Comment #: 25

919 18th Street, NW
Suite 300
Washington, DC 20006

Jeffrey A. Tassey
Executive Director
Phone: 202-466-8815

America's Community Bankers
TransUnion
State Farm Insurance
USAA
AFSA
Nationwide On Your Side
MetLife
MBNA
CBA Consumer Bankers Association
MasterCard
JPMorganChase
Household
CUNA
GE
Ford Credit
Farmers
ICBA Independent Community Bankers of America
Fair Isaac
Allstate
National Retail Federation

# COALITION TO IMPLEMENT THE FACT ACT

August 16, 2004

Federal Trade Commission
Office of the Secretary
Room H-159 (Annex N)
600 Pennsylvania Ave., N.W.
Washington, DC 20580

Re: FACT Act Scores Study, Matter No. P044804

Dear Sir or Madam:

This comment letter is submitted on behalf of the Coalition to Implement the FACT Act ("Coalition") in response to the Federal Trade Commission's (FTC's) request for public comments on the above-referenced study. Coalition members represent a broad cross-section of financial services companies and associations and are among the nations leading providers of credit and insurance.[1] Each of the Coalition members, or their affiliates, are active participants in the credit reporting system as furnishers and/or users of consumer credit information; all utilize credit-based scores as a part of their underwriting programs; and, all understand the indispensable role scores play in extensions of credit and in providing insurance coverage for automobiles and property and casualty purposes.

The Coalition appreciates the opportunity to comment on the joint FTC-Federal Reserve study of (1) the effects of credit scores and credit-based insurance scores on the availability and affordability of financial products; (2) the statistical relationship, controlling for ECOA prohibited factors, between scores and the quantifiable risks and actual losses experienced by businesses; and, (3) whether the use of scores or specific factors comprising those scores, results in "negative or differential treatment" of ECOA protected classes.

Because Coalition membership is divided between companies that grant credit and companies that provide insurance; because our members use credit-based scores in many different ways for multiple purposes; and, because many different scoring models are utilized by the members, these comments, on behalf of the Coalition in its entirety, are somewhat general in nature. We anticipate that many of the individual members of the Coalition will be filing their own, more detailed comments.

# COALITION TO IMPLEMENT THE FACT ACT

**Summary Views On Study Issues Pertaining To The Effects Of Credit Scores And Credit-Based Insurance Scores On the Availability And Costs Of Credit And Insurance, Including The Ability Of Scores To Predict Risk**

Coalition members share the views of the Chairman of the Federal Reserve Board[2] and senior officials of the Federal Trade Commission[3] that use of credit scores has been of significant benefit to consumers and has contributed greatly to the vitality of our nation's credit markets. With respect to the use of credit-based insurance scores as one of a number of important factors in the underwriting and rating of auto and property & casualty insurance, we share the conclusion of the American Academy of Actuaries (based on its own analysis and its evaluation of four studies on insurance credit scoring), that "credit scoring is an effective tool in the underwriting and rating of personal lines of insurance".[4]

The experience of Coalition companies (confirmed by a number of academic studies) is that credit scores are highly accurate predictors of risk both for credit and insurance purposes; and have been instrumental in allowing financial services companies to increase the availability and decrease the costs of their products and services to consumers (including historically underserved populations). Additionally, the use of credit scores has reduced underwriting costs; allowed credit decisions to be made virtually within minutes of an application; and, in contrast to the old system of manual underwriting of loan decisions - where subjectivity and bias were sometimes difficult to control - provide a fully objective and non-discriminatory basis for determining a consumer's credit worthiness or risk.

The June 18th *Federal Register* request for public comment states that "An effect [ie, the benefits conferred by the use of scores] can often only be measured relative to a counterfactual (that is, relative to some hypothetical alternative situation)". The Coalition believes the evidence of such benefits for credit purposes is so well established that a "counterfactual" may be unnecessary. Nevertheless, if the Federal Reserve and FTC seek additional information, we would suggest consideration of the following possible approaches:

-- **Request That Companies Which Make Extensive Use of Scores Voluntarily Submit "Before & After" Data & Analysis.** Financial services companies which rely on credit-based scores could be asked to voluntarily provide data and analysis relating to the "before and after" effects of the use of scores on (1) the availability and affordability of their products to consumers, including historically underserved populations; (2) the company's costs of underwriting their extensions of credit or insurance; (3) losses; and, (4) the time required to make underwriting decisions.

-- **Manual Re-Underwriting By Lenders.** In connection with the "before and after" analysis referenced in the paragraph above, mortgage lenders and other companies which grant credit might be asked to voluntarily re-underwrite a sample of previous loan applications, both accepted and rejected, which had been manually underwritten. Using data from the original applications, these loans would be re-underwritten using a credit score; and a comparison made between the "accepts" and "rejects" under a manual underwriting system vs. an automated one. Freddie Mac conducted such a re-underwriting study in 2002.

-- **Competition.** An analysis could be performed to determine whether the availability of scores has fostered competition among providers of credit and insurance.

## Summary Views On Study Issues Pertaining To Whether Credit & Insurance Scoring Systems Could Result In "Negative Or Differential Treatment" Of ECOA Protected Classes

With respect to that portion of the study being performed by the Federal Reserve relating to "negative or differential impacts" of credit scoring on protected classes, the Coalition offers the following observations:

First, although the study seeks to address ambitious and important questions, we believe there are extremely difficult and possibly insurmountable obstacles to its proper execution -- obstacles that could undercut the usefulness of the study's findings on the "differential impact" issue. We are concerned, for example, that there may not be publicly available data or reliable proxies that would permit analysis of the relationship between quantifiable risks, credit scores and protected classes. We also wonder about the utility of an analysis conducted on an aggregate basis, given that scores are used differently not only for different financial products but even for the same product offered by different companies; and, given that there are many different score models in use.

Second, analysis of this issue should be performed and understood in the context of the enormous benefits that the use of scores confers on consumers (including historically underserved populations), businesses and the efficiency of the credit markets.

Third, the study should focus on whether scores and their attributes are valid predictors of risk for protected classes. Any findings as to whether the use (or absence) of specific factors results in negative or differential treatment, should include an analysis of whether these factors are nevertheless valid predictors of risk. It is also important, in cnsidering specific information that is not used, whether such information is readily available and in a cost effective manner.

Fourth, when evaluating "negative or differential" effects, we believe it is essential to take into account the financial and other qualifications of applicants. Simple comparisons of credit score distributions across protected classes are misleading, at best, and meaningless, at worst because such comparisons do not involve groups of similarly qualified applicants.

We hope these comments are helpful to the FTC and the Board. Because the Coalition is continuing to collect the views of its members on the credit and insurance score study, we trust we will be able to provide additional and more detailed written comments in the near future.

Sincerely,

Jeffrey A. Tassey

Jeff Tassey,
Executive Director

# COALITION TO IMPLEMENT THE FACT ACT

[1] Members include Allstate Insurance Company, America's Community Bankers, American Financial Services Association, Consumer Bankers Association, Credit Union National Association, Fair Isaac, Farmers Insurance, Ford Motor Credit Company, General Electric Company, HSBC Household, Independent Community Bankers of America, J.P. Morgan Chase & Co., MasterCard International, MBNA, MetLife, National Retail Federation, Nationwide, State Farm Insurance, TransUnion, USAA.

[2] "Credit scoring enables creditors to evaluate, quickly and inexpensively, the risk of lending to virtually any credit applicant, and promotes the making of expedited credit decisions in a safe and sound manner. Consumers benefit from the increased availability and lower cost of credit that results from the use of credit scoring models. Credit scoring also may help to reduce unlawful discrimination in lending to the extent that these systems are designed to evaluate all applicants objectively and thus avoid issues of disparate treatment. As Chairman Greenspan recently noted, 'the emergence of credit scoring technologies...has proven useful in expanding access to credit for us all, including for lower-income populations and others who have traditionally had difficulty obtaining credit. It has also enabled financial institutions to offer a wide variety of customized insurance, credit and other products'." Testimony of Dolores Smith, Director, Division of Consumer and Community Affairs, Federal Reserve Board, before the House Committee on Financial Services, June 4, 2003.

[3] "The modernization of credit reporting has played a key role in providing American consumers rapid access to consumer credit.... Consumers today can use the internet from the comfort of their home to comparison shop for a wide array of credit products and get a virtually instantaneous offer, including rate and other terms.... In each instance, their eligibility for the lowest rate or most favorable terms depends on a sophisticated credit scoring system that produces rapid, reliable scores based on information from a consumer report." Testimony of Howard Beales, Director of the Bureau of Consumer Protection, FTC, before the House Financial Services Committee, June 4, 2003.

[4] Testimony of the National Association of Insurance Commissioners, Before the House Committee On Financial Services, June 4, 2003.