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THE DEBT DILEMMA

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CHARGING AHEAD: THE GROWTH AND REGULATION OF PAYMENT CARD MARKETS. By *Ronald J. Mann*. New York: Cambridge University Press. 2006. Pp. v, 308. Hardcover, \$65; paper, \$30.

INTRODUCTION

The ubiquity of credit cards in modern economic life inspires much dismay,¹ but little nuanced discourse. Lamentations, about undisciplined consumers or manipulative card issuers, lead to policy prescriptions aimed at reducing credit card use.² Such efforts generally have failed to garner the support of consumers, who demonstrate continued preference for cards over cash or checks.³ These efforts have also roused the ire of opponents to market regulation⁴ and the credit industry lobby.⁵ The current dynamic of increasing credit card use juxtaposed with regulatory pressure on card markets reflects our society's deep ambivalence about credit cards.⁶

Charging Ahead: The Growth and Regulation of Payment Card Markets offers a refreshingly balanced perspective on the optimal use of credit cards.

* Associate Professor of Law, University of Iowa College of Law. I thank Angie Littwin, John Pottow, and Tara Twomey for their helpful comments on this Review. Brian Locke provided able research assistance, and Kati Jumper provided cheerful encouragement.

1. Richard Hynes & Eric A. Posner, *The Law and Economics of Consumer Finance*, 4 AM. L. & ECON. REV. 168, 169 (2002) ("The credit card industry has attracted a great deal of criticism for its aggressive marketing efforts, confusing credit terms, and high interest rates."); Walecia Konrad, *How Americans really feel about credit card debt*, BANKRATE.COM, Feb. 20, 2007, http://www.bankrate.com/bnm/news/Financial_Literacy/Feb07_credit_card_poll_national_a1.asp (last visited Sept. 7, 2007).

2. *Examining the Billing, Marketing, and Disclosure Practices of the Credit Card Industry, and Their Impact on Consumers: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 110th Cong. (2007) (statement of Sen. Christopher J. Dodd, Chairman, S. Comm. on Banking, Housing and Urban Affairs), available at <http://banking.senate.gov/index.cfm?Fuseaction=Hearings.Testimony&TestimonyID=1386&HearingID=246> (last visited Sept. 7, 2007).

3. See Geoffrey R. Gerdes et al., *Trends in the Use of Payment Instruments in the United States*, FED. RES. BULL., Spring 2005, at 180, 184, available at http://www.federalreserve.gov/pubs/bulletin/2005/spring05_payment.pdf.

4. See, e.g., DAVID EVANS & RICHARD SCHMALENSEE, PAYING WITH PLASTIC: THE DIGITAL REVOLUTION IN BUYING AND BORROWING xii (2000); see also Christopher C. DeMuth, *The Case Against Credit Card Interest Rate Regulation*, 3 YALE J. ON REG. 201 (1986) (discussing the problems with credit card market regulation).

5. Donald L. Barlett & James B. Steele, *Soaked by Congress*, TIME, May 15, 2000, at 64 (describing strategies of credit lobby used to support bankruptcy reform).

6. Kathleen Day, *A Highly Charged Relationship: Americans Can't Do Without Their Credit Cards, But the Credit Card Companies Are Another Matter*, WASH. POST, May 27, 2007, at F01.

Authored by Ronald J. Mann,⁷ the book manages to be provocative without resort to polemic. Even rarer, *Charging Ahead* reveals how payment systems law—perhaps the most esoteric topic in the already esoteric world of commercial law⁸—shapes our society and its pursuit of the good life. Private transactions have public effects, and *Charging Ahead* elucidates the public effects of our often mindless act of paying with plastic.

The centerpiece of the book is regression analysis of the economic effects of credit cards. Scholars have struggled to understand these relationships,⁹ shrouded in the mystery of the Holy Grail, or at least its commercial law equivalent. Relying on aggregate macroeconomic data from several countries, Mann establishes consistent and robust relationships between credit card use and increased consumer spending, borrowing, and debt. He isolates credit card spending—as opposed to credit card debt—as the significant variable in increased levels of consumer debt (p. 53).

Mann then turns to the relationship between credit card debt and bankruptcy, which he uses as a public measure of financial distress. Mann shows that borrowing on cards—distinguished from noncard borrowing—is separately associated with bankruptcy filings. Credit card debt, distinct from consumer debt generally, corresponds with an increased bankruptcy rate. He posits that bankruptcy and financial distress impose externalities on society and proposes legal reforms to deter harmful credit card borrowing and reduce the bankruptcy rate. *Charging Ahead* concludes with a cogent and carefully circumscribed set of strategies for reshaping American appetites for credit card use. These reforms aim to moderate the externalities caused by credit cards without eliminating their efficiency benefits.

This Review explores Mann's empirical analysis and identifies an important limitation inherent in it. Despite Mann's findings, reducing credit card spending and borrowing would have only a modest effect on reducing the number of bankruptcies. Decades of research from the Consumer Bankruptcy Project¹⁰ show the importance of an adverse event such as job loss or illness in precipitating financial collapse.¹¹ Mann does not fully integrate the

7. Professor of Law, Columbia Law School.

8. See Larry T. Garvin, *The Strange Death of Academic Commercial Law*, 68 OHIO ST. L.J. 403, 409–10 (2007).

9. See Lawrence M. Ausubel, *Credit Card Defaults, Credit Card Profits, and Bankruptcy*, 71 AM. BANKR. L.J. 249 (2007); Ian Domowitz & Robert L. Sartin, *Determinants of the Consumer Bankruptcy Decision*, 54 J. FIN. 403 (1999); Diane Ellis, *The Effect of Consumer Interest Rate Deregulation on Credit Card Volumes, Charge-offs, and the Personal Bankruptcy Rate*, BANK TRENDS, Mar. 1998, at 1, available at http://www.fdic.gov/bank/analytical/bank/bt_9805.pdf; David B. Gross & Nicholas S. Souleles, *An Empirical Analysis of Personal Bankruptcy and Delinquency*, 15 REV. FIN. STUD. 319 (2002).

10. For a description of the Consumer Bankruptcy Project, see *infra* note 45 and accompanying text.

11. TERESA A. SULLIVAN, ET AL., *THE FRAGILE MIDDLE CLASS: AMERICANS IN DEBT* (2000); ELIZABETH WARREN & AMELIA WARREN TYAGI, *THE TWO-INCOME TRAP: WHY MIDDLE-CLASS MOTHERS AND FATHERS ARE GOING BROKE* (2003); David U. Himmelstein et al., *Market Watch: Illness and Injury as Contributors to Bankruptcy*, HEALTH AFF., Feb. 2, 2005, <http://content.healthaffairs.org/cgi/reprint/hlthaff.w5.63v1.pdf>.

implications of this research into his conclusions. Credit cards may ratchet up consumer spending, borrowing, and debt, leading families to divert a higher percentage of their income to current consumption and debt service (p. 64). Most bankruptcies, however, are still triggered by a financial shock.

An aggregate examination of the effects of credit cards does not reveal how card use affects a family's response, or ability to respond, to an adverse financial event. This shortcoming in Mann's analysis reveals the limitation of credit card reform to spare families and society the harms of financial distress. Credit card reform may effectively alter Americans' calculus about whether to pay with credit cards, but such behavioral change does not itself provide families with the income and savings necessary to protect them from adverse financial events. Drawing on original data showing that many families eschew credit cards after bankruptcy, I highlight the vulnerability of "cardless" families to financial hardship. This critique applies Mann's aggregate, macroeconomic analysis to the microeconomic context of individual families and emphasizes the relevance of non-credit card use factors in exposing families to financial stress.

Part I describes the nature of credit card spending and explores the usefulness of Mann's comparative approach to studying credit cards. Part II evaluates Mann's findings on the overall relationships between individual credit card transactions and aggregate levels of spending, borrowing, and bankruptcy. It also briefly analyzes the relationship between his findings and policy recommendations. Part III explores data on families who refrain from credit card use and struggle with serious financial distress. Part IV revisits Mann's policy recommendations in light of this new data. I conclude that implementing credit card reform would offer families only partial, albeit valuable, protection from the risks of our modern economy.¹²

I. THE POWER OF PLASTIC

Payment cards of all types are growing in popularity. Credit cards combine borrowing and spending capacities in a single plastic instrument—a key feature that simultaneously enhances the utility and risk of credit cards.

A. Nature of Card Transactions

In America, cash is no longer king. Consumers prefer to pay with plastic cards, and such payments outnumber both cash transactions and check transactions (p. 17 fig.1.3). A variety of payment cards exist, including credit cards, debit cards, and types of stored-value cards, such as payroll cards or gift cards. *Charging Ahead* provides a concise and readable explanation of the variety of payment cards, focusing on the benefits and burdens of debit cards versus credit cards.

12. Mann never asserts the contrary. He acknowledges that reducing credit card use "would not solve the problem [of consumer financial distress] entirely." P. 6.

Given the ubiquity of cards in our daily lives and their dominance of the U.S. economy, we probably should know the answer—or at least the reasons for the question—to the everyday dilemma: “credit or debit?”¹³ The structure of debit and credit card transactions vary significantly along both economic and legal dimensions. Lamentations about the decline of cash and ferocious condemnations of the evils of “paying with plastic” fail to consider fully the differences among card-based transactions or to parse the effects of such differences. Mann situates credit cards within a timeless framework of “payment system” devices, showing how concerns about transaction costs, risk of fraud and error, anonymity, universality, and finality shape preferences for payment devices.¹⁴

Mann responds to a substantial, and somewhat surprising, weakness in prior literature by penning a “defense of credit cards” (p. 37). Rather than assuming that cards must be superior (or dangerous) simply because they are a modern innovation, Mann identifies the key benefits of card-based transactions, both to consumers and to the overall economy. For example, nearly every consumer has access to a credit card. Card issuers have used price differentiation and technology to offer cards to nearly every segment of the market, a strategy that banks have not deployed for many conventional lending products.¹⁵ Credit cards are also ideal for flexible and open-ended financing because cardholders are excused at the time of the card transaction from committing to specific terms of repayment (pp. 42–43). On a larger scale, card transactions are nearly all electronically processed. Mann reports that the current cost of processing paper checks in the United States equals about one-half of one percent of the gross domestic product (p. 39 n.5). Thus, the transaction costs savings of card-based transactions are quite significant.¹⁶ Mann rightly observes that any proposed regulation of

13. P. 33. I refuse to give you the answer here, offering additional encouragement for readers to open Mann’s book for themselves. I will advise that expounding on the “credit/debit” query makes decent cocktail party conversation, at least among law professors who secretly wonder if they missed something of significance because they never studied commercial law.

14. RONALD J. MANN, *PAYMENT SYSTEMS AND OTHER FINANCIAL TRANSACTIONS* xxiii (3d ed. 2006) (noting “deep structural similarities of all the different payment systems” and giving a few examples of such similarities).

15. Pp. 40–41. *See also* Oren Bar-Gill, *Seduction by Plastic*, 98 NW. U. L. REV. 1373 (2004) (analyzing credit card market trends). The expansion of mortgage credit to subprime customers is a relatively recent phenomenon compared to credit card product differentiation, and the current situation suggests that mortgage lenders may have been less successful in accurately forecasting default and making lending decisions accordingly. *See, e.g.*, Carrick Mollenkamp, *Faulty Assumptions*, WALL ST. J., Feb. 8, 2007, at A1; David Streitfeld, *The Mortgage Meltdown; Foreclosure Pace Nears Decade High*, L.A. TIMES, Apr. 17, 2007, at C1.

16. Many of the benefits of credit cards as a payment device, as opposed to a borrowing device, are paralleled by debit cards. These transactions are also rapid, electronically processed, and secure. Indeed, one of the main disadvantages to debit cards instead of credit cards as a *payment* device is the law’s different treatment of credit and debit cards for fraud or loss protection. P. 29. Changes to the Truth In Lending Act could level the playing field in this regard between debit and credit cards, although consumers’ knowledge about these rules may be limited. The Check 21 Act should reduce the costs of processing paper checks. *See* 12 U.S.C. §§ 5001–18 (2000). But payment cards will still have efficiency advantages such as faster processing at the point of sale.

credit cards should be evaluated against its potential to weaken or eliminate the benefits of credit cards (pp. 37, 40, 119, 177).

More than three-quarters of all Americans have one or more credit cards,¹⁷ and the average number of cards per wallet is estimated to be between seven and eight.¹⁸ Debit cards, and other plastic cards, are growing, but have not yet eclipsed the popularity of the credit card in America. Mann usefully contrasts the advantages of debit cards with credit cards, noting that some aspects of the law privilege credit cards (p. 29). Understanding such benefits partially explains Americans' voracious appetite for credit cards and refutes simplistic arguments that the choice to transact with a credit card is necessarily profligate.

B. Global Patterns in Card Use

Concern about credit card use is neither novel nor peculiarly American. Fears about unwise consumer borrowing predate the arrival of the credit card.¹⁹ Like many credit innovations, however, the credit card has spawned a new bout of concern about prodigal spending and overindebtedness.²⁰ Social and economic features of different countries shape these worries, but credit cards inspire nearly universal apprehension.

Mann devotes an entire section of *Charging Ahead* to exploring the comparative differences in card use among nations. His explanation is largely historic, relying on America's role as birth mother of the credit card and persistent regulatory obstacles in other nations (pp. 91, 114). He concludes that path-dependence is the best explanation for the credit card phenomenon in America (p. 80). U.S. banks invented the product, and the predominance of credit cards in Americans' financial lives has markedly increased in successive generations (pp. 81, 90). Future research could evaluate the contributing role of alternate explanations. In particular, cross-cultural research on behavioral and cognitive differences in individual spending and borrowing decisions seems likely to yield useful insights.²¹

17. Brian K. Bucks et al., *Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances*, FED. RES. BULL., Mar. 22, 2006, at A1, A31, available at <http://www.federalreserve.gov/Pubs/oss/oss2/2004/bull0206.pdf>; Liz Pulliam Weston, *The Truth about Credit Card Debt*, MSN MONEY, <http://moneycentral.msn.com/content/Banking/creditcardsmarts/P150744.asp> (last visited Sept. 7, 2007).

18. See *Frontline: Secret History of the Credit Card* (PBS television broadcast Nov. 23, 2004), available at <http://www.pbs.org/wgbh/pages/frontline/shows/credit> (last visited Sept. 7, 2007) (reporting that the average American has eight credit cards); Kim Kahn, *How Does Your Debt Compare?*, MSN MONEY, <https://www.moneycentral.msn.com/content/SavingandDebt/P70581.asp> (last visited Sept. 7, 2007) (stating that the average American has 2.7 bank cards, 3.8 retail cards and 1.1 debit cards for a total of 7.6 cards).

19. LENDOL CALDER, *FINANCING THE AMERICAN DREAM: A CULTURAL HISTORY OF SECURED CREDIT 202-08* (1999); see also BRUCE H. MANN, *REPUBLIC OF DEBTORS: BANKRUPTCY IN THE AGE OF AMERICAN INDEPENDENCE 251* (2002) (describing concerns in the 1800s that consumers were using bankruptcy protection to obtain credit to purchase luxury items).

20. See, e.g., Ausubel, *supra* note 9; Ellis, *supra* note 9.

21. For example, cognitive errors in evaluating the consequences of borrowing could be shaped by educational curricula, depending on their attention to rote memorization or problem

Regardless of its explanation, America's high rate of card use ratchets up the total harm and total benefit of credit cards. In America, these fears about credit card use are exacerbated by worry about declining savings. Americans' strong preference for credit cards may heighten the harmful social consequences of card use. Alternatively, social or cultural factors may themselves fuel card use, requiring broad reforms that reshape norms about spending and borrowing. Anxiety about credit cards often disintegrates into unsupported assertions about the declining moral fiber of Americans.

A comparative approach tests the validity of these arguments. Mann's analysis employs comparative data on cards and debt from five nations with large, modern economies: Australia, Canada, Japan, the United Kingdom, and the United States (p. 51). He identifies consistent, empirical effects of credit cards in these jurisdictions, breaking new ground by establishing a global pattern of card effects.

Mann is somewhat opaque on the usefulness of his comparative approach. He rightly observes that credit cards are a global phenomenon, but devotes little space to delineating the benefits of an international perspective on cards (pp. 3, 51). Imbedded in the structure of his arguments are several suggestions for how comparative analysis can inform our understanding of credit cards. First, such research is useful for refuting nationalistic perspectives that rely on the prodigality or restraint of their citizenry to explain credit card patterns. To the extent a positive relationship between card use and debt exists in multiple nations, the risk likely derives from features peculiar to credit cards as devices, rather than relating to other economic or social features of the country (pp. 68-69). This conclusion suggests that interventions that target the unique qualities of credit cards as payment mechanisms could reduce consumer debt.

Mann's global analysis also makes practical and political points. Depending on their relative use of credit and debit cards, countries will face different challenges in optimizing payment card preferences. The transactional efficiency of cards as payment and spending devices is a substantial benefit to be balanced against the drawbacks of card use for consumers. The potential for credit card reform to alter consumer debt levels is greater in America than in countries where card use is relatively infrequent. Mann documents how the United States is "dependent on a credit-centered cards market to an extent unmatched in any other economy" (p. 4, Part III). The dominance of credit cards extends both to the number and value of transactions. Along nearly every metric,²² the United States exhibits a significantly

solving. In some cultures, borrowing may be scorned as a sign of financial distress, rather than prized as a mark of confidence and entrepreneurial spirit. Mann's prior work in Japan is an exemplar of this type of research. See Ronald J. Mann, *Credit Cards and Debit Cards in the United States and Japan*, 55 VAND. L. REV. 1055 (2002). Sociologists and anthropologists who delve more deeply into shared attitudes in a society could extend this line of research, aiding economists who increasingly admit that behavior insights can contribute to economic theory.

22. The number of card transactions per capita in Canada modestly exceeds the number in America. See p. 76 fig.6.1. This disparity results from the high use of debit cards in Canada. See *id.*

greater preference for credit card transactions than other nations do.²³ Other countries may actually want to foster greater reliance on credit cards to stimulate efficient small loans, while being attentive to the harms of widespread card use that Mann isolates. Correspondingly, the financial stakes of such reform for consumers and the card industry are higher in America.

Putting America's card use in global context explains Mann's pessimism about the likelihood of credit card reform.²⁴ The dominance of large, national banks in the credit card market²⁵ and the weak enforcement activity of their regulator, the Office of the Comptroller of the Currency,²⁶ compound the difficulties of achieving and implementing credit card reform. In the face of these challenges, *Charging Ahead* nonetheless manages to articulate a persuasive agenda for credit card reform that has international applicability.²⁷

II. CONSEQUENCES OF CARD USE

Having built an argument for the advantages of payment cards and described their relative importance across economies, Mann then constructs a model to measure the effects of credit cards on consumer spending and borrowing. He teases out the positive relationship between credit card use and bankruptcy, isolating the particular aspects of credit cards (distinct from other payment cards) that may drive increased financial distress.

23. Mann uses data from 2001 for each of these comparisons. In America, debit cards are a significantly newer product than credit cards. EVANS & SCHMALENSSEE, *supra* note 4, at 297. Perhaps as Americans gain more familiarity with debit cards, use of debit cards will climb. This may or may not result in a decline in credit card use, depending on whether debit cards substitute for cash or check transactions or erode use of credit cards.

24. P. 207 ("I am realistic enough to recognize the political implausibility of what I propose."). The card issuers apparently share Mann's view. See Capital One Fin. Group, Annual Report (Form 10-K), at 16–17 (Mar. 1, 2007) (noting that although Congress is holding hearings on credit card regulations, analysts believe broad regulatory changes are unlikely).

25. Ten credit card issuers control over eighty-four percent of the credit card market share. The top three issuers—Chase, Citibank, and MBNA (now part of Bank of America)—control nearly half of the market. *Card Chiefs*, CARDTRAK.COM, Feb. 4, 2005, <http://www.cardweb.com/cardtrak/news/2005/february/4a.html> (last visited Sept. 7, 2007) (citing www.carldata.com).

26. *Credit Card Practices: Current Consumer and Regulatory Issues: Hearing Before the Subcomm. on Fin. Insts. and Consumer Credit of the H. Comm. on Fin. Servs.*, 110th Cong. (2007) [hereinafter *Credit Card Practices Hearing*], available at http://www.house.gov/apps/list/hearing/financialsvcs_dem/hr042607.shtml (last visited Sept. 7, 2007) (written testimony of Arthur E. Wilmarth, Jr., Professor of Law, George Washington University Law School, 13–20, available at http://www.house.gov/apps/list/hearing/financialsvcs_dem/htwilmarth042607.pdf).

27. Mann reveals his own biases in undertaking the research and acknowledges his own surprise at his recommendations (pp. 6, 207). Whether a calculated tactic to persuade other skeptical readers or a natural product of Mann's (successful) effort to make the book more readable, Mann's personal voice enhances the reader's connection to his analysis.

A. Untangling Card Spending and Card Borrowing

Mann's empirical analysis establishes a positive relationship between credit card use and increased consumer debt.²⁸ Neither the concise nature of the foregoing sentence nor its "obviousness" to an armchair empiricist should diminish the power of Mann's achievement. People repeatedly have denied the existence of any such effects of credit cards, including in Congressional hearings on the need for credit card reform.²⁹ *Charging Ahead* should quash such unsupported assertions. The debate should now advance to an examination of the desirability of the established effects of credit cards on consumer behavior.

The empirical core of the book, Chapter 4, analyzes the relationships between aggregated credit card spending, credit card debt, and consumer debt. Mann pays only fleeting attention to the relationship between card use and savings.³⁰ Instead, he focuses on the nexus between credit cards and debt. Card spending and card borrowing are combined in a model with total consumer debt and macroeconomic conditions (p. 58 tbl.4.4). Mann finds that credit card spending, rather than credit card debt, is the significant factor that correlates with total consumer debt. An increase in \$100 of credit card spending corresponds, one year later, with a \$105 increase in total consumer debt (p. 54). This relationship is statistically significant when credit card spending and credit card debt are considered simultaneously and when total consumer debt is lagged by one, two, or three years (p. 57 tbl.4.2).

As credit cards become more favored payment devices, countries experience an increase in overall consumer borrowing (p. 53, 57 tbl.4.2). This relationship reinforces the findings of psychologists and credit industry researchers that paying with a credit card increases spending.³¹ However, credit card borrowing has no separate effect on total debt. Frequent credit card use as a payment device heightens consumers' total borrowing, regardless of whether the card transaction is paid when consumers get their statements. Put another way, card use does drive consumer debt upward, but much of that borrowing occurs in forms other than credit cards.

Mann terms this spending-debt relationship of credit cards an "instrument-induced risk" (p. 119). Other forms of plastic payment—most prominently debit cards—offer the efficiency benefits of credit cards but may not stimulate overall debt. By isolating the dangers of credit cards' dual

28. The operative word in this sentence is "use." Mann's analysis does not focus solely on credit card debt or credit card spending but considers the separate and combined effects of the two functions of credit cards—payment and borrowing.

29. P. 53 n.27; *Credit Card Practices Hearing*, *supra* note 26 (testimony of Todd Zywicki, Professor of Law, George Mason University Law School, 5–8,12, available at http://www.house.gov/apps/list/hearing/financialsvcs_dem/htzywicki042607.pdf); *id.* (written statement of Oliver I. Ireland, partner, Morrison & Foerster, 2, available at http://www.house.gov/apps/list/hearing/financialsvcs_dem/htireland042607.pdf).

30. *See infra* text accompanying notes 76–78. He points to widespread variation in government social services as a barrier to comparing savings data across nations (pp. 55–56).

31. P. 48. These studies focused on individual consumer behavior, not aggregate effects, and usually studied only one transaction or transactions at a particular business.

function as a spending and borrowing device, Mann justifies narrow reform of credit cards that would tweak the structure of card transactions to shift spending transactions onto debit cards (p. 120).³²

B. *The Bankruptcy Connection*

Higher levels of consumer debt may not be a cause for concern. Borrowing can fuel economic growth, spur entrepreneurial activity, and enhance consumer quality of life. On the other hand, debt is the *sine qua non* of bankruptcy because the major economic benefit of bankruptcy is a discharge of most unsecured debts.³³ Mann uses bankruptcy as a proxy for financial distress throughout *Charging Ahead*. However, financial distress does not always lead to bankruptcy and, in fact, may occur without debt.³⁴ Extrapolating from bankruptcy to financial distress is further complicated by different legal regimes of debt relief among the countries that Mann studies (pp. 64, 66). Notwithstanding these issues, bankruptcy is the best available public, tangible way to quantify financial distress; no other measure of financial distress is comparable between nations. Further, research confirms that nearly all families arrive in bankruptcy in deep financial distress, struggling with both high debts and low incomes.³⁵

Mann posits that financial distress generates externalities that society must bear collectively and imposes serious consequences on individuals other than the borrower.³⁶ He relies on these externalities to justify his concern with any effect of credit cards on bankruptcy filings. Mann does not profess any sympathy for the plight of individuals suffering from debt. Claiming that his “approach is intended to be solely economic,” Mann emphasizes the social costs of financial distress to nonborrower parties

32. Presumably, Mann disciplines himself to use a credit card only when he intends to finance a transaction and relies on a debit card for spending activity. Despite my complete agreement with his conclusion about the appropriate relative uses of debit versus credit cards, I would never show Mann my credit card statement. Behavioral and cognitive barriers may hinder policy efforts to switch consumers to debit cards from credit cards. See *infra* notes 83–84 and accompanying text.

33. See 11 U.S.C. § 524(a) (2000).

34. Most obviously, a family can experience an income shortage (for example, caused by unemployment, the failure of an ex-spouse to pay support, or the death of a wage-earner) and not have any debt. The family simply has too few dollars to pay for necessary expenses; we may say that such families are “broke” but note that bankruptcy provides no income assistance to aid these families. See Katherine Porter & Deborah Thorne, *The Failure of Bankruptcy’s Fresh Start*, 92 CORNELL L. REV. 67, 121 (2006).

35. See SULLIVAN ET AL., *supra* note 11, at 70–72; cf. MARTIN RYAN, *THE LAST RESORT: A STUDY OF CONSUMER BANKRUPTS* 95, 128 (1995) (reporting income and debt figures from study of Australian bankruptcy debtors).

36. Pp. 49–50. Marshalling existing literature, he identifies several externalities of financial distress: harm to the dependents of the debtor, strain on the welfare safety net, reduction in workers’ economic productivity, and losses to other creditors.

(pp. 62–63) and assumes that at some undocumented level these externalities exceed the benefits from increased borrowing.³⁷

The book then examines the possible role of credit cards in financial distress. Mann deploys a regression analysis on aggregate, comparative data to isolate the effects of credit cards, macroeconomic factors, and country-specific differences on rates of bankruptcy. His key finding is that a rise in credit card debt leads to higher bankruptcy rates.³⁸ This effect does not depend on the significant and positive relationship between overall borrowing and bankruptcy. Even when overall borrowing is held constant, increased credit card borrowing correlates with higher bankruptcy rates (p. 66). Mann finds that “an increase of \$100 per capita in credit card debt would increase bankruptcy filings by about 200 filings per million” (p. 67). Bankruptcy rates climb as consumers exhibit stronger preferences for credit card borrowing over other forms of borrowing and as overall borrowing increases.³⁹ Mann uses the effects of time lags to establish which direction the relationship runs—from credit card use to bankruptcy rather than vice versa. A one-year lag is the best fit for the model, but the effects increase with longer lag periods. On the strength of this analysis, Mann suggests that regulating credit cards could reduce the bankruptcy rate and, by broader implication, the amount of financial distress in a society.

Applying Mann’s insights on these macroeconomic relationships to the behavior of individual families is complex. As Mann acknowledges, aggregate data do not reveal how the effects of credit card use are distributed across individual families.⁴⁰ The distribution could show that either a relatively small number of families in bankruptcy borrowed quite heavily on credit cards before bankruptcy or that nearly all families in bankruptcy modestly increased their credit card borrowing before bankruptcy. Identifying this pattern is critical to formulating effective credit regulation. Reforms could broadly target all users of credit cards, or alternatively, their impact could be limited to the types of families for whom credit cards create a particular risk of future financial distress.

Increased credit card use may precede bankruptcy for a variety of reasons. Families could borrow, in Mann’s words, with a “calculated indifference” to their repayment obligations (p. 63). These “strategic” debtors are posited to load up on debt before using bankruptcy as a financial planning tool to escape from their obligations.⁴¹ Alternatively, families could

37. See John A.E. Pottow, *Private Liability for Reckless Consumer Lending*, 2007 U. ILL. L. REV. 405, 412 (“To be sure, the case for negative bankruptcy externalities is more intuitive than empirical at this juncture.”).

38. Mann ran this model with varying lags between the independent variables and the bankruptcy rate. The sign and size of the coefficients were similar in each model. P. 71 tbl.5.3.

39. Ausubel, *supra* note 9, at 253; see also Ellis, *supra* note 9.

40. Mann notes that aggregate data cannot explain the reasons that people have large amounts of credit card debt. P. 62.

41. *Credit Card Practices Hearing*, *supra* note 26 (testimony of Todd Zywicki, Professor of Law, George Mason University Law School, 5–12, available at <http://www.house.gov/apps/>

borrow in response to an adverse event that causes a change in their income or expenses. If the adverse event is severe, these families could “crash” into bankruptcy mired in huge credit card debts that they could not repay even after the adverse situation abated. In yet another scenario, families could borrow gradually to improve their standard of living during times of financial stability, and this borrowing could heighten their overall financial risk (p. 64). Card use increased these families’ risk to a financial shock, helping them “slide” into deeper distress and, ultimately, bankruptcy. There are doubtless other formulations, and I suspect that families may use credit cards differently as staged responses to their deepening financial distress.⁴² *Charging Ahead* abandons an effort to untangle these relationships, relying on the aggregate relationship of cards to debt and bankruptcy to justify its reforms. To hone such regulation, research must examine how card use and its consequences vary among families and be cognizant of the importance of non-credit card factors in causing financial distress.

III. BROKE WITHOUT BORROWING

To illustrate the limits of the relationship between cards and financial distress, I offer original empirical data on “cardless” families. This sample comes from a longitudinal study of consumer bankruptcy debtors. These families virtually all incurred substantial credit card debt before bankruptcy, but many of them eschew credit cards after bankruptcy. The survey and interview data that I use herein enrich and complement Mann’s findings in *Charging Ahead*, illustrating the importance of family-level analysis of how credit card decisions map to financial well-being.

I find that despite restraint from any credit card use, many families report a worsening financial situation after a bankruptcy. On a microeconomic level, these families highlight a limitation of credit card reform. Cards may heighten a family’s risk, but the cards themselves do not create adverse financial events or low incomes.

A. Methodology

A vast majority of Americans have credit cards.⁴³ Given the ubiquity of credit cards in modern life, it is difficult to obtain a sample of non-credit card users for comparative analysis. The dataset of the Consumer Bankruptcy Project III (“CBP”) facilitates study of how families’ financial situations are related to credit card use because many families avoid credit

list/hearing/financialsvcs_dem/htzywicki042607.pdf); Ronald J. Mann, *Bankruptcy Reform and the “Sweat Box” of Credit Card Debt*, 2007 U. ILL. L. REV. 375, 403 n.16.

42. Cf. Sumit Agarwal et al., *The Age of Reason: Financial Decisions Over the Lifecycle* (Mass. Inst. of Tech. Dep’t of Econ., Working Paper No. 07-11, 2007), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=973790 (analyzing how borrowing decisions change over individuals’ lifetimes).

43. 74.9% of families had credit cards in 2004. Bucks et al., *supra* note 17, at A31; see also Weston, *supra* note 17.

cards after bankruptcy.⁴⁴ I term this group “cardless” families, a concept developed further in this section.

The CBP is a multiresearcher, interdisciplinary study of American consumer bankruptcy cases filed in 2001.⁴⁵ The core sample consisted of 1250 cases drawn equally from five judicial districts.⁴⁶ The core sample contains both Chapter 7 and Chapter 13 cases,⁴⁷ but I limit the analysis here to Chapter 7 cases. Because families who file Chapter 13 remain under court supervision for a period of years, their financial decisions are regulated and monitored.⁴⁸ The sample was constructed by asking bankruptcy debtors to complete a written survey that was distributed at a mandatory meeting during the bankruptcy process. As with most survey research, selection bias could limit the sample’s usefulness in generalizing about the bankrupt population, but a high response rate and prior analysis soften this concern.⁴⁹ The cases in the CBP sample were filed in 2001, more than four years before the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.⁵⁰ Although that law made extensive changes to the consumer bankruptcy system, the reforms do not limit the data’s usefulness for examining how card use bears on financial distress.

Four instruments provide data: the initial survey; public bankruptcy court records that detail each debtor’s assets, liabilities, and income; a telephone interview conducted approximately one year after each debtor’s bankruptcy; and a telephone interview conducted approximately three years after each debtor’s bankruptcy. Response bias is a potential flaw with all instruments other than the court records. Mann identifies this drawback of survey data as a benefit of his aggregate approach, noting that families may be unable to accurately report their borrowing activity (p. 61). The blunt reality is that no ideal data set for household-level financial analysis is cur-

44. Regardless of the actual size of the household, a debtor’s marital status, or whether the bankruptcy case was filed as a single or joint petition, I use the word “families” to describe the individual or individuals who filed bankruptcy and their dependents, if any.

45. Several published accounts have extensively described the methodology of the Consumer Bankruptcy Project. See WARREN & TYAGI, *supra* note 11, at app.; Robert M. Lawless & Elizabeth Warren, *The Myth of the Disappearing Business Bankruptcy*, 93 CAL. L. REV. 743, 769 (2005); Porter & Thorne, *supra* note 34, at app. The Consumer Bankruptcy Project was funded by the Robert Wood Johnson Foundation, the Ford Foundation, Harvard Law School, and New York University Law School. All data from the CBP included in this Review is on file with the author.

46. The five districts sampled were Central District of California, Northern District of Chicago, Eastern District of Pennsylvania, Middle District of Tennessee, and Northern District of Texas.

47. Of the 1250 cases, 780 were filed as Chapter 7 bankruptcies. The remaining 470 were Chapter 13 cases.

48. Katherine Porter, *Bankrupt Profits: The Credit Industry’s Business Model for Postbankruptcy Lending*, 93 IOWA L. REV. (forthcoming May 2008) (manuscript at 46) (explaining legal constraints on credit access after filing Chapter 13 bankruptcy).

49. See Porter & Thorne, *supra* note 34, at 127.

50. Pub. L. No. 109–8, 119 Stat. 23 (codified in scattered sections of titles 11, 12, 15, 18, and 28 of the United States Code).

rently available.⁵¹ CBP data, however, can be useful to illuminate the interplay between credit cards and financial distress, even without requiring debtors to recall and divulge details about their credit card activity. The findings below do not purport to be definitive on the relationship between credit cards and financial distress but instead may modestly improve our knowledge on this complex dynamic. This perspective seeks to enrich and supplement Mann's work, rather than disprove it.

There are benefits and drawbacks to using a sample of former bankruptcy debtors for analyzing how card use affects financial health. A principal advantage is that bankruptcy debtors are not inherently adverse to or unfamiliar with credit cards. At the time of their bankruptcy, such families are even more likely to have credit cards than the general American population. CBP court record data show that 91.44% of all bankruptcy debtors had at least one credit card obligation.⁵² Further, these families virtually all incurred substantial credit card debt before bankruptcy.⁵³ Before bankruptcy, these families relied heavily on cards to make ends meet. Yet, after bankruptcy, many debtors report having no credit cards at all.⁵⁴ According to the CBP, about one-third of families who filed Chapter 7 bankruptcy still do not have a single credit card three years after bankruptcy.⁵⁵ Comparing these "cardless" families with cardholding families offers a novel perspective on credit card use and financial health.

The drawback to a sample of bankruptcy debtors is obvious. Because these families filed bankruptcy, their financial practices and experiences are not typical of all Americans. The cardless families in my sample are not identical, or necessarily even similar, to nonbankrupt American families who refuse to use credit cards, relying exclusively on other payment or borrowing devices. Neither are cardholding families representative of American credit card users in general. Bankruptcy itself may be a transformative eco-

51. Credit card companies have excellent data on individual level card use. Given the size of the largest card issuers, each company has a portfolio that reflects a diverse sample of households along demographic and economic criteria. The problem, of course, is that these data are not available for public use. See *infra* notes 80–82 and accompanying text.

52. $N = 1250$. It is possible that other debtors had credit cards at the time of their bankruptcy but did not owe any debts on these cards so they were omitted from the bankruptcy court records on debts. However, given the financial distress of the families at the time of their filing, any such effect seems unlikely or very small. Credit card debt is more frequently found in Chapter 7 cases (96.41%) than Chapter 13 cases (83.40%), a finding that is worth more detailed analysis than permitted in this Review.

53. The median Chapter 7 debtor in the core sample of the CBP owed \$19,404 in credit card debt (including retail and charge cards) at the time of their bankruptcy filing. The credit card debt data were obtained from each debtor's court records. Because credit card debts appear with other unsecured debts on debtors' bankruptcy forms, it is difficult to identify credit card debts with a high degree of accuracy.

54. Porter, *supra* note 48, at 27 (finding that one year after bankruptcy, only twenty-five percent of Chapter 7 bankruptcy debtors report having accepted *any* new form of credit).

55. The second round of telephone interviews was completed by 302 debtors, and the question on current credit cards was answered by 300 debtors. Thirty-four percent (102) of these families reported that they had no credit cards at all. This included both new cards accepted after bankruptcy and any cards that may have survived their bankruptcy (perhaps because they reaffirmed the debt).

conomic moment, radically altering the spending and borrowing habits of families. I rely exclusively on a comparative analysis between cardholding and cardless families, each group of which filed bankruptcy. While the findings may not be generalizable to all Americans, they present a framework for future individual-level research on the effects of credit card use.

*B. Income and Financial Well-being of
Cardless and Cardholding Families*

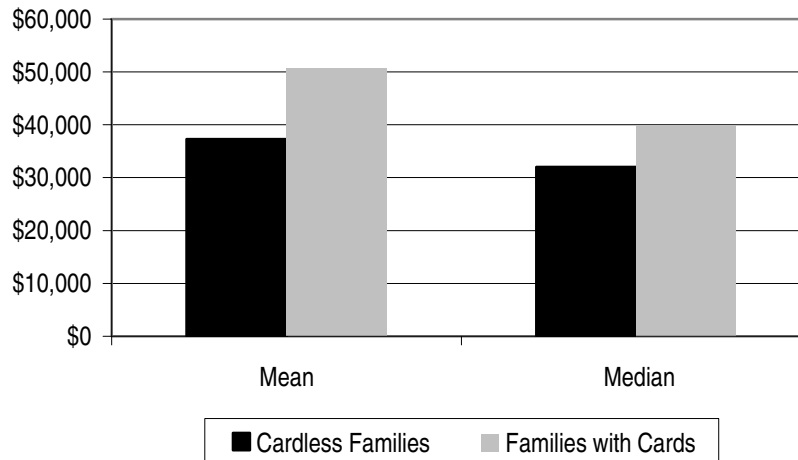
Analysis of individual-level data from the CBP shows that cardless families have different economic profiles than families who have credit cards. The most notable difference is that postbankruptcy families who use credit cards report higher incomes. Approximately three years after their bankruptcies, families in the study reported their annual household income before taxes.⁵⁶ Analysis shows a statistically significant relationship between whether a family has credit cards and its household income. The average family with credit cards has \$50,665 of annual pre-tax income. The average cardless family has about one-third less income, reporting household earnings of \$37,255.⁵⁷ This difference is statistically significant.⁵⁸ The median figures reflect the same pattern. Cardholding families earn more household income. The median for this group is \$40,000, compared to \$32,000 for cardless families. Families without credit cards have lower household incomes than families who have cards.

56. This income question was more likely to be refused than most questions, which is typical in surveys. See John R. Pleis & James M. Dahlhamer, *Family Income Nonresponse in the National Health Interview Survey (NHIS): 1997–2000*, 2003 AM. STAT. ASS'N SEC. SURV. RES. METHODS 3309, available at <http://www.amstat.org/Sections/Srms/Proceedings/y2003/Files/JSM2003-000666.pdf>. Of the 302 Chapter 7 debtors who completed the three-year mark telephone interviews, 275 answered the question on income. *Id.*

57. These figures are in 2004 dollars. Adjusted to 2006 dollars, the average card-holding family would earn \$54,071, and the average cardless family would earn \$39,760.

58. A *t*-test was performed to measure whether the difference between the means was statistically significant. $t = -2.643$. $p = .009$.

FIGURE I
FAMILY INCOME AFTER BANKRUPTCY



The income divide among card users and noncard users shown in Figure 1 has a number of possible explanations. One possibility is that families with lower incomes after bankruptcy remain too risky to attract credit card lenders. This is not a very likely hypothesis because the rampant marketing of credit cards to families after bankruptcy means nearly everyone can get a credit card.⁵⁹ The lesson of *Charging Ahead* is that credit cards are linked to financial distress. Yet, with this sample of families, the indications seem to point in the opposite direction. Families without cards are trying to make ends meet with fewer dollars. Refraining from cards during the years after bankruptcy does not seem to have improved these families' financial profiles, although the data do not address the possibility that only families with higher incomes chose to accept credit cards. A lower income reduces a family's ability to deal with unexpected expenses, sharpening the effect of an adverse event. Surprisingly, these cardless families appear to be at greater risk of further hardship than their card-carrying counterparts.

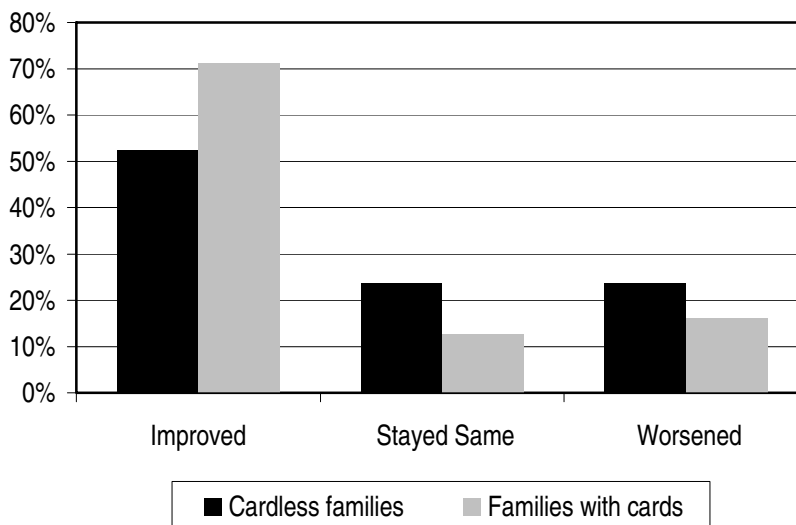
Other CBP data reinforce the income finding. Card use correlates with the trajectory of a family's self-reported financial well-being. Families were asked to compare their financial situation at the time of the interview approximately three years after bankruptcy with their financial situation immediately *after* they filed for bankruptcy.⁶⁰ Families with credit cards were more likely to report that their financial situation had improved as

59. See Porter, *supra* note 48, at 40; Caroline E. Mayer, *Bankrupt and Swamped with Credit Offers*, WASH. POST, Apr. 15, 2005, at A1.

60. The exact query posed was, "When you compare your financial situation NOW with your financial situation immediately AFTER you filed for bankruptcy, has it improved, stayed about the same, or gotten worse?" Three families chose the response that they "didn't know" the answer to this question. Data are from the 299 respondents who answered the question.

years elapsed after their bankruptcy. Cardless families were overrepresented in the group whose financial situation had worsened postbankruptcy.⁶¹ These differences were statistically significant.⁶² Refraining from cards does not seem to have aided these families in improving their financial situations.

FIGURE 2
SELF-REPORTED CHANGE IN FINANCIAL SITUATION THREE YEARS AFTER
BANKRUPTCY



One interpretation of these correlations is that credit cards themselves may be a reason that families report an improved financial situation. Cards may give a family a false sense of financial health by allowing it to increase its spending. By borrowing on cards to meet expenses, the cards could be boosting their living standard. While these families are incurring debt to achieve this effect, the low minimum payments on card balances alleviate the immediate pinch.⁶³ It may take years for families to appreciate the consequences of card use. Cardless families who must pay cash come to direct

61. It is disheartening to see any substantial fraction of families report that their financial situation has worsened after their bankruptcy. This erosion of bankruptcy's fresh start just three years after bankruptcy exposes the difficulty that some families have in achieving and sustaining financial recovery—despite a bankruptcy discharge. The findings reported here come from the second round of interviews conducted three years after bankruptcy. Previous research has analyzed how families fare one year after bankruptcy and examined the reasons that some families report post-bankruptcy financial problems. See Porter & Thorne, *supra* note 34.

62. A chi-square analysis was used to evaluate the data. The Pearson chi-square value was 10.743. The *p*-value was .005.

63. See p. 194 n.21; Memorandum from Office of the Comptroller of the Currency, Account Management and Loss Allowance Guidance 3 (Jan. 8, 2003), available at <http://www.federalreserve.gov/BoardDocs/press/bcreg/2003/20030108/attachment.pdf>.

terms with the economic realities of their incomes each month. In this way, cards could facilitate financial distress in the long term because they permit a family to defer difficult budgeting issues. This dovetails with the observation in *Charging Ahead* that the unique element of credit cards is their dual function as either a payment device or a borrowing device. Because consumers can decide later whether they wish to pay off their charges or finance them over time, the spending decisions and borrowing decisions occur separately. Consumer Bankruptcy Project data do not reveal the degree to which cardholding families used their credit cards for spending or borrowing. In the short-term, however, card use corresponds with an upward-trending financial outlook.

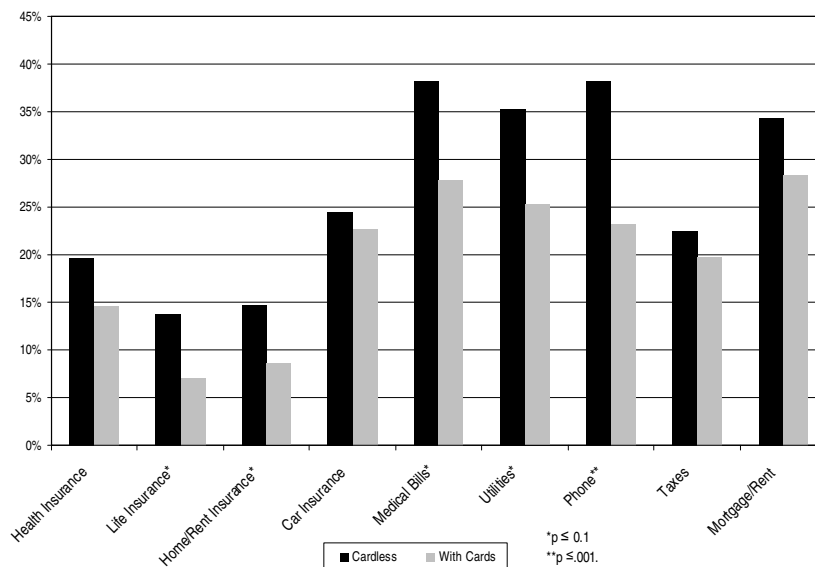
Another measure of a family's financial situation is their ability to meet current expenses. In the CBP interviews, families were asked whether they were struggling to pay a particular type of bill.⁶⁴ Responses to this inquiry are shown in Figure 3. For every bill, cardless families were more likely to report difficulty in payment. However, the differences between cardholders and the cardless were not statistically significant for each bill.⁶⁵ Life insurance, homeowners' insurance, medical bills, and utility bills were significant at the ten-percent level. Phone bills were significant at the one-percent level. These data offer additional support for the prior finding that postbankruptcy families without credit cards experience greater financial difficulties.

64. The following language was used for this question: "Some people have told us that even after bankruptcy, they are still struggling to pay some of their bills. As I read the following list, would you tell me if you are struggling to pay that type of bill?" The list included credit card bills, health insurance, life insurance, homeowners'/renters' insurance, automobile insurance, medical bills, utility bills (heat, water, garbage, etc.), phone bills, taxes (property and income), mortgage or rent payments, student loan payments, and child support or alimony.

65. The chart below gives the value of the Pearson coefficient and the related *p*-value for each type of bill.

	Health Insurance	Life Insurance	Home/Rent Insurance	Car Insurance	Medical Bills	Utilities	Phone	Taxes	Mortgage/Rent
Pearson Chi-Square	1.213	3.523	2.646	0.120	3.422	3.32	7.462	0.334	1.159
<i>p</i> -value	0.271	0.061	0.100	0.729	0.064	0.068	0.006	0.563	0.282

FIGURE 3
DIFFICULTY IN PAYING BILLS



With the exception of medical bills, none of the bills shown in Figure 3 are usually paid with credit cards, although increasingly every type of bill can be paid this way.⁶⁶ Assuming that families in both groups are paying most of these bills with a payment form other than a credit card (such as a check or automatic bank account withdrawal), cardless families' increased difficulty in bill paying is provocative. Cardholding families may be making routine use of cards for routine purchases such as food or clothing. That credit card spending at the checkout lane may become credit card borrowing at bill-paying time, freeing up families' incomes to meet other expenses. By stretching their incomes further, these families may find it easier to pay their monthly bills.

Along three measures of financial well-being (income, self-reported financial status, and difficulty with bill-paying), I find that families who eschew credit cards after bankruptcy fare worse than those who accept cards. Aggregate data may show a strong and positive relationship between credit card use and bankruptcy in the aggregate, but at an individual level the effects of credit cards on financial well-being are complex.

C. Conclusions from Research

My findings demonstrate that credit card use does not necessarily correlate with worse financial outcomes for individual families. Indeed among

66. See, e.g., Lingling Wei, *AmEx Plans Mortgage Rewards*, WALL ST. J., May 23, 2007, at D4.

former bankrupts, those who have cards seem to be better off than those who lack cards. These data illustrate the usefulness of individual-level empirical research for assessing the potential of credit card reform. The findings also support my critique that credit card reform is an incomplete solution to the problem of financial distress.

As a prefatory matter, I emphasize that my data are from families who filed for bankruptcy. Research on a broader population may show a different pattern between credit cards and financial well-being. With the findings presented here, the principal accomplishment perhaps is to emphasize the potential to test the aggregate dynamic between cards and financial distress on a household level, rather than relying solely on aggregate data.

Notwithstanding this limitation, these data are provocative because they confound expectations about credit cards and financial distress and refute the general relationship that Mann identifies in *Charging Ahead*. Spinning out the reasons for these findings highlights the complexity of the connection between credit cards and financial distress. One hypothesis is that families who accept cards actually achieve improved financial situations. Cardholding families earn higher incomes and are more likely to report improved financial situations. At least for the relatively short period measured by these data (three years), cards do not correlate with financial harms. This outcome may reflect postbankruptcy families' heightened awareness about the risks of cards. Having incurred substantial credit card debts before filing bankruptcy, some families may refrain from accepting a credit card if their financial situation is tenuous or their income is low. These consumers may remember the ways credit cards contributed to their financial collapse into bankruptcy and consciously be refusing to obtain credit cards for fear of worsening their financial prospects. This behavior toward credit cards could be particularly prevalent among the bankrupt sample examined here. Data on the general population could test whether a similar pattern exists: do people stop using cards if they struggle to pay credit card debts?⁶⁷ The results would help measure the extent to which bankruptcy transforms financial decision making,⁶⁸ particularly with regard to discretionary spending. Families may themselves be capable of making insightful choices about whether they can manage a credit card, but such lessons may only be learned through years of experience and painful struggle to repay card debts.

A related hypothesis is that cardholding families may be less likely to report a strained financial situation because their use of credit cards deludes them about the realities of their financial condition. On a family level and in the short term, credit cards may be palliative, masking the pain of income shortages, unexpected expenses, or prodigal behavior. Credit cards may delay families from facing difficult financial realities; the ability to borrow on

67. See Angela K. Littwin, *Beyond Usury: A Study of Credit Card Use and Preference Among Low-Income Consumers*, 86 TEX. L. REV. (forthcoming 2008) (reporting that non-bankrupt, low-income women who had difficulty repaying credit card debts gradually reported trying to avoid credit cards and use other forms of borrowing).

68. See generally Porter, *supra* note 48.

cards buoys their perceived financial status and aids them in paying bills. This function of a credit card seems destructive, at least if used in this manner for any sustained period. Confronting the realities of their financial situations without resort to borrowing may give families the best options for responding to financial pressures from gaps between income and expenses.⁶⁹ While credit cards may relieve the strain of short-term financial distress, the findings in *Charging Ahead* suggest that, in the aggregate, the use of credit cards increases financial distress. More research on the relationship between upward-trending card use and bankruptcy at the individual level would help determine whether cards are a useful “lifeline” for families struggling with financial distress (p. 63), or just a “cement life raft,” which families cling to as their distress deepens into financial collapse or bankruptcy.⁷⁰

This brief look at a particular subset of “cardless” families—former bankruptcy debtors—suggests that policymakers should refrain from pinning too much hope on credit card reform to substantially reduce financial distress. Card reform is likely to reduce the bankruptcy rate, as Mann shows, but the data highlight the reality that families will nonetheless continue to suffer from the economic fallout of job layoffs, illness, injury, or divorce. Helping families weather these adverse events may require more than credit card reform.

IV. REDIRECTING CARD REFORM

Charging Ahead proposes several legal reforms that could reduce the contribution of cards to financial distress. Rather than complain that these reforms are too tentative, I critique the tendency in current policymaking to view sweeping credit card reform as a panacea for bankruptcy and financial distress. Collectively, the greater hardship of the cardless postbankruptcy families highlights the limits of credit card reform to reduce financial distress. I end the Review with brief discussion of how payment cards (including credit cards) could actually be incorporated into solutions for financial distress.

A. *The Limits of Card Regulation*

The regulatory proposals in *Charging Ahead* are designed to constrain undesirable credit card use. Mann divides these reforms into two categories. The first group of proposals attempts to curb the use of credit cards as a payment device because credit card spending (apart from credit card debt) increases total consumer debt (Part IV). The thrust of these proposals is to regulate interactions between cardholders and card issuers. Each reform is relatively modest in scope, targeting a limited aspect of cards’ attractiveness as payment devices, such as affinity programs (pp. 167–71). Given the bil-

69. WARREN & TYAGI, *supra* note 11, at 266.

70. *Id.* at 123–62.

lions of card transactions each year, however, a slight shift in consumer payment preferences could dramatically lower overall consumer debt.

The second group of reforms tackles the ways in which credit cards may stimulate undesirable borrowing (Part V). Mann is cautious here, exhibiting a libertarian fear of overregulation and an economic deference to the overall benefits of borrowing (pp. 178, 188, 207). Policymakers should carefully consider Mann's recommendations, but not allow them to distract their attention from the underlying causes of financial distress. Credit card reform should dampen the bankruptcy rate, but it does not substitute for improving the social safety net to catch those who experience dramatic income losses or catastrophic expenses from illness or injury.

The cardless families offer an illustrative reminder that financial distress can occur without credit cards. Job layoffs, cancer, premature infants, and failed marriages are exogenous to card use.⁷¹ On an individual level, cards may be used differently by some families than others, and cards themselves do not cause the adverse events that exist in the vast majority of bankruptcies. Along these lines, a cardless family's greater likelihood of experiencing a precarious financial situation after bankruptcy illustrates the multiple contributors to financial risk. The lower incomes of cardless families make it harder for them to save. These families simply have fewer dollars to meet routine bills and thus fewer dollars left for savings. Admonitions to save do not tell these families how to make ends meet on incomes that are below those of most American families.⁷² The ability to save turns, in part, on the ability to earn. Yet, it is hard to see how card use determines income. The cardless family data make a simple point: one can eliminate cards entirely for a sustained period of years and still face privations and eroding financial health.

While Mann convincingly shows that, in sum, increasing card use leads to more bankruptcies, cards are only part of a family's debt dilemma. Indeed, cards may be merely the "front man" for bankruptcy, miring families in more debt, thus heightening a family's vulnerability to bankruptcy when an adverse financial event occurs. Using cards to cope with unexpected expenses or a low income may increase the chances of bankruptcy as an ultimate outcome to hardship.⁷³ Thus, the role of credit cards in financial

71. Three decades of Consumer Bankruptcy Project research shows that a substantial majority of consumers experience either a decline in income, illness or injury to self or a dependent, or a family breakup in the two years before bankruptcy. SULLIVAN ET AL., *supra* note 11, at 186; WARREN & TYAGI, *supra* note 11, at 84; Elizabeth Warren, *Financial Collapse and Class Status: Who Goes Bankrupt?*, 41 OSGOODE HALL L.J. 115, 126–27 (2003).

72. The 2004 median household income was \$44,389. U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES: 2007, at 447 tbl.673 (2007), available at <http://www.census.gov/prod/2006pubs/07statab/income.pdf>.

73. Existing family-level data on credit card use and bankruptcy is limited. See *supra* text accompanying notes 70–71. The last extended discussion of credit cards and bankruptcy was based on data collected in 1991. See, e.g., p. 60–69; SULLIVAN ET AL., *supra* note 11, at 285. Given the growth in card use in America and the continued marketing of cards to subprime customers with risky credit, these data may be outdated. More recently, Elizabeth Warren and Amelia Tyagi de-emphasized credit cards as a "cause" of bankruptcy. WARREN & TYAGI, *supra* note 11, at 131, 230 n.28.

distress could be an incremental one. This card-driven effect should not distract from the primacy of income for household well-being.⁷⁴ Steady income facilitates planning for future financial problems, while income shocks make credit card spending and its deferral of consequences more attractive.⁷⁵

An unexplored element of this dynamic is the role of savings and its relationship with card use. Mann does speculate that the real harm of credit cards may be that they lead consumers to divert income toward spending, rather than savings.⁷⁶ He then somewhat blithely dismisses the relationship between savings and credit cards, deeming it of “little concern” to his analysis (p. 56). Yet savings of a few months’ income could help consumers weather a moderate reduction or temporary stoppage of income.⁷⁷ Savings are also a vital cushion against unexpected expenses. The dichotomy between spending and saving appears crucial to preventing financial distress, but the connection between spending and saving remains a mystery.⁷⁸

The policy reality is that it is easier to focus on credit cards as a tangible marker that accompanies bankruptcy than to tackle directly the problems of income volatility, stagnant wages, and spiraling health care expenses. The latter focus raises fundamental questions about whether individuals or society should bear the risks of a market economy. Credit card reform seems imminent.⁷⁹ The proposals in *Charging Ahead* merit consideration by Congress. They are grounded in empirical reality about card use, enhancing the chances that the reforms will work in a desirable way and limit undesirable side effects of regulation. However, the data on cardless families warn against excessive optimism about the potential of card reform, serving as a reminder that the larger problems driving financial distress are risks unrelated to card use.

Jean Braucher has pointed to the limitations of Warren and Tyagi’s analysis of these data and suggested alternate interpretations. Jean Braucher, *Middle-Class Knowledge*, 21 EMORY BANKR. DEV. J. 193, 211–16 (2004).

74. See Braucher, *supra* note 73, at 202–03; Porter & Thorne, *supra* note 34, at 94–98.

75. JACOB S. HACKER, *THE GREAT RISK SHIFT: THE ASSAULT ON AMERICAN JOBS, FAMILIES, HEALTH CARE, AND RETIREMENT—AND HOW YOU CAN FIGHT BACK* 27–29 (2006) (describing a fivefold increase in income instability between 1970 and 1990 and attributing that risk to job insecurity, erosion of state benefits, and other new risks to American households).

76. P. 49 (“Furthermore, excessive credit card spending or debt might lead to a reduction in savings.”).

77. WARREN & TYAGI, *supra* note 11, at 24; see generally G. VICTOR HALLMAN & JERRY S. ROSENBLUM, *PERSONAL FINANCIAL PLANNING* (2003); LIZ PULLIAM WESTON, *DEAL WITH YOUR DEBT: THE RIGHT WAY TO MANAGE YOUR BILL\$ AND PAY OFF WHAT YOU OWE* (2006); JOHN L. WHITE, *I’M IN DEBT, OVER 40, WITH NO RETIREMENT SAVINGS: HELP!* (2004). The importance of savings can be overstated. Severe and permanent hardships are difficult or impossible to insure against with savings, and private insurance for such events is often expensive or unavailable. For example, an infant with profound special needs may severely strain a family’s financial resources for decades.

78. See pp. 50–51 (“Similarly, deferred consumption and savings can provide a backup cushion against risks for which insurance is not available.”).

79. H.R. 873, 110th Cong. (1st Sess. 2007); S. 1176, 110th Cong. (1st Sess. 2007); S. 1309, 110th Cong. (1st Sess. 2007); SULLIVAN ET AL., *supra* note 11, at 254–55.

B. Advancing the Regulatory Agenda

As an adjunct to combating harmful effects of cards, reforms could harness consumers' preferences for plastic payment to reduce financial distress. Proponents and opponents of credit cards and other payment cards agree on their tremendous power to alter consumer transactions. My proposals identify card research or card reform that exploits cards' power.

The first is informational. Credit cards generate more detailed transactional records than other forms of payment, such as cash or checks. Credit card companies have the ability to categorize these expenditures by type,⁸⁰ to measure how the frequency and value of transactions change in response to changes in interest rates or in the period before a customer bankruptcy, and to compare card use across demographic and economic groups. Such data would be complete and accurate, two significant improvements over the current individual-level data. However, card issuers' data are proprietary, and companies have only infrequently granted access to researchers.⁸¹ Recent efforts to improve the quality of public statistics on credit cards, while a definite move in the right direction, would not provide family-level data.⁸² Research needs aside, the agencies charged with regulating credit cards such as the Office of the Comptroller of the Currency cannot intelligently evaluate the utility and safety of a lending product without knowing, in any meaningful sense, how that product works. As credit cards have replaced cash and paper checks, the opportunities for data documenting consumer financial decisions and their relationship to financial distress have increased. Yet this potential remains untapped, leaving policymakers to operate on assumptions or aggregate analyses about card effects.

A second innovation would focus on encouraging savings. New card products attempt to draw on the allure of cards to stimulate savings, typically providing a very small contribution from the card issuer to a savings account.⁸³ These cards function as an alternative to rewards programs, which Mann criticizes for unduly influencing consumers to prefer credit cards to debit cards.⁸⁴ The current "savings" cards are fairly useless because of their

80. Indeed, some companies provide annual statements to cardholders that show a breakdown of one's total spending by category. See Tyler Thomas, *Use Your Chase Credit Card as a Budgeting Tool*, CREDIT CARD BLOG, Sept. 18, 2007, <http://blog.creditcardflyers.com/2007/09/18/use-your-chase-credit-card-as-a-budgeting-tool/> (last visited Oct. 1, 2007).

81. See, e.g., Agarwal et al., *supra* note 42, at 15; Michael E. Staten & Fred H. Cale, *The Impact of Opt-In Privacy Rules on Retail Credit Markets: A Case Study of MBNA*, 52 DUKE L.J. 745, 772 (2003).

82. See Stop Unfair Practices in Credit Cards Act of 2007, S. 1395, 110th Cong. (1st Sess. 2007); Credit Card Accountability Responsibility and Disclosure Act of 2007, H.R. 1461, 110th Cong. (1st Sess. 2007).

83. Dana Dratch, 'Spend to Save' Credit Card: Can it Work for You?, BANKRATE.COM, Oct. 1, 2006, <http://www.bankrate.com/brm/news/sav/2006savmg/savings-cardsa1.asp?caret=17> (last visited Sept. 8, 2007) (describing variety of savings-linked credit cards).

84. Mann recommends banning reward programs as a tool to curb imprudent credit card use, observing that these programs "are a major part of the competition by which different issuers retain customers and encourage them to spend." P. 167.

small effect. However, the savings concept could be more deeply integrated into credit card transactions, for example by affirmatively prompting consumers to make a savings contribution at the point of sale. As payroll cards become more popular,⁸⁵ a type of “swipe to save” initiative that allows a transfer from the card to a savings account to occur automatically upon the card’s first use would deter an impulse to spend the card to zero. To the extent that card use is a habit, strategies for savings that tap into the convenience and efficiency of cards could be fruitful. If regulators had data on the efficacy of the new savings cards, they could begin to evaluate the usefulness of this proposal.

Advances in credit card technology may permit improved disclosures at the point of sale. Mann describes the Japanese system of *ikkai barai* in which a cardholder must make an affirmative decision about whether a transaction will be immediately paid or borrowed—and if the latter, over what period.⁸⁶ He proposes adapting this idea of point-of-sale disclosure to prevent consumers from mistakenly incurring fees for over-the-limit transactions (p. 163). This idea has great merit, harnessing card technology and Americans’ card habit to improve financial practices. I would suggest that advising consumers of the amount of their current card balance at the point of sale could have a further benefit that Mann does not identify, which is to dampen additional spending. For example, I speculate that consumers may use their cards less in the days immediately after they receive their card statements after the shock of seeing the monthly bill. Point-of-sale balance disclosures would mirror the practice of some automated teller machines, which include the account balance on the receipt after any transaction.

While the current thrust of card reform is to curb those practices seen as most egregious,⁸⁷ the relationship between credit card use and bankruptcy requires reform aimed at more subtle alterations of the entire payment card market and consumer economy. Mann’s novel proposals meet these criteria, but will not alone suffice to make substantial inroads in reducing the incidence and severity of financial distress in America.

CONCLUSION

Credit cards are a global phenomenon with consistent macroeconomic effects, not a mere sign of American prodigality to be attacked with moral castigation about the good old days of cash. Embracing card technology for its positive transactional benefits requires attention to the possible harms of cards. Mann’s analysis reveals a consistent, cross-jurisdictional pattern of

85. See Samuel Frumkin et al., *Payroll Cards: An Innovative Product for Reaching the Unbanked and Underbanked*, COMMUNITY DEVS. INSIGHTS, June 2005, at 1, 2, available at <http://www.occ.treas.gov/Cdd/payrollcards.pdf>; Gail Hillebrand, *Questions for Employees to Ask About Payroll Cards*, CONSUMERSUNION.ORG, Jan. 2006, http://www.consumersunion.org/pub/core_financial_services/000920.html (last visited Sept. 8, 2007) (advising consumers to ask about using a payroll card to save).

86. P. 163; Mann, *supra* note 21, at 1074–75.

87. See S. 1395, 110th Cong.

undesirable credit card effects. His research indicates that credit cards stimulate excessive borrowing and that card use correlates with higher bankruptcy rates. Serious policymaking should abandon wholesale arguments against credit cards and incorporate Mann's recommendation to shift non-borrowing card use to debit cards.

The new data presented in this Review highlight the importance of extending credit card research to document the variations in card use among families. The finding that cardless families can struggle with financial problems emphasizes the importance of approaching credit card reform as only a single building block in constructing a defense against bankruptcy and financial distress. Further research would help isolate the importance of factors such as income and savings in shielding families from bankruptcy and identify how card use intersects with families' financial stability.

