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July 16, 2004

Federal Trade Commission
Office of the Secretary
Room H-159 (Annex M)
600 Pennsylvania Avenue, NW
Washington, DC 20580

Re: FACT Act Section 318(A)(2)(c) Study, Matter No. P044804
Providing Consumers with the Same Credit Report
On Which an Adverse Action was Based

Dear Sir or Madam:

The Independent Community Bankers of America (ICBA)¹ appreciates the opportunity to comment on the Federal Trade Commission's (FTC) study of the feasibility and issues involved with providing the same credit report to a consumer that served as the basis for an adverse action. The study is required by section 318 of the Fair and Accurate Credit Transactions (FACT) Act.

Background

Currently, creditors must provide an adverse action notice to consumers when information in a credit report is used to deny credit, offer credit on substantially different terms or terminate credit.² As a practical matter, most creditors combine the adverse action notice required by the Fair Credit Reporting Act (FCRA) with the adverse action notice required by the Federal Reserve's Regulation B that implements provisions of the Equal Credit Opportunity Act. While the FCRA does not impose a time limit for providing the adverse action notice, the Regulation B notice must be provided within 30

¹ The Independent Community Bankers of America represents the largest constituency of community banks of all sizes and charter types in the nation, and is dedicated exclusively to protecting the interests of the community banking industry. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.

² For the purposes of this study, an adverse action does not include situations that could trigger a risk-based pricing notice.

days of the adverse action. An adverse action notice provides the consumer with information about the credit bureau that provided the report, how to contact the credit bureau for a free copy of their credit report, and steps that can be taken regarding the accuracy or completeness of information in the credit report.

It is possible that consumers who request a free copy of their credit report may see a different version of the credit report than the one relied on by the creditor. This is not the case for employees or prospective employees in an employment setting, since employees or prospective employees are entitled to a copy of the same credit report information that an employer used for the adverse action. As a result, the FACT Act requires the FTC to conduct this study.

ICBA Comments

Generally, the ICBA does not believe that it is necessary for consumers to receive a credit report that is identical to the one that served as the basis for an adverse action. Unlike employment situations, a separate regulation requires creditors to furnish an adverse action notice within a specified time period – 30 days. As a result, consumers are given notice and an opportunity to access their credit report within a short period of time after the lender reviewed the report.

While there might be some benefits to providing an identical credit report, the costs associated with ensuring that the consumer sees the same report would far outweigh any minimal benefits, especially since it is unlikely that there will be any significant or substantial differences between the credit report relied on by a creditor and the one reviewed by the consumer. Since one of the primary goals of increasing consumer access to their credit reports – preventing identity theft – is already addressed by a number of other provisions of the FACT Act, especially the availability of a free annual credit report, any minimal benefits produced by ensuring a consumer receives the identical credit report on which an adverse action was based will be far outweighed by the associated costs.

Community Banks Use of Credit Reports

At the outset, it is extremely important to recognize that loan underwriting is an art and not a science. While the increased use of technology have advanced the ability of banks to streamline the process and use automated techniques to grant or deny a loan request, the final decision to underwrite a loan may not be a cut-and-dried decision. This is especially true for borrowers with borderline qualifications. It is also important to recognize that bankers and other lenders are constantly encouraged to work with low- and moderate-income consumers to help enhance their access to financial services under federal mandates such as the Community Reinvestment Act. Lenders also are constantly encouraged to reach out to consumers that do not have banking relationships with new and innovative programs, an area where the Treasury Department and other federal government agencies have been taking an active role. If

these outreach programs are to succeed, banks must continue to be permitted flexibility in their underwriting practices. The FTC should keep this in perspective as it analyzes the use of credit reports, since additional restrictions or requirements could have an unintended consequence on the ability of banks to serve consumers and maintain these outreach programs by limiting or otherwise restricting existing flexibility through new requirements.

Use of More than One Credit Reporting Agency. Many community banks report obtaining credit reports from more than one credit reporting agency for a variety of reasons. For example, different bureaus may have different information on a consumer and access to more than one credit report allows the lender to obtain as much information as possible when making the underwriting decision. Some companies do not report information to all credit bureaus.³ And, some secondary market purchasers require more than one credit report in the consumer's file in order for them to purchase a loan.

However, not all lenders use multiple credit reports for underwriting a loan. Some lenders do not find it necessary: a single credit reporting agency meets their needs. However, the ICBA believes that if consumer loan applicants were required to receive the same credit report on which an adverse action was based, the need to streamline operations and reduce costs might force lenders to use a single credit report. This would reduce the amount of information available for underwriting decisions, potentially affecting borderline loan applicants particularly, since the reduced information might increase the number of loan denials.

A number of community banks also report that they currently use merged credit reports provided by a service bureau. In these arrangements, the service bureau collects the credit report information from more than one credit reporting agency to produce a merged report. However, this is more expensive than a single report from one national credit reporting agency, and so community banks tend to use these merged reports only in limited circumstances, primarily for loans secured by real estate or mortgage loans where the bank intends to sell the loan on the secondary market and the loan purchaser requires it. However, the use of merged credit reports is a complicating factor that must be considered as part of the FTC's analysis.

One possible solution to these issues would be to simply require the lender to furnish the consumer with a copy of the credit report or merged report on which the adverse action was based. However, that would require all existing statutory and regulatory impediments that restrict this practice to be identified and eliminated. For example, lenders would have to be exempted from the definition of credit reporting agency. Another factor would be the resulting increase in the cost for loan applications to cover the additional requirement. The added costs would not be limited to a simple matter of photocopying and furnishing the credit report. Rather, proper policies and procedures would have to be developed, including audit and compliance procedures, to ensure that the bank properly satisfies any new mandate.

³ Media reports and consumer activists were highly critical when Sallie Mae stopped providing student loan repayment history to two of the three major national credit bureaus.

A Credit Reports is not the Only Factor Used in the Credit Decision. In most instances, banks and other lenders do not base credit decisions solely on the information in a credit report. Virtually all community banks use additional information such as payment history on prior loans and other relationships with the bank; employment history and income verification; length of residence and homeownership status; a variety of financial ratios; information from tax returns provided by the consumer; available collateral; and other factors. The adverse action notices currently used by lenders specify that an underwriting decision may have been based *in whole or in part* on information from a credit report, i.e., other factors may have affected the underwriting decision. The rationale for notifying consumers that the decision may have been based on information from a credit report is to give consumers the opportunity to review and correct any errors in a credit report. However, the new FACT Act requirement of a free annual credit report already addresses this issue.

As noted above, the underwriting process is an art, and many other factors may also contribute to the final lending decision. In fact, compliance experts encourage banks to furnish more than one reason for loan denial,⁴ and no one element may be the deciding reason for an adverse action. However, if a credit report were furnished as part of the adverse action notice, no matter how it was provided to the consumer that would serve to elevate the importance of the credit report as the decisive factor in consumers' minds.

Use of Credit Scores. In recent years, increasing focus has been given to the use of credit scores in loan underwriting as the use of technology in lending has expanded. While community banks are increasing the use of credit scores in underwriting, the banks that use them report they are a guide but not the sole basis for an underwriting decision. If and when credit scores are used, some community banks report preparing them in-house. However, due to Federal Reserve Regulation B, which requires validation of credit scoring mechanisms, many community banks that use credit scores report they rely on credit scores furnished by one of the three major national credit reporting agencies or another service provider, another factor that must be weighed into the FTC's analysis.

Providing Adverse Action Notices. As required by the Federal Reserve's Regulation B, community banks provide consumers with an adverse action notice within 30 days of reaching a decision. Some provide the notice verbally within a day or two of the decision and then follow the oral notice with the requisite written notice. Because community banks strive to provide good customer service, many community bankers report mailing the written notice within one week of reaching an adverse action decision.

⁴ Federal regulations under the Home Mortgage Disclosure Act (HMDA) permit lenders to report up to three reasons for denial on the HMDA-Loan Application Register. See 12 CFR 203, Appendix A. However, lenders are not limited to three variables when providing an adverse action notice. For example, the Federal Reserve's sample adverse action notice under Regulation B, Appendix C-1, allows up to 24 different reasons for an adverse action, with the final item being an open-ended "other."

To ease compliance burdens, many community bankers use one of the sample forms provided by the Federal Reserve in an appendix to Regulation B. Those sample forms ensure compliance and include the necessary language that the decision may have been based in whole or in part on information from a credit report, with information about how the consumer can contact the credit reporting agency to obtain a copy of the full credit report. However, community bankers report that they believe that consumers rarely contact the credit reporting agency for a copy of the credit report. Although this is anecdotal evidence, the general consensus of these bankers is that most consumers that receive an adverse action notice know in advance that there is a problem and are not surprised by the adverse action notice.

Consumers Likely to Receive Substantially Similar Credit Reports.

Community bankers report that the few consumers that request a copy of their credit report are likely to receive a report that is very similar to the credit report reviewed by the bank. This is especially likely since community bankers report furnishing the adverse action notice as soon as possible after an underwriting decision is made. If there are differences between the information in the report on which the bank relied and the report supplied to the consumer, most community bankers believe those differences will be insignificant. ICBA members also report that if there is a reason that the consumer believes there is an error that produced the adverse action, the consumer will contact the credit reporting agency as soon as possible to get a copy of their report. As a result, this helps limit the time that elapses between the time a credit reporting agency provides the bank with a credit report and the time the consumer sees the credit report, further ensuring that the information in the two reports will be substantially similar or virtually identical.

However, there is one key distinction in the credit report that a credit reporting agency furnishes the bank and the one sent to a consumer, and that is that the report sent to the consumer is reformatted to be more understandable by consumers. As a result, any change requiring consumers to receive the same credit report used by a lender as the basis for an adverse action will entail changes to how banks and other lenders currently process credit report information, especially companies that use automated lending processes to make credit reports used by banks more comprehensible to consumers. Otherwise, additional means will be needed to help consumers understand and interpret the information provided in the credit report format as presented to lenders. This reconciliation and disclosure process is likely to be both expensive and burdensome.

Discrepancies or Errors in a Credit Report. If a consumer detects an error in the credit report, community bankers report very few consumers contact the bank. When consumers do contact, most community bankers report that they must refer the consumer to the credit reporting agency since the error is likely to be something outside the bank's knowledge or control. However, if the error appears related to information that the bank may have furnished, the banks will work with the customer to help resolve any discrepancies.

Banks Should Not Furnish a Copy of the Credit Report. As a general rule, community bankers do not believe that it would be appropriate to require the bank to provide a copy of the credit report on which an adverse action is taken, for reasons described below. In any event, most community banks make every effort to provide an adverse action notice as quickly as possible after an adverse action is taken, but certainly within the 30 days mandated by the Federal Reserve's Regulation B. If a consumer contacts the credit reporting agency as soon as the adverse action notice is received, it is likely to ensure that the credit report the consumer receives is substantially similar or virtually identical to the one used by the bank.

Under current procedures, if there are inaccuracies in the credit report, the consumer contacts the credit reporting agency. Community bankers believe that a mechanism that places consumers into direct contact with the credit reporting agency to resolve the error creates an incentive for the credit reporting agency to ensure that the information is accurate. Having consumers contact the credit reporting agency directly eliminates a "middleman" in the process. A bank is not in a position to explain or correct errors in the credit report that are based on information furnished by other creditors. If the bank did not provide the inaccurate or contested information, the additional step might delay the correction of errors or inaccuracies, or the posting of an alert or other steps needed to address identity theft. By contacting the credit reporting agency directly, a consumer can immediately answer any possible questions the credit reporting agency may have about potential discrepancies, as well as possible verification information required under recently adopted regulations under the FACT Act.

While community bankers do not believe it would be difficult to provide consumers with a copy of the credit report on which an adverse action notice was based, they do have other concerns. First, legal and regulatory impediments that currently prevent banks from providing a copy of the credit report would have to be resolved, such as exempting banks from being defined as credit reporting agencies if they furnish the report. Second, once that hurdle is overcome, contractual agreements with credit reporting agencies and service bureaus that preclude the creditor from giving the consumer a copy of the credit report would have to be changed. Third, there are potential procedures that may need to be implemented to ensure that the privacy and security of consumer credit report information is properly maintained.

If community banks were required to provide a copy of the credit report, other procedures would also need to be changed. For example, additional resources would be required to permit banks to work with consumers to address perceived inaccuracies in credit reports, including proper training for bank employees. This is a role that greatly expands on existing practices and procedures and would require the deployment of additional resources. All these changes would entail costs beyond photocopying the credit report, and it is likely these would be passed on to the consumer in the form of increased fees.

Conclusion

Many other elements of the FACT Act address problems associated with identity theft, such as free annual credit reports and alerts on credit reports. The substantial costs associated with providing consumers an identical copy of the credit report used for an adverse action would far outweigh any minimal benefits. For these reasons, the ICBA does not believe it is necessary for consumers to receive a copy of the identical credit report. This is especially true since those few consumers that do request a copy of their credit report following an adverse action are likely to see a report that is substantially similar to the one used by the lender.

Anecdotal evidence suggests that most consumers are not surprised by an adverse action. Even so, and assuming existing legal and regulatory hurdles could be overcome, requiring banks to provide consumers with a copy of the credit report on which an adverse action was based would interpose the underwriter between the consumer and others, including the credit reporting agency, who are in a better position to address and correct any inaccuracies in the credit report. This addition of a new middleman might actually delay steps needed to correct inaccuracies and prevent and deter instances of identity theft.

Thank you for the opportunity to comment. If you have any questions or need any additional information, please feel free to contact me at 202-659-8111 or by e-mail at robert.rowe@icba.org.

Sincerely,

Robert G. Rowe, III
Regulatory Counsel