It's the end of credit as we know it

Your first (legal) drink might not be the only reason to celebrate the big 21 anymore . . .

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While some students were beginning their summer travels in late May and starting to rack up hefty credit card balances, Congress was busy passing a bill to protect credit card users, which included special provisions for college-aged adults.

The Credit Card Responsibility and Disclosure Act was signed into law by President Barack Obama on May 22. The provisions pertaining to college students were hailed as extremely necessary by supporters of the bill, but some think the bill will restrict student's access to credit.

The most talked-about element of the bill is the provision that anyone under 21 will have to secure a co-signer to obtain a credit card unless they can demonstrate proof of an "independent means of repaying an obligation." This rule, along with most of the bill's other guidelines, will go into effect in late February 2010.

Supporters of the bill say this provision will reduce the number of students who fall prey to the predatory lending practices of credit card companies, which have resulted in students accumulating large debts.

"This regulation will help prevent students from getting into repayment plans that aren't the best for them," Jake Stillwell, spokesman for the United States Student Association, a student advocacy group based in Washington D.C., said. "[It] will enable students to have a second set of eyes look over credit card offers."

Boston University business policy and law professor James Post said the new laws should reduce the number of students that get into untenable financial situations because of credit cards.

"Young people have sometimes gotten into considerable debt, so this is a small step in protecting against that," Post said.

Others in the banking community believe the co-signer rule will limit the access college students have to credit, which will prevent them from developing a credit history.

"Credit cards are an excellent way for building a credit history," Peter Garuccio, a spokesman for the American Bankers Association, which represents banks of all sizes across the country, said. "If credit cards are no longer available that will have an impact on students' ability to establish a good credit history, which is needed when they want to get a car loan or buy a house."

Another expert said students who cannot find a co-signer and want to meet the "independent means" threshold to get a card will take a second job and spend less time focusing on their studies.

"Research has shown that the more college students work, the less likely they are to graduate on time, which is a major concern," Mark Calabria, the Director of Financial Regulation Studies at the Cato Institute, a libertarian think tank based in D.C., said.

Calabria also said that the co-signer rule will make it much harder for students from low-income backgrounds to get credit cards and will create wider chasms on campus between the rich and the poor.

"If you are from a well-off family you won't have a problem getting your parents to sign for a card," Calabria said. "But many students from working-class families will have parents who won't sign for a card. This will create a two-tiered system."

STUDENT REACTION

College of Arts and Sciences senior Karma Salem said the co-signer rule will prevent students from being able to fully act as adults and have financial independence.

"At 18, you are an adult and your parents are able to throw you out of the house," Salem said. "It doesn't make sense that you can't get a credit card without a co-signer."

Emma Walters, a CAS freshman, said she has many friends in college that are in credit card debt and is glad Congress is taking steps to prevent other young people, like her friends, from falling into financial difficulties. Walters said she doesn't plan on getting a credit card any time soon.

"I'm only 18 and don't have the means to pay for a credit card," she said.

CAS junior Daniel Ellis also has shunned credit cards and said he thinks Congress was wise to pass credit card restrictions for young people.

"A lot of 18 and 19-year-olds aren't very responsible," Ellis said. "If they can't pay for the card, they should at least have to prove their parents can."

INDEPENDENT MEANS

Both supporters and detractors of the bill expressed concern over the ambiguity of the "independent means" threshold in the law. There is no place in the law that sets specific guidelines for an income or debt to income ratio that would make someone under 21 eligible to obtain a credit card without a co-signer.

"The ambiguous terms seem ripe for credit card companies to exploit," Stillwell said. "The whole reason why the law was needed is that credit card companies are so good at finding their way into deals."

Calabria said without specificity in the regulations, credit card companies will be able to individually decide what constitutes sufficient income to pay back debts without needing a co-signer and the provision shows that Congress rushed passage of the bill without concern for setting concrete rules.

"Unless you have a clear set of guideposts you are going to have across the board lending practices," Calabria said.

The Federal Reserve is charged with determining what the new standards for sufficient income will be. Calabria said the Fed will decide on a debt to income ratio ranging anywhere from 20 to 100 percent.

Federal Reserve spokeswoman Susan Stawick said the Fed will not give any information about the "independent means" guidelines until they release them prior to the law going into effect.

A proper balance needs to be struck between tightening current regulations, while not preventing all students from needing a co-signer to get a credit card said Christine Lindstrom, Higher Education Program Director for U.S. PIRG, a federation of state public interest groups, which supported the bill.

"You don't want to block a student's access to credit, but you don't want to make the regulations insubstantial that they don't tighten up the standards," Lindstrom said.

NO MORE FREE PIZZA

A second provision of the new credit card bill that affects college students is that creditors are prevented from offering any free gifts, such as t-shirts or food, to entice students to sign up for a credit card on or near college campuses. The law also has a requirement that colleges and universities disclose any agreements or contracts they have with creditors who plan on marketing credit cards.

BU currently has no agreements with credit card companies for marketing credit cards and bans all credit card solicitations on campus, BU spokesman Colin Riley said. BU's policy was established over 10 years ago, according to Riley.

"Students who want a credit card can get one on their own without dealing with needless gimmicks or tschotkes," Riley said.

Stillwell said while the ban on gifts as an inducement to buy credit cards doesn't directly affect BU students, the regulation will protect thousands of students across the country from accumulating more debt.

"When faced with mounting debt a gift can entice students to get locked into pretty bad deals," he said.

Lindstrom said while the disclosure of relationships provision will lead to transparency in the often hidden relationships between colleges and creditors.

"It will be useful to have the [relationships] information so we can see if more action needs to be taken," Lindstrom said.

EDUCATION

In another effort to prevent students from signing up for credit cards with exorbitant rates and getting duped by marketers, Congress recommended that schools include credit card and debt education sessions as part of new students orientation.

Riley said consumer credit education has been part of BU's orientation programs for incoming students and their parents for many years. Riley thinks students should turn to their parents for credit advice before purchasing a credit card or if they are accumulating debt.

"Students should begin with their parents and then go to independent credit counselors if necessary," he said.

Riley said the new federal regulations will prevent some students from getting into credit card debt and suffering emotional stress as a result.

Riley also said that graduating students will benefit by entering the working world without credit card debt on top of other payments they will have to make.

"For people who are making the transition from young adulthood to adulthood and assuming financial obligations, it is a real challenge to balance many different bills they have — including loans and utilities," he said. "Some people manage that better than others, but there is no need to compound that with credit card debt."

Calabria of Cato said college students need to learn how to handle credit while in the supportive environment of college and not wait until after they graduate.

"You want people to make mistakes when they have resources there to back them up," he said.

Post said there are currently reasonable credit card offers available for students who want to start developing a credit history without facing extreme interest rates.

"By being aggressive and using internet resources, you can find a reasonable deal," Post said.