PREPARED STATEMENT OF

THE FEDERAL TRADE COMMISSION

on

THE FAIR CREDIT REPORTING ACT

Before the

FINANCIAL INSTITUTIONS AND

CONSUMER CREDIT SUBCOMMITTEE

of the

HOUSE FINANCIAL SERVICES COMMITTEE

Washington, D.C.

June 4, 2003

[1] While the views expressed in this statement represent the views of the Commission, my oral presentation and responses to questions are my own and do not necessarily reflect the views of the Commission

exponentially.[2] Indeed, consumer spending accounts for over two-thirds of U.S. gross domestic product and consumer credit markets drive U.S. economic growth.[3]

The credit reporting industry developed in tandem with the burgeoning of consumer credit. Early on, credit reporting was local or regional and relatively unsophisticated; the amount of information collected was limited and not standardized. Credit bureaus (consumer reporting agencies)[4] manually recorded consumer information on index cards, updated irregularly, and often retained indefinitely. Over time, however, small credit bureaus grew to become large repositories of information on consumers.[5]

Today, the credit reporting system, consisting primarily of three main credit bureau repositories, contains data on as many as 1.5 billion credit accounts held by approximately 190 million individuals.[6] Creditors and others voluntarily submit this information to centralized,

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[2] In 1946, the beginning of the post-war period, total outstanding consumer credit stood at $55 billion; by 1970, the time of enactment of the FCRA, it had grown to $556 billion. [Figures adjusted for inflation.] Today it is $ 7 trillion. *See* Fred H. Cate, Robert E. Litan, Michael Staten, and Peter Wallison, "Financial Privacy, Consumer Prosperity, and the Public Good: Maintaining the Balance," AEI-Brookings Joint Center for Regulatory Studies, March 2003, at 1.

[3] *Id.* at 8.

[4] "Consumer reporting agency" is the term used in the FCRA, and reflects the fact that consumer information is collected and reported for a variety of purposes in addition to credit transactions. In common terminology, however, the agencies are known as "credit bureaus" or "credit reporting agencies." (Similarly, "credit report" and "credit history" are commonly-used non-technical terms for "consumer report.") The term "repository" is most often reserved for the large, national bureaus that collect and store information on over 190 million consumers. The "repository" agencies, in turn, are sometimes referred to as the "big three," in recognition of the three major companies that have predominated for several years – Equifax, Experian, and Trans Union. A fourth company, Innovis Data Services (an affiliate of CBC Companies), also maintains "a national database of consumers with unfavorable current or past credit histories." *See* http://www.innovis-cbc.com/products.htm.

[5] For a more complete recitation of the early history of the consumer reporting industry, *see* Retail Credit Co., 92 F.T.C. 1 at 134-36 (1978).

[6] *See* "An Overview of Consumer Data and Credit Reporting," *Federal Reserve Bulletin*, February 2003, at 49.

nationwide repositories. Lenders analyze this data and other information to develop sophisticated predictive models to assess risk, as reflected in the consumer's credit score.[7] The flow of information enables credit grantors to make more expeditious and accurate credit decisions, which benefits consumers as a whole. These benefits are illustrated by a study of credit bureau files that found that nearly 20% of the currently-reported active accounts had been open for less than 12 months.[8]

The modernization of credit reporting has played a key role in providing American consumers rapid access to consumer credit. It was not that many years ago that applying for credit required a personal visit to a loan officer. The loan officer, if he did not know you personally, contacted your references, including other creditors, before making a decisi

[7] Scoring products are based on analyses of historical consumer credit data, which allow creditors to develop models that help them predict the risk of default of a particular consumer. (The products are thus sometimes referred to as "risk scores" or "credit scores.") When the consumer applies for credit or other goods or services, the scoring programs that are developed from the complex analysis of past data compare the scoring factors to the individual information of the particular consumer, with the result reflected in a score that is generated for that application.

[8] *See* "An Overview of Consumer Data and Credit Reporting," *Federal Reserve Bulletin*, February 2003, at 52, table 2 ("All credit accounts and balances...").

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some other countries (and, indeed, with some credit bureaus in the early years of their development in this country) where only negative

Bulletin, February 2003, at 50, 68. To the extent that consumers have positive payment history only from non-traditional credit such as rent and utilities, this may limit their access to credit.

[12] *See, e.g.,*The World Bank, "World Development Report 2002," at 95 (2002); John M. Barron and Michael Staten, "The Value of Comprehensive Credit Reports: Lessons from the U.S. Experience," at 14, available online at http://www.privacyalliance.org/resources/staten.pdf (2000) (comparing the U.S. comprehensive credit reporting system to the Australian negative-information-only system).

[13] *See* http://www.cdiaonline.org/data.cfm for information on the uniform reporting format utilized by most creditors and other furnishers of information to consumer reporting agencies.

[14] *See* "An Overview of Consumer Data and Credit Reporting," *Federal Reserve Bulletin*, February 2003, at 50-51, 70-71.

others, without regard to the purpose for which the information was sought. Consumer awareness of credit reports was low due in part to the fact that users of reports were contractually prohibited by credit bureaus from disclosing the reports to consumers.[18] Even if a consumer could learn what was in his or her credit report, there was no way for the consumer to challenge erroneous information.

In response to rising concerns about the consumer reporting system, and recognizing its importance to business and consumers, Congress held hearings that resulted in passage of the FCRA to provide a framework for the industry and to secure protections for consumers. In enacting the FCRA, Congress specifically recognized that consumer credit "is dependent upon fair and accurate credit reporting."[19]

The 1970 FCRA imposed duties primarily on consumer reporting agencies, with very limited requirements on those that use credit reports, and no provisions aimed at those who furnished information to the reporting agencies.

The consumer reporting industry and the consumer credit economy changed tremendously in the decades following the enactment of the FCRA. The computerization of credit histories into vast databases accelerated markedly. The industry further consolidated, eventually comprising three major credit bureau repositories that maintain large, automated databases of consumer

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[18] Congress was especially concerned about this lack of awareness in the context of "investigative consumer reports" – reports on a consumer's character, general reputation, personal characteristics, or mode of living, obtained through personal interviews with neighbors, friends, or associates of the consumer – and thus provided special notice and disclosure requirements, together with other provisions, for investigative reports. Section 606 of the FCRA; 15 U.S.C. § 1681d.

[19] Section 602(a)(1), the Congressional findings and statement of purpose for the FCRA. 15 U.S.C. § 1681(a)(1).

[22] Prescreened offers, which are discussed in more detail below, are unsolicited "firm offers" of credit or insurance that are based on information from consumer reports. Generally they take the form of list

As recognized by Congress in its initial passage of the FCRA, the confidentiality of consumer report information is a fundamental principle underlying the statute.[24]

a. Permissible purposes

The FCRA is designed to protect consumer privacy in a number of ways. Primarily, it limits distribution of credit reports to those with specific, statutorily-defined "permissible purposes."[25] Generally, reports may be provided for the purposes of making decisions involving credit, insurance, or employment.[26] Consumer reporting agencies may [illegible]

[24] The congressional findings note the "...need to insure that consumer reporting agencies exercise their grave responsibilities with fairness, impartiality, and a respect for the consumer's right to privacy." Section 602(a)(4); 15 U.S.C. § 1681(a)(4). Under the "reasonable procedures" portion of the statement of purpose for the FCRA, Congress noted the importance of the "confidentiality" of consumer report information. Section 602(b); 15 U.S.C. § 1681(b).

[25] What constitutes a "consumer report" is a matter of statutory definition (Section 603(d); 15 U.S.C. § 1681a(d)) and case law. Among other considerations, to constitute a consumer report, information must be collected or used for "eligibility" purposes. That is, the data must not only "bear on" a characteristic of the consumer (such as credit worthiness, credit capacity, character, general reputation, or mode of living), it must also be *used* in determinations to grant or deny credit, issue insurance, make employment decisions, or make other determinations regarding permissible purposes. Trans Union Corp. v. FTC, 81 F.3d 228, 234 (D.C. Cir. 1996).

[26] Section 604(a)(3); 15 U.S.C. § 1681b(a)(3). Credit reports may also be furnished for certain on-going account-monitoring and collection purposes.

[27] 15 U.S.C. § 1681b(a)(3)(F). *See also* Note 33, *infra*, and text accompanying.

[28] Under Section 608 of the FCRA, government entities may obtain limited identifying information (name, address, employer) without a "permissible purpose." 15 U.S.C. § 1681f. The FCRA additionally now contains express provisions on government use of consumer reports for counterintelligence and counter-terrorism. Sections 625 and 626, respectively; 15 U.S.C. §§ 1681u, 1681v.

[29] Other permissible purposes specified in the FCRA include (1) in response to an order of a court or a Federal grand jury subpoena; (2) in connection w

some relationship with a business, could be said to implicitly waive the Act's privacy to help further that relationship."[32]

The 1996 amendments added provisions that reflected Congress' awareness of increased public concern about the privacy of personal information. For example, Congress added, for the first time, an express provision stating that the "legitimate business need" permissible purpose requires that the transaction be "initiated by the consumer."[33] Congress also added express language prohibiting any person from *obtaining* a consumer report without a permissible purpose.[34]

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[32] *Id.*

[33] Section 604(a)(3)(F)(i); 15 U.S.C. 1681b(a)(3)(F)(i). The review of an account "to determine whether the consumer continues to meet the terms of the account" supplies the other "legitimate business need" of this permissible purpose. Section 604(a)(3)(F)(ii); 15 U.S.C. 1681b(a)(3)(F)(ii).

[34] The 1970 FCRA prohibited consumer reporting agencies from *furnishing* consumer reports to those who do not have a permissible purpose, but there was no analogous provision aimed at those who obtained consumer reports (with the exception of a criminal provision imposed on those who obtained information on a consumer "under false pretenses." Section 619, 15 U.S.C. § 1681q).

b. Consumer right to opt out of prescreening.

The 1996 amendments also added an express permissible purpose for prescreening. As noted above, prescreened offers are unsolicited offers of credit or insurance that are made (typically in mass mailings) to consumers who were selected for the offer based on information in their credit reports. Prior to the 1996 amendments, the FCRA did not specifically address the use of consumer reports for such unsolicited offers. The Commission, however, had issued an interpretation of the FCRA in 1973 that permitted the use of consumer reports by creditors for unsolicited offers of credit if creditors followed guidelines set forth in the Commission's interpretation.[35] Those guidelines required every consumer on any list resulting from the use of consumer reports to receive a firm offer of credit – *i.e.*, the offer must be unconditional; all the consumer had to do to receive the credit was to accept the offer.

In the 1996 amendments, Congress added a number of provisions to the FCRA to provide an explicit statutory framework for prescreening.[36] The legislative process leading to the 1996

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[35] 16 C.F.R. § 600.5 (withdrawn in 1990 when the Commission *Commentary* was published; *see* notes 52-53, *infra*). The Commission's rationale for permitting prescreening was that the minimal invasion of consumer privacy involved in prescreening was offset by the fact that every consumer received an offer of credit. The four banking regulatory agencies also interpreted the FCRA to sanction prescreening for the entities under their jurisdiction.

[36] Sections 603(*l*); 604(c) and (e); and 615(d); 15 U.S.C. §§ 1681a(*l*), 1681b(c) and (e), and 1681m(d), respectively. "Firm offer of credit or insurance," the term used by Congress for what is commonly known as "prescreening," is defined in Section 603(*l*), which also contains much of the operable language governing prescreening. The permissible purpose is set out in Section 604(c) and the opt-out scheme is contained in Section 604(e). Section 615(d) recites the disclosures required of those who use consumer reports to make prescreened offers. *See* H. Rep. 103-486, 103rd Cong., 2nd Sess., 32 (1994)("The bill permits a consumer reporting agency to furnish limited information, commonly referred to as a prescreened list, in connection with such transactions only if the transaction consists of a 'firm offer of credit,' the consumer reporting agency has established a notification system whereby consumers can opt out to have their names excluded from consideration from such offers of credit, and the consumer has not elected to be so excluded. Under the bill, a pre-screened list, furnished by a consumer reporting agency in connection with a credit transaction that is not initiated by the consumer, may contain only certain types of information.").

[37] Section 603(*l*) limits permissible postscreening to verifying that consumers continue to meet the criteria used in the prescreening and to verify any application information (such as income or employment) that is used in the process of granting credit or insurance. Credit grantors are also permitted to require that consumers furnish collateral so long as the collateral requirement is established before the prescreening is conducted and is disclosed to the consumer in the solicitation that results from the prescre

[41] Section 604(d)(6); 15 U.S.C. § 1681b(d)(6). The opt-out is effective for two years if conveyed by telephone, or permanently (unless revoked) if conveyed in writing. Section 604(d)(4)(B); 15 U.S.C. § 1681b(d)(4)(B).

[42] Section 602(a)(1) of the F

[44] 15 U.S.C. § 1681g.

[45] Section 612 provi

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The 1996 amendments also made changes in the relationship between the FCRA and state laws. As originally enacted in 1970, the FCRA provided that the federal statute did not exempt persons from complying with state laws "with respect to the collection, distribution, or use of any information on consumers, except to the extent that those laws are inconsistent" with the FCRA. The 1996 amendments retained this language, but significantly modified the provision to preempt state laws in certain specified areas covered by the amended FCRA.[49]

Section 624 of the FCRA ("Relation to State Laws") now provides that no state laws may be imposed in the areas of (i) prescreening (including the definition of the term "firm offer of credit or insurance" and the disclosures which must be made in connection with prescreened offers), (ii) the time within which a consumer reporting agency must complete its investigation of disputed information, (iii) the adverse action notice requirements of Section 615, (iv) the obsolescence limitations and other provisions of Section 605, (v) furnisher obligations under Section 623, (vi) the consumer summary of rights required by Section 609(c) to be provided by consumer reporting agencies to consumers who obtain disclosure of their files, and (vii) information sharing by affiliates.[50] The specific preemptions are qualified in a number of respects, including specifying particular pre-existing state enactments to which the preemptions do *not*

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concerns have been introduced. In 2000, the Commission commented (*see* http://www.ftc.gov/os/2000/03/ltrpitofskysessions.htm) and testified with respect to one such proposal (*see* http://www.ftc.gov/os/2000/05/fcratestimony.htm). The Commission remains of the opinion that a legislative remedy of the type endorsed by the Commission in 2000 is the most appropriate response to these concerns.

[49] Thus, both before *and after* the 1996 preemptions, states were free to legislate in areas covered by the FCRA but not specifically preempted. *See, e.g.*, Colo. Rev. Stat. § 12-14.3-104 (providing for free annual credit reports).

[50] Section 624(b); 15 U.S.C. § 1681t(b).

apply.[51] The primary proviso with respect to the preempted provisions, however, is that after January 1, 2004, states may enact laws that (i) are specifically intended to supplement the FCRA, and (ii) give greater protection to consumers than is provided under the FCRA.

Finally, other significant additions of the 1996 amendments include authorizing states to enforce the FCRA, and adding civil penalty authority for the Federal Trade Commission.

IV. FTC Interpretive Guidance and Enforcement

When it enacted the FCRA in 1970, Congress provided that the Commission would be the principal agency to enforce the statute. To help foster understanding and ensure compliance with the law, the Commission engaged in extensive business education and guidance, including, in the first two decades, publishing over 350 staff opinion letters, a staff guidance handbook, and six formal Commission interpretations.[52] All of this material was then brought together in the Commission's 1990 *Commentary on the FCRA*.[53] The *Commentary* was well received and has served as a valuable explanatory and enforcement guide to industry and other affected parties. It also has assisted the staffs of the Commission and other regulatory agencies in interpreting the Act efficiently and consistently.

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[51] Section 624(d); 15 U.S.C. § 1681t(d). There is, moreover, a blanket "grandfathering" of state laws relating to the obsolescence limits of Section 605. Section 624(b)(1)(E); 15 U.S.C. § 1681t(b)(1)(E). An example is N.Y. Gen. Bus. L. § 380-j(f)(1)(ii)(paid judgments may not be reported for more than five years).

[52] The interpretations were published at 16 C.F.R. § 600 and were withdrawn when the Commission published the 1990 *Commentary*.

[53] 55 Fed. Reg. 18804 (May 4, 1990). The 1990 Commentary was the culmination of a proposal published in August 1988 and the Commission's review of over 100 submissions it received in response to its request for public comments on that proposal. 53 Fed. Reg. 29696 (August 8, 1988).

[54] The Commission also drafted and published language for the three notices required by the 1996 amendments to be distributed by credit bureaus: (1) a notice to consumer re

[58] Over the past seven years, 3.9 million of the five most popular FCRA brochures were distributed by the Commission. The information is duplicated on the Commission's web site, where the same brochures have registered over 1.6 million visits during the past five years. FCRA brochures such as "Building a Better Credit Record," "How to Dispute Credit Report Errors," and "Fair Credit Reporting" have each been distributed in numbers exceeding 100,000 per year over the past five years.

[59] Hospital & Health Services Credit Union, 104 F.T.C. 589 (1984); Associated Dry Goods, 105 F.T.C. 310 (1985); Wright-Patt Credit Union, 106 F.T.C. 354 (1985); Federated Department Stores, 106 F.T.C. 615 (1985); Winkleman Stores, Civ. No. C 85-2214 (N.D. Ohio 1985); Strawbridge and Clothier, Civ. No. 85-6855 (E.D. Pa. 1985); Green Tree Acceptance, Civ. No. CA 4 86 469 K (M.D. Tex. 1988); Quicken Loans Inc., D-9304 (April 8, 2003). *See also,* Aristar, Civ. No. C-83-0719 (S.D. Fla. 1983); Allied Finance, Civ. No. CA3-85-1933F (N.D. Texas 1985); Norwest Financial, Civ. No. 87 06025R (C.D. Cal. 1987); City Finance, Civ. No. 1:90-cv-246-MHS (N.D. Ga. 1990); Tower Loan of Mississippi,

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[62] *See*

[69] *See, e.g.*, Sabrina Jones and Sandra Fleishman, "One Claim Too Many? Insurance's New Policy: Use It and Lose It," Washington Post, November 10, 2002, at H01; Dan Oldenburg, "Car Insurers Take Credit Into Account," Washington Post, October 15, 2002, at C10; Albert Crenshaw, "Bad Credit, Big Premiums; Insurers Using Bill-Payment History to Help Set Rates," Washington Post, June 18, 2002, at E01.

[70] *See* Fred H. Cate, Robert E. Litan, Michae

[72] *Id. See also* Fred H. Cate, Robert E. Litan, Michael Staten, and Peter Wallison, "Financial Privacy, Consumer Prosperity, and the Public Good: Maintaining the Balance," AEI-Brookings Joint Center for Regulatory Studies, March 2003, at 12.

[73] *See, e.g.,* "An Overview of Consumer Data and Credit Reporting," *Federal Reserve Bulletin*

[75] *See, e.g.,* "An Overview of Consumer Data and Credit Reporting," *Federal Reserve Bulletin*, February 2003, at 70; Fred H. Cate, Robert E. Litan, Michael Staten, and Peter Wallison, "Financial Privacy, Consumer Prosperity, and the Public Good: Maintaining the Balance," AEI-Brookings Joint Center for Regulatory Studies, March 2003, *passim.*

[76] *See* http://financialservices.house.gov/media/pdf/040

[79] Section 602(a)(3) of the FC