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S.F. bank's startling interest: 79 percent

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A new credit card product from Sioux Falls-based First Premier Bank is getting national attention because of its record-high interest rate: 79.9 percent.

While consumer advocates are concerned it might take advantage of users, the bank stands by the card as a way for those with damaged credit to rebuild it.

But both sides agree on one thing: The high interest rate is an unintended consequence of well-intended credit card reform legislation going into effect in February.

The card, which is issued through Premier Bankcard and has a \$300 credit line, is a response to new regulations that limit the fees on a credit card to 25 percent of a credit card's line.

Typically, this First Premier card comes with a \$250 credit line with 9.9 percent interest and \$256 in annual fees in the first year. That card will not be offered after February 21, in compliance with the new law.

The 79.9 percent interest card is being offered as part of a limited test to gauge interest in the product, said Dana Dykhouse, the chief executive of First Premier, which is the 10th largest issuer MasterCard and cards in the country with more than 3.5 million customers. But he said he thinks the demand is there for users the company views as high risk.

"We use the example of high-risk auto insurance. If you have a bad driving record, you have to pay more and once your driving record has improved, it will come down," Dykhouse said. "People who have damaged or no credit pay a higher cost, but if they make timely payments, after awhile their cost comes down dramatically."

Industry analysts have never seen anything like it.

"It is the highest on the market," said Anuj Shahani, an analyst with Synovate, a research firm that tracks credit card mailings. "It is the highest we've ever seen."

The average national variable interest rate is 11.68 percent. But this card is directed at sub-prime credit card users, or those who have poor or no credit.

First Premier's biggest card, according to Dykhouse, is one that charges 59.9 percent for a \$300 credit line. "They are looking at about \$70 or \$80 a year to re-establish their credit," he said. "That is a pretty small price to pay in order to establish their credit."

The new regulations pose challenges for both credit card companies and consumers who want to build credit, Dykhouse said.

"There is a reason in an economic downturn that consumer credit has shrunk for 10 months in a row," said Dykhouse. "It isn't because they are flush with cash. It is because if we restrict credit it eliminates the ability to establish credit. These are the unintended consequences to what they think are well-intended laws."

On this point, consumer counselors agree.

"The legislation is meant to protect people," said Tracy Gran, the director for Consumer Credit Counseling in Sioux Falls. "But this is an unintended consequence."

So how do people with damaged credit rebuild it?

"I wouldn't advocate for 79.9 percent cards, but they need to build credit somehow," Gran said. "There is a good likelihood that those kinds of products will be all that will be offered for that."

This is because once the new rules go into effect, several provisions, including the limitation on fees, discourage credit companies from extending credit to sub-prime users. They cannot make money from these borrowers except by shifting the premium on risk to the interest rate.

Already credit card mailings, which are down for the year, are ticking up for the most desirable credit card customers, according to a recent study by Mintel Comperemedia, which tracks card mailings.

The upcoming credit card reform legislation, "will eat into credit card issuers' revenue stream, so they're looking for any legitimate means possible to recoup that income," said Andrew Davidson, senior vice president of Mintel Comperemedia. "This has led to whirlwind changes as issuers adapt and test new ways to bring in revenue."

Consumer counselors such as Gran say that financial literacy and personal accountability are as much a problem as high interest rates.

"I would guess that most people who get that card will have no idea that it is a 79 percent interest rate," she said. "It goes back to consumer awareness."

She said interest rate blindness is not limited by educational level. "A lot of people think the laws are protecting them," she said. "They assume these kinds of rates couldn't be charged."

Dykhouse thinks the intended user will see the benefits of the card.

"The people who accept it understand what the fees are and what the interest rate is and that they can re-establish their credit, they will have the opportunity to get lower priced credit," he said. "If at any point in time they are not satisfied, they have a 100 percent refund. It isn't our intent to do anything but re-establish their credit."

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