Federal Trade Commission

§ 640.3 General requirements for risk-based pricing notices.

(a) In general. Except as otherwise provided in this part, a person must provide to a consumer a notice ("risk-based pricing notice") in the form and manner required by this part if the person both—

(1) Uses a consumer report in connection with an application for, or a grant, extension, or other provision of, credit to that consumer that is primarily for personal, family, or household purposes; and

(2) Based in whole or in part on the consumer report, grants, extends, or otherwise provides credit to that consumer on material terms that are materially less favorable than the most favorable material terms available to a substantial proportion of consumers from or through that person.

(b) Determining which consumers must receive a notice. A person may determine whether paragraph (a) of this section applies by directly comparing the material terms offered to each consumer and the material terms offered to other consumers for a specific type of credit product. For purposes of this section, a "specific type of credit product" means one or more credit products with similar features that are designed for similar purposes. Examples of a specific type of credit product include student loans, unsecured credit cards, secured credit cards, new automobile loans, used automobile loans, fixed-rate mortgage loans, and variable-rate mortgage loans. As an alternative to making this direct comparison, a person may make the determination by using one of the following methods:

(1) Credit score proxy method—(i) In general. A person that sets the material terms of credit granted, extended, or otherwise provided to a consumer, based in whole or in part on a credit score, may comply with the requirements of paragraph (a) of this section by—

(A) Determining the credit score (hereafter referred to as the "cutoff score") that represents the point at which approximately 40 percent of the consumers to whom it grants, extends, or provides credit have higher credit scores and approximately 60 percent of the consumers to whom it grants, extends, or provides credit have lower credit scores; and

(B) Providing a risk-based pricing notice to each consumer to whom it grants, extends, or provides credit whose credit score is lower than the cutoff score.

(ii) Alternative to the 40/60 cutoff score determination. In the case of credit that has been granted, extended, or provided on the most favorable material terms to more than 40 percent of consumers, a person may, at its option, set its cutoff score at a point at which the approximate percentage of consumers who historically have been granted, extended, or provided credit on material terms other than the most favorable terms would receive risk-based pricing notices under this section.

(iii) Determining the cutoff score—(A) Sampling approach. A person that currently uses risk-based pricing with respect to the credit products it offers must calculate the cutoff score by considering the credit scores of all or a representative sample of the consumers to whom it has granted, extended, or provided credit for a specific type of credit product.

(B) Secondary source approach in limited circumstances. A person that is a new entrant into the credit business, introduces new credit products, or starts to use risk-based pricing with respect to the credit products it currently offers may initially determine the cutoff score based on information
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derived from appropriate market research or relevant third-party sources for a specific type of credit product, such as research or data from companies that develop credit scores. A person that acquires a credit portfolio as a result of a merger or acquisition may determine the cutoff score based on information from the party which it acquired, with which it merged, or from which it acquired the portfolio.

(C) Recalculation of cutoff scores. A person using the credit score proxy method must recalculate its cutoff score(s) no less than every two years in the manner described in paragraph (b)(1)(iii)(A) of this section. A person using the credit score proxy method using market research, third-party data, or information from a party which it acquired, with which it merged, or from which it acquired the portfolio as permitted by paragraph (b)(1)(iii)(B) of this section generally must calculate a cutoff score(s) based on the scores of its own consumers in the manner described in paragraph (b)(1)(iii)(A) of this section within one year after it begins using a cutoff score derived from market research, third-party data, or information from a party which it acquired, with which it merged, or from which it acquired the portfolio. If such a person does not grant, extend, or provide credit to new consumers during that one-year period such that it lacks sufficient data with which to recalculate a cutoff score based on the credit scores of its own consumers, the person may continue to use a cutoff score derived from market research, third-party data, or information from a party which it acquired, with which it merged, or from which it acquired the portfolio. A person that generally uses two or more credit scores in setting the material terms of credit granted, extended, or provided to a consumer must determine the cutoff score using the same method the person uses to evaluate multiple scores when making credit decisions. These evaluation methods may include, but are not limited to, selecting the low, median, high, most recent, or average credit score of each consumer to whom it grants, extends, or provides credit. If a person that uses two or more credit scores does not consistently use the same method for evaluating multiple credit scores (e.g., if the person sometimes chooses the median score and other times calculates the average score), the person must determine the cutoff score using a reasonable means. In such cases, use of any one of the methods that the person regularly uses or the average credit score of each consumer to whom it grants, extends, or provides credit is deemed to be a reasonable means of calculating the cutoff score.

(iv) Credit score not available. For purposes of this section, a person using the credit score proxy method who grants, extends, or provides credit to a consumer for whom a credit score is not available must assume that the consumer receives credit on material terms that are materially less favorable than the most favorable credit terms offered to a substantial proportion of consumers from or through that person and must provide a risk-based pricing notice to the consumer.

(v) Examples. (A) A credit card issuer engages in risk-based pricing and the annual percentage rates it offers to consumers are based in whole or in part on a credit score. The credit card issuer takes a representative sample of the credit scores of consumers to whom it issued credit cards within the preceding three months. The credit card issuer determines that approximately 40 percent of the sampled consumers have a credit score at or above 720 (on a scale of 350 to 850) and approximately 60 percent of the sampled consumers have a credit score below 720. Thus, the card issuer selects 720 as its cutoff score. A consumer applies to the credit card issuer for a credit card. The card issuer obtains a credit score for the consumer. The consumer’s credit score is 700. Since the consumer’s 700 credit score falls below the 720 cutoff score, the credit card issuer must provide a
(B) A credit card issuer engages in risk-based pricing, and the annual percentage rates it offers to consumers are based in whole or in part on a credit score. The credit card issuer takes a representative sample of the consumers to whom it issued credit cards over the preceding six months. The credit card issuer determines that approximately 80 percent of the sampled consumers received credit at its lowest annual percentage rate, and 20 percent received credit at a higher annual percentage rate. Approximately 80 percent of the sampled consumers have a credit score at or above 750 (on a scale of 350 to 850), and 20 percent have a credit score below 750. Thus, the card issuer selects 750 as its cutoff score. A consumer applies to the credit card issuer for a credit card. The card issuer obtains a credit score for the consumer. The consumer’s credit score is 740. Since the consumer’s 740 credit score falls below the 750 cutoff score, the credit card issuer must provide a risk-based pricing notice to the consumer.

(C) An auto lender engages in risk-based pricing, obtains credit scores from one of the nationwide consumer reporting agencies, and uses the credit score proxy method to determine which consumers must receive a risk-based pricing notice. A consumer applies to the auto lender for credit to finance the purchase of an automobile. A credit score about that consumer is not available from the consumer reporting agency from which the lender obtains credit scores. The lender nevertheless grants, extends, or provides credit to the consumer. The lender must provide a risk-based pricing notice to the consumer.

(2) Tiered pricing method—(i) In general. A person that sets the material terms of credit granted, extended, or provided to a consumer by placing the consumer within one of a discrete number of pricing tiers for a specific type of credit product, based in whole or in part on a consumer report, may comply with the requirements of paragraph (a) of this section by providing a risk-based pricing notice to each consumer who is not placed within the top pricing tier or tiers, as described below.

(ii) Four or fewer pricing tiers. If a person using the tiered pricing method has four or fewer pricing tiers, the person complies with the requirements of paragraph (a) of this section by providing a risk-based pricing notice to each consumer to whom it grants, extends, or provides credit who does not qualify for the top tier (that is, the lowest-priced tier). For example, a person that uses a tiered pricing structure with annual percentage rates of 8, 10, 12, and 14 percent would provide the risk-based pricing notice to each consumer to whom it grants, extends, or provides credit at annual percentage rates of 10, 12, and 14 percent.

(iii) Five or more pricing tiers. If a person using the tiered pricing method has five or more pricing tiers, the person complies with the requirements of paragraph (a) of this section by providing a risk-based pricing notice to each consumer to whom it grants, extends, or provides credit who does not qualify for the top two tiers (that is, the two lowest-priced tiers) and any other tier that, together with the top tiers, comprise no less than the top 30 percent but no more than the top 40 percent of the total number of tiers. Each consumer placed within the remaining tiers must receive a risk-based pricing notice. For example, if a person has nine pricing tiers, the top three tiers (that is, the three lowest-priced tiers) comprise no less than the top 30 percent but no more than the top 40 percent of the tiers. Therefore, a person using this method would provide a risk-based pricing notice to each consumer to whom it grants, extends, or provides credit who is placed within the bottom six tiers.

(c) Application to credit card issuers—(1) In general. A credit card issuer subject to the requirements of paragraph (a) of this section may use one of the methods set forth in paragraph (b) of this section to identify consumers to whom it must provide a risk-based pricing notice. Alternatively, a credit card issuer may satisfy its obligations under paragraph (a) of this section by providing a risk-based pricing notice to a consumer when—

(i) A consumer applies for a credit card either in connection with an application program, such as a direct-
mail offer or a take-one application, or
in response to a solicitation under 12
CFR 226.5a, and more than a single pos-
sible purchase annual percentage rate
may apply under the program or solici-
tation; and
(ii) Based in whole or in part on a
consumer report, the credit card issuer
provides a credit card to the consumer
with an annual percentage rate ref-
erenced in §640.2(n)(1)(ii) that is greater
than the lowest annual percentage rate referenced in §640.2(n)(1)(ii) avail-
able in connection with the application
or solicitation.

(2) No requirement to compare different
offers. A credit card issuer is not sub-
ject to the requirements of paragraph (a)
of this section and is not required to
provide a risk-based pricing notice to a consumer if—
(i) The consumer applies for a credit
card for which the card issuer provides
a single annual percentage rate ref-
erenced in §640.2(n)(1)(ii), excluding a
temporary initial rate that is lower
than the rate that will apply after the
temporary rate expires and a penalty
rate that will apply upon the occur-
rence of one or more specific events,
such as a late payment or an extension
of credit that exceeds the credit limit; or
(ii) The credit card issuer offers the
consumer the lowest annual percentage rate referenced in §640.2(n)(1)(ii) avail-
able under the credit card offer for
which the consumer applied, even if a
lower annual percentage rate ref-
erenced in §640.2(n)(1)(ii) is available
under a different credit card offer
issued by the card issuer.

(3) Examples. (i) A credit card issuer
sends a solicitation to the consumer
that discloses several possible purchase
annual percentage rates that may
apply, such as 10, 12, or 14 percent, or a
range of purchase annual percentage
rates from 10 to 14 percent. The con-
sumer applies for a credit card in re-
sponse to the solicitation. The card
issuer provides a credit card to the con-
sumer with a purchase annual percent-
age rate of 12 percent based in whole or
in part on a consumer report. Unless an
exception applies under §640.5, the card
issuer may satisfy its obligations under
paragraph (a) of this section by pro-
viding a risk-based pricing notice to
the consumer because the consumer re-
ceived credit at a purchase annual per-
centage rate greater than the lowest
purchase annual percentage rate avail-
able under that solicitation.

(ii) The same facts as in the example
in paragraph (c)(3)(i) of this section,
except that the card issuer provides a
credit card to the consumer at a pur-
chase annual percentage rate of 10 per-
cent. The card issuer is not required to
provide a risk-based pricing notice to the
consumer even if, under a different
credit card solicitation, that consumer
or other consumers might qualify for a
purchase annual percentage rate of 8 per-
cent.

(d) Account review—(1) In general. Ex-
cept as otherwise provided in this part,
a person is subject to the requirements
of paragraph (a) of this section and
must provide a risk-based pricing no-
tice to a consumer in the form and
manner required by this part if the per-
son—
(i) Uses a consumer report in connec-
tion with a review of credit that has
been extended to the consumer; and
(ii) Based in whole or in part on the
consumer report, increases the annual
percentage rate (the annual percentage
rate referenced in §640.2(n)(1)(ii) in the
case of a credit card).

(2) Example. A credit card issuer peri-
odically obtains consumer reports for
the purpose of reviewing the terms of
credit it has extended to consumers in
connection with credit cards. As a re-
result of this review, the credit card
issuer increases the purchase annual
percentage rate applicable to a con-
sumer’s credit card based in whole or
in part on information in a consumer
report. The credit card issuer is subject
to the requirements of paragraph (a) of
this section and must provide a risk-
based pricing notice to the consumer.

§640.4 Content, form, and timing of
risk-based pricing notices.

(a) Content of the notice—(1) In gen-
eral. The risk-based pricing notice re-
quired by §640.3(a) or (c) must include:
(i) A statement that a consumer re-
port (or credit report) includes infor-
mation about the consumer’s credit
history and the type of information in-
cluded in that history;