The Risk-Based Pricing Rules

Outlook Live Webinar – February 16, 2011

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Agenda

- Risk-Based Pricing Notices
- Credit Score Disclosures
- Account Review Notices
- Exceptions and Rules of Construction
- Enforcement

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Background

- Joint rulemaking between the Federal Reserve Board and Federal Trade Commission (FTC) implementing requirements of the Fair and Accurate Credit Transactions (FACT) Act
- Intended to complement adverse action notice requirements
- Became effective on January 1, 2011

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Risk-Based Pricing Rule

A person is required to provide a consumer with a risk-based pricing notice if the person:

- Uses a consumer report in connection with an extension of credit for personal, family, or household purposes, and
- Based on the report, extends credit to the consumer on material terms that are less favorable than the most favorable terms available to a substantial proportion of consumers

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Application of the Rule

- The rule applies to the person to whom the obligation is initially payable – the original creditor
- Even if the credit agreement is immediately assigned, the original creditor has the obligation to provide a notice to the consumer

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Two Paths to Compliance

- Provide risk-based pricing notices
  - Requires analysis
  - Does not require consumer-specific information
  - Only provide to some consumers

- Provide credit score disclosures
  - Does not require analysis
  - Requires a consumer's credit score and related information
  - Generally, provide to all consumers (with some exceptions)

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Risk-Based Pricing - Methods

Methods to determine which consumers must be provided with a risk-based pricing notice:

1. Direct Comparison
2. Credit Score Proxy
3. Tiered Pricing

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Definition of "Material Terms"

Generally, the Annual Percentage Rate (APR)

- For open-end credit, excludes promotional rate, penalty rate, or fixed rate HELOC option
- For credit cards, the purchase APR
  - If no purchase APR, then the APR that varies based on information in a consumer report and that has the most significant financial impact on consumers
- For credit for which there is no APR (e.g., utility or charge card)
  - The financial term that varies based on a consumer report and that has the most significant financial impact on consumers
  - Examples: a utility deposit or a charge card annual membership fee

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Definition of "Specific Type of Credit Product"

- One or more credit products with similar features that are designed for similar purposes
- Examples:
  - Student loans
  - Unsecured credit cards
  - Secured credit cards
  - New auto loans
  - Used auto loans
  - Fixed-rate mortgage loans
  - Variable-rate mortgage loans

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Direct Comparison Method

A creditor must:

- Make a direct comparison between all consumers for each specific type of credit product offered, and
- Give a risk-based pricing notice to those consumers that receive materially less favorable terms

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Credit Score Proxy Method

- Set cutoff credit score where 40% of consumers have a credit score above the cutoff and 60% have a credit score below the cutoff

- Risk-based pricing notices given to all consumers with credit scores below the cutoff

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Credit Score Proxy Method (Variation)

- If a creditor historically has given the best terms to more than 40% of consumers, creditor may deviate from the 40/60 cutoff and set its cutoff score based on its historical experience
  - Example: A creditor historically has given the best terms to 80% of its customers; 80% of its customers have a credit score of 720 or higher, and 20% have a credit score lower than 720. Creditor may set its credit score proxy at 720. Creditor must provide risk-based pricing notices to consumers whose credit score is less than 720.

- Creditor may only deviate from the 40/60 percentage if <u>more than</u> 40% of its customers receive the most favorable terms
  - This means no more than 60% of consumer may receive a notice.

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Tiered Pricing Method

- Provide risk-based pricing notices depending on the pricing tier in which the consumer is placed based on APR
  - If 4 or fewer tiers, creditor must give a notice to all consumers not in the top (lowest-priced) tier
  - If 5 or more tiers, creditor must give a notice to all consumers not in the top two tiers, plus any other tier that represents at least the top 30% but no more than the top 40% of the total number of tiers

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Special Rule for Credit Cards

- May use any of the other methods
- Or, may provide a risk-based pricing notice when:
  - A consumer applies for a credit card for which more than one APR is offered, and
  - The credit card issuer provides a card to the consumer with a rate that is greater than the lowest APR offered
- No notice required when:
  - A consumer applies for a card offered at a single rate
  - An issuer offers the lowest rate on an offer, even if there is a lower rate under a different offer

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Risk-Based Pricing Notice (H-1)

[Name of Entity Providing the Notice]
Your Credit Report[s] and the Price You Pay for Credit

What is a credit report?	A credit report is a record of your credit history. It includes information about whether you pay your bills on time and how much you owe to creditors.
How did we use your credit report[s]?	We used information from your credit report[s] to set the terms of the credit we are offering you, such as the [Annual Percentage Rate/down payment]. The terms offered to you may be less favorable than the terms offered to consumers who have better credit histories.
What if there are mistakes in your credit report[s]?	You have a right to dispute any inaccurate information in your credit report[s]. If you find mistakes on your credit report[s], contact **[insert name of CRA(s)]**, which [is/are] the [consumer reporting agency/consumer reporting agencies] from which we obtained your credit report[s]. It is a good idea to check your credit report[s] to make sure the information [it contains/they contain] is accurate.
How can you obtain a copy of your credit report[s]?	Under federal law, you have the right to obtain a copy of your credit report[s] without charge for 60 days after you receive this notice. To obtain your free report[s], contact **[insert name of CRA(s)]**: *By telephone:* Call toll-free: 1-877-xxx-xxxx *By mail:* Mail your written request to: **[Insert address]** *On the web:* Visit **[insert web site address]**
How can you get more information about credit reports?	For more information about credit reports and your rights under federal law, visit the Federal Reserve Board's web site at www.federalreserve.gov, or the Federal Trade Commission's web site at www.ftc.gov.

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Risk-Based Pricing Notice - Form

- Use of model form provides a safe harbor
- Clear and conspicuous
- Provided to the consumer in writing, electronically, or orally
  - No Electronic Signature in Global and National Commerce Act (E-SIGN) required
  - Different from credit score disclosure form requirements

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Risk-Based Pricing Notice - Timing

- For closed end credit, risk-based pricing notice must be given no earlier than when the approval is communicated to the consumer, but before consummation.
- For open end credit, risk-based pricing notice must be given no earlier than when the approval is communicated to the consumer, but before the first transaction is made.
- Special rules:
  - Auto Lending
  - Instant Credit

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Credit Score Disclosure

- Instead of determining which consumers require a risk-based pricing notice, credit score disclosures generally must be given to all consumers applying for credit
- In addition to model risk-based pricing notices, the agencies developed model credit score disclosures which may be used by creditors:
  - The model notices are available in the final rule, which can be found in the Federal Register
  - 75 Fed. Reg. 2724 (Jan. 15, 2010)

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Credit Score Disclosure

- Three model forms
  - Mortgages (H-3)
  - Non-mortgage (H-4)
  - Not credit score available (H-5)
- Use of these forms provides a safe harbor for the creditor

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Credit Score Disclosure - Form

- Clear and conspicuous
- Segregated from other information provided to the consumer
  - Except that disclosures required by FCRA section 609(g) may be provided on the mortgage credit score disclosures
- Provided in writing and in a form the consumer can keep
  - A credit score disclosure complying with the Electronic Signature in Global and National Commerce Act (E-SIGN) satisfies the “in writing” requirement

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Credit Score Disclosure - Timing

- A mortgage credit score disclosure must be provided at the same time as the disclosure required by section 609(g) of the FCRA
- A non-mortgage credit disclosure must be provided as soon as reasonably practicable after the credit score has been obtained

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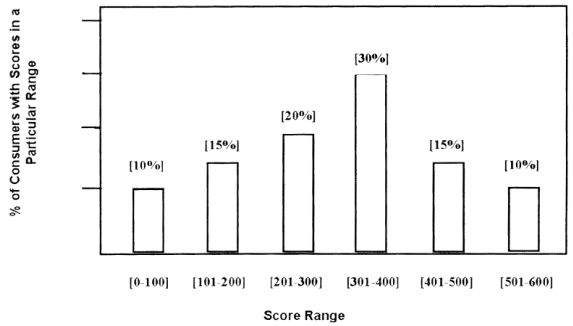
Credit Score Disclosure - Mortgage

H-3. Model form for credit score disclosure exception for loans secured by one to four units of residential real property

[Name of Entity Providing the Notice]
Your Credit Score and the Price You Pay for Credit

Your Credit Score	
Your credit score	**[Insert credit score]** Source: **[Insert source]** Date: **[Insert date score was created]**

Understanding Your Credit Score	
What you should know about credit scores	Your credit score is a number that reflects the information in your credit report. Your credit report is a record of your credit history. It includes information about whether you pay your bills on time and how much you owe to creditors. Your credit score can change, depending on how your credit history changes.
How we use your credit score	Your credit score can affect whether you can get a loan and how much you will have to pay for that loan.
The range of scores	Scores range from a low of **[Insert bottom number in the range]** to a high of **[Insert top number in the range]**. Generally, the higher your score, the more likely you are to be offered better credit terms.
How your score compares to the scores of other consumers	 **[or]** [Your credit score ranks higher than [X] percent of U.S. consumers.]

Understanding Your Credit Score (continued)	
Key factors that adversely affected your credit score	**[Insert first factor]** **[Insert second factor]** **[Insert third factor]** **[Insert fourth factor]** **[Insert fifth factor, if applicable]**

Checking Your Credit Report	
What if there are mistakes in your credit report?	You have a right to dispute any inaccurate information in your credit report. If you find mistakes on your credit report, contact the consumer reporting agency. It is a good idea to check your credit report to make sure the information it contains is accurate.
How can you obtain a copy of your credit report?	Under federal law, you have the right to obtain a free copy of your credit report from each of the nationwide consumer reporting agencies once a year. To order your free annual credit report— *By telephone:* Call toll-free: 1-877-322-8228 *On the web:* Visit www.annualcreditreport.com *By mail:* Mail your completed Annual Credit Report Request Form (which you can obtain from the Federal Trade Commission's web site at http://www.ftc.gov/ bcp/conline/include/requestformfinal.pdf) to: Annual Credit Report Request Service P.O. Box 105281 Atlanta, GA 30348-5281
How can you get more information?	For more information about credit reports and your rights under federal law, visit the Federal Reserve Board's web site at www.federalreserve.gov, or the Federal Trade Commission's web site at www.ftc.gov.

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Credit Score Disclosure – Mortgage (cont.)

Notice to the Home Loan Applicant

In connection with your application for a home loan, the lender must disclose to you the score that a consumer reporting agency distributed to users and the lender used in connection with your home loan, and the key factors affecting your credit scores.

The credit score is a computer generated summary calculated at the time of the request and based on information that a consumer reporting agency or lender has on file. The scores are based on data about your credit history and payment patterns. Credit scores are important because they are used to assist the lender in determining whether you will obtain a loan. They may also be used to determine what interest rate you may be offered on the mortgage. Credit scores can change over time, depending on your conduct, how your credit history and payment patterns change, and how credit scoring technologies change.

Because the score is based on information in your credit history, it is very important that you review the credit-related information that is being furnished to make sure it is accurate. Credit records may vary from one company to another.

If you have questions about your credit score or the credit information that is furnished to you, contact the consumer reporting agency at the address and telephone number provided with this notice, or contact the lender, if the lender developed or generated the credit score. The consumer reporting agency plays no part in the decision to take any action on the loan application and is unable to provide you with specific reasons for the decision on a loan application.

If you have questions concerning the terms of the loan, contact the lender.

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Mortgage – Relationship to 609(g)

- Appropriate use of model form H-3 intended to be compliant with the requirements of FCRA section 609(g), which requires disclosure of:
  - Credit score
  - Other information about the credit score

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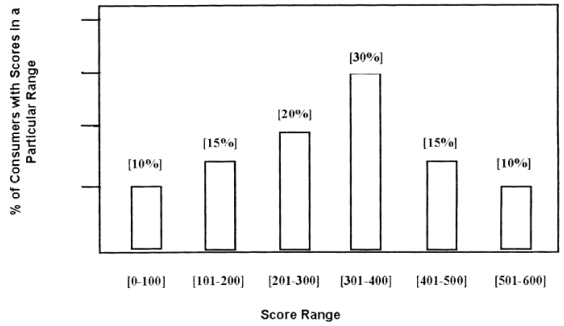
Credit Score Disclosure – Non-Mortgage

H-4. Model form for credit score disclosure exception for loans not secured by residential real property

[Name of Entity Providing the Notice]
Your Credit Score and the Price You Pay for Credit

Your Credit Score	
Your credit score	**[Insert credit score]** Source: **[Insert source]** Date: **[Insert date score was created]**

Understanding Your Credit Score	
What you should know about credit scores	Your credit score is a number that reflects the information in your credit report. Your credit report is a record of your credit history. It includes information about whether you pay your bills on time and how much you owe to creditors. Your credit score can change, depending on how your credit history changes.
How we use your credit score	Your credit score can affect whether you can get a loan and how much you will have to pay for that loan.
The range of scores	Scores range from a low of **[Insert bottom number in the range]** to a high of **[Insert top number in the range]**. Generally, the higher your score, the more likely you are to be offered better credit terms.
How your score compares to the scores of other consumers	 **[or]** [Your credit score ranks higher than [X] percent of U.S. consumers.]

Checking Your Credit Report	
What if there are mistakes in your credit report?	You have a right to dispute any inaccurate information in your credit report. If you find mistakes on your credit report, contact the consumer reporting agency. It is a good idea to check your credit report to make sure the information it contains is accurate.
How can you obtain a copy of your credit report?	Under federal law, you have the right to obtain a free copy of your credit report from each of the nationwide consumer reporting agencies once a year. To order your free annual credit report— *By telephone:* Call toll-free: 1-877-322-8228 *On the web:* Visit www.annualcreditreport.com *By mail:* Mail your completed Annual Credit Report Request Form (which you can obtain from the Federal Trade Commission's web site at http://www.ftc.gov/ bcp/conline/include/requestformfinal.pdf) to: Annual Credit Report Request Service P.O. Box 105281 Atlanta, GA 30348-5281
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Credit Score Disclosure - Content

Both disclosures (H-3 and H-4):

- Explain that credit scores are affected by a consumer's credit history
- Can affect the availability and cost of credit
- Provide the consumer's credit score
  - Compare score with a distribution of credit scores among consumers
    - In a graphical form, or
    - Through a clear and readily understandable statement
  - Inform the consumer how his or her credit score compares with the scores of other consumers

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Credit Score Disclosure - Content

Disclosures include:

- A statement encouraging the consumer to verify the accuracy of the information contained in the consumer report
- A statement of the consumer's right to dispute any inaccurate information in the report
- Information on how the consumer can obtain a consumer report

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Credit Score Disclosure – No Credit Score Available

H-5. Model form for loans where credit score is not available

[Name of Entity Providing the Notice]
Credit Scores and the Price You Pay for Credit

Your Credit Score	
Your credit score	Your credit score is not available from **[Insert name of CRA]**, which is a consumer reporting agency, because they may not have enough information about your credit history to calculate a score.
What you should know about credit scores	A credit score is a number that reflects the information in a credit report. A credit report is a record of your credit history. It includes information about whether you pay your bills on time and how much you owe to creditors. A credit score can change, depending on how a consumer's credit history changes.
Why credit scores are important	Credit scores are important because consumers who have higher credit scores generally will get more favorable credit terms. Not having a credit score can affect whether you can get a loan and how much you will have to pay for that loan.
Checking Your Credit Report	
What if there are mistakes in your credit report?	You have a right to dispute any inaccurate information in your credit report. If you find mistakes on your credit report, contact the consumer reporting agency. It is a good idea to check your credit report to make sure the information it contains is accurate.
How can you obtain a copy of your credit report?	Under federal law, you have the right to obtain a free copy of your credit report from each of the nationwide consumer reporting agencies once a year. To order your free annual credit report— *By telephone:* Call toll-free: 1-877-322-8228 *On the web:* Visit www.annualcreditreport.com *By mail:* Mail your completed Annual Credit Report Request Form (which you can obtain from the Federal Trade Commission's web site at http://www.ftc.gov/bcp/conline/include/requestformfinal.pdf) to: Annual Credit Report Request Service P.O. Box 105281 Atlanta, GA 30348-5281
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Credit Score Disclosure – No Credit Score Available

- Model notice H-5 is to be used when:
  - Credit score is not available form the consumer reporting agency from which the creditor regularly obtains credit scores, and
  - Creditor does not obtain a score on the consumer from another consumer reporting agency
    - There is no obligation for the creditor to pull a score from another consumer reporting agency, but must disclose a score if one is obtained
- The disclosure states that a credit score was unavailable, which may indicate a lack of credit history
- Other disclosures describe what credit scores are, why they are important and how to obtain a copy of the consumer's credit report

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Multiple Credit Scores

- If the creditor obtains two or more credit scores for a consumer and uses one of those scores as the basis for setting material terms, that score must be disclosed.
- If instead the creditor uses multiple scores to set the material terms, the creditor may disclose one of the scores obtained or may disclose more than one score.
- Regardless of which method the creditor uses, the information specified in 222.74(d)(1)(ii) or (e)(1)(ii), as applicable, must be provided for each credit score disclosed.

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Account Review Notice

- IF a creditor does an account review of an existing customer and, based in whole or part on a consumer report, increases the account's APR,
- THEN the creditor must provide the consumer with an account review notice
  - This notice must be provided regardless of whether the creditor typically provides risk-based pricing notices or credit score disclosures
  - Typically occurs in the credit card context, but may occur in other types of credit contexts

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Account Review Notice (H-2)

[Name of Entity Providing the Notice]
Your Credit Report[s] and the Pricing of Your Account

What is a credit report?	A credit report is a record of your credit history. It includes information about whether you pay your bills on time and how much you owe to creditors.
How did we use your credit report[s]?	We have used information from your credit report[s] to review the terms of your account with us. Based on our review of your credit report[s], we have increased the annual percentage rate on your account.
What if there are mistakes in your credit report[s]?	You have a right to dispute any inaccurate information in your credit report[s]. If you find mistakes on your credit report[s], contact **[insert name of CRA(s)]**, which [is/are] [a consumer reporting agency/consumer reporting agencies] from which we obtained your credit report[s]. It is a good idea to check your credit report[s] to make sure the information [it contains/they contain] is accurate.
How can you obtain a copy of your credit report[s]?	Under federal law, you have the right to obtain a copy of your credit report[s] without charge for 60 days after you receive this notice. To obtain your free report[s], contact **[insert name of CRA(s)]**: *By telephone:* Call toll-free: 1-877-xxx-xxxx *By mail:* Mail your written request to: **[Insert address]** *On the web:* Visit **[insert web site address]**
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Account Review Notice – Delivery Requirements

- Form
  - Use of model form provides a safe harbor
  - Clear and conspicuous
  - Provided to the consumer in writing, electronically, or orally
    - No E-SIGN required
- Timing
  - Must be provided at the time the decision to increase the APR is communicated to the consumer

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Multiple Consumers

- In the case of transactions involving two or more consumers, a creditor must provide a notice to each consumer to satisfy the requirements of 222.72(a) or (c)
  - If the consumers have the same address, a creditor may satisfy the requirements by providing a single risk-based pricing notice addressed to both consumers

- Credit score disclosures have different requirements. When a transaction involves two or more consumers, the creditor must provide a separate disclosure to each consumer to satisfy the exceptions in 222.74(d), (e), or (f), regardless of whether the consumers have the same address.

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One Notice Per Transaction

- A consumer is entitled to only one notice per extension of credit, unless the creditor must provide an account review notice to the consumer

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Exceptions

- A consumer applies for specific material terms and is granted those terms, unless those terms were specified by the creditor using a consumer report after the consumer applied for or requested credit and after the creditor obtained the consumer report.
- A creditor obtains a consumer report that is a prescreened credit list and uses that report to make a "firm offer of credit."
  - However, if a consumer receives a solicitation, applies for credit, and a risk-based pricing notice is triggered under Section 222.72, the creditor must provide the notice.
- A creditor provides an adverse action notice to the consumer under section 615(a) of the FCRA.

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Enforcement

- There is no private right of action for violations of the risk-based pricing rules
- The rule is subject to regulatory enforcement actions

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Questions?

- Don't forget – www.consumercomplianceoutlook.org

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