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Secrets Of The Banking Industry

If you have been keeping up with my newsletters for any extended period of time, you have probably come to one of two conclusions. Either I have completely lost my mind, or... the Banking Industry is not your best friend.

Maybe it is a little of both.

Nevertheless, over the years, banks have slowly but surely, found ways to squeeze more and more money out of unsuspecting consumers. So today I would like to put an article by Caroline Fouts on showcase. Let's take a look at some dirty little secrets about your bank that you may not be aware of. Stay tuned for the grand finale!

Filthy Rich: Dirty Secrets of The Banking Industry

By Caroline Fouts

In recent years, banks have adopted some practices that impose high fees and other penalties on some of their most vulnerable customers. We'll take a look at two of the most dangerous pitfalls, and show you how to avoid them.

THE UNIVERSAL DEFAULT CLAUSE

Banks have been promoting low "teaser" rates on new cards and balance transfers, but there's often a catch. Those preferable interest rates can jump into the high 20s and even in the low 30s if a borrower is late with a single payment.

Banks that include a Universal Default Clause in their credit card agreements can raise interest rates if their customers are late paying any debt. This means that if you don't pay a utility bill on time, or forget to send a check to a book club, the interest rate on all of your credit cards can make a sharp jump upwards.

Changing the Rules in the Middle of the Game

It's one thing to use a consumer's payment history to underwrite a new loan. But credit card companies are applying these new, much higher interest rates to existing loan balances.

There is no other form of lending where this happens. If a bank tried to double the interest rate on an existing car loan, the courts would smack it down. Even with adjustable rate mortgages, there are established limits on when and by how much the interest rate can change.

Only with credit card debt are the banks allowed to increase rates on the slightest bad credit news. Worse yet, the amount of the increased interest rate they charge the consumer, as well as the event that triggers the increase, are at the bank's discretion.

Even Without a Late Payment, Banks Can Raise their Rates

Mary Ann was shocked then she opened a credit card statement to discover her APR on the loan jumped from 8.99% to 18.49%. The bank informed her that, after reviewing her credit records, they determined her high debt-to-income ratio made her a higher risk borrower.

"I consider myself to be very capable with my finances, but I've had a few years where I ran up more debt than usual, including a home equity loan," said Mary Ann. "I made all of my payments on time, but evidently my new debt affected what used to be a stellar credit record. It's frustrating."

Then another credit card statement arrived, raising the interest rate from 8.99% to 27.4%. Mary Ann was appalled, "In all the years that I held this card, I never made a late payment."

Preying on the Inexperienced

When Seth Woodworth was a student at Central Washington University, he ran up over \$3,000 in credit card debt. "I was pretty terrified of listening to my voice mail because of all the messages about the money I owed," said Woodworth.

Students are an easy mark for unscrupulous credit card providers, because they often don't have any experience using a card.

Woodworth didn't read the credit card agreement, and had never heard of a Universal Default Clause. "I had no idea that my interest rate would rise the way that it did because I missed one payment," said Woodworth. He also didn't know that there is no regulation limiting the amount a bank can charge for a late fee on a credit card payment, until he was charged \$39.

In their defense, issuers of credit cards say they emphasize consumer education. And, of course, they give every customer a disclosure of the terms and conditions of the credit card agreement. These agreements are often 30 pages long, and contain sophisticated legal terms.

Citibank promised to stop imposing a Universal Default Clause on its credit card customers, and has done so. But as of the middle of 2007, a survey by the advocacy group Consumer Action, reported that 8 out of 10 banks still employ a Universal Default Clause to raise interest rates based on customers' credit reports.

As for Woodworth, he had to quit school and work for 2 years to pay off his credit card debt before he could finally resume his college education. He said, "If I could do it over again, I never would have gotten a credit card."

BOUNCE PROTECTION

Many people are not aware that if they try to make an ATM withdrawal for more money than they have in their account, the ATM will allow them to do so, but the bank will impose an overdraft fee that can be as high as \$35.

Bounce Protection, or "Courtesy Overdraft Protection" as some banks call it, is a program that many banks and other financial institutions routinely impose on their checking accounts. It used to be that a customer had to request overdraft protection on their account. Now it is quietly slipped into the terms and conditions agreement.

Getting Rich on Overdraft Fees

According to the National Consumer Law Center, Bounce Protection was designed and promoted to banks by several banking consulting companies, who sold it as a complete package, including software, consumer marketing materials, and operational assistance. The consultants promised that banks would increase their overdraft fee income by 100% to 300% or more—and they kept that promise.

One consultant calculated that a customer who makes only one overdraft transaction per month generates the same income to the bank as a depositor with a \$12,000 average account balance. Since there are many more depositors who are likely to use Bounce Protection than there are affluent depositors, it benefits the bank to encourage customers to overdraw their accounts.

Maximizing Multiple Overdraft Fees

Where the banks are really making money is on multiple overdraft fees. Once an account has gone into a negative balance, any check, ATM or debit card transaction that hits the account generates another \$20 to \$35 NSF fee.

What's worse, is the banks structure their accounting so that the largest transaction hit the account first, so if it puts the depositor over their account balance, each of the smaller transactions will trigger a new \$35 fee. It would be easier to apply the transactions to the account in the order in which they occurred—but that wouldn't generate the as many fees.

More Expensive than Payday Loans

In essence, banks are competing with payday loans. At least with a payday loan, borrowers know up front how much they are borrowing, and how much they are paying for the advance of funds against their paycheck. With Bounce Protection, a depositor

often doesn't know their account is overdrawn until the damage has been done, and it's too late.

Since most overdraft loans are repaid within a couple of days, they may pay as high as 20,000% APR on their overdraft advances.

Unlimited Fees

There are no limits to prevent consumers from getting mired down in multiple overdraft fees, creating perpetual debt. And banks have a disturbing history of accessing the social security deposits of low-income and fixed-income depositors to cover their multiple Bounce Protection fees. These are not hypothetical situations, but real depositors that banks have literally put out on the streets without money for rent and food.

HOW YOU CAN PROTECT YOURSELF

Read the fine print

Be one of the few who actually reads the boilerplate contracts the bank gives you, containing the terms and conditions that control their credit cards. Since this is a legally binding contract, it's worth the time to read the agreement and ask questions about any provisions you don't understand—before you open an account.

And the fine print doesn't end when you open the account. Most banks reserve the right to change the terms and conditions agreement at any time. You've probably received notices of changes of the terms of your credit card or bank account in the mail, with more legal disclosures. The only way to know what new terms the bank is imposing, is to read these as well.

Shop Around

Not all banks include a universal default clause or bounce protection provision in their consumer agreements. Look for a bank that will provide you the financial services you need, without putting your finances or credit rating at risk.

Check your Monthly Statements

With any credit card, it's important to read your monthly statements, and to compare them with previous months. Interest rates have a way of creeping up over time. Even on fixed rate cards, interest rates can balloon on as little as 15 days notice from the bank.

If the bank does raise your rate, consider calling to ask for a lower interest rate. You'd be surprised how often they will do what is necessary to keep your business.

Conclusion

At some point, Congress may pass a law prohibiting these types of abusive fees and exorbitant interest rates. But in the meantime, the rampant greed of the banks that use Universal Default provisions and Bounce Protection fees to generate income goes unchecked. Thus, it is up to consumers to protect themselves.

Consumer Publishing Group is the publisher of the Credit Secrets Bible (in print since 1994) and the all new Debt Free Bible. For more information, visit their website at <http://www.debtfreebible.com>

Even BIGGER Banking Industry Secrets!

Do you have a mortgage? You may want to take a strong look at the video below. It piggybacks off of a previous article that I did on Understanding The Federal Reserve System, and also the Economic Bail out Update that I did after last months "Don't do a budget" newsletter. Pay special attention to the discussion of the 1969 Jerome Daly court case. This information is not something that is regularly circulated. This following 20 minute clip is from a documentary called Zeitgeist: Addendum.

More Dirty Banking Industry Secrets

<http://www.youtube.com/watch?v=67OmYvzr9tY>

Considering the Federal Reserve's 5 Trillion Dollar spending spree... Do you still believe the U.S. Dollar isn't going to become obsolete?

Until next time,

Free Your Mind... Online,

Matt Mason

For more resources, visit the Resource Center
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