



FEDERAL RESERVE BANK *of* KANSAS CITY

January 14, 2010

FINAL RULE ON RISK-BASED PRICING NOTICES

Attention: Chief Executive Officer of Each Tenth District State Member Bank

Subject: New Final Rule that Require a Creditor to Provide a Risk-Based Pricing Notice

In Brief: On December 22, 2009, the Federal Reserve Board (Board) announced a final rule that implements section 311 of the Fair and Accurate Credit Transactions Act (FACT Act) of 2003, which amends the Fair Credit Reporting Act (FCRA). The final rule generally requires a creditor to provide a consumer with a notice when, based on the consumer's credit report, the creditor provides credit to the consumer on less favorable terms than it provides to other consumers. Consumers who receive this "risk-based pricing" notice will be able to obtain a free credit report to check the accuracy of the report. The final rule provides creditors with several methods for determining which consumers must receive risk-based pricing notices.

Highlights: Risk-based pricing is the practice of setting price or other credit terms based on the consumer's risk of nonpayment. Creditors often use consumer report information to set or adjust credit price and terms offered. Creditors that utilize risk-based pricing typically extend more favorable terms to those consumers with good histories and less favorable terms to those with poor histories.

The final rule requires that creditors provide a risk-based pricing notice when stated requirements are met. The requirements for notification apply to credit that is primarily for personal, household, or family purposes; it does not apply to business credit. Creditors must provide a risk-based pricing notice to consumers when information in consumer reports leads to the extension of credit price or terms that are materially less favorable than the most favorable price or terms offered by that creditor to a substantial portion of consumers. The notice is intended to improve consumer awareness of the information contained in their credit history, resulting in more accurate information in consumer reports. Notification of negative information can encourage consumers to check their reports for accuracy and correct any information that is not accurately reported.



**Highlights
(cont.):**

The final rule provides two alternative methods for determining which consumers must receive risk-based pricing notices.

- 1) Credit score proxy method - Creditors will determine the credit score that represents the point at which approximately 40 percent of its consumers have higher credit scores and provide the notice to all consumers with a score below that cutoff score. The final rule requires periodic updating of the cutoff score.
- 2) Tiered pricing method - Creditors who set terms based on pricing tiers related to consumer report information must provide a notice to each consumer that does not qualify for the top tier.

In lieu of providing a risk-based pricing notice, creditors may provide a notice to all consumers which contains the consumer's credit score, explains how the creditor uses credit score information to set the terms of credit, and explains to the consumer how to obtain a free credit report.

A risk-based pricing notice also must be provided when a creditor reviews account information, and based on the consumer's credit history, increases the annual percentage rate applicable to the account of the consumer.

To assist creditors in complying with the final rule, Appendices H-1 through H-5 of Regulation V provide model form risk-based pricing notices and exception notices. However, use of the model forms is not required. The notices must be provided to the consumer after the terms of the credit have been set, but before the consumer becomes contractually obligated on the credit transaction. For account reviews, the notice must be provided at the same time that the rate increase is communicated to the consumer.

Effective

Dates:

The final rule is effective on **January 1, 2011**.

Further

Information:

Questions regarding the final rule may be directed to the Consumer Affairs Department at one of the numbers below:

Kansas City Office

(800) 333-1010, ext. 12488

Denver Office

(800) 333-1020, ext. 22605

Internet:

A copy of the final rule is available on the Board's Web site at:

<http://www.federalreserve.gov/newsevents/press/bcreg/20091222b.htm>