

Credit cards and access to the digital marketplace:  
A priceless necessity?

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## EXECUTIVE SUMMARY

The use of a credit card is becoming more and more important for consumers as electronic payment methods and networks proliferate in the Canadian marketplace. Credit cards are essential for renting cars or hotel rooms, purchasing airplane tickets or making purchases online. The credit card is rapidly evolving into the preferred mode of payment for the 21<sup>st</sup> century.

Unfortunately, there is a growing class of people in Canada who are not able to easily access the features and benefits of a credit card. This group of people includes large numbers of new Canadians, aboriginals and people with no previous credit history. It is this group that is the principal focus of this report. In general terms, the objectives of our study were to describe:

- What are the main consequences of not having access to credit cards in consumers' financial lives, and;
- To what extent does this group find other financial products as substitutes, and whether the unavailability of a credit card precludes them from meaningfully engaging in electronic commerce and electronic payment transactions?

In order to better understand this group of consumers, focus groups were conducted in Toronto to discuss their credit histories and experiences regarding credit cards. Panel members were all employed but did not have credit cards.

In addition to examining the role of the credit cards in the lives of Canadian consumers and the effects that a lack of access to credit cards may have on them, the report also provides a history of credit cards, an overview of the Canadian credit card market and presents some possible alternatives to credit cards for Canadian consumers.

The report concludes by making policy recommendations that seek to assist and protect Canadian consumers who are not able to obtain a conventional credit card. The recommendations are as follows:

- 1 A consumer's credit rating is taking on increasingly important social and economic dimensions. Therefore, consumers need more options to build their credit ratings outside of conventional or secured credit cards. The credit reporting system should not become a barrier or a burden for consumer access to electronic payments and economic activity.
- 2 Under the current recession affecting the household sector in Canada, an electronic payment method that could help users with no credit history to more actively engage in electronic transactions at a minimal would help to ease economic tensions. Pre-paid and secured credit cards are inadequate and too costly to fill such a role.

- 3 It is important to ensure that a reputational or creditworthiness system allowing for enhanced access exists that provides consumers with specific and detailed reasons why access is declined. This will afford her a reasonable opportunity to build such essential financial record.
- 4 Both the government and credit card issuers could work together in crafting a scheme that could facilitate the creation of a new financial product. This product could serve as a financial credential and be also used as the key component of a payment system that can be recognized by issuers' networks and databases. Eligibility for such payment method could be proportional to income level, so as to avoid a lower income becoming a barrier to build a level of creditworthiness according to a consumer's means.
- 5 There are potential efficiencies that could be gained by enhancing access to the cash-only population to the online and E-commerce market. The access would not be intended to induce them to accumulate debt. Instead, it allows them to engage in economic activity through electronic-based transactions in a way that they would otherwise be unable to do so.
- 6 The increase in the number of credit checks as an employment screening practice is a growing privacy concern. Indiscriminate credit checks for employment purposes should be avoided, and only be conducted upon specific consent granted by the applicant.
- 7 When declining a consumer's credit card application, the consumer does not always receive the reason for the refusal. Creditors and credit reporting agencies should offer reasons for refusals to the customer to give them a reasonable opportunity to be approved.
- 8 Under the current system, immigrants and new Canadians are not given recognition of the fact that many of them arrive into Canada with credit cards issued in their original countries. It would be useful to create a way for new Canadian residents to be able to have their financial credentials given consideration when they apply for a credit card in Canada. Patronizing a multi-national bank may offer some form of a solution, but a more widespread solution needs to be made available to everyone.

If these recommendations were implemented, both Canadian consumers and merchants would stand to benefit by the greater adoption of secure, efficient electronic payment methods. This could lead to greater economic growth, providing a benefit to all Canadians.

## INTRODUCTION

The main features of credit cards and their efficiency as payment system are often overlooked. The criticism focuses on their credit feature; their most controversial aspect. Little is mentioned about the potential efficiency gains and cost savings to be realized by consumers, as well as merchants and issuers from expanding the user base of their electronic payment features. To date, seems to be a privilege enjoyed only by credit card holders. The reality for those Canadians who do not have access to credit cards is more complex than not having access to personal credit for emergencies and certainly more complex than simply not having access to a credit card. It is a lack of access to an efficient electronic payment method and a fair opportunity to build a credit history. This is what acts as an economic barrier for these Canadians.

An important finding that can be elicited from the respondents' answers is that having access to a credit card today means having access to the most widely accepted method of electronic payment. The participants were selected on the basis of having been declined or not having been able to start their credit history. They were fully employed; having no history of bankruptcy and being fully conversant with the internet. They indicated in their answers that not carrying a credit card imposed on them extra costs for many transactions. Some of the extra costs are imposed in the form of payment barriers to making purchases on the internet; others are for not being able to arrange activities such as leisure or travel. This study also attempts to relate the experiences of the respondents and in the first part explores credit cards as payment method and their centrality in building a credit history and also engaging in online transactions and payments. The second part discusses alternatives these consumers referred to in the study and their associated costs, some of which may be a form of financial exclusion.

Many Canadians are not able to establish a credit rating outside the use of a credit card. Being new to Canada can mean that unfair barriers, such as no established Canadian credit rating, preclude them from obtaining a credit card. This lack of Canadian credit rating is unfortunate, as it is unavoidable for many new Canadians. The use of credit cards in Canada, is among the highest in the world. However, many economically active and employed Canadians do not have the benefit of the electronic payment feature of credit cards and their credit-building feature.

## CREDIT CARDS IN THE CONSUMER MARKETPLACE

Issuing credit is an old and well-established practice. For some, credit cards as they are used today by consumers are perhaps one of the most important financial innovations of the twentieth century.<sup>1</sup> However, the first credit cards did not have the revolving credit features that most cards do today. The first cards of the mid 20<sup>th</sup> century were convenience cards; a payment system that allowed business travellers the ability to make payments without having to carry cash. For merchants, the client's ability to pay with a card represented a better means to verify the creditworthiness of the client. Credit cards payments were more reliable than payments made by cheque.<sup>2</sup> After the 1970s, advances in computer technology allowed the construction of networks and databases that enabled the processing of transactions across national borders.

The history of consumer credit in the form of instalment payments is separate from the history of credit cards. In the nineteenth century, instalments were used to facilitate the sale of goods such as furniture or sewing machines. Until the 1920s, there were fewer lenders extending credit to consumers compared to today. The ability of lenders to assess the creditworthiness of individual borrowers was also more difficult than it is today. Mass industrialization and the development of urban centres brought with them the need for credit to facilitate the rotation of inventories of mass-produced goods.<sup>3</sup>

Predecessors of the current credit card were the 'courtesy card' used in the 1900s by oil companies, as well as the 'charge-plates' issued by department stores, which allowed users to charge their purchases at associated stores within a limited geographic area. Full payment for purchases had to be made each month.<sup>4</sup> The instalment payment feature and the revolving credit feature were added to the plastic card payment method between the 1950s and 1960s.<sup>5</sup> These cards had similar features to today's Visa, American Express and MasterCard cards. The most significant change since that time has been the transition from a paper-based transaction clearing and settlement, to a paperless, digitized process.

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<sup>1</sup> Ronald J. Mann, *Charging Ahead, The Growth and Regulation of Payment Card Markets*, Cambridge University Press, New York, at 35.

<sup>2</sup> *Ibid.*

<sup>3</sup> Board of Directors of the Federal Reserve System, *Report to the Congress on Practices of the Consumer Credit Industry in Soliciting and Extending Credit and their Effects on Consumer Debt and Insolvency*, June 2006, online: Board of Directors of the Federal Reserve System <<http://www.federalreserve.gov/boarddocs/rptcongress/bankruptcy/bankruptcybillstudy200606.pdf>>.

<sup>4</sup> William Baxter, *Bank Interchange of Transactional Paper: Legal and Economic Perspectives*, *Journal of Law and Economics*, Vol. 26, October 1983, at 541-588.

<sup>5</sup> Lewis Mandell, *The Credit Card Industry, A History*, Twayne Publishers, 1990.

Diners Club was the first “travel and entertainment” charge card issued. It was used as a general-purpose card that allowed the cardholder to pay for purchases beyond their local geographic area.<sup>6</sup> It was followed in 1958 by the American Express’ Green Card. The use of these cards allowed consumers the convenience to buy any product from participating merchants and slowly introduced payment alternatives beyond month-end payment. The general-purpose credit card as it is known today was invented in 1966 when Bank of America established the BankAmerica Service Corporation. This company franchised the BankAmericard (a Trademark known today as Visa) to banks based across the country. To compete against BankAmericard, other banks joined efforts and launched the Interbank Card Association, later known as MasterCard.<sup>7</sup>

### **Credit cards as payment method**

Many of the practices used by credit card issuers to extract additional revenue from card holders have been widely reported and documented in the last few years. However, credit cards as payment method have enjoyed wide acceptance by consumers in the last decades.<sup>8</sup> There has also been a great amount of criticism concerning the credit solicitation strategies used by card issuers. These strategies may have resulted in encouraging inadvertent or incautious consumers to the territory of unsustainable indebtedness.<sup>9</sup> However, the central feature of credit cards is that they have predominantly been a convenient method of payment, whereas their credit function is less important. This fact that has been pointed at in scholarly studies since early in the development of the product:<sup>10</sup>

“Car tel est bien le premier role des cartes de credit, ces mal-nommées, qui servent d’abord et toujours à effectuer des achats de biens ou de services. L’élément de credit n’est qu’accessoire. Et l’on

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<sup>6</sup> Jerry W. Markham, *A Financial History of the United States*, Vol.3, M.E. Sharpe Ed., New York, December 2001, at 306.

<sup>7</sup> Stan Sienkiewicz, *Credit Cards and Payment Efficiency*, Federal Reserve Bank of Philadelphia, Discussion Paper, Payment Cards Center, August 2001, online: <[http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2001/PaymentEfficiency\\_092001.pdf](http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2001/PaymentEfficiency_092001.pdf)>.

<sup>8</sup> Sujit Chakravorti, *Theory of Credit Card Networks: A Survey of the Literature*, Review of Network Economics, Federal Reserve Bank of Chicago, Vol. 2 Issue 2, June 2003, online: Review of Network Economics <[http://www.rnejournal.com/artman2/uploads/1/chakravorti\\_june03.pdf](http://www.rnejournal.com/artman2/uploads/1/chakravorti_june03.pdf)>.

<sup>9</sup> John A. E. Pottow, Private Liability for Reckless Consumer Lending, University of Illinois Law Review, February 2007 (1), online: Social Science Research Network SSRN <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=960979](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=960979)>.

<sup>10</sup> Patrick Grayll Chabrier, *Les Cartes de Crédit*, Librairies Techniques, Paris, 1968, at 7.

parle plus justement de «cartes de paiement» ou de «cartes accréditives».”<sup>11</sup>

It can be argued that it is the payment feature what has made credit cards wildly popular and not the credit feature, despite popular belief. As mentioned in the above quote from a French legal author in 1968, the credit function is an accessory. This idea was raised in the answers of several of the people who were interviewed as part of this study’s focus groups. Among the most important reasons why they wanted to have access to a credit card was the fact that they could have access to a method of payment that is not only convenient but perhaps the most widely method accepted in today’s information economy.<sup>12</sup>

*“You wouldn’t have to carry a bunch of cash all the time if you were out shopping.”*

*“Cash, you don’t need cash. Pull it out; whip it out wherever you go.”*

*“You can rent cars, make reservations at hotels. You can buy on the internet.”<sup>13</sup>*

*“You need a credit card even to rent movies.”<sup>14</sup>*

To illustrate this point, there is the example of the consumer who likes to make online arrangements for travel or make purchases online. These are two important areas of electronic commerce. It is true that some online merchants accept debit payments by entering a bank account details. However this mode of payment is not well adopted and generally only local or national merchants i accept it.

Credit cards are most widely accepted electronic payment method worldwide. In order for consumers to have access to the actual payment method (the card), a consumer must apply for credit in most cases. This stipulation applies even if the consumer does not need credit at all but the card only, and its number. Access to the credit card number is what allows the consumer to make an online payment, regardless if credit is required to finance the purchase or not. Credit is a separate, distinct product tied to the original convenience card as payment method. There are exceptions to this general rule, but they are not well known to

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<sup>11</sup> *Ibid.*

<sup>12</sup> Many transactions cannot be engaged in solely by cash payment, such as a car rental and even a movie rental. As mentioned before, a debit card or a PayPal accounts are not as widely accepted for online purchases as credit cards are.

<sup>13</sup> Annex at 10-11.

<sup>14</sup> Annex at 22.

consumers. A limited number of credit cards are available to consumers that do not require the consumer to apply for credit. These are pre-paid credit cards and gift cards issued by the major credit card issuers in Canada. Both of these types of cards present a number of important disadvantages to consumers.

Pre-paid cards function the same way a conventional credit card does. They can be used to make purchases online, at merchants and may also be used abroad or at ATMs. They are much more expensive to use than conventional credit cards as many of their functions incur significant fees that are not charged to conventional card holders. There is typically an upfront fee for the card to be issued, a significant monthly maintenance fee, a fee for statements mailed to the consumer and a fee for live customer service. Some cards charge fees for every transaction debited to the account, for each use of an automated teller machine and even fees to add more money to the account. Clearly any user of a pre-paid credit card would incur much higher transaction costs than a user of a conventional credit card. This can represent a particular burden to low income consumers who do not qualify for a conventional credit card. Pre-paid cards represent an option to consumers who wish to have a credit card but do not qualify for a conventional card or do not wish to undergo a credit check. The fees imposed by pre-paid card issuers can rapidly add up to very significant sums. Because of this, they are a poor choice for many consumers, in spite of the benefits they offer.

Gift cards issued financial institutions such as Visa gift cards and Mastercard pre-paid gift cards. The cards are different from pre-paid cards in that they are not reloadable. Instead, consumers pay a smaller fee of a couple of dollars to purchase one and add funds to them. When the balance reaches zero, the card is no longer valid. Gift cards suffer from a number of disadvantages compared to conventional credit cards. First, is that gift cards are only a temporary solution for consumers. Consumers cannot link bills to them to pay them on a monthly basis, or use them for other similarly long term financial arrangements. The gift cards also charge a monthly maintenance fee which starts after a grace period. This grace period is typically 6 months and is exempt from provincial laws which forbid this practice for gift cards not issued by financial institutions. After a particular amount of time elapses, typically one year in Canada, the remaining balance is forfeited on the card and it is no longer valid. Gift cards cannot be used in automatic teller machines for cash advances. Additionally, some gift cards are not issued with the raised numbers and lettering of conventional cards which would make them incompatible with merchants who use the older carbon imprint card processing method. These factors make gift cards issued by a financial institution a poor choice for consumers in many scenarios. They are generally less costly than pre-paid credit cards but are hampered by fewer features.

An important element in the new payment systems landscape is that payment credentials have become directly linked to the economic reputation of the

individual. There are many products and services that could not be purchased without a credit card. From car and equipment rentals to travel arrangements and online transactions, there are many possibilities.

For the consumers in the study, it is certainly clear to them that utility of a credit card exceeds the benefit of being able to conveniently purchase items. Credit cards also connote a certain degree of status. For decades, credit card companies have relied heavily upon the premise of status and the nature of credit cards as a financial credential for the marketing strategies of their products. But while credit cards may have been seen as status symbols in the past, it is not so clear that they would be considered as such today. A large number of consumers use credit cards. Moreover, businesses such as gas stations, hardware stores, supermarkets and sports clubs issue them to consumers. No longer a status symbol, credit cards are now a widespread form of financial credentials.<sup>15</sup>

There are other benefits related to the use of credit cards that are perceived by consumers. In a recent discussion paper published by the Bank of Canada, a brief survey of economic literature on the topic is listed and included benefits such as widespread acceptance, speed and security of the transaction, simplified access to funds, record keeping, budgeting control and rewards such as incentive points or cash rebates.<sup>16</sup>

### **Credit card use and access to credit history building**

Today's consumers are faced with the necessity of having a credit history in order to operate in the modern financial marketplace. The relationship between consumer credit reporting agencies and credit card issuers is a very difficult one for consumers to avoid. Credit card issuers recently announced they intend to enter the Canadian debit card market.<sup>17</sup> Their close relationship with consumer reporting agencies could be an advantage over the Interac debit network if creditworthiness score were to be awarded for debit transactions performed

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<sup>15</sup> Stan Sienkiewicz, *Credit Cards and Payment Efficiency*, Federal Reserve Bank of Philadelphia, Discussion Paper, Payment Cards Center, August 2001, online:

<[http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2001/PaymentEfficiency\\_092001.pdf](http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2001/PaymentEfficiency_092001.pdf)>.

<sup>16</sup> Carlos Arango and Varya Taylor, *Merchant Acceptance, Costs, and Perceptions of Retail Payments: A Canadian Survey*, online: Bank of Canada <<http://www.bank-banque-canada.ca/en/res/dp/2009/dp09-8.pdf>>.

<sup>17</sup> Proceedings of the Standing Senate Committee on Banking, Trade and Commerce, *Oral Statement of Kevin Stanton, MasterCard Canada*, 22 April 2009, online: Parliament of Canada <[http://www.parl.gc.ca/40/2/parlbus/commbus/senate/Com-e/bank-e/05eva-e.htm?Language=E&Parl=40&Ses=2&comm\\_id=3](http://www.parl.gc.ca/40/2/parlbus/commbus/senate/Com-e/bank-e/05eva-e.htm?Language=E&Parl=40&Ses=2&comm_id=3)>.

through credit cards.<sup>18</sup> This possibility could compel many users to switch from Interac to a credit card franchise such as Visa or MasterCard. If debit payments made through a credit card were reported as credit card activity to credit bureaus they might help build a better credit record. Responsible use of a credit card is widely recognized as the best method for consumers to build a credit reputation in the form of a credit history. Participants in the focus groups were generally aware of this situation and of the role of a credit card as a means to build a credit rating, or damage it:

*“It can help you establish your credit if you don’t have any.”*

*“Like a personal reference when I want credit for a mortgage or something, if you want to buy anything, just show them your card. It’s like that, automatically accepted, because they already got all your information from when you applied for the card. Automatically you qualify.”*

*“You can ruin your credit if you misuse it.”*

*“It can damage your credit rating if you’re poor with your payments and what have you.”<sup>19</sup>*

Secured credit cards are by far, the most recommended method to start repairing a bad credit history or to build one from zero.<sup>20</sup> The credit “record” has been made increasingly essential for today’s consumers, to the point where it can determine eligibility for employment in many workplaces.<sup>21</sup>

*“Your credit report determines everything from qualifying for a loan, the rate you’ll pay on that loan, getting a new job, renting an apartment and obtaining car insurance.”<sup>22</sup>*

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<sup>18</sup> Rita Trichur and Dana Flavelle, *Taking a Swipe at the Debit Card Competition*, Toronto Star, 21 February 2009, online: Toronto Star <<http://www.thestar.com/Business/article/590977>>.

<sup>19</sup> Annex at 12.

<sup>20</sup> In Canada, for example, the Financial Consumer Agency of Canada explains that a secured credit card may be suitable for a consumers who have trouble being approved an unsecured credit card due to having no credit history; having bad credit and damaged credit history; having filed for bankruptcy or being new to Canada. See: Financial Consumer Agency of Canada, *Secured Credit Cards* (booklet), online: Financial Consumer Agency of Canada <<http://www.fcac-acfc.gc.ca/eng/publications/CreditCardsYou/PDFs/Secured-eng.pdf> >.

<sup>21</sup> Jonathan D. Glater, *Another Hurdle for the Jobless: Credit Inquiries*, New York Times, 9 August 2009, online: New York Times <<http://www.nytimes.com/2009/08/07/business/07credit.html>>.

<sup>22</sup> Visa Practical Money Guides, *Credit History: your credit history and how it affects your future*, (accessed February 2009) online: Practicalmoneyskills.com <[http://www.practicalmoneyskills.com/orders/pdfs/PMSFL\\_Guide\\_CreditHistory\\_1.pdf](http://www.practicalmoneyskills.com/orders/pdfs/PMSFL_Guide_CreditHistory_1.pdf)>.

Credit cards combine a payment system with credit features. The consumer who wants to have access to the convenience provided by the payment device is generally required to apply for credit as it is not possible to separate the two features. However, a credit application cannot be approved if the applicant has no recorded history with a credit bureau. However, the best way to establish a credit history is through the use of a credit card. Therefore, a consumer, who wants to be able to use a credit card as payment device, and not a credit device, must generally apply for credit. Conversely, a consumer who wants to establish a credit history (which is essential in today's increasingly sophisticated marketplace), is always strongly encouraged to start by obtaining a credit card first. Consumers who are not able to acquire a conventional credit card can build credit through the use of a secured credit card. This option represents a significant challenge for some consumers since it requires the applicant to set aside an amount of money for security equal to their credit limit. This figure can easily amount to several hundred dollars a consumer must commit in order to have a worthwhile credit limit. This option may not be viable for low income consumers.

Admittedly, consumers can simply forgo holding credit cards, but the cost can be significant, given that the credit card is a financial credential. The end result for such consumers is increased costs either by not having an efficient electronic payment method and /or as a consequence of not having a credit history or credit reference reported by a credit card issuer. For consumers, abstaining from the use of credit cards is usually not an efficient option. On the contrary, the rational consumer is compelled to use credit cards in order to achieve cost savings or even rewards. This applies only if the consumer chooses not to revolve a balance on their card:

*"It's like a catch-22, if they will give you a credit card, you need good credit history, but there's no way to have good credit history if you don't have a credit card."*<sup>23</sup>

*"I don't want to go into a whole bunch of political stuff, but it's just like that score, whatever it is, is who you are in this world. And, if you don't have that score, you're nothing and you're nobody."*<sup>24</sup>

*"Some ads you read, 'must pass criminal and credit check'. If you have bad credit, you ain't getting that job."*<sup>25</sup>

However, such credit can only be built upon previous use of credit. A financial reputation cannot be built without applying for a credit product that is reported to a credit bureau instead of just relying on some alternative payment method, like cash. In other words, while either a credit card or a line of credit may be useful to

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<sup>23</sup> Annex at 28.

<sup>24</sup> Annex at 27.

<sup>25</sup> Annex at 15.

build a credit history, a debit card, a cheque or cash, are not. Lines of credit may be much easier to obtain if the applicant is a credit card holder with a good record. A financial reputation in the consumer economy today can be largely determined by whether or not a consumer has been a credit card holder.

Credit card issuers and consumer credit reporting agencies are constitutive parts of a self-reinforcing system consumers avoid at their own peril. Both credit issuers and credit bureaus are tied products outside of which, a consumer's creditworthiness is presumed not to exist in most cases. In some instances, consumers originally from the United States may be able to carry over some of their credit history with them. One credit bureau operating in Canada, Trans Union, also operates in the United States and there is some evidence to suggest that they are able to transfer their American records to Canadian consumers' files.<sup>26</sup> Additionally, clients of large multi-national banks abroad may have an easier time acquiring credit from the same bank in Canada. Many banks rely upon internal scoring and risk assessment to make credit decisions for their clients. If a consumer had credit with a multi-national bank in another country, that bank may transfer that existing credit or award them new credit in Canada, as the situation warrants. Consumers who do not have credit records establish a personal credit line to establish a credit record, if they choose not to have a credit card.

For some commentators, the understanding of the incentives created by the payments system is essential to the understanding of the consumer credit system. The costs associated with the rewards consumers receive for using credit cards are borne by the merchants. These costs borne by merchants are ultimately passed on to consumers).<sup>27</sup> In fact, there is an emerging trend of charging merchants higher fees for accepting higher end credit cards that offer more generous or sophisticated reward programs. Merchant financial services providers argue that these consumers will spend more, since they have a more prestigious card. This change may just be a way of recouping the costs involved in providing more elaborate rewards to consumers. Because of rewards and other incentives, consumers will choose to favour credit cards payments over cash or debit. None of the focus groups participants had a credit history nor a credit card. However, some of their responses demonstrated knowledge of the kinds of rewards some credit cards entitle their holders to:

*“When you pay with an American Express you get free insurance for that rental car, and if you leave the country for a week or something like that, you pay for your airline tickets, maybe with*

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<sup>26</sup> <http://ezinearticles.com/?Does-Credit-History-Follow-You-Upon-Relocation-From-The-United-States-To-Canada?&id=671033>

<sup>27</sup> Sujit Chakravorti and William R. Emmons, *Who Pays For Credit Cards?* Federal Reserve Bank of Chicago Policy Studies, February 2001, online: Social Science Research Network SSRN <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=294482](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=294482) >.

*American Express or some of those cards, you get free Blue Cross.*<sup>28</sup>

In the online marketplace, notwithstanding the rewards, the use of a credit card is by far the easiest and most convenient payment method from the consumer standpoint. A mix of cognitive biases as well as documented behavioural economic behaviour can be used to explain the overuse of the credit card as a payment device into a borrowing device.<sup>29</sup> The end result is the creation of a number of undesirable social outcomes such as unsustainable indebtedness, erosion of household financial stability inflation and consumer bankruptcies.<sup>30</sup>

### **New Canadians and credit history**

For new Canadians in particular, building a credit history is very important. A lack of credit history may have the effect of delaying access to necessary goods or services or even employment, which can make a world of difference in the transition to a new life in Canada. Moreover, establishing a credit history is essential for access to significant purchases such as a car or a house. These purchases may be of importance to the national economy. Credit cards are seen as the best tool to start building a credit history by relevant stakeholders in the consumer credit landscape, including creditors, consumer credit reporting agencies, and government. The Financial Consumer Agency of Canada also views credit cards as an effective tool to build a credit history:

“It is important to have a credit history. If you don't have a credit history, you can begin building one by using a credit card - as long as you use the credit card wisely! (...) If you are having difficulty obtaining a credit card because you have no credit history, you are new to the country, you have recently filed for bankruptcy or you have had credit problems in the past, a "secured credit card" might be appropriate for you.”<sup>31</sup>

A well known website whose target audience is the new Canadian population also acknowledges the importance having access to the features offered by a credit card and recommends:

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<sup>28</sup> Annex at 11.

<sup>29</sup> Supra note 9. [Pottow].

<sup>30</sup> Adam J. Levitin, *Priceless? The Social Costs of Credit Card Merchant Restraints*, 45 Harvard Journal on Legislation 1, 2008, at 3.

<sup>31</sup> Financial Consumer Agency of Canada, *Understanding your Credit Report and Credit Score; Building a Credit History; How can a credit card help?* Online: Financial Consumer Agency of Canada <<http://www.fcac-acfc.gc.ca/eng/publications/CreditReportScore/PDF/CreditReportScore-eng.pdf>>.

“For those new to Canada, one of the easiest, most effective ways to start building a credit history is to get a Canadian credit card.”<sup>32</sup>

New Canadians who participated in the focus groups that are part of this study agree on the importance of credit cards. They understood that a lack of access to these products impeded the creation of their own credit reputation and facilitating their new financial lives.

### **‘Addicted to credit’ or ‘compelled to credit’? Consumers and credit reporting**

Maintaining a reputational database where data on a consumer’s credit transactions is reported, stored, and analyzed helps reduce the cost of lending for creditors. It also facilitates a clearer picture of a consumer’s creditworthiness. Standardised credit scoring systems for assessing creditworthiness have been developed by many major creditors internally, such as banks and finance companies. However, credit reporting agencies are the predominant players in this system, specializing in the collection and dissemination of credit information.

In the retail lending market, credit scoring facilitates ‘risk based pricing’, so that lenders are able to sort through customers in relation to the perceived risk levels and assign an interest rate payable on their balances.<sup>33</sup> The use of credit scoring by credit card issuers requires consumers to borrow first in order to have access to most kinds of credit cards.. Credit cards are the most effective creditworthiness-building tool for consumers. Unfortunately, the way in which both the credit scoring system and credit cards operate can be compared to tied selling. Tied selling is present where a supplier, as condition of supplying a product (the ‘tying’ product), requires or induces a customer to purchase another product (the ‘tied product’).<sup>34</sup>

The difficulty in applying tied selling to credit cards is the fact that they do not represent two separate products: a payment method and a source of credit. Credit cards combine two different features that are contained in one single product. There are implications to having these two features that are essential to a modern, digitized economy. The payments industry and lawmakers should work together to devise consumer payment solutions that would increase consumer access to the electronic economy without requiring unnecessary

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<sup>32</sup> CanadianImmigrant.ca, *Build a Credit History, Establish your Financial Future*, online: CanadianImmigrant.ca <<http://www.canadianimmigrant.ca/microsites/article/933>>.

<sup>33</sup> Iain Ramsay, *Consumer Law and Policy, Text and Materials on Regulating Consumer Markets*, 2<sup>nd</sup> Ed. Hart Publishing, Oxford and Portland, 2007 at 546.

<sup>34</sup> Michael Trebilcock, *The Law and Economics of Canadian Competition Law* (2002), University of Toronto Press at 450.

credit. Pre-paid and secured cards offer a partial solution to this problem but present too many drawbacks and fees to make them effective for consumers.

For legislators, the public policy questions raised by the consumer credit rating system are a challenging issue. Questions such as electronic payments substitute physical currency and the tracking and storage of consumers' transactions can create difficulties:

“Credit reference agencies are therefore important institutions of regulation and governance, admitting some and excluding others. Given the importance of these ‘private’ systems in sorting consumers into increasingly segmented markets, it is essential that such systems be democratically accountable.”<sup>35</sup>

The sharing of private personal financial information raises concerns about invasions of privacy. Consumption patterns, geographical information and even behavioural profiles can be easily extracted from the data captured. Although consent is often viewed as a way to ensure that consumers know the uses given to their data there are few viable alternatives for the consumer who refuses consent. This is a concern that policymakers around the world agree should not be taken lightly. The right to privacy is a fundamental human right that goes to the heart of the protection of liberty,<sup>36</sup> intimacy, and dignity, fundamental values of a modern democratic order.<sup>37</sup>

### **The credit card and the electronic payments market in Canada**

Most of the adult population in Canada and the United States would have trouble imagining their daily life without using credit cards. Beyond the individual sphere of use, credit card transactions make up the largest share of payments made for products and services in many areas of the economy. With one of the highest number per capita of credit and debit card transactions in the world, Canada is at the global forefront in usage of electronic payments.

In Canada's retail economy, the great majority of consumer payment transactions are cashless. The vast majority of the \$425 billion worth of goods and services sold by merchants in 2006, were paid for by consumers with credit cards, debit

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<sup>35</sup> *Supra* note 32 at 550.

<sup>36</sup> Electronic Privacy Information Center, Privacy & Human Rights and Privacy International, *An International Survey of Privacy Laws and Developments*, Washington D.C. 2007, 1 to 22.

<sup>37</sup> Federico Ferretti, *The ‘Credit Scoring’ Pandemic and the European Vaccine: Making Sense of EU Data Protection Legislation*, *Journal of Information, Law and Technology (JILT)*, 28 May 2009, online: University of Warwick <[http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2009\\_1/ferretti/ferretti.pdf](http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2009_1/ferretti/ferretti.pdf)>.

cards, cash and to a much lesser extent, cheques.<sup>38</sup> Canadians are also among the greatest users of credit cards in the world. While on average each Canadian holds only one debit card, each Canadian holds an average of two credit cards.<sup>39</sup> From 2001 to 2008 the total number of cards circulating grew by 50% but the gross credit card sales slips processed (or number of transactions) doubled from \$1,22 billion to \$2,43 billion. Similarly, the net credit card payments went from \$121 billion to \$266 billion (a 120% increase) while the average credit card transaction increased from \$99 to \$112 in the same time period.<sup>40</sup> Some answers provided by focus groups participants provided clear ideas on the popularity of the credit card as payment instrument and referred to it as part of a

*“It’s a standard way of living here in Canada.”*

*“I think they’re commonplace now, by far. I know some people who never use cash, just credit, credit cards – a lot of people.”*

*“It’s the norm. It’s the in thing. You don’t got it, you don’t fit in.”<sup>41</sup>*

This belies an important fact about the nature of credit cards: they are the leading method used as part of the electronic payment system to date.<sup>42</sup> Aside from allowing access to credit, the credit card payment method is a driving force behind the growth of the online economy. Credit cards are widely accepted as a payment method on the internet.. This is reflected in the Canadian electronic payments marketplace both online and for physical payments, where credit cards have been the preferred method of payment. This trend has occurred despite the consistent growth in debit card use as well as the impact of the 2008-2009 economic recession on consumer borrowing.

An important fact of Canadian credit card use is the fact that approximately 70% of Canadians card holders pay their credit card bills in full every month, according to the Canadian Bankers Association (CBA).<sup>43</sup> This data seems to

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<sup>38</sup> *Supra* note 16. [Arango and Taylor]

<sup>39</sup> Canadian Bankers Association, *Credit Card Statistics - Visa and Master Card*, online: Canadian Bankers Association <[http://www.cba.ca/contents/files/statistics/stat\\_20081031\\_cc\\_db038\\_en.pdf](http://www.cba.ca/contents/files/statistics/stat_20081031_cc_db038_en.pdf)>.

<sup>40</sup> *Ibid.*

<sup>41</sup> Annex A at 14.

<sup>42</sup> United States Government Accountability Office (GAO), *Credit Cards , Increased Complexity in Rates and Fees Heightens Need For More Effective Disclosures to Consumers*, Report to the Ranking Minority Member, Permanent Subcommittee on Investigations, Committee on Homeland Security and Government Affairs, U.S. Senate, September 2006, online: United States Government Accountability Office <<http://www.gao.gov/new.items/d06929.pdf>>.

<sup>43</sup> Canadian Bankers Association, *Payment Cards in Canada: Choice and Competition for Consumers and Businesses*, Remarks by Nancy Hughes Anthony, President and CEO of the Canadian Bankers Association to the Senate Committee on Banking, Trade and Commerce, 1 April, 2009, online: Canadian Bankers Association <[http://www.cba.ca/contents/files/presentations/pre\\_20090401\\_nha\\_01\\_en.pdf](http://www.cba.ca/contents/files/presentations/pre_20090401_nha_01_en.pdf)>.

correspond to the previous data released by Statistics Canada placing this number at 73% in 2005.<sup>44</sup> These figures seem to suggest that the average credit card user in Canada does not use the card as a source of credit, but instead as plastic currency, either for point of sale (POS) payment method or online payment transactions.

The answers given by the participants in the focus groups raised important issues that these consumers face in their financial lives. One of them is the centrality of the new economy based on networks and consumer access to those networks. With the advent of plastic money, the banking business has transitioned from a model of safety to an information exchange model. This transition was accelerated by the adoption of networks and electronic banking. In today's information economy, the idea of banking is difficult to understand without the existence of electronic networks. These networks provide access for users to banks, for banks to users, and connect branches and exchange information between financial institutions. It leads one to consider whether or not banking has become so intrinsically linked and dependent on networks that banking today is simply an added service to be rendered through an information services network.

In the realm of credit cards, Canada is best situated at the global level to craft the solutions that will enhance the growth potential of the Canadian economy. Integrating the largest number of Canadians possible to the electronic payments realm is imperative to the new networked economy and electronic commerce. Such market can offer limitless opportunities to enterprises and electronic payments issuers, included credit cards. However, enabling required access to the payment networks must come with increased regulatory oversight and consumer protection mechanisms. These measures must ban contractual abuses in the terms consumers to which consumer must consent in order to use the payment networks. The financial industry's abuses have helped create the latest economic recession. Greater control by payments companies of the monetary system will also mean new, greater and unpredictable risks for the stability of the economy.

Credit cards provide relatively secure transactions for non-face-to-face transactions as shown by the overwhelming use of credit cards for online

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<sup>44</sup> Almost 11 million Canadian families reported owning a credit card in 2005. Of the over two million family units that reported not owning one, nearly 19% of these families were refused this type of credit. Nearly 73% of families who had credit cards reported they pay off their balances each month. The median credit limit on all credit cards owned was \$10,000. See: Statistics Canada, *Survey of Financial Security: Public Use Microdata User Guide*, Pension and Wealth Research Paper Series, 2005, online: Statistics Canada <<http://www.statcan.gc.ca/dli-ild/meta/sfs-esf/2005/sfs-esf2005guide-eng.pdf>>.

transactions.<sup>45</sup> While merchants may lose business by not accepting credit cards, it seems that for this group credit cards are the most expensive payment instrument to accept given the fees extracted by merchant banking service providers. There is evidence that, generally speaking, the cost of using cash increases with the transaction value. However, this cost only rises as compared with the cost of accepting debit cards, which have fixed costs per transaction. The reason that credit cards entail the highest cost per transaction for merchants is that their fees are based on a percentage of the value of the transaction.<sup>46</sup>

### **Chip-embedded credit cards**

Currently, the debit and credit cards payment systems in Canada are in the process of a system-wide technological overhaul. This change will bring about a chip embedded in every credit and debit card, making integrated circuit (IC) cards the standard method of payment in the country.<sup>47</sup> According to ACT Canada, the payments' industry association promoting the implementation of the EMV chip technology in Canada,<sup>48</sup> the benefits of the chip technology are mostly for merchants and issuers. The chip cards allow for greater security during transactions and a consistent payment experience for debit and credit transactions.

There are advantages of the use of chip-embedded cards for consumers in terms of convenience and security. However, as cash payments are substituted by credit and debit chip-based payments, some potential disadvantages may arise. These disadvantages will affect lower income consumers and small scale merchants who rely upon cash only. The cost of the use of cashless payments in terms of access fees for consumers could potentially exceed the actual benefits of its use. Conversely, network proprietors could proceed to raise access fees to merchants to increase profitability. All these potential costs will probably end up being assumed by consumers. Additionally, privacy will continue to be an

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<sup>45</sup> Sujit Chakravorty and Ted To, *A Theory of Credit Cards*, Federal Reserve Bank of Chicago, July 2001, online: Federal Reserve Bank of Chicago <<http://www.philadelphiafed.org/research-and-data/events/2002/financial-services-and-payments/papers/Chakrovorti%20To.pdf>>.

<sup>46</sup> *Supra* note 16. [Arango and Taylor]

<sup>47</sup> According to ACT Canada, the payments industry stakeholders' association behind the implementation of the EMV chip-based technology for retail payments in Canada, the main driver behind chip-embedded cards in Canada is the prevention of payment fraud. Among the principal members of ACT are Canada's large financial and electronic payments institutions: Visa Canada, TD Merchant Services, Credit Union Central of Canada, HSBC Credit Card Services, Scotiabank, Home Trust Company, Citi Cards Canada, Chase Card Services, Vancity Savings Credit Union and ATB Financial. See: ACT Canada, *Membership*, online: ACT Canada <<http://www.actcda.com/actmembers.html>>.

<sup>48</sup> EMV technology, originally named after the association of EuroPay MasterCard and Visa in Europe to adopt integrated circuit cards (known also as "IC" or "ICC"), is becoming the global standard for payment card technology and is being phased in around the world.

important concern since payment networks produce data that is inherently personal and therefore protected by privacy laws. These are very serious consumer issues that deserve further exploration and research.

There has been some acknowledgement that technology and electronic payments have lowered the cost of producing a payment alternative to notes printed by a central bank.<sup>49</sup> Moreover, electronic payment technologies do exert competitive pressure on central banks, at least for advanced economies. These provide a strong incentive for monetary policy discipline that has contributed to keep a check on inflation over nearly two decades.<sup>50</sup> On the other hand, this competition is expected to become an increasing challenge to both consumers and central banking. A challenge that is of particular concern to Canada, is the technological consolidation of credit and debit electronic payments. By the end of 2012, all credit and debit cards in Canada as well as all automatic banking machines (ABMs) will migrate to chip-based technology. By 2015 all points of sale (POS) in the country will read chip cards. The EMV chip technology is a proprietary technology currently being deployed by ACT Canada members. Payment systems are currency substitutes and can directly have an impact monetary policy. Concerns about shifting from a public monopoly of the payment system to a single private, proprietary electronic payment method has been expressed by the Federal Reserve authorities:

“When the technology in an industry appears to be enduringly inconsistent with good public policy outcomes under unfettered competition, ongoing intervention by government or government-sponsored regulators may be an effective alternative. In the context of the payments system, specifically, the Federal Reserve System currently acts as a consumer-protection regulator in consumer payment and credit markets, under legislative authority”.<sup>51</sup>

A closer scrutiny not only by financial authorities but also by monetary authorities seems to be necessary. The European Central Bank has also explored the possible risks of potential monopolistic behaviour by payments systems. These could create barriers to interconnection and access to payments. This behaviour parallels that of telecommunications operators and how they have historically been reluctant to allow interconnection and access by different networks:

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<sup>49</sup> Randall S. Kroszner, *Currency Competition in the Digital Age*, Prepared for the Federal Reserve Bank of Cleveland, May 2001, online:

<<http://www.clevelandfed.org/research/conferences/2001/May/kroszner.pdf>> .

<sup>50</sup> *Ibid.*

<sup>51</sup> Edward J. Green and Richard M. Todd, *Thoughts on the Fed's Role in the Payments System*, Federal Reserve Bank of Minneapolis Quarterly Review, Winter 2001, online: Federal Reserve Bank of Minneapolis <<http://www.minneapolisfed.org/research/QR/QR2512.pdf>>.

“...if the cost of entry - for instance due to necessary investments in research and development - is high enough to deter any new entrants, monopoly behavior will prevail. As highlighted in our short overview of the literature on natural monopoly, a market that has a single producer can still be contestable if the cost of entry is low enough or if a firm is ready to enter and propose a service at a competitive price, thus forcing the present producer to maintain prices at marginal cost. Hence, it is important that the central banks support measures that will render markets contestable.”<sup>52</sup>

A further issue worth examining is the relationship between merchants, issuers and consumers. Consumers constitute the single most important constituent of the market and largest number of stakeholders. It may be assumed that consumers' interests are advanced by legislators and regulators, however, this has not always been the case. Consumers and consumer organizations rarely find their positions implemented during the formulation of legislative and regulatory reform of consumer credit. For merchants, particularly small and independent retailers, the concern is not only major credit card companies and their ability to extract fees from every sale in a monopolistic fashion. There are fears of financial exclusion as well:

“...in accepting a credit card, will make extra sales, and these sales will cover the extra cost involved. This argument has merit when few of a merchant's competitors are also members of a credit network. Today, when almost all merchants accept credit cards, extra sales are unlikely to occur. What was once a way for merchants to offer customers something they could not easily obtain elsewhere now has become an expected service that no longer distinguishes one merchant from another. The expanded sale argument for merchants to accept credit cards is now essentially an argument for merchants to accept credit cards not to lose sales.”<sup>53</sup>

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<sup>52</sup> Cornelia Holthausen and Cyril Monnet, *Money and Payments: A Modern Perspective*, European Central Bank, Working Paper Series, Working Paper No. 245, July 2003, online: European Central Bank <<http://www.ecb.int/pub/pdf/scpwps/ecbwp245.pdf>>.

<sup>53</sup> Stan Sienkiewicz, *Credit Cards and Payment Efficiency*, Federal Reserve Bank of Philadelphia, Discussion Paper, Payment Cards Center, August 2001, online: <[http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2001/PaymentEfficiency\\_092001.pdf](http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2001/PaymentEfficiency_092001.pdf)>.

Legislators can enact payments legislation prioritizing the interest of the public and enhancing economic welfare. Creditors and payment network operators have a corporate mandate to act in the best interest of the enterprise. They naturally attempt to persuade legislators and elected officials to frame laws in a flexible manner to allow for financial innovation according to their companies' interests. The challenge for legislators is to frame laws that protect the consumer while enhancing opportunities for industry to offer innovative financial and payment services.

### **Regulatory changes to credit card fees**

The credit card as payment method, as it has been pointed out above, allows a number of advantages to consumers. It has become the payment method of convenience for consumers. However, it is the credit feature of the cards that has and continues to attract criticism. The bulk of such criticism is targets the way in which lenders' practices have overburdened many cardholders. With greater debt liabilities and extra charges, financial obligations have contributed to undermine the financial stability of many consumers. Some of the responses in the focus groups indicated how card holders were encouraged to incur debt. They also demonstrated that credit cards lower awareness of money being spent or borrowed when all is to be done when paying is to swipe the card.<sup>54</sup>

*"With a card, it encourages to spend because it's not the same if you have the money here. You think more because you have the cash."*

*"It encourages compulsive spending if you don't need your cash on hand."<sup>55</sup>*

As mentioned above, due to the current historic high levels of consumer debt, the common assumption is that our society is addicted to credit. There is no doubt about the central role of credit and available finance in a modern economy. However the recent spike in the use of debit show that,<sup>56</sup> rather than an addiction, a combination of factors have played a role in the current levels of over-indebtedness. There is abundant evidence showing increasingly aggressive credit solicitation practices by creditors in recent years may have standardized such unwise use. In the case of credit cards, hidden charges, low introductory

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<sup>54</sup> *Supra* note 9 at 431. [Pottow].

<sup>55</sup> Annex at 12.

<sup>56</sup> Marianne Crowe, Vice President, Emerging Payments Research Group/Business Development, Federal Reserve Bank of Boston, presentation *Emerging Payments, Changing Landscape*, to the Maine Association of Community Banks on April 15, 2008 and to the New Hampshire Community Bankers Association on April 17, 2008, online: Federal Reserve Bank of Boston <<http://www.bos.frb.org/economic/eprg/presentations/2008/crowe04151708.pdf>>.

interest rates that increase by as much as 10 times after the introductory period and inadequate disclosures have all contributed to increase debt levels.

According to statistics released by the Office of the Superintendent of Bankruptcy of Canada in 2007, the most frequent declared debt burden in consumer proposals and consumer bankruptcies is credit card debt. A total of 88.3 per cent of consumers filing for bankruptcy had credit card debt outstanding, followed by finance loans, reported in 77.9 per cent of the filings.<sup>57</sup>

In May 2009, in response to public criticism of credit card industry practices federal minister of Finance, Jim Flaherty announced two sets of measures designed to protect credit card users in Canada. The first set of measures, under the name of “*Credit Business Practices Regulations*” introduced the following changes into the market, mandating:

- a) a 21 days interest-free period since the date of purchase for consumers who pay their balances in full each month;
- b) requires credit card issuers to allocate payments to high-interest items first, or proportionally, to the benefit of the consumer;
- c) places a requirement of consent to raise consumer’s credit limits;
- d) restricts prescribed credit collection practices deemed unfair and
- e) eliminates fees for reaching credit limit based solely on merchant holds.<sup>58</sup>

A second set of measures, the *Regulations Amending the Cost of Borrowing Regulations*, directs issuers to make additional disclosures to users. One important measure is the requirement of notice for increasing interest rates upon exhaustion of time term for promotional introductory rates. Another measure is the requirement to disclose to consumers the calculation of the amount of time necessary to pay down the debt based on the minimum payment only.<sup>59</sup>

Charges for late payments and sharp interest rate increases, a widespread practice among credit card issuers can be a cause for deep concern in the current context of economic downturn. According to Equifax, a consumer credit reporting agency, the number of consumer credit payments overdue or consumer credit delinquency, increased by 24% from 1.19 per cent in June 2008 to 1.56

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<sup>57</sup> Industry Canada, Office of the Superintendent of Bankruptcy, *An Overview of Canadian Insolvency Statistics up to 2006, June 2007*, online: <[http://www.ic.gc.ca/eic/site/bsf-osb.nsf/vwapj/Statsbooklet2007-EN.pdf/\\$FILE/Statsbooklet2007-EN.pdf](http://www.ic.gc.ca/eic/site/bsf-osb.nsf/vwapj/Statsbooklet2007-EN.pdf/$FILE/Statsbooklet2007-EN.pdf)>.

<sup>58</sup> Government of Canada, *Credit Business Practices (Banks, Authorized Foreign Banks, Trust and Loan Companies, Retail Associations, Canadian Insurance Companies and Foreign Insurance Companies) Regulations*, 21 May 2009, online: Department of Finance Canada <[http://www.fin.gc.ca/n08/data/09-048\\_1.pdf](http://www.fin.gc.ca/n08/data/09-048_1.pdf)>.

<sup>59</sup> Government of Canada, *Regulations Amending the Cost of Borrowing Regulations*, 21 May 2009, online: Department of Finance Canada <[http://www.fin.gc.ca/n08/data/09-048\\_2.pdf](http://www.fin.gc.ca/n08/data/09-048_2.pdf)>.

per cent in June 2009.<sup>60</sup> Delinquency is defined by the agency as credit facilities that are 90 days or more past due. The average delinquency rate is calculated by comparing the number of delinquent credit facilities to the total number of credit facilities.

The race to augment revenues by credit issuers, propped up by contractual clauses that may present dangerous financial pitfalls for cardholders has gone largely unchecked. This is coupled with the massive employment losses of the current economic recession. The by-product of such precedent may well have a direct impact on individuals and households in terms of financial stress and over-indebtedness. Recent insolvency numbers released by the Office of the Superintendent of Bankruptcy of Canada illustrate this problem. In June 2009 a total of 14,418 Canadians filed for bankruptcy, compared to 9,538 filings in June 2008, representing a 52% jump.<sup>61</sup> Similarly, on a per quarter annualized basis, the 40,249 consumer bankruptcies registered in the second quarter of 2009 were a 40.3 per cent higher than the 28,686 registered in the second quarter of 2008.<sup>62</sup>

Commentators have pointed at the fact that part of the reason for the increase in delinquencies and default may be beyond consumers' control. Factors such as the current financial downturn, have resulted in high unemployment and income disruption.<sup>63</sup> The role of interest rates considerably higher than the prime lending rate and credit card service fees in gobbling up disposable income may be understated in estimates. PIAC has documented current consumer travails and how issues such as emergencies, family problems and health issues are also often linked to financial distress and are sometimes the root cause of it.<sup>64</sup> A further issue that perhaps deserves exploration is the reverse: the extent to which financial distress may have a role in the deterioration of health conditions among the public.<sup>65</sup>

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<sup>60</sup> CNW Group, *Equifax Canada data Reveals 24% jump in Annualized Delinquency Rate*, 6 August 2009, online: CNW Group

<<http://www.newswire.ca/en/releases/archive/August2009/06/c3151.html>>.

<sup>61</sup> Office of the Superintendent of Bankruptcy of Canada, *Insolvency Statistics in Canada, June 2009*, online: Office of the Superintendent of Bankruptcy of Canada

<[http://www.ic.gc.ca/eic/site/bsf-osb.nsf/vwapj/june09\\_eng.pdf/\\$FILE/june09\\_eng.pdf](http://www.ic.gc.ca/eic/site/bsf-osb.nsf/vwapj/june09_eng.pdf/$FILE/june09_eng.pdf)>

<sup>62</sup> Office of the Superintendent of Bankruptcy of Canada, *Insolvency Statistics in Canada, Second Quarter 2009*, online: Office of the Superintendent of Bankruptcy of Canada

<[http://www.ic.gc.ca/eic/site/bsf-osb.nsf/vwapj/Q2\\_2009\\_eng.pdf/\\$FILE/Q2\\_2009\\_eng.pdf](http://www.ic.gc.ca/eic/site/bsf-osb.nsf/vwapj/Q2_2009_eng.pdf/$FILE/Q2_2009_eng.pdf)>.

<sup>63</sup> Craig Alexander (Vice President and Deputy Chief Economist), *Recession Drives Sharp Increase in Personal Insolvency*, TD Economics Observation, 11 August 2009, online:

<[http://www.td.com/economics/special/ca0809\\_insolvency.pdf](http://www.td.com/economics/special/ca0809_insolvency.pdf)>.

<sup>64</sup> Esteban Uribe, *Not Ready for Prime Time: Canadians In the Sub-Prime, High-interest Lending*, Public Interest Advocacy Centre PIAC, Ottawa, October 2008, online:

<[http://www.piac.ca/financial/consumer\\_group\\_report\\_reveals\\_high\\_interest\\_borrowing\\_pitfalls](http://www.piac.ca/financial/consumer_group_report_reveals_high_interest_borrowing_pitfalls)>.

<sup>65</sup> While some studies have been conducted on the health effects associated with financial distress, it can be expected that the current recession will spark research activity in this area. A

Despite the fact that both debt distress among consumers and credit card industry abuses have been widely documented, it is not reasonable to suggest that credit cards should be restricted or consumers should be prevented from using them. Important issues such as secure access to the payment system networks and credit history creation should not be overlooked because of fear of promoting consumer indebtedness. The difficulties consumers face with building their credit rating bring with them with increased transaction costs. In addition, the national economy loses the increased growth provided by the excluded consumers who do not participate

While credit cards have become a mainstream payment method, there's some indication that consumers may be learning to be wary of contractual pitfalls and to be more careful when it comes to using them.<sup>66</sup> Fees and penalties imposed by credit card issuers have an enforcement component that is turned into knowledge by the 'revolver' user. Late payments have the short term effect of raising consumers' alertness and aversion to making late payments. However, this effect fades over time and the further a late payment recedes in the past, the greater the likelihood of another penalty, for some reason, arises in the future. What seems clear is that learning generates a substantial net reduction in fee payments.<sup>67</sup> These findings lend credence to the policy effort at the Financial Consumer Agency of Canada to raise financial literacy levels at all age levels among Canadians, with a special focus on young Canadians attending school.

### **The role of credit cards on E-Commerce**

In the online payments environment, credit cards are the most widely available payment system. There is little doubt that the development and growth of E-commerce has relied upon credit card use as payment method.<sup>68</sup> According to a recent global survey, by 2008 more than 85% percent of the world's online

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survey from 2005, a year considered as one of economic growth, two to three years before the recession, reported that 4 out of 10 respondents indicated that their health was affected by their financial distress. See: Barbara O'Neill, Benoit Sorhaindo, Jing Jian Xiao and E. Thomas Garman, *Negative Health Effects of Financial Stress*, Consumers Interests Annual, Volume 51, 2005, online: PersonalFinanceFoundation.org <<http://www.personalfinancefoundation.org/research/efd/Negative-Health-Effects-of-Financial-Stress.pdf>>.

<sup>66</sup> Sumit Agarwal, John C. Driscoll, Xavier Gabaix, and David Laibson, *Learning in the Credit Card market*, Federal Reserve Bank of Chicago, online: Harvard University Department of Economics <<http://www.economics.harvard.edu/faculty/laibson/files/Learning%2Bin%2Bthe%2Bcredit%2Bcard%2Bmarket.pdf>>. This article contains the results of a study that suggests the importance of "learning by doing" in the realm of credit usage and particularly in the area of credit card use.

<sup>67</sup> *Ibid.*

<sup>68</sup> Elliot Maxwell, Shukri Wakid and Judi Moline, *A Policy Perspective on Electronic Commerce*, IEEE Communications Magazine, September 1999 at 88.

population had made a purchase online. Out of all those global online consumers, 60% used a credit card for a recent online purchase, while 25% of online consumers chose alternative means to pay online, such as PayPal. However, other estimates place the percentage of online consumers having used credit cards to pay online at 83.6%, tracked by PayPal, at 55%.<sup>69</sup> Despite the importance of the online economy, a lack of access to credit cards seems represent a barrier for consumers to take advantage of the possibilities and efficiencies offered by that market:

*“I had to ask a friend to pay for those tickets.”*

*“I have a debit card that I can use a lot, but you can’t use everywhere. A credit card is more convenient.”*

*“If you’re going to get a plane ticket now, then you’ve got to go down there and you’re paying a higher price than you would if you paid in advance. So, in my books, it would be cheaper for me to travel if I did have a credit card.”<sup>70</sup>*

In the realm of online payments, credit cards also rank among the highest in the levels of satisfaction by users, with 48% of users reporting their experience as “excellent”; 42% describing it as “good” and 10% as “satisfactory”. Only 1% of users were of the opinion that the method needed to improve.<sup>71</sup> Canada, as a global high volume user of electronic payments and credit cards, occupies an important place in the global e-commerce context. In 2007, Canadians placed \$12,8 billion worth of orders, an increase of 61% from 2005 when online orders where worth \$7,9 billion.

It is important to note, however, that a large number of alternative methods of payment such as PayPal are normally linked to a client’s credit card. Most of them debit charges to a credit card, while some are debited to bank accounts. Since for many of those methods the underlying method of payment is a credit card, it can be expected that the percentage of credit card use for internet purchases is significantly higher than the numbers reported above. Visa is the most widely used credit card for internet purchases, followed by Master Card and American Express. Of all payments made online through credit cards, more than half used a Visa card, at 53 per cent.<sup>72</sup> According to the Nielsen Media

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<sup>69</sup> J.P. Morgan Global Equity Research, *Nothing but Net, 2009 Internet Investment Guide*, January, 2009.

<sup>70</sup> Annex at 23.

<sup>71</sup> *Supra* note 68 [JP Morgan].

<sup>72</sup> Nielsen Media Research, *Nielsen Global Online Research*, December 2007, online: PR Newswire <<http://www.prnewswire.co.uk/cgi/news/release?id=217674>>. The Nielsen Global Online Research was conducted from October to November 2007 and polled 26,312 Internet

Research, by 2006 over 627 million people had shopped online, the equivalent to over 10 percent of the world's population. By 2008, the number increased to 875 million people; a 40 per cent global increase in only two years.

## Plastic cards and E-banking

Branch closures seem to have played an important role in the process of increased adoption of plastic methods of payment. Due in part to changes in market structure and branch network reorganization, electronic banking has been intensively implemented by banks. Consequently, consumers have been encouraged to continue to do their personal banking by electronic means.<sup>73</sup> Since 1998, the average bank's branch network shrunk by 23 per cent and the total number of branches fell by 29 per cent despite a 37 per cent increase in deposits that year. In contrast, in the period between 1982 and 1997, the top six Canadian banks closed only 2.3 per cent of their branches. This suggests that the pre e-banking period was characterized by a relatively stable decline in the number of branches.<sup>74</sup>

Since the inception in 1997 of electronic banking in Canada, the number of transactions climbed to more than 300 million in 2006. Electronic banking is a term used in this report to refer to the provision of personal banking services over the internet. The share of consumers who did at least some online banking increased from 3 per cent in 1997 to 49 per cent in 2006. From 1998 to 2006 Canadians also quickly became some of the world's heaviest users of electronic payment systems. The fraction of Canadian households having adopted electronic banking has risen quite substantially, from 17.3 per cent in 1999 to nearly 60 per cent in 2006. There are currently 64.1 million Visa and MasterCard credit cards in circulation in Canada, with Visa holding about 72 per cent of market share.<sup>75</sup>

In the context of today's ubiquitous electronic means of payment, it may be that the use of cash may impose an inconvenience to the consumer in some, circumstances. It is clear that some cash transactions may entail less privacy risks for consumers than electronic payments since the risks of data mining by a network operator are eliminated. The answers that participants gave in the focus

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users in 48 markets from Europe, Asia Pacific, North America and the Middle East. The survey is representative of all Internet users aged 15+.

<sup>73</sup> Jason Allen, Robert Clark and Jean-François Houde, *Market Structure and the Diffusion of E-Commerce: Evidence from the Retail Banking Industry*, Bank of Canada Working Paper 2008-32, September 2008, online: Bank of Canada <<http://www.bankofcanada.ca/en/res/wp/2008/wp08-32.pdf>>.

<sup>74</sup> *Ibid.*

<sup>75</sup> Bank of Canada, *Bank of Canada Review, Winter 2008-2009*, online: Bank of Canada <[http://www.bankofcanada.ca/en/review/winter08-09/review\\_winter08-09.pdf](http://www.bankofcanada.ca/en/review/winter08-09/review_winter08-09.pdf)>.

groups included in this study discussed their lives without credit cards. They pointed out that being excluded from the payment advantages and credit reporting feature of credit card specifically obliged them to a greater reliance on cash payments. This reliance on cash did not mean lower costs for them. Instead, the opposite was true: using cash for their payments imposed extra costs for them which could easily escalate, both in terms of time spent, convenience and added monetary cost.

### **Credit card companies and consumer protection**

One aspect of the use of credit cards for consumers is their advantage over other methods of payment in the area of protection against fraud, merchant abuse and theft. In a typical credit card transaction, the funds do not normally settle between financial institutions and merchants until one or two days after the transaction takes place. When customers are not satisfied with the transaction, the credit card company normally has dispute resolution mechanisms in place that help both merchant and consumers to reconcile their differences. In some cases, the credit card company can be particularly helpful in protecting its customers against fraud. Merchant banking systems are also developed specifically to prevent unauthorized card use. Elaborate fraud prevention schemes track a card holder's typical spending pattern and automatically block transactions which stray from the profile and could be fraudulent.

Merchants and credit card issuers' ability to reverse charges and credit back consumers' cards can be seen as a benefit, if very small.<sup>76</sup> Debit payment does not feature this kind of protection since the money is immediately withdrawn from the consumer's bank account. Any dispute arising from a debit transaction is left to the consumer and the merchant, in the same way as a cash purchase.<sup>77</sup> Privacy rights advocates have even gone as far as to recommend to consumers the use of credit cards for their online transactions, with the caveat that they are used responsibly:

“The first credit card protection shields you against liability for unauthorized use of your credit card, that is, when someone steals or otherwise uses your card or card number without permission.

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<sup>76</sup> Daniel D. Garcia-Swartz, Robert W. Hahn and Anne Layne-Farrar, *The Move Toward a Cashless Society: A Closer Look at Payment Instrument Economics*, Review of Network Economics, Vol. 5 Issue 2, June 2006, online: Review of Networks Economics  
<[http://www.rnejournal.com/artman2/uploads/1/garcia\\_swartz\\_1\\_RNE\\_june\\_2006.pdf](http://www.rnejournal.com/artman2/uploads/1/garcia_swartz_1_RNE_june_2006.pdf)>.

<sup>77</sup> *Ibid.*

The second protection involves disputes about your bill (billing errors). These disputes may include a merchant overcharging you or charging you for products you never received.

The third protection is the right to stop payment. Stopping payment is a powerful tool that you can use when you are dissatisfied with the quality of goods or services that you paid for with a credit card.”<sup>78</sup>

Some authors have argued that as millions of users become connected to the electronic networks of credit card companies chargeback systems can be a tool to protect consumers against rogue merchants. Furthermore, greater degrees of disclosure about the reputation of certain merchants can be made to consumers, depending on the outcomes of prior credit card transactions. Such a system could resemble the system of buyers and sellers’ reputational reviews posted by Ebay users.<sup>79</sup>

Debit card users in Canada enjoy some level of protection with regards to errors in billing, misrepresentations, fraud and warranties.<sup>80</sup> Debit card users are also covered by consumer protection legislation which has been enacted in every province. The *Canadian Code of Practice for Consumer Debit Card Services* establishes a procedure to follow by the financial institution or “PIN issuer”.<sup>81</sup> The process starts with an investigation when unauthorized use of the card is reported. The investigation may result in the card being blocked to prevent further misuse or the reimbursement of fraudulently withdrawn funds, if in the balance of probabilities the loss occurred due to no fault of the user.<sup>82</sup> The *Code* is endorsed by the Canadian Bankers Association, the Canadian Federation of Independent Business, The Credit Union Central of Canada, the Consumers’ Association of Canada, La Fédération des caisses Desjardins du Québec and the Retail Council of Canada. According to Interac’s website, a total of \$106 million was reimbursed to consumers whose were victims of fraud in 2007.<sup>83</sup>

Credit card companies have announced their intention to enter the debit market in Canada. With the new combined debit and credit cards, the expectation of

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<sup>78</sup> Privacy Rights Clearinghouse, *Paper or Plastic, What Have you Got to Lose?* Fact Sheet 32, online: <<http://www.privacyrights.org/fs/fs32-paperplastic.htm>>.

<sup>79</sup> Arnold S. Rosenberg, *Better than Cash? Global Proliferation of Payment Cards and Consumer Protection Policy*, Columbia Journal of Transnational Law, Vol. 44, 2006, online: University of Columbia: <[http://www.columbia.edu/cu/jtl/vol\\_44\\_2\\_files/rosenberg.pdf](http://www.columbia.edu/cu/jtl/vol_44_2_files/rosenberg.pdf)> at 524.

<sup>80</sup> Consumer protection legislation in every Canadian Province contemplates basic rights consumers are afforded across Canada and generally sets out rules as to warranties, cooling off periods, remedies, written requirements, disclosures, and misrepresentations.

<sup>81</sup> *Canadian Code of Practice for Consumer Debit Card Services*

<sup>82</sup> *Canadian Code of Practice for Consumer Debit Card Services*, s.6.6.

<sup>83</sup> Interac, *What we’re Doing about Fraud*, online: Interac <[http://www.interac.ca/consumers/security\\_fraud.php](http://www.interac.ca/consumers/security_fraud.php)>.

consumers will be that both electronic payment methods guarantee consumers the highest level of protection, especially for online use. It is anticipated that with the introduction of chip-embedded cards across the debit and credit payment system in Canada, an additional layer of consumer protection and safety will benefit consumers. This protection will be gained in spite of fears of market consolidation which will result from the use of the same card for both payment technologies.

## WHERE DO CONSUMERS GO WHEN THEY ARE REFUSED A CREDIT CARD?

The credit function of the credit card is vital to the issue of access to credit. The relationship between lack of access to a credit card as a borrowing instrument and resort to high-interest loans and other forms of predatory lending has been argued and contested by academics.<sup>84</sup> But it seems clear that the vast majority of borrowers who use high-interest, payday loans and other forms of predatory lending are located in mid-to-lower income neighbourhoods across Canada.<sup>85</sup> According to Statistics Canada, households without a credit card available are more likely to use a payday outlet than those who hold credit cards. Those households who had been declined for a credit card were over three times as likely to use a payday outlet.<sup>86</sup>

However, this study does not focus specifically on the subject of access to credit in general, and instead is concerned with barriers created by a lack of access to the features of credit cards. In particular the study has a special focus on consumers whose lack of access to a credit card is not based on misuse of credit. Consumers who participated in the focus groups that provided information for this study were fully employed, with access to the internet and not declared bankrupt but had been declined when applying for a credit card. Many of them were young, aboriginal Canadians and New Canadians. Their experiences relating to their credit alternatives reflect some of the findings reported by Statistics Canada in that they consider using payday loans. They also reported to heavily rely on family members and friends, not only for online purchases but also for borrowing:

*“Money Mart. You have to have actually a pay stub.”*

*“Borrow from your friends. If your friend is willing to give it to you, that’s the thing.”*

*“Yeah, I just ask my dad to forward the money into my account and I give it back later on. I wouldn’t risk Payday loans or anything like that.”<sup>87</sup>*

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<sup>84</sup> Angela K. Littwin, *Beyond Usury, A Study of Credit Card Use and Preference Among Low Income Consumers*, Harvard Law School Faculty Scholarship Series, 2007, online: Nellco Legal Scholarship Repository <[http://lsr.nellco.org/harvard\\_faculty/8/](http://lsr.nellco.org/harvard_faculty/8/)>.

<sup>85</sup> United Way, *Losing Ground: The Persistent Growth of Family Poverty in Canada’s Largest City*, online: United Way <<http://www.unitedwaytoronto.com/downloads/whatWeDo/reports/LosingGround-fullReport.pdf>> at 45.

<sup>86</sup> Statistics Canada, *Perspectives on Labour and Income, Payday Loans*, April 2007, online: Statistics Canada <<http://www.statcan.gc.ca/pub/75-001-x/75-001-x2007104-eng.pdf>>.

<sup>87</sup> Annex at 33.

Since all of the participants did have some form of internet access and were internet users, it is not surprising that they resorted to electronic alternatives for online payment with credit cards. There were some who used electronic payment tools such as Interac email transfers, and payment by online debit:

*“I think now, especially too with this new email money transfer, that’s what I see here, because a lot of things now you can just transfer the money. Where before you would use a credit card, now you can do email money transfer.”*

*“I do grocery and things with the email money transfer. When I found out it was like, woo-hoo!”*

*“There’s another way you can buy stuff online too. You have to give them your cheque number, your account number and something like that, and the cheque number, and they will send the thing to you and they’re going into your account.”<sup>88</sup>*

It is clear that the consumers interviewed were making use of innovative payment methods online. However, many of these online payment methods such as money transfers by email and checking account debiting are accepted to a very limited degree in the online payments universe. Even services such as PayPal, which can be linked to a checking account, are not accepted as widely as credit cards. Email money transfers are only valid between some major banks who participate in the program.<sup>89</sup> Generally speaking, all these payments do not contribute to establishing a consumer credit history with credit reporting agencies.

### **Costs associated with alternatives**

Studies conducted by merchant associations suggest that debit is the least costly electronic payment method for merchants in relative terms, given the fixed fee per transaction. Credit cards are the most expensive option, given that the fee per transaction is based on a percentage and therefore it increases in direct proportion to the transaction amount.<sup>90</sup> The least expensive method for most

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<sup>88</sup> Annex at 31.

<sup>89</sup> Interac email transfer participating financial institutions: BMO Bank of Montreal, CIBC, Community Savings Credit Union, Island Savings Credit Union, Mennonite Savings and Credit Union, Prospera Credit Union, RBC Royal Bank of Canada, Scotiabank, TD Canada Trust, Teachers Credit Union, United Communities Credit Union, Westminster Savings Credit Union.

<sup>90</sup> *Supra* note 16 [Arango and Taylor]. Arango and Taylor’s paper discusses the results of a survey conducted among merchants. The study did not include merchants who do not or cannot

consumer transactions from the merchant point of view is, cash. However, it is not entirely clear if cash is the less costly payment method for consumers. The use of cash imposes other costs and risks from the standpoint of safety and convenience compared to widespread electronic methods of payment. A consumer faced with a lack of payment alternatives to cash is faced with costs in terms of time, inconvenience, decreased access to important goods and services and opportunity cost.

The situation for Canadian consumers during the recent recession has been difficult. There has been a sharp increase in the number of consumer insolvencies and many households are limiting their expenses as much as possible. Many services important to Canadian households are delivered online. Therefore, a payment method that can accommodate such distressed households in their transition to a more stable financial state may go a long way in helping them to get back on their feet. Records of bankruptcies and proposals are kept on consumers' financial credit records for 6 and 3 years respectively. An indication of a bankruptcy or bankruptcy proposal on a consumer's credit report effectively precludes them from unsecured credit until that indication disappears. Not having access to the payment features of a conventional credit card increases for these consumers the cost of their financial transactions. In particular, the costs of their access to and cost of online transactions are augmented. For consumers who contemplate undertaking entrepreneurial activity as employment option, the availability of a credit history can be critical to the viability of their business plans.

While it may be argued that a modern consumer could engage only in cash transactions, it is reasonable to expect that such consumer would face certain barriers and disadvantages by limiting herself to use of cash alone. One disadvantage is the fact that cash may increase certain costs in terms of time and convenience. Another significant cost is the higher interest rate that a cash-only consumer is bound to pay absent a credit record. There may be other costs, such as the time and expense associated with items such as travel tickets and other online purchases that need to be arranged through a friend or relative; or the travel expense to acquire the item in person. Other costs that can be difficult to measure but can be considered real are opportunity costs for the consumer; search costs, ATM fees, and time expenditures. These are all part of the overall cost entailed in not having a credit history. Building a credit history is not something consumers are obliged to do. However, it can reasonably be said that

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take cash only (such as car or equipment rentals) and excluded online internet transactions. For the purposes of the present study, the results of this survey are useful in that its insights suggests the importance of credit cards for the merchants surveyed, since at least 89 percent of them accepted credit cards as method of payment. Whether or not the high percentage of merchants that accept credit cards do so due to the benefits entailed in attracting credit card holders or to market dominance by credit card payments' networks may be contentious and beyond the scope of this study.

the burden of coping without a credit card drives consumers to build a credit rating to acquire one.<sup>91</sup> The question that arises from this situation is clear: are credit card companies effectively the gatekeepers to the credit score system? To the extent that the modern financial economy and its credit market is based upon reputational credit, there is a second question. Is the consumer economy and household sector influenced more by consumer credit providers and lenders than by national financial authorities?

By contrast, transactions paid with credit card are part of the credit-building exercise and are eligible for credit-reporting. If a consumer uses a credit card for a reasonable number of transactions and is careful to pay his minimum balance every month, the consumer will be building a credit rating. This rating has a significant effect on reducing his borrowing costs and increasing his likelihood of being approved for major credit such as a mortgage or an automobile loan. In comparison, a consumer who uses a debit card as payment method for the exact same purposes would have not improved their credit rating at all. In fact, such a consumer would have incurred significant opportunity costs by not having used a credit card as payment method.

## Financial exclusion

The two most common terms used as indicators of financial exclusion are *unbanked* and *underbanked*.<sup>92</sup> The term *unbanked* is used to refer to a particular demographic group that may not have access to any banking services, including a basic service such as savings account. Unbanked consumers have to rely on financial services provided by alternative and fringe lending or cheque-cashing outlets. Consumers who are *underbanked* do have access to some basic banking services, such as a savings account, but have limited access and therefore must resort to financial services from alternative lending or cheque-cashing shops. The participants in the focus groups, despite having access to bank accounts and many banking services, still do not have access to conventional credit cards. Among the most relevant characteristics of financial exclusion are:<sup>93</sup>

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<sup>91</sup> PIAC contacted the largest credit reporting agencies in Canada, TransUnion and Equifax to request their advice to consumers as to how to start building a credit history for first time. Neither one of the companies responded to our requests.

<sup>92</sup> Jerry Buckland and Wayne Simpson, *Analysis of Credit Constraint and Financial Exclusion with Canadian Microdata*, Canadian Economics Association, May 2008, online: <<http://economics.ca/2008/papers/0300.pdf>>.

<sup>93</sup> Government of Canada, *Why Financial Capability Matters, Synthesis Report on Canadians and their Money from the National Symposium on Financial Capability*, held on June 9-10, 2005 in Ottawa, online: Policy Research Initiative <[http://www.policyresearch.gc.ca/doclib/SR\\_PEX\\_fincap\\_200603\\_e.pdf](http://www.policyresearch.gc.ca/doclib/SR_PEX_fincap_200603_e.pdf)>.

- Restrictions to access to financial services through the processes of risk assessment and other bank procedures;
- Exclusion due to conditions and rules for financial products (like credit scoring, minimum balances, and overdraft) that make it difficult or inappropriate for the needs of certain subgroups;
- Exclusion based on the actual cost of using a financial product or providing service to specific subgroups;
- Targeted marketing and sales that do not seek to gain business from certain subgroups; and
- Self-exclusion based on the unwillingness to access financial products or a belief that products are not appropriate for their circumstance (Connolly and Hajaj, 2001).

However, there are other important factors in determining financial exclusion in a modern market. In the United Kingdom, The Treasury (the Ministry of Economics and Finance), set out some of the costs related to financial exclusion for the individual. They include.<sup>94</sup>

- Higher charges for basic financial transactions and credit. Lack of access to a bank account means that certain financial transactions, such as money transfers and cheque cashing, may be more expensive.
- No access to certain products or services. A range of services, such as contract mobile telephones, require a bank account for regular direct debits.
- Lack of security in holding and securing money. Operating solely on a cash budget leaves more people vulnerable to loss or theft.
- Barriers to employment. A bank account for receipt of wages is a basic requirement for most employers; and
- entrenching exclusion. Having no formal banking or credit history at all can be as much a disadvantage as an impaired credit history in accessing certain financial services.

These constraints are widely linked to financial exclusion, along with lack of access to bank accounts.<sup>95</sup> There is an understanding today that paying higher fees for financial transactions, relying solely on cash and lack of access to building a credit rating are all factors contributing to financial exclusion. The absence of effective access to electronic or plastic payment methods or to a favourable credit rating are starting to attract the attention of some financial authorities. This may be due to the fact that these elements are central to consumers' financial lives in modern economies. A very important issue

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<sup>94</sup> HM Treasury (United Kingdom's economic and finance ministry) Promoting Financial Inclusion, December 2004, online: HM Treasury <[http://www.hm-treasury.gov.uk/d/pbr04\\_profininc\\_complete\\_394.pdf](http://www.hm-treasury.gov.uk/d/pbr04_profininc_complete_394.pdf) > at 2.

<sup>95</sup> *Supra* note 91.[Buckland and Simpson]

emerging is the practice of some employers to perform credit checks as precondition for employment. This makes the issue of a favourable credit rating more than an issue of efficient payments. In today's recession, this is a practice that deserves attention of government authorities that can have human and employment rights implications.

## CONCLUSIONS

Recent conventional wisdom seems to indicate that today's society is credit-addicted. However, credit cards and the central position they occupy in today's economy demonstrate how we have become a society whose economy increasingly relies on electronic payment systems for economic exchange. This exchange mostly occurs aside from credit use. Plastic and electronic methods of payment have largely replaced physical bank notes. Plastic and electronic payments contest the traditional monopoly of the national currencies of central banks as a method of payment.

Credit cards are the most popular method of payment by consumers, in Canada and in several other advanced economies. The main functions of credit cards, the electronic and online payment method and the personal creditworthiness-generating tool are increasingly instrumental for consumers' adequate market access today, including possible employment repercussions. Credit cards function primarily as an electronic and online payment tool and a way to build a personal credit rating. These functions have important repercussions, including a person's employability.

For consumers, the use of credit cards today goes beyond simply presumed addiction to credit and is probably more related to rational choice. There are costs entailed by consumers for payments by means other than a credit card. These costs may actually serve as a form of economic pressure to acquire a credit card, given the financial consequences of not having one. The consumers interviewed in the focus groups in this study demonstrate some level of financial literacy. Focus group members possess an understanding of how credit cards work and the risks associated with mismanagement. There are sound economic reasons for some to want to use credit cards in preference to debit cards. While the credit card user is the recipient of a net benefit, the debit or cash-only consumer receives no net benefit at all in terms of building their credit rating.

The availability of payment method with the characteristics of credit cards can make an enormous difference in terms of costs for consumers without access to one. Moreover, the costs for such a payment method such as a pre-paid or secured card are significantly higher for those consumers in the lower end of the income scale. This serves to thin disposable income in sensitive households and push them to increased financial risk.

Plastic and electronic payment methods with a credit-building feature are increasingly an essential element of a modern economy. There are astounding numbers regarding the use of credit cards as a unique method of payment and their widespread use. It seems clear that regardless of the economic status of an individual, a lack of access to credit cards or adequate substitutes with equivalent functions, places them in a position of economic disadvantage.

Credit-issuing policies are risk-based and take into account the levels at which a particular company can predict a client's risk and profitability. However, conventional credit card-granting policies may create barriers for consumers. These are not limited to a lack of access to borrowing by credit card and instead may have ramifications that impede access to other goods and services.

## RECOMMENDATIONS

1 Credit cards are a favoured method of payment for electronic transactions in Canada and their use is very often directly linked to a consumer's credit rating. A consumer's credit rating is taking on increasingly important social and economic dimensions. Therefore, consumers need more options to build their credit ratings outside of conventional or secured credit cards. The credit reporting system should not become a barrier or a burden for consumer access to electronic payments and economic activity. To facilitate access, other transactions could be included as indicators of creditworthiness, such as payments for utilities, phone and internet bills, in addition to banking information.

2 Under the current recession affecting the household sector in Canada, an electronic payment method that could help users with no credit history to more actively engage in electronic transactions at a minimal would help to ease economic tensions. Pre-paid and secured credit cards are inadequate and too costly to fill such a role. The Bank of Canada should be involved in devising such mechanism, since the payments market is inherently a currency matter. Additionally, it is in the best interest of the economy to implement mechanisms for consumers pushed to insolvency so they can be swiftly reintegrated to the economic process.

3 Access to a payment system aside from the conventional credit card network would provide benefits to consumers, issuers and merchants. Increased transactional volumes from such a system would also have a positive impact on the economy. It is important to ensure that a reputational or creditworthiness system allowing for enhanced access provide consumers with specific and detailed reasons why a consumer is declined. This will to afford her an reasonable opportunity to build such essential financial record.

4 Canada is in a privileged position to create a system that could help to integrate cardless consumers to a credit card-based payment system. Both the government and credit card issuers could work together in crafting a scheme that could facilitate the creation of a new financial product. This product could serve as a financial credential and be also used as a payment system that can be recognized by issuers' networks and databases. Eligibility for such payment method could be proportional to income level, so as to avoid a lower income becoming a barrier to build a level of creditworthiness according to a consumer's means.

5 There are potential efficiencies that could be gained by enhancing access to the cash-only population to the online and E-commerce market. The access would not be intended to induce them to accumulate debt. Instead, it allows them to engage in economic activity through electronic-based transactions in a way they otherwise would not be able to.

6 The increase in the number credit checks as an employment screening practice is a growing privacy concern. The link between the ability of an employment candidate to perform the duties of a certain position and her financial standing can only be minimally related. It is true some positions may exceptionally require candidates to undergo credit checks, such as employment in financial counselling or intense handling of significant sums of cash. However, indiscriminate credit checks for employment purposes should be avoided and only be conducted upon specific consent granted by the applicant.

7 When declining a consumer's credit card application, the consumer does not always receive the reason for the refusal. For many consumers, an application for a credit card entails more than an approval for credit; it is a chance to build a financial reputation. Creditors and credit reporting agencies should be offered reasons for refusals to give them a reasonable opportunity to be approved.

8 Under the current system, immigrants and new Canadians are not given recognition to the fact that many of them arrive into Canada with credit cards issued in their original countries. It would be useful to create a way for new Canadian residents to be able to have their financial credentials given consideration for the granting of a credit card in Canada. Patronizing a multi-national bank may offer some form of a solution, but a more widespread solution needs to be made available to everyone.

## **ANNEX**

### **Experiences of consumers with no credit history**

The main data source for the study was the views and experiences of 20 consumers who participated in 2 focus groups in the city of Toronto.

All participants were employed on a full-time basis and were not just internet users but also had some form of internet access. They were all knowledgeable about the interest charges that are for using plastic credit cards and of the differences in interest rates between card issuers. They also had a good understanding of the risks entailed by not meeting payment deadlines and the escalating nature of interest rates combined with fees. The consequences of mishandling credit cards were clear to all of them. This may suggest a level of basic financial education and skills.

It is fair to say that while this group of consumers who are not given access to conventional credit card use are economically productive active and fully employed, none of them are in an income group above the national average, and some of them are in a lower income bracket. While this can mean that they are able to save less due to less surplus income, it is unclear whether or not their consumption patterns are comparable to the consumption patterns of an average Canadian. Among the wider population there may be consumers with higher incomes who have access to plastic credit who use it sparingly. There may also be consumers with lower disposable income who may use it responsibly yet more liberally.

Interesting insights of the interviewed:

- Allusions to the gradual dwindling of cash transactions were common among participants and some mentioned envisioning a future of where a great majority of consumer transactions will be cashless.
- Credit records were likened, to criminal records by some of the participants, mainly due to the increasing practice of performing background checks for employment purposes that include both criminal records and credit histories.
- There was some impression of randomness in the process of eligibility. Some respondents had work or social acquaintances in a similar or worse financial situation who possessed one or more credit cards.

**DRAFT  
REPORT**

Attitudes toward Access to Credit Cards –  
Qualitative Research

*Prepared for:*  
Public Interest Advocacy Centre

November 2008

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## **INTRODUCTION**

### **Background**

In the current information economy, plastic credit has become, more than a financial convenience item, a sort of credential or 'passport' that enables consumers to be validated to perform economic and commercial transactions in a more efficient and convenient manner, while offering retailers, suppliers and merchants in general the benefit of engaging the credit card user base, who constitute the mainstream of all adult consumers. For consumers and merchants, there is value in reducing the need of having to carry, stock and use cash for all transactions

However, little attention has been paid to the barriers that a substantial number of consumers face in their efforts to access the online marketplace and other important services such as online retail, car rentals, travel reservations and transportation in general, hospitality, government services, and most other services.

Not having access to a credit card, entails higher overall costs for those consumers who have no credit history and must resort to alternative sources of financing. These consumers are in their vast majority young adults and newcomers who are in need to swiftly integrate and participate in the economy. Increased difficulties to access credit card use may create inefficiencies that are exploited by high interest lenders through mechanisms such as pay day loans and fringe lending, whose interest rates are adjusted to the risk posed by loans made to consumers with damaged credit. However, according to the recent paper co-authored by Shubhasis Dey, a Senior Analyst at the Bank of Canada, "households who are denied credit could well turn out to have ex post higher repayment probabilities than some credit card holders who borrow large portions of their borrowing limits".

### **Research purpose and objectives**

The purpose of this research is to assess the benefits of increased consumer access to credit card use with respect to the facilitation of consumers' access to market exchanges in an economic environment where digital transactions have become the norm, and conversely, cash transactions have become the exception. To further this goal, the research examines the daily life realities of Canadians who do not have access to credit card and the impact of this situation in their lives.

The primary focus of this research is to explore the following issues:

- What are the specific consequences of not having access to credit cards in consumers’ financial lives; and
- To what extent consumers without access to credit find other financial products as substitutes, and whether the unavailability of a credit card precludes them from meaningfully engaging on electronic commerce.

## Methodology

Two (2) focus groups were conducted in Toronto. Both groups were conducted with participants, both men and women, who are not credit card holders, and who said they had never held a credit card in Canada in the past. All participants were between the ages of 20 and 70.

Location	Dates	Group Composition
Toronto	Monday October 27 5:30 pm	Not credit card holders
Toronto	Monday October 27 8:00 pm	Not credit card holders

For each group, 10 people were recruited, with an expectation that each group would have approximately eight participants. Recruiting guidelines specified:

- All participants are employed, with no more than three part-time employees recruited for each group.
- All participants use the Internet at least occasionally – either at home, work or Internet cafes or libraries.
- In each group, at least three of those recruited are recent immigrants.
- All participants were people who have never had a credit card in Canada because they have been rejected for them, NOT people who may have had them in the past but who lost them due to bankruptcy or a poor credit rating and also NOT people who don’t have credit cards because they don’t believe in them or don’t want them.

Each focus group session was approximately two hours in length and was conducted according to a discussion guide developed in consultation with the client team. A \$75 cash incentive was given to each participant in appreciation.

Derek Leebosh, Senior Associate – Public Affairs, of Environics Research Group, acted as Project Director and moderated the focus groups.

All qualitative research work was conducted in accordance with the professional standards established by the Marketing Research and Intelligence Association (MRIA – previously the Professional Market Research Society and the Canadian Association of Market Research Organizations).

### **Statement of Limitations**

The objectives of this research initiative are exploratory and therefore best addressed qualitatively. Such research provides insight into the range of opinions held within a population, rather than the weights of the opinions held, as would be measured in a quantitative study. The results of this type of research should be viewed as indicative rather than projective.

## EXECUTIVE SUMMARY

Environics Research Group is pleased to present this summary of key results from research into attitudes toward access to credit among those who are not credit card holders. The purpose of this research is to assess the benefits of increased consumer access to credit card use with respect to the facilitation of consumers' access to market exchanges in an economic environment where digital transactions have become the norm, and conversely, cash transactions have become the exception. The research consisted of two focus groups held in Toronto on October 27, 2007.

### Key Findings

#### GENERAL ATTITUDES TOWARD CREDIT CARDS

From the perspective of those who do not have access to credit cards, the main advantages of having a credit card fall into several categories:

- Uses of a credit card that are similar to the use of cash in that they could be readily managed without having access to a card, but preferable in that they permit convenience and ease of making purchases and carrying out other financial transactions such as paying bills;
- Uses of a credit card as a short-term loan to cover temporary cash flow problems, handle emergencies or provide up-front funds for large-ticket purchases or major expenditures;
- Uses of a credit card that lead to additional benefits that are desirable but not necessary, such as loyalty programs, travel insurance, extended warranties, and special discounts;
- Uses where a credit card is the best, and sometimes the only, way of engaging in the desired transaction or obtaining the desired outcome, such as internet shopping and making travel reservations; and
- Use of a credit card to build a good credit history that will allow further access to credit, such as a mortgage.

Most participants saw one of the main disadvantages as the ease with which one can use credit unwisely, or excessively, opening up the possibility of making purchases without thinking of the consequences, and risking the possibility of going into debt. Related to this is the awareness that misuse of a credit card or being unable to make regular payments can damage one's credit rating. Participants also mentioned high interest rates – as opposed to other forms of credit such as loans, lines of credit and mortgages – as a disadvantage of having a credit card.

Other disadvantages mentioned include risk of theft, fraud or identity theft, particularly when the credit card is used online, lack of security precautions on the part of

merchants, and the sometimes disastrous consequences that can ensue if other people gain fraudulent access to one's credit cards or personal information.

Many participants see the ownership of a credit card as an important part of life in Canada – something that is not just accepted as a common method of making purchases and payments, but expected, even assumed. Some participants suggested that those who do not have credit cards are looked on as second-class citizens, or as people who carry a stigma because the lack of access to credit is assumed to indicate a lack of fiscal responsibility or a state of financial insufficiency.

Some did point out that the use of debit cards is also becoming more and more a standard way of doing business, and that debit cards are accepted almost everywhere that credit cards are.

#### **EXPERIENCES WITH CREDIT CARDS**

All participants had applied for a credit card at least once and been denied. Only a few participants were certain that they knew why their application(s) for a credit card had been refused.

Most assumed that they had been denied because of low income or employment history. This can be a particular problem for recent newcomers to Canada, because they have not had time to find a job or to build up an employment and credit history in Canada, and it is their experience that their history with respect to credit or employment in their country of origin is not taken into account in making a decision on whether to accept their application for a Canadian-based credit card. Other participants speculated that the refusal was related to their credit history or to the amount of loans they were carrying. Several people had been denied credit as a result of damage to their credit ratings as a consequence of identity theft.

Most participants said that they had received some kind of information on how to find out more about the decision not to offer them credit along with the notification they received; this was generally in the form of a phone number. Others did make attempts to contact the credit card provider in the manner suggested to them, but found the process difficult and frustrating. Many gave up without getting a clear answer concerning their refusal of credit. The general impression received by most participants was that credit card providers were not particularly forthcoming about the details of the application and decision processes. Some participants said that they were offered alternatives to the credit card they had applied for and been denied; a few were advised to contact a credit bureau for information about their Beacon score.

**IMPACT OF ACCESS TO AND DENIAL OF CREDIT CARDS**

Most participants in this research said they would like to have a credit card, if only for emergencies, making travel arrangements, or for purchases that cannot be made easily by other means. Some want access to the “extras” that come with credit card ownership – extended warranties, travel insurance, “points” in loyalty programs, special sales available only to holders of certain credit cards – even more than they want access to credit on a regular basis. Others want to be able to have all of the same advantages, including convenience in purchasing, that credit card holders already have.

Credit cards are often the only way to reserve rooms in hotels, leave security deposits when renting cars, place orders for tickets with telephone services such as Ticketmaster, or reserve travel arrangements directly with the providers (airlines, etc). In other cases, the lack of a credit card means that they must deal with certain issues in a way that is either more expensive, or less convenient. Having a credit card (or some other way of demonstrating a good credit history) is also important when applying for apartment rentals, certain jobs, and utility hook-ups.

For some participants, these circumstances do not arise very often, and they either do without, or find ways around their difficulties. Others find the inconvenience of not having a credit card, and even more so, the inability to pay for certain things or to have access to credit in an emergency, to be more serious, even distressing.

Some saw their inability to gain access to credit as unfair, because there are some things that can only be managed using a credit card, or some benefits only available to credit card holders. Access to credit – and its associated benefits – is seen as approaching the status of a right, and in some cases a necessity of life.

**KNOWLEDGE OF CREDIT CARDS**

Participants identified several groups that they believed have limited access to credit cards:

- People with low incomes, the working class or “working poor.”
- Unemployed people and people with inconsistent employment records, including temporary workers, the self-employed, or those working in the underground economy.
- People with no credit history, including recent newcomers to Canada, students and recent graduates.
- People with a poor credit history

Most participants have at least some idea of what a credit rating or a credit score is, and what it means in terms of their ability to access credit. However, there are some who do not know what their own score is, or how to find this information. Others have requested a copy of their credit report, or have discovered their credit score through other means, either through a credit bureau or through their bank. Some have a relatively clear idea of how a credit score can be damaged, but others are unsure about how a good credit score can be achieved

#### **ALTERNATIVES TO CREDIT CARDS**

Participants have had to find ways of managing their financial and consumer needs without access to credit cards. Most have bank accounts, which give them access to alternate financial products and services, including debit cards, Interac payments, internet or phone banking, and overdrafts, which provide many of the same functions as credit cards do. Possession of a bank account also makes it possible for participants to use services such as Pay Pal for electronic payments to online vendors. Some participants also mentioned the availability of pre-paid credit cards. Others rely on friends and family who do have access to credit to take care of these needs on their behalf.

The main disadvantage most participants find with alternatives such as debit cards and Pay Pal is that these are not accepted everywhere, as credit cards appear to be. On the other hand, many noted that acceptance of these methods of electronic payment is growing, and they expect that as time goes by, it will become more common, reducing the need for credit cards. On the other hand, these options are seen as having many of the advantages of credit cards without the disadvantages of high interest rates and exposure to debt accumulation.

## PROPOSED SOLUTIONS

Participants' recommendations on improving access to credit for people like themselves fall into four general categories:

- Changes to the criteria used to make decisions on who should be allowed to hold a credit card, placing more weight on employment history of any kind and less on credit history;
- More widespread adoption of alternatives to credit cards, such as debit cards, and services that allow payment directly from one's bank account over the Internet;
- Making available credit cards with modest limits, and keeping these limits modest rather than increasing limits over time, in order to reduce risk of overuse; and
- Greater availability of pre-paid credit cards, or credit cards that are secured by an initial deposit.

## DETAILED FINDINGS

### Attitudes toward Credit Cards

In order to determine the context for participants' experiences of applying for credit cards and their feelings about being denied access to the level of credit that these cards offer, participants were asked first to engage in a team exercise in which they identified the advantages and disadvantages of having a credit card. Participants were also asked whether they felt that credit cards were becoming more necessary or important, and whether their own opinions about credit cards have changed over time.

#### ADVANTAGES OF HAVING A CREDIT CARD

From the perspective of those who do not have access to credit cards, the main advantages of having a credit card fall into four broad categories:

- Uses of a credit card that are similar to the use of cash in that they could be readily managed without having access to a card, but preferable in that they permit convenience and ease of making purchases and carrying out other financial transactions such as paying bills;
- Uses of a credit card as a short-term loan to cover temporary cash flow problems, handle emergencies or provide up-front funds for large-ticket purchases or major expenditures;
- Uses of a credit card that lead to additional benefits that are desirable but not necessary, such as loyalty programs, travel insurance, extended warranties, and special discounts; and
- Uses where a credit card is the best, and sometimes the only, way of engaging in the desired transaction or obtaining the desired outcome, such as internet shopping and making travel reservations.

Convenience means somewhat different things to different participants, but the main themes expressed were about being able to purchase what you want, when you want it, whether or not you have immediate access to cash. The credit card is seen as an alternative to cash, in that having it means that you don't have to carry sufficient cash with you at all times, and you can gratify desires to buy or order goods and services immediately without having to go to a bank to take out funds, or wait a few days or weeks until you have the needed cash in hand.

For some, convenience also included being able to make certain transactions, such as bill-paying, easier and faster because you can use the internet or the telephone rather than having to mail a cheque or money order, or travel to a location where you can pay in person.

You wouldn't have to carry a bunch of cash all the time if you were out shopping.

Cash, you don't need the cash. Pull it out; whip it out wherever you go.

Just paying bills, because some bills you have to pay – like the phone bill you have to mail it in, and if you have a credit card you can pay easily it on the phone.

Credit cards were seen as being particularly convenient when travelling, because there is no need to deal with currency exchanges, or having to carry large amounts of cash in an unfamiliar place. Also, participants expected that they might encounter emergencies requiring unexpected expenses while travelling, and that any such expenses could be easily handled with a credit card.

Especially when you're going travelling, too, at the hospital and you don't have insurance and you're in another country. You have to pay it. And, you don't have money left, so the credit card is good for that.

Some participants, however, saw a major advantage of having a credit card in the fact that they could in fact buy larger-ticket items that they could not immediately pay for. For these participants, the credit card is seen as a kind of short-term loan, with the added bonus of being interest-free if they can repay the loan within the interest-free period. It would be a means of managing temporary cash flow problems.

I consider the credit card as a short-term loan. Like, let's say when I needed to buy my bed, because I didn't have anything, and it was \$500/\$600 and I had to pay that right away. And, I didn't have at that moment. And, I paid the next month for it.

If you buy a lot of stuff, if you're renovating a project, you don't have to pay for a month on it. Maybe six weeks.

Participants also noted that having a credit card means being able to take advantage of affinity and loyalty programs and other special deals. Most were aware of benefits offered by credit card providers such as points programs, travel insurance, extended warranties on item purchased with the credit card. Some have also seen or heard of situations where special sales or priority access to limited products or services are offered to holders of a specific credit card. Some of these benefits, such as travel insurance, were seen as important advantages that could be of significant benefit, while others were seen more as "perqs" that they might like to have, but could do without.

Some of the credit cards, you can collect points and get some free stuff.

When you pay for a car rental with American Express, you get free insurance for that rental car, and if you leave the country for a week or something like that, you pay for your airline tickets, maybe, with American Express or some of those charge cards, you get free Blue Cross.

If you deal with one of those things, and sometimes you can get an extended warranty on a product, say you're buying a china plate. It might break, so if you buy it on there, you might be insured for three months.

Credit cards were also seen as being necessary in some cases; participants can readily name a variety of circumstances in which having a credit card by far the easiest, or even the only, way to meet their needs. Most mentioned such uses as making reservations for travel by plane, rental cars and hotel accommodations, making purchases on the internet or over the telephone from suppliers without a local address or distributor, and the ability to use the card in emergencies when you may actually have the cash, but can't access it quickly enough, or when an unexpected expense must be incurred, such as a dental or medical bill.

You can rent cars, make reservations at hotels. You can buy on the Internet.

Renting a car or a hotel reservation, Christmas shopping, hospital or dentist meaning if you don't have insurance.

If you needed something on the Internet, and if you didn't have a credit card and couldn't purchase it, especially if it's on sale price or something like that.

Some participants also thought that one advantage of having a credit card was that it could be used as a credit reference or to establish a good credit rating through judicious use of the card. There was a clear sense that the possession of a credit card implies to others that the card holder is financially responsible and deserving of other opportunities for credit. A few also mentioned the use of credit cards as identity documents.

It can help you establish your credit if you don't have any.

Like a personal reference when I want credit for a mortgage or something, if you want to buy anything, you just show them your card. It's like that, automatically accepted, because they already got all your information from when you applied for the card. Automatically you qualify.

#### **DISADVANTAGES OF HAVING A CREDIT CARD**

Participants were also able to think of a range of disadvantages to having a credit card. Most participants saw one of the main disadvantages as the ease with which one can use credit unwisely; for these participants, one of the primary advantages of credit

cards, their convenience, can also become a major disadvantage – it opens up the possibility of making purchases without thinking of the consequences, and risking the possibility of going into debt. Many participants felt that credit cards can be “too easy to use,” and require one to be disciplined about spending and make regular payments on time in order to avoid going into debt. Some participants noted that this kind of temptation to spend more than you can afford is built into the credit card system – that once you have a credit card and use it responsibly for a while, the limit keeps being raised until it is possible to drive the balance beyond your ability to manage it. Others noted that once you have one card, you can get others and run up large balances on all of them.

Keep spending, running up more cards and maxing out.

Addicted to buying things or addicted to spending money.

It encourages compulsive spending if you don't need your cash on hand.

Not being able to pay the debt.

With a card, it encourages you to spend because it's not the same if you have the money here. You think more because you have the cash.

And, then when you max out one card, you have another one and you max that out. Now when you're making payments you're trying to figure out who is going to pay.

Related to this is the awareness that misuse of a credit card or being unable to make regular payments can damage one's credit rating. Again, the advantages of having a credit card – access to credit – were seen as a two-edged sword; using the card's advantages can ultimately be disadvantageous. Most participants were aware that defaulting on credit card payments was likely to damage their credit rating. As well, many of the participants had learned – sometimes after being told by representatives of banks or credit bureaus – that one's credit rating is also affected by the number of times one applies for credit cards.

You can ruin your credit if you misuse it.

It can damage your credit rating if you're poor with your payments and what have you.

Participants also mentioned high interest rates as a disadvantage of having a credit card. There was an awareness that not everyone pays off their credit cards in full each month, and that once interest is applied to a purchase, the rates can add significantly to

the cost of the purchase. Not all, however, had a clear idea of what those interest rates might be. There was little mention of annual fees that are applied to some credit cards.

Okay, the disadvantages are the interest fees, if you don't pay it on time.

They say the interest rate on a card is worse than the interest rate on when you buy a car.

Interest rates. Some of them are more reasonable than others, but interest rates. Say you're buying something retail at \$100, you're approximately paying \$150 for that product actually when you're finished paying it off.

Other disadvantages mentioned include risk of theft, fraud or identity theft, particularly when the credit card is used online, lack of security precautions on the part of merchants, and the sometimes disastrous consequences that can ensue if other people gain fraudulent access to one's credit cards or personal information. This was a real concern for many participants in this research; in fact, several participants volunteered that even without having a card, they had been the victim of identity theft, and that it had in some cases been exactly for this reason that they had been unable to qualify for a credit card – because someone else using their personal information had ruined their credit.

When you're using it there is a person that has a machine that can scan your card.

We were talking about online identity theft. It's a bit of a stretch, but it does happen.

If you lose it, or it's stolen, then you could be in for a lot of problems.

I was thinking identity theft, but then when you're using them, etcetera, they never check who's signing it. If you throw out the card, anybody can sign this. As long as it looks like it's the same name as on the card, they just say 'thanks'.

It is of interest to note that while most participants presented themselves as able to handle credit cards sensibly when discussing the advantages of having a card, many focused strongly on the consequences of excessive use of the cards and the possibility of running into unmanageable debt when listing the disadvantages.

#### **IMPORTANCE OF CREDIT CARDS**

Many participants see the ownership of a credit card as an important part of life in Canada – something that is not just accepted as a common method of making

purchases and payments, but expected, even assumed. Many participants commented that almost all of their acquaintances or everyone they see around them has, and regularly uses, credit cards. Others noted that everywhere you go, you can use credit cards, even at parking meters, and that there are so many different cards available from financial institutions and retailers.

It's a standard way of living here in Canada.

I think they're more commonplace now, by far. I know some people that never use cash, just credit, just credit cards - a lot of people.

I can say they assume everything. Like the selling stores, whoever wants to give you something, it's like a default. You have to have a credit card.

I never ran into an emergency, never used it. So, that was like the old days. That was if, maybe, an insurance. Today, you've got to have one. So, my thinking has changed on them.

It's the norm. It's the in thing. You don't got it, you don't fit in.

Some did point out that the use of debit cards is also becoming more and more a standard way of doing business, and that debit cards are accepted almost everywhere that credit cards are. It was the perception of most that the use of credit cards – and debit cards – has in fact become more common in recent years. A few envision a future in which there will be no cash, only cards.

So much more people are getting credit cards. I think, in some stores, instead of having – in some stores, going in there and it'll be like, oh, we don't have the card for that machine. In some stores in the future, like the way, way future, they might not have cash.

But there's a debit card for that too, because I mean if you go into a hotel or something, they'll usually accept a debit card. Most places will accept the debit card now.

Some participants suggested that those who do not have credit cards are looked on as second-class citizens, or as people who carry a stigma because the lack of access to credit is assumed to indicate a lack of fiscal responsibility or a state of financial insufficiency. In short, participants felt use of credit is seen as part of the normal way of managing purchases and finances, and that people without credit cards are assumed to have something wrong with them. For some, the fact that some jobs are advertised as requiring someone who must pass a background check that includes both criminal and credit histories is an indication of how important a "good credit rating" is.

If you have no charge card, then people sort of question you, like, 'what can you afford? Why not?'

When you're asked whether it be in a store or an organization, if you don't have a credit card it's kind of like you're frowned upon, so to speak. It's like you're not financially responsible if you don't have a credit card.

Some ads you read, 'must pass criminal and credit check'. If you have bad credit, you ain't getting that job.

A few participants commented on the use of credit in other countries where they had lived. Perceptions varied; some said that the use of credit in the countries they are familiar with is similar to how it is used in Canada. Others reported that in their home country, credit is less extensively used, and may only be available to members of the upper middle or upper classes.

## Experiences with Credit Cards

Most participants had applied for a credit card at least once, and been denied. Several had tried to qualify for a credit card on several occasions. Most had a clear sense of what they would expect to be different if they had a credit card, and how not having a credit card has an impact on their lives. A few of the participants who are New Canadians had held credit cards in other countries, but almost all discussion of experiences with credit cards related to experience in Canada.

### APPLYING FOR CREDIT CARDS

All participants had applied for a credit card at least once. Some participants had made an active decision to apply for a credit card – either a bank card such as MasterCard or Visa, or a store card – but many had applied for cards in response to marketing campaigns, usually mass mailings or store promotions or intercepts.

I guess the last time I applied was a year or two back. I kept getting, ‘you’ve been pre-approved by Capital One’ in the mail for a platinum card or whatever, so I applied and sent it away.

About a year ago last August I was into the Home Depot and you get 30 percent off on your first purchase if you went for a credit card on a \$100 purchase, max.

I was walking through a mall one day, I wasn’t planning on getting a credit card, but you know how you have those people standing there trying to make you get a credit card? And, they give away little gifts to make people want to get them more. So, one day I was just walking around there and then I tried filling it out.

Only a few participants were certain that they knew why their application(s) for a credit card had been refused. Most assumed that they had been denied because of low income or employment history. A few seemed somewhat baffled by the fact that they had been refused after receiving a mass mailing saying that they had been “pre-approved,” but in general participants tended to chalk their refusal up to “not making enough money” or issues having to do with their employment.

I think I was rejected because I wasn’t making enough money.

I think it’s because I work a lot of temp assignments. So, when I tried to apply for a card they said my work history wasn’t stable enough.

I didn't have enough established history, because of jobs, not staying long enough.

Being seasonal they look at your work history.

This can be a particular problem for recent newcomers to Canada, because they have not had time to find a job or to build up an employment and credit history in Canada, and it is their experience that their history with respect to credit or employment in their country of origin is not taken into account in making a decision on whether to accept their application for a Canadian-based credit card.

First I was new to the country; I had no job or anything, so they didn't give me one.

Other participants speculated that the refusal was related to their credit history or to the amount of loans they were carrying. Some were paying on loans at the time they applied for a card, and others had a credit history that included a default on a loan or "money owed to the government." They did not necessarily know their credit score, but they had an expectation that their rating was poor because of loans or other monies owed, and that this was likely why they had been refused a credit card.

I'm pretty sure it was my credit rating. It's not so good. After that, I didn't even bother to try it again. To hell with it.

I think I owed some money, not that much, but because of that my credit rating was off.

I still have my student loan and I couldn't get a job for about six months, almost six months to a year, and then when I did start paying on it, it had already defaulted.

Many of those participants who gave other, specific reasons for why they had been refused a credit card had actually followed up on the initial refusal. Several people discovered that they had been victims of identity theft during this process, and that their credit ratings had been damaged by other people who had taken out credit cards in their name. One woman found that she had been denied credit due to inconsistencies in documentation stemming from the fact that naming conventions in her country of origin are different from those in common use in Canada. One participant, who did not actually investigate the reasons for his refusal, believed that he had been refused credit because his name is similar to that of a family member who has had several problems with his credit cards, including identity theft and a dispute over a purchase of an appliance that was defective.

I was denied to have my credit card, because in Peru we use two last names, father's last name and mother's last name. ... So, that's all my documents from back home. So, I opened a bank account with all my complete documents' names. And, then they said what's your name? .... If I am in Canada it's on the father's last name. And, they said, okay. So, then I sent my application for the credit card. It said 'denied'. Why, I said. Because you are trying to fraud the bank. Because you have two last names, how come?

I applied, and got rejected. I called the 1-800 number and they said that the problem was that I had a credit card and I was owing over \$3,000 in Ottawa. I know that I never went to Ottawa. I went down to the branch, which is this branch down here, and talked to them. They said the record shows, actually, I was owing. I couldn't take it. I had to walk into College Street to the cops. We talked about it, and they said they had to do a proper investigation and noticed that somebody with the same name, the same birth date was also receiving money from the government.

When I applied, that's when I was denied and then I went to find out why I was denied and then they said that you had all these credit cards, which I never applied for a credit card before. So, I contacted the Credit Bureau and I said, what the hell are you talking about? I never lived at this address and I never lived at that address. Somebody stole my identity.

Most participants said that they had received some kind of information on how to find out more about the decision not to offer them credit along with the notification they received, although for some who had applied in-store and were refused on the spot, this information was sketchy or was provided in such a way that they did not make a note of it for later follow-up. Others said that they were never given a reason, and did not recall being given a way to find out more about the decision.

Most participants who remembered receiving some information about their refusal of credit said that they had been given a phone number to call for more details about the decision to deny their application. Some simply did not bother to call and find out any of the specifics of the company's decision. Others did make attempts to contact the credit card provider in the manner suggested to them, but found the process difficult and frustrating. Many gave up without getting a clear answer concerning their refusal of credit. The general impression received by most participants was that credit card providers were not particularly forthcoming about the details of the application and decision processes.

I applied for my credit card about three years ago, and I got rejected. They didn't give me an explanation. They just gave me a number to call.

Then, after about three to four weeks, I received the letter, 'wow, maybe I have my credit card.' Then, I open it and it's a letter, really kind letter, 'Hi, thank you for applying for a credit card. At the moment, you do not qualify', but they don't give any reason why. I called them to ask them why and they say, 'you have to call another phone call. I know there is a number, but this is not the one. You have to call a specific credit acceptances, something like that.' 'Okay, then give me the number, then.' I give up, too many options. It's taking so long. It's ridiculous.

Some participants said that they were offered alternatives to the credit card they had applied for and been denied, such as the option to get a co-signer or guarantor for their card or to set up a secured or pre-paid card instead. Some were told that the provider offered other credit card options that they might be eligible for and were invited to reapply for one of these. A few were advised to contact a credit bureau for information about their Beacon score.

And, then they gave me a thing to put my mom to write or something. But I didn't want to do that.

They offered me a secured credit card, but that means that half of my money will be frozen for a certain period of time. They told me when I find a job to go, but at least one year after. I went there, but I was already 32 weeks, so they didn't give me one.

They got back to me months and months and months later to decline me for the highest one, which was the platinum or whatever, and they didn't go into detail, as they never do. Your income had to be like \$100,000 a year or something, but they said I didn't qualify because of my income, but I would qualify for the other one, but I applied and never heard back from them.

They told me, actually, the last time that I applied to contact Equifax. I guess that's a credit bureau or whatever, but I don't know how, because I've never had a credit card.

Many participants did not make much distinction between credit cards offered by banks and other financial institutions, and credit cards offered through retail stores such as Zeller's or Canadian Tire. Some, however, thought that it was easier to qualify for a retail store card than for a card issued by a financial institution. There did not appear to be much awareness that the retail store cards often carry higher interest rates than the cards issued by financial institutions.

Sears is the easiest. And, you know who is the easiest too? Leon's. You can go in there, purchase stuff, your credit is okay. If you don't have credit, they'll give it to you and tell you when do you want to pay? Do you want to pay it off in a year?

**DESIRE FOR CREDIT**

Most participants in this research said they would like to have a credit card, if only for emergencies, making travel arrangements, or for purchases that cannot be made easily by other means. Some want access to the “extras” that come with credit card ownership – extended warranties, travel insurance, “points” in loyalty programs, special sales available only to holders of certain credit cards – even more than they want access to credit on a regular basis. Others want to be able to have all of the same advantages, including convenience in purchasing, that credit card holders already have.

Just for travelling. But it would be staying under my mattress unless I’m going somewhere out of the country.

...it sure would be handy to have one, but I think it’s difficult to get one these days.

If you can book a rental car at the same time as your airplane ticket, the rental car usually will be cheaper. So, you’ve got to have the card.

A few, however, said that they did not really want a credit card because they were not “good with money,” or because they did not want to accumulate debt.

But, honestly, living without a credit card, a lot of people who are in debt – like, you are in a better place, because when I don’t have money, I just don’t have money. I’m not building up all this other stuff. You know what I mean?

For some, their inability to gain access to credit is seen as unfair, because there are some things that can only be managed using a credit card, or some benefits only available to credit card holders. The widespread expectation that everyone has a credit card, and the heavy marketing of credit cards with special benefits, appears to have eroded the idea of credit as being something that is extended to specific people because they have given evidence of being a “good risk.” Access to credit – and its associated benefits – is seen by some as approaching the status of a right.

I think it’s unfair, though, because for people with bad credit, they don’t have the same advantages other people have that have good credit. They’re losing out on a lot of stuff, I would say.

It’s understandable if you’ve got bad credit and there’s a reason, maybe you’ve screwed your credit before and you can’t get one, but for newcomers or people like ourselves that just can’t [get] one because of certain stipulations, then it is unfair.

It's unfair because they should make them easily accessible to everybody. Because right now any way you go to get a cell phone, you need a credit card, which is hard. People come into the country, you can't get a cell phone, and you have to get this pre-paid because you don't have a credit card.

Some participants, however, felt that the ways in which credit works in Canada make sense from the point of view of banks, retailers and service providers. They recognized that when a company provides credit to an individual, it is their right to have a reasonable expectation of being repaid, and that the best way to ensure that is to offer credit only to people with a proven record of being able to manage their finances and repay debts. They also saw the wisdom, from the retailer's point of view, of requiring a credit card number for reservations.

If I was an economic entity, I have to look at it from that side too. Somebody who I don't know if they're going to pay me back or not. If say they didn't have a job and said can I have money, or people are asking you to borrow money and they have no way of paying them back, would you want to lend them money?

I think a lot of it is because they want to guarantee that reservation, for example. Because anybody can call and say I want a hotel room, but are they going to show up? The credit card is pretty much guaranteed.

#### **IMPACT OF DENIAL OF CREDIT**

Participants have no difficulty in identifying specific ways in which the denial of credit cards affects them or what they could use credit cards for if they had the opportunity. Credit cards are often the only way to reserve rooms in hotels, leave security deposits when renting cars, place orders for tickets with telephone services such as Ticketmaster, or reserve travel arrangements directly with the providers (airlines, etc). In other cases, the lack of a credit card means that they must deal with certain issues in a way that is either more expensive, or less convenient. Having a credit card (or some other way of demonstrating a good credit history) is also important when applying for apartment rentals, certain jobs, and utility hook-ups.

If I want to rent a vehicle, I can't do that, and if I want to travel, if I want to go home, or get a plane ticket in advance, I can't.

I'm going to be moving soon, and even for renting apartments, they'll ask [to see a credit card].

You need a credit card even to rent movies.

Right now, the way things are going, you actually need a credit card for almost everything.

The hotels always want you to have a credit card for a reservation.

For some participants, these circumstances do not arise very often, and they either do without, or find ways around their difficulties. If they could, they would make their lives less complicated by using a credit card rather than having to work around it and sometimes do without, but it is rarely a significant problem for them

For me it's just things like if I want to go to a concert and tickets are going on sale. You know, I don't have a credit card, so I have to get a friend to do it. Or, if I want to go away and book a hotel.

The only thing I found is that, like, for my cell phone bill, you know how if you pay for your bill and you mail it in, it takes five business days to do it. And, if you're paying your bill late it's going to get disconnected, right. It's going to take time to go there. If you have a credit card, you just call there and it instantly goes onto Bell, or whatever company you deal with.

Just periodically if there is something you really want to have. Or, again, if an emergency arises and you don't have the cash, then you're thinking, I don't have a credit card to take care of it. So, you either have to wait or borrow it from someone depending on the emergency.

Just once in a while it might happen. Like, the other day I had to pay for my daughter, she has to write her SAT and I wanted to register for her, but they needed a credit card. So, I had to get a friend to do it for me. But, it's just once in a while.

But for these participants, the biggest change if they had a card would, they expect, be one of greater convenience, or greater peace of mind in knowing that they had a back-up source of funds in an emergency.

I'll survive without one, but I think it's the convenience. It makes life easier, easier access for everything.

You know what I think a credit card is good for? To stay in your pocket and use as emergency for when you're going on trips.

I am still surviving. I'm still buying the things that I wanted and working, but it would be good and maybe convenient if I had a credit card.

For some, having a credit card would mean they would be able to save money by paying in advance, taking advantage of special offers and discounts, and making use of similar offers and opportunities available to someone who is able to shop with credit.

If you're going to get a plane ticket now, then you've got to go down there and you're paying a higher price than you would if you paid in advance. So, in my books, it would be cheaper for me to travel if I did have a credit card.

Even cell phones, for example. I have to go with a pay-as-you-go, which is really costly, as opposed to a three-year contract plan because I didn't have a credit card. That's just one example.

Others find the inconvenience of not having a credit card, and even more so, the inability to pay for certain things or to have access to credit in an emergency, to be more serious, even distressing. For these participants, inability to access credit is a significant problem, and they tend to expect that having a credit card would result in some major changes in their lives in terms of what they could do and what financial resources they would have.

Credit cards, like I said, can be something that's necessary. For whatever reason. Medical or whatever. And, you know, what is a person to do? For example, if you have a toothache, they can't get a credit card, they don't have cash, and they have to suffer for days? Because sometimes, even myself, like I said I'm doing all this temp work and I don't have benefits. So, everything that I need to do, with the dentist and whatnot, I have to pay for.

Participants appeared, for the most part, to make the assumption that they themselves would pay off such charges on a monthly basis, thus avoiding interest and an accumulation of debt. This was particularly true of those who see themselves as using the card as a replacement for the use of cash or as a way to gain access to the savings and additional benefits of having a credit card (points, warranties, etc.). In one group, participants were shocked to hear one person mention that he had read that half of Canadians do not pay off their balance each month; it appeared that, while all participants were well aware of the ramifications of overuse of credit cards and accumulation of credit card debt, they assumed that most people with access to credit acted as they believed they would, limiting use of credit to what they could reasonably and quickly pay off.

When I don't have money it's upsetting to me, because then I'm like if I had a credit card right now I could just do it because I know that I can pay it back. I just don't have the money today.

## Knowledge of Credit

Part of the context of participants' perceptions of access to credit is the degree of knowledge they have about credit – who is more or less likely to have access to credit, and what role credit ratings and credit histories have in determining access.

### GROUPS WITH LIMITED ACCESS TO CREDIT

Participants had some clear ideas about what groups are likely to have limited access to credit. While they found it easy to identify certain groups, most felt that access to credit is not affected by discrimination against visible minorities. The most frequently mentioned groups seen as having limited access included:

- People with low incomes, the working class or “working poor.”
- Unemployed people, or people with inconsistent employment records, including temporary workers, the self-employed, or those working in the underground economy.
- People with no credit history, including recent newcomers to Canada, students and recent graduates.
- People with a poor credit history.

At the same time, some mentioned examples from their personal experience or anecdotes they had heard indicating instances in which people in these categories had received credit cards. Some felt that certain people are able to “work the system” in order to gain access to credit, even though they may not really be qualified.

I have no idea because most people in kind of similar things, they have it. All the girls in my store have them, and in my work, in the company,

Yes, I know a lot of people that have the same job as I do and they have more than one credit card. They do the same thing, they pay off and spend, pay off and spend.

I don't know how they do it, but they told me why didn't I apply when I came back. I'm like, 'really?' They said many people coming into the country newly, they get it right away. I don't know how they do that. Maybe it depends on the bank. I don't know.

But this girl I know is on welfare and she got a credit card. And, I go, what the heck?

I think it's a lot easier to get credit cards in school, because like when I was in university they push credit cards at you all the time.

Some have the sense that “honest, hard-working people” are being denied credit while other, less deserving people are finding ways to get credit cards.

I think it's people that are working that are trying to do their best, trying to keep their families going that are ...

I think the people that don't work, the bums in life, they could probably get one because they know how to fangle something. You want your credit to look good, if you're worried about it. You are, right?

#### **CREDIT RATINGS AND BUILDING A CREDIT HISTORY**

Most participants have at least some idea of what a credit rating or a credit score is, and what it means in terms of their ability to access credit. A few acknowledge that while they have heard the term, they really don't know what it is or how it is used by credit companies. They understand it to be an assessment of their financial stability and reliability that in part if not entirely determines whether a company will extend credit to them, whether it be a credit card, a loan, a mortgage, or other credit situation.

I think it is like how much you pay on credit, how much you're behind or how much you're ahead. Whether you keep up with your balance.

One of the ladies at work said that because she never had credit she couldn't even get a mortgage. She saved up her money to buy a house, right, and the first thing they said to her, go to Zellers and get a card. And, she said, for what, I have the money, I have \$20,000 to put as a down payment. They refused to give her a mortgage. So, the only place that would give her a mortgage is a private lending company. And, she said she is not going there because the interest rate would kill her.

It's used to check to see if, I guess, you're financially responsible.

If you have a good credit score, you can get a good mortgage rate or loan or credit line.

Some perceive it as a very important element in determining their access, not just to credit cards, but to almost anything acquired by a significant financial transaction.

I don't want to go into a whole bunch of political stuff, but it's just like that score, whatever it is, is who you are in this world. And, if you don't have that score, you're nothing and you're nobody.

If you don't have credit in this country, you ain't getting nothing. You can't even get an apartment to rent if you don't have credit.

Even though many are aware of what a credit score is, there are some who do not know what their own score is, or how to find this information.

I know what it is, but I don't know what mine is.

I don't really know exactly where to check, but I'm assuming I don't have one because I've never had a credit card. I pay my dad, he pays my bills.

Some participants have requested a copy of their credit report, or have discovered their credit score through other means, either through a credit bureau or through their bank.

I wanted to know. You can do a written one for free but it just kind of tells you, like, so it just had like my cell phone on it, right, because I pay that. But that's it. So, I must have some kind of score somewhere.

You know how you're going to find your score, go to the bank. Your bank will tell your score. That's how I found that.

And, the free one, like I said, will just tell you what they have that you have on your history. I just have the one thing, but it will tell you, like everything. And, then you can pay for one, I think it's like \$19.95. It's like \$20 or something like that, and it will give you whatever this number is.

Most know that defaulting on loans or going over the limit on credit cards can damage their credit rating. Others, who have done some research into credit ratings, are also aware that late payment on bills and excessive seeking of credit are also noted on their credit reports and can lower their scores.

It doesn't take very much to ruin it. All you have to do is not pay your gas bill or something like that and your credit rating is gone.

Each and every time somebody checks your credit, there is a notice of that date and time when they looked at your report. TD, CIBC, Scotiabank, Montreal, keep going around, and I want one now. When you're doing it, it's on the credit report.

Every time you applied it actually kills your credit. I didn't know. The last year, I kept doing that. Any time I did the form, any time I go into any store, I did. I didn't know I was wrong. So, I came down again. I didn't know. So, they had to sit me down and explain. They said I should stop, just about at least for three years, I shouldn't even apply.

When you don't pay them, it's an R9 on your credit report. So, if you pay your Bell bill all the time, in full, on time, that never shows up on your credit history, it's right there in spades. Same thing with your gas bill because gas companies will ask for a \$200 security deposit just to hook them up.

Some participants are baffled as to how one can build a good credit history and earn the kind of score that would give them access to credit, if they are not eligible for credit. These participants feel as if they are caught in a paradox – they can't get credit unless they already have it.

It's like a catch-22. If they will give you a credit card, you need good credit history, but there is no way to have good credit history if you don't have a credit card.

Of course, because what's the cliché, having no credit's almost like having bad credit. They've got nothing to base it on, so you would get declined also.

Others have some ideas about how to go about building a good credit rating – in addition to paying their bills on time and avoiding too many credit checks that suggest they are desperate for credit. Strategies mentioned included taking out small bank loans and repaying them, or applying for prepaid credit cards or low-limit store cards.

I want to figure out what is it then; if you don't have credit then how do you build history? That's why I think if you have a debit/credit card, a prepaid credit card, it will help you do that. I just haven't invested in the time to go look that stuff up.

You know the best way to get a good credit score is by borrowing money from the bank and pay it back. Yes, take a loan and pay it back. That's how you really credit strong.

When I was speaking to the lady at the credit bureau, she says to me ... if you want to buy a house or you want to establish credit in Canada, get a store credit card. They start you off at \$500. She said, all you spent on that card is \$100, and then you make sure you pay that. You don't go over that limit. You spend \$100 and keep doing that for the next three or four years, you build up your credit rating, and you can take that card and cut it up and throw it in the garbage. You don't have to use it again.

### **Managing without Credit Cards**

Participants have had to find ways of managing their financial and consumer needs without access to credit cards. Some have found alternative financial products and services, including debit cards, Interac payments, internet or phone banking and Pay

Pal, which provide many of the same functions as credit cards do. Others rely on friends and family who do have access to credit to take care of these needs on their behalf.

#### **BILL-PAYING AND USE OF OTHER FINANCIAL SERVICES**

Most participants have bank accounts with chartered banks, trust companies or credit unions. A few mentioned that “bank accounts” are available through companies such as MoneyMart, and those few who do not have bank accounts do make use of such companies for cashing cheques, and occasionally for “payday” loans.

Those who have bank accounts tend to have and use their debit cards, where it is possible to do so, to get the cashless convenience of a credit card. Bank accounts also give these participants access to other services which can be used as alternatives to credit card use in some circumstances, such as internet and telephone banking, overdraft protection

Most have a lease or utility bills such as electricity, heat or telephone in their own name. These participants tend to use debit cards, cheques, and internet or phone banking to pay their bills. However, some, especially those who live with others, pay their share of the bills in cash to the other person whose name is on the lease or the utility bills. Some live with a parent or spouse/partner who has a credit card as well as a bank account.

#### **SHOPPING ONLINE**

One of the situations frequently mentioned by participants as a problem for people without credit cards involves making online purchases. However, when asked if the shop online, many reported that they do, and listed several ways they have found of shopping online. Most of those who shop online said that they use Pay Pal or other forms of electronic money transfer, although this is not a fully satisfying alternative since not all online vendors are able to accept such payments. However, some noted that its use seems to be spreading and that more and more vendors are accepting this method of payment.

I think now, especially too with this new email money transfer, that’s what I see here, because a lot of things now you can just transfer the money. Where before you would use a credit card, now you can do email money transfer.

You can use Pay Pal. Pay online your bills and that’s it. You just need to register, and then you put some money from your bank account in the Pay Pal account.

I do grocery and things with the email money transfer. When I found out it was like, woo-hoo!

There's a show that I want to go to now and it actually has a link, if you do not have credit cards you can do an email money transfer. So, I guess now they're going to start doing that.

Other participants have found vendors who are willing to accept payment via bank transfers.

There's another way you can buy stuff online too. You have to give them your cheque number, your account number or something like that, and the cheque number, and they will send the thing to you and they're going into your account.

As with bill paying, some participants either use the credit cards of friends or family members, or ask their friends or family to order the items they want for them, and then pay their friends or family in cash or via bank transfer.

#### **ALTERNATIVES TO USING CREDIT CARDS**

For daily transactions, most participants who have bank accounts with financial institutions that offer debit cards use these as an alternative to credit cards wherever possible. There are some disadvantages, as debit cards are not as widely accepted as credit cards, but most agree that this is changing as more and more retailers recognize that many of their customers prefer using debit cards.

Some mention the possibility of using a pre-paid credit card. Both of these options are seen as having many of the advantages of credit cards without the disadvantages of high interest rates and exposure to debt accumulation.

If you've got a debit card, you have both sides of the coin covered. So, you don't even have to go to the bank. We're talking convenience. You go and buy \$100 worth of groceries, and you ask for \$300 back.

I have a debit card that I use a lot, but you can't use it everywhere. A credit card is more convenient.

One thing I noticed lately, with a lot of people, is they are actually getting prepaid credit cards. And I think the reason for that is because they don't have a bill coming in every month. So, there's the convenience of that. You just have money on the card as long as you're putting money on the card.

Capital One does that. You can send \$200, if you use that up on your credit card, that's it. You have to reload it. And, I think that is better, because then you are in control of how much money you want to spend. So, you could put \$500 and you go, look, I've got \$500.

Some participants rely on friends or family who are credit card holders when they want to buy something that would ordinarily only be available with a credit card, or when they need to make a large-ticket purchase.

I get other people to buy tickets for me if I'm going to buying something in advance.

For WWF, wrestling thing, I take my son, I had to ask a friend to pay for those tickets. Three of them were for a friend and him and me, and then I paid her.

My wife looks after it. She has the charge card. So, I know about going to Home Depot to buy a new roof for the house and spent \$2,700 and they take my signature. I just write 'Barb'.

One function of a credit card, that of serving as a short-term loan, is not something that a debit card or pre-paid credit card can provide. When such a circumstance arises, participants generally prefer to borrow money from family or friends, and some mentioned having overdraft protection which can serve as a short-term loan, depending on the amount required and the overdraft limit. Some mentioned using "pay day" loans if necessary in emergency situations or where they need a large cash advance for some reason. On the other hand, some are wary of "pay day" loans and try to avoid using them at all costs.

Yeah, I just ask my dad to forward the money into my account and I give it back later on. I wouldn't risk Payday loans or anything like that.

Money Mart. You have to have actually a pay stub.

Borrow from your friends. If your friend is willing to give it to you, that's the thing.

## Proposed Solutions

Most participants agree that some kind of solution is required to the problem of managing in today's world without access to credit cards. For some, the solution lies in changes to the criteria used to make decisions on who should be allowed to hold a credit card. They find it particularly distressing that people with a record of regular employment – even if it is at a succession of temporary or contract positions – are not qualified. These participants feel that the fact that they are always, or almost always working should count for more, even if their income is low and they have not had an opportunity to establish a credit rating.

They need to stop stereotyping, because I think what they're doing – because your income is not high and because you work in temp, and this and that, I think that's stereotyping. What they're doing is stereotyping a group of people and saying, because she's temping and because she works at Tim Horton and she's not making \$12 an hour, that's unfair because that's stereotyping.

I think you should review your policy because if it's based on income, which I don't know about., it's based on income, the economy and with everything going on, they should be understanding. It's such a race that they're judging to give a credit card. They should come down a bit.

Why can't they take into account more so if somebody's been responsibly, gainfully employed for like five years at the same place? Like score Brownie points in some kind of area like that.

I think they should lessen the penalty on people who do not have credit cards. The reason the credit card companies are denying most of them is because of the income.

A few think that much of the problem can be solved if there is more widespread adoption of alternatives to credit cards, such as debit cards, and services that allow payment directly from one's bank account over the Internet.

Well, I think they're starting to – like with the email money transfers, that's starting to change things around for me. So, I think that would help.

Some felt that making available credit cards with modest limits, and keeping these limits modest rather than increasing limits over time, would be an appropriate solution for some. These participants argued that if the credit card limit were more closely matched to the holder's income and overall ability to pay, then credit card providers would be better able to manage their risk and could therefore offer credit cards to more people.

I think that they should know that basically, okay, fine, if they're going to pick a credit card, give you something where they check how much you're making per month at your workplace. And, say give you a credit card for \$20 or \$50. You have a limit. And they don't up your limit until they know that you're making above your means. Then they'll up your credit card.

Starting people on a very small limit. Like, \$200, if you can't maintain \$200 or \$250, then maybe you have a right to tell somebody, you know what, you don't get any more credit.

If you have a credit card you can pay off something slowly, right. If you don't have a lot of money, you can pay it off, you know, like \$100 a month or something, right. So, I think you're building your credit rating. You're proving that you're willing to pay, right. So, the fact that they give you a credit card with a low limit, I think that would be fair, because it's not a great risk for the company.

Others advocate greater availability of pre-paid credit cards, or credit cards that are secured by an initial deposit. As with the previous suggestion, this idea also has the advantages of limiting the individual card-holder's use of a card to what they can afford, and at the same time limiting the credit card provider's exposure to risk, thus making it possible to make some form of credit available to more people.

And, yeah, the prepaid credit cards, you know what I mean? Where people could have access.

All you have to do is just pay – on Money Mart they have a thing called a Titanium. All you have to do is pay the \$20 and every time you're putting money on it, you just pay Money Mart two dollars to put money on it.

For those new immigrants that come to Canada and don't have credit history here, at least allow us to have, like a locked amount of money and then we can have a credit card.

## CONCLUSIONS

Use of credit has become an accepted way of life in Canada – most financial transactions are organised in such a way as to facilitate the use of credit cards, in some cases over the use of cash. Furthermore, key financial transactions are increasingly occurring online, where credit cards are still the major method of payment despite the growing availability of methods based on direct transfer of funds from a bank account, such as Pay Pal.

Those who are unable to access credit because of a lack of credit history are thus at a disadvantage as their ability to participate in the marketplace is hampered. Further, the inability to access credit carries with it a stigma in that it is assumed to indicate a lack of fiscal responsibility or a state of financial insufficiency.

Lack of access to credit in the current marketplace not only renders certain kinds of transactions difficult if not impossible, it eliminates the possibility of rapid access to short-term credit in cases of emergency or a temporary situation where need exceeds cash on hand. It also excludes the non-holder from associated benefits of credit card use, such as loyalty programs, insurance and warranties, and special discounts. Those without access to this form of credit are also denied one of the most common methods of establishing the kind of credit history necessary to achieve home ownership or to facilitate applications for loans for home improvement or start-up costs on small business ideas.

Many see the limitations faced by non-card holders as unfair, and have in some cases elevated access to credit as approaching the status of a right or even a necessity of life.

Some of the consequences of limited access to credit can be ameliorated by more widespread acceptance in the marketplace of alternatives to credit cards, such as debit cards and convenient methods of electronic transfer of funds. However, the other issues of reduced access to short-term credit, access to a means of building a good credit rating, and access to loyalty benefits can best be addressed by the promotion of new credit products providing prepaid credit cards and low-limit credit cards for use by people without a credit or employment history sufficient to qualify them for a standard card.



October 27, 2008

**Discussion Guide – FINAL**  
**Enviro-nics Research**  
**Attitudes towards Access to Credit**  
**PN 6393**  
**Public Interest Advocacy Centre**

**1.0 Introduction to Procedures (10 minutes)**

Welcome to the group. We want to hear your opinions. Not what you think other people think – but what you think!

Feel free to agree or disagree. Even if you are just one person among ten that takes a certain point of view, you could represent millions of Canadians who feel the same way as you do.

You don't have to direct all your comments to me; you can exchange ideas and arguments with each other too.

You are being taped and observed to help me write my report.

I may take some notes during the group to remind myself of things also.

The host/hostess will pay you your incentives at the end of the session.

Let's go around the table so that each of you can tell us your name and a little bit about yourself, such as what kind of work you do if you work outside the home and who lives with you in your house.

**2.0 Advantages and disadvantages of credit cards (15 minutes)**

As you know from the questions we asked you to recruit you to this session, we are going to be discussing the issue of credit cards and whether or not people can get access to them.

I want you to work together in pairs and spend a few minutes with your partner and create two lists – one on each side of the paper. On one side I want you to make a list of all the advantages or good things there are to having a credit card. On the other side I want you to list any disadvantages or possible negative things about credit cards.

Once everyone has done that I want each team to report back to the group about what they came up with.

What are the disadvantages or negatives of having a credit card?

**PROBE:** not being able to get one, the annual fees, high interest rates, risk of spending money you don't have, risk of it being lost or stolen, fraud, etc...

What are the advantages or positives of a credit card?

**PROBE:** Convenience of not carrying cash, access to credit, being able to make on-line purchases, being able to book hotels, tickets, rent DVDs etc..., use as ID etc..., ease of travel.

Has your view of credit cards changed over the years? Do they seem more or less necessary now than they might have been in the past?

### **3.0 Experiences with trying to get a credit card (20 minutes)**

I want to hear from each of you about your own experiences with credit cards. Have you ever applied for a credit card in Canada? What happened?

Why were you rejected?

Are some credit cards easier to get than others?

Are there certain kinds of people who tend to have the hardest time ever getting a credit card? Why?

**PROBE:** Poor people, people with no credit rating? New Canadians? Aboriginal people? People who have gone bankrupt?

In general, is it easy to get a credit card or are there obstacles that you face?

Do you think that it is fair that many people (such as yourselves) can't get credit cards, or is it unfair now that we live in a world where credit cards are almost becoming a necessity?

As far as you know, do you have a credit rating? Do you know what one is?

I'm curious what other financial services you do make use of.

Can you each tell me if you have things like a bank account (checking or savings)? Do you pay utility bills that are under your name? Do you have a lease under your name?

Have any of you ever had a credit card in another country? If so, do you have a credit rating in another country?

As far as you know, if you had a credit card in another country – does that help you get one in Canada?

#### **4.0 Desire for a credit card (15 minutes)**

Do you want to have access to credit card? Why?

In what ways, does not having one have an impact in your life?

Are there things you simply cannot do because of that?

How do you feel about that?

Do you think you are at an economic disadvantage as compared to a person who has a credit card? Why do you say that?

How would your life change if you were able to get a credit card? Do you think that having access to a credit card does make a difference in terms of quality of life of the user?

Thinking specifically about your financial circumstances, how do you think having a credit card would change things?

## 5.0 Alternatives to credit cards and on-line purchases (20 minutes)

Have any of you ever made purchases over the internet? What sorts of things have you bought?

Do you think that being able to buy on the internet could save you money? How so?

Are there cases where you end up paying more for some products and services because you don't have a credit card and cannot make online purchases?

What other advantages do you think you could have if you had a credit card to pay for online purchases?

What payment system have you used for online purchases? Is it possible to shop on-line without a credit card?

**PROBE:** Interac payment? Getting a friend to pay for you? Other methods...?

In general, if you don't have a credit card, what do you do if you need a small, short-term loan?

**PROBE:** borrow from friends? Payday loans? Loan sharks? Bank overdrafts?

## **6.0 Solutions (10 minutes)**

Now that we have discussed this whole issue of access to credit cards, I want to discuss what you think can be done about it?

Should there be new policies so that either it gets easier to get a credit card or so that people who don't have credit cards don't face some of the disadvantages we have discussed?

What should be done?

**Thanks for your participation!**



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### **Voluntary codes:**

*Canadian Code of Practice for Consumer Debit Card Services.*