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August 18, 2008

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Federal Trade Commission
Office of the Secretary
Room H-135 (Annex M)
600 Pennsylvania Avenue, N.W.
Washington, DC 20580

Re: Docket No. R-1316 – FACT Act Risk-Based Pricing Rule / FACT Act Risk-Based Pricing Rule, Project No. R411009

To Whom It May Concern:

The Credit Union National Association (CUNA) appreciates the opportunity to comment on the proposed rule issued jointly by the Federal Reserve Board (Board) and the Federal Trade Commission (FTC) that will require creditors to provide consumers with a risk-based pricing notice in situations in which credit is offered to the consumer on terms that are materially less favorable than those offered to a substantial proportion of other consumers. The notice informs the consumer that they may be receiving credit on less than favorable terms and provides additional information regarding the use of credit reports. The proposal is being issued pursuant to Section 311(a) of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act), and the proposal also provides certain exceptions to these requirements when credit score information is provided to all consumers who apply for credit. By way of background, CUNA represents approximately 90% of our nation's 8,300 federal and state-chartered credit unions, which serve 91 million members. This letter was developed under the auspices of the CUNA Consumer Protection Subcommittee.

Summary of CUNA's Comments

- CUNA agrees that the standard annual percentage rate (APR) should generally be the credit term for purposes of determining who should receive a risk-based pricing notice.
- The proposed rule will require that these notices go to consumers who are receiving "materially less favorable" credit terms. This needs clarification as it may lead to situations in which one creditor would send more risk-based pricing notices than another, even if both offer similar APRs to consumers with similar credit histories. The terms "most favorable terms" and "substantial portion of consumers" also need further clarification.

- The risk-based pricing rule needs further clarification with regard to indirect automobile lending as it is unclear in certain situations as to which party should provide the risk-based pricing notice. CUNA believes the dealer is in the best position to provide the notice.
- As proposed, the requirement to provide risk-based pricing notices will result in delay and inconvenience for members who participate in multi-featured, open-end lending. CUNA believes there should be an exception to the timing requirements in these situations.
- The proposed rule should also clarify who receives these notices when there is a joint application for credit.
- CUNA supports the credit proxy method and the tiered pricing method for determining which consumers should receive the risk-based pricing notices.
- The proposed rule will only apply to credit that is primarily for personal, family, or household purposes, and it should not be expanded to include credit that is primarily for business purposes.
- CUNA believes the risk-based pricing notices should be modified to alleviate burdens for creditors by allowing creditors to use the current mortgage loan credit score disclosure, with appropriate modifications. CUNA provides examples of this approach.
- Compliance with the risk-based pricing rule should not be required until at least two years after these changes are issued in final form, due to the complexity of this rule and the requirement to comply with a number of other rules that are being issued by the Board and the FTC.

Discussion

For creditors that use risk-based pricing when offering credit, the proposal will require them to provide notice to certain consumers. More specifically, a notice must be given to a consumer when the creditor: 1) uses a consumer report in connection with an application or extension of credit to a consumer; and 2) based on that report grants or extends credit to the consumer on material terms that are materially less favorable than the most favorable terms offered by that creditor to a substantial portion of consumers. Below are our comments with regard to the specific notice requirements, along with our comments on the proposed exceptions to these requirements when creditors provide credit score information to all consumers, followed by our comments on the significant operational costs imposed by these requirements, which for these and other reasons will necessitate a significant delay in the effective date of these rules.

Determining Who Should Receive a Risk-based Pricing Notice

The proposal provides definitions or guidance for the terms “material terms,” ”materially less favorable,” “most favorable terms,” and “a substantial portion of consumers.” Under the proposal, “material terms” will generally be defined as the standard or purchase APR. We agree with this definition as it will be the

easiest for consumers to understand and the least burdensome approach for credit unions.

In the proposal, the agencies requested comment as to whether similar rates also vary as a result of risk-based pricing and whether they should be included within the definition. These similar rates include “temporary initial rates,” “penalty rates,” “balance transfer rates,” and “cash advance rates.” These rates do vary based on the credit history of the consumers and another rate term that would vary would be the margin added to an index for variable rate mortgage loans.

However, we do not believe these should be incorporated within the definition of “material terms” as it would be very confusing for consumers, and it would be very burdensome for creditors to analyze all these rates for purposes of determining who would receive a risk-based pricing notice. Many of these other rates are only in effect for a limited period of time so it would not be useful to incorporate these terms within the definition. Also, rates such as “temporary initial rates” are actually lower than the rate that would otherwise apply on the account. This is beneficial to all consumers, regardless of whether their lower rate is better or worse than a lower rate offered to another consumer, and it therefore would not make sense to use this as a basis for determining who among these consumers should receive a risk-based pricing notice.

We believe the term “materially less favorable” needs clarification as it may actually lead to situations in which one creditor would send more risk-based pricing notices than another, even if both offer similar APRs to consumers with similar credit histories. This would lead to a false perception that one creditor is offering more unfavorable APRs than the other, which would diminish the reputation of that creditor, even though this results solely from a difference in how each of them complies with these requirements.

For example, two creditors using risk-based pricing could each offer a credit card with a 10% APR to consumers with the best credit scores. However, one may decide that any credit card it issues that is higher than 10% would be “materially less favorable” than its best rate, while the other may decide that only cards it issues with an APR above 14% should be considered “materially less favorable.” The result would be that the first creditor would likely be issuing more risk-based pricing notices only because it is taking a more cautious approach to complying with these requirements, but the effect may be that it will suffer harm to its reputation if more consumers believe that this creditor is more likely to offer less favorable APRs.

We recognize this problem may primarily apply to creditors using the “consumer-to-consumer comparison” approach, as opposed to the “credit score proxy method” or the “tiered pricing method” for purposes of determining who receives the risk-based pricing notice. However, we believe further clarification of the term “materially less favorable” is nonetheless in order to avoid a result in which

a creditor would suffer reputational harm solely because it is more cautious in complying with this proposal by issuing more risk-based pricing notices.

For similar reasons, we also believe the terms “most favorable terms” and “substantial proportion of consumers” should be further clarified. This will help creditors in their effort to comply with these requirements and will benefit consumers by treating them all relatively equal for purposes of determining who should receive the risk-based pricing notices.

Indirect Lending

In addition to the terms described above, we are concerned with regard to provisions that describe which party is required to provide the risk-priced notices in certain situations, specifically in connection with indirect automobile lending. The proposed rule makes distinctions based on how the transaction is conducted. In general, the distinction is made based on “to whom the loan obligation is originally payable,” which would be the party responsible for providing the risk-based pricing notice.

For automobile lending, the proposal gives an example of when the dealer is the original creditor under a retail installment sales contract, in which case the dealer would be responsible for providing the risk-based pricing notice, even though the contract is immediately assigned to a financial institution. We understand this may be intended to address indirect automobile lending practices in which it is recognized that the dealer would be in the best position to provide the notices.

However, it is our understanding that indirect automobile lending practices may differ and there are situations in which the financial institution would be listed as the creditor on the sales contract and would be the party “to whom the obligation is originally payable.” Under the proposal, we would be concerned this would mean that the financial institution would be required to provide the notice in these situations.

In our view, it would be very difficult for the financial institution to provide the notice in a timely manner in these situations, and in some cases it may not be possible. For example, many consumers may choose to purchase an automobile on a weekend or during the evening after the financial institution is closed. If they decide to purchase an automobile during that visit, they expect to be able to consummate the purchase at that time and to leave the dealer with their new car. However, the financial institution would not be able to provide the notice before the consummation of the transaction in these circumstances.

For these reasons, we believe the better, and simpler, approach would for the proposal to require the automobile dealer to provide the notice in all indirect lending situations and for the regulators not to determine who provides the notice based on which party is listed on the retail installment sales contract. Otherwise,

there may be a significant delay in consummating the transaction, which would be contrary to the consumer's expectation of being able to take possession of the new car at the time he or she decides to make the purchase.

The financial institution may, of course, be able to provide in advance the notice that the dealer would give to the consumer who is entitled to receive it, whether in paper or electronic form. However, the institution would have to rely on the dealer to identify which consumer must receive the form and to provide the dealer with the form before the transaction is consummated.

Multi-faceted Credit Plans

For similar reasons, we are concerned with the requirement to provide risk-based pricing notices for those credit unions that use multifeatured, open-end lending. Under these plans, a credit union member has one credit plan with the credit union with a number of credit features, or sub accounts, that are available to the member. This arrangement allows the member to access a variety of different types of loans at different times under a single credit plan.

When a member accesses credit under these plans, he or she can often just place a call with the credit union and then have access to the funds shortly thereafter. With regard to the proposal, the concern here is that providing the additional notice under these circumstances will result in a delay in receiving the funds, whether it is the risk-based pricing notice that is required to be sent to those members who are entitled to receive them or the credit score information that credit unions may send to all members as a substitute for the risk-based pricing notice. This may require the member to wait for the notice to be faxed or mailed or require the member to take time and incur expense by traveling to the credit union to complete the transaction and receive the required notice.

Both of these alternatives will result in delay and inconvenience for the member. Although sending the required notice by email may alleviate these concerns, this assumes the member has access to the computer at the time he or she requested the funds and that he or she has provided the required consent to receive this information electronically, as required by the Electronic Signatures in Global and National Commerce Act. We anticipate this may significantly hamper the ability to provide email notifications.

For these reasons, we urge the Board and the FTC to provide exceptions to the timing requirements for providing these notices. As proposed, these notices have to be provided before the consummation of the transaction or the first transaction under an open-end credit plan. In order to avoid the delay and inconvenience that would occur for those using a multifeatured, open-end plan, we believe creditors should be permitted to provide these notices shortly after the consumer receives the funds. The purpose of the risk-based pricing notice is to provide information so consumers may improve their credit histories for purposes

of receiving more favorable credit terms in the future, and a short delay in providing the notice will not hamper these efforts.

Joint Applications

We also believe there needs to be further clarification as to who receives the notice when there is a joint application for credit. In these situations, creditors should have the flexibility to provide only one notice to either of the joint applicants, whether it is a risk-based pricing notice that needs to be provided or the credit score information that may be used as an exception to the risk-based pricing notice.

Joint applicants invariably have a special relationship with each other, whether it is a family relationship or similar connection. It is natural to assume these individuals will likely share information and consult with each other when they receive important information about their application, including the notices required under the proposed rule. Any requirement to send these notices to each applicant is especially questionable when they live in the same household, which is often the case. For these reasons, any requirement to provide the same notice to each joint applicant would be duplicative and would impose unnecessary costs, without any corresponding benefits for consumers.

Credit Score Proxy Method

The proposal sets forth three methods for determining which consumers should receive these risk-based pricing notices. One method is the "direct consumer-to-consumer comparison," which involves comparing each consumer to an adequate sample of consumers who have engaged in similar transactions. Another method is the "credit score proxy method." Under this method, a creditor, based on credit score information, may comply with the risk-based notice requirements by: 1) determining the credit score that represents the point at which approximately forty percent of its consumers have higher credit scores and approximately sixty percent of its consumers have lower credit scores, and 2) providing a risk-based pricing notice to consumers with a score below this threshold.

The Board and the FTC have requested specific comment on the credit score proxy method, specifically whether providing notices to the sixty percent of consumers with the lowest scores is appropriate or whether another threshold would be preferable. We support a threshold of either fifty or sixty percent and believe this will target those consumers who should be receiving these risk-based pricing notices.

Under the credit score proxy method, the Board and the FTC have proposed that a risk-based pricing notice should automatically be provided to a consumer in which a credit score is not available and have requested comment as to whether

this is appropriate. We agree this is an appropriate assumption and that these consumers generally do not receive the best interest rates. One possible exception would be for loans that are co-signed by others in which the interest rate is based, at least in part, on the credit history of the co-signer.

Tiered-Pricing Method

The third method for determining who receives risk-based pricing notices is the "tiered pricing method." A creditor using this method may place the consumer within one of a discrete number of pricing tiers based on a consumer report, with each tier representing a different APR. The notices are then provided to those consumers who receive rates that are not in the approximately 30-40% of the tiers that represent the lowest APRs.

As opposed to assigning an APR to each tier, the Board and the FTC have requested comment as to whether this method should take into account the percentage of consumers who are placed within each tier and whether this could be accomplished without creating undue burdens. We would oppose such an approach as this would create significant burdens and excessive complexities.

For some creditors, we understand the Board and the FTC may be concerned that the tiered pricing method may result in a significant portion of consumers being placed in the lowest APR tiers who, therefore, would not receive the risk-based pricing notices. Taking into account the percentage of consumers within each tier may address these concerns if this information were used to make adjustments so that more consumers receive these notices.

However, we do not believe these concerns justify the additional burdens for creditors. Consumers who receive a very good interest rate from a specific creditor do not need a risk-based pricing notice, regardless of the number of consumers who receive this low rate from a specific creditor. These notices need only go to those who are receiving higher interest rates so they have information for purposes of taking actions to improve their credit histories.

Expansion of the Proposal to Business Credit

As proposed, the risk-based pricing rule will only apply to credit that is primarily for personal, family, or household purposes. In the proposal, the Board and the FTC have requested comment as to whether the risk-based pricing rule should also apply to credit that is primarily for business purposes. We would oppose such an expansion of these requirements. Pricing for consumer credit is very often based primarily on credit score information. However, for business credit, there are many other factors that may be involved, which may include how long the business has existed and other intangible factors. Also, interest rates for business credit are much more negotiable than it is for consumer credit. For

these reasons, we believe it would be very difficult for creditors to apply these rules to business credit.

Format for the Risk-Based Pricing Notice and the Exceptions

The proposed rule provides creditors with a number of exceptions to the requirement to provide risk-based pricing notices. These include exceptions in which creditors would not be required to provide these notices if they instead offer credit score information to all consumers who apply for credit. This information must include the score and additional disclosures regarding the use of consumer reports and credit scores during the underwriting process.

We believe the risk-based pricing notices will be helpful for consumers and that changes should be made to the proposal to facilitate and encourage creditors to use these notices. Otherwise, creditors will likely rely on the credit score exceptions. These changes would involve simplifying the risk-based pricing notices to relieve burdens for creditors, while providing the information to consumers as envisioned under Section 311(a) of the FACT Act.

Without these changes, it is likely that most creditors may elect to provide credit score information under these exceptions to all consumers who apply for credit. In our view, this contradicts the intent of Section 311(a) of the FACT Act, which is to provide additional information to those consumers who are receiving higher-priced credit, based on their credit report information.

Although we appreciate that the exceptions may be intended to alleviate burden for creditors, we believe the same goal can be achieved by streamlining the risk-based pricing notices in a manner that will also provide useful information for consumers, as contemplated under Section 311(a) of the FACT Act. As described below, this will involve allowing creditors to modify the mortgage loan credit score disclosure that creditors are currently required to provide under Section 212(c) of the FACT Act. Under these provisions, which apply to mortgage loans, a creditor must provide a copy of the credit score obtained from a credit reporting agency, and a "Notice to Home Loan Applicants," along with other information, which explains the use of credit scoring by lenders, the factors that determined the score, and who to contact with questions concerning the credit score or the terms of the loan.

For mortgage loans, the risk-based pricing notice can simply be a modified form of the current mortgage loan credit score disclosure that all mortgage loan applicants receive. Instead of the current disclosure, the modified form would be provided to those consumers who are entitled to receive a risk-based pricing notice, based on the methods outlined in this proposal. The modified form would essentially be the same as the current form, with the exception of adding the following introductory paragraph, or comparable language, which is similar to the provisions of the model form that is included in the proposal:

> We used information from your credit report[s] to set the terms of the credit that we are offering you, such as the Annual Percentage Rate. These terms may be less favorable than the terms offered to consumers who have better credit histories.

With this form, recipients will be told that they are receiving credit on less favorable terms and, similar to those who receive the current mortgage loan credit score disclosure, the form will provide the credit score, the range of possible scores, the source of the information, how this information is used and how it may change based on the recipient's payment patterns, the factors adversely affecting the score, and who to contact for more information.
We believe this is the type of information that is contemplated under the risk-based pricing provisions of the FACT Act, which will be very valuable for consumers. Under this approach, the information can be provided with less burden for creditors, as opposed to the requirements under the proposal, since it is largely based on the currently existing mortgage loan credit score disclosure.

A similar notice may be provided to those who apply for non-mortgage credit and who will receive credit on less favorable terms. For non-mortgage credit, the notice would be the same as the current mortgage loan credit score disclosure, except the first paragraph would be modified as follows to provide the specific information as required under the risk-based pricing provisions of the FACT Act and to delete the specific reference to mortgage loans:

> We used information from your credit report[s] to set the terms of the credit that we are offering you, such as the Annual Percentage Rate. These terms may be less favorable than the terms offered to consumers who have better credit histories. In connection with your loan application, the lender is providing to you the score that a consumer reporting agency distributed to users and the lender used in connection with your loan, and the key factors affecting your credit score.

Again, we believe this approach complies with the language and intent of the risk-based pricing provisions of the FACT Act in a manner less burdensome than what would be required under the proposal. We also recognize that these notices would need to be modified for those consumers in which a credit score is unavailable. We believe the modified notices should inform these consumers that they are receiving credit terms that may be less favorable than the terms offered to others due to the fact that the credit score is unavailable, along with details as to how these consumers may obtain more information about their credit histories, which again would be similar to the information in the current mortgage loan credit score disclosure.

Prescreened Solicitations

Although we oppose the proposed exceptions described above, we do support the exception for prescreened solicitations. Under this exception, a creditor would not be required to provide a risk-based pricing notice if the creditor obtains a consumer report that is a prescreened list and uses the report to make firm offers of credit to consumers. We agree with the agencies that in these circumstances it should not matter to the consumer how the material terms of such an offer differ from the terms that the creditor includes in firm offers of credit to other consumers, especially in these situations in which consumers have expressed no interest in pursuing these offers. We also agree with the agencies that it would be very burdensome to impose a notice requirement on creditors in these situations in which there is very little benefit for consumers, since most do not respond to prescreened solicitations.

Implementation Period

Because this proposal is very complex and will impose significant regulatory burdens, we believe credit unions and others should be given a significant amount of time to prepare for these changes. For this reason, we believe that mandatory compliance should not be required until at least two years after these changes are issued in final form. This time will be necessary in order to allow credit unions and others sufficient time to develop and adopt the new risk-based pricing notices, provide appropriate staff training, and implement the necessary data processing changes.

Although we realize two years is a significant period of time, we believe it is warranted for this proposal. Not only is this proposal complex, but the Board and FTC have issued a significant number of new, complex consumer protection rules over the past several years and will issue several more in the near future. In light of this, we believe a delay in the mandatory compliance date for a longer period of time, at least two years, is fully warranted.

The Board and the FTC have invested a significant amount of time in developing these rules to ensure that they provide useful information for consumers. We now request that the Board and the FTC provide credit unions and others with the amount of time they will need to ensure successful implementation of these changes.

Thank you for the opportunity to comment on the proposed rule issued jointly by the Board and the FTC that will require creditors to provide certain consumers with risk-based pricing notices. If you have questions about our comments, please contact Senior Vice President and Deputy General Counsel Mary Dunn or me at (202) 638-5777.

Sincerely,

Jeffrey P. Bloch
Senior Assistant General Counsel