PENNSYLVANIA
CREDIT UNION
ASSOCIATION

4309 North Front Street
P.O. Box 60007
Harrisburg, PA 17106-0007
www.pcua.coop

August 18, 2008

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: ***FACT Act Risk-Based Pricing Rule, Docket No. R-1316***

Dear Ms. Johnson:

The Pennsylvania Credit Union Association (PCUA) and its member credit unions appreciate this opportunity to provide comments to the Federal Reserve Board of Governors regarding its proposed rule to implement the risk-based pricing provisions of the Fair and Accurate Credit Transaction Act of 2003(FACT Act).

The PCUA is a statewide trade association that represents over eighty percent (80%) of the approximate 589 credit unions located within the Commonwealth of Pennsylvania. To respond to this request for comments, the PCUA consulted with its Regulatory Review Committee (the Committee). This Committee consists of 12 credit union CEOs who lead the management teams of Pennsylvania federal and state-chartered credit unions. Members of the Committee represent credit unions of all asset sizes.

The comments offered by our Committee members and PCUA staff respond to the following specific questions as set forth in the proposed rule.

1. <u>Are there any circumstances under which creditors should be required to provide risk-based pricing notices in connection with credit primarily used for business purposes</u>?

No. Our group unanimously agreed with the analysis included in the proposed rule. Specifically, the underwriting and pricing process used in analyzing a commercial loan is quite different than those utilized in the consumer lending process. It would not be operationally feasible to compare the terms of credit granted for different business purposes because some types of business ventures pose a greater degree of risk than other types of businesses.

Our group does not believe that there are any circumstances under which creditors should be required to provide risk-based pricing notices in connection with credit primarily used for business purposes. The inclusion of risk-based pricing notices in a commercial lending transaction would only lead to additional confusion for the borrower(s).

Ph. 800-932-0661 • 717-234-3156 • Fax 717-234-2695

2. Is the proposed definition of "materially less favorable" helpful? Should the interrelated terms "most favorable terms" and "a substantial proportion of consumers" also be defined and, if so, how should it be defined?

The phrase "materially less favorable" is defined under the proposed regulation to mean: "when applied to material terms, that the terms granted or extended to a consumer differ from the terms granted or extended to another consumer from or through the same person such that the cost of credit to the first consumer would be *significantly greater* than the cost of credit granted or extended to the other consumer. For purposes of this definition, factors relevant to determining the significance of a difference in cost include the type of credit product, the term of the credit extension, if any, and the extent of the difference between the material terms granted or extended to the two consumers." *See* F.R. 28992, § 222.71(j).

The section-by-section analysis further advises that creditors, in assessing the extent of the difference between two sets of material terms, "should consider how much the consumer's cost of credit would increase as a result of receiving the less favorable material terms and whether that difference is likely to be important to a reasonable consumer." F.R. 28972.

The proposed definition and guidance are unwieldy and vague. Our members request more definitive criteria in the final regulation for purposes of determining whether the cost of credit would be "significantly greater" than the cost of credit granted or extended to the other consumer. F.R. 28972.

In its narrative, the proposed rule provides that a credit card issuer considering these factors may conclude that a 25 basis points difference in the annual percentage rate is not material, whereas a mortgage lender may conclude that a 25 basis points difference is material. This example emphasizes our concern and exemplifies the need for objective and standard criteria, such as a specific difference in basis points. F.R. 28972.

It is certain that lenders in banks, credit unions, mortgage lending companies, etc., will view "whether the difference is likely to be important to a reasonable consumer" differently. In order to ensure that the notices are provided on a consistent and uniform basis, the final rule must provide more clarity as to when the material terms are different enough to cause the cost of credit to a consumer to be significantly greater than the cost to other consumers.

3. Do creditors vary temporary initial rates, penalty rates, balance transfer rates, or cash advance rates, on either closed-end or open-end credit, as a result of risk-based pricing? If those rates do vary as a result of risk-based pricing, should any of them be treated as "material terms," in addition to the general APR, and would it be possible to apply to those rates the existing test-consumer-to-consumer comparison, credit score proxy method, and tiered pricing method? If new tests would be required under such a broader definition of "material terms," what might those tests be?

Some of our member credit unions vary the loan term (length of time), the loan-to-value ratio, or the loan amount on the factors and scores included in a consumer/member's credit report. While we are not necessarily encouraging the Federal Reserve to include those items in the "material terms" definition, those factors could be viewed by some consumer groups and courts to be items that significantly increase the cost of credit to consumers. Again, we submit that objective versus subjective criteria for determining when risk-based pricing notices must be provided would be helpful to the lending industry and alleviate unnecessary lawsuits that are driven by subjective and unclear requirements.

4. Will the credit score proxy method generally result in risk-based pricing notices being provided to consumers who are likely to have received materially less favorable terms? Will setting the cutoff score at approximately the point at which 40 percent of a creditor's consumers have higher scores and 60 percent have lower scores be appropriate and workable, or should a different point, such as the point at which 50 percent of a creditor's consumers have higher scores and 50 percent have lower scores, be more appropriate? Do you know of any empirical data regarding the point at which consumers typically begin to receive materially less favorable terms that may suggest the most appropriate point at which to set the cutoff score?

For the reasons noted below, our members believe that the credit score proxy method, as proposed, will only increase confusion and be of little benefit to consumers.

5. What should the requirements be to recalculate the credit score cutoff, specifically regarding whether two years, as opposed to a shorter or longer period, is the appropriate interval at which the recalculation generally should be conducted? Is one year the appropriate period of time within which a person using the secondary source approach must recalculate its cutoff score using the sampling approach? The secondary source approach is determining the appropriate cutoff score based on information derived from appropriate market research or relevant third-party sources for similar products.

The proposed rule recognizes that the sampling approach used to calculate the credit score cutoff will not be feasible for some creditors, such as new entrants to the credit business, that introduce new credit products, or entities that have just started to use risk-based pricing and have not yet developed a representative sample of consumers. F.R. 28975.

The proposed rule permits such creditors initially to determine the appropriate cutoff score based on information from appropriate market research or relevant third-party sources for similar products, such as information from companies that develop credit scores.

Under the proposed rule, persons using the sampling approach will need to recalculate their cutoff scores at least every two years. A person whose cutoff was determined using the secondary source approach will be required to recalculate its cutoff score based on a representative sample of its own data.

Our members indicated that they would likely use information and data available to them through *FairIssac* http://www.fairisaac.com/fic/en/company/, which develops consumer FICO scores.

The recalculation requirements included in the proposed rule are overly burdensome and costly without providing any real benefit to consumers. Our group requests that the final rule allow creditors to use the information and data available through a secondary source on an ongoing basis to calculate and recalculate the cutoff score under the credit score proxy method approach.

By using data and information available through a secondary source, such as *FairIssac*, the application of this option will be more uniform and subject to fewer challenges based upon claims of sufficiency or adequacy of the information used to establish the cutoff score.

6. <u>Regarding the credit score proxy method, when a consumer's credit score is not available, the Agencies have proposed an assumption that the consumer receives credit on less favorable terms than other consumers and should therefore receive a risk-based pricing notice. Is this an accurate assumption? If no credit score is available, are there other reasonable means by which a creditor may determine whether the consumer received materially less favorable credit terms?</u>

This is one of the aspects of the credit score proxy method that leads to increased confusion on behalf of the consumer. To the extent available, creditors should be permitted to rely on information and data available from secondary sources that collect such information to determine if a consumer will be more likely than not to receive materially less favorable credit terms.

7. <u>The proposed rule would require that the risk-based pricing notice contain a statement alerting consumers that a free consumer report can be obtained for 60 days following receipt of the notice. Is it appropriate to require disclosure of the 60-day period in the notice?</u>

This requirement appears to be reasonable.

8. <u>Should the notice state that the terms "may be" less favorable, as proposed, or should a different phrase be used, such as that the terms "are likely to be" less favorable? What language would best serve the dual goals of most accurately describing the probability that the consumer received materially less favorable terms while prompting consumers to obtain and review their consumer reports?</u>

Our members did express concern over the uncertainty that using the term “may be” less favorable could cause. Again, this is another aspect of the credit score proxy method that our group believes will result in greater confusion to the consumer. The idea that their terms maybe, but may not necessarily be, less favorable seems to negate any beneficial value of the risk-based pricing notice.

As a general matter, our group stated that consumers need to be encouraged to shop for their credit and find the best terms that meet their financial needs. Often, terms of the loan, other than the APR, can be important in assisting a consumer/member to meet their financial needs at a particular point in their lifetime.

Including language in the notice which states that the terms offer to the consumer are based, in part, on the consumer’s credit score and that the consumer should shop for credit to find the best loan terms to meet their needs would, in our opinion, be more useful.

9. <u>Would requiring disclosure of the key factors that adversely affected the credit score in the credit score notice be helpful to consumers or would it impose undue burdens on the industry? Would including the four key factors simplify compliance with the rules by making the content of this notice more similar to the content of the credit score notice for loans secured by residential real property?</u>

We encourage the agencies to include notice content requirements under this rule that are similar or the same as the content requirements already in place for loan secured by residential real property.

10. The Agencies solicit comment on all aspects of the proposal, particularly on the methods contained in the proposal that creditors may use to identify which consumers must receive risk-based pricing notices, and the approach of providing creditors with several options for complying with the rules. The Agencies also solicit comment on any other operationally feasible tests or approaches that would enable creditors to distinguish consumers who must receive notices from consumers who should not receive notices. The Agencies also solicit comment on the appropriateness of the proposed exceptions, and whether any additional or different exceptions should be adopted.

The tiered pricing method appears to be the most operationally feasible test for identifying consumers entitled to risk-based pricing notices.

Thank you again for this opportunity to comment on behalf of Pennsylvania credit unions. Please feel free to contact me or any of the PCUA staff at 1-800-932-0661 if you have any questions or if you would like to discuss our comments.

Sincerely,

Laurie S. Kennedy

Laurie S. Kennedy
Associate Counsel

LSK:llb

cc: Association Board
Regulatory Review Committee
J. McCormack
R. Wargo
M. Dunn, CUNA