

FEDERAL RESERVE SYSTEM

12 CFR Part 222

Regulation V; Docket No. R-1187

Fair Credit Reporting Act

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final Rule.

SUMMARY: The Board is publishing revisions to Regulation V, which implements the Fair Credit Reporting Act. The revisions add model notices that financial institutions may use to comply with the notice requirement relating to furnishing negative information contained in section 217 of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act). Section 217 of the FACT Act amends the FCRA to provide that if any financial institution (1) extends credit and regularly and in the ordinary course of business furnishes information to a nationwide consumer reporting agency, and (2) furnishes negative information to such an agency regarding credit extended to a customer, the institution must provide a clear and conspicuous notice about furnishing negative information, in writing, to the customer. Section 217 defines the term “financial institution” to have the same meaning as in the privacy provisions of the Gramm-Leach-Bliley Act. The Board’s model notices may be used by all financial institutions, as defined by section 217.

DATES: The rule is effective July 16, 2004.

FOR FURTHER INFORMATION CONTACT: Krista P. DeLargy, Senior Attorney, or David A. Stein, Counsel, Division of Consumer and Community Affairs, at (202) 452-3667 or 452-2412; or Thomas E. Scanlon, Counsel, Legal Division, at (202) 452-3594; for users of Telecommunications Device for the Deaf (“TDD”) only, contact (202) 263-4869.

SUPPLEMENTARY INFORMATION:

I. Background

On December 4, 2003, the President signed into law the FACT Act, which amends the FCRA. Pub. L. 108-159, 117 Stat. 1952. In general, the FACT Act enhances the ability of consumers to combat identity theft, increases the accuracy of consumer reports, and allows consumers to exercise greater control regarding the type and amount of marketing solicitations they receive. The FACT Act also restricts the use and disclosure of sensitive medical information. To bolster efforts to improve financial

literacy among consumers, the FACT Act creates a new Financial Literacy and Education Commission empowered to take appropriate actions to improve the financial literacy and education programs, grants, and materials of the Federal government. Lastly, the FACT Act establishes uniform national standards in key areas of regulation regarding consumer report information.

Section 217 of the FACT Act requires that if any financial institution (1) extends credit and regularly and in the ordinary course of business furnishes information to a nationwide consumer reporting agency, and (2) furnishes negative information to such an agency regarding credit extended to a customer, the institution must provide a clear and conspicuous notice about furnishing negative information, in writing, to the customer. Section 217 defines the term “negative information” to mean information concerning a customer’s delinquencies, late payments, insolvency, or any form of default. The term “credit” is defined under the FACT Act to have the same meaning as in section 702 of the Equal Credit Opportunity Act, which defines “credit” to mean “the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment or to purchase property or services and defer payment therefor.” 15 U.S.C. 1691a. The provisions in Section 217 will become effective December 1, 2004. 69 FR 6526, (February 11, 2004).

Section 217 specifies that an institution must provide the required notice to the customer prior to, or no later than 30 days after, furnishing the negative information to a nationwide consumer reporting agency. After providing the notice, the institution may submit additional negative information to a nationwide consumer reporting agency with respect to the same transaction, extension of credit, account, or customer without providing additional notice to the customer. If a financial institution has provided a customer with a notice prior to the furnishing of negative information, the institution is not required to furnish negative information about the customer to a nationwide consumer reporting agency. A financial institution generally may provide the notice about furnishing negative information on or with any notice of default, any billing statement, or any other materials provided to the customer, so long as the notice is clear and conspicuous. Section 217 specifically provides, however, that the notice may not be included in the initial disclosures provided under section 127(a) of the Truth in Lending Act (15 U.S.C. 1637(a)).

Section 217 also provides a safe harbor for institutions concerning their efforts to comply with the notice requirement. Section 217 provides that a financial institution shall not be liable for failure to perform the duties required by this section if, at the time of the failure, the institution maintained reasonable policies and procedures to comply with the section or the institution reasonably believed that the institution was prohibited by law from contacting the customer.

Under section 217, the term “financial institution” is defined broadly to have the same meaning as in section 509 of the Gramm-Leach-Bliley Act (GLB Act), which generally defines financial institution to mean “any institution the business of which is engaging in financial activities as described in section 4(k) of the Bank Holding Company Act of 1956,” whether or not affiliated with a bank. 15 U.S.C. 6809(3). Thus,

the term “financial institution” includes not only institutions regulated by the Board and other federal banking agencies, but also includes other financial entities, such as merchant creditors and debt collectors that extend credit and report negative information. 16 CFR 313.3(k), 65 FR 33646, 33655 (May 24, 2000).

Section 217 requires the Board to publish, after notice and comment, a concise model notice not to exceed 30 words in length that financial institutions may, but are not required to, use to comply with the notice requirement. Under section 217, a financial institution shall be deemed to be in compliance with the notice requirement if the institution uses the Board’s model notice, or uses the model notice and rearranges its format.

In April 2004, the Board issued the following proposed model notice: “We [may provide]/[have provided] information to credit bureaus about an insolvency, delinquency, late payment, or default on your account to include in your credit report.” 69 FR 19123 (April 12, 2004). The Board received approximately 50 comment letters in response to the proposal. Around 40 letters were submitted by financial institutions and their representatives. One letter was received from consumer representatives, two letters from government entities, and six letters from individuals.

II. Comments Received

Comments on the Model Notice

Most commenters suggested that the Board revise the model notice language to enhance the readability and clarity of the disclosure for consumers. In light of these comments and its own analysis, the Board has revised the language of the model notice to make the disclosure more understandable to consumers. As discussed in more detail below, the final rule provides two model notices – one that may be used by a financial institution if the institution provides the notice in advance of providing negative information to a consumer reporting agency, and one that can be used if an institution provides the notice after providing negative information to a consumer reporting agency. The Board found it more useful to craft a precise, focused notice for each situation, rather than providing one model notice for use in both situations.

Several commenters also requested additional guidance from the Board on use of the model notices. Several commenters asked the Board to incorporate into the regulation the safe harbor for use of the model notice that is contained in section 217. The safe harbor in section 217 essentially provides that a financial institution shall be deemed to be in compliance with the notice requirement relating to furnishing negative information if the institution uses the model notice issued by the Board, or uses such model notice and rearranges its format. Several commenters also requested guidance on how financial institutions may rearrange the format of the model notice without losing the safe harbor from liability provided by the model notice. The Board has incorporated the safe harbor into the text of the regulation, and has provided additional guidance on use of the model notices.

Comments on Other Substantive Issues

Many commenters also asked the Board to provide guidance on a number of substantive issues raised by section 217 that are not related to the contents of the model notice. For example, several commenters asked the Board to clarify issues relating to existing customers, such as whether the notice should be given to existing customers, or whether a substantially similar notice previously given to existing customers is sufficient to satisfy the notice requirement. In addition, some commenters asked the Board to clarify the timing of the notice. Consumer groups asked the Board to make clear that the notice may only be sent to consumers about whom there is negative information that the financial institution either intends to send to credit bureaus or has sent to credit bureaus. On the other hand, several industry commenters wanted clarification that the notice may be delivered at any time prior to the furnishing of negative information, and may be included on credit applications, loan closing documents, or with periodic notices (such as a privacy notice).

The final rule does not address substantive issues raised by commenters that are not related to the contents of the model notice. Such issues are beyond the scope of this rulemaking. Under section 217, the Board was given authority to issue model notices, and certain guidance relating to the model notices, but was not given the authority to issue general regulations implementing section 217. Section 621(e) of the FCRA provides the banking agencies (the Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation and the Office of Thrift Supervision) with the authority to prescribe joint regulations necessary to carry out the purposes of the FCRA, including section 217 which amends the FCRA. 15 U.S.C. 1681s(e). The Board will share with the other banking agencies the comments the Board received on substantive issues not related to the contents of the model notice.

III. Section by Section Analysis

Section 222.1 Purpose, scope, and effective dates

The Board proposed paragraph 222.1(b)(2) to clarify the scope of the Board's Regulation V, which implements the FCRA. Generally, the Board's Regulation V covers the institutions under the Board's jurisdiction. 15 U.S.C. 1681s(e). Nonetheless, the Board proposed paragraph (b)(2) to specify that the Board's model notice in Appendix B relating to furnishing of negative information may be used by all financial institutions (as that term is defined in section 509 of the GLB Act) to comply with the notice requirement contained in section 217 of the FACT Act. The Board received no comments on the proposed paragraph 222.1(b)(2). The Board is adopting this provision with several technical revisions. The Board has revised paragraph (b)(2)(i) to reflect more accurately the institution's under the Board's jurisdiction. In addition, the Board has revised paragraph (b)(2)(ii) to pluralize the reference to model notices.

Appendix B – Model Notice of Furnishing Negative Information

The Board proposed the following model notice that financial institutions may use to comply with the notice requirement under section 217 of the FACT Act: “We [may provide]/[have provided] information to credit bureaus about an insolvency, delinquency, late payment, or default on your account to include in your credit report.” 69 FR 19123 (April 12, 2004).

Model Notice Language

Most commenters suggested that the Board revise the model notice language to enhance the readability and clarity of the disclosure for consumers. Many commenters provided suggested language on how the model notice should be revised to achieve this goal. In light of these comments and its own analysis, the Board has revised the language of the model notice to make the disclosure more useful and more understandable to consumers.

Appendix B provides two model notices. Model Notice B-1 may be used by financial institutions that give the notice prior to furnishing negative information to a consumer reporting agency. This model notice reads: “We may report information about your account to credit bureaus. Late payments, missed payments, or other defaults on your account may be reflected in your credit report.” This model notice has a Flesch readability score of 52.1, and a Flesch-Kincaid grade level score of 9.3. (The proposed model notice has a Flesch readability score of 27.5, and a Flesch-Kincaid grade level score of 12.0.) Model Notice B-2 may be used by financial institutions that give the notice after furnishing negative information to a consumer reporting agency. This model notice reads: “We have told a credit bureau about a late payment, missed payment or other default on your account. This information may be reflected in your credit report.” This model notice has a Flesch readability score of 58.3, and a Flesch-Kincaid grade level score of 8.4.

In commenting on the proposed model notice, both consumer groups and industry commenters believed that the terms “delinquency” and “insolvency” are not readily understandable to consumers. In addition, several industry commenters noted that they were not aware that financial institutions furnished information about “insolvency” of a customer to credit bureaus. Several industry commenters suggested that the model notice should simply use the terms “late payment” and “default” because they believed those terms are understandable to consumers, and would be sufficient to convey to the customer the types of negative information that the furnisher may provide. Consumer groups suggested including the language “late payments, missed payments, or partial payments, other default or bankruptcy” as specific examples of the negative information furnished by financial institutions. Model Notices B-1 and B-2 use the terms “late payment(s),” “missed payment(s),” and “other default(s).” The Board believes that these terms are understandable to consumers, and adequately convey to customers the types of negative information that furnishers may provide to consumer reporting agencies.

Several industry commenters also believed that the proposed language may imply to customers that a financial institution only provides information about an “insolvency, delinquency, late payment, or default” to a consumer reporting agency. These commenters pointed out that many financial institutions report more than these four types of information to consumer reporting agencies; many institutions furnish both positive and negative information on accounts. These commenters suggested that the Board adopt model notice language that more accurately reflects the nature of a financial institution’s likely behavior with respect to furnishing information to consumer reporting agencies. As revised, the Board believes that the language of Model Notice B-1 no longer suggests that a financial institution only provides information about “insolvency, delinquency, late payment, or default” to a consumer reporting agency.

Several industry commenters suggested that the Board delete the last clause – “to include in your credit report” – from the proposed model notice because the furnisher of negative information is not responsible for deciding whether such information is, in fact, included in the relevant credit reports. The Board has revised the language of Model Notices B-1 and B-2 so the model notices no longer imply that negative information will be included in the credit report. Nonetheless, these model notices still include a reference to a customer’s credit report – indicating that negative information may be reflected in the customer’s credit report. The Board believes that it is important to alert customers to the possible consequences of negative information being furnished to credit bureaus.

Several industry commenters asked the Board to provide multiple model notices that would give financial institutions options from which to choose when providing the required disclosures to customers. The Board believes that the two model notices given in Appendix B are sufficient. The Board notes that financial institutions may, but are not required to, use the model notices issued by the Board to meet the notice requirement contained in section 217.

Consumer groups requested that the Board require financial institutions to take certain steps to make the disclosure readily noticeable. These groups suggested that the Board require the disclosure to be on the front page of the notice or billing statement, and require it to be in bold face type and in larger print than the information that accompanies it. The Board notes that section 217 requires financial institution to provide the notice of furnishing negative information in a clear and conspicuous manner. The Board does not believe it is necessary to place additional format requirements on financial institutions that decide to use the model notices to meet the notice requirements.

Safe Harbor and Additional Guidance on Use of Model Notices

Several commenters requested additional guidance from the Board on use of the model notices. Several commenters asked the Board to incorporate into the regulation the safe harbor relating to use of the model notice contained in the statute. In particular, section 217 provides that a financial institution may, but is not required to, use the model notice issued by the Board. Section 217 also provides that a financial institution shall be deemed to be in compliance with the notice requirement relating to furnishing negative information contained in section 217 if the institution uses the model notice issued by the

Board, or uses such model notice and rearrange its format. Several commenters believed it would be helpful to include this safe harbor in the text of the regulation, because many examiners and financial institutions use the regulation as a point of reference.

Some commenters also requested guidance on how financial institutions may rearrange the format of the model notices without losing the safe harbor from liability provided by the model notices. In particular, these commenters requested clarification that the critical elements of the model notice's reference to late payment, default, and reporting to a credit bureau may be rearranged or combined with other language and still come within the safe harbor of the model notice, provided that the meaning of the model notice is retained.

In light of these comments and its own analysis, the Board has revised Appendix B to incorporate the safe harbor contained in section 217, and to provide additional guidance on the use of the model notices. In particular, Appendix B provides that although use of the model notices is not required, a financial institution shall be deemed to be in compliance with the notice requirement if the institution properly uses the model notices in Appendix B. In addition, Appendix B provides that financial institutions may make certain changes to the language or format of the model notices without losing the safe harbor from liability provided by the model notices. Appendix B provides examples of acceptable changes, including rearranging the order of the references to "late payment(s)" and "missed payment(s)," or pluralizing the terms "credit bureau," "credit report" and "account" as used in the model notices. Nonetheless, Appendix B provides that changes to the model notices may not be so extensive as to affect the substance, clarity, or meaningful sequence of the language in the model notices. Financial institutions making such extensive revisions will lose the safe harbor from liability that Appendix B provides.

IV. Regulatory Flexibility Analysis

In accordance with section 3(a) of the Regulatory Flexibility Act, the Board has certified that the final revisions to Regulation V relating to the model notices will not have a significant economic impact on small entities. Section 217 of the FACT Act amends the FCRA to provide that if any financial institution (1) extends credit and regularly and in the ordinary course of business furnishes information to a nationwide consumer reporting agency, and (2) furnishes negative information to such an agency regarding credit extended to a customer, the institution must provide a clear and conspicuous notice about furnishing negative information, in writing, to the customer. Section 217 defines the term "financial institution" to have the same meaning as in the privacy provisions of the Gramm-Leach-Bliley Act. Thus, the term "financial institution" includes not only institutions regulated by the Board and other federal banking agencies, but also includes other financial entities, such as merchant creditors and debt collectors that extend credit and report negative information.

The final revisions to Regulation V would provide financial institutions with model notices (provided in Appendix B) that they may use to comply with the notice requirement under section 217 of the FACT Act relating to furnishing negative

information. The final revisions to Regulation V also would provide financial institutions with additional guidance on how to use these model notices.

The final revisions to Regulation V relating to the model notices are not expected to have a significant economic impact on small entities. By providing model notices and additional guidance on use of the model notices, the Board has minimized the burden imposed on financial institutions by the notice requirement contained in section 217 of the FACT Act. A financial institution that properly uses the model notices in Appendix B will be deemed to be in compliance with the notice requirement of section 217. The Board also notes that the revisions to Regulation V do not require financial institutions to use the model notices. Financial institutions may, but are not required to, use the model notices in Regulation V to meet the notice requirement contained in section 217.

V. Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3506; 5 CFR 1320 Appendix A.1), the Board reviewed the final rule under the authority delegated to the Board by the Office of Management and Budget (OMB). The Federal Reserve may not conduct or sponsor, and an organization is not required to respond to, this information collection unless it displays a currently valid OMB control number. The OMB control number for this final rule is 7100-0308.

The collection of information involved in this rulemaking is found in section 217 of the FACT Act, Pub. L. 108-159, 117 Stat. 1952. This information is mandatory for financial institutions that furnish negative information to credit bureaus regarding credit extended to customers. The respondents are financial institutions as defined in the privacy provisions of the GLB Act. The term “financial institution” includes not only institutions regulated by the Board and other federal banking agencies, but also includes other financial entities, such as merchant creditors and debt collectors that extend credit and report negative information.

The final revisions to Regulation V would provide financial institutions with model notices (provided in Appendix B) that they may use to comply with the notice requirement under section 217 of the FACT Act relating to furnishing negative information. The final revisions to Regulation V also would provide additional guidance to financial institutions on how to use these model notices.

The estimated annual burden for financial institutions is approximately 240,000 hours. Financial institutions would face a one-time burden to reprogram and update systems to include the new notice requirement. With respect to financial institutions, approximately 30,000 furnish information to consumer reporting agencies. The estimated time to update systems is approximately 8 hours (one business day). In conjunction with the proposed revisions to Regulation V, the Board sought comment on the burden estimate for the proposed changes. The Board did not receive any comments specifically responding to the paperwork reduction analysis published with the proposed rule.

List of Subjects in 12 CFR Part 222

Banks, banking, Holding companies, state member banks.

For the reasons set forth in the preamble, the Board proposes to amend Regulation V, 12 CFR part 222, as set forth below:

PART 222 – FAIR CREDIT REPORTING (REGULATION V)

1. The authority citation for part 222 is revised to read as follows:

Authority: 15 U.S.C. 1681s; Secs. 3 and 217, Pub. L. 108-159; 117 Stat. 1953, 1986-88.

2. Section 222.1 is revised by adding a new paragraph (b) to read as follows:

Subpart A—General Provisions

§ 222.1 Purpose, scope, and effective dates.

* * * * *

(b) Scope.

(1) [reserved]

(2) Institutions covered.

(i) Except as otherwise provided in paragraph (b)(2), these regulations apply to banks that are members of the Federal Reserve System (other than national banks), branches and Agencies of foreign banks (other than Federal branches, Federal Agencies, and insured State branches of foreign banks), commercial lending companies owned or controlled by foreign banks, organizations operating under section 25 or 25A of the Federal Reserve Act (12 U.S.C. 601 et seq., and 611 et seq.), and bank holding companies and affiliates of such holding companies (other than depository institutions and consumer reporting agencies).

(ii) For purposes of Appendix B, financial institutions as defined in section 509 of the Gramm-Leach-Bliley Act (12 U.S.C. 6809), may use the model notices in Appendix B of this part to comply with the notice requirement in section 623(a)(7) of the Fair Credit Reporting Act (15 U.S.C. 1681s-2(a)(7)).

* * * * *

3. Part 222 is revised by adding a new Appendix B to read as follows:

APPENDIX A – [Reserved]

APPENDIX B – Model Notices of Furnishing Negative Information

a. Although use of the model notices is not required, a financial institution that is subject to section 623(a)(7) of the FCRA shall be deemed to be in compliance with the notice requirement in section 623(a)(7) of the FCRA if the institution properly uses the model notices in this appendix (as applicable).

b. A financial institution may use Model Notice B-1 if the institution provides the notice prior to furnishing negative information to a nationwide consumer reporting agency.

c. A financial institution may use Model Notice B-2 if the institution provides the notice after furnishing negative information to a nationwide consumer reporting agency.

d. Financial institutions may make certain changes to the language or format of the model notices without losing the safe harbor from liability provided by the model notices. The changes to the model notices may not be so extensive as to affect the substance, clarity, or meaningful sequence of the language in the model notices. Financial institutions making such extensive revisions will lose the safe harbor from liability that this appendix provides. Acceptable changes include, for example,

1. Rearranging the order of the references to “late payment(s),” or “missed payment(s)”
2. Pluralizing the terms “credit bureau,” “credit report,” and “account”
3. Specifying the particular type of account on which information may be furnished, such as “credit card account”
4. Rearranging in Model Notice B-1 the phrases” information about your account” and “to credit bureaus” such that it would read “We may report to credit bureaus information about your account.”

Model Notice B-1

We may report information about your account to credit bureaus. Late payments, missed payments, or other defaults on your account may be reflected in your credit report.

Model Notice B-2

We have told a credit bureau about a late payment, missed payment or other default on your account. This information may be reflected in your credit report.

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By order of the Board of Governors of the Federal Reserve System, June 8, 2004.

Jennifer J. Johnson (signed)

Jennifer J. Johnson
Secretary of the Board