

**FEDERAL RESERVE BANK
OF NEW YORK**

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PRESCREENING UNDER THE FAIR CREDIT REPORTING ACT

*To All State Member Banks, and Others
Concerned, in the Second Federal Reserve District:*

On November 22, 1991, the Federal Financial Institutions Examination Council (FFIEC) issued a policy statement regarding prescreening by financial institutions under the Fair Credit Reporting Act (FCRA). Prescreening is a process by which a consumer reporting agency compiles a list of consumers meeting credit-granting criteria specified by a financial institution; the list is then provided to the institution for use in soliciting specific consumers for credit products. The FFIEC recommended that each of the Federal banking agencies adopt the policy statement.

On January 7, 1992, the Director of the Division of Consumer and Community Affairs, of the Board of Governors of the Federal Reserve System, adopted the policy statement under delegated authority. Enclosed is the text of the statement as it applies to State member banks.

The banking agencies received numerous inquiries about prescreening, especially after the issuance of the Federal Trade Commission's commentary on the FCRA in May 1990. The policy statement addresses a number of these issues. For example, it provides that only under *limited* circumstances may an institution withhold or withdraw an offer of credit to a consumer whose name appears on the list, such as foreclosure, filing for bankruptcy, or garnishment, when these occur *between* the prescreen and the consumer's acceptance. Also, the institution must make a firm offer of credit to all consumers whose names appear on the list; thus the institution would not be permitted to withdraw the offer for failure of the consumer to meet minimum income requirements.

We believe that the policy strikes the proper balance between the need to safeguard the confidentiality of consumer credit information, as provided in the FCRA, and the ability of institutions to minimize the risk of offering credit to non-creditworthy individuals. The policy will be used by our bank examiners to measure the compliance of institutions with the FCRA. Questions regarding this matter may be directed to our Compliance Examinations Department (Tel. No. 212-720-5914).

CHESTER B. FELDBERG,
Executive Vice President.

PRESCREENING BY FINANCIAL INSTITUTIONS UNDER THE
FAIR CREDIT REPORTING ACT

What is prescreening?

Prescreening is a process by which a consumer reporting agency (credit bureau) compiles or edits a list of consumers meeting specific credit-granting criteria provided by an institution. The list is provided to the institution or a third party acting for the institution (for example, a mailing service) for use in soliciting specific consumers for credit products.

Is a prescreen a consumer report?

A prescreened list represents a series of consumer reports since the list conveys that each consumer named on the list meets certain criteria for creditworthiness.

Is prescreening permissible under the FCRA?

While the Fair Credit Reporting Act (FCRA) does not expressly authorize it, prescreening is permissible if the institution follows certain rules. The act permits prescreening if the institution makes a firm offer of credit to each consumer whose name appears on the prescreened list. To obtain a consumer report, the institution must have a "permissible purpose" under the FCRA. Section 604(3)(A) of the FCRA permits an institution to obtain a consumer report if it intends to use the information in connection with a credit

transaction involving the extension of credit to the consumer. (Prescreening cannot be used to solicit responses for insurance, employment or other purposes.) Therefore, an institution cannot use a prescreened list solely to send promotional material.

The purpose of the FCRA is to safeguard the confidentiality of consumer credit information. The statute requires a clear connection between the creditor and consumer before the creditor obtains a credit report. A firm offer of credit to the consumer provides this connection. Permitting the practice of prescreening without this link would be contrary to the purpose of the act.

What controls can the institution use to develop a list?

- o The institution may wish to be specific in the credit-granting criteria it designates for targeting creditworthy consumers. This will ensure that the institution is not obligated to extend credit to individuals who do not meet its standards. In addition, prompt use of the prescreened list after receipt from the credit bureau will further ensure that credit is extended only to individuals meeting the specified standards.

- o The institution may request "tiered" lists that identify consumers with different characteristics, enabling the institution to make different credit offers (e.g., various credit limits).
- o The institution may include demographic analysis, such as geographic data (for example, to establish a service area) or data on income and type of employment (for example, by the use of specialized magazine subscription lists) in the credit-granting criteria. This analysis may be applied by the credit bureau or by a third party after the initial screen. The application of demographic analysis must not have the effect of excluding persons on a prohibited basis.
- o If the institution wishes to limit the number of consumers it makes an offer of credit to, it may request the credit bureau or a third party to make random deletions from the list if it is too lengthy.

In all cases, whether or not an additional screen is obtained (either demographic or random), the institution must make an offer of credit to all consumers whose names appear on the final screened list.

What constitutes an offer of credit?

The institution must make a firm offer of credit to all consumers whose names appear on the screened list. A conditional offer of credit is inadequate since it indicates that the institution does not intend to enter into a credit transaction unless the consumer meets a subsequent condition. For example, imposing a minimum income requirement on the credit application it provides to consumers on the screened list would not be a firm offer of credit.

Can the institution withhold or withdraw an offer of credit to a consumer whose name appears on the list?

Once the consumer has accepted the offer of credit, the institution cannot, except in limited circumstances, withdraw or deny the credit, even when based on new information concerning the consumer. Errors in applying the criteria to the data base of the credit bureau during the prescreening or failure of the prescreening to retrieve all information about the consumer do not qualify as permissible reasons for withdrawing an offer.

Only in certain, specified, rare and unusual circumstances that occur between the prescreen and the consumer's acceptance, may the institution withdraw the offer

of credit. These circumstances include: foreclosure; attachment; garnishment; repossession; charge-offs; filing for bankruptcy; or entry of liens or judgments. These criteria must have been part of the original prescreening in order to qualify as valid reasons for withdrawing or denying the offer.

Other reasons for withdrawal of an offer:

The institution may withdraw the offer if it determines that the consumer:

- o is below the age required to create a valid contract;
- o has moved beyond the institution's service area for the product offered (if the service area is limited); or
- o has fraudulently altered information in the credit report.

Other permissible practices:

- o The institution may initially offer a modest credit limit and then increase the limit after a full credit report has been obtained, if the terms of the initial guaranteed credit are clearly specified. A modest credit limit may not be lower than the usual minimum limit offered for a particular product. Once the consumer has accepted the initial credit offer, the institution may request information verifying income for the purpose of offering a higher credit limit.

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- o The institution may ask for identifying information (such as the home address and social security number) in the offer of credit.
- o The institution may impose a reasonable time limit on the period during which the offer of credit is available. It may treat any response received after the deadline as a regular credit application, and may obtain a full credit report to evaluate the consumer's creditworthiness.
- o Only when the consumer accepts the credit offer may the institution obtain a full credit report on the consumer. The consumer's account may be reviewed regularly and if the consumer does not prove to be creditworthy, the institution may close the account. The institution's timing for closing the account, however, must not make the offer illusory.
- o The institution may prescreen using its own records related to the institution's prior transactions or experiences with particular consumers without making an offer of credit. Any prescreening that uses records held by either subsidiaries or affiliates will trigger coverage by the FCRA.
- o The institution may require consumers accepting prescreened offers to take the steps necessary to create a legal obligation for the credit offered, such as signing a credit contract or security agreement.