

***Consumer Protection Update on Credit
Reports and Scores, the CARD Act,
Overdraft Rules, and the Mortgage
Forgiveness Debt Relief Act of 2007***

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Understanding and Improving Credit Scores

Your Credit Score

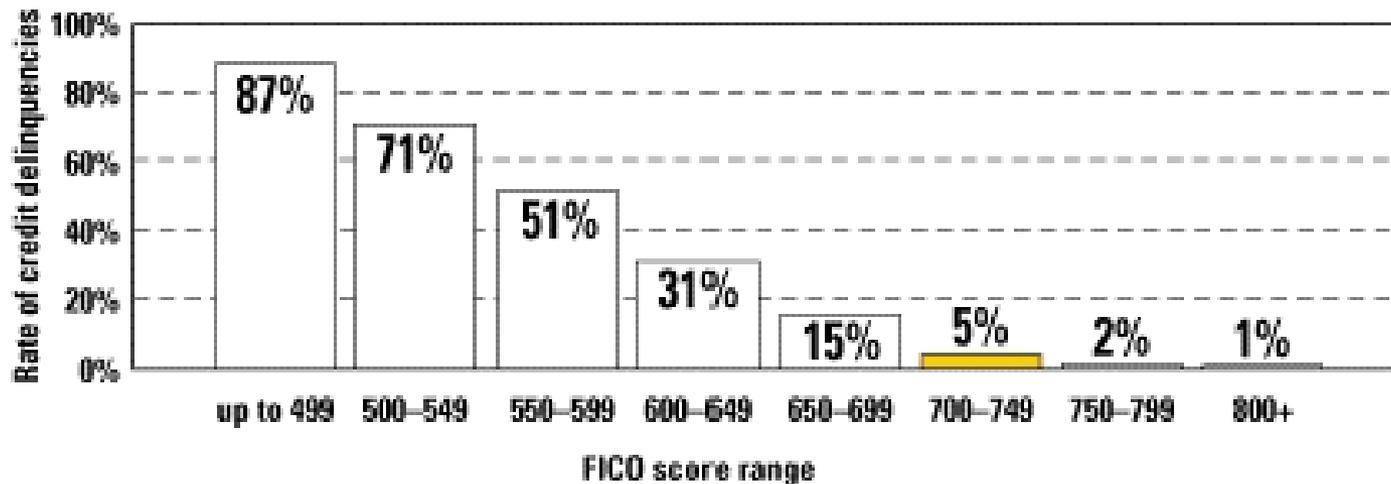
- Fair Isaac Corporation (FICO) pioneered credit scoring in 1989. FICO scores most commonly used by lenders. Scores range from 300-850
- Credit bureaus (Experian, Equifax and TransUnion) collect information about your credit history from your creditors and public records (bankruptcy, judgments, etc)
- Credit score predict risk of default in 2 years
- High credit score indicates low default risk
- Other companies offer credit scores, including Vantage score. *Vantage score based on range of 501-990*

What You Don't Know Can Hurt You!

- When you apply for credit, your credit report and score help determine if you're approved for credit and the interest rate and terms/conditions of your loan
- Your credit report is also used by many insurance companies to compute insurance score, which affects your premiums
- Many employers and landlords use credit reports to screen applicants

Credit Scores & Delinquencies

Delinquency rates by FICO score



Ranking of FICO Credit Scores

760-850	EXCELLENT
700-759	VERY GOOD
723	MEDIAN FICO SCORE
660-699	GOOD
687	AVERAGE FICO SCORE
620-659	NOT GOOD
580-619	POOR
500-579	VERY POOR

Credit Scores and Loan Rates

FICO® score	APR [?]	Monthly payment
760-850	4.663%	\$1,549
700-759	4.883%	\$1,589
680-699	5.059%	\$1,621
660-679	5.272%	\$1,661
640-659	5.699%	\$1,741
620-639	6.241%	\$1,845

Location: Pennsylvania Loan amount: \$300,000

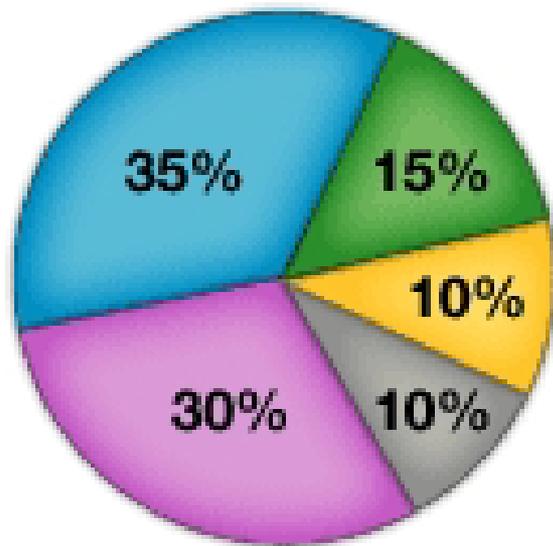
Source: Informa Research Services

Interest rates accurate as of February 22, 2010.

The difference between the monthly loan payment for the highest credit score (\$1,549) and the lowest (\$1,845) = \$296 month.

That's a difference of \$106,560 over the life of the 30 year loan!

Factors Affecting FICO Score



- Payment history
- Amounts owed
- Length of credit history
- New credit
- Types of credit used

Payment History: 35% of Your Score

- Number and severity of delinquencies
- Number of accounts paid as agreed
- Adverse public records (bankruptcy, judgments, suits, liens, wage attachments, etc.), collection items, and/or delinquency (past due items)
- Amount past due on delinquent accounts or collection items
- How recent past due items (delinquency), adverse public records (if any), or collection items (if any)

Amounts Owed: 30% of Your Score

- Credit utilization: proportion of balances relative to total credit limits on certain types of revolving accounts
- The amount owed on all accounts, and on different types of accounts
- Number of accounts with balances
- Proportion of installment loan amounts still owing (proportion of balance to original loan amount on certain types of installment loans)

Types of Credit Used: 10% of Your Score

- Types of credit accounts: the mixture of revolving credit (e.g., credit card) and installment loan (e.g., auto loan or mortgage)

Length of Credit History: 15% of Your Score

- Time since account opened
- Time since accounts opened by account type
- Time since account activity

New Credit: 10% of Your Score

- **Number of recently opened accounts and inquiries**
- **Time since last credit inquiry**
- **Re-establishment of positive credit history following past payment problems**
- **How long since you opened a new account**

How Your Credit Report Can Be Used (§604 of Fair Credit Reporting Act)

- Credit applications
- Employment applications
- Insurance applications
- Leasing applications

Negative Information in Your Credit Report under §605 of Fair Credit Reporting Act

- Bankruptcy : 10 years
- Civil suits, judgments and arrests from date of entry: 7 years or until statute of limitations expires (whichever is longer)
- Tax lien: 7 years from date of *payment*
- Late payments, collection, charged off accounts and any other adverse information: 7 years
- Hard Credit Inquiry: 2 years

Tips to Increase Your Credit Score

- Review credit report for inaccuracies and file a dispute if you find an error
- Pay bills on time!
- Keep credit card balances low relative to credit limits (30% or lower is recommended; less than 10% ideal)
- Pay off debt rather than moving it around
- Open new credit accounts only as needed; *new accounts decrease average age of accounts*
- Avoid closing credit card accounts
- Apply for all installment loans (mortgages, car loans, etc) within 30 day period (count only as 1 inquiry with FICO)

Obtaining Credit Reports and Scores

- Free Reports: Experian, Equifax, TransUnion; score not included
www.annualcreditreport.com 877-FACT-ACT (877-322-8228)

Free Credit Scores

- Credit Karma: <http://www.creditkarma.com> (TransUnion score 850 scale)
- Quizzle: <https://www.quizzle.com/> (Experian credit report/score 850 scale)

FICO Scores (fee required)

- FICO score for both TransUnion and Equifax credit bureau data:
<https://www.myfico.com/Store/BureauSelection.aspx>
- Transunion FICO Score: <https://www.transunioncs.com> (\$14.95)
- Equifax FICO Score (the score power option \$15.95):
<http://www.equifax.com/fico-credit-score/>
- Experian: FICO score not available as of 2/14/09

***New Consumer Protections
under the Credit Card
Accountability Responsibility
and Disclosure Act of 2009***

Implemented in 3 Phases

- August 20, 2009 (45 day change in terms notice, statements mailed 21 day before due date)
- February 22, 2010 (most provisions)
- August 22, 2010 (penalties proportionate to violation, mandatory account review for default rates, gift card rules)

Prevents Unfair Increases in Interest Rates and Changes in Account Terms

- *Prohibits increases in APR or fees during first year account is opened or on outstanding balances, with limited exceptions: 1) 60 day late 2) workout 3) temporary rate 4) variable rate*
- Issuers can raise rates for *future* transactions (except 1st year) with 45 day notice
- *Issuer who increases interest rate must periodically review and decrease rate if indicated by the review (8/22/10)*
- Promotional rates must generally last at least 6 months.

Enhanced Disclosure of Card Terms

- Issuers must provide cardholders with 45 days notice for changes to interest rate, fees, and other “significant changes” and the right to opt-out (but no opt-out if 60 days late)(8/20/09)
- Issuers must print minimum payment warnings on billing statements based on actual balance
- Issuers must disclose payment due date and penalty for late payment prominently on billing statements
- Issuers cannot use term “fixed rate” unless the APR or interest rate will not vary for any reason over the period specified

Restricts Certain Fees and Interest Charges

- Issuers cannot impose fees to make payment except for live services to make expedited payments
- Issuers cannot impose over the limit fees unless cardholder opts-in and even then fees are restricted
- Penalty fees must be proportional to violation (8/22/10)
- Sub-prime card protections: fees during 1st year cannot exceed 25% of credit limit
- Issuers cannot use double-cycle billing method
- When grace periods are offered, they must extend to partial payments if cardholder meets requirements for grace period.

Fairness in Timing and Application of Card Payments

- Payment allocation: payments in excess of minimum applied to card balance with the highest interest rate
- Credit card statements must be mailed 21 days before due date (currently 14 days) (8/20/09)

Responsible Lending Requirement

- Issuers must evaluate repayment ability when issuing credit cards or increasing credit limits

Safeguards for Credit Cards for Young People

- For consumers under 21, issuer must obtain signature of adult who is liable for debt or prove applicant can repay credit
- Limits prescreened offers of credit to young consumers
- Prohibits issuers from using inducement on-campus to market cards to students, and increases transparency of affinity arrangements (“Penn State Visa”)

Gift Card Protections (8/22/10)

- Requires certain gift cards to have at least a five-year life span
- Eliminates practice of declining values and hidden fees for gift cards not used within a reasonable period of time

New Overdraft Rules under Regulations DD and E

Regulation DD: Enhanced Overdraft Disclosures on Periodic Statements and for Balance Inquiries

Aggregate Fee Disclosures on Periodic Statements

- Depository institutions must disclose on periodic statements aggregate costs of the overdraft service for the statement period and the calendar year-to-date.

	Total For This Period	Total Year-to-Date
Total Overdraft Fees	\$60.00	\$150.00
Total Returned Item Fees	\$0.00	\$30.00

Balance Inquiry Disclosures

- Institutions must disclose balance that does not include amounts the institution may provide to cover overdrafts.
 - Applies to balance inquiries made through any automated system, such as an ATM.
 - Amounts from overdraft lines of credit and linked accounts also must be excluded.
- Second balance that includes available overdraft funds may be provided with prominent statement that balance includes those amounts (and if applicable, that those amounts are not available for all transactions).

Regulation E: No Overdraft Fee Unless Consumer Opts in to Overdraft Protection

- Four requirements for opt-in:
 1. Provide opt-in notice, segregated from other information
 2. Provide reasonable opportunity to opt in
 3. Obtain consumer's affirmative consent
 4. Provide written confirmation to the consumer
- Consumer has ongoing right to consent and revoke consent

Exceptions

- Rule does not apply to checks, ACH, or recurring debit card transactions (e.g. auto-pay monthly gym membership from checking).
- Consumer testing shows consumers want checks and other important bills paid.
- Banks can still offer an opt-in or opt-out for those transactions.
- Institutions must have systems to identify whether or not a debit card transaction is recurring, but once they do, they may rely on merchant coding.

Conditioning the Opt-In

- Financial institutions are prohibited from requiring consumers to opt into the overdraft service for ATM and one-time debit card transactions in order to have checks, ACH and other types of transactions paid.
- Financial institutions are also prohibited from declining to pay checks and other transactions just because a consumer has not opted in.

Variation of Account Terms

- Financial institutions must provide consumers who do not opt in with the same account terms, conditions, and features as provided to consumers who do opt in.

Exceptions to Notice and Opt-In Requirements

- Institutions that have a policy of declining transactions when there is a reasonable belief consumer has insufficient funds are exempt from notice and opt-in requirements.
- But this is not an exception to prohibition on charging fees for ATM and one-time debit card overdrafts
- If institutions that have a policy of not paying overdrafts want to impose overdraft fees when an overdraft slips through system (e.g. because of signature debit delay), they must comply with opt-in requirement

Effective Dates

- **New customers:** For accounts opened on or after July 1, 2010, notices must be provided and opt-in obtained before overdraft fees may be assessed.
- **Existing customers:** For any consumer who has not opted in by August 15, 2010, institution must stop assessing overdraft fees.

The Mortgage Forgiveness Debt Relief Act of 2007

Debt Forgiveness

- IRS treats debt forgiveness as taxable income unless exception applies
- When lenders “forgives” all or part of a debt, they must file a 1099-c with IRS and copy borrower

CORRECTED (if checked)

CREDITOR'S name, street address, city, state, and ZIP code <i>Goodold Bank 54 Happy Street Anytown, DC 20002</i>		OMB No. 1545-1424 2008 Form 1099-C		Cancellation of Debt
CREDITOR'S federal identification number <i>10-6543210</i>	DEBTOR'S identification number <i>123-00-6789</i>	1 Date canceled <i>8-31-2008</i>	2 Amount of debt canceled \$ 40,000.00	
DEBTOR'S name <i>Nancy Oak</i>		3 Interest if included in box 2 \$	4	Copy B For Debtor This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if taxable income results from this transaction and the IRS determines that it has not been reported.
Street address (including apt. no.) <i>360 Degree Circle</i>		5 Debt description <i>Home mortgage loan</i>		
City, state, and ZIP code <i>Anyplace, DC 20000</i>				
Account number (see instructions)		6 Bankruptcy (if checked) <input type="checkbox"/>	7 Fair market value of property \$	

Form **1099-C** (keep for your records) Department of the Treasury - Internal Revenue Service

Mortgage Forgiveness Exception

- The Mortgage Forgiveness Debt Relief Act creates an exception to treating debt forgiveness as taxable income when borrower obtains debt cancellation on mortgage debt used to buy, build or substantially improve principal residence, or to refinance debt incurred for those purposes
- *Second homes, vacation property, and rentals don't qualify*
- Eligible period: calendar years 2007 through 2012
- The maximum eligible amount is \$2 million for married couple and \$1 million if married filing separately
- For refinance that involved both refinancing of purchase and cash-out, only refinancing is eligible for tax relief.

Cash-out Example

- If only part of the loan forgiven is “qualified indebtedness,” income exclusion applies to amount of discharged debt that exceeds nonqualified indebtedness.
- Example: consumer with \$300,000 mortgage on principal residence, of which \$60,000 is a cash-out refinance. If lender “forgives” \$100,000 of loan in foreclosure (or loan modification or short sale), only \$40,000 (\$100,000 discharged debt — \$60,000 refi cash-out) qualifies for exclusion from income. Borrower would have to pay tax on \$40,000 unless another exception applied (e.g., insolvency or bankruptcy)

Other Ways to Exclude Loan Forgiveness from Income under §108 of Tax Code

- Bankruptcy
- Insolvency— but exempt assets (e.g., pension) are used to calculate insolvency
- Nonrecourse Loan
- IRS Pub. 4681 provides details on these exceptions and include insolvency worksheets <http://www.irs.gov/pub/irs-pdf/p4681.pdf>

IRS Form 982

- Borrower *must* file IRS form 982 (Reduction of Tax Attributes Due to Discharge of Indebtedness) to exclude amount of debt forgiveness from income
- For Mortgage Forgiveness Debt Relief Act, see below

Form **982**
(Rev. March 2009)
Department of the Treasury
Internal Revenue Service

Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)

OMB No. 1545-0046
Attachment Sequence No. **94**

▶ Attach this form to your income tax return.

Name shown on return _____ Identifying number _____

Part I General Information (see instructions)

1 Amount excluded is due to (check applicable box(es)):

a Discharge of indebtedness in a title 11 case	<input type="checkbox"/>
b Discharge of indebtedness to the extent insolvent (not in a title 11 case)	<input type="checkbox"/>
c Discharge of qualified farm indebtedness	<input type="checkbox"/>
d Discharge of qualified real property business indebtedness	<input type="checkbox"/>
e Discharge of qualified principal residence indebtedness	<input checked="" type="checkbox"/>
f Discharge of certain indebtedness of a qualified individual because of Midwestern disasters	<input type="checkbox"/>

2 Total amount of discharged indebtedness excluded from gross income. **2**

3 Do you elect to treat all real property described in section 1221(a)(1), relating to property held for sale to customers in the ordinary course of a trade or business, as if it were depreciable property? Yes No

Part II Reduction of Tax Attributes. You must attach a description of any transactions resulting in the reduction in

Check Box 1e for mortgage forgiveness

insert amount of forgiveness on line 2

IRS Form 982 (cont.)

For insolvency, check line 1b and amount on line 2

Form 982 (Rev. March 2009) Department of the Treasury Internal Revenue Service	Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment) ▶ Attach this form to your income tax return.	OMB No. 1545-0046 Attachment Sequence No. 94
Name shown on return	Identifying number	
Part I General Information (see instructions)		
1 Amount excluded is due to (check applicable box(es)):		
a Discharge of indebtedness in a title 11 case	<input type="checkbox"/>	
b Discharge of indebtedness to the extent insolvent (not in a title 11 case)	<input checked="" type="checkbox"/>	
c Discharge of qualified farm indebtedness	<input type="checkbox"/>	
d Discharge of qualified real property business indebtedness	<input type="checkbox"/>	
e Discharge of qualified principal residence indebtedness	<input type="checkbox"/>	
f Discharge of certain indebtedness of a qualified individual because of Midwestern disasters	<input type="checkbox"/>	
2 Total amount of discharged indebtedness excluded from gross income	2	\$50,000
3 Do you elect to treat all real property described in section 1221(a)(1), relating to property held for sale to customers in the ordinary course of a trade or business, as if it were depreciable property?	<input type="checkbox"/> Yes <input type="checkbox"/> No	
Part II Reduction of Tax Attributes. You must attach a description of any transactions resulting in the reduction in basis under section 1017. See Regulations section 1.1017-1 for basis reduction ordering rules, and, if applicable,		

Reduction in Basis in Property

- If a homeowner takes advantage of discharge of qualified principal residence indebtedness and still owns the home, he must reduce his basis in the property by the amount of the debt forgiven
- Fill out line 10b of Form 982, Part II in addition to 1e and 2 (see next slide)
- The effect of this to is to defer the tax on the cancellation of debt until the homeowner sells the house
- *Although homeowner's basis in property drops, meaning a larger capital gain when the property is sold, the IRS allows homeowners to exclude from tax \$250,000 in capital gains on the sale of a principal residence (\$500,000 for married couples)*

Form 982 Reduction in Basis of Principal Residence

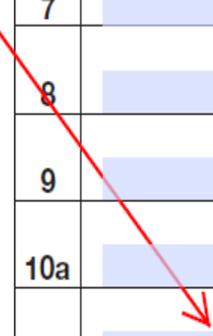
customers in the ordinary course of a trade or business, as if it were depreciable property? Yes No

Part II Reduction of Tax Attributes. You must attach a description of any transactions resulting in the reduction in basis under section 1017. See Regulations section 1.1017-1 for basis reduction ordering rules, and, if applicable, required partnership consent statements. (For additional information, see the instructions for Part II.)

Enter amount excluded from gross income:

4	For a discharge of qualified real property business indebtedness, applied to reduce the basis of depreciable real property	4	
5	That you elect under section 108(b)(5) to apply first to reduce the basis (under section 1017) of depreciable property.	5	
6	Applied to reduce any net operating loss that occurred in the tax year of the discharge or carried over to the tax year of the discharge	6	
7	Applied to reduce any general business credit carryover to or from the tax year of the discharge	7	
8	Applied to reduce any minimum tax credit as of the beginning of the tax year immediately after the tax year of the discharge	8	
9	Applied to reduce any net capital loss for the tax year of the discharge including any capital loss carryovers to the tax year of the discharge	9	
10a	Applied to reduce the basis of nondepreciable and depreciable property if not reduced on line 5. <i>DO NOT use in the case of discharge of qualified farm indebtedness.</i>	10a	
10b	Applied to reduce the basis of your principal residence. Enter amount here ONLY if line 1e is checked	10b	\$50,000

reduce basis of principal residence by amount of forgiveness



Consult IRS Pub 4681 for further details



Department
of the
Treasury

Internal
Revenue
Service

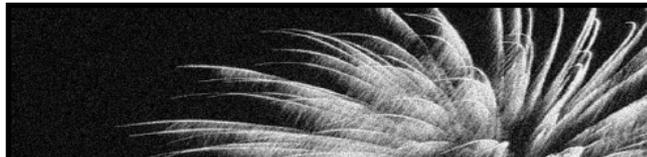
Publication 4681

Cat. No. 51508F

Canceled Debts, Foreclosures, Repossessions, and Abandonments

(for Individuals)

For use in preparing
2008 Returns



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Consequences for Not Filing IRS Form 982

- IRS can reconcile 1099-C with borrower's tax return and flag return for unreported income
- IRS can file tax lien if borrower ignores IRS notices
- *Tax liens remain on credit report for 7 years after lien is satisfied*
- But remember: taxpayer can always amend return
- *Borrowers should consult tax professionals for advice on debt forgiveness and adjusted basis in property*

