

## Federal Reserve Board and the Federal Trade Commission Propose Changes to Risk-Based Pricing and Adverse Action Notices

By Robert Birnbaum and Robert Morgan

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Section 1100F of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Pub. L. No. 111-203, 124 Stat. 1376) amended sections 615(a) and (h) of the Fair Credit Reporting Act (FCRA) (15 U.S.C. §1681m). The provision was intended to create an obligation on those persons using credit scores to provide notice to consumers adversely affected by those scores in adverse action and risk-based pricing notices required by the FCRA. Section 1100F added a requirement that consumers are to be notified of the numerical scores and how those scores adversely impacted the credit decision. The amendment did not change existing FCRA obligations to provide consumers with the reasons why credit decisions were negatively impacted by information in consumer credit reports.

On March 1st, the Federal Reserve Board and the Federal Trade Commission (the Agencies) proposed regulations to implement the provisions of Section 1100F, including proposed changes to both Regulation V (Risk-Based Pricing) and Regulation B (Equal Credit Opportunity). The proposed changes, if promulgated, will require changes to risk-based pricing and adverse action notices to incorporate numerical credit scores as well as other mandated disclosures.

### Risk-based pricing notices under FCRA

*Existing Requirements.* The Final Rule implementing the provisions of the Fair and Accurate Credit Transactions Act of 2003 (FACTA), which amended the FCRA, was published on Jan. 10, 2010 (75 Fed. Reg. 2724). Pursuant to existing provisions of the FCRA, a user of a consumer report generally must provide a risk-based pricing notice to a consumer when the user has used a consumer report and has provided credit on terms that are materially less favorable than the most favorable terms available to a substantial proportion of consumers. Specifically, the risk-based pricing notice must include the following information:

1. A statement that the user of the consumer report has set the credit terms offered based on information in the consumer report;
2. A statement that those terms may be less favorable than credit terms offered to consumers with better credit histories.

For account review notices (i.e., notices sent after an existing account has been reviewed to determine if a different APR should be provided), the following information must be included:

1. A statement that the user of the consumer report has conducted a review of the account based in whole or in part on information from a consumer report;
2. A statement that as a result of such review the APR has been increased.

The notices must also provide certain information about the credit bureau that provided the information (e.g., name, address, toll-free telephone number) and that the consumer has the right to obtain a free copy of the consumer report. Consumers are to be encouraged in such notices to obtain copies of the reports in order to verify the accuracy of the information contained in such reports.

*Proposed Changes to Risk-Based Pricing Notices.* The proposed changes to Regulation V would require the following additional disclosures be provided when a credit score is used in either setting the initial material terms of credit or as part of the account review process *and* the credit score adversely affected material terms of the account:

1. A numerical credit score used in making the credit decision;
2. The range of possible credit scores under the credit scoring model that was used;
3. The key factors that adversely affected the credit score (generally not to exceed 4 factors) in the credit scoring model that was used. If one of the key factors is the number of inquiries made, the number of key factors disclosed shall not exceed five in total;

4. The date on which the credit score was created;
5. The name of the person or entity that provided the credit score;
6. A statement that a credit score is a number that takes into account information in a consumer report and that credit scores may change over time as a consumer's credit history changes.

It is to be noted with respect to subparagraph "5" above that the use of proprietary models is not discussed. While not free from doubt, it appears that if a user of credit scores is using a proprietary credit scoring model, which proprietary score is used in conjunction with a credit scoring model provided by a third-party, it is not necessary to provide the proprietary model's credit score. Generally, the Agencies believe the disclosure of two (2) credit scores will be confusing to consumers. See § \_\_.73(d)(1).

The proposal will not require changes to risk-based pricing notices (either those required on initial application for credit or on account review) if a decision was not made using a credit score.

*Co-borrowers.* In the event the credit scores of co-borrowers are used in the credit review process, the notices required in the Proposal must be sent separately, even if the co-borrowers reside at the same address. Each notice would disclose the relevant credit score and additional information related to that score for that borrower. (Query: What would the disclosure be to a co-borrower if that co-borrower had superlative credit and the only reason for an adverse determination was based on the other co-borrower's credit score?) If the notices do not require the disclosure of a credit score (i.e., a credit score was not used in the determination of any material term), a single notice addressed to the co-borrowers may be provided. See § \_\_.75(c).

*Use of Credit Scores in Reviewing Guarantors, Co-signers, Sureties or Endorsers.* Risk-based pricing notices, including any revised notices that will be required if these proposals are adopted, will not be required to be provided to any guarantors, co-signers, sureties or endorsers. The notices are only required to be provided, when necessary, to borrowers (i.e., consumers to whom the credit is actually extended). Users of credit scores will be required to provide risk-based pricing notices to borrowers even if the only credit score used in the decision-making process was that of a guarantor, co-signer, surety or endorser, but users will not be required to provide the credit scores of the guarantor, co-signer, surety or endorser. The Agencies do not believe it to be appropriate to disclose the credit score of one consumer (e.g., a guarantor) to another (e.g., the borrower). See §§ \_\_.73(a)(1)(ix) and \_\_.73(a)(2)(ix).

*Model Forms.* The Agencies provided model forms in the Final Rule. The proposal incorporates the content requirements of section 615(a) of the FCRA to reflect the new content requirements added by section 1100F of the Dodd-Frank Act. Appropriate use of the model forms is deemed to be in compliance with the Final Rule. These proposed amendments to the Final Rule include two (2) additional model forms that incorporate the newly proposed disclosure requirements. See Appendices B-6 and B-7 of the FTC's proposed rule and Appendices H-6 and H-7 of the Board's proposed rule. Use of the model forms will remain optional.

*Use of Multiple Credit Scores.* From time to time, creditors may use multiple credit scores from consumer reporting agencies in determining the material terms of credit. When a creditor uses only one of those scores in setting the material terms of credit, the notices would be required to disclose only that score and the information related to that score. See § \_\_.73(d)(1).

When a creditor uses two or more credit scores in setting the material terms of credit, the notices would require the disclosure of any one of those scores and the information related to that score. (See proposed sections \_\_.73(a)(1)(ix) and (a)(2)(ix). At the creditor's option, more than one credit score may be disclosed together with the information related to each credit score. (See §§ \_\_.73(d)(1)(ix) and (d)(2)(ix).

It is to be noted that one example deals with a creditor who obtains multiple credit scores from several consumer reporting agencies but only uses the low scores in setting credit terms. In those circumstances, the proposal requires the creditor to disclose the low score in its notices. See § \_\_.73(d)(ii)(A).

*Equal Credit Opportunity.* The Equal Credit Opportunity Act (ECOA) requires creditors to provide a statement of reasons for taking an adverse action to affected consumers. (See 15 U.S.C. 1691 et seq.) Regulation B implements ECOA's adverse action notice requirements, but there are no implementing regulations that specifically implement the FCRA's notice requirements. Nevertheless, Regulation B's model notices include the content required by both FCRA and ECOA, so those notices may be used to comply with both statutes. The Board, therefore, proposes to update Regulation B's model notices for consistency with the FCRA, as amended by Section 1100F of Dodd-Frank. See § Appendix C to Part 202 (Regulation B).

**Effective date**

The effective date of the final Rules is intended to be July 21, 2011, the "Designated Transfer Date" as determined by the Secretary of the Treasury pursuant to the provisions of Dodd-Frank.

It is of some significance that there aren't any proposed changes to the "exception notices" under the existing risk-based pricing rule (§ 615(h)(3) of FCRA). This means that those notices may continue to be used by creditors after the effective date of the new rule. These include the customary adverse action notices when consumers have been declined for credit and, in those instances where consumers have applied for specific credit terms and have received those terms (unless those terms were specified by the lender after receiving a consumer report or credit score was obtained), a risk-based pricing notice will not be required.

A number of additional exception notices are permitted. These include those notices that permitted the disclosure of the credit score pursuant to §609(g) of the FCRA and specific exceptions from providing risk-based pricing notices for credit card issuers. See §\_\_.72(c)(2). These disclosures must be accompanied by additional information which will provide context to the meaning of the scores.

Comments must be received within 30 days of publication in the Federal Register. The Agencies specifically are requesting comments regarding (1) the proposed additional content to be provided in the disclosure notices and (2) whether the order of content in the model forms is appropriate. The Agencies intend the final Rule amendments to be effective on the Designated Transfer Date (when authority for implementing and enforcing these rules are transferred (for the most part) to the Consumer Financial Protection Bureau.

The FCRA proposed rules can be found [here](#), the ECOA proposed rules can be found [here](#), and the Dodd-Frank Wall Street Reform and Consumer Protection can be found [here](#).

Future advisories will summarize the final Rules together with other relevant information. If you have any comments or would like more information, please contact Robert Birnbaum, James H. Mann, or Robert Morgan.

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