July 23, 2004

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
Office of the Secretary
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551
Attention: Docket No. OP-1195

RE: Request for Information for Study on Prescreened Solicitations or Firm Offers of Credit or Insurance- Comments of the American Financial Services Association

Dear Ladies and Gentlemen:

The American Financial Services Association ("AFSA") appreciates the opportunity to comment on issues raised by the Board of Governors of the Federal Reserve System with respect to the study concerning prescreened solicitations pursuant to section 213(e) of the Fair and Accurate Credit Transaction Act ("FACT Act") of 2003. The FACT Act requires the Board to conduct a study of the potential impact that any further restrictions on providing consumers with prescreened solicitation would have on consumers.

Preface

Many AFSA members are big users of, and enthusiastic proponents of prescreening systems. Why? The reason is that effective prescreening systems directly result in the highest number of qualified individuals applying for and receiving credit products offered by the creditor. This process directly results in lower customer acquisition costs, which reduces the overall costs of doing business, and hence enhances the profitability of AFSA members. In a highly competitive credit marketplace, the more efficient a creditor can become in identifying and acquiring customers while at the same time striving to become the lowest cost provider, it is clear that the use of effective systems such as prescreening yields substantial benefits to the creditor.

But, what about the consumer? AFSA asserts that, as a consequence of prescreening systems, consumers receive direct and derivative benefits in the form of lower costs, access to providers with whom they might not have otherwise considered doing business, and, almost paradoxically, a *decreased* amount of unwanted business marketing communications. In short, prescreening is one of the most highly effective, cost efficient and minimally intrusive forms of direct marketing.

In order to avoid submitting an unmitigated "cheerleading" comment letter extolling the "win-win" benefits of prescreening, we do want to comment in a manner befitting the seriousness of the issue, on the potential "adverse effects" inquiry that the Board has posed for comment. AFSA does want to address what we would characterize as *the most important* question in the series of questions posed by the Board. That is, what costs and adverse effects do consumers incur as a result of prescreening? The subset of the question is whether prescreening is a significant factor in identity theft.

AFSA maintains that there are few if any adverse effects to consumers as a result of receiving prescreening solicitations. Moreover, the evidence demonstrates that prescreening is not a significant factor in contributing to the problem of identity theft.

There are consumers who do not wish to receive unwanted mail, and may consider this to be an adverse effect worthy of regulatory action. We do not agree. In our society, there are a number of "trade-offs" that must be considered before adopting and acting on a view held by a vast *minority* of individuals. For example, there are a number of individuals who do not like television advertisements. On the other hand, we would surmise that most of these individuals (whom we have already identified as television viewers, given the fact that they dislike television advertisements), would be horrified at the prospect of not having the option of "free" television reception. Obviously, it is the existence of television advertising which permits the option of "free" television reception. This is an example of a "trade-off" which we believe most people would agree has been, on balance, a good deal for television viewers.

Similarly, those who object to receiving prescreening solicitations on the grounds that they do not like receiving excessive "junk mail", or on the basis of some kind of inchoate privacy concern, are also experiencing the benefits of a "trade-off". Creditors do not want to send such solicitations to these individuals any more than these consumers do not want to receive the solicitations. However, just as television viewers can "click" off a TV commercial, systems have been developed to allow consumers to minimize the amount of unwanted solicitations they receive through the "opt-out" process. Meanwhile, the cost benefits of prescreening systems which directly lead to reduced costs for credit products in what is undeniably a highly competitive marketplace, is, at the end of the day, a "good deal" for consumers.

Everybody would agree that the most pernicious adverse effect of prescreening would be identity theft, *if*, in fact, that was the case. However, there is scant evidence of any relationship between prescreening and identity theft. Any *ad hominem* assertions to the contrary by any commenter should be closely examined by the Board. If the Board concludes that sufficient uncertainty exists as to the relationship between prescreening and identity theft, AFSA hereby requests that the Board conduct a hearing to examine the issue. Such a hearing should include not only witnesses who purport to have evidence of a clear and uncorrectable linkage between prescreening and identity theft, but also representatives from Federal and State Law Enforcement agencies who can either conclusively establish or debunk the existence of any relationship between prescreening and identity theft. AFSA does not believe such a relationship between prescreening and identity theft exists to any significant extent. However, we would nevertheless welcome the opportunity to have the question more closely examined in a fact-finding inquiry held in connection with a public hearing conducted by the Board.

Interest of AFSA

AFSA, as the national trade association for consumer credit providers, would like to specifically address the benefits consumers receive from prescreened solicitations. The credit products offered by AFSA's members include personal loans, first and second mortgage loans, home equity lines of credit, credit card accounts, retail sales financing and credit insurance. Many of our members use the prescreening process as a way of identifying potential customers, targeting solicitations, and offering a variety of products at competitive prices.

AFSA references several studies in this letter and fully supports the findings of these studies. In 2002 the Privacy Leadership Initiative released a report by Michael Staten and Fred Cate entitled "*The Adverse Impact of Opt-In Privacy Rules on Consumers: A Case Study of Retail Credit*" and in 2003 the Information Policy Institute released a study entitled "*Access, Efficiency & Opportunity*". AFSA supports the research methodology used in these studies, and encourages the Federal Reserve Board to consult their conclusions.

Overview of Prescreening

Prescreening is the practice by which a creditor provides consumer credit criteria to a Consumer Reporting Agency ("CRA") to solicit new business. The CRA will use its files to create and sell lists of consumers who meet the particular underwriting criteria issued by a creditor. After receiving a list, the creditor will then extend a "firm offer of credit". Under the Fair Credit Reporting Act ("FCRA") credit grantors and insurers who obtain such lists, with very limited exceptions, are required to provide all of the individuals on the list a firm offer of credit.

When a consumer receives a pre-selected credit offer, the company who sent the offer is legally required to extend a line of credit *if* the consumer still meets the predetermined criteria and furnishes the necessary documentation.

The prescreening process contains additional consumer protections:

- Consumer credit information is summarized and coded for confidentiality.
- Federal law requires credit grantors to extend credit in a fair and consistent manner. They cannot consider such factors as sex, marital status, race or religion.

Responses to Board's Questions

1. "What statutory or voluntary mechanisms are available to a consumer to notify lenders and insurance providers that the consumer does not wish to receive prescreened solicitations?

The Background "Supplementary Information" accompanying the Board's "Request for Information for Study on Prescreened Solicitations or Firm Offers of Credit and Insurance" appears to accurately state the current law regarding consumer's rights not to receive prescreened solicitations.

2. "To what extent are consumers currently utilizing existing statutory and voluntary mechanisms to avoid receiving prescreened solicitations?"

We have not been able to empirically ascertain from AFSA's membership the extent to which consumers are using existing mechanisms to avoid receiving prescreened solicitations. While we have some anecdotal knowledge that consumers' use of existing mechanisms to avoid receiving prescreened solicitations is relatively infrequent, AFSA cannot provide useful data in response to this question.

3. "What are the specific benefits to consumers in receiving prescreened solicitations?"

Prescreening has become an integral process in the development and operation of the American credit system. Without the prescreening process, the credit market would be drastically different. Notably, it would be far less efficient in identifying the potential customer who not only may desire a particular credit product being offered, but also qualifies for this given product. "Prime" (as opposed to "subprime" or "nonprime") candidates would receive offers with rates characteristic of non-prime loans, and vice versa. Companies would send out mass solicitations which would only inform a consumer of the existence of products, but not whether the consumer would qualify for such products. Such a system is certain to result in confusion for the consumers as they blindly search through offers and haphazardly apply for credit products. Companies would be forced to send more adverse action notices to consumers as a greater number of consumers apply for credit for which they do not qualify.

More importantly, prescreen solicitations reduces the price of credit for the consumer. The reduction in the price of credit occurs in a variety of ways, as listed below.

(a) *Eases shopping for credit*

Consumers in need of credit have a wealth of options and incentives not possible decades ago. Credit card attributes such as no annual fees, cash back, car rebates, chip technology, college contributions, merchandise rewards, no telemarketing, and home rebates are just a few of the possibilities for which consumers can apply.

With the number of companies in business, and the variety of products offered, the amount of information relating to credit can be overwhelming. The term “credit card” has 14,200,000 links on the internet; “mortgage lending” has 10,700,000, and “auto finance” has 7,370,000 links when typed into the search engine Google. Prescreened solicitations minimize the amount of information a consumer is forced to sift through to obtain the best rate for a mortgage loan, credit card or financing of an automobile.

Prescreening reduces the time-consuming and burdensome process of shopping for credit by delivering the best products at the best prices to the consumer’s mailbox. Without the ability to target potential customers that is currently possible under a system of prescreening, consumers would likely be sent even more solicitations, via mail, phone or email, than they now receive. Such solicitations would be of less interest to the consumer, as an untargeted mass mailing offers little incentive to apply for credit compared to a prescreened solicitation which guarantees the extension of credit.

Without prescreen solicitations, application of credit for consumers would become a guess and check system, whereby consumers would be forced to apply to every company in order to find the best rate for which they qualify. Instead of companies offering their products and services at the best, and often cheapest price, the burden would be placed on a consumer to contact every possible company and apply for a product, in order to determine the best product the consumer is qualified to receive.

(b) *Minimizes the negative impact of shopping for credit*

Not only are consumers saved from the time and hassle of researching the extensive variety of credit products for the best offer and product for which they qualify, prescreened solicitations actually improve a consumer’s credit score. A consumer’s credit report contains a section on all inquiries into the consumer’s credit file for the past two years. A consumer’s FICO score generally decreases as the number of inquiries into the record increases. Consumers searching for the best rate on a product that they receive easily now under prescreened solicitations would actually be harmed by shopping for these rates.

(c) *Expands access to borrowers*

Credit report data reduce redlining by providing creditors with the information necessary to base cost of credit for the consumer on the consumer’s risk profile, as opposed to geography or other types of information. Prescreened information also increases the supply of credit while minimizing the price, thereby allowing for a greater access to credit. Prescreening also allows for consumers to move high-interest loan balances from one credit card to a lower-rate on a different company.

(d) *Fosters competition among businesses*

Companies of all sizes benefit from the ability to solicit specific customers. Smaller companies are able to enter a marketplace that might otherwise be dominated by larger players. Such competition in the marketplace increases access to credit for all consumers and lowers the price of credit.

Competition in the credit card market has lowered interest rates paid by many consumers, saving them billions of dollars, as new companies enter the market and offer credit at better terms to gain new business. According to the IPI study “Access, Efficiency & Opportunity”, assuming constant prices for credit card credit since 1997, consumer savings from the increased competition in the credit card industry is about $30 billion per year from 1998 to 2002.

Prescreened solicitations enable companies to compete with one another to offer the best product at the best price to a consumer. A competitive marketplace offers consumers a wide variety of products and services, while at the same time restricting the price companies are able to charge for credit.

By drastically reducing the cost of assessing the risk of new borrowers, prescreened credit information facilitates the entry of new lenders into the market. At the same time, the cost of credit, as reflected in interest rates and yearly fees, has decreased substantially over time allowing a greater number of individuals access to credit.

(e) *Reduces the costs of finding a borrower*

A study conducted by the Information Policy Institute in 2003 found that in the absence of prescreening, total costs to consumer would increase between $269 million to $1.36 billion per year. These costs stem from the expense of acquiring new customers through different systems of mailings and telephone solicitation.

If issuers could not easily utilize the data sent by CRAs, companies would be forced to market blindly to the general public resulting in more adverse action notices, at a greater expense for the company and frustration for the consumer.

In a study by the Privacy Leadership Initiative, MBNA found that marketing blindly would result in marketing materials being 27 percent less well targeted. As a result, 109 million people who should not have received solicitations would do so.

Prescreening allows companies to carefully and efficiently target customers who would meet their underwriting criteria. Companies are able to offer credit on terms that are unavailable elsewhere, as they are based on the specific individual. Some of the best customer benefits may not be advertised in a mass solicitation, as companies do not want the expense of processing applications, obtaining consumer reports and sending adverse action notices to a large number of unqualified applicants.

4. “What significant costs or other adverse effects, if any, do consumers incur as a result of receiving prescreened solicitations?”

AFSA is not aware of any *significant* (i.e. enough to warrant Board action) costs or adverse effects associated with consumers’ receipt of prescreened solicitations.

5. “What additional restrictions, if any, should be imposed on consumer reporting agencies, lenders, or insurers to restrict the ability of lenders and insurers to provide prescreened solicitations to consumers? How would these additional restrictions benefit consumers? How would these additional restrictions affect the cost consumers pay to obtain credit or insurance, the availability of credit or insurance, consumers’ knowledge about new or alternative products and services, the ability of lenders or insurers to compete with one another, and the ability of creditors or insurers to offer credit or insurance products to consumers who have been traditionally underserved?

AFSA believes that the current regulatory requirements regarding prescreening are more than adequate. Indeed, AFSA submits that the present requirements may be approaching a level where the requirements would fail a “cost/benefit” or “benefit/burden” analysis.

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We appreciate the opportunity to respond to the Notice. If you have any questions about this letter, please contact the undersigned at (202) 466-8606.

Sincerely,

Robert McKew
Senior Vice President and General Counsel
American Financial Services Association