# Consumer-Reporting Value Proposition: Consumer Protection, Safety and Soundness, and Economic Implications of Regulated Consumer-Data Collection

**Prepared by the Consumer Data Industry Association**

February 20, 2020

# Executive Summary

The consumer credit reporting system has important positive effects on consumers and the economy, according to a new report. In this report, the Consumer Data Industry Association (CDIA)* for the first time presents a survey of the most authoritative research on U.S. consumer credit reporting in concert with original research based on established, transparent data sources such as those maintained by the Federal Reserve and Bureau of Consumer Financial Protection. This presents a current, thorough assessment of the value proposition of regulated consumer reporting to U.S. consumers, lenders, and economic opportunity. It thus contributes to the literature and policy debate as the first meta-analysis of regulated U.S. consumer reporting to analyze all available research and data with direct, current bearing on the benefits and risks of regulated third-party repositories of personally-identifiable information. To assess the overall U.S. experience in light of other nations with and without regulated consumer reporting, we also present a first-time analysis of international research on consumer reporting provided by the World Bank and other government authorities in concert with relevant academic research.

CDIA and its members believe that sound public policy is best crafted on the basis of thorough, current, and objective analytics. We seek to contribute to policy decisions with the most current and thorough assessment of the U.S. consumer-reporting value proposition of which we are aware.

Key conclusions include:

- Original research based on publicly-available and verifiable data presented here for the first time demonstrates that consumer reporting has direct and meaningful impact on overall U.S. economic opportunity. The more Americans with credit histories that are housed at regulated consumer reporting agencies, the higher grows U.S. employment. Improvements in credit scores are also shown not only to predict increased employment and wages, but also to increase the ability of consumers to open a small business that then employs others.
- Original research in this paper also finds that consumers with more robust credit histories are more confident in their credit search, less financially fragile, and better able to meet both planned and unplanned financial needs. This clearly enhances consumer well-being in addition to economic opportunity and growth.
- Although challenges continue based on increased cyber threats and other operational risks, current law and rule provide such robust consumer protections for data housed in consumer reporting agencies that the U.S. Government Accountability Office has urged like-kind standards for large technology companies and others who hold certain personally-identifiable consumer information even if not regulated by the Fair Credit Reporting Act (FCRA). In sharp contrast to demonstrable risk at technology companies, consumer reporting companies are found by their chief federal regulator to have gone beyond the letter of the law to protect consumers and to have a sound, compliance-focused corporate culture.

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* The Consumer Data Industry Association (CDIA) is the voice of the consumer reporting industry, representing consumer reporting agencies including the nationwide credit bureaus, regional and specialized credit bureaus, background check companies, and others. Founded in 1906, CDIA promotes the responsible use of consumer data to help consumers achieve their financial goals, and to help businesses, governments and volunteer organizations avoid fraud and manage risk. Through data and analytics, CDIA members empower economic opportunity, helping ensure fair and safe transactions for consumers, facilitating competition and expanding consumer access to financial and other products suited to their unique needs.

- Original research based on publicly-available and verifiable data presented here also finds that low- and moderate-income consumers with robust credit histories have greater access to credit, controlling for age, gender, race, and other factors due to credit reports that overcome barriers to credit availability. This research also confirmed by Federal Reserve studies makes it clear that credit reports accurately predict credit risk.
- Because credit reporting is an accurate and non-discriminatory indicator of creditworthiness, it also protects both lenders and borrowers against debt the borrower cannot reasonably be expected to repay. Sustained macroeconomic growth and long-term household wealth equality are only possible if consumer debt supports long-term investment in homes or small businesses, prudent consumption, or short-term financial-stress management. True financial inclusion occurs only when larger amounts of consumer credit support family financial security and wealth accumulation, not a greater amount of high-risk household debt.
- Original research demonstrates that credit reporting facilitates economic mobility, making it possible for Americans to move as far as across the country without losing access to the credit essential to buy a new home, start a business, or otherwise prosper in ways once made far more difficult by the absence of nationwide, standardized credit reporting. We also show that credit reporting makes it possible for small or regional lenders to make loan decisions quickly and accurately, allowing them to diversify their risk by acquiring loans from outside their markets and thus reducing overall credit risk while enhancing financial-system resilience.
- The U.S. consumer reporting system leads the world, meeting or exceeding standards established by the World Bank, Bank for International Settlements, and other international bodies. These groups have also found that a secure, comprehensive consumer-data reporting construct enhances economic opportunity, sound finance, and economic growth.
- U.S. law governing credit reporting creates a framework[1] in which consumers have rights not matched in most other nations to know why credit may have been denied to them and to contest that decision. Prior to the establishment of this legal framework, credit availability was far more idiosyncratic and arbitrary and required a much lengthier time for lending decisions.

Indeed, a World Bank study of credit reporting concluded that, "One of the most important institutional elements supporting a well-functioning credit market is credit reporting firms."[2] As this study will demonstrate, Americans who become what the Bureau of Consumer Financial Protection calls "credit visible" by virtue of credit histories housed at CDIA members are Americans poised for economic opportunity, access to sound credit, increased chances of gainful employment, quicker loan decisions, and greater family financial security.

[1] A detailed analysis of the legal and regulatory framework governing consumer reporting in the U.S. may be found in the annex to this report.

[2] Matías Gutiérrez Girault and Jane Hwang, "Public Credit Registries as a Tool for Bank Regulation and Supervision," *World Bank Policy Research Working Paper 5489*, 3 (December, 2010), available at http://documents.worldbank.org/curated/en/934021468177872103/pdf/WPS5489.pdf.

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# I. The Consumer Reporting Construct

Credit bureaus (also now called consumer reporting agencies (CRAs)*) or credit-reporting companies (CRCs) first emerged in the late 19th century to assist merchants in identifying customers who might not repay the credit then traditionally extended by even the smallest groceries to increase sales. As a 2017 report from the Bureau of Consumer Financial Protection (CFPB) details,[3] credit bureaus have made it easier for merchants to go beyond their own knowledge of individual consumers and to be more secure in extending larger amounts of credit. As new forms of credit were developed (e.g., installment loans), credit bureaus and the data they gathered became still more important to the flow of credit to consumers, to lenders, to landlords, to insurers, to employers, to identity-theft protection, and across the U.S. economy. As of 2018,[4] 200 million Americans had their data submitted to credit-reporting agencies by 10,000 entities generally known as "furnishers" under the Fair Credit Reporting Act (FCRA).[5] Given the importance of consumer data to economic opportunity, consumer reporting companies also rely on public records and increasingly also on non-traditional furnishers such as telecommunications and utility companies to identify new forms of data that guide credit, employment, insurance, and other economic-opportunity decisions.

These furnishers voluntarily supply traditional and emerging data to credit-reporting agencies because they need objective information gathered from across the country to inform decisions in ways not possible from their own data resources or even from a complex, time-consuming search of public records on facts such as home ownership or bankruptcy filings. Consumer reporting also creates an accountability construct in which consumers realize that failing to honor credit obligations or engaging in high-risk activities is captured in data that then may compromise the consumer's ability to achieve his or her own life goals. A study by the Federal Reserve Bank of New York has in fact found that, when lenders discount the warnings provided by low credit scores and provide additional credit, borrowers feel themselves free to take on loans they are unlikely to repay, ultimately exposing households to significant economic harm.[6] Conversely, credit reports ensure that consumers making timely payments and

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[*] It is important to differentiate consumer reporting agencies (CRAs) discussed in this report from credit rating agencies sometimes also signified as CRAs. In sharp contrast to the consumer reporting agencies analyzed here, credit rating agencies (e.g., Standard & Poors, Moody's) assess large corporate and sovereign debt issuers and are regulated in the U.S. by the Securities and Exchange Commission. There is no overlap in function, ownership, regulation, or purpose between consumer reporting agencies and credit rating agencies. In this report, we assess consumer reporting agencies and the overall consumer-reporting process as defined in the Fair Credit Reporting Act.

[3] Kenneth P. Brevoort and Michelle Kambara, *CFPB Data Point: Becoming Credit Visible*, Consumer Financial Protection Bureau (CFPB) Office of Financial Research, (June, 2017), available at https://files.consumerfinance.gov/f/documents/BecomingCreditVisible_Data_Point_Final.pdf.

[4] CFPB Office of Supervision Policy Assistant Director Peggy Twohig, *Testimony before the Senate Committee on Banking, Housing, and Urban Affairs: Statement of Peggy Twohig: Hearing on An Overview of Credit Bureaus and the Fair Credit Reporting Act*, (July 12, 2018), available at https://www.banking.senate.gov/imo/media/doc/Twohig%20Testimony%207-12-18.pdf.

[5] Fair Credit Reporting Act (FCRA), 15 U.S.C. §§ 1681 et seq, Pub. L. No. 91-508, 84 Stat. 1114-2 (October 26, 1970), available at https://www.govinfo.gov/content/pkg/STATUTE-84/pdf/STATUTE-84-Pg1114-2.pdf.

[6] Julia Fonseca, Katherine Strair, and Basit Zafar, "Access to Credit and Financial Health: Evaluating the Impact of Debt Collection," *Federal Reserve Bank of New York (FRB-NY) Staff Report No. 814*, (May, 2017), available at https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr814.pdf?la=en.

honoring other obligations are rewarded by better data that increase credit availability on more favorable terms and conditions along with a path to less costly insurance services and other benefits. Consumer reports are also widely used for identity verification, simplifying a consumer's life in many daily transactions and providing a robust barrier against identity theft. Many lenders and consumer reporting agencies now provide consumers with free monthly reports based on credit-reporting company files, for the first time giving consumers a widely sought-after tool with which to monitor their own financial activity and protect themselves against identity theft. If these reports were not so useful, it is unlikely that consumers would avidly seek them, nor would lenders incur the costs of supplying them as part of their value proposition so frequently to so many customers.

Although furnishers come under legal requirements (see the annex to this report) to ensure accuracy when submitting data to a reporting agency, most entities with these data voluntarily ensure adherence to quality standards due to compelling incentives to share in a system that provides top-quality, current data no individual furnisher on its own could hope to accumulate without far more cost, risk, and omissions. A standardized form created by the CDIA facilitates furnisher interaction with credit bureaus, reducing costs, improving compliance, and enhancing reliability according to the CFPB.[7]

Beginning in 2012, the CFPB assumed authority to regulate the credit-reporting process and to supervise the national consumer reporting agencies (NCRAs), i.e., Equifax, TransUnion, and Experian, the largest of the CRAs. As the head of the Bureau at that time said, "For the first time, it became possible for a single agency to see across the entire credit reporting ecosystem and hold all of the key parties responsible for issues of data accuracy and dispute handling; no finger-pointing could deflect accountability."[8]

Consumer reporting* and the credit files created by it are governed by an extensive body of federal and state law and rule also described in detail in the annex. Law, rule, and CRA practice also determine which type of information is appropriate for maintenance in a credit file and how this information is to be secured, corrected when needed, and provided to the consumer and/or entities with a demonstrated, permissible need for the data. Credit reports do not contain data on a consumer's personal information or assets, nor do they include transaction-specific information (i.e., the type of goods purchased with a credit card) or information such as a consumer's race, gender identity, color, marital status, national

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* Consumer credit data often result in credit scores. These scores are numeric representations of creditworthiness based on the data gathered by a consumer-reporting agency. Specialized reporting agencies may also generate scores or otherwise provide conclusions about insurance or employment risk or likelihood to repay a specialized form of credit (e.g., a residential mortgage). Credit-reporting data may feed into established scores such as the FICO or VantageScore often cited in press reports or reviewed by consumers when they obtain their own credit scores. While some credit bureaus also provide credit scores, the functions are distinct. This report assesses only the gathering, reporting, and securing of personal data for permissible uses by consumer reporting agencies, not the scoring or other ancillary businesses some companies may also conduct.

[7] CFPB, *Key Dimensions and Processes in the U.S. Credit Reporting System: A review of how the nations' largest credit bureaus manage consumer data*, (December, 2012), available at https://files.consumerfinance.gov/f/201212_cfpb_credit-reporting-white-paper.pdf.

[8] CFPB Director Richard Cordray, "Prepared Remarks of Richard Cordray at the Consumer Advisory Board Meeting," (speech, Washington, D.C., March 2, 2017), available at https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-cfpb-director-richard-cordray-consumer-advisory-board-meeting-march-2017/.

origin, or sexual orientation.[9,10] Specialized agencies do not collect these protected data, but may collect data beyond that collected by credit bureaus (e.g., employment history).

## II. Credit Reporting and the Consumer Value Proposition

As is made clear above, consumer reporting involves a complex inter-relationship between credit bureaus, furnishers, users, and the consumers whose data power all the decision-making made possible by organized, searchable databases. Importantly, only a few of these protections apply to personally-identifiable consumer data (including health information) used by large technology companies or others that develop their own data analytics instead of relying on consumer-reporting companies and their consumer histories. It is for this reason that the Government Accountability Office in 2019 called upon the U.S. Congress to mandate an array of new consumer rights related to data currently held outside consumer-reporting companies.[11] As the CFPB has observed, "Credit reporting plays a critical role in consumers' financial lives."[12]

One reason policy-makers are seeking to replicate consumer reporting as technology changes is that current law gives consumers the right to know why credit may have been denied and, if an adverse action is based on what the consumer believes to be erroneous information, then also to contest that decision. As we shall show, prior to the establishment of this legal framework, credit availability was not only idiosyncratic based on individual character or personal relationships, but also often far more arbitrary.

Unregulated data may also lead to credit or other forms of consumer discrimination. Discrimination is of course not only illegal and contrary to the values of CDIA and its members, but also very much against the interests of women, people of color, those with disabilities, those with minority sexual orientations, and other protected classes of prospective borrowers under the Equal Credit Opportunity Act[13] and the Fair Housing Act.[14] As discussed in more detail below, data demonstrate that credit reporting actually

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[9] Based on a review of sample reports from Experian, Equifax, and TransUnion. Sample Experian report is available at https://www.experian.com/credit_report_basics/pdf/samplecreditreport.pdf; Sample Equifax report is available at https://www.creditcardinsider.com/wp-content/uploads/2019/03/Equifax-example-credit-report.pdf; Sample TransUnion report is available at https://www.transunion.com/docs/rev/personal/Credit_Report_Explanations.pdf.

[10] Francis Creighton, *Testimony before The House Financial Services Committee Oversight & Investigations Subcommittee*, (October 29, 2019), available at https://financialservices.house.gov/uploadedfiles/hhrg-116-ba09-wstate-creightonf-20191029.pdf.

[11] Government Accountability Office (GAO), "Internet Privacy: Additional Federal Authority Could Enhance Consumer Protection and Provide Flexibility," *GAO-19-52*, (January, 2019), available at https://www.gao.gov/assets/700/696437.pdf.

[12] CFPB, "Supervisory Highlights Consumer Reporting Special Edition," *Supervisory Highlights Issue 14, Winter 2017*, 2 (March, 2017), available at https://files.consumerfinance.gov/f/documents/201703_cfpb_Supervisory-Highlights-Consumer-Reporting-Special-Edition.pdf.

[13] Fair Credit Billing Act and Equal Credit Opportunity Act Title V (ECOA), Pub. L. No. 93-495, 88 Stat. 1500, 1521 (October 28, 1974), available at https://fraser.stlouisfed.org/title/1033.

[14] Civil Rights Act Title VIII (Fair Housing Act), Pub. L. No. 90-284, Title VIII, 82 Stat. 73, 81 (April 11, 1968), available at https://www.govinfo.gov/content/pkg/STATUTE-82/pdf/STATUTE-82-Pg73.pdf.

reduces the likelihood that a borrower will face discrimination, especially that embodied in the most subtle form of credit discrimination: disparate impact, where no overt discrimination is seen but protected borrowers nonetheless do not equitably receive access to fairly-priced credit or other services and opportunities.

### *A. The Credit-Availability Value Proposition*

Former CFPB Director Cordray has said of credit reporting companies that:

> Without credit reporting, consumers would not be able to get credit except from those who have already had direct experience with them, for example from local merchants who know whether or not they regularly pay their bills. This was the case fifty or a hundred years ago with "store credit," or when consumers really only had the option of going to their local bank. But now, consumers can instantly access credit because lenders everywhere can look to credit scores to provide a uniform benchmark for assessing risk.[15]

It is of course important to assess not just whether consumers are able to obtain credit, but also whether consumers can then repay their loans without undue economic hardship that jeopardizes long-term economic equality and financial stability. Much discussion of "financial inclusion" focuses on the ability of borrowers to obtain credit, but the credit-reporting system is uniquely focused on ensuring that credit obtained is credit repaid. Extensive research, including that of the Federal Reserve,[16] demonstrates a critical value-add resulting from regulated credit reporting: objective, non-discriminatory, and transparent scoring with a demonstrable record of accurately predicting a consumer's ability to repay debt obligations. In a 2007 report to Congress, the Fed concluded that, "Credit scoring, as a cost- and time-saving technology that became a central element of credit underwriting during [the prior twenty-five years] contributed to improved credit availability and affordability."[17] This Federal Reserve report to Congress also notes that these credit-availability and affordability benefits extend across the U.S. population as a whole, a finding reflected in other research specifically addressing credit discrimination discussed below.

Other research assessing the differences in credit availability for consumers with good credit histories uses the elimination of adverse information to study consumer credit access before and after an impediment to credit recorded by a reporting agency is removed.[18] Pulling credit

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[15] CFPB Director Richard Cordray, "Prepared Remarks by Richard Cordray on Credit Reporting," op. cit.

[16] Board of Governors of the Federal Reserve System (FRB), *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, (August, 2007), available at https://www.federalreserve.gov/boarddocs/rptcongress/creditscore/creditscore.pdf.

[17] FRB, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, *op. cit.* at S-2.

[18] Will Dobbie, Benjamin J. Keys, and Neale Mahoney, *Credit Market Consequences of Credit Flag Removals*, (July 7, 2017), available at https://pdfs.semanticscholar.org/d06e/1f920993125e6e1df16d63939030c25b3264.pdf.

histories from 2001 to 2015 and evaluating the impact of adverse information removals related to bankruptcy status, significant increases in credit-card availability are observed for consumers who have had adverse information fall off their reports over times. Another study assessing adverse information removal then found[19] that affected consumers gain employment earning more, increasing their access to credit. Specifically, those who gain employment following the removal of adverse information earn $1,800 more per year on average relative to individuals who gain employment prior to the removal of adverse information. More consumers then also become small-business owners who in turn employ others just entering the work force. Given that start-up small businesses are a vital engine of economic equality and employment,[20] the value of credit reports and of score improvements have demonstrable social-welfare and macroeconomic impact not because credit availability is increased, but because responsible borrowers – and potential improved-credit borrowers – are identified who obtain sustainable credit that generates bottom-up economic growth.

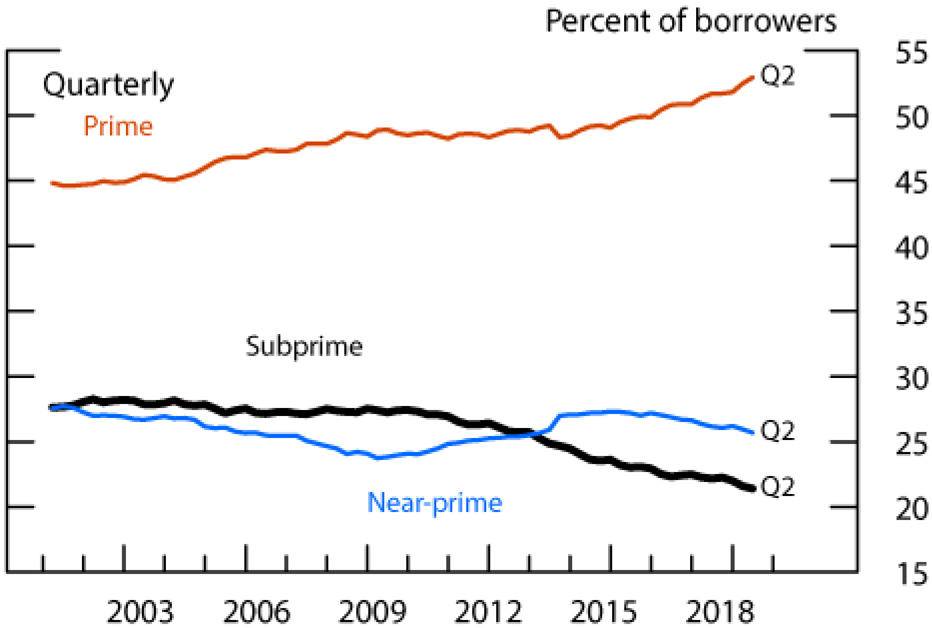
More recent Federal Reserve research has also substantiated the virtuous-cycle credit-availability impact of consumer reports.[21] In this work, FRB staff evaluated the impact of changing credit scores on credit availability, concluding that nearly all of the net rise in aggregate household debt between 2015 and 2018 was to borrowers with near-prime credit scores in 2015 whose scores either remained near-prime or rose to prime by 2018. This makes it clear that more credit did not mean more household risk since credit growth was not concentrated in subprime borrowers whose ability to repay under stress is at best uncertain. Notably, the share of borrowers with prime scores increased over these three years, rising on average one percentage point per year, as demonstrated in the chart below from that study. Fed researchers attributed this growth in the share of borrowers with prime scores – and decreases in the shares of both near- and sub-prime borrowers – to improving macroeconomic conditions that enhance household income and otherwise support creditworthiness.

[19] Kyle Herkenhoff, Gordon Phillips, and Ethan Cohen-Cole, "The Impact of Consumer Credit Access on Employment, Earnings, and Entrepreneurship," *NBER Working Paper 22846*, (November, 2016), available at https://www.nber.org/papers/w22846.pdf.

[20] John Haltiwanger, Ron S. Jarmin, and Javier Miranda, "Who Creates Jobs? Small Versus Large Versus Young," *The Review of Economics and Statistics*, XCV(2), 347 (May, 2013), available at https://www.mitpressjournals.org/doi/pdf/10.1162/REST_a_00288.

[21] Sarena Goodman and Steve Ramos, "Understanding Changes in Household Debt by Credit Risk Category: The Role of Credit Score Transitions," *FEDS Notes*, (June 25, 2019), available at https://www.federalreserve.gov/econres/notes/feds-notes/the-role-of-credit-score-transitions-20190625.htm.

## Distribution of Credit Scores




Source: Analysis of FRBNY CCP/Equifax data contained in: Sarena Goodman and Steve Ramos, "Understanding Changes in Household Debt by Credit Risk Category: The Role of Credit Score Transitions," *FEDS Notes*, (June 25, 2019).

Our own research brings these findings forward and corroborates them with additional evidence derived from publicly-available and verifiable data. Looking at data from all fifteen rounds of the Federal Reserve Bank of New York's Survey of Consumer Expectations[22] between October 2013 and June 2018 and also at the 2016 Survey of Consumer Finances,[23] we find that consumers with more robust credit histories are more confident in their credit search, less financially fragile, and better able to meet both planned and unplanned needs.

Using credit scores as a proxy for credit history, we find that, as credit scores increase – that is, as the robustness of a consumer's credit history improves – the likelihood that consumers will not apply for credit for fear of rejection decreases, as shown in the chart below. Put another way, the higher a consumer's credit score, the more confident she is that an application for credit will be accepted. Readiness to apply for credit ensures that eligible borrowers obtain sustainable credit, helping them avoid short-term financial stress and to enter the economic mainstream through home ownership, small-business formation, and other opportunities fueled by sustainable, affordable credit.

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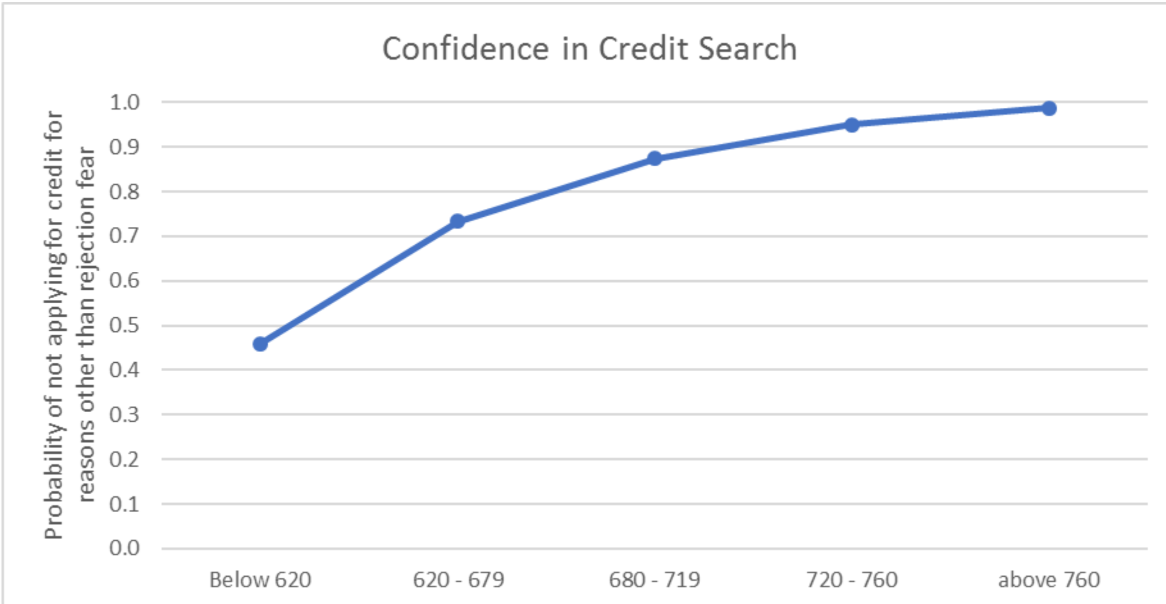
[22] FRB-NY, *Survey of Consumer Expectations Credit Access Survey*, available at https://www.newyorkfed.org/microeconomics/sce/credit-access#/.

[23] Board of Governors of the Federal Reserve System (FRB), *Survey of Consumer Finances*, (2016), available at https://www.federalreserve.gov/econres/scfindex.htm.



Source: Based on a regression analysis of data from the Federal Reserve Bank of New York Survey of Consumer Expectations Credit Access Survey

When credit balances to credit-limit ratios are compared, we find also that a higher credit utilization ratio implies worse credit health. An incremental increase in the credit utilization ratio increases the likelihood of declaring bankruptcy and of taking a payday (small dollar unsecured) loan, controlling for age, race, gender, and other factors. This thus indicates a greater degree of financial fragility among those with higher credit-utilization ratios (i.e., those with less robust credit histories). Similarly, an incremental increase in the credit-utilization ratio reduces the likelihood of having a savings account, suggesting that consumers with less robust credit histories are also less able to meet both planned and unplanned needs.

### *B. Consumer Rights and their Value Propositions*

#### *1. The Right to Know*

As noted, financial inclusion resulting from additional debt only supports long-term economic opportunity if the consumer is able to repay his or her obligations without economic hardship. Consumers who know their credit scores and reports are well prepared to judge credit in terms of real value, not just the putative benefits of a set of interest rates or fees as represented to them by parties with their own interests at stake in a transaction. Credit reporting also ensures that consumers have rights should an offer of credit be denied or made with materially less-favorable conditions.

As discussed in the annex, the FCRA requires lenders to provide consumers with free credit reports on an annual basis and additional reports when they receive "adverse-action" notices detailing why credit, employment, or insurance has been denied if the decision to do so is based on a credit report. Prior to these adverse-action notices, credit decisions and many others critical to a consumer were literally black boxes – that is, the consumer filled out an application (often lots of different ones), sent it in, and never found out why a request was honored or denied. Consumers thus often sought out lenders willing to extend credit on terms far less favorable than those to which the consumer was actually entitled had correct information guided an initial credit decision. This high-cost debt of course poses significant risk to individual borrowers and the financial system as a whole.

### *2. The Right to Correct*

Although banking-agency rules require lenders under their jurisdiction to maintain accurate records,[24] many furnishers are nonbank lenders with little or no regulatory scrutiny. The data they provide to credit bureaus may be faulty or incomplete. As a result, in the absence of regulated consumer reporting agencies and the scores generated based on their data, lenders could send in poor quality data to unregulated or even conflicted registries or rely only on their own idiosyncratic data. This could well lead them into incorrect inferences about a consumer's risk or even conclusions based on wholly incorrect data. This risk is significantly reduced because consumer reporting agencies regularly scrutinize the quality of data provided to them, counsel furnishers on ways to improve, demand correction when this does not occur, or even exclude a furnisher from an agency's network. No individual consumer could resolve disputes with this much market power or wield such discipline over his or her data except by providing them to each and every lender, insurer, or employer at considerable cost and time burden likely to delay decisions or even simply exclude some consumers from the market. Alternatively, lenders could rely on their own information, but much of this is now in high-tech "black boxes" full of personal data gathered without consumer knowledge or the transparency needed to ensure data fairness, accuracy, and long-term debt sustainability.

Further, consumer-reporting companies have robust quality assurance processes internally to identify and correct problematic data. The FCRA requires consumer reporting agencies to provide consumers with reports throughout this process according to strict timelines. Although disputes regarding credit-report accuracy remain, the CFPB has found significant improvements at the largest CRAs.[25] According to the CFPB, consumer reporting agencies now have a "proactive" compliance culture.[26] This ensures that CRAs not only meet the letter of law and rule on a continuing basis, but also that any failures to do so are readily corrected in ways that enhance the consumer value proposition.

CRAs also improve accuracy through updated methodologies and new technology. An example is work underway at several CRAs – including all three nationwide CRAs – to introduce "trended data." Trended data allow a credit report user to view more than the

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[24] Office of the Comptroller of the Currency (OCC), FRB, Federal Deposit Insurance Corporation (FDIC), Office of Thrift Supervision (OTS), National Credit Union Administration (NCUA), and Federal Trade Commission (FTC) Procedures to Enhance the Accuracy and Integrity of Information Furnished to Consumer Reporting Agencies," 74 Fed. Reg. 31484 (to be codified at 12 C.F.R. §§ 41, 22, 334, 571, 717 and 16 C.F.R. § 660), (July 1, 2009), available at https://www.govinfo.gov/content/pkg/FR-2009-07-01/pdf/E9-15323.pdf.
[25] CFPB, "Supervisory Highlights Consumer Reporting Special Edition," *op. cit*.
[26] CFPB, "Supervisory Highlights Consumer Reporting Special Edition," *op. cit*.

moment-in-time snapshot of consumer credit use provided by a traditional consumer report. Instead, trended data provide a trajectory of likely consumer credit risk, using up to 30 months of account history on loans and credit accounts to provide insights such as whether a consumer is paying off debt each month or carrying a balance, whether balances are trending up or down, and how consumer credit-utilization growth has changed. These trends improve consumers opportunities for more credit offerings that fit their current and future economic needs.

As the CFPB has also made clear,[27] ensuring the accuracy of millions of reports with hundreds of data points is a complex undertaking. As a result, complaints about accuracy are an ongoing concern for policymakers. Although the CFPB has concluded that the extent to which inaccuracies are material – i.e., sufficient to present an obstacle to credit, employment, or insurance – is unknown, extensive data suggest that most errors are immaterial to economic opportunity. When examining this question in 2012, the Federal Trade Commission (FTC) found that consumers assert potential inaccuracies for about nineteen percent of credit reports from the nationwide CRAs.[28] However, not all alleged inaccuracies are in fact material to credit scoring or inaccurate; 37 percent of potential disputes were found to relate only to "header" information that does not bear on one's credit score (e.g., name, date of birth),[29] and more than thirty percent of alleged inaccuracies were not modified after investigation by a CRA due to the lack of an actual material error.[30] A claim of inaccuracy therefore does not necessarily mean that a report is inaccurate or that an inaccuracy has a material impact on a consumer's ability to obtain credit or its cost. The FTC study also found that only two percent of all credit reports are modified due to a reported inaccuracy and then see a credit score increase of more than 25 points; only 2.2 percent had scores that increase enough to propel the consumer into a preferable classification (e.g., from near-prime to prime). Similar research from the Policy & Economic Research Council has found these figures to be less than one percent and 0.5 percent, respectively.[31] The table below from the FTC study compares PERC's findings with its own. Updated research since the 2012 FTC report would benefit policy decision making going forward.

[27] CFPB, *Key Dimensions and Processes in the U.S. Credit Reporting System: A review of how the nations' largest credit bureaus manage consumer data*, *op. cit.*

[28] FTC, *Report to Congress Under Section 319 of the Fair and Accurate Credit Transactions Act of 2003*, (December, 2012), available at https://www.ftc.gov/sites/default/files/documents/reports/section-319-fair-and-accurate-credit-transactions-act-2003-fifth-interim-federal-trade-commission/130211factareport.pdf.

[29] *Ibid*.

[30] FTC, *Report to Congress Under Section 319 of the Fair and Accurate Credit Transactions Act of 2003*, *op. cit*. at 38-39.

[31] Michael A. Turner, Robin Varghese, and Patrick D. Walker, *U.S. Consumer Credit Reports: Measuring Accuracy and Dispute Impacts*, Policy and Economic Research Council (PERC), 8 (May, 2011), available at https://www.perc.net/wp-content/uploads/2013/09/DQreport.pdf.

## Comparison of PERC and FTC Accuracy Studies

| | PERC | FTC |
|---|---|---|
| Number of reports examined | 3,876 | 2,968 |
| Percentage of reports with no identified potential disputes | 80.8% | 81.0% |
| Percentage of reports with one or more potential disputes (including reports with *only header errors*) | 19.2% | Not Available |
| Percentage of reports where participant indicated they had disputed information or intended to dispute | 15.6% | 21.6% |
| Number of reports with any information disputed (i.e., dispute filed) | 286 (7.4%) | 708 (23.9%) |
| Number of reports with tradeline disputes filed (i.e., material information) | 210 (5.4%) | 572 (19.3%) |
| Number of *reports disputed* that were modified by the CRA in response to consumer dispute | 181 (estimated based on PERC study report of % modified) | 399 |
| Percentage of *reports disputed* by consumer that leads to any modification | 86.2% | 69.9% |
| Percentage of *reports disputed* that resulted in a score change | 59.1% (42% score increase, 17% score decrease) | 36.9% (34.1% score increase, 2.8% score decrease) |
| Percentage of *reports examined* that resulted in a score increase | 3.1% | 6.6% |
| Percentage of *reports examined* that resulted in score increase of more than 25 points | 0.9% | 2.0% |
| Percentage of *reports examined* that had credit scores increase such that participant moves to a lower credit risk classification as a result of consumer dispute | 0.5% | 2.2% |

Source: FTC, *Report to Congress Under Section 319 of the Fair and Accurate Credit Transactions Act of 2003, op. cit*. at A-4.

### *3. The Right to Deny Data Access*

One unique aspect of personally-identifiable data held by consumer reporting companies is that consumers may "freeze" their data so that new accounts cannot be opened, either by the consumer, or by a perpetrator of identity theft.[32] No such rights exist for personally-identifiable data held by giant tech companies who may freely "monetize" personal data nor do any of these companies need to ensure that consumers have annual access to personal data as demanded by federal law of credit-reporting companies. The GAO as noted thus recommended to Congress in 2019 that consumers enjoy the rights they already have with consumer-reporting companies at other holders of their information.[33]

Federal law[34] also requires that the NCRAs provide active-duty military and veterans with personal-data control rights above and beyond those generally required due to the unique circumstances of military service. Servicemembers on active duty may contact any of the three NCRAs and request an "active-duty alert" in their file, which then requires the credit bureau to provide the servicemember with electronic credit monitoring services free of charge for one year, renewable for the time of deployment. An NCRA notified of a consumer's active-duty status must inform the other two NCRAs, with the NCRAs also required to remove those with active-duty alerts in their files from their marketing lists for prescreened credit card offers for two years unless otherwise directed by the servicemember.[35] Veterans also have special protections under the law limiting the appearance of medical debt on their credit reports.[36]

As an alternative to the freeze noted above, consumers also have the right under Federal law to place a fraud alert in their credit files.[37] By placing this type of alert in a credit file, consumers who believe they have been or suspect that they are about to become victims of fraud or a related crime such as identity theft can communicate this to any business that runs a credit check and compel lenders or other credit-history users to verify that it is indeed that consumer who is seeking to open a new account. This allows consumers to add an extra layer of security when they suspect they may be victimized while still allowing access to their credit files. As with active-duty alerts, an NCRA must notify the other NCRAs when a consumer has requested a fraud alert.

### *4. The Right to Fair Decisions*

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[32] Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA) § 301, Pub. L. No. 115-174, 132 Stat. 1296, 1326 (May 24, 2018), available at https://www.govinfo.gov/content/pkg/PLAW-115publ174/pdf/PLAW-115publ174.pdf.

[33] GAO, "Internet Privacy: Additional Federal Authority Could Enhance Consumer Protection and Provide Flexibility," *op. cit*.

[34] EGRRCPA § 302, Pub. L. No. 115-174, 132 Stat. 1296, 1332 (May 24, 2018), available at https://www.govinfo.gov/content/pkg/PLAW-115publ174/pdf/PLAW-115publ174.pdf.

[35] 15 U.S.C. § 1681c–1(c) (2018), available at https://www.govinfo.gov/content/pkg/USCODE-2018-title15/pdf/USCODE-2018-title15-chap41-subchapIII-sec1681c-1.pdf.

[36] EGRRCPA § 302, Pub. L. No. 115-174, 132 Stat. 1296, 1332 (May 24, 2018), available at https://www.govinfo.gov/content/pkg/PLAW-115publ174/pdf/PLAW-115publ174.pdf.

[37] 15 U.S.C. § 1681c–1(a) (2018), available at https://www.govinfo.gov/content/pkg/USCODE-2018-title15/pdf/USCODE-2018-title15-chap41-subchapIII-sec1681c-1.pdf.

In addition to the right to know and the right to correct, credit reporting has significantly enhanced consumer rights to fair decision-making that does not take race, gender identity, ethnicity, disability, marital status, national origin, or sexual orientation into account; the credit file simply does not include such information. An FTC report has found that credit-based insurance scores that use credit bureau data are not proxies for racial and ethnic groups.[38] Relationships between scores and claims risk were found to be strong after controlling for demographic factors. The FTC also found that scores effectively predict claims risk within racial and ethnic groups. Despite constructing numerous alternative scoring models, the FTC also could not develop an alternative credit-based insurance scoring model that would predict risk accurately and decrease the differences in average racial group scores.

Similarly, the Federal Reserve has found that credit characteristics in credit scoring models are not proxies for race, ethnicity, or gender.[39] Indeed, credit scoring using credit bureau data contributed to improved credit availability and affordability, with credit increasing for the overall population and across major demographic groups, including different races and ethnicities. The Federal Reserve's report thus also suggests supplying the credit bureaus with information regarding rent, other recurring bill payments, and foreign credit histories to provide a broader picture of the credit experiences of recent immigrants, observing that disciplined, innovative scoring expands access to sustainable credit.

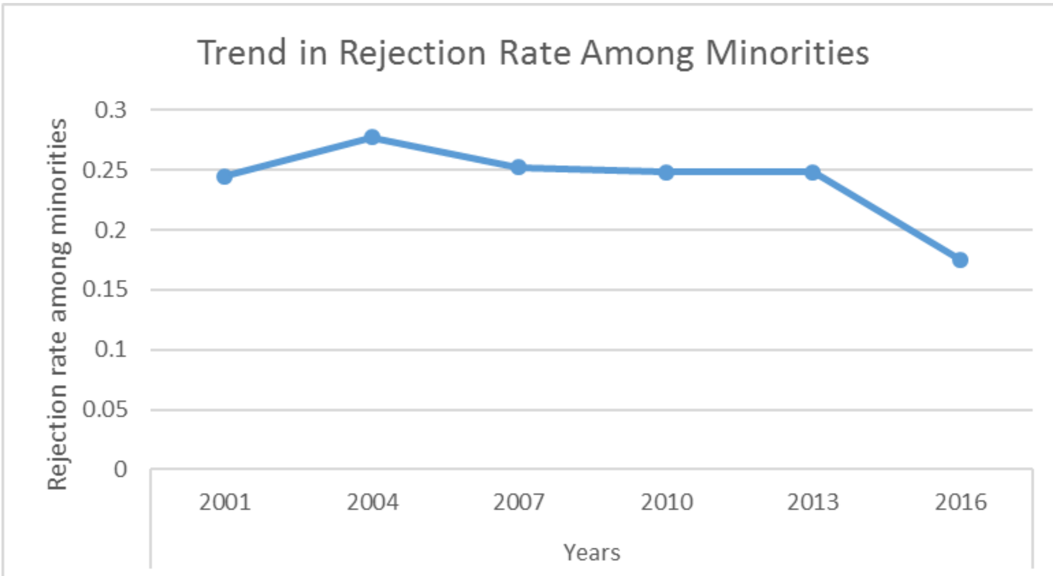
Federal Reserve researchers have also examined the potential disparate impacts of certain credit characteristics in credit reports using credit bureau records and demographic information from the Social Security Administration.[40] They found little or no evidence of disparate impact by race or gender when examining credit records used in constructing credit scoring models. The distributions of credit scores across races and genders were found to be unaffected by reconstructing the baseline credit scoring models. While finding disparate impact by age, the study recommends taking no action because the effects are so small.

Our own analysis updates prior research and confirms that credit reports do not discriminate based on status as a low-or-moderate income (LMI) and/or minority individual; instead lower scores are predictive of greater risk.

Looking again at Federal Reserve 2016 data[41] and defining LMI individuals as those with less than 300 percent of the Federal poverty line, we find that LMI consumers with robust credit histories have greater access to credit, controlling for age, gender, race, and

[38] FTC, "Credit-Based Insurance Scores: Impacts on Consumers of Automobile Insurance: A Report to Congress By the Federal Trade Commission," July 2007, available at https://www.ftc.gov/sites/default/files/documents/reports/credit-based-insurance-scores-impacts-consumers-automobile-insurance-report-congress-federal-trade/p044804facta_report_credit-based_insurance_scores.pdf.
[39] FRB, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, *op. cit.*
[40] Robert Avery, Kenneth Brevoort, and Glenn Canner, "Does Credit Scoring Produce a Disparate Impact?," Finance and Economics Discussion Series Working Paper 2010-58, October 12, 2010, available at https://www.federalreserve.gov/pubs/feds/2010/201058/201058pap.pdf.
[41] FRB, *Survey of Consumer Finances*, (2016), *op. cit.*

other factors than those without robust histories. Similarly, analysis of this same Fed data for 2001-2016 finds that minority borrowers with robust credit histories have greater access to credit than those without robust histories. Notably, rejection rates among minorities declined by about ten percentage points between 2004 and 2016, as shown in the chart below.




Source: Based on analysis of data from the Federal Reserve Survey of Consumer Finances

### *5. The Freedom to Move*

The existence of nationwide credit-reporting agencies makes consumer data a national resource. Due to it, consumers need not rely solely on lenders offering credit in their neighborhood, but may instead double-check local credit providers against regional or nationwide ones. This not only offers greater choice, but also ensures that local areas such as rural or under-served ones are not disadvantaged by virtue of the lack of lenders with a local physical presence. Further, when consumers move, credit reporting ensures that they need not begin all over again to introduce themselves to local creditors and gradually regain access to essential financing. This is vital to all consumers, but perhaps most importantly to those moving from one part of the country experiencing economic challenges to another in which the prospects for employment are brighter. The Federal Reserve has established that, for low-skilled workers, economic mobility is particularly critical.[42]

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[42] Cynthia L. Doniger, "Do Greasy Wheels Curb Inequality?," *FRB Finance and Economic Discussion Series 2019-021*, (March 12, 2019), available at https://www.federalreserve.gov/econres/feds/files/2019021pap.pdf.

[42] World Bank, *General Principles for Credit Reporting*, (September, 2011), available at http://documents.worldbank.org/curated/en/662161468147557554/pdf/70193-2014-CR-General-Principles-Web-Ready.pdf.

Based on an analysis of both Home Mortgage Disclosure Act (HMDA) data[43] and a Federal Reserve Bank of Philadelphia analysis[44] of public account-level data from one of the largest U.S. online nonbank lenders relying on credit scores, we conclude that consumer reporting enables consumers to borrow from a variety of lenders that operate across geographies, thus allowing consumers to move anywhere within the U.S. without losing access to credit. Large financial-technology mortgage lenders, who also generally operate on a national level, also increased their share of the mortgage market from 5.3 percent to 9.3 percent between 2013 and 2018, with credit reporting essential to this growth due to the role it plays in the automated-underwriting systems mandated by U.S. housing finance agencies. Traditional depository institution market share fell over this same period, with our research indicating that nontraditional lenders have stepped in to at least maintain, and in many cases increase, the amount of available credit in regions from which banks have receded. It seems most unlikely that this nationwide credit availability and innovation would have occurred if each start-up lender needed to generate its own credit records for borrowers with whom no prior relationship existed.

## III. Credit Reporting and the Lender Value Proposition

### *A. General Framework*

A World Bank study of credit reporting has concluded that, "One of the most important institutional elements supporting a well-functioning credit market is credit reporting firms."[45] Benefits of credit reporting include:

- ***Provisioning:*** Credit reports ensure that loan-loss reserving is well calibrated from loan origination to reflect expected loss. With the advent of current expected credit loss (CECL) accounting,[46] the need for reserve precision has taken on urgent proportions in the U.S. because of the need to establish reserves at the outset of a credit exposure that reflect risk over the life of the loan under a range of reasonable economic circumstances. As many banks have noted,[47] CECL raises the risk that lending will become procyclical – i.e., go up during benign scenarios and sharply down under stress,

[43] Home Mortgage Disclosure Act (HMDA) data for 2013-2018 may be accessed at: CFPB, "Download Mortgage Data," *Mortgage data (HMDA)*, accessed October 30, 2019, available at https://www.consumerfinance.gov/data-research/hmda/.
[44] Julapa Jagtiani and Catharine Lemieux, "Do Fintech Lenders Penetrate Areas That Are Underserved by Traditional Banks?," *Federal Reserve Bank of Philadelphia Working Paper 18-13*, (March, 2018), available at https://www.philadelphiafed.org/-/media/research-and-data/publications/working-papers/2018/wp18-13.pdf.
[45] Matías Gutiérrez Girault and Jane Hwang, "Public Credit Registries as a Tool for Bank Regulation and Supervision," *op. cit*.
[46] Financial Accounting Standards Board (FASB), "FASB Issues New Guidance on Accounting for Credit Losses," (June 6, 2016), available at https://www.fasb.org/jsp/FASB/FASBContent_C/NewsPage&cid=1176168232900.
[47] American Bankers Association (ABA) Banking Journal, "ABA Calls for 'Full, Indefinite' Delay of CECL for All Banks," American Bankers Association, September 16, 2019, available at https://bankingjournal.aba.com/2019/09/aba-calls-for-full-indefinite-delay-of-cecl-for-all-banks/.

increasing both macroeconomic stress and systemic risk. The better the credit-risk information lenders have on hand with which to set reserves over the life of an exposure, the less procyclical CECL is likely to prove with regard to retail decisions that take credit-report data into account either in credit scores or lender underwriting. The U.S. mortgage market is also likely to be less procyclical under CECL than it would otherwise be due to the important role credit scores play in government-sponsored enterprise (GSE) underwriting and pricing decisions.[48] The importance of the U.S. consumer reporting system is even more profound with the new CECL accounting standard set to go into effect.

- ***Capital Standards:*** Although loan-loss reserves account for expected credit risk, regulatory-capital requirements are meant to buffer lenders against unexpected loss. Objective reports inform regulatory decisions about calibration for an array of retail exposures, enhancing the extent to which regulatory capital strengthens banks because internal ratings approaches are validated by objective criteria. To the extent regulatory capital is set too high, borrowers may be under-served by regulated financial institutions, exposing vulnerable households to personal financial hardship and/or predatory lending products. When regulatory-capital standards are too lenient, then banks are exposed to unanticipated risk and their solvency may be tested under stress. In credit categories where many banks have large exposures (e.g., mortgages, credit cards, auto loans), inappropriate capital allocation can have dire equality consequences and even pose significant systemic risk.
- ***"Credit Culture:"*** The World Bank study concludes that a credit culture "facilitates access to credit as it addresses the fundamental problem of credit markets: asymmetric information between borrowers and lenders, which leads to adverse selection and moral hazard."[49] Adverse selection results when lenders fail to anticipate likely loss due to insufficient information about borrower risk and, as a result, high-risk borrowers migrate to them. Moral hazard increases when borrowers expect that prior defaults or even bankruptcies will have no consequences for future credit availability – i.e., that bad behavior does not increase the likelihood of outcomes the borrower seeks to avoid. The advent of financial technology and online, mobile lending has only increased these issues of significance with the importance of consumer reporting.
- ***Competitiveness:*** Credit bureaus also increase the ability of smaller lenders to judge credit risk accurately and thus to compete more effectively against larger lenders.

### *B. Safety and Soundness*

According to the Federal Reserve's 2007 report to Congress, "The credit history scores evaluated here [i.e., those based on data from the three largest U.S. credit-reporting companies] are predictive of credit risk for the population as a whole and for all major demographic groups. That

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[48] Federal Housing Finance Agency (FHFA) Validation and Approval of Credit Score Models, 84 Fed. Reg. 41886 (August 16, 2019) (to be codified at 12 C.F.R. § 1254), available at https://www.govinfo.gov/content/pkg/FR-2019-08-16/pdf/2019-17633.pdf.

[49] Matías Gutiérrez Girault and Jane Hwang, "Public Credit Registries as a Tool for Bank Regulation and Supervision," *op. cit*.

is, over any credit-score range, the higher (better) the credit score, the lower the observed incidence of default."[50] This is because credit scores based on NCRA-generated consumer reports increase the consistency and objectivity of credit evaluation so as to diminish the possibility that credit decisions are influenced by personal characteristics, including those prohibited by law, as well as conscious or unconscious bias.[51]

Objective credit evaluation also encourages more accurate risk pricing, allowing lenders to reduce the cost of cross-subsidization of risk among a pool of borrowers.[52] By reducing this cross-subsidization, lenders can better discourage excessive borrowing by risky customers and ensure that less risky ones are not discouraged from taking on credit to the extent their financial conditions warrant, thus increasing the overall performance of a lender's portfolio.

Research from the World Bank[53] has also found that the data produced by credit reporting not only improves credit analysis by financial institutions, but also strengthens bank regulation and supervision. Looking across 57 countries with credit reporting frameworks, it finds that all but four look at financial institution use of credit reports in lending as part of the supervision process and more than 80 percent use credit-reporting data to analyze trends in banking and credit.[54] Regulatory and supervisory uses include calculating the total indebtedness of borrowers within the financial system, supporting forward-looking provisioning policies, and monitoring credit-risk concentrations.

### *C. Geographic Diversification*

As detailed in bank-regulatory standards limiting credit-exposure concentrations,[55] lenders increase risk when they have concentrations to single creditors and/or narrow geographic regions that may be subject to risk that can be reduced in a portfolio diversified with other, offsetting risk. It is for this reason that portfolio diversification is a fundamental tenet of financial-risk mitigation.

Our review of CFPB data on mortgage credit and FDIC data on branch networks demonstrates the value proposition of credit reporting to bank safety and soundness resulting from more diverse credit risks than would be possible in the absence of objective information on borrowers outside the direct experience of individual banks and credit unions. Using data on mortgage lending

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[50] FRB, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, *op. cit.* at S-1.
[51] *Ibid*. at S-4
[52] *Ibid*. at O-5.
[53] Andrew Powell, Nataliya Mylenko, Margaret Miller, and Giovanni Majnoni, "Improving Credit Information, Bank Regulation and Supervision: On the Role and Design of Public Credit Registries," *World Bank Policy Research Working Paper 3443*, (November, 2004), available at http://documents.worldbank.org/curated/en/958501468779185412/pdf/WPS3443.pdf.
[54] *Ibid.* at 17
[55] FRB Single-Counterparty Credit Limits for Bank Holding Companies and Foreign Banking Organizations, 83 Fed. Reg. 38460 (to be codified at 12 C.F.R. § 252), (August 6, 2018), available at https://www.govinfo.gov/content/pkg/FR-2018-08-06/pdf/2018-16133.pdf.

required under HMDA,[56] we find that mortgage lending does not correlate well with the physical presence of bank branches or similar offices. This risk dispersion would not be possible without credit histories because the GSEs that purchase mortgages and the Federal Housing Administration (FHA) that insured loans sold to Ginnie Mae require a reliable source of credit data or, in general, the scores developed based on credit bureau reports. The GSEs' regulator, the Federal Housing Finance Agency (FHFA), has affirmed the importance of credit histories in its new rule on the role of credit scores in mortgage finance.[57] Mortgage credit-underwriting standards similarly require a robust source of reliable, verifiable credit history.[58]

### *D. Efficiency*

The process of obtaining credit, employment, and/or insurance is made considerably more efficient from both the consumer and provider's perspective as a result of consumer-data reports. These are not only more complete, objective, and accurate than would be the case if individual providers sought to assemble them, but also far more efficiently gathered due to the resources of consumer-reporting companies and the standardized format known as Metro 2 established by the Consumer Data Industry Association. Quality checks performed by the consumer-reporting companies prior to adding data to these files also enhance the value of reports otherwise unavailable in the marketplace.

### *E. Identity Verification*

As described in the annex to this report, U.S. rules designed to prevent money laundering and violations of official sanctions (e.g., those against Iran) require financial institutions to identify their customers to ensure that those with whom they do business are those with whom they intend to do business.[59] In addition, other businesses – e.g., nonbank mortgage lenders – must file "suspicious activity reports" (SARs) when they have reason to believe that a transaction is not as represented or otherwise violates law or rule.[60] Identity verification is an important step in ensuring compliance with these SAR filings just as it is with broader AML and sanctions compliance for regulated lenders. Further, auto dealers (many of which are also lenders) must also report if they receive more than $10,000 in cash.[61] Identity verification is thus also critical

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[56] HMDA, Pub. L. No. 95-200, Title III, 89 Stat. 1124, 1125 (December 31, 1975), available at https://www.govinfo.gov/content/pkg/STATUTE-89/pdf/STATUTE-89-Pg1124.pdf.

[57] FHFA Validation and Approval of Credit Score Models, *op. cit.*

[58] CFPB, Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 12 C.F.R. § 1026 (2013), available at https://www.govinfo.gov/content/pkg/FR-2013-01-30/pdf/2013-00736.pdf.

[59] Financial Crimes Enforcement Network (FinCEN), OCC, FRB, FDIC, OTS, and NCUA, Customer Identification Programs for Banks, Savings Associations, Credit Unions and Certain Non-Federally Regulated Banks, 12 C.F.R. §§ 21, 208, 211, 326, 563, and 748 and 31 C.F.R. § 103 (2003), available at https://www.govinfo.gov/content/pkg/FR-2003-05-09/pdf/03-11019.pdf.

[60] FinCEN, FinCEN Suspicious Activity Report (FinCEN SAR) Electronic Filing Requirements, (October, 2019), available at https://bsaefiling.fincen.treas.gov/docs/XMLUserGuide_FinCENSAR.pdf.

[61] FinCEN, Internal Revenue Service (IRS), Report of Cash Payments Over $10,000 Received in a Trade or Business, (Revised August 2014), available at https://www.irs.gov/pub/irs-pdf/f8300.pdf.

across the broad spectrum of lenders to ensure compliance with federal standards that, if violated, can result in heavy fines or even criminal penalties.

Identity verification through the information provided by consumer reporting agencies is a critical tool on which almost all lenders rely to ensure compliance with all of these requirements. Indeed, many will refuse to do business with a consumer who does not permit access to his or her credit report precisely because the risks of mis-identification are so high and the cost of identity verification without reliance on a credit report is so great. As a result, consumer reporting provides lenders with information to enhance adherence to law-enforcement rules essential to national security and sound finance.

### *F. Case Histories*

To assess the value proposition of credit reporting to both borrowers and lenders, it is helpful to assess loan categories in which credit reporting either does not exist or has been only sporadically adopted. To the extent credit reporting is found to improve credit availability without also increasing default rates, then the benefits discussed above are demonstrable not just via policy analysis, but also difference-over-difference methodological assessment.

One recent case history assesses the impact of credit reporting on equipment lending, a critical sector funding three quarters of private non-residential U.S. investment.[62] This sector had not generally relied on credit reporting until a company entered this market in 2001. This case history concludes that lender information sharing through a credit-reporting company makes it easier for borrowers to "shop" for lenders and for lenders to evaluate prospective borrowers, especially for smaller credit amounts. Lenders are also less likely to make loans to problematic borrowers in this sector due to the information shared with a third-party credit-reporting company that competitors otherwise would not and often could not share with each other.

A second useful case study involves small business commercial lending. As a recent World Bank study shows for the U.S. and around the world,[63] credit for small-and-medium enterprises (SMEs) as each country defines this moving target has unique characteristics that make it challenging for private banks and even innovative non-banks to serve this equality-critical sector. First, determining the chances of success and then forecasting SME income is a significant challenge, especially for start-ups.[64] Small businesses are also very different in terms of products, services, legal requirements, local zoning ordinances, relevant employment wage and benefit requirements, and even applicable sanitary or recycling requirements.

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[62] Andrew Sutherland, "Does Credit Reporting Lead to a Decline in Relationship Lending" Evidence from Information Sharing Technology," *Massachusetts Institute of Technology (MIT) Sloan Research Paper No. 5170-16*, (March, 2018), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2626924.
[63] Meghana Ayyagari, Asli Demirgüç-Kunt, and Vojislav Maksimovic, SME Finance World Bank Policy Research Working Paper 8241, (November, 2017), available at http://documents.worldbank.org/curated/en/860711510585220714/pdf/WPS8241.pdf.
[64] *Ibid.*

Further, there is no equivalent to a mortgage down payment for small-business lending, with investor or other highly-variable collateral serving this purpose to the extent local law or other legal requirements allow a lender to take possession of any such collateral. Even where legal possession of collateral is possible, small-business collateral – handyman tools, etc. – is often extremely portable or illiquid (e.g., restaurant equipment for a particular type of cuisine). Some nations have created "collateral menus" or rating systems to standardize small-business collateral to good effect,[65] but the U.S. has no comparable system nor is there yet any other accepted way to standardize small-business loans to create a deep, liquid secondary market suitable for funding even very small loans.

In the U.S., there is only a limited version of these collateral ratings for U.S. small business lending, challenging large-volume, standardized lending and requiring small businesses often to rely on an owner's personal credit or home equity to fund a start-up or continuing operation. The Fed's most recent assessment[66] found that 86 percent of small businesses with employees rely on their owners' personal credit scores to obtain a loan. 58 percent of small businesses with debt secure that debt with a personal guarantee from owners and 31 percent secure it with the owners' personal assets. Lenders are desperate for standardized data on small-business borrowers,[67] but it is likely that any such data will lack the reliability, discipline, and rights associated with data provided by regulated credit-reporting companies.

## IV. International Evidence

Credit reporting is internationally recognized as a vital part of a country's financial infrastructure and as an "activity of public interest,"[68] meaning credit reporting generally is viewed as beneficial to the welfare of the public at large as well as to individuals within a particular society. The World Bank also found[69] that credit reporting results in more efficient credit markets and lower credit costs to borrowers, which in turn lead to greater capacity for productive investment spending. Put another way, holding all else equal, countries with CRAs have more productive economies than those that do not because the benefits of credit reporting result in greater capacity for investments in the people, machinery, equipment, and other goods that increase an economy's productive capacity. Credit reporting thus creates a virtuous cycle in which greater efficiency and lower costs produce greater growth and productivity, the profits from which can then be fed into further investments producing still more growth and productivity.

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[65] *Ibid.*

[66] FRB, "Small Business Credit Survey," *Report on Employer Firms* 2019, 9 (April 16, 2019), available at https://www.fedsmallbusiness.org/press/2019/sbcs-report-on-employer-firms-04162019.

[67] Nathan DiCamillo, "Bank vendors hungry for small-business analytics," *American Banker*, July 9, 2019, available at https://www.americanbanker.com/news/bank-vendors-hungry-for-small-business-analytics.

[68] World Bank, *General Principles for Credit Reporting*, (September, 2011), available at http://documents.worldbank.org/curated/en/662161468147557554/pdf/70193-2014-CR-General-Principles-Web-Ready.pdf.

[69] *Ibid*.

The benefits to both individuals and the economy as a whole are so large that the World Bank with the support of the Bank for International Settlements (BIS) has published general principles for credit reporting outlining best practices that countries should incorporate into their credit-reporting frameworks. These principles[70] urge jurisdictions without credit reporting systems to adopt them, arguing that the insights provided by credit reporting mitigate a "fundamental problem" of asymmetric information between borrowers and lenders in credit markets. Information asymmetry means that participants in a transaction – e.g., borrowers and lenders – have different and/or more or less complete information and thus can gain undue advantage. For example, a borrower who knows that he or she is not a responsible borrower but needs credit can in conditions of information asymmetry portray creditworthiness and thus obtain credit that puts the lender at risk. Conversely, a borrower without access to a transparent credit score may think he or she is a high-risk borrower, obtaining credit at predatory prices even though regulated lenders would readily take the risk.

The World Bank study also finds that the share of a country's population with access to credit and other financial products increases with the improved information flows resulting from consumer reporting.[71] Conversely, countries in which credit reporting is lacking or completely absent may experience "credit rationing," a phenomenon in which lender credit supply is mismatched with potential borrower demand because lenders may view potential borrowers as more risky than they in fact are and thus deny credit or raise its price to prohibitive levels. Further, when credit is offered in countries without credit reporting, it may be subject to adverse selection – i.e., when safe borrowers are unwilling or unable to accept the higher interest rates necessary to satisfy low-information lenders, only risky borrowers will seek loans. As noted earlier, this results in moral hazard – i.e., borrowers are sanguine about obtaining credit because they do not expect to pay it back.

The ability of credit reporting to mitigate adverse-selection and moral-hazard problems through reductions in information asymmetries between lenders and borrowers is reflected in research from the European Corporate Governance Institute (ECGI).[72] By improving lender knowledge of an individual applicant's credit characteristics (e.g., past behavior, current debt exposure), credit bureaus are found to reduce problems that lead to adverse selection, thus diminishing the share of loans originated that will go into default. This is particularly important in countries where creditors have limited legal recourse to pursue repayment or when lending occurs across borders. Lenders are also found to increase extensions of credit as information asymmetries drop without adversely affecting overall loan performance. Additionally, borrower knowledge that credit performance on current loans will affect future ability to borrow increases borrower incentives to repay, diminishing the incentives that lead to moral hazard and contributing to the observed decrease in non-performing loans.

Evidence from internationally-focused research also demonstrates both quantitatively and qualitatively the positive impact of consumer reporting on the abundance, performance, and price of credit for consumers and businesses. Looking at countries in Eastern Europe and the former Soviet Union that previously lacked credit-reporting systems, researchers at the ECGI found[73] that the introduction of credit

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[70] *Ibid*.

[71] *Ibid*.

[72] Martin Brown, Tullio Jappelli, and Marco Pagano, "Information Sharing and Credit: Firm-Level Evidence from Transition Countries," *European Corporate Governance Institute (ECGI) Working Paper No. 201/2008*, (April, 2008), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=967485.

[73] *Ibid*.

information sharing systems such as those provided by private credit bureaus resulted in a multitude of benefits for consumers and businesses. As consumer-reporting frameworks were established, private sector credit grew as a percentage of GDP to 25 percent at the end of 2004, up from 15 percent only five years earlier. In addition to the expansion of private credit, the introduction of credit-information sharing also led to improvements in the quality of lending, with the ratio of non-performing loans decreasing by more than half over the same period. Notably, the introduction of consumer reporting bureaus was found to produce these positive results even in nations where lending conditions are otherwise disadvantageous (such as regimes that have poor protections of creditor rights or low accounting transparency).

However, it is not only the direct effects of the reduction in information asymmetries that lead to better credit outcomes. By levelling the informational playing field, credit bureaus also facilitate the entrance of new lenders – particularly cross-border ones – into previously-opaque lending markets. Research from the European Credit Research Institute (ECRI)[74] shows that the absence of credit reporting in a particular nation or the inability of lenders outside of that country to access credit reporting information leads cross-border institutions either to refrain completely from entering these markets or to do so only through mergers with or acquisitions of domestic companies. In either case, there is limited or no impact on competition. However, when credit bureaus eliminate information asymmetries between domestic and foreign lenders, then foreign banking organizations tend to enter new markets through either branches or *de novo* entry, thus increasing the number of competitors. Increased competition among creditors then leads to reductions in the cost of credit to borrowers. The beneficial impacts of allowing foreign-based lenders access to domestic consumer reports are now recognized in EU law, which mandates that Member States may not discriminate between domestic and foreign creditors in the provision of access to any databases used in the Member State for assessing consumer creditworthiness.[75]

As the research cited above makes clear, increasing the ability of consumer reporting agencies to report across borders would bestow large economic benefits on immigrants to the U.S. Although U.S. CRAs have historically not engaged in cross-border data sharing due at least in part to complex regulation, specialized consumer reporting bureaus that operate on a cross-border basis have emerged in recent years[76] and at least one of the NCRAs is also now exploring how to facilitate cross-border data sharing.[77] By facilitating lender access to immigrants' credit history in their country of origin, these consumer reporting agencies are ensuring that immigrants do not become credit invisible after years of hard work building robust credit files.

[74] Caterina Giannetti, Nicola Jentzsch, and Giancarlo Spagnolo, "Information-Sharing and Cross-Border Entry in European Banking," *European Credit Research Institute (ECRI) Research Report No. 11*, (February, 2010), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1604537.

[75] European Union (EU), "Council Directive 2008/48/EC on credit agreements for consumers and repealing Council Directive 87/102/EEC" (2008) *Official Journal L133*, 69 (May 22,2008), available at https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:133:0066:0092:EN:PDF.

[76] Allen Taylor, "Moving Credit Data Across Borders With Big Data," *Lending Times*, February 21, 2017, available at https://lending-times.com/2017/02/21/moving-credit-data-across-borders-with-big-data/.

[77] Melissa Luz T. Lopez, "TransUnion exploring cross-border credit data sharing," *BusinessWorld*, March 29, 2019, available at https://www.bworldonline.com/transunion-exploring-cross-border-credit-data-sharing/.

## V. The Economic-Opportunity Value Proposition

As we have demonstrated above through original research and analysis of studies from the Federal Reserve, global agencies, and academics, consumer reporting has enhanced the ability of consumers to obtain sustainable credit, to enjoy wide choice among competitive lenders, to move without risk of losing access to credit, and to receive robust protection from credit, employment, and insurance discrimination. For example, we have for the first time demonstrated that consumers with more robust credit histories are more confident in their credit search, less financially fragile, and better able to meet both planned and unplanned needs.[78] We have also shown that LMI and minority borrowers have achieved greater access to credit due to the objectivity of credit reports.[79] We have also noted research concluding that credit reporting enables consumers to gain employment that earns more, increases their access to credit, and helps them to become more likely to start a small business that employs others because credit histories reflect credit performance.[80] We now also demonstrate that consumer reporting has direct and meaningful impact on overall U.S. economic opportunity – as we shall show, the greater the access to credit due to a credit report, the more robust the U.S. economy.

### *A. Ending Credit Invisibility*

Because of the importance of credit reporting to economic opportunity, the CFPB has studied potential obstacles to establishing a credit history, calling persons without them the "credit invisibles" because of the dire inequality consequences lack of a credit history is likely to have on household economic opportunity. A recent study notes that credit-invisible Americans "suffer from reduced access to lower-cost, mainstream credit and thus utilize payday lenders, pawn shops, check cashing, and rent to own."[81] As the agency's most recent assessment of credit invisibles found, credit reporting is in fact a strong platform for economic opportunity – 91 percent of Americans between 25 and 29 surveyed by the CFPB had a credit report, indicating to the Bureau that, even though few Americans have a report before turning 18, the vast majority do by the time they are thirty,[82] proving that credit histories quickly reach those demonstrating ability to earn the trust of creditors, employers, or insurers even before they have established a home of their own, obtained permanent employment, or needed insurance coverage.

Indeed, CFPB research indicates that even credit-invisible individuals gain benefits from credit reporting despite initial lack of a credit file. Simply the existence of regulated credit reporting enhances access to credit to invisible consumers. The CFPB found that credit cards are the most common product to trigger the creation of a consumer credit record,[83] suggesting that lenders

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[78] See pages 6-7.
[79] See page 12-13.
[80] See page 5.
[81] Michael Turner, Patrick Walker, and Chet Wiermanski, *Changing the Lending Landscape: Credit Deserts, the Credit Invisible, and Data Gaps in Silicon Valley*, Policy and Economic Research Council (PERC), 4 (November, 2017), available at https://www.perc.net/wp-content/uploads/2017/11/Credit_Desert.pdf.
[82] Kenneth P. Brevoort and Michelle Kambara, *CFPB Data Point: Becoming Credit Visible*, *op. cit.*
[83] *Ibid.*

are willing to extend credit to consumers who lack a credit file at the time they apply for credit in order to enhance longer-term customer relationships.

The CFPB found that only 5.6 percent of consumers whose first credit file entry was a credit card used a secured credit card, a more costly form of credit card that requires a pre-posted balance to offset charges.[84] Notably, the CFPB postulates that commercial banks are often willing to lend to credit invisible consumers with whom they have existing deposit account relationships. These extensions of credit then are reported, bringing the consumer out of credit invisibility.

Credit reporting also allows credit invisibles to transition out of invisibility through means other than opening an individual credit account, although this is clearly the dominant method. The CFPB found that about 65 percent of those who transition out of credit invisibility do so by opening an account themselves despite the lack of credit history.[85] Another 20 percent were able to transition out of invisibility by either opening an account as a co-borrower with another individual who may have already had a credit history or by becoming an authorized user on someone else's account.[86]

This sharp improvement in credit visibility in part results from the fact that credit reports now include significant amounts of non-traditional data – e.g., rental histories, bill-payment records for telecommunications devices, etc. As the CFPB has noted,[87] LMI households use very different "entry products" to begin credit histories under traditional reporting data, a fact that often delays credit availability to later ages and thus increases obstacles to economic mobility and long-term wealth accumulation. Additional applications and uses of alternative data could produce even better results. A recent academic study of alternative data's benefits on financial inclusion found that combining call-detail records – logs of phone calls between a telecommunication provider's customers – with traditional data contained in consumer reports in credit scoring models significantly increases scoring-model performance.[88] This research used call-detail records in combination with credit and debit account information of customers to build "call networks," which were then analyzed to understand how the influence of prior defaulters propagates through this network. Including these results in scoring methodology resulted in more accurate prediction of creditworthiness compared to methodologies using only traditional data. However, current scoring models developed by VantageScore and FICO do not take this data into account. Currently the only mobile phone information being used in credit decisions is whether or not a consumer has paid her or his bill on time.

It is likely that innovations using alternative data also have had positive benefits on recent immigrants. The Federal Reserve Board's 2007 study posited that potential challenges to immigrant credit scores and resulting credit access derived from the failure of scoring

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[84] *Ibid.*
[85] *Ibid.*
[86] *Ibid.*
[87] *Ibid.*
[88] María Óskarsdóttir, Cristián Bravo, Carlos Sarraute, Jan Vanthienen, Bart Baesens, "The value of big data for credit scoring: Enhancing financial inclusion using mobile phone data and social network analytics," *Applied Soft Computing Journal* 74, 26 (2019), available at https://www.sciencedirect.com/science/article/pii/S156849461830560X.

methodology at that time to use alternative data such as rental payments.[89] As these alternative data have become available, immigrant credit access has grown. The most recent data from the FDIC[90] indicate that more than 70 percent of immigrants who have obtained U.S. citizenship have at least one credit card, and over half of immigrants who are not citizens also have at least one credit card. Between 2015[91] and 2017, the share of foreign-born citizens with a credit card increased more than three percentage points and the share of foreign-born noncitizens with a credit card increased by almost nine percentage points.

Non-traditional methods of analyzing data – whether those data are traditional or not – have also in recent years attempted to improve underwriting and other lending functions with an eye towards increasing inclusion and fairness. Algorithmic underwriting techniques in particular have proliferated as fintech lenders have gained greater market share. However, it remains unclear as to whether such methods are capable of increasing fairness across different groups of individuals. In a recent Congressional hearing focused on examining bias in algorithmic underwriting, one subject matter expert testified that in order to increase fairness by race in a particular algorithm, it may be necessary to decrease fairness by gender.[92] As this study shows, neither the FRB[93] nor the FTC[94] believe such a trade-off exists using methodologies relying on CRAs and consumer reports (e.g., VantageScore/FICO credit scores). Several U.S. Senators have also recently raised concerns that the use of algorithmic underwriting by fintech lenders is having a disparate impact on borrowers of color.[95]

### *B. U.S. Economic Growth*

As the chart below demonstrates, in recent years an increase in the growth of credit invisibles is correlated with a drop in employment growth, controlling for GDP growth rate. An increase in the growth of the unbanked population is also associated with a reduction in employment growth, although to a lesser degree. Thus, as U.S. employment growth remains positive, the growth rate of U.S. households that are credit invisible and/or unbanked falls.

Specifically, we find that the number of credit-invisible individuals grew 1.5 percent in 2011, with this growth rate decreasing on an annual basis between 2011 and 2016, becoming negative starting in 2015. That is, the number of credit-invisible individuals began to decrease

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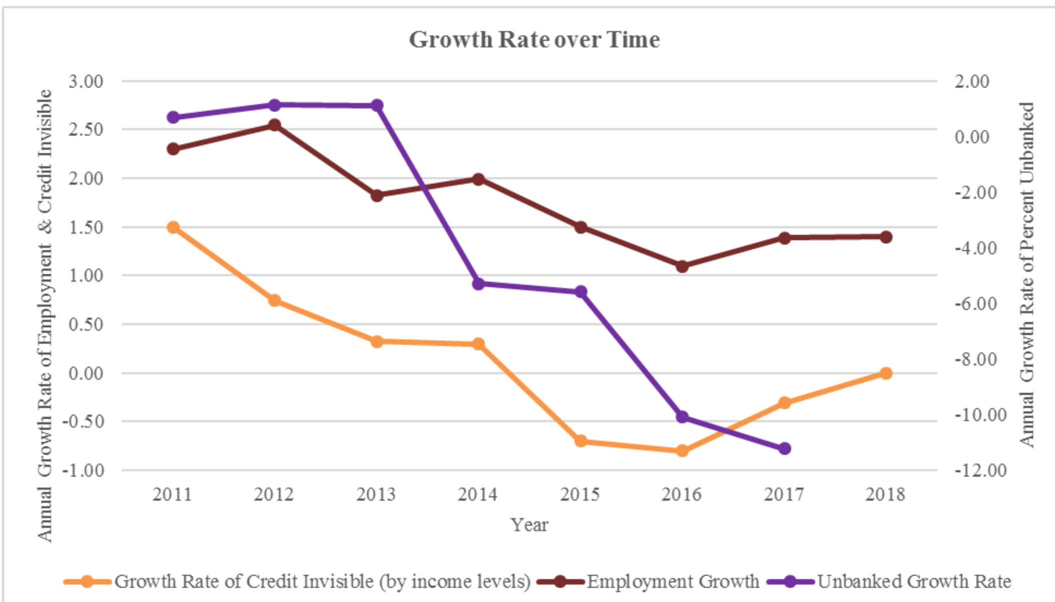
[89] FRB, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, *op. cit.*
[90] FDIC, *2017 FDIC National Survey of Unbanked and Underbanked Households Appendix Tables*, (October, 2018), available at https://www.fdic.gov/householdsurvey/2017/2017appendix.pdf.
[91] FDIC, *2015 FDIC National Survey of Unbanked and Underbanked Households Appendix Tables*, (October 20, 2016), available at https://www.fdic.gov/householdsurvey/2015/2015appendix.pdf.
[92] Michael Kearns, *Testimony before the House Financial Services Committee's Task Force on Artificial Intelligence: Testimony of Prof. Michael Kearns*, 2 (February 12, 2020), available at https://financialservices.house.gov/uploadedfiles/hhrg-116-ba00-wstate-kearnsm-20200212.pdf.
[93] See page 4.
[94] See page 12.
[95] Sen. Kamala Harris, "Harris, Senate Democrats Press Upstart, Lenders for Answers Following Reports of Higher Interest Rates for Students of Minority-Serving Institutions," February 13, 2020, available at https://www.harris.senate.gov/news/press-releases/harris-senate-democrats-press-upstart-lenders-for-answers-following-reports-of-higher-interest-rates-for-students-of-minority-serving-institutions.

on an annual basis starting in 2015. Annual credit-invisible growth remained negative or was zero from 2015 through 2018, the most recent available data. Over the eight years in which credit visibility improved, the annual growth rate of employment was positive in every single year, with our analysis concluding that employment growth is negatively correlated with the growth of the number of credit invisibles. As credit invisibility decreased, employment increased.

Further, the annual growth rate of unbanked households as a share of all households became negative. That is, unbanked households as a share of all households began to decrease as the growth rate of credit invisibles approached zero. The decline in the share of unbanked households accelerated annually as credit-invisibility growth also became negative starting in 2015.




Source: Based on analysis of data from Bureau of Labor Statistics, American Factfinder, FDIC Survey of Unbanked and Underbanked Households, *Data Point: Credit Invisible* (CFPB, 2015).

As a result, the penetration of credit reporting across the spectrum of U.S. households regardless of income, race, gender, sexual orientation, ethnicity, religion or other factors is correlated with U.S. economic growth and has far-reaching economic-equality implications for all of those once left out of the U.S. economic mainstream. As previously noted,[96] direct employment rises in concert with credit visibility, with wage increases and higher rates of small-business formation also tracking entry into the credit-reporting arena.

## VI. Future Research

[96] See page 5.

Although some of the most authoritative research cited above is recent, much dates back at least a decade. Since then, both consumer finance and financial regulation has changed in often critical ways even as economic inequality has continued to grow, especially in the U.S. With U.S. and global policy-makers looking to enhance financial inclusion without risk to vulnerable households or the broader financial system, additional research would illuminate:

- Alternative-Data Risk: In 2019, U.S. financial regulators finalized a new policy on "alternative" data,[97] defined here to mean data outside credit reporting agency reports or resulting credit scores. This policy encourages innovation while binding firms to safety-and-soundness and anti-discrimination requirements. However, it is unclear if effective consumer protections are ensured due to the exemptions noted above for consumer financial data derived from or housed outside the framework governed by FCRA and the CFPB. Given the GAO's recommendations for like-kind protections for alternative data when compared to that housed at consumer reporting agencies, it is timely to assess whether financial regulators should condition alternative-data use on additional consumer-protection and prudential safeguards. The FHFA has adopted a different approach to alternative scoring systems,[98] suggesting also that varying regulatory policies may soon complicate credit availability, innovation and competitiveness in the absence of consistent inter-agency approaches.
- Sustainable Credit: As described above, there is extensive research validated by our original analytics demonstrating that current credit-reporting methodologies and resulting scores predict the likelihood of delinquency or default. However, it can be difficult to discern whether credit access resulting from sound credit histories is due to credit-bureau methodology or underlying creditworthiness data (e.g., prior existence of a savings account). Access to anonymized individual credit files is necessary to enhance understanding of the extent to which credit reporting captures data lenders or insurers might not otherwise obtain and organizes it in ways individual lenders are unlikely to match. This would illuminate whether borrowers with certain characteristics (i.e., savings accounts) are better able to obtain credit from lenders without direct access to these data. This would also assess the economic-opportunity value proposition, adding to our assessment of the mobility, efficiency, and legal protections. Research here could, for example, identify individuals or households with like-kind financial characteristics to determine the extent to which those with credit files are better able to obtain credit that is then repaid as promised versus households denied credit or obtaining it from less-regulated providers on terms and conditions that cannot be repaid as required. This research would need to ensure that analysis is over the full course of the business and financial cycle to ensure that like-kind borrowers are not only able to repay loans on like-kind terms, but also to do so under stress. As we have noted, it is not sufficient to show only that credit histories at regulated reporting agencies enhance credit access, but also to build on our research to ensure that sustainable, equality-enhancing credit is caused by or at least significantly correlated with credit-report agency methodologies and resulting scores along with related consumer protections.
- Economic Opportunity: The GAO has recently assessed the extent to which Americans aged 18 to 37 (i.e., millennials) have achieved greater income or wealth as their parents at the same age.[99] The

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[97] FRB, CFPB, FDIC, NCUA, and OCC, *Interagency Statement on the Use of Alternative Data in Credit Underwriting*, December 3, 2019, available at
https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20191203b1.pdf.

[98] FHFA Validation and Approval of Credit Score Models, *op. cit.*

[99] GAO, "Millennial Generation: Information on the Economic Status of Millennial Households Compared to Previous Generations," *GAO-20-194*, (December, 2019), available at https://www.gao.gov/assets/710/703222.pdf.

study's findings show distressing gaps in inter-generational economic mobility, in part because millennials on average have student loans of over 100 percent of their income. Worse, lower-income millennials have student loans over 372 percent of income. As noted above, existing research demonstrates that some adverse information can be dropped from credit reports without putting borrowers at risk and with considerable economic-equality benefit. Additional research could identify ways credit bureaus could refine their methodology to enhance access to sustainable credit for millennials to ensure ongoing student-loan repayment without undue financial risk or day-to-day hardship. Particular attention might here be paid to ways to enhance home ownership given its importance to wealth accumulation and retirement security.

- Counter-Cyclicality: As noted above, consumer reporting agencies have begun to use "trended" data to track consumer behavior over thirty months. While this is still shorter than the full business or financial cycle (often considered to be approximately seven to ten years), it enhances understanding of consumer behavior under household stress. Additional research is needed to determine if "snapshot" data make reporting and resulting scoring "procyclical" – i.e., if assuming that borrowers are low-risk (i.e., high-score) borrowers at the top of the cycle increases credit availability that then creates undue household debt burden and financial-market risk in a downturn. This research could then assess whether broader trending is warranted or if alternative methodologies would permit lenders and policy-makers to rely on credit reports and scores across the business cycle.

## VII. Conclusion

The consumer credit reporting system has important positive effects on consumers and the economy. This meta-analysis of regulated consumer reporting demonstrates that the process of gathering personally-identifiable information from traditional and non-traditional sources using traditional and non-traditional personal data makes it more likely that low-income, young, minority, and otherwise disadvantaged Americans will more quickly enter the economic mainstream, thus enhancing prospects for personal prosperity and national economic equality. Regulated consumer reports also enhance the safety and soundness of U.S. consumer finance, a critical policy objective in light of the macroeconomic damage of financial downturns and the personal hardship that results when consumers cannot meet their financial obligations. These personal and macro results in aggregate support U.S. economic growth by increasing employment, a vital economic-opportunity result especially for low-and-moderate income households for whom employment opportunity is particularly critical.

This evidence combined with that from the international comparative analysis confirms that regulated U.S. consumer reporting has significant social-welfare and personal well-being implications. These would be at risk if the objectivity and completeness of consumer reporting is damaged or if critical economic opportunity decisions such as the granting of credit or employment migrate outside the reach of current legal safeguards. Were this to occur, the chances of credit and employment discrimination would increase in concert with the potential for negative economic-opportunity and macroeconomic-growth effects.

# Annex
# Credit Reporting Legal Safeguards

### *A. FCRA*

First, the Fair Credit Reporting Act (FCRA)[100] governs consumer reporting agencies, furnishers, and third parties that request and use consumer reports by, among other things, regulating the collection, maintenance, and disclosure of a consumer's personal information. The law also applies to any communications prepared by a CRA that bear on a consumer's creditworthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living when these reports are used or collected to establish eligibility for personal or household credit, insurance, employment, or for other authorized purposes (e.g., identity verification).

Pursuant to the FCRA, credit bureaus must also maintain procedures to ensure the accuracy of their consumer reports and provide a dispute-resolution process in which consumers may contest the completeness or accuracy of any item on their report. Further, a consumer's ability to review a free annual report provided nationwide by the largest CRAs and identify inaccuracies ahead of seeking credit, employment, or insurance enhances the chances that consumers achieve their economic goals. Consumers may well not have the opportunity to correct the data on which these critical decisions are made when they are derived from other sources. Credit reports also enhance economic opportunity and identity protection because credit reports lead to scores by which consumers can readily anticipate third-party judgments about credit worthiness, employability, or insurance risk. Sudden changes in scores are also a critical early warning of identity risk.

Another important avenue through which inaccuracies may be brought to the consumer's attention and then corrected are "adverse action" notices, which the FCRA requires[101] credit-report users to provide to consumers who have been denied credit, insurance, or employment based on the contents of a credit report. Adverse action notices provide consumers with the specific items in their credit report that resulted in their application being denied and the identity of the credit bureau providing the credit report. Consumers who believe an adverse action notice is based on inaccurate or incomplete information may then file a consumer dispute verification (CDV) form provided upon request by credit bureaus notifying them of the potential inaccuracies. Once a credit bureau has been alerted to a possible inaccuracy, it must conduct an investigation to determine the accuracy of disputed items within thirty days. If disputed items are found to be inaccurate or unverified, or if the required investigation is not completed within thirty days, then CRAs must delete any disputed item. If a consumer feels the dispute-resolution process has failed to address his or her concerns, then the consumer may challenge the CRA in court.[102]

[100] 15 U.S.C. §§ 1681 et seq., *op. cit.*
[101] FCRA, 15 U.S.C. § 1681m(a), *op. cit.*
[102] FCRA, 15 U.S.C. § 1681p, *op. cit.*

In order to provide additional layers of protection, CRAs may only provide a consumer credit report to parties with a permissible purpose (e.g., credit or insurance underwriters) and must implement procedures to ensure that reports are provided only to authorized users for legitimate purposes. These procedures must include that prospective users of credit reports identify themselves and certify the purpose for which the credit report is sought and that the information will not be used for any other purpose. Examples of specific actions in which credit bureaus engage with report users to fulfill these procedural requirements under the FCRA and go beyond them to protect report integrity include:

- reviewing public information sources and filings;
- reviewing websites and other public materials;
- checking financial references;
- visiting places of business;
- requiring contractual representation and warranties that credit report information will be used only for specified purposes;
- conducting on-boarding and training procedures; and
- ongoing monitoring to ensure credit report use is for legitimate and permissible purposes.

### *B. FACTA*

Statutory responsibilities under FCRA were augmented by the Fair and Accurate Credit Transactions Act (FACTA),[103] signed into law as an amendment to FCRA in 2003. FACTA mandates that the nationwide credit bureaus provide to consumers upon request a free copy of their credit report once per year.[104] It also required CRAs to implement policies to combat identity theft, including by allowing consumers to easily place fraud alerts in their files if they suspect they may be or are about to be a victim of fraud.[105] FACTA additionally provides military servicemembers with the ability to have CRAs place active-duty alerts in their file to prevent identity theft or other fraud while deployed.[106]

CRAs are also required under FACTA to take steps to repair the credit histories of victims of identity theft, including by blocking the reporting of information resulting from identity theft within four days of receiving evidence that identity theft has occurred.[107] FACTA further mandates that affected credit reports are disposed in a secure manner.[108]

### *C. Regulation V*

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[103] Fair and Accurate Credit Transactions Act (FACTA), Pub. L. No. 108-159, 117 Stat. 1952, (December 4, 2003), available at https://www.govinfo.gov/content/pkg/STATUTE-117/pdf/STATUTE-117-Pg1952.pdf.
[104] FACTA, 15 U.S.C. § 1681j(a), *op. cit.*
[105] FACTA, 15 U.S.C. § 1681c–1, *op. cit.*
[106] *Ibid*.
[107] FACTA, 15 U.S.C. § 1681c–2(a), *op. cit.*
[108] FACTA, 15 U.S.C. §1681w, *op. cit.*

The CFPB implements these statutory requirements under Regulation V.[109] It demands that data furnishers implement written policies to ensure that the information they provide to credit bureaus for use in credit reports is accurate, thus enhancing the quality of data CRAs provide. As with CRAs, furnishers are required to investigate information disputed by a consumer within thirty days, with consumers allowed to bring their dispute directly to the furnisher rather than a CRA. Regulation V also imposes on CRAs specific duties intended to prevent identity theft,[110] provide consumers with easy access to disclosures required by FCRA,[111] and prohibit CRAs from circumventing legitimate treatment as a nationwide CRA.[112]

### *D. Enforcement*

The CFPB is empowered to enforce the FCRA at all CRAs, not just the largest ones it also supervises and to wield similar authority over furnishers. In the event of violations, the CFPB may initiate administrative enforcement proceedings[113] or bring civil actions in federal court.[114] The CFPB is granted authority to obtain any appropriate legal or equitable relief and may do so through actions including requiring restitution, disgorgement, or compensation for unjust enrichment; mandating payment of damages or other monetary relief; imposing activity limits; or instituting civil monetary penalties.[115] However, the Bureau does not have criminal enforcement authority.

With specific regard to the nationwide consumer reporting agencies (NCRAs) – Equifax, TransUnion, and Experian, often referred to as the "Big Three" – the CFPB also has supervisory authority[116] to examine their policies, procedures, controls, and practices on a regular basis. This allows the CFPB to ensure that the CRAs with which consumers are most likely to engage are meeting their statutory and regulatory requirements at all times, not just after a violation is alleged. During these regular on-site examinations, supervisors assess the adequacy of the NCRAs' compliance management systems, procedures to handle disputes and to ensure the maximum possible accuracy of credit reports, credentialing procedures, and other activities subject to CFPB rules. If problems are found, the CFPB can take several actions to ensure issues are resolved, including the enforcement actions noted above. The CFPB itself under both Obama- and Trump-appointed directors has praised the efficacy of this supervisory regime for

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[109] Fair Credit Reporting (Regulation V), 12 C.F.R. § 1022 (2018), available at https://www.govinfo.gov/content/pkg/CFR-2018-title12-vol8/pdf/CFR-2018-title12-vol8-part1022.pdf.
[110] Regulation V, 12 C.F.R. §§ 1022.120-1022.129, *op. cit.*
[111] Regulation V, 12 C.F.R. §§ 1022.130-1022.138, *op. cit.*
[112] Regulation V, 12 C.F.R. § 1022.140, *op. cit.*
[113] Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) § 1053, 12 U.S.C. 5563 (2017), available at https://www.govinfo.gov/content/pkg/USCODE-2017-title12/pdf/USCODE-2017-title12-chap53-subchapV-partE-sec5563.pdf.
[114] Dodd-Frank § 1054, 12 U.S.C. 5564 (2017), available at https://www.govinfo.gov/content/pkg/USCODE-2017-title12/pdf/USCODE-2017-title12-chap53-subchapV-partE-sec5564.pdf.
[115] CFPB, *CFPB Supervision and Examination Manual*, Overview 7 (August, 2019), available at https://files.consumerfinance.gov/f/documents/cfpb_supervision-and-examination-manual.pdf.
[116] CFPB Defining Larger Participants of the Consumer Reporting Market Rule, 12 C.F.R. § 1090 (2018), available at https://www.govinfo.gov/content/pkg/CFR-2018-title12-vol9/pdf/CFR-2018-title12-vol9-part1090.pdf.

the positive benefits it has already bestowed on consumers and lenders and those still to come.[117]

Further, the courts may enforce many of the FCRA's provisions if a consumer brings suit on his or her own behalf. Litigation may lead to monetary compensation for damages inflicted due to either willful[118] or negligent[119] noncompliance with the FCRA as well as for litigation costs, giving even those with minimal financial resources the ability to bring suit. However, courts have generally held that neither injunctive nor declaratory relief for FCRA violations is available to private litigants.[120]

### *E. GLBA*

The Gramm-Leach-Bliley Act of 1999 (GLBA)[121] also governs consumer reporting agencies with regard to their adherence to privacy regulation. The FTC's "safeguards rule"[122] implements these provisions. Now pending revision,[123] the rule imposes standards governing the security and confidentiality of consumer records and information, provides for cyber-protection standards, and protects against unauthorized access or use. Safeguards also govern service providers and other aspects of a consumer reporting agency's use of consumer data and related information. Like-kind standards issued by the federal banking agencies[124] govern banking-organization and credit-union furnishers.

### *F. FTC Act*

In addition to the Federal Trade Commission's (FTC's) authority under GLBA, the FTC Act[125] imposes significant requirements CRAs must meet with regard to cybersecurity and data protection practices. The Act gives the FTC additional authority to take action against any business except banks, savings and loan institutions, federal credit unions, and common

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117 CFPB, "Supervisory Highlights Consumer Reporting Special Edition," *op. cit.*

118 FCRA, 15 U.S.C. § 1681n, *op. cit.*

119 FCRA, 15 U.S.C. § 1681o, *op. cit.*

120 *Washington v. CSC Credit Services., Inc.*, 199 F.3d 263, 268–69 (5th Cir. 2000), available at https://casetext.com/case/washington-v-csc-credit-services-inc

121 Gramm-Leach-Bliley Act (GLBA), Pub. L. No. 103-102, 113 Stat. 1338, (November 12, 1999), available at https://www.govinfo.gov/content/pkg/STATUTE-113/pdf/STATUTE-113-Pg1338.pdf.

122 FTC Standards for Safeguarding Customer Information (FTC Safeguards Rule), 16 C.F.R. § 314 (2018), available at https://www.govinfo.gov/content/pkg/CFR-2018-title16-vol1/pdf/CFR-2018-title16-vol1-part314.pdf.

123 FTC Standards for Safeguarding Customer Information, 84 Fed. Reg. 13158 (proposed April 4, 2019) (to be codified at 16 C.F.R. § 314), available at https://www.govinfo.gov/content/pkg/FR-2019-04-04/pdf/2019-04981.pdf

124 OCC, FRB, FDIC, and OTS, Interagency Guidelines Establishing Standards for Safeguarding Customer Information and Recession of Year 2000 Standards for Safety and Soundness, 66 Fed. Reg. 8616 (February 1, 2001) (to be codified at 12 C.F.R. §§ 30, 208, 211, 225, 263, 308, 364, 568, and 570), available at https://www.govinfo.gov/content/pkg/FR-2001-02-01/pdf/01-1114.pdf.

125 FTC Act, Pub. L. No. 63-311, 38 Stat. 717, (September 26, 1914), available at https://legcounsel.house.gov/Comps/Federal%20Trade%20Commission%20Act.pdf.

carriers[126] (e.g., wireless telecommunication providers) but including credit bureaus. The law provides for sanctions against "unfair or deceptive acts or practices," which the FTC has interpreted to include inadequate data security practices.[127]

While the FTC has not finalized a rule implementing specific cybersecurity requirements under the FTC Act, it has issued guidance[128] detailing cybersecurity safeguards sufficient to comply with the FTC Act. These include the use of encryption, firewalls, and breach detection systems as well as the maintenance of physical security of the hardware on which sensitive information is stored and stringent authentication standards (e.g., multi-factor authentication).

### *G. Illicit Finance*

The rule[129] implementing the 2001 Patriot Act[130] for banks, savings associations, and credit unions allows these firms to meet consumer identity verification requirements by verifying identifying information with a trusted third-party source, such as a credit bureau. Similar rules were issued by Treasury and the Securities and Exchange Commission (SEC) for broker-dealers[131] and by Treasury and the Commodity Futures Trading Commission (CFTC) for futures commission merchants and introducing brokers.[132] The rules recognize that consumer identity cannot be verified with government-issued IDs when consumers open accounts over the internet or by telephone or mail. Even when accounts are opened in person, the rules encourage firms not to rely solely on government-issued IDs for verification because these documents can be fraudulent and the elderly or other individuals may not legitimately be able to present unexpired photo IDs. In addition, Treasury's Office of Foreign Assets Control (OFAC) notes that credit reports provide information on whether entities on are on OFAC's list of Specially Designated Nationals and Blocked Persons. [133] U.S persons are generally prohibited from dealing with these OFAC-listed entities.

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[126] 15 U.S.C. § 46(a) (2017), available at https://www.govinfo.gov/content/pkg/USCODE-2017-title15/pdf/USCODE-2017-title15-chap2-subchapI.pdf.

[127] Congressional Research Service (CRS), "The Federal Trade Commission's Regulation of Data Security Under Its Unfair or Deceptive Acts or Practices (UDAP) Authority," *CRS Report 7-5700*, (September 11, 2014), available at https://fas.org/sgp/crs/misc/R43723.pdf.

[128] FTC, "Protecting Personal Information: A Guide for Business," accessed October 11, 2019, available at https://www.ftc.gov/system/files/documents/plain-language/pdf-0136_proteting-personal-information.pdf.

[129] FinCEN, OCC, FRB, FDIC, OTS, and NCUA, Customer Identification Programs for Banks, Savings Associations, Credit Unions and Certain Non-Federally Regulated Banks, *op. cit.*

[130] Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (Patriot Act), Pub. L. 107-56, 115 Stat. 272, (October 26, 2001), available at https://www.govinfo.gov/content/pkg/PLAW-107publ56/pdf/PLAW-107publ56.pdf.

[131] FinCEN, Securities and Exchange Commission (SEC), Customer Identification Programs for Broker-Dealers, 31 CFR Part 103 (2003), available at https://www.govinfo.gov/content/pkg/FR-2003-05-09/pdf/03-11017.pdf.

[132] FinCEN, Commodity Futures Trading Commission (CFTC), Customer Identification Programs For Futures Commission Merchants and Introducing Brokers 17 CFR § 42 and 31 CFR § 103 (2003), available at https://www.govinfo.gov/content/pkg/FR-2003-05-09/pdf/03-11016.pdf.

[133] Office of Foreign Assets Control (OFAC), OFAC FAQ 70, What Is This OFAC Information On My Credit Report?, available at https://www.treasury.gov/resource-center/faqs/Sanctions/Documents/faq_all.html.

### *H. State Law*

Beyond the litany of requirements with which CRAs must comply at the Federal level, a patchwork of state laws applies that often increases obligations when operating in certain states. Many states, such as California,[134] require heightened data-security standards, greater consumer file access, additional disclosures, and augmented security alert and freeze requirements (such as automatic freezes when certain events occur). Various state laws also place restraints on when CRAs are allowed to furnish consumer credit reports and contain additional limits as to what information may be placed into a consumer's file and how long it may stay there. For example, Texas and Maine in 2019 enacted laws prohibiting the inclusion of medical debt on consumer reports. All 50 states, the District of Columbia, and various U.S. territories have enacted laws requiring the CRAs to notify individuals of security breaches when personally identifiable information may have been compromised.[135]

### *I. Industry Actions*

Although the requirements placed on CRAs through law and rule at both the federal and state level are numerous, the consumer reporting industry has taken further actions in addition to the "reasonable procedures" required of it to ensure that consumer reporting data are of the highest quality. In addition to the actions noted above taken by CRAs to meet the requirements of federal and state law and rule, the CFPB has highlighted as praiseworthy[136] many activities the industry has voluntarily undertaken to improve the quality of consumer reporting data. Most notably, the industry has developed:

- a standardized reporting format (Metro 2) to facilitate information transfer between the CRAs and furnishers and to simplify interpretation of credit information. This form is required by all CDIA members and thus creates an industry standard that not only holds furnishers to account, but also creates positive incentives across the entire sector of credit-reporting agencies and furnishers. These standards protect consumers and create "network" effects – that is, the value of data across the lending, insurance, and employment system is high-quality and standardized so that consumer and provider objectives (see above) are more readily achieved;
- an automated system (e-OSCAR) to quickly resolve consumer disputes when an NCRA needs to interface with furnishers. This also significantly enhances credit-reporting network effects and resulting value;

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[134] California Consumer Credit Reporting Agencies Act, Cal. Civ. Code Tit. 1.6, §§ 1785, et seq., accessed October 15, 2019, available at https://leginfo.legislature.ca.gov/faces/codes_displayexpandedbranch.xhtml?lawCode=CIV&division=3.&title=1.6.&part=4.&chapter=2.&article=&goUp=Y.

[135] National Conference of State Legislatures, "Security Breach Notification Laws," September 29, 2018, accessed October 15, 2019, available at http://www.ncsl.org/research/telecommunications-and-information-technology/security-breach-notification-laws.aspx.

[136] CFPB, *Key Dimensions and Processes in the U.S. Credit Reporting System: A review of how the nations' largest credit bureaus manage consumer data*, *op. cit.*

- sophisticated processes at each of the NCRAs to match trade line data to the correct consumer despite challenges such as consumers with similar – or in some cases identical – names or addresses, typos in credit and other applications, colloquial variations, and other complexities; and
- the National Consumer Assistance Plan.[137] This initiative includes voluntary restraints on the appearance of certain debts on consumer reports, including debts that did not arise from a contract or agreement by the consumer to pay (e.g., traffic tickets) and medical debt that is less than 180 days old. It also requires debt collectors to include original creditor information with each account being reported for collection, regularly update the status of unpaid debts, and promptly remove debts no longer being pursued for collection. The Plan additionally calls for CRAs to monitor furnisher adherence to reporting requirements and to take corrective action when furnishers are noncompliant.

Due to the patchwork of state laws, the NCRAs in many instances will also apply the most stringent state requirements across all consumers, providing the benefit of these requirements without any legal obligation to do so.

[137] National Consumer Assistance Plan, "See how the credit reporting agencies are making changes as part of the National Consumer Assistance Plan," accessed November 4, 2019, available at http://www.nationalconsumerassistanceplan.com/highlights/.