An exception to this general rule is gas stations, which often do offer a discount for cash.


62. See *Mann*, supra note 34, at 402-03.

63. Credit card companies contributed over twenty-five million dollars to politicians and political parties between 1999 and 2005 in efforts to lobby for bankruptcy reform. Robert H. Scott III, *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005: How the Credit Card Industry’s Perseverance Paid Off*, 41 J. Econ. Issues 943, 945 (2007). They succeeded. Thanks to BAPCA, they now recoup four billion dollars a year, representing a 7.5 percent increase in revenue. *Id.* This increase is due to more stringent requirements preventing people from filing bankruptcy sooner, allowing the credit card companies to collect fees and interest rates and garnish wages longer. *Id.* Statistics belie the propaganda supporting the credit card companies’ lobbying campaign that accused consumers of abusing the existing bankruptcy laws. The most important predictor of personal bankruptcy is children, and forty percent of personal bankruptcies result from medical emergencies. Watkins, *supra* note 12, at 418-19.

64. Bar-Gill, *supra* note 7, at 1427 (“‘Credit issuers are willing to risk nonpayment because the profits on finance charges exceed their risks. Thus, the same industry that seeks customers who will spend more than their means requests that discharge be denied to these customers because of an implied promise (which courts must infer) not to spend more than their means.’” (quoting David F. Snow, *The Dischargeability of Credit Card Debt: New Developments and the Need for a New Direction*, 72 Am. Bankr. L.J. 63, 80-81 (1998))).
The original conception of the paradigmatic credit card user was the lifestyle user. Cultivating this type of consumer required a change in values surrounding credit. In the late nineteenth and early twentieth centuries, the use of credit was considered “an economic sin” that led “straight to serfdom” by setting “utterly false standards of living and causing “hopelessly distorted” judgment. A change in values came in the wake of industrialization, which refocused a societal emphasis from production to consumption through urbanization, rising incomes, and the abundance of new goods. By the 1920s, it became “old-fashioned to limit [] purchases to the amount of [] cash balances” and consumers used credit to finance up to ninety percent of durable goods purchases.

The introduction of a universal credit card in 1948 attracted many lifestyle users, many of whom paid their balances in full, leading card issuers to impose annual fees on cards in the 1970s. During this decade, the National Welfare Rights Organization led a successful grassroots campaign to ‘democratize’ credit by extending it to women on welfare. Activists in the movement viewed the possession of a credit card as a status symbol the absence of which relegated individuals to second class citizenry. The idea that possession of a credit card confers privilege that can overcome class or racial discrimination is still prevalent today. Credit card companies, however, do not solicit low-income users for the purpose of elevating

65. Watkins, supra note 6, at 913 (quoting CLYDE WILLIAM PHELPS, THE ROLE OF THE SALES FINANCE COMPANIES IN THE AMERICAN ECONOMY (1952)).
66. Id. at 913-14.
67. Id. at 915 (quoting FREDERICK ALLEN, ONLY YESTERDAY: AN INFORMAL HISTORY OF THE 1920’S (1931)).
68. Id. at 922.
70. Id. Middle and upper class women also viewed the lack of access to credit cards as a symbol of discrimination. Neither the mayor of Davenport, Iowa, Kathryn Kirshbaum, nor tennis star Billie Jean King could get credit cards without their husbands’ signatures until Congress passed the Depository Institutions Amendments Act banning sex discrimination in lending in 1974. GAIL COLLINS, WHEN EVERYTHING CHANGED 250 (2009).
71. See Littwin, supra note 8, at 465-66.
their social status, but with the sole intention of profiting from their reliance on the cards. After the democratization of credit, credit card companies shifted their marketing and advertising campaigns\(^\text{72}\) in an effort to attract the second-to-lowest income consumer, the one that charges more than she can afford but has not yet descended into bankruptcy.\(^\text{73}\)

This part begins by describing how psychology and behavioral economics account for consumers’ conduct in relation to credit cards and discusses the relevance of these theories to racial debt disparities. It then identifies two new categories of credit card users and reports the distribution of credit card debt and wealth along racial lines. It follows with a brief review of historical, political, economic, and social explanations for racial debt disparities.

### A. Behavioral Economics and Credit Cards

Legal scholars, psychologists, and economists have done extensive work exploring theories of human consumption as it relates to credit cards, seeking explanations for the ability of the credit card to promote overspending and borrowing, and the failure of the credit card market. One economist, building on Thorstein Veblen’s social institutional theory of consumption, describes the relationship between the credit card companies and their indebted borrowers as purely parasitical, with the parasite draining its host by charging numerous fees and penalties amounting to over ninety billion dollars in revenue each year.\(^\text{74}\) Veblen viewed companies that, like the credit card issuers, produce nothing of tangible value as blackmailers, trying to get something for nothing.\(^\text{75}\)

The Veblenian analysis rejects neoclassical market theory because of its failure to recognize that overborrowing often results from income inequality, not rational decision-making. An approach that ignores inequality and instead seeks only to change people’s attitudes

\(^\text{72}\). For a thorough and fascinating account of shifting marketing strategies and descriptions of the representative ads, see MANNING, supra note 23, ch.1.

\(^\text{73}\). See Mann, supra note 34, at 384 (noting that “the most profitable customers are sometimes the least likely to ever repay their debts in full”).


\(^\text{75}\). Id. at 570-571.
toward overconsumption will be futile. Veblen’s work in Theory of the Leisure Class focused on the inelasticity of demand for credit when users rely on it to provide the level of consumption they believe is necessary to create the illusion of status they desire.76 I identify these consumers as lifestyle users. Demand is also inelastic, or fixed, however, for subsistence users, who rely on credit for survival.

Angela Littwin discusses two of the major cognitive deficiency theories, hyperbolic discounting and advance commitment, or imperfect self-control, that developed to explain credit card overuse in the context of low-income women. Hyperbolic discounting describes the mental process of preferring present pay-offs to future gains.77 For example, a hyperbolic discounter will choose to receive $100 today instead of $110 in thirty days because she discounts the value of future rewards. This discounting will also prompt her to prefer to receive $110 in thirty-one days over $100 in thirty days, because she considers both of those dates equivalently far in the future. On day thirty, however, she will revert to preferring to receive $100 on that day instead of $110 the next.

Applying this theory to credit card use, a credit card user who obtains a card in the present believes that both future borrowing and repaying will be manageable. She accordingly acquires a credit card, believing that she will not make purchases she cannot afford. On the date of purchase, however, she discounts the pain of paying off the debt because it is in the future. She therefore decides to borrow, and repeats this pattern at every point of purchase. The immediate emotional gratification of spending consistently dominates the hyperbolic discounter’s mind. Compounding the problem is the use of a plastic card, which eliminates the pain of spending often associated with cash payments.78

Imperfect self-control can also lead a consumer to make a series of borrowing decisions that lead to the accumulation of unmanageable debt. In other words, “debtors who never dream of seeking a $5000

73. THORSTEIN VELBEN, THE THEORY OF THE LEISURE CLASS 68 (1899).
77. Both Littwin and Bar Gill offer good descriptions of this phenomenon. See Littwin, supra note 8, at 467-69; Bar Gill, supra note 7, at 1396-97. This mental process can also be viewed as part of short-termism, a cultural phenomenon that values instant gratification over long-term rewards.
78. For studies on the effects of negative emotions on purchasing decisions, see Wiener et al., supra note 28; Lowenstein & O’Donoghue, supra note 33.
bank loan might run up $5000 in charges of $50 at a time.” While succumbing to minor temptations may seem relatively harmless at the point of purchase, piecemeal borrowing can eventually plunge the user into debt that she can only escape through bankruptcy. Low-income users are particularly susceptible to this slippery slope of debt accumulation because they often need small-value items, such as cleaning supplies, which one would not normally associate with the type of extravagant purchasing that leads to financial distress. The relative ease of making purchases with a credit card also exacerbates the temptations of incremental borrowing.

Another popular theory of credit card use is the over-optimism, or underestimation, bias. Under this model, consumers underestimate the likelihood of adverse events that could create a need to borrow, such as being in an accident, requiring costly medical treatment for themselves or their loved ones, or losing a job. Underestimation interacts with the other theories, which can lead to stressful financial conditions that increase a person’s vulnerability to unexpected unfortunate circumstances. Underestimation bias accounts for the credit card market’s unique pricing patterns, where up-front, short-term prices, such as annual and transaction fees, are underpriced, and long-term elements such as interest rates and penalty fees are over-priced.

Finally, ‘miswanting’ may also account for non-rational borrowing behavior. Miswanting is the desire to purchase items that do not promote a person’s welfare, or the opposite, a lack of desire for things that would increase an individual’s well-being. A desire to

80. See id. at 111 (labeling consumers who fall into this trap “sliders”).
81. Littwin, supra note 8, at 469.
82. Bar-Gill, supra note 7, at 1400; see also Sean Hannon Williams, Sticky Expectations: Responses to Persistent Over-Optimism in Marriage, Employment Contracts, and Credit Card Use, 84 NOTRE DAME L. REV. 733, 742-46 (2009).
83. Bar-Gill, supra note 7, at 1400.
84. Id.
85. Id. at 1376.
86. See Sunstein, supra note 33, at 253. Sunstein attributes excessive borrowing to five problems: cumulative cost neglect (described as incremental borrowing and imperfect self-control above); procrastination and inertia, leading to
improve one’s social position relative to friends and associates often drives miswanting, leading a person to use credit to fund a purchase that ultimately does not in fact provide any long-lasting emotional or physical benefits.\textsuperscript{87}

The emphasis in the literature on credit card use on these psychological and behavioral theories obscures the realities of the subsistence user, whose behavior does not require elaborate explanation. While a subsistence user could exacerbate her debt due to the cognitive disabilities described above, “households with low incomes tend to use credit to help cope with budgeting troubles instead of increasing purchasing power.”\textsuperscript{88} Any serious attempt to improve the subsistence user’s circumstances therefore should not focus on the consumer’s own complicity in her financial distress but on the part played by the credit card companies.

Psychology and behavioral economics may, however, partially explain debt disparities, although there does not appear to be any work in this area that seeks to account for cognitive responses to credit cards along racial or class lines. Investigation into consumer credit card use that analyzes economic behavior by race and class would help to identify the most effective solutions by determining what part cognitive disabilities, actions by the industry, and structural inequalities each play in creating and perpetuating debt disparities. This paper therefore calls for behavioral economics and socioeconomics scholars to pursue research along these lines.

late fees (this factor might also explain consumers’ tendency not to transfer their balances after the expiration of low introductory or ‘teaser’ rates); unrealistic optimism; myopia and self-control problems (similar to hyperbolic discounting in that it describes an emphasis on the short term at the expense of the future); and miswanting or relative position. \textit{See id.} at 251-53.


B. Credit Card Users and Statistics

Over eighty percent of households now possess credit cards. Card usage varies greatly, mostly along class lines. Credit card issuers identify four types of users: non-users, who possess credit cards but don’t use them; convenience users (or ‘deadbeats’), who pay off their bills at the end of each month; revolvers, who maintain a balance; and late payers. Consumers in the last two categories generate the most profits for the companies. Transactions by convenience users generate merchant fees, but these fees pale in comparison to the interest rates and late fees generated by revolving balances and late payments. I have further identified two types of consumers: subsistence users and lifestyle users. Subsistence users depend on credit cards to provide basic needs for themselves and their families, such as diapers, gas, and groceries. Lifestyle users can survive without amassing debt, but use credit cards to cover lifestyle-maintaining purchases, such as holiday presents and work clothes, or to deal with emergencies such as unforeseen medical expenses and car repairs, or to fund leisure activities such as eating in restaurants and attending cultural and entertainment events. At the lower end of the spectrum of lifestyle users, the line between this group and subsistence users is not bright. Many lifestyle users may be only one catastrophic event away from becoming a subsistence user. These two categories also overlap with the ones identified by the industry. Lifestyle users may be convenience users, revolvers, or late payers. Subsistence users are likely to be revolvers and late payers but might sometimes be convenience users.

In an attempt to understand low-income women’s relationship to credit, Angela Littwin conducted a study of credit card use and preference among fifty women, seeking ultimately to enhance these consumers’ ability to repay debt free of unreasonable penalty fees and

91. Middle and low-income convenience users are the primary beneficiaries of the expansion of credit. Steven Mercatante, The Deregulation of Usury Ceilings, Rise of Easy Credit, and Increasing Consumer Debt, 53 SAN DIEGO L. REV. 37, 43-44 (2008).
interest. Some of the study participants, who all resided in public or subsidized section 8 housing, expressed the view that credit cards allowed them to gain access to mainstream American society. They identified many situations that led them to incur debt on their credit cards, including interruption in food stamps, threats of eviction, administrative issues with health insurance, and car breakdowns. Littwin notes the complex interrelationship between the ability to cope with these types of emergencies and mental health issues. Financial stress leads to mental and physical problems that in turn can create greater financial burdens and reliance on credit.

Subsistence users are born of necessity. Lifestyle users, on the other hand, are the product of societal pressure to maintain a certain standard of living combined with intense marketing and advertising campaigns by the credit card companies. As described by Juliet Schor in The Overspent American, Americans who are not simply struggling to survive no longer strive to emulate their neighbors. Instead, they now seek to attain a quality of life manifested through materialist acquisition and overt consumption that matches that flaunted by celebrities, television characters, and co-workers. A single mother of four may therefore believe that she must maintain the outward appearance of good living established by her supervisor, a woman whose spouse earns two hundred thousand dollars a year and who has no children. Veblen’s present-day leisure class thus transmits its taste and values to Americans through fictional families portrayed on television, and studies reveal that the majority of people report dissatisfaction with their class status, regardless of what it is.

92. Littwin, supra note 8, at 454. Littwin also used this study to determine whether credit card regulation would force borrowers into using other, less desirable forms of credit, such as pawn shops and rent to own stores. See Littwin, supra note 9.

93. Littwin, supra note 8, at 464. This study is particularly informative for the purposes of this paper because forty percent of the participants were African American and forty-two percent were Latina. See id. app. at 503.

94. Id. at 458.

95. Id. at 458-59.


97. Id. at 5, 28-34

98. Id. at 7-8, 11-19.
Credit card companies exploit this dissatisfaction and futile desire for cross-class lifestyle equality by featuring celebrities in their ads, insisting that certain experiences must be had at any cost (“priceless”), and providing the means to indulge now, pay later. To woo the subsistence user, credit card companies devote their resources to massive mail-outs of pre-approved credit cards. These mailings prey on many low-income people’s fears that they are not credit-worthy, eliminate the often prohibitive cost of card shopping, and offer the worst terms, often disguised by a seductive introductory teaser rate.99 Through these mailings, the credit card companies continually recruit new crops of subsistence users that serve as major sources of revenue at the cost of their own financial integrity.100

The category of subsistence user is most likely to encompass low-income African Americans and Latinos. People relying on credit to survive will almost always be in the lowest socio-economic class because they do not have sufficient income or wealth to cover their basic necessities. In the United States, blacks and Latinos are overrepresented in this class due to disparities in income, wealth, education, health, and criminalization, which in turn arise from structural inequalities and legal barriers to growth such as immigration policies. While many, if not most, subsistence users will therefore be low-income African Americans and Latinos, lifestyle users at the higher end of the socio-economic spectrum will tend to be white, as will most convenience users, and lifestyle users in danger of becoming subsistence users will tend to be lower-income blacks and Latinos. Protection for subsistence users is particularly important as many low-income African Americans and Latinos lack a political voice, do not have lobbyists, and may wish to avoid drawing attention to themselves due to complicated relationships with institutions such as law enforcement, the penal system, welfare, and immigration.

99. Littwin proposes that instead of the current opt-out system of unsolicited mailings, there should be an opt-in system. Littwin, supra note 8, at 484.

Statistics from before the 2008 financial crisis show that while only fifty-four percent of white households carry a revolving balance on their credit cards, eighty-five and seventy-nine percent of African American and Latino households, respectively, do. African American and Latino households also pay disproportionately high interest rates on their credit cards, with fifteen percent of African Americans and thirteen percent of Latinos paying over twenty percent in interest, while only seven percent of whites pay that much. These groups also pay more late fees than whites. Additionally, fourteen percent of Latinos fall victim to credit card fraud as compared to only six percent of whites.

According to a 2010 report, African Americans have one tenth the amount of wealth that whites have. This gap exists even where levels of income and employment are the same and leads to much greater reliance on credit cards for black families. Generally, African Americans have lower incomes and employment rates. In 2009, the median net worth of Latino households was $7,932, as compared to $88,651 for white households. There are also alarming health disparities between African Americans, Latinos, and whites that create

101. In 2004, 84% of African American households (90% earning between 1 and 25,000) and 79% of Latino households carried credit card debt compared to 54% of white households. NAACP Fact Sheet: Usury – The Impact of Credit Card Debt and High Interest Rates on African American Wealth, NAACP, 1 (Sept. 29, 2009), http://backup.naacp.org/advocacy/economic/USURY_Fact_Sheet_92909.pdf [hereinafter NAACP Fact Sheet].


103. Id. at 8.


105. NAACP Fact Sheet, supra note 101, at 3.

106. CONLEY, supra note 23.

107. On average, African Americans and Latinos earn 62 and 69 cents, respectively, for every dollar earned by their white counterparts. NAACP Fact Sheet, supra note 101, at 3.

108. In April 2009, the overall unemployment rate for African Americans was 15%, whereas the national average was 8.9%. Id. Statistics for Latinos can be unreliable because of undocumented workers.

a greater likelihood of medical emergencies in black and Latino households.\textsuperscript{110}

Many African American and Latino families use credit cards as a safety net to cope with drops in income and unexpected expenses,\textsuperscript{111} and to provide health care in medical emergencies, particularly if they are un- or under-insured. The wealth gap and resulting racial disparities in credit card debt reflect structural inequities that derive in part from, in the case of African Americans, the legacy of slavery, Jim Crow, and economic exploitation, and, for Latinos, wage theft, legal insecurity, and hostility towards immigrants, among other things. Racism against these two putative groups, although in some cases overt, is also deeply entrenched in society, requiring structural reform to effectuate the eradication of debt disparities.\textsuperscript{112}

\textit{C. Causes of Racial Debt Disparities}

The categories of ‘black’ or ‘African American’ and ‘Latino’ do not represent homogeneous groups. Attempts to explain racial debt disparities must accordingly generalize. Most explanations generalize to one or the other group, but some affect both groups, which

\textsuperscript{110} For example, Latinas and black women have the highest rates of cervical cancer, \textit{Cervical Cancer Rates by Race and Ethnicity}, CDC, http://www.cdc.gov/cancer/cervical/statistics/race.htm (last updated Sept. 28, 2010), black men have the highest incident rate of and are more likely to die from prostate cancer than any other group, \textit{Prostate Cancer Rates by Race and Ethnicity}, CDC, http://www.cdc.gov/cancer/prostate/statistics/race.htm (last updated Sept. 28, 2010); and have the highest rates of lung cancer, \textit{Lung Cancer Rates by Race and Ethnicity}, CDC, http://www.cdc.gov/cancer/lung/statistics/race.htm (last updated Sept. 27, 2010). Some of these disparities may even be attributable to credit card use. Black women have higher rates of high blood pressure, high cholesterol, and diabetes than white women, and, according to the American Heart Association, a significantly greater percentage of African American men and women than whites suffer from heart disease, \textit{Heart Disease, Race, and Ethnicity}, LIFEHEART.COM, http://www.lifeheart.com/patient/angina/ethnicity.asp (last updated June 1, 2009). Some of these disparities may be attributable to credit card use. \textit{See} Manoj Thomas et al., \textit{How Credit Card Payments Increase Unhealthy Food Purchases: Visceral Regulation of Vices}, 38 J. CONSUMER RES. (forthcoming June 2011), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1675826.

\textsuperscript{111} \textit{NAACP Fact Sheet, supra} note 101, at 3.

\textsuperscript{112} I use the word ‘putative’ to acknowledge that these are socially constructed racial groups that in reality are non-homogeneous.
currently represent the most economically and structurally disadvantaged racial groups in the United States.

1. African Americans

For African Americans, the 2008 financial crisis exacerbated the existing wealth gap to the point where some have predicted the demise of the black middle class. In their seminal book, Black Wealth/White Wealth, Melvin Oliver and Thomas Shapiro, in 1995, estimated that most middle class blacks could survive on their savings for only one month after a loss of income. After the unprecedented loss of property and jobs in 2009 and 2010, we can speculate that that number has been cut at least in half. Oliver and Shapiro trace the modern origins of this increasing wealth gap to blacks’ exclusion from social programs such as Social Security, which initially did not include agricultural and service workers, which represented the occupations held by many African Americans. They also explain how the government frustrated the efforts of African Americans to purchase homes through discriminatory policies embodied in and facilitated by the Fair Housing Act.

Historical restrictions on the types of business in which African Americans could participate also steered them into specific industries, the majority of which did not represent the potential for substantial profits. Moreover, black businesses were traditionally confined to black neighborhoods and catered to mostly black clientele, many of

113. Walker, supra note 22.
114. OLIVER & SHAPIRO, supra note 23, at 99. They report that, at poverty living standards, thirty-five percent of the black middle class might survive for one month, and twenty-seven percent might hold out for three.
115. Walker, supra note 22.
116. OLIVER & SHAPIRO, supra note 23, at 40-42. Due to minimum amount requirements, even blacks in eligible occupations often did not qualify for benefits. For example, in 1935, forty-two percent of blacks in eligible occupations failed to meet the minimum income requirements, while only twenty-two percent of whites did. Id. at 40.
117. Id. at 41-43.
118. See, e.g., Olney, supra note 18, at 425 (citing a study reporting that, in 1920, over half of black businessmen were in the grocery industry).
whom did not have high levels of disposable income.\textsuperscript{119} Whereas some of these niche industries have flourished, such as hair and beauty products, which ironically depend for the most part on negative societal images of their clientele to prosper,\textsuperscript{120} many black businesses struggled to survive, particularly as successful blacks emigrated away from all-black neighborhoods. Ghettoized economies prevented economic growth for small black businesses and individual consumers, forcing them to rely on debt to meet monthly expenses.

African Americans seeking access to credit for store purchases historically encountered significant obstacles. Martha Olney’s study of store credit in the 1910s reveals that, while most whites relied on merchant credit to make purchases, stores offered African Americans only highly inferior installment credit.\textsuperscript{121} Under the informal merchant credit system, merchants did not require the customer to pay either a downpayment or interest.\textsuperscript{122} Consumers could pay off goods over time without threat of repossession, and build a good credit history in the process.\textsuperscript{123} Installment credit, in contrast, involved hefty down payments, gave the merchant the legal right to repossess the good upon default, and did not allow consumers to build a positive credit history.\textsuperscript{124} Additionally, merchants officially retained possession of goods purchased through installment credit until the consumer rendered full payment.\textsuperscript{125}

As a result of poor treatment by or exclusion from the formal credit market, blacks have often turned to alternative sources of credit such as pawn shops, cash checking places, and payday loans. Scholars have written extensively on the inferiority of these sources of credit, which typically take exorbitant cuts in exchange for speed,

\textsuperscript{119} See OLIVER & SHAPIRO, supra note 23, at 48-51 (describing the “economic detour” that compelled a black businessman to “seek his customers or clients ‘from within his own race,’ no matter what the business” (internal citation omitted)).
\textsuperscript{120} GOOD HAIR (Chris Rock Productions & HBO Films 2009).
\textsuperscript{121} Olney, supra note 18, at 410, 411 tbl. 1.
\textsuperscript{122} Id. at 415.
\textsuperscript{123} Id. at 426.
\textsuperscript{124} Id. at 429.
\textsuperscript{125} Id. at 427.
convenience, and access to cash when no other options are available.\textsuperscript{126} Cultural stereotypes also feed into and create barriers to good credit for African Americans. In a 2001 study of black financial habits, Sheila Ards and Seth Myers debunk the myths that African Americans overspend, fail to save, and are not creditworthy.\textsuperscript{127} Contrary to popular mythology, the study demonstrates that blacks have high saving rates, a factor ordinarily correlated with good credit, and that their spending is primarily on rent.\textsuperscript{128} In general, the necessity of funneling most of one’s income into rent prevents individuals from amassing wealth. Before the mortgage crisis, homeownership represented one of the primary reasons for the wealth gap between black and white families in the United States.\textsuperscript{129} The study also reveals no statistically significant difference in bad credit rates between black and white households at both the lowest and highest wealth levels.\textsuperscript{130} Ards and Myers attribute the observed differences in credit rates in the middle wealth range to differential treatment of blacks and whites in credit markets.\textsuperscript{131}

Despite the statistical realities, many blacks have internalized stereotypes that lead them to believe that they have bad credit even when they do not.\textsuperscript{132} These mistaken beliefs lead black consumers to agree to bad terms and conditions in credit card agreements without investigating the possibility of finding a card with better terms. Credit card companies, equipped with extensive information about applicants’ creditworthiness, knowingly exploit these beliefs, in addition to relying on the general tendency of credit card users not to negotiate.\textsuperscript{133} Creditors also likely often rely on the stereotype of blacks possessing bad credit, either consciously or unconsciously.

\textsuperscript{126} See, e.g., Nathalie Martin, \textit{1,000\% Interest—Good While Supplies Last: A Study of Payday Loan Practices and Solutions}, 52 ARIZ. L. REV. 563 (2010).
\textsuperscript{127} Ards & Myers, \textit{supra} note 18.
\textsuperscript{128} \textit{Id.} at 224, 230-31. Olney offers as explanation for high savings rates in low-income African American households the necessity of saving to pay off goods purchased on installment credit. \textit{Olney, supra} note 18, at 428-29.
\textsuperscript{129} \textit{Oliver & Shapiro, supra} note 18, at 111 & tbl 5.4.
\textsuperscript{130} Ards & Myers, \textit{supra} note 18, at 237 & tbl. 8.
\textsuperscript{131} \textit{Id.} at 236 & tbl. 6.
\textsuperscript{132} \textit{Id.} at 225.
\textsuperscript{133} See \textit{Mann, supra} note 28, at 113-14 (discussing the credit card
One of the most damaging stereotypes degrading African Americans’ financial habits is that of the conspicuous consumer. This stereotype originated in post civil war United States, when “the central debate in American social life was about how the newly freed slaves would participate in labor and consumer markets as well as in the polity.” 134 During this period, as part of the White supremacist narrative, the integration of freed slaves into society was tainted by the Black consumer myth, a stereotype that African-American consumption was “indulgent, impulsive and wasteful.” 135 Whites deeply resented black attempts to best whites in displays of status as well as blacks’ participation in middle class activities such as attending the theater. 136 This type of resentment continues to the present day, as reflected in the common critique of hip hop as a reflection of black consumerism and materialism, an expression of the companies’ reliance on extensive personal data to identify ideal customers and maintain profitability).


135. See id. (discussing the black consumer myth as understood by historian Ted Ownby in “American Dreams in Mississippi,” stated as “the proverbial fool to be soon parted from his money”); see also Jason Chambers, Equal in Every Way: African Americans, Consumption and Materialism from Reconstruction to the Civil Rights Movement, 7 ADVERTISING & SOC’Y REV., no. 1 (2006) (Abstract), available at http://muse.jhu.edu/login?uri=/journals/advertising_and_society_review/v007/7.1chambers.html (surveying African Americans’ encounter with material goods from the end of the Civil War through the end of the Second World War). Chambers describes consumption as a tool of anti-oppression:

[B]lacks have long understood the difference between materialism and a materially-intensive life and have used goods as a way to demonstrate their desire to be equal in every way with their fellow [white] citizens. Hence, consumption becomes a means of political and social activism on par with other better-known efforts such as the battle for voting rights or an end to racial discrimination.

Id.

136. See, e.g., Hannah Rosen, “Not That Sort of Women”: Race, Gender and Sexual Violence During the Memphis Riot of 1866, in SEX, LOVE, RACE: CROSSING THE BOUNDARIES IN NORTH AMERICAN HISTORY 267, 269-71 (Martha Hodes ed. 1999) (describing how white peoples’ resentment of black women and men entering leisure spaces and consuming luxury goods contributed to the tensions that sparked the Memphis Riot of 1866).
need to acquire “bling” even if the consequences are overspending and debt.

African Americans have also internalized the conspicuous consumer stereotype. Bill Cosby popularized it with his comment at the NAACP 50th anniversary celebration of *Brown v. Board of Education* that black parents are willing to spend five hundred dollars on a pair of sneakers for their children but won’t spend two hundred and fifty dollars to teach them to read with Hooked on Phonics.\(^{137}\) Similarly, E. Franklin Frazier attacked the black bourgeoisie in his bestselling book, and many other African American authors have identified profligate materialism and consumerism as problematic.\(^{138}\) Other stereotypes that interfere with blacks’ ability to obtain credit on fair terms are a belief in black intellectual inferiority that implies that money is worth more in a white (financially savvy) person’s hands and the association of African Americans with dishonesty and crime, leading to a view that black money is tainted.\(^{139}\)

Many low-income African Americans have a higher cost of living than whites at the same income levels. Companies target ‘urban consumers’ for the marketing of expensive products such as running shoes and hip hop style clothing. Low-income blacks living in poor neighborhoods also pay more for goods and services than people in other neighborhoods pay for identical goods, including basic food items.\(^{140}\) Many inner-city residents lack the means of transportation to shop for cheaper goods in other places, or cannot travel due to child care, time, or health issues.\(^{141}\) Transportation costs also may be prohibitive.


\(^{139}\) Austin, *supra* note 19, at 1218.

\(^{140}\) *See* Andrea Freeman, Comment, *Fast Food: Oppression Through Poor Nutrition*, 95 CAL. L. REV. 2221, 2240 (2007).

\(^{141}\) People working at more than one job to support a family are extremely unlikely to have time to travel to other neighborhoods to save money on a purchase, particularly one that is relatively urgent.
Finally, there is a dearth of formal and informal education and awareness within low-income communities about how to develop good credit and manage finances. While many community organizations have sought to promote and provide financial literacy through programs such as Los Angeles’ Operation Hope, these programs are by no measure widespread. Below, I propose that, under the Community Reinvestment Act, the government require large financial institutions to partner with local organizations to spread financial literacy throughout low-income communities of color. Ideally, financial education would begin in high school (or earlier) as standard curriculum in social sciences classes and become an integral part of participation in the financial system. Increased financial savvy likely would lead to a reduction in debt disparities by creating more sophisticated consumers that challenge existing stereotypes.

2. Latinos

The category of Latinos refers to a very broad spectrum of people living in the United States who have a wide range of interactions with the credit card industry. Many of the problems leading to debt disparities between Latinos and whites, such as language barriers, cultural differences, and the need to send remittances, apply much more strongly to immigrant than to native-born Latinos. Differences also depend on national origin. For example, Puerto Ricans share a financial culture with the United States but Cubans and Mexicans do not. Generally, there is a significant wealth gap between Latinos and whites, for which the following explanations of debt disparities may also partially account.142

Many Latinos lack credit history or have a bad credit history, for reasons explored below. A study revealed that twenty-two percent of Latino borrowers have no credit score as compared to only four percent of whites and three percent of African Americans.143 Individuals without credit scores receive fewer credit card solicitations, increasing the search costs of consumers who want a

142. See supra text accompanying note 109.
Bad credit histories lead to high interest rates which, in turn, make it more difficult for consumers to transfer balances to new cards with better rates and terms.

Latinos often suffer from misconceptions about how to develop good credit. For example, some Latinos obtain cards with the goal of building their credit but do not understand the impact that a bad credit score, caused by late payments, spending over the limit, or canceling accounts, have on future credit opportunities. According to the National Council of La Raza, the few financial education programs that have developed in Latino communities are often generic and offer limited distribution of materials.

Also, many Latinos are immigrants who are unfamiliar with the United States credit system and financial products, have cultural differences regarding finances, and/or face language barriers. The CARD Act mandated the Government Accountability Office to conduct a study of the effect of lack of proficiency in English on credit card use. The resulting report stated that most financial documents and financial educational materials in this country are available only in English; that the information and documents related to financial products are highly complex and confusing, even for native English speakers, and that there are significant problems with translation and interpretation from English to Spanish.

Latinos are less likely than whites to shop for a credit card. A fear of rejection also causes some Latinos not to apply or to reapply for cards. Countering this trepidation, the credit card companies

144. On the bright side, fewer solicitations, particularly of pre-approved cards, could reduce the temptation of acquiring cards for lifestyle users.
146. IBARRA & RODRIGUEZ, supra note 143, at 14.
147. CARD Act, § 513.
149. Only seven percent of Latinos who carry a balance reported card shopping as opposed to twelve percent of whites. IBARRA & RODRIGUEZ, supra note 143, at 7.
150. Id.
actively seek out Latino customers. All of the major credit card issuers invest money in advertising targeted directly at Latinos.\textsuperscript{151} They also manufacture affinity cards designed specifically for Latinos.

\textsuperscript{151} 2008 data from Nielsen Monitor-Plus revealed that credit card brands and issuers injected $15.2 million into Spanish television in 2008, $36.5 million in 2007, and $43.1 million in 2006. \textit{Hispanic Advertising: Credit Cards}, HISPANIC MARKET WKLY., Apr. 16, 2009, available at http://spanishypinfo.com/media/industry_snapshots/Hispanic_Advertising-Credit_Cards.pdf In 2008, credit card companies invested $6.7 million in spot television dollars, but only $1.6 in 2007. Id. In 2006, they invested $2.6 million in spot radio, and $1.1 million in 2007. Id. Visa was the number one advertiser in the Spanish-speaking market with $19.8 million in 2006 but only $26.3 in 2007. Id. The decrease was the result of a strategy shift from national media to local initiatives. Id. From 2005 to 2007, Visa increased its total ad expenditure in the market from $16.8 to 26.3 million. Id. Mastercard was the second biggest spender in 2005 and 2006 with $19.2 million. Id. In 2007 it was third after Chase with $6.8 million and in 2008 it left the national Hispanic networks and shifted to spot radio and television and magazines. Id. One of Mastercard’s more popular ads featured a luchador (Mexican wrestler) paying for a makeover with a Mastercard. Id. Mastercard also partnered with Chase and Telemundo to create a Latino-themed financial education tour that paired a financial expert with telenovela star Natalia Streignard in sessions designed to educate Latinos on finance and credit card use. Id. JP Morgan Chase emerged as a major investor in the Spanish-speaking market in 2006 and invested $7.8 million in 2007. Id. It subsequently retreated from the market in 2008 due to the credit crisis and its unplanned merger/acquisition of Washington Mutual. Id. It did, however, launch a Spanish website tied to its “Clear & Simple” advertising initiative at www.chaseclaroysimple.com. Id. The site provided financial tools to help customers manage their accounts to avoid fees, maintain good interest rates and protect their access to credit. Id. The bank also ran Spanish ads in LA to transition WaMu customers to Chase. Id. GE Money Bank was the only other company to invest more than $1 million in the Latino market by advertising a Wal-Mart money card and a prepaid Visa card and investing $1.7 million in network Spanish television and $53,400 in Spanish cable television in 2007, but it was not active in 2008. Id. Purpose Money MasterCard targeted African Americans and Latinos with less than perfect credit and invested $782,550 in the Spanish-speaking market in 2007 but vanished in 2008. Id. Citigroup invested $278,600 in advertisements in Spanish-language magazines and Bank of America ran spot television ads targeted at Latinos in 2008 and spent $187,120 in Spanish glossies. Id. HSBC created a website called ‘el banco local del mundo’ and in 2008 replaced its spot television ads with magazine ads, investing $40,000. Id. In 2008, many previous advertisers such as American Express, US Bank, Capital One, Discover, Wells Fargo bank, PNC Bank, Poder, and Amigomoney disappeared from the market, \textit{id.}, presumably in response to financial constraints caused by the recession.
with less desirable terms than the ones offered to white consumers. 152
Additionally, Latinos have greater vulnerability to credit card fraud. 153

Many immigrant Latinos also fall into credit card debt due to their obligation to send remittances to family members in their home countries. 154 At least thirty-five percent of remittance senders have a household income under twenty thousand dollars a year, and send fifteen percent of their earnings to their country of origin. 155 Their ability to do this reflects a choice to prioritize remittances over paying their own bills, thereby increasing their credit card debt. 156

3. Racial Discrimination

Although the Equal Credit Opportunity Act does not allow credit issuers to inquire about, inter alia, an applicant’s race or ethnicity, issuers can surmise an applicant’s identity through face-to-face encounters with walk-in customers, or make assumptions based on the applicant’s zip code or name. In 2006, the Boston Federal Reserve Bank published “Credit Card Redlining,” a study by Ethan Cohen-Cole comparing the terms of credit card agreements entered into by credit card owners with identical risk profiles and payment histories living in different areas. 157 The study revealed significant differences in credit card terms based on the racial makeup of the users’ neighborhoods. 158 The practice of redlining became notorious in association with the subprime mortgage crisis. Its use in the credit card industry is therefore not surprising. It is important to raise awareness of this practice in the credit card industry to generate opposition sufficient to support regulation to compensate for and eliminate it.

152. GONZALEZ, supra note 104, at 5.
153. 14.3% of Latinos are fraud victims compared to 6.4% whites. ANDERSON, supra note 20, at 55.
154. Undocumented immigrants, however, face barriers to entering the financial system, such as the lack of a social security number, that force them to deal only in cash.
156. Id. at 20.
158. Id. at 14-15.
A 2010 study also revealed significant racial discrimination in the consumer credit card market. This study appears to be the first of its kind, and highly accurate due to the use of multiple regressions. The study unveiled a significant negative effect on African Americans’ probability of owning a credit card, the number of cards they owned, the average credit line per card, and the likelihood of an issuer rejecting an application for consumer credit based on race. Latinos’ likelihood of owning a card and the number of credit lines per card were similarly affected. Issuers did not discriminate against Latinos in the initial application stage but gave them cards with less favorable conditions. The study also found a positive correlation between a higher negative net worth and the ability to get a credit card. While the study attributed this finding to the prevalence of young educated households with loans, it could also represent the industry’s targeting of low-income consumers who are more likely to pay late and have higher fees and interest rates. The study also found that black credit applicants benefit more from owning a house than white applicants, and from owning a car, having a job, having a higher income, and possessing a greater net worth. These statistics indicate that whiteness often serves as a proxy for creditworthiness.

All of the preceding explanations for racial debt disparities underscore the need for consumer protection. The following part evaluates the potential for existing protections to shield the most vulnerable communities from the industry’s deceptive, discriminatory, and exploitative practices.

II. CONSUMER PROTECTION

Two statutes, the Equal Credit Opportunity Act (“ECOA”) and the CARD Act, govern consumer protection in the American credit card
industry. The ECOA prohibits racial discrimination in the provision of credit and allows for a private right of action for violations of its provisions. The ability of defendants to account for their behavior with a ‘legitimate non-discriminatory explanation’ in these cases presents a significant obstacle to plaintiffs, however, and, in the unlikely event of a victory, available remedies are minimal. The ECOA’s deterrent effect is consequently nominal, particularly as to date no litigation against a credit card company for racial discrimination has been successful.

The CARD Act reverses some of the abuses of deregulation but focuses mainly on disclosure, a source of protection that has little effect on consumers without real choice in their financial providers or practices. Two contract law doctrines, unconscionability and good faith, could protect credit consumers who enter into contracts with significantly unfair terms if courts embraced racial discrimination as a symbol of unconscionability or bad faith. Remedies would, however, in most cases be limited. Courts have occasionally used contract law’s penalty doctrine to invalidate excessive late and over the limit fees in credit card class actions.

This part begins by analyzing the role of consumer protection in the context of racial debt disparities. Effective consumer protection for low-income African American and Latino consumers should not look the same as protection designed for white, middle-class consumers. It should also differ depending on whether the consumer is African American, Latino, monolingual Spanish-speaking, an immigrant, a lifestyle user, or a subsistence user. After identifying some specific needs of these distinct consumers, this part evaluates the usefulness of contract law. Next, it looks at the ECOA and explains why it provides inadequate protection from racial discrimination. Finally, it examines the CARD Act and concludes that the changes brought about by this amendment to the Truth in Lending Act largely bypassed the needs of consumers affected by racial debt disparities.

A. The Scope and Limitations of Consumer Protection

Most of the protection required to reduce racial debt disparities will benefit all credit card consumers. Consumer protection needs differ, however, for subsistence and lifestyle users, and for African Americans and Latinos. This section explores how these differences
affect policy concerns and shape the subsequent analyses and proposal.

The credit card industry’s creation of the subsistence user raises the question of whether people who previously would not have had access to credit have a right to maintain the access they presently have. The reforms proposed in this article, if implemented, would greatly reduce the profits credit card companies could generate from subsistence users, perhaps leading the companies to abandon these consumers altogether and revert back to more severe limitations on credit card issuance. Access to credit, however, should not be simply a matter of profit maximization and shareholder accountability. Consumer protection should ensure that both racial and economic justice inform policymaking in this area.

Credit cards offer consumers an anonymous and dignified manner in which to meet their expenses, and allow for creative financial juggling. Other sources of credit can be problematic, inconvenient, or insufficient. Bank loans usually require collateral. Borrowing from friends and families can create significant stress in interpersonal relationships, particularly as poor people tend to have poor friends and relatives. Pawn shops require the possession of valuable items and generally pay out only small amounts. Payday lenders often charge two hundred or three hundred percent interest, and installment purchases increase the price of goods considerably. Nonetheless, most low-income or subsistence users use a combination of all these types of borrowing to get by.

Subsistence users should be able to receive the benefits of credit card use that will allow them to avoid the consequences of insolvency, such as bankruptcy or homelessness. Credit card companies, in turn, should be able to compensate for the higher risk of default associated with low-income credit card users by charging appropriate interest rates and fees. The interest rates and fees presently levied, however, are disproportionate to costs and risks. Moreover, the practice of using race as a proxy for creditworthiness is both discriminatory and

167. Littwin, supra note 9, at 437.
168. See id. at 436; Martin, supra note 126, at 564.
169. Littwin, supra note 9, at 433-44.
170. For example, the average credit card interest rate of twenty percent is significantly higher than the prime lending rate and three times that of a home mortgage. Mercatante, supra note 91, at 50.
Consumer protection is therefore necessary to ensure equitable access to credit, reasonable rates and fees, and non-discriminatory lending.

The call by some academics for a return to a credit system that matches the amount of credit extended with the consumers’ anticipated ability to repay fails to take into account the potential negative consequences of this policy on the subsistence user. Creating law around this principle could plunge families who presently subsist through credit card use into crises that entail homelessness and hunger, which in turn can lead to the disintegration of families, loss of jobs and educational opportunities, and physical and mental illness. After actively encouraging low-income people to rely on credit cards for all of their expenses, it would be dangerous and unreasonable for the government or the industry suddenly to remove the ‘plastic safety net’ without substituting another means of providing for the purchase of necessities. Lifestyle users, on the other hand, might benefit from laws requiring funds lent to match an estimated future to pay, to the extent that these laws, while imposing on lower-income users significant limitations on their participation in society and greater hardship in coping with unexpected expenses, could prevent higher-income users from spiraling into debt due to the cognitive deficiencies described above.

Subsistence users also do not benefit from disclosure, which is currently the largest area of consumer protection outside of product safety laws, because they are not in a position to make meaningful choices about their credit card providers and use. Although many African American consumers bypass the formal credit card industry, receiving credit instead from institutions such as pawn shops and

171. See Ards & Myers, supra note 18.


payday loans, once a consumer has used formal credit, often in response to a targeted and usually pre-approved solicitation, she has no way to exit the system gracefully. Disclosure thus provides information that may alert the subsistence user to impending fees, rate increases, and debts, but offers no escape route. Subsistence users might, however, benefit from protections grounded in the contract law doctrines of unconscionability and good faith, if courts interpreted these doctrines to provide relief to the consumer who lacks bargaining power and consequently enters into an agreement with a credit card company that imposes unfair terms based on the consumer’s race or class.

In 1991, Ian Ayres conducted a study of the used car industry that revealed dramatic disparities in bargained prices depending on the race and gender of the consumer. The study showed that dealers made $362 in profit on the sale of a car to a white male, and $1,237 in profit on the sale of the same car to a black female using identical bargaining tactics. Attributing this significant difference to discrimination, Ayres remarked on the inability of market equilibrium to correct discrimination derived not from rational statistical inferences, but from irrational or stereotypical inferences, which are often self-reinforcing. For example, if a seller refuses to bargain with African American customers based on a belief that they are too poor to purchase a car, these customers will respond by making fewer purchases, thereby reaffirming the seller’s original mistaken belief. Ayres further emphasizes the importance of correctly identifying the

174. See Austin, supra note 19; Littwin, supra note 9.
175. Disclosure may lead a consumer to seek out a debt settlement industry that might, in some cases, provide limited assistance in consolidating and managing debt. See infra notes 195-196 and accompanying text.
176. Troutt, supra note 173, at 40 (“A norm of consumer fairness is more easily susceptible to empathic evaluation when the subject is the individual consumer seeking necessities and basic conveniences.”).
178. Id. at 828.
179. Id. at 842, 850.
180. Id. at 850-51.
nature of the discrimination to ensure that regulation arises from an accurate theory of market failure.\textsuperscript{181}

Ayres suggests reform in both civil rights and consumer protection laws.\textsuperscript{182} First Ayres argues that 42 U.S.C. §§ 1981 and 1982, laws that apply to private citizens and provide that non-whites and whites have the same rights to make and enforce contracts and purchase personal property, prohibit racial discrimination in the retail context.\textsuperscript{183} Ayres acknowledges, however, that the required showing of intentional discrimination would preclude most suits under these sections.\textsuperscript{184} Ayres thus proposes “modernized versions” of these sections that would allow plaintiffs to use disparate impact to prove discrimination.\textsuperscript{185}

Ayres also suggests “reinvigorating” consumer protection laws by reconceptualizing definitions of unfair and deceptive practices to encompass equal racial treatment as an implied representation.\textsuperscript{186} Ayres supports this argument with his assertion that the Supreme Court, in \textit{Patterson v. McLean Credit Union}, implied that consumers could read nondiscrimination provisions into state contract remedies.\textsuperscript{187} Ayres further proposes government-mandated reforms to the used car industry, including prohibition of high mark-up sales under a strengthened notion of unconscionability, restrictions on the amount of permissible price dispersion, and disclosure to consumers of information such as the average price of each make of car.\textsuperscript{188}

Ayres’ work informs the present analysis because discrimination in the used car industry based on race and gender has several important elements in common with racial disparities in credit card debt. Statistically, African Americans, Latinos, and women pay the highest interest rates and fees to credit card companies, just as African Americans and women pay the highest prices for used cars.\textsuperscript{189} Studies

\begin{enumerate}
\item Id. at 852.
\item Id. at 857.
\item Id. at 858.
\item Id. at 858-63.
\item Id. at 863-64.
\item Id. at 866.
\item Id. at 867.
\item Id. at 868-870.
\item Wheary \& Draut, \textit{supra} note 14, at 6.
\end{enumerate}
demonstrate that these disparities are attributable at least in part to discrimination on the part of the credit card issuers. While the issuers may believe this discrimination is rational, it is likely that they are in fact mistaken about the creditworthiness of many black consumers who receive and agree to unfair terms based on a shared but incorrect belief that blacks do not have good credit, and stereotypes that portray African Americans as financially irresponsible.

Without Ayres’ investigation into and documentation of a pattern of discrimination, these disparities would have continued and appeared to be merely reflections of negotiations between individual buyers and sellers. The documentation of racial debt disparities in the credit card industry is similarly an integral step towards recognizing and reducing these disparities. Because companies will not initiate documentation on their own, however, the government must compel it. I therefore recommend below that the Consumer Financial Protection Agency require disclosure of credit card issuers’ practices and policies and report findings of discrimination to the public.

Latinos require specific protection based on their disproportionate victimization through credit card fraud. Criminal divisions investigating identity theft and fraud should focus special attention on this phenomenon to reduce this disparity. Immigrants also need protection from discrimination based on a lack of English proficiency, relative unfamiliarity with American financial culture combined with the habits of financial customs learned in their countries of birth, as well as stereotypes and hostility towards immigrants.

Both African Americans and Latinos may turn to the debt settlement industry to alleviate unmanageable debt. Consumers must heed the difference, however, between credit counselors, which are often funded by the credit card companies and consequently serve

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190. See supra notes 15-16 and accompanying text.
191. Ards & Myers, supra note 18, at 255.
192. See Austin, supra note 19, at 1218-20.
193. See ANDERSON, supra note 20, at 55.
194. See generally Steven W. Bender, Consumer Protection for Latinos, 45 AM. U. L. REV. 1027 (1996); GONZALEZ, supra note 104.
their interests, and debt settlement companies that can sometimes negotiate with the credit card companies to discharge the consumer’s debt in exchange for a lump sum payment.\textsuperscript{196} This lump sum payment may, however, may simply represent the foregoing of payment of other bills, a practice that ultimately harms the consumer. Consumers should thus be wary of all forms of debt settlement.

Although many small adjustments of consumer protection law could lead to incremental improvements, broad strokes are necessary for significant change, and the current financial climate demands immediate reform. The following section evaluates the potential of existing laws to reduce debt disparities.

\textbf{B. Contract Law}

\textit{1. Unconscionability}

To void a contract or some of its provisions on the basis of unconscionability, a court must find “an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party.”\textsuperscript{197} The doctrine has two

\textsuperscript{196} Credit counseling companies are nonprofit organizations authorized to receive sizable “grants” from various donors under the United States Tax Code. Derek S. Witte, \textit{The Bear Hug That Is Crushing Debt-Burdened Americans: Why Overzealous Regulation of the Debt-Settlement Industry Ultimately Harms the Consumers It Means to Protect}, 14 TEX. REV. LAW & POL. 277, 285 (2010). A substantial amount of the grant money paid to national credit counseling companies comes directly from credit card companies. \textit{Id.} The credit counseling process provides the credit card companies access to debtors’ spending habits. \textit{Id.} Credit counselors encourage debtors to make automatic payments directly from their checking accounts, without offering discharge or debt reduction in exchange. \textit{Id.} at 285-86. Approximately one-half of the debt management plans drafted by credit counselors fail after six months, and some debtors agree to pay more disposable income to creditors than they actually have. Robert M. Hunt, \textit{Whither Consumer Credit Counseling?}, BUS. REV., Fourth Quarter 2005, at 13, available at http://www.philadelphiafed.org/research-and-data/publications/business-review/2005q4/Q4_05_ConsumerCounsel.pdf. Credit card companies are often willing to discharge a consumer’s debt in exchange for a lump sum payment totaling far less than the amount owed. Witte, \textit{supra}, at 287-88. Debt-settlement companies, on the other hand, enter into adversarial negotiations with credit card companies to reduce or discharge consumer debt. \textit{Id.}

\textsuperscript{197} Williams v. Walker-Thomas Furniture Co., 350 F.2d 445, 449 (D.D.C. 1965). For an interesting article on the assumption that Ora Lee Williams was black
components. Procedural unconscionability is unfairness in the process by which the agreement was reached, and substantive unconscionability is unfairness in the agreed upon terms.\textsuperscript{198} Both must ordinarily be present for a court to find unconscionability.\textsuperscript{199} Procedural unconscionability usually takes one of two forms. In one version, the powerful party exploits the other party’s lack of knowledge by denying that party a reasonable opportunity to understand the contract’s terms because of deliberately obscure or buried terms or the individual’s lack of education.\textsuperscript{200} A lack of proficiency in the contract’s language could also lead to this type of procedural unconscionability.\textsuperscript{201} The other type of procedural unconscionability involves a lack of voluntariness arising from grossly unequal bargaining power, where one party cannot meaningfully negotiate the contract’s terms.\textsuperscript{202} “[I]t is possible for a contract to be oppressive taken as a whole, even though there is no weakness in the bargaining process and no single term which is in itself unconscionable.”\textsuperscript{203}

Originally a common law doctrine, unconscionability was codified in the UCC and is present in several state laws. The UCC provides:

If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it

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199. \textit{Id. But see id.} n.142 (noting a possible exception where substantive unconscionability can be sufficient).

200. \textit{Id.}

201. \textit{Id.}

202. \textit{Id.}

may so limit the application of any unconscionable clause as to avoid any unconscionable result.\textsuperscript{204}

Neil Williams argues that, because victims of racial discrimination often lack knowledge and voluntariness when negotiating contracts, the unconscionability doctrine is well-positioned to assume the task of generally prohibiting racial discrimination in contract formation.\textsuperscript{205} Steven Bender also asserts that unconscionability can be a useful doctrine to protect Spanish-only speakers in the marketplace, and points to a line of cases, primarily from the 1960s and 1970s, that have applied it to this effect.\textsuperscript{206} Bender recognizes its limited effectiveness, however, based on courts’ reluctance to award restitution or punitive damages after a finding of unconscionability.\textsuperscript{207} Additional considerations lead to the conclusion that the doctrine is not likely to be useful in reducing racial debt disparities.

Dante David Troutt identifies several problems with the unconscionability doctrine as applied to low-income people of color. The doctrine depends on the perception of the low-income consumer as an “economic victim, rather than an actor.”\textsuperscript{208} But the consumer may actively and consciously agree to an unconscionable or unfair deal based on her misperceptions of her own worth arising from her class status,\textsuperscript{209} or learned cultural stereotypes. These stereotypes include, for African Americans, associations with crime that leads to the possession of tainted money and lack of financial acuity such that white hands must touch money before it becomes valuable.\textsuperscript{210} A long history of exclusion from mainstream financial markets could also lead to acceptance of undesirable terms upon entry.

Another potential problem with using unconscionability to protect consumers from racial discrimination in contract terms is that,

\begin{footnotesize}
\begin{enumerate}
\item U.C.C. § 2-302 (2003).
\item Williams, supra note 198, at 204-05.
\item Bender, supra note 194, at 1040-42.
\item Id. at 1042.
\item Troutt, supra note 173, at 33.
\item Id. at 34-35 (citing Jeffrey Harrison, Class, Personality, Contract, and Unconscionability, 35 WM. & MARY L. REV. 445, 491-92 (1994)).
\item Austin, supra note 19, at 1250-51.
\end{enumerate}
\end{footnotesize}
although ideally it should deter only unscrupulous lenders, it could have the unintended effect of creating reluctance to extend credit card agreements to African Americans and Latinos, thereby significantly restricting their purchasing power and right to enter into contracts, as well as their ability to engage in certain transactions that require a credit card such as car rentals and the purchase of some plane tickets. Further, at least in the seminal Walker-Thomas Furniture case, a finding of unconscionability did not deter the company from exploiting legions of future customers. On balance, the minimal nature of its remedies and deterrence effect along with its potential psychological and financial harmfulness render unconscionability inadequate as a form of consumer protection in the context of racial disparities in credit card debt.

2. Duty of Good Faith and Fair Dealing

“Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.” “Community standards of decency, fairness or reasonableness” define good faith. This fluid standard lends itself well to the proposition that racial discrimination constitutes bad faith. Good faith could therefore provide a viable alternative to antidiscrimination statutes, particularly in the credit card context, where the ECOA has failed to provide relief to almost all plaintiffs. The primary obstacle to recovery under this doctrine is a lack of precedent. Neil Williams points, however, to two cases, Reid v. Key Bank of Southern Maine, Inc. and Ricci v. Key Bancshares of Maine, Inc., that equate racial discrimination with bad faith. Williams further argues that good faith can reach a

211. DOROTHY BROWN, CRITICAL RACE THEORY 141 (2d ed. 2003) (asking the question).
214. Id. cmt. a.
215. 821 F.2d 9 (1st Cir. 1987).
217. Williams, supra note 195, at 218-20 (citing Reid, 821 F.2d at 15-16 (court of appeals allowed finding of bad faith based on “ulterior considerations,” including racial prejudice); Ricci, 662 F. Supp. at 1138, 1141 (jury found the same
broader range of discriminatory acts than the ECOA because it does not require a showing of either intent or motive.  

Anne-Marie Harris, in a study of racial consumer profiling, contends that Williams’ optimism about the movement of contract law towards protecting consumers against racial discrimination in the “formation, performance, enforcement, or termination of a contract” may be premature. Harris’ skepticism seems appropriate in light of the lack of progress in this area after Reid and Ricci. Thus, while the doctrine of good faith has the potential to provide an avenue for relief for consumers carrying disproportionate amounts of debt in the future, it is not presently useful.

3. Penalty

Contract law’s penalty doctrine precludes the imposition of damages that exceed the true harm to the injured party, or a reasonable estimate of that harm. Two courts have used the doctrine to hold late and over-the-limit fees to be illegal liquidated damages in class action suits against banks. These types of fees often appear to be disproportionate to the cost incurred by credit card issuers, particularly in cases where a thirty dollar late fee applies to a payment that is only hours or days late on a balance that may be only a few hundred dollars. An obstacle to widespread use of this doctrine to deter excessive fees, however, is the difficulty of calculating the true cost of damages to the credit card issuers. It is therefore unlikely that this doctrine, as with the others explored above, will have a significant impact on racial debt disparities.

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218. Id. at 228.
222. Bar-Gill, supra note 7, at 1425.
4. Reforming Credit Card Contracts

Extensive work on the contract-based problems with credit card agreements has generated numerous suggestions for reforms. Adam Levitin and Roger Mann advocate for the standardization of most credit terms, which would allow consumers to shop for a card based on actual differences between cards on the terms that matter most to them, thereby increasing competition. Credit card agreements in their present form do not allow even the most sophisticated consumer to be able to understand or even read their contents, due to the complex language, small and voluminous print, and complicated structure (agreements often consist of several different documents, often mailed separately). Further, Oren Bar-Gill and Elizabeth Warren assert that the ease with which lenders can change the terms of their product at low cost by simply printing and mailing a new form, especially after a customer uses the product, renders credit cards dangerous to consumers.

Simplifying the language of credit card agreements and increasing market competition by reducing the number of negotiable terms would undoubtedly benefit consumers that would then be more equipped to make wiser choices about their credit card providers and terms. These changes likely would not alter racial debt disparities, however, because credit card issuers would continue to penalize low-income consumers with high interest rates and fees. Any improvement in credit card terms resulting from increased competition would likely affect only middle or higher-income users.

C. The Equal Credit Opportunity Act

The Equal Credit Opportunity Act provides that it is unlawful “for any creditor to discriminate against any applicant, with respect to any
aspect of a credit transaction on the basis of race.” 226 The Act defines an adverse action as “a denial or revocation of credit, a change in the terms of an existing credit arrangement, or a refusal to grant credit in substantially or on substantially the terms requested.” 227 The definition does not include “a refusal to extend additional credit under an existing credit arrangement where the applicant is in delinquent or otherwise in default, or where such additional credit would exceed a previously established credit limit.” 228 An applicant who suffers an adverse action is entitled to a statement of specific reasons for the action by the creditor. 229

The regulations, promulgated by the Federal Reserve, also state that a creditor may not discourage prospective credit applicants from applying based on a protected ground. 230 A creditor may not inquire about a person’s race or national origin in relation to a credit transaction (including persons other than the applicant), but may inquire into an applicant’s permanent residence or immigration status. 231 The regulations allow for the existence of “special purpose credit programs” where a creditor may extend credit to a class of persons who otherwise likely would not receive such credit or would receive it on less favorable terms. 232 For the purposes of establishing eligibility for one of these programs, creditors may inquire into otherwise prohibited areas, such as race and national origin. 233


227. § 1691(d)(6).

228. Id.

229. § 1691(d)(2)(3).


231. § 202.5(e).


233. § 202.8(b)(2).
If an individual suspects that a credit issuer has violated her rights under the ECOA, she may complain to the creditor, ask the state attorney general’s office for advice, sue the creditor in federal court individually or as part of a class action, and/or report violations to the appropriate government agency.\textsuperscript{234} In the event of a suit, the ECOA allows for actual damages, punitive damages, equitable relief, and attorneys’ fees.\textsuperscript{235} ECOA cases adhere to the same standards as cases brought under Title VII.\textsuperscript{236} Plaintiffs without direct evidence of discrimination must therefore follow the analysis established in \textit{McDonnell Douglas Corporation v. Green}.\textsuperscript{237} This test first requires the plaintiff to establish a prima facie case of discrimination, and then shifts the burden to the creditor to proffer a legitimate non-discriminatory reason for its actions.\textsuperscript{238} After this showing, the burden shifts back to the plaintiff to establish that this reason is in fact pretextual, and that illegal discrimination provided motivation for the adverse action.\textsuperscript{239} Plaintiffs may proceed under a disparate impact theory, which allows the use of statistics to establish a prima facie case.\textsuperscript{240}

As of the beginning of 2011, there were two ECOA investigations into national origin discrimination against Latinos by credit card issuers that resulted in settlements. In the first case, plaintiffs alleged that Associates National Bank (“ANB”) discriminated on the basis of national origin by requiring higher credit scores for applicants using a Spanish-language application form; offered lower credit limits to approved Spanish-language applicants; and failed to offer favorable

\begin{thebibliography}{99}
\bibitem{235} 15 U.S.C. §§ 1691e(a)-(c), 1691(d).
\bibitem{236} \textit{See, e.g.}, Hood v. Midwest Sav. Bank, 95 Fed. App’x 768, 777-78 (6th Cir. 2004).
\bibitem{237} 411 U.S. 792 (1973).
\bibitem{238} \textit{Id.} at .802.
\bibitem{239} \textit{Id.} at 804-05.
\end{thebibliography}
credit promotions to Spanish-language account holders. After a year of discovery, Citigroup acquired ANB and settled with the plaintiffs, a class of several hundred individuals, for $1.5 million in 2001. In 2002, Fidelity federal bank settled with plaintiffs who alleged that it engaged in abusive collection practices in its subprime credit card program that harassed customers based on their “Hispanic national origin.” Fidelity paid out $1.6 million to victims of its ECOA violations and agreed to fund a consumer education program.

These two settlements have not so far led to subsequent successful race or national origin suits against credit card issuers. A new development that may increase the likelihood of future successful cases, however, is the fairly recent appearance of studies documenting discriminatory practices, such as the Boston Federal Reserve redlining


242. Id.


244. Id.

report and Chi Jack Lin’s study of racial discrimination in the credit card industry, which could help future plaintiffs establish a prima facie case based on a disparate impact theory. This paper calls, for several reasons, for documentation and disclosure of racially discriminatory practices by credit card companies. The documentation itself should serve to deter discriminatory practices, as well as possibly increase plaintiffs’ chances of obtaining relief under the ECOA. Even with documentation, however, a radical increase in successful suits is unlikely, because the McDonnell Douglas standard allows corporations to justify almost all practices as legitimate business decisions and, in the context of Title VII, overwhelmingly favors corporations over individuals.

The ECOA, in addition to prohibiting discrimination in credit transactions on the basis of race, color, and national origin, provides relief for discrimination based on gender, marital status, age, religion, and the exercise of the rights it incorporates. Despite all of this protection, it has led to almost no victories for plaintiffs. Interestingly, one of the two published cases resulting in a win for the plaintiff entered judgment for a white male who offered direct evidence of discrimination based on the Farmers Home Administration’s denial of his application to purchase property under a program for socially disadvantaged applicants because the plaintiff was white. The second case involved the denial of a Federal Housing Act loan to an African American couple without explanation.

To date, racial discrimination has cost credit card companies almost nothing. Even if documentation of discriminatory practices facilitates a slightly increased number of successful ECOA suits, these

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246. See supra notes 15-16 and accompanying text. However, a 1980 attempt to establish a prima facie case of racial discrimination based on redlining against the issuer of a gasoline credit card company failed in part due to the complexity of the credit grading system and the lack of information about the common characteristics of the hypothesized applicant pool in the plaintiff’s zip code. Cherry v. Amoco Oil Co., 490 F. Supp. 1026, 1030-31 (N.D. Ga. 1980).


suits remain unlikely to have a significant financial impact on credit card companies, although they have some potential to cause reputational harm. The ECOA’s value is thus largely as a symbol of the principle of antidiscrimination in the context of consumer credit. It is unlikely to serve as a vehicle for the meaningful reduction of racial disparities in credit card debt.

D. The Credit CARD Act

The 2009 CARD Act imposed some significant limitations on the credit card companies’ practices. The new restrictions affect consumers differently according to their status as credit card users. Significantly, credit card issuers responded to the bill by finding new ways to generate profits, often from its lowest-income customers, such as through exorbitant processing fees on new cards. This section describes and evaluates the most significant changes created by the bill as they affect low-income African American and Latino credit card consumers. While there is some cause for optimism with regard to potential changes improving services to consumers lacking English proficiency, the CARD Act for the most part is not likely to reduce current debt disparities in any significant way.

The CARD Act prohibits the use of universal default, a practice that previously allowed a change in an individual’s credit score to lead to increased interest rates on all of that individual’s credit cards, even though the score increase resulted from an action unrelated to most of the consumer’s accounts.252 The change in score could result, for example, from one late payment on one card or the addition of new mortgage or car payments. Most consumers were unaware of this practice and, even if they were aware of it, in many cases could do nothing to prevent its pernicious effects, as most consumers do not make late payments or incur additional expenses if they can

250. Some provisions, such as a ban on inactivity fees, are not relevant to the users who are the focus of this Article.


252. See Nelson, supra note 172, at 5 & nn. 15, 17 (citing CARD Act § 101(b)).
reasonably avoid doing so. The ban on universal default is a positive change that increases consumer protection for all credit card users.

To reduce fees resulting from consumers unwittingly exceeding their credit limits, the CARD Act established an opt-in procedure that requires consent to the extension of credit beyond pre-set limits with an accompanying charge for the privilege. This provision does little to help the subsistence consumer, who must choose to exceed her limit when necessary for survival. It does, however, increase lifestyle users’ awareness of the consequences of their purchases and allow them to make more informed choices regarding the value of their purchases based on their true costs.

Another significant aspect of the CARD Act is the imposition of disclosure requirements. Credit card bills now communicate to the user the effects of a minimum payment by clearly stating how long it will take to pay off the principal if the consumer chooses only to make a minimum payment. This notification appears next to the number representing the minimum payment required on the bill in reasonably-sized print. This change has the capacity to influence the behavior of lifestyle users who could choose to make fewer purchases and put more money towards increased payments based on their awareness of the extent of their debt commitment arising from their existing balance. It is unlikely to alter the purchasing choices of subsistence users.

The CARD Act identifies several groups that might require unique protections. One of these, consumers with limited proficiency in English, represents some consumers identified as Latino, although it is unclear how large this group is. The Government Accountability Office (“GAO”) produced a report, mandated by the CARD Act, describing the likely impact of lack of English proficiency on credit card use. It reported significant barriers to financial literacy due to lack of availability of documents and education materials, the complexity of translated documents, problems with interpretation done by minor children, cultural

253. See id. (citing CARD Act § 101(a)).
254. CARD Act, § 201.
255. See id. tit. III (focusing on protection of underage consumers and college students); id. § 513 (mandating investigation of “the relationship between fluency in the English language and financial literacy”).
256. GAO REPORT, supra note 148.
differences in regard to financial norms, and a negative view of carrying debt in some countries that would prevent consumers from establishing a credit history.\footnote{257} Responses to these identified problems, if implemented, likely would contribute to a reduction in debt for affected consumers. It remains to be seen, however, whether Congress will incorporate them into future iterations of the CARD Act.

One of the disclosure provisions of the CARD Act compelled the Federal Reserve to create an online database listing the terms and conditions of more than three hundred credit card issuers, with the goal of assisting consumers in finding a card that meets their personal financial needs.\footnote{258} This database responds in part to the finding that Latinos are less likely than any other group to shop for credit cards.\footnote{259} The database in its current form is unlikely to increase or facilitate credit card shopping, however, because the language of the agreements is overly technical and complex. Nonetheless, the publication of the database has brought these issues to the attention of consumer advocates who may be able to wield sufficient pressure on the credit card companies to develop agreements with clearer, more user-friendly terms.\footnote{260} Until that occurs, Internet-savvy consumers can bypass the arduous task of sifting through the information in the database by going to a website called lowcards.com that identifies the best terms in the different cards.\footnote{261} The ability of this site to reach and help low-income consumers depends on access to the Internet, awareness of the site’s existence, and the availability of choice in the selection of a card.

Consumer advocates, including at least one senator and house representative, have criticized the CARD Act for some of its more glaring omissions.\footnote{262} Many lobbyists have called for a cap on interest

rate hikes. Senator Carl Levin co-sponsored a bill that would impose a cap at seven percent; other advocates seek a cap of thirty-six percent.\textsuperscript{263} Noting that late fees of thirty-five dollars incur on accounts regardless of their balances and that these fees bear no relationship to the actual cost of default, advocates have also called for a cap on these fees.\textsuperscript{264} They have additionally singled out twelve to fifteen dollar fees for telephone or electronic payments as particularly unfair.\textsuperscript{265}

In response to the CARD Act, the National Consumer Law Center has created a list of eleven features of a safer credit card.\textsuperscript{266} They are: a single, reasonable interest rate for all balances with no penalty rate increases; few and modest fees that cover relevant costs but are not hidden profit centers; hard credit limits that cannot be exceeded; stable, convenient payments that quickly reduce debt; simple grace period and payment rules; lending based on ability to repay; no dangerous deferred interest plans; no co-signer surprises; agreements that change only with mutual consent; simple, clear terms that meet expectations; and compliance with the law and access to justice.\textsuperscript{267} Implementation of these features would create a generally safer credit card but, as discussed above, not necessarily improve the circumstances of subsistence users or reduce racial debt disparities. The next iteration of the CARD Act must identify racial debt disparities as a significant problem in the industry, one requiring immediate study and swift action in response. Every day that passes without reform directed at low-income African American and Latino consumers can lead to another family falling into bankruptcy or facing other economic and social perils.

The following section proposes a sweeping reform that would quickly and dramatically reduce debt for a large number of consumers. It also offers a less radical proposal that would begin to

\begin{flushright}
\url{news/what-new-credit-card-rules-dont-cover-1282.php}.
\end{flushright}
implement structural reform and increase awareness of credit cards companies’ complicity in racial debt disparities. Most importantly, it calls for disclosure of the credit card industry’s practices, profit sources, and policies as an initial step to effective regulation.

III. TWO PROPOSALS AND A CALL FOR DISCLOSURE OF INDUSTRY PRACTICES

“The legal foundations of consumer credit reflect the ideology of neoclassical theory: a rationally informed individual allocating income intertemporally to maximize utility. Reality differs.” Due to the strong incentives the credit card companies have to continue to pursue their present business model, including the vast profitability of revolving balances and new competition in the market for payment devices, legislation is necessary to change the structure of the industry in a way that will reduce racial debt disparities. The Truth in Lending Act, as encompassed in its name, relies primarily on disclosure to restore fairness to the credit lending process. Disclosure to consumers is, however, largely ineffective for several reasons. First, research shows that most consumers cannot understand financial documents, even ones that are far less complex than a credit card agreement. Second, even if terms are communicated in simple language, consumers will not change their behavior based on disclosure if they believe, as the theories described above assert, that they will not borrow or over-borrow. Disclosure is highly unlikely to overcome cognitive biases and distortions.

Industry disclosure to the government that is publicly available, however, is essential. The Bureau of Consumer Financial

268. Watkins, supra note 12, at 419.
269. MANN, supra note 28, at 134.
270. Bar-Gill, supra note 7, at 1418 (“Knowledge of credit terms is meaningless if the consumer mistakenly believes that she will not borrow.”)
271. See Sunstein, supra note 153, at 258-59 (“The strategy of ‘provide more information,’ favored on standard economic grounds, should be helpful when people merely lack knowledge; but as a response to biases and self-control problems, it is most likely to be inadequate.”).
Protection should require all credit card companies to disclose how they generate their profits, which consumers they target with pre-approved offers, how they identify these consumers, and what terms they offer to different consumers. In other words, credit card issuers should make a full accounting of their products and processes. Interpretation of this information should include an appraisal of whether the issuer engages in racially discriminatory practices. Public disclosure of profits, policies, and practices would in itself likely lead to reform.

Slavery disclosure laws provide an excellent example of the power of public disclosure. Some states and cities require corporations to disclose past ties to slavery to become eligible for government contracts and other work. Although the laws only punish failure to disclose and not the ties themselves, disclosure has led in many cases to corporate investment in low-income African American communities and boycotts of complicit banks. Disclosure of inequitable practices in the credit card industry could similarly lead to community investment and a public demand for change, even though credit card victimization does not provoke the same moral outrage that slavery profiteering does. The states and cities that enacted the slavery disclosure laws might be the most open to introducing similar requirements for credit card issuers.

Disclosure is an essential first step to regulation. Cass Sunstein favors regulation responding to market failure in the credit card

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274. Eight major cities (Berkeley, Chicago, Detroit, Los Angeles, Milwaukee, Oakland, Philadelphia, and San Francisco), and three states (Iowa, Illinois, and California) have some type of slavery disclosure laws. Although these laws require only research and disclosure, the results have led to some voluntary payments to low-income African American communities. Both J. P. Morgan and Wachovia made sizable contributions to community organizations. Jason Levy, Note, Slavery Disclosure Laws: For Financial Reparations or for ‘Telling the Truth’?, 2009 COLUM. BUS. L. REV. 468, 472, 473, 516 (2009).

industry that maintains consumer choice. An example of this would be the use of default provisions in credit card agreements, which a consumer can opt not to use. Sunstein concedes, however, that “prohibitions on voluntary agreements might be justified, at least if the aggregate benefits exceed the aggregate costs.”

He describes the “very structure of [the credit card] market” as one that “lead[s] many companies to appeal to bounded rationality, rather than to attempt to counteract it.” Recognizing the “perverse system of redistribution, from less wealthy people who maintain debt to relatively wealthy people who pay on time,” Sunstein asserts that usury laws, which he labels a form of strong paternalism, might be appropriate because of their potential to restructure the credit card pricing system in the same way that the market would absent cognitive and psychological barriers such as myopia, cumulative cost neglect, and unrealistic optimism.

Usury laws have been used to protect consumers from exploitation for centuries, and their recent unpopularity in the United States is a reflection of the power of big banks and corporations over individual consumers.

In “Making Credit Safer,” a paper that successfully argued for a federal consumer protection agency, Oren Bar-Gill and Elizabeth Warren explain in detail how the credit card market has failed, and

276. See Sunstein, supra note 33, at 251.
277. Id. at 267.
278. Id. Bounded rationality in the credit card context refers to excessive borrowing that leads to financial distress.
279. Id. at 267-69.
280. See Timothy A. Canova, The Transformation of U.S. Banking and Finance: From Regulated Competition to Free-Market Receivership, 60 BROOK. L. REV. 1295, 1336 n.136 (1995). (“For many centuries, lending at high interest rates has been considered morally indefensible, violating religious dictates and the laws of civil society. See, e.g., The Bible: Exod. 22:25; Neh. 5:7; Prov. 28:8; Lev. 25:36; Ps. 15:5; Ezek. 18:08, 18:13, 18:17, 22:12; Matt. 6:12, 18:27, 18:30, 18:32; see also The Koran (N.J. Dagwood trans., 4th ed. 1974): Sura II:276, III:130, XXX:39; The Politics of Aristotle 29 (Ernest Barker trans., 1978). In acknowledging the primary purpose of money ‘as a means of exchange’ Aristotle also recognized that ‘usury’ (the charging of interest) tries to make money increase as though it were an end in itself. ‘The trade of the petty usurer,’ said Aristotle, ‘is hated most, and with most reason: it makes a profit from currency itself, instead of making it from the process (i.e. of exchange) which currency was meant to serve.’ Id. at 28-29.)
identify the high social costs of this failure. Bar-Gill and Warren are conscious of distributional concerns, recognizing that African Americans, Latinos, and women have greater disadvantages in the credit market, and that previous legislation likely benefited only well-educated, affluent borrowers. Legislation specifically designed to alleviate these distributional concerns and reduce racial debt disparities is long overdue. Below I make two such proposals. The first would have a significant impact on credit card issuers’ bottom line and require dramatic restructuring of their present business model. Its implementation in the near future is therefore highly unlikely. Nonetheless, it may serve as an ideal that makes room for bolder legislation by expanding the spectrum of possibilities. The second proposal, despite its roots in reparations theory, is far less controversial because it attempts to remedy universally-recognized wrongs perpetrated by credit card issuers, and will not compromise either their business model or financial integrity. In an ideal world, the implementation of both of these proposals would effectively eliminate racial disparities in credit card debt.

A. A Proposal for Subsistence Amnesty

Although the CARD Act in its present incarnation has very limited impact on the debt disparities between whites and African Americans and Latinos, an amendment eradicating fees and interest rates on subsistence purchases by consumers living under the poverty line, or ‘subsistence amnesty’, could lead to a significant reduction in these disparities, in addition to benefitting low-income consumers across racial lines. Special protection for a specific group of credit consumers is not without precedent. For example, the John Warner National Defense Authorization Act for Fiscal Year 2007 imposed a thirty-six percent annual interest rate cap on certain types of consumer loans to military borrowers. This amendment came in the wake of scholarly arguments in favor of enhanced protection from predatory

281. See Bar-Gill & Warren, supra note 5. Bar-Gill and Warren argue persuasively in this article for the creation of a federal regulatory body to oversee consumer credit products. See id. at 98-100.

282. See id. at 64-69.

lending for military personnel. Legal scholars have also made persuasive arguments for regulation to protect vulnerable populations such as students and the elderly from abuses by the credit card industry, and to eliminate barriers to credit for ex-offenders. The CARD Act responded to concerns about student borrowing by implementing targeted restrictions on credit card agreements with students. Military personnel, students, the elderly, and ex-offenders include some low-income African Americans and Latinos, and increased consumer protection for these groups might lead to a slight decrease in racial debt disparities. In light of the disparities directly associated with race and class, however, it is necessary to enact protections beyond those proposed or implemented to assist those four groups.

Subsistence amnesty would represent a significant reduction in profits for the credit card companies, which have already seen substantial losses attributable to the first incarnation of the CARD Act. Many of these profits, however, derived from discrimination and the exploitation of consumers’ weaknesses and vulnerability. Competition has failed to reverse the injustice perpetrated by the industry, and society has borne its costs. Values of social welfare, fairness, and equality support legislation that comes at a cost to credit card shareholders but restores some measure of social and economic equilibrium. Large companies should not build their fortunes on the backs of the citizens possessing the fewest resources and the least societal power. Racial discrimination and subordination are unacceptable. These are non-controversial principles that the present


286. See CARD Act, tit. III.

regulatory system violates. Because companies will not self-regulate discriminatory and unjust practices primarily due to shareholder obligations and managerial elite’s desire to strive to maximize compensation, the government must intervene. Social welfare legislation in this area is both essential and appropriate.\footnote{288}

The poverty line, although arbitrary, would serve as a reasonable cut-off point for purposes of this law. The 2009 poverty guidelines for the forty-eight contiguous states and the District of Columbia are $22,050 for a family of four, $14,570 for a couple or family of two, and $10,830 for an individual.\footnote{289} Government programs that use these guidelines include Head Start, the Food Stamp Program, the National School Lunch Program, the Low-Income Home Energy Assistance Program, and the Children’s Health Insurance Program. To alleviate the more dramatic losses that subsistence amnesty would entail, it could incorporate some compensation and protection for the credit card companies in the form of tax breaks and mandated minimum payments supported when necessary by government programs.

The intent of subsistence amnesty is not to create a public welfare system out of the credit card industry. Instead, it seeks to institute temporary relief from debt accumulation that would allow for some reduction in debt disparities and the restoration of credit cards to their previous role as financial tools for convenience or pleasure, not for redistribution of wealth from the poor to the coffers of large corporations. It would be reasonable to attach a time limit to this law that allows for re-evaluation, with an eye to creating better government support for low-income families that will allow them to relinquish dependence on exploitative credit systems, both formal and informal. After a period of respite, credit card issuers could reinstate the eliminated interest rates and fees, adjusted to reflect true costs and risks.

The next section proposes amendments to the Community Reinvestment Act that would bring much-needed financial counseling into underserved areas, provide opportunities for low-income

\footnote{288. If the industry cannot construct a profitable business model that is not exploitative, it may simply cease to exist. Although its absence could create consumer credit problems, the alternative is likely to be an improvement over the current system. \textit{See, e.g.}, Littwin, \textit{ supra} note 9.}

entrepreneurs, and help individuals create and maintain savings accounts.

B. Proposed Amendments to the Community Reinvestment Act

Traditional modes of consumer protection, even at their most successful, can prevent or redress individual instances of exploitation or discrimination but they generally do not operate on a more structural level to reduce disparities based on the wealth gap and its origins. Attempts to level the playing field to the point where credit card debt would be distributed proportionately among racial groups are more controversial because they embrace the values behind reparations movements and other redistributive political philosophies. Without these types of measures, however, it is unlikely that there will be any significant change in this area, because discoverable racial discrimination accounts only for a small part of the disparities. This part therefore proposes amendments to the Community Reinvestment Act that would lead to a more equitable distribution of credit card debt.

First I explain why the CRA is the appropriate vehicle for the proposed amendments. Next I describe three types of investments that credit card issuers should make: free community-based financial planning services; individual development accounts; and domestic micro-finance loans.

1. Why the CRA?

The Community Reinvestment Act, enacted in 1977, begins with a statement of Congress’s findings that

regulated financial institutions are required by law to demonstrate that their deposit facilities serve the convenience and needs of the communities in which they are chartered to do business; the convenience and needs of communities include the need for credit services as well as deposit services; and regulated financial institutions have continuing and affirmative obligation to help meet
the credit needs of the local communities in which they are chartered.\textsuperscript{290}  

It then states its purpose to be “to require each appropriate Federal financial supervisory agency to use its authority when examining financial institutions, to encourage such institutions to help meet the credit needs of the local communities in which they are chartered consistent with the safe and sound operation of such institutions.”\textsuperscript{291} These rather vague statements lend themselves to creative interpretation.  

The practical effects of the law in its current form are as follows. Supervisory agencies, such as the Office of the Comptroller of the Currency and the Federal Reserve Board, assign ratings to financial institutions based on their compliance with the CRA.\textsuperscript{292} Institutions receive a rating of outstanding, satisfactory, needs to improve, or substantial compliance.\textsuperscript{293} These ratings are available to the public. The appropriate financial supervisory agencies must take an institution’s rating into account when considering requests from the institution such as applications for branch openings, relocation of a home office, a merger, or an acquisition.\textsuperscript{294} The CRA is related to the ECOA, because ECOA violations should lower an institution’s rating significantly.\textsuperscript{295} The CRA regulations presently focus primarily on loans and other similar forms of credit, as opposed to credit cards.\textsuperscript{296}  

Consequently, the CRA does not adequately motivate financial institutions to meet the credit card needs of the low-income communities they serve. I therefore recommend changes to the regulations that would require institutions that issue credit cards to take the following actions to serve low-income communities better.

\begin{itemize}
\item \textsuperscript{290} 12 U.S.C. § 2901(a)(1)-(3).
\item \textsuperscript{291} 12 U.S.C. § 2901(b).
\item \textsuperscript{293} McKinley, \textit{supra} note 292.
\item \textsuperscript{294} \textit{Id.}
\item \textsuperscript{295} \textit{Id.}
\item \textsuperscript{296} \textit{See} Community Reinvestment (Regulation BB), 12 C.F.R. pt. 228 (2010).
\end{itemize}
The CRA should impose these requirements on credit card issuers that are independent of banks as well as banks, because the independent companies function as banks by lending to consumers and the issuers should not perform this function absent accountability.

2. *Partnerships with Community Organizations*

The larger United States banks that dominate the credit card industry generally do not provide financial counseling to underserved communities. Some smaller institutions, such as credit unions, however, have set up programs specifically directed at lower-income communities of color. Non-profit groups and churches have also developed financial counseling programs. Grassroots programs of this type, although effective, often lack the considerable resources at the disposal of larger, more established institutions. As the primary holders of the bank accounts of the rich and the poor, large financial institutions should bear the majority of the burden for financial education in partnership with community organizations that can most accurately identify a community’s particular needs. Market failure also leads to the necessity of education to guide consumers to make rational choices, and the banks’ complicity in this failure implicates their responsibility to provide counseling that helps correct for it.

Several existing programs could serve as models for partnerships between large financial institutions and community organizations to provide financial counseling. For example, the Latino Community Credit Union in Durham, North Carolina, offers six-week sessions of financial education to assist un-banked Latinos enter the financial mainstream.297 Participants need not be members of the credit union.298 The program began as a reaction to the finding that up to fifty percent of Latinos do not have a checking or a savings account, and census bureau data from 2000 demonstrating that North Carolina had the fastest growing Latino population in the country.299 Workshops offered by the credit union also improve participants’

298. *Id.*
299. *Id.*
financial literacy by teaching them how to build a credit history, how to buy a car, and how to use an ATM.300

Local characteristics often shape financial needs. To facilitate determination of those needs, the National League of Cities published a municipal action guide specifically directed at immigrants.301 This guide could help financial institutions structure their organizations in Latino communities. Other excellent models for community financial development are the Operation Hope credit counseling program302 based in Los Angeles and Pastor DeSoaries’ DFree workshops, designed to help his parishioners live without debt, deficits, and delinquency.303

Although banks may push to create financial service programs independent of community organizations, partnerships are necessary to ensure that the services are designed to benefit the community, not to generate profits, and that they are tailored to the specific needs of the community.

3. Individual Development Accounts

The close relationship between the wealth gap and racial disparities in credit card debt indicates that banks must also facilitate saving by individuals to meet the credit needs of the communities they serve. Some banks have already taken steps in this direction by

300. Id.
setting up Individual Development Accounts (“IDAs”) for eligible lower-income families.\textsuperscript{304} IDAs are matched savings accounts wherein participating private or public entities reimburse dollar-for-dollar the money drawn from the account holder’s IDA when she has used the funds to purchase a first home, small business, or education. Many of the IDA-sponsoring institutions require participating accountholders to attend financial education courses that teach how to budget, save, and build a credit history.

Historically, savings plans have served to marginalize lower-income Americans because many plans, such as 401(k)s, generally enable individuals and families who are already above the federal poverty line to accumulate assets. An extensive study of IDAs found that IDA account holders had $5,892 in real assets and $6,181 in total assets more than the control group of individuals without IDAs.\textsuperscript{305} The researchers noted that, “[a]lthough the significance level is small, the differences in the values of real assets and total assets are meaningful, especially for a low-income population.”\textsuperscript{306} Children’s Savings Accounts, based on the same model, also demonstrate potential to facilitate upwardly class movement.\textsuperscript{307}

4. Domestic Micro-Lending

In 2008, Grameen Bank, pioneer of micro-lending in Bangladesh, began implementing their model in the United States.\textsuperscript{308} Grameen

\begin{enumerate}
\item See Chang Kuen-Han et al., Assets Beyond Saving in Individual Development Accounts 17 (Washington Univ. in St. Louis, Ctr. for Soc. Dev. Working Paper No. 07-25 (2007), available at http://csd.wustl.edu/Publications/Documents/WP07-25.pdf (reporting that IDA participants had more real and total assets than members of a control group without such accounts).
\item Id.
\item OLIVER & SHAPIRO, supra note 23, at 245-46.
\item Amanda M. Fairbanks, Lending Plan Won Prize, But Will It Work Here?, N.Y. TIMES, Apr. 1, 2008, at B5. In Bangladesh, the Grameen Bank “helped start
America provides small loans to individuals, almost all women, who are living below the poverty line and want to start or grow a small business.\(^{309}\) Although there are no statistics documenting all of the beneficiaries of micro-lending, it appears that they are almost exclusively low-income women of color.\(^{310}\) These women form groups of borrowers who go through a financial training program together then meet weekly to repay their loans and discuss their progress.\(^{311}\) Each woman receives a small loan to start or expand a business.\(^{312}\) After every woman in a group fully repays her loan, borrowers are eligible for new loans.\(^{313}\) The model relies solely on peer pressure to ensure repayment.\(^{314}\)

Citigroup partnered with Grameen to create savings accounts for the borrowers, most of whom were previously unbanked.\(^{315}\) The CRA should require all banks that issue credit cards to participate in domestic micro-lending. This participation would create a new class of customers for the banks, as well as alleviate some of the poverty that contributes to financial distress.

CONCLUSION

In addition to top-down reform, individual and community action can have a significant impact on the reduction and eventual elimination of racial credit card debt disparities. One consumer advocate suggests that concerned individuals who use credit cards and

the microloan movement . . . by providing advances of as little as a few dollars to impoverished women to start village businesses, with very positive results.” Amy Zipkin, Small Business: For Some, A Little Loan Goes a Long Way, N.Y. TIMES, Dec. 22, 2007, at C5.  


310. For example, the center in St. Albans Queens New York “consists predominantly of Caribbean and African-American women.” See Fairbanks, supra note 306.  

311. Id.  

312. Id.  

313. Id.  

314. Id.  

can afford to give up some of the associated perks should stop using rewards cards, which draw on the fees and interest rates of lower-income consumers to pay out rewards.\textsuperscript{316} Convenience users could choose to stop using credit cards altogether, a choice that, if made by enough people, could reduce merchants’ fees that raise the costs of goods for all consumers. Banked individuals could divest from banks that have abusive credit card practices and keep their money in community-friendly credit unions.\textsuperscript{317} Opportunities for self-help also abound, with a number of books directed towards increasing wealth and financial literacy in and through the African American community.\textsuperscript{318}

Financial literacy should not be the exclusive province of the white middle and upper classes. Financial education should begin in the public school system, where social science curricula should provide basic lessons on financial institutions and planning. Education should continue upon a consumer’s initial acquisition of a card, which should be accompanied by a workshop in credit card use, and continue throughout an individual’s lifetime, as the law and the industry undergo changes, and the consumer’s personal needs evolve.

Structural inequality entrenched throughout a long history of subordination likely cannot be eradicated, however, through self-help and education. It is essential that anti-poverty measures, implemented with an awareness of racial disparities in wealth, income, and debt, be at the forefront of reform. The proposals described in this paper would begin this work.

The devastating impact of racial disparities in credit card debt should serve to capture the attention of the media, politicians,


\textsuperscript{317} The beginning of the financial crisis provoked an informal campaign urging people to ‘fire their banks’ primarily through social networking sites.

academics, and activists in the same way that race and class elements of the mortgage and financial crisis have. This article calls for creative and inclusive strategizing to resolve the problem of racial debt disparities, including further research in the law and economics and behavioral economics communities that recognizes and attempts to reduce these disparities.