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AN OVERVIEW OF THE CREDIT BUREAUS AND THE FAIR CREDIT REPORTING ACT

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED FIFTEENTH CONGRESS

SECOND SESSION

ON

EXAMINING THE CONSUMER REPORTING AGENCIES AND THE FAIR CREDIT REPORTING ACT

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AN OVERVIEW OF THE CREDIT BUREAUS AND THE FAIR CREDIT REPORTING ACT

THURSDAY, JULY 12, 2018

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:04 a.m., in room SD–538, Dirksen Senate Office Building, Hon. Mike Crapo, Chairman of the Committee, presiding.

OPENING STATEMENT OF CHAIRMAN MIKE CRAPO

Chairman CRAPO. The Committee will come to order. The Committee hearing today is entitled "An Overview of the Credit Bureaus and the Fair Credit Reporting Act".

Credit bureaus play a valuable role in our financial system by helping financial institutions assess a consumer's ability to meet financial obligations and also facilitating access to beneficial financial products and services.

Given this role, they have a lot of valuable personal information on consumers and, therefore, are targets of cyberattacks.

Last year, Equifax experienced an unprecedented cybersecurity incident which compromised the personal data of over 145 million people.

Following that event, the Banking Committee held two oversight hearings on the breach and consumer data protection at credit bureaus. The first hearing with the former Equifax CEO examined details surrounding the breach, while the second hearing with outside experts examined what improvements might be made surrounding credit reporting agencies and data security.

This Committee also recently held a hearing on cybersecurity and risks to the financial services industry. These hearings demonstrated bipartisan concern about the Equifax data breach and the protection of consumers' personally identifiable information, as well as support for specific legislative measures to address such concerns.

Some of these were addressed in Senate bill 2155, the "Economic Growth, Regulatory Relief, and Consumer Protection Act", which included meaningful consumer protections for consumers who become victims of fraud.

For example, it provides consumers unlimited free credit freezes and unfreezes per year. It allows parents to turn on and off credit reporting for children under 18 and provides important protections for veterans and seniors.

Last month a *New York Times* article commenting on the bill noted that "one helpful change . . . will allow consumers to 'freeze' their credit files at the three major credit reporting bureaus—without charge. Consumers can also 'thaw' their files, temporarily or permanently, without a fee."

Susan Grant, director of consumer protection and privacy at the Consumer Federation of America, expressed support for these measures, calling them "a good thing."

Paul Stephens, director of policy and advocacy at the Privacy Rights Clearinghouse, similarly noted that the freeze provision "has the potential to save consumers a lot of money."

But there is still an opportunity to see whether more should be done, and today's hearing will help inform this Committee in that regard.

Today I look forward to hearing more from the witnesses about the scope of the Fair Credit Reporting Act and other relevant laws and regulations as they pertain to credit bureaus; the extent to which the Bureau of Consumer Financial Protection and the FTC, whom the two witnesses represent today, oversee credit bureau data security and accuracy; the current state of data security, data accuracy, data breach policy, and dispute resolution processes at the credit bureaus; and what, if any, improvements could be made.

States have begun to react in their own ways to various aspects of the public debate on privacy, data security, and the Equifax data breach.

Two weeks ago, California enacted the California Consumer Privacy Act which will take effect on January 1, 2020. The act, which applies to certain organizations conducting business in California, establishes a new privacy framework by creating new data privacy rights, imposing special rules for the collection of minors' consumer data, and creating damages frameworks for violations and businesses failing to implement reasonable security procedures.

Many members are interested in learning more about what California and other States are doing on this front.

Additionally, 2 weeks ago, eight State banking commissioners jointly took action against Equifax in a consent order requiring the company to take various actions regarding risk assessment and information security.

I have long been concerned about data collection and data privacy protections by the Government and the private sector.

Given Americans' increased reliance and use of technology where information can be shared by the swipe of a finger, we should be careful to ensure that companies and Government entities who have such information use it responsibly and keep it safe.

Senator Brown.

OPENING STATEMENT OF SENATOR SHERROD BROWN

Senator BROWN. Thank you, Mr. Chairman. Thanks very much to our witnesses. Thanks for holding this hearing today. I hope my colleagues would excuse me to particularly welcome Ms. Twohig to our Committee. She is from the Consumer Protection Bureau, grew up in Fairview Park, a westside suburb of Cleveland. She graduated from Ohio State. She worked for the Cleveland Foundation, the preeminent community foundation in the United States of

America. She has a long career as a public servant with the FTC, the Treasury Department, and was an early employee of this terrific agency, the Consumer Financial Protection Bureau. And not to leave you out, but thank you both for joining us.

The consumer credit reporting system is stacked against Americans. A bad credit report can keep you out of a job; it can put you on a list where you will be targeted with expensive credit cards or high-cost loans. You are almost powerless to do anything about it.

Americans have basically no control over these reports that can dictate their lives and their family's plans for the future. They often do not know whether they are accurate or whether they are inaccurate.

Six years ago I chaired a Subcommittee hearing where consumer advocates in the CFPB identified problems in the credit reporting industry. We have had several hearings in this Committee over the last year on credit reporting companies and on data privacy. In the meantime, breach after breach has occurred.

Last year, as we know, 148 million Americans had their sensitive data stolen as hackers exploited a known security flaw that Equifax did not fix. Millions more have been affected by breaches at banks like JPMorgan Chase, stores like Target, Whole Foods, even Trump hotels. Congressional efforts, including provisions included in S. 2155, have not done anything meaningful to address accuracy of credit reports, to fix privacy concerns, or to give consumers controls over their own personal data.

At the same time, big tech companies continually add more and more of our personal information to their digital warehouses. They have financial and personal details about hundreds of millions of Americans. They see the potential for a big payday in selling that data to credit reporting companies. These companies are amassing more and more of our data, but still seem totally unprepared to deal with cyberattacks. They are building virtual, shall we say, silver platters for hackers.

People want and deserve a lot more control over their personal information. Credit reporting presents a unique problem because often Americans do not even know these corporations collect their data in the first place. Right now consumers cannot vote—as many of my colleagues like to say, cannot simply vote with their feet when a company does not treat them well, when a credit bureau fails to protect their privacy. Congress passed the Fair Credit Reporting Act in the first place to rein in credit bureaus that originally functioned as unsupervised supervisory agencies collecting personal information that we would be appalled to see in someone's credit report today.

After scandals at Facebook, people are rightfully worried about big companies once again compiling and selling piles of personal data on every American without our knowledge, out of our control or our consent. More Americans would be surprised at how lenders are putting this data to use. Last week the *Washington Post* ran a story about a company called "Mariner Finance" that uses a loophole in the FCRA to look at people's credit records without their permission and then targets them with scams. Mariner sends checks for thousands of dollars to struggling families that can be cashed the day they are plucked from the mail. But the checks are

really just expensive loans waiting to trap the consumer who cashes them.

Now, Mariner will tell you they are increasing "access to credit"—their term. But that was exactly what we were told about subprime loans. Some will say, including potentially your boss at the CFPB, that the market will take care of that. Well, the market clearly has not. The fact is Mariner is weaponizing people's credit history to target them with an expensive loan and making huge profits for the hedge fund that owns it. Your credit report can be used to force you into court, rightly or wrongly, to settle debts. But what if your credit card company or your cable provider erroneously reports a missed payment or defaulted account? They are protected. You cannot take them to court at all. And that is just absolutely outrageous.

It turns out that is a big problem. A CFPB paper found last year that credit reporting companies have not been doing enough to ensure the information they get is accurate. They are protected and consumers are not, in part because of the behavior of this U.S. Senate and because of a Supreme Court that moves more and more to protect corporate interests. What incentive do these companies have? The people they hurt will not be able to have their day in court.

We have heard all this before. The credit reporting system is backward. Like so much of our economy, it works for big corporations. It works for people with privilege. It does not work for regular Americans.

The Fair Credit Reporting Act is 50 years old. The amount and type of information collected today would have been unthinkable when it was created. It is time for a serious overhaul that puts Americans in control of their own data. I have introduced bills and so have many of my colleagues that would do just that. I hope the Committee will not only listen to the advice we get today, but will also take action to give people control over what should be their personal information.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you, Senator Brown. We will now move to our witnesses and their testimony.

First we will hear from Ms. Peggy Twohig, who currently serves as the Assistant Director for Supervision Policy in the Division of Supervision, Enforcement, and Fair Lending at the Bureau of Consumer Financial Protection. The Office of Supervision is responsible for developing strategy across bank and nonbank markets and ensuring that policy decisions are consistent across markets, charters, and regions.

After that we will hear from Ms. Maneesha Mithal, who serves as the Associate Director for the Division of Privacy and Identity Protection in the Bureau of Consumer Protection at the Federal Trade Commission. In this capacity she supervises the work in the area of data security, identity theft, credit reporting, and behavioral advertising and general privacy.

We appreciate both of you joining us today, and we will proceed in the order that you were introduced. Ms. Twohig.

STATEMENT OF PEGGY L. TWOHIG, ASSISTANT DIRECTOR, OFFICE OF SUPERVISION POLICY, DIVISION OF SUPERVISION, ENFORCEMENT, AND FAIR LENDING, BUREAU OF CONSUMER FINANCIAL PROTECTION

Ms. TWOHIG. Good morning, Chairman Crapo, Ranking Member Brown, and thank you for that special introduction. I am very proud of my Cleveland roots. And thank you for the opportunity to testify today about the work of the Bureau of Consumer Financial Protection to address consumer protections in the credit reporting market. My name is Peggy Twohig, and I am Assistant Director for Supervision Policy at the Bureau.

Credit reporting plays a critical role in consumer financial services and has enormous reach and impact. Over 200 million Americans have credit files with tradelines furnished voluntarily by over 10,000 providers. This information is used by creditors and other types of businesses to make decisions about individual transactions with consumers. In particular, creditors rely on this information to decide whether to approve loans and what terms to offer. Accurate credit reporting is important to creditors and other businesses to make good business decisions. For an individual consumer, an accurate credit report can be even more important given the significant impact that information can have on that consumer's ability to obtain financial and other products and services.

Because of the importance of accuracy to businesses and consumers, the structure of the Fair Credit Reporting Act creates interrelated legal standards and requirements to support the policy goal of accurate credit reporting. These requirements anticipate that all reports will not be perfect; instead, the FCRA requires that credit reporting agencies, or CRAs, have "reasonable procedures to assure maximum possible accuracy" of reports. It also imposes certain accuracy obligations on furnishers of credit report information. And the FCRA has a dispute and investigation framework, with obligations on both CRAs and furnishers, to ensure that potential errors are investigated and errors are corrected promptly.

The written testimony of the Bureau reviews the legal authority of the Bureau to supervise and enforce the Federal consumer financial laws applicable to CRAs. I will focus here on the work the Bureau has done exercising these authorities.

In both its supervision and enforcement work, the Bureau has focused on credit reporting accuracy and dispute handling by both CRAs and furnishers. As discussed in a special edition of Supervisory Highlights published last year, the Bureau's supervisory work has prioritized reviews of key elements underpinning accuracy. As a result of these reviews, the Bureau directed specific improvements in data accuracy and dispute resolution at one or more CRA, including: improving oversight of incoming data from the furnishers; instituting quality control programs of compiled consumer reports; monitoring furnished dispute metrics to identify and correct root causes; improved investigations of consumer disputes, including a review of relevant information provided by consumers; and improving communication to consumers of dispute results.

In supervising bank and nonbank furnishers, the Bureau has found furnishers that were not complying with their FCRA obligations and directed them to comply, including developing reasonable

written policies and procedures regarding the accuracy of information they furnish; taking corrective action when they furnished information they determined to be inaccurate; and bringing their dispute handling practices into compliance. The Bureau has also brought enforcement actions and entered into a number of settlements related to violations of the FCRA's accuracy and dispute investigation requirements.

Turning to data security, CRAs hold a tremendous amount of sensitive information about consumers. If CRAs do not protect this data, it may lead to data breaches, creating the risk of substantial harm to consumers, including the risk of identity theft. Since the Equifax breach, the Bureau has increased its attention to data security issues in our supervisory and enforcement work.

The Bureau has the authority to conduct data security investigations and to conduct examinations at certain nonbanks, including larger CRAs. This authority includes assessing the facts and circumstances to determine whether a CRA's data security practices constitute a violation of Federal consumer financial law, including the prohibition against unfair, deceptive, or abusive acts and practices, or the FCRA.

Our supervisory, enforcement, and consumer education efforts will continue in this important area. Consumers should have confidence that their credit reports are secure and comply with all applicable legal requirements.

Thank you again for the opportunity to testify today at this important hearing. I would be happy to answer your questions about the Bureau's work related to credit reporting.

Chairman CRAPO. Thank you very much.

Ms. Mithal.

STATEMENT OF MANEESHA MITHAL, ASSOCIATE DIRECTOR, DIVISION OF PRIVACY AND IDENTITY PROTECTION, BUREAU OF CONSUMER PROTECTION, FEDERAL TRADE COMMISSION

Ms. MITHAL. Thank you. Chairman Crapo, Ranking Member Brown, and Members of the Committee, my name is Maneesha Mithal, and I am the Associate Director of the Division of Privacy and Identity Protection at the Federal Trade Commission. I appreciate the opportunity to appear before you today to discuss the Fair Credit Reporting Act, credit bureaus, and data security.

As you know, the FCRA is intended to help consumers in three ways.

First, it helps consumers prevent the misuse of sensitive consumer report information by limiting recipients to those who have a legitimate need for it.

Second, it works to improve the accuracy and integrity of the consumer reporting system.

And, third, it promotes the efficiency of the Nation's banking and consumer credit systems.

Now, the Commission has played a key role in the implementation, enforcement, and interpretation of the FCRA since its enactment. Let me mention three key examples.

First, in 2012 the Commission published a study of credit report accuracy. According to the study findings, one in four consumers identified errors on their credit reports that might affect their cred-

it scores. Four out of five consumers who filed disputes experienced some modification to their credit report. And 5 percent of consumers experienced a change in their credit score that could impact their credit risk classification.

The second activity that the FTC engages in is enforcement. Enforcement continues to be a top priority for the Commission. Since 2011, the Bureau has been examining the nationwide credit bureaus. As a result, the FTC has focused its FCRA law enforcement efforts on other entities in the credit reporting area and other aspects of the consumer reporting industry more broadly. One example is enforcing a law against furnishers that are not supervised by the Bureau. The FTC has settled cases against data furnishers that allegedly had inadequate policies and procedures for reporting accurate information to CRAs.

Another example is employment background screening CRAs. For instance, in the InfoTrack case, the Commission alleged that a background screening CRA failed to have reasonable procedures to ensure the maximum possible accuracy of the consumer reports it provided, and as a result, it provided inaccurate information suggesting that job applicants may have been registered sex offenders when they were, in fact, not.

Third, the Commission continues to educate consumers and businesses on their consumer reporting rights and obligations under the FCRA. One example is our publication "Credit and Your Consumer Rights", which provides an overview of credit for consumers, explains consumers' legal rights, and offers practical tips to help solve credit problems.

Now, let me close by mentioning the importance of credit bureaus maintaining reasonable security of the consumer information that is entrusted to them. Since 2001, the Commission has undertaken substantial efforts to promote data security in this and other sectors. We enforce several laws requiring companies to maintain reasonable security, including the FTA Act, the Gramm–Leach–Bliley safeguards rule, and certain provisions of the FCRA. The Commission has brought over 60 law enforcement actions against companies that allegedly engaged in unreasonable data security practices.

Last year the Commission took the unusual step of publicly confirming its investigation into the Equifax data breach due to the scale of the public interest in the matter. And although we aggressively enforce our data security laws, I believe there are some gaps in our authority. For example, we cannot seek civil penalties for violations of most data security laws. To fill in these gaps, the Commission has supported Federal data security legislation on a bipartisan basis for over a decade. My written testimony discusses these issues in further detail, and I am happy to answer any questions you might have.

Chairman CRAPO. Thank you, Ms. Mithal. And my first question is for you. This is primarily just sort of a housekeeping item, but as I indicated in my opening statement, the Economic Growth, Regulatory Relief, and Consumer Protection Act has some significant provisions in it in this arena in terms of protecting consumers with the ability to place security freezes on their credit files with credit bureaus. This provision will empower consumers to protect their

credit in the event of future data breaches or incidents of identity theft. I am just seeking your commitment that you and the FTC will move expeditiously to implement these credit bureau provisions in Senate bill 2155.

Ms. MITHAL. Absolutely, you have our commitment to implement those provisions expeditiously, and we have already begun. We issued a consumer blog post, and we have begun our rulemaking process, so thank you.

Chairman CRAPO. Thank you.

Ms. Twohig, credit bureaus—well, let me put it this way: I have long been concerned about the ever increasing amounts of big data that are being collected, both in the private sector and in the public sector by the Government. And as you know, one of the agencies that I have been worried about is the Consumer Financial Protection Bureau.

Are credit bureaus required to provide data to the Bureau?

Ms. TWOHIG. So, Senator, thank you for that question. In our supervisory work, they are required to respond to our requests when we are conducting an examination, and the requests that we make of the credit bureaus are similar to the requests we make of other financial service providers that we oversee through our examination authority. So that would be we request information such as how they are complying with the law and their compliance management systems, so, for example, their board and management oversight, their policies and procedures, their monitoring, their training, what audits they are doing. So all the elements that go into a compliance management system, we ask for that general information.

And then more specifically, we ask for more specific information when we are determining particular compliance with particular provisions of the law. So, for example, we may need specific information about consumer files when we are doing transaction testing to ensure, for example, that they were complying with the law in following up on a consumer's dispute.

Chairman CRAPO. My understanding is that the agency is seeking to collect specific credit card transactional data on hundreds of millions of accounts. Is that not correct?

Ms. TWOHIG. My understanding, Senator, is that a separate part of the Bureau, its research arm, collects in a credit panel de-identified information on consumers for research purposes.

Chairman CRAPO. But you are not in a position to describe exactly what they are collecting?

Ms. TWOHIG. Correct. We would need to follow up with you and get you the details on that.

Chairman CRAPO. All right. Let me go back again to the information that you are familiar with. Is the data that you are requiring provided by mandate or is it purchased?

Ms. TWOHIG. So the area that I work in, Supervision, the legal requirement under Dodd–Frank is that they are required to respond to supervisory requests for the information we need to conduct the examination.

Chairman CRAPO. All right. And are there other private sector entities that are required to provide data in addition to the credit

bureaus? And what are they? For example, credit card companies, banks, others?

Ms. TWOHIG. So there are various provisions of different kinds of law that do require reporting to the Bureau. I believe, for example, under the CARD Act, credit card issuers are required to provide their agreements that then the Bureau posts on the website. I am not familiar, sitting here right now, with all the different provisions that might require reporting to the Bureau, but there are a number of different requirements that would come into play.

Chairman CRAPO. All right. I appreciate that. And just quickly, I have only got about a minute left, so if you could each give me about a 30-second answer, sort of a high-level answer as to what have we learned from the Equifax data breach about what we need to do from here?

Ms. TWOHIG. So, Senator, I can tell you that even though the Bureau's investigations are not public, in this instance it is a matter of public record that the Bureau is investigating Equifax. We are coordinating with the FTC on that investigation, so that is in process. So I think it is premature to really answer that question.

Chairman CRAPO. All right. Ms. Mithal.

Ms. MITHAL. Like Ms. Twohig, I cannot comment on the specifics, but what I can say is two things.

One is that we have learned that credit bureaus do hold the most sensitive information about consumers available in the marketplace, and it is incumbent on these credit bureaus to protect that information.

And, second, I think that in terms of the big data breaches, I think the FTC could use more authority to seek civil penalties against companies that violate the laws that we enforce.

Chairman CRAPO. All right. Thank you.

And Senator Brown has indicated that he wants to yield his first slot to Senator Schatz, so, Senator Schatz, please go ahead.

Senator SCHATZ. Thank you, Chairman, and thank you to Ranking Member Brown. I promise I will not make a habit out of this. I appreciate it very much.

Thank you very much for your testimony. Ms. Twohig, I wanted to follow up on something Ms. Mithal described. There was an FTC report that found that 5 percent of credit reports contain confirmed material errors. So these are confirmed material errors. There are more errors than that. But even if it is just 5 percent, that is the bare minimum of confirmed material errors. You are talking about 10 million people. And worse than that, 2 years later 84 percent of those errors remained on the credit reports.

Can you tell me a little bit about what your supervisory work is entailing and what you found as it relates to accuracy and dispute resolution?

Ms. TWOHIG. Thank you for that question, Senator. I would be happy to talk about that.

As I said, because of the concerns about credit report accuracy, the Bureau did its first rule to identify what larger participants in the marketplace it was going to establish a nonbank supervision program for that was not already in a statute with respect to credit bureaus, consumer reporting agencies, because of the priority that the Bureau gave to look into that market and to be able to apply

first ever supervisory authority on that industry. So they had never, before the Bureau, been examined by any Federal or State regulator. We prioritized that, and we have been conducting that work. And so we have been very focused on looking at their compliance with the accuracy and the dispute resolution provisions of the FCRA.

Senator SCHATZ. And what have you found?

Ms. TWOHIG. We found that, in general, as a big-picture matter, supervision is an attempt to get companies to have a preventive—to prevent law violations, to have a proactive approach to compliance, to make sure that they have their compliance house in order so that violations do not occur in the first place. We think we have made progress in shifting their attitude and culture toward more of a proactive compliance posture. But we have found problems with their compliance with the law, and we have given them directives to improve where we have found they have fallen short, and we have seen improvements over time. But that is not to say there is not more work to do, Senator.

Senator SCHATZ. Thank you.

Ms. Mithal, Senator Kennedy and I have a bill that would give consumers more tools to manage their credit reports, and I think it is really important for this Committee, especially for Republicans on this Committee, to recognize that we all know that we cannot blow up the system, that although there are consumers problems related to these credit bureaus, we still need some measure of creditworthiness, and we are not intending to be so disruptive as to create problems in lending. But there are some basic things that we can do to empower consumers, and I want to make sure that—they are not customers. They have not enlisted. People generally speaking do not sign up with these credit bureaus. But they are consumers, and our bill tries to empower consumers to, for instance, know what the credit bureaus know, be able to see those same lines, and to have an online portal that is no labyrinthine that allows a person to resolve any dispute in a straightforward manner.

Is it fair to say, Ms. Mithal, that you support the goals of this legislation?

Ms. MITHAL. Absolutely. I think credit report inaccuracy issues continue to harm those consumers that are affected by it. Not only is it the lack of credit in the future; it is the time and expense it takes to clear up their credit report. So I think the tools that you are aiming to provide consumers through your bill, those are the types of tools that are absolutely worth considering.

Senator SCHATZ. Can you talk a little bit about the importance of an online portal?

Ms. MITHAL. Sure. So I think one of the problems for consumers is that it is very difficult to know how to navigate the credit reporting system, and so I think the easier we can make it for consumers, the more tools we could provide for them, the more one-stop shops we can provide for them, I think that is very useful, consistent with, as you said, the kind of free flow of credit information.

Senator SCHATZ. One final question, which I think I will take for the record for both of you. It is sort of twofold.

First, we should draw a distinction between breaches which create credit score problems and credit inaccuracies, and the endemic

problem of these credit bureaus basically getting it wrong anywhere from 5 to 15 percent of the time, but at least 5 percent of the time in a material way. So although the Equifax breach caused us to think about these bureaus and focus on that question, this is not a cybersecurity question exclusively. It is also a basic consumer rights question.

So my question for the record is: What specifically are the pain points for consumers as they go about trying to resolve these questions?

Senator SCHATZ. And I have run out of time, and I appreciate the indulgence of the Chair and the Ranking Member.

Chairman CRAPO. Thank you.

Senator Scott.

Senator SCOTT. Thank you, Mr. Chairman. And thank you to the witnesses for being here today.

I have worked for the last 6 or 7 years on something called the "opportunity agenda," trying to find a way to empower those folks living in distressed communities. As you probably both know, we have about 50 million Americans today who live in those distressed communities, and as I think about ways to empower those folks living in distressed communities, the access to credit issue jumps out very clearly.

The BCFP has found that 26 million Americans are credit invisible; another 19 million Americans are unscorable because their information is either insufficient and/or just too old. It should come as no surprise that there is a strong correlation between your income and whether you have a credit score or a credit record. Almost 30 percent of Americans living in low-income areas are credit invisible. An additional 15 percent of Americans living in those areas are unscorable. In South Carolina, when you combine those two numbers together, that means about nearly one out of every four South Carolina adults are in that category.

A solution to bring credit invisibles out of the shadows is S. 3040, the Credit Access and Inclusion Act. Credit invisibles regularly make payments for their rent, gas, water, electricity, and cell phones. New credit scoring models recognize these payments are payments that are predictive of your actual credit risk.

Unfortunately, the FCRA ensures that missed payments and collection are reported to the credit bureaus, but not necessarily the ones you make on time.

The Brookings Institution states that the consideration of this payment data will lead to a 21-percent increase to prime credit for those earning less than $20,000 a year and a 15-percent increase to prime credit for those earning between $20,000 and $30,000 a year. That will make a huge difference for creditworthy folks trying to climb the economic ladder, and my bill helps us get there.

Ms. Twohig, what is the impact on a consumer of being credit invisible when it comes to interest rates, applying for a job, or finding an apartment?

Ms. TWOHIG. Senator, first of all, I want to say that the Bureau shares your concern about access to credit. In fact, one of the Bureau's strategic goals is to ensure that all consumers have access to consumer financial services.

With respect to the particular impact, the particular impact will vary for each consumer and what they are applying for and what they are trying to do in the particular credit or other markets. But I think it is fair to say that if a consumer does not have a credit file with one of the national credit reporting companies or if it does not have enough in that file to score, then that consumer is basically shut out of the mainstream credit markets.

Senator SCOTT. Well, that kind of leads to my second question. The BCFP has suggested that more of this information at the credit bureaus will help credit invisibles access mainstream credit sources. It sounds like you would concur that that would be accurate?

Ms. TWOHIG. So alternative data of the type you are discussing is also something that the Bureau is interested in learning more about and is monitoring. In fact, the Bureau issued last year a Request for Information from the public to get information about different kinds of alternative data and the aspects of that alternative data and how it could help consumers and access to credit. We received over 100 comments. We are currently monitoring that information and studying that information and learning more about it. But I think also it is fair to say that if that information is accurate and predictive, then that could be part of the solution to increase access to credit.

Senator SCOTT. Thank you.

I will just say to my Chairman and the Ranking Member, who I know both have a passion for finding ways to bring those folks who are today credit invisible out of the shadows and into a place where they can rely on a strong credit score to be able to have lower interest rates, greater access to better jobs, and certainly be able to find places to live in higher-quality communities, and all that is anchored in your credit score and not being credit invisible. So hopefully S. 3040 will be on the top of the docket for both of you. Thank you both.

Chairman CRAPO. Thank you, Senator Scott.

Senator Menendez.

Senator MENENDEZ. Thank you.

Ms. Twohig and Ms. Mithal, let me start off by asking you each to give me the last four digits of your Social Security number.

Ms. TWOHIG. Senator, I really do not want to do that in a public forum.

Ms. MITHAL. I have the same reaction.

Senator MENENDEZ. All right. How about telling me which stores you opened credit cards with?

Ms. TWOHIG. Which stores?

Senator MENENDEZ. Yeah.

Ms. TWOHIG. I do not think I have opened any credit cards with a store lately.

Ms. MITHAL. That is not something I would be willing to share in a public forum.

Senator MENENDEZ. Or maybe can you tell us the outstanding balance on your home mortgage loans?

Ms. TWOHIG. Senator, I would prefer not to share that kind of information either.

Ms. MITHAL. Same.

Senator MENENDEZ. I am not surprised. But that information, which I am sure you would not want to be shared or sold without your permission, and yet under current law consumer reporting agencies like Equifax can share and sell your information, where you live, where you pay your bills, and whether you pay on time, what you filed for, whether you filed for bankruptcy, without ever having to get your consent. Isn't that right?

Ms. MITHAL. That is correct, although there are certain limitations on how they can use the data.

Senator MENENDEZ. Now, American consumers are at the mercy of three megacompanies who control the security and safety of their personal information, and that makes no sense. Consumers should have the ability to control when, how, and to whom their data is shared, just like you wanted to control it here in this public forum.

Last year a massive Equifax data breach laid bare the systemic problems with the credit reporting industry. Its failure to guard sensitive data left 145.5 million Americans exposed to identity theft and fraud.

Ms. Mithal, Equifax waited an inexplicable 6 weeks to disclose a breach that had occurred. Worse, over months after the breach, millions of consumers were still unaware of the breach in part because there is no national requirement to alert consumers. My bill, S. 2188, the Consumer Data Protection Act, would require consumer reporting agencies to quickly notify the Federal Trade Commission, the CFPB, law enforcement, and consumers of a breach while keeping intact existing strong State consumer protection laws.

Generally speaking, does the FTC support the idea of requiring companies to provide notification to consumers where there is a data security breach?

Ms. MITHAL. Absolutely, and the Commission has done so for almost—for over a decade on a bipartisan basis.

Senator MENENDEZ. Now, let me ask you, another issue we need to address here is the ability to hold consumer reporting agencies accountable when there is a breach, when they have clearly failed to protect consumers' personal data. My legislation also provides FTC the authority to pursue fines against a consumer reporting agency such as Equifax that negligently, knowingly, or willingly causes a data breach.

In your view, would the institution of a monetary penalty framework incentivize consumer reporting agencies to better secure consumer data?

Ms. MITHAL. Yes.

Senator MENENDEZ. Let me ask another question for both witnesses. Given the unique and varied nature of consumer harm that results from a data breach at a consumer reporting agency, which includes everything from identity theft to difficulty purchasing a home or securing employment, would it be helpful to have a comprehensive study analyzing both the immediate and long-term costs and damages to individuals affected by data breaches at consumer reporting agencies?

Ms. MITHAL. So I think that there is no question that there is tremendous harm to consumers from data breaches of their sen-

sitive information, and I think it would be worth considering a study to quantify that harm.

Senator MENENDEZ. Ms. Twohig.

Ms. TWOHIG. I would agree with Ms. Mithal, and to the extent the Bureau can be helpful providing technical expertise in analyzing that topic, we would be happy to do so.

Senator MENENDEZ. Well, thank you. I really did not want to know your Social Security numbers, by the way, or your balances on your mortgages, which I hope is virtually nil. But this is the very essence of what we are talking about as we deal with this issue here today.

Thank you, Mr. Chairman.

Chairman CRAPO. Senator Kennedy.

Senator KENNEDY. Thank you, Mr. Chairman.

Ms. Mithal, can we agree that the work of the CRAs facilitates commerce in America?

Ms. MITHAL. Absolutely.

Senator KENNEDY. Do you agree with that, too, Ms. Twohig?

Ms. TWOHIG. Yes.

Senator KENNEDY. And I think we can also agree, can we not, that that is a good thing in our free enterprise system?

Ms. MITHAL. Yes.

Ms. TWOHIG. Yes.

Senator KENNEDY. When the CRAs gather information about me, do they ask my permission?

Ms. MITHAL. No.

Ms. TWOHIG. No.

Senator KENNEDY. Do they pay me for the information?

Ms. MITHAL. No.

Ms. TWOHIG. No.

Senator KENNEDY. They gather this information, and they assign me a score basically making an evaluation, a judgment about me, whether I am a creditworthy person or not. Is that correct?

Ms. MITHAL. Correct.

Senator KENNEDY. And in 5 to 10 percent of the cases, they get it wrong. They have some bad data. Is that correct?

Ms. MITHAL. Yes.

Senator KENNEDY. If they have bad data and I call them up and I say, "Hey, you have got bad data on me. You did not talk to me first. I could have fixed this up front, but you did not talk to me. But you have got some bad data on me, and it is affecting my life and my family's life," and the CRA says, "OK. We will get back to you," and they never get back to me, or they get back to me and say, "We disagree." What is my recourse?

Ms. MITHAL. So under the FCRA there is a dispute process where credit reporting agency is required to respond within a particular amount of time, and though at the end of the day, when the credit bureau says that, "No, you, in fact, owe this debt," the consumer owes the debt.

Ms. TWOHIG. That is right. The consumer can put a statement on their credit report if they are not satisfied with the results of the dispute investigation.

Senator KENNEDY. How long does that take?

Ms. MITHAL. I believe under the FCRA the investigation process is 30 to 45 days.

Ms. TWOHIG. That is right.

Senator KENNEDY. I have to fill out a bunch of forms, do I?

Ms. MITHAL. Yes.

Senator KENNEDY. OK. How long do you think it takes to fill out all those forms and make the phone calls and say, "Hey, you have got my information wrong"?

Ms. MITHAL. So I think there is certainly some time it takes on the part of the consumer to kind of understand the dispute process, to go through the dispute process, and to implement it.

Senator KENNEDY. And if I have got a day job, I cannot do that at work, right?

Ms. MITHAL. Yes, it is certainly a lot of time and expense to dispute——

Senator KENNEDY. I might do it at night or on the weekends? Can I call them up on the weekends? Do the CRAs work on the weekends, do you know?

Ms. TWOHIG. I believe they have an online portal that you can file a dispute online and submit documents. Now the consumers can submit documents in support of their dispute online.

Senator KENNEDY. OK. And let us suppose at the end of the process they come back to me and they say, "No, we are not changing anything," or—I know this does not happen very often, but you get somebody having a bad day, and they say, "Hey, we are not changing anything. And, by the way, we do not care because we do not have to. You are not my customer." What do I do?

Ms. MITHAL. So I think speaking for——

Senator KENNEDY. Do I file a complaint with the FTC?

Ms. MITHAL. Sure, you can file a complaint with the FTC, and we have——

Senator KENNEDY. Do I need a lawyer?

Ms. MITHAL. No, you do not need a lawyer.

Senator KENNEDY. Does it take time? I bet it is not a one-page form.

Ms. MITHAL. Yes, it takes time.

Senator KENNEDY. It is not a one-page form, is it?

Ms. MITHAL. It is multiple pages.

Senator KENNEDY. And how quickly would the FTC act?

Ms. MITHAL. It would take a while.

Senator KENNEDY. Like how long is "a while"?

Ms. MITHAL. It could take—so let me just clarify. We do not act on behalf of individual consumers.

Senator KENNEDY. I understand. How long would it take?

Ms. MITHAL. It would take several months to investigate, probably——

Senator KENNEDY. It could take a year, couldn't it?

Ms. MITHAL. Sure.

Senator KENNEDY. It could take 2 years sometimes, doesn't it?

Ms. MITHAL. Sure.

Senator KENNEDY. In the meantime, they have got bad data about me, and they did not pay me for it. They did not even ask me.

Now, I think the CRAs perform an important service and do facilitate commerce. But it seems to me that we ought to be smart enough, particularly with technology, to come up with a system that says we are going to make it as easy as possible for the people with respect to whom the CRAs have bad information so those people can get it fixed and they can get it fixed quickly and they can get it fixed efficiently and they can get it fixed inexpensively and they can get it fixed so they do not have to miss their kids' ball games.

Now, I think Senator Schatz and I have a bill that will do that. What is wrong with that bill? You think it is a good bill, don't you?

Ms. MITHAL. I do think it is a good bill, and I would support the goals of the legislation, which is, as you articulated, to make it a lot easier for consumers to file disputes with consumer reporting agencies.

Senator KENNEDY. Ms. Twohig.

Ms. TWOHIG. Senator, I would say that all the issues you have just pointed out are the reason why we have prioritized at the Bureau supervising both the CRAs and furnishers——

Senator KENNEDY. Yes, ma'am, I know you prioritized, and I am not fussing at you, but you are still part of the bureaucracy. And it is pretty intimidating for the average American who did not ask to be brought into this system—it is a good system, but it is pretty intimidating when the CRAs get it wrong. And we ought to make it as easy as possible for them to get it fixed. That is good for them. That is good for the companies. That is good for the free enterprise system. And I think we can do better.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you.

Senator Warner.

Senator WARNER. Well, thank you, Mr. Chairman. First of all, thank you for holding this hearing. I think you are hearing bipartisan concern. I want to thank the Ranking Member for also yielding to us. I also want to point out, though, that Ms. Twohig and Ms. Mithal are long-time career professionals. I think they would lean in to being willing to try to help us fix this problem. But they cannot fix this problem on their own without Congress acting.

So I want to reiterate what I think a lot of Members have said. I had no choice in Equifax having my data. Senator Menendez raised this, Senator Kennedy has, Senator Schatz has. To me, as a former business guy, it is remarkable that a data breach based upon sloppy cybersecurity standards that took place over a year ago that the public was not notified until 11 months ago, that we still—and this is not your fault at this point, because Congress has not acted—that they have paid no penalty to date. They took a little bit of a hit in the market, but they have almost recovered from that because they do not expect Congress to do its job to give the FTC the ability to put a civil penalty process in place.

Now, Senator Warren and I have a very comprehensive bill that I am sure she will speak to as well that would put a liability regime in place that would particularly in the event of negligent behavior put a real incentive to make sure that credit reporting agencies up their game.

Let me just again, for the record, Ms. Mithal, the FTC at this point does not have the ability to put any civil penalty on a CRA based on performance, do they?

Ms. MITHAL. Not on the basis of data security violations generally, no.

Senator WARNER. So unless the Congress acts, whether it is Senator Warren's bill, Senator Menendez's bill, Senator Kennedy's bill, Senator Schatz's bill, you do not have the tools. As a matter of fact, if we go and look at the so-called Safeguards Rule—and we have heard from Ms. Twohig's testimony that CFPB does not have authority under the Safeguards Rule to examine or look at the practices of the CRA. Ms. Mithal, does the FTC have the authority under the Safeguards Rule to examine credit reporting agencies to ensure that that rule is being followed?

Ms. MITHAL. So just to be clear, we do not have examination authority, but we can investigate CRAs to make sure that they are following the Gramm–Leach–Bliley Safeguards Rule. But, significantly, as you point out, we do not have the authority to seek civil penalties under the Safeguards Rule.

Senator WARNER. Right, and if memory serves, I am sure Senator Kennedy remembers as well, FTC indicated they had opened an investigation into the Equifax breach, but here we are over a year after the breach took place and 11 months after the public was finally notified, yet we still do not have a result. And even if you come up with a result, you do not have the ability to impose penalties because you have no liability regime in place.

Ms. MITHAL. Not under data security, yes.

Senator WARNER. Well, Mr. Chairman, I think this is an area, because I can assure you, sitting from the intel side, this is a problem that is not going to go away. This is a problem that is going to only exponentially increase. And Senator Menendez went down the path of would you be willing to offer your personal information, you wouldn't. But if somebody has hacked in and got that information from Equifax and contacts you with that personalized information and you combine that with the next realm of misinformation and disinformation, and you suddenly have a live stream video of what appears to be a face of somebody you recognize popping up on your social media account asking you to do something, either invest in some company or vote for some candidate, you put those two together, and you have a potential crisis that goes well beyond just financial concerns. And if we do not act, I think we are going to be irresponsible in ensuring that kind of activity does not take place, because I agree with Senator Kennedy, the incentives are not there at all for any CRA to clean up its act at all. There are no civil penalties, there is no liability regime. And I think we can do better, and I think these career professionals actually would want us to do better if we would give them the tools.

Let me just say in my last 30 seconds, Senator Scott raised a little bit of this question about some of the folks who are unbanked. I am concerned as well, as we think through—Ms. Mithal, this is for you. As we start looking at the use of artificial intelligence, machine learning, you know, there are going to be a lot of tools used particularly by nonbank financial institutions who may provide credit lending, how we make sure that we ensure fairness in this

new regime. But at this moment in time, again, I do not believe the FTC has the appropriate ability to look at a nonbank financial institution who is using AI techniques to grant a loan under FCRA. Is that correct?

Ms. MITHAL. So we did do a report on this issue a few years ago, and we did mention that there are certain circumstances when companies use AI technology to make decisions about credit or housing or employment eligibility that we would have authority to take action under the FCRA, but that is against a limited set of entities that are third parties using the information. So there are some gaps there.

Senator WARNER. And I would only say, Mr. Chairman and Ranking Member, that if we think what is happen with Equifax was something, wait until you see the nonbank financials start to use AI in the sophisticated way. And if we do not get ahead of this in terms of we ought to be able to use good data and good information, but if we do not put some rules in place, the Equifax breach will pale in comparison to what the next generation of attacks will look like.

Thank you, Mr. Chairman.

Chairman CRAPO. I share your concerns, Senator Warner.

Senator Warren.

Senator WARREN. Thank you very much, Mr. Chairman. Thanks for holding this hearing. Thank you, Ranking Member Brown, for letting us go ahead of you here.

I want to pick up on the same theme that my colleagues have been talking about. After Equifax disclosed its massive data breach last year, I sent letters to Equifax and the other large credit bureaus and Federal regulators seeking information about the breach and the options for holding Equifax accountable.

My staff compiled that information in an investigative report that my office issued in February, and I would like to submit a copy of that report for the record, Mr. Chairman. Mr. Chairman?

[Laughter.]

Senator BROWN. Without objection.

Senator WARREN. Without objection.

Chairman CRAPO. Without objection.

Senator WARREN. Thank you, Mr. Chairman. Thank you.

Chairman CRAPO. What did I just agree to?

[Laughter.]

Senator WARREN. So we put this report together, and one of the key findings of this report is that Federal agencies do not have the legal tools they need to stop data breaches at credit bureaus and hold credit bureaus accountable for compromising sensitive personal information. As Senator Warner was just pointing out, the FTC has some authority to oversee data security at credit bureaus, but it currently has no authority to seek civil penalties against the bureaus for compromising consumer information.

So let me just ask, Ms. Mithal: Do you think the FTC should have that authority?

Ms. MITHAL. Yes.

Senator WARREN. Good. Thank you. In fact, the response the FTC sent to my letter specifically requested legislation that would

"allow the FTC to seek civil penalties to help ensure effective deterrence of cybersecurity breaches," so asking for it.

Meanwhile, the CFPB has some supervisory authority over large credit bureaus, but limited ability to issue rules on how the bureaus must safeguard sensitive consumer data. Is that right, Ms. Twohig?

Ms. TWOHIG. That is correct.

Senator WARREN. Good. In other words, even if the CFPB spots serious cybersecurity problems at the credit bureaus it supervises, it cannot issue new rules to try to address these problems. Is that right?

Ms. TWOHIG. So we do not have the authority under the safeguards provisions of the Gramm–Leach–Bliley Act or the Safeguards Rule.

Senator WARREN. OK. So in response to my letter to the CFPB, then-Director Cordray said that the agency supported new legislation because "Federal laws that are applicable to data security have not kept pace with technological and cybersecurity developments." In other words, want the authority to do this.

So after receiving these responses, Senator Warner and I spent months working with each other and with experts in the field to develop the Data Breach Prevention and Compensation Act. Our bill would authorize the FTC to impose large and automatic penalties on any large credit bureau that allowed sensitive consumer information to be accessed. The way we see it, if credit bureaus collect our personal information without our permission, then they should have an absolute obligation to protect that data from hackers and thieves.

The bill would also create a new Office of Cybersecurity at the FTC with the responsibility to establish cybersecurity standards at credit bureaus and supervise compliance with those standards.

Ms. Mithal, do you think the FTC would be better equipped to oversee how credit bureaus protect sensitive information if Senator Warner's and my bill became law?

Ms. MITHAL. So I certainly do think we have the expertise. I think it is a question of resources. And so if your law comes with resources, that would be welcome.

Senator WARREN. OK, good. Fair enough. Fair enough. But you have got to have the authority, or you cannot do anything.

Ms. MITHAL. Correct.

Senator WARREN. So thank you.

Mr. Chairman, I know that you and many of your Republican colleagues on this Committee are concerned about the lack of adequate protection of consumer data at credit bureaus, and I hope you will work with Senator Warner and with me to push this legislation forward.

Our Federal agencies have made absolutely clear that they need more legal authority to protect consumers. We cannot just cross our fingers and hope that another breach does not happen because another breach will happen. And if we fail to act, then we bear some responsibility for that. More of our constituents will be harmed unless Congress acts.

So I urge you to join with Senator Warner and me and others on this Committee to try to push our bill forward.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you, Senator Warren.

Senator Cortez Masto.

Senator CORTEZ MASTO. Thank you. Thank you, Mr. Chair and Ranking Member for, I agree, this important discussion. And thank you to both of you for being here and all of the work that you do.

I am curious. I want to talk a little bit about exclusive contracts. Last October, right after the announcement of Equifax's massive data breach, the *New York Times* ran an article about how Equifax and Freddie Mac have an exclusive relationship that harms both consumers and small businesses. I am curious if either one of you are familiar with that article or familiar with this concept that there are exclusive contracts.

Ms. MITHAL. I am not.

Ms. TWOHIG. I am not familiar either.

Senator CORTEZ MASTO. So this is not something that either one of your organizations is looking into as something that is harmful to individual consumers or small businesses?

Ms. MITHAL. I can only speak to privacy and cybersecurity issues, and that is not something that is on our radar screen.

Senator CORTEZ MASTO. OK.

Ms. TWOHIG. And for the Bureau of Consumer Financial Protection, as I said at the outset, we can confirm that we are investigating Equifax's data security practices in coordination with the FTC. Beyond that, our investigations are not public.

Senator CORTEZ MASTO. Thank you very much.

Ms. Twohig, let me jump back then to the concept of—and I agree with my colleagues—this concern that all of this data is being collected on all of us individually, and we have no control over it. So, Ms. Twohig, let me start with you. As you well know, credit systems around the world have differing standards for consumer control of their own privacy. For instance, the new privacy laws in the European Union provide more privacy options than we do here in the United States. In fact, Americans have really little say over what data can be aggregated by these credit bureaus.

If an opt-in system for credit bureaus was established, how would that impact people, our communities, and our economy? In other words, also—and as you address that, what is the reaction we are seeing to the implementation of the general data protection regulations in the European Union? And the reason I bring this up is because we have all been talking about opt-in, but there is this concern that somehow it is going to have an impact on our economy, on our businesses, and so I am curious if you have any insight into that, either one of you. Let me start with you, Ms. Twohig.

Ms. TWOHIG. So at the outset, I would say that the Economic Growth, Regulatory Relief, and Consumer Protection Act provides additional important consumer protections in my view to allow consumers to get a free security freeze. And so even though that is not exactly what——

Senator CORTEZ MASTO. That is not an opt-in.

Ms. TWOHIG. That is not an opt-in, but it is one step toward more control if consumers choose to exercise it.

Senator CORTEZ MASTO. But it is less than what the European Union requires?

Ms. TWOHIG. I believe so.

Senator CORTEZ MASTO. Any other——

Ms. MITHAL. Yes, I guess I would say that I would have a bit of a concern about an across-the-board opt-in. I could see people who have a bad credit history or who have criminal records or bankruptcies not wanting that information to be reported and thus not opting into the system, and I think that could raise the cost of credit across the board. So I do have some concerns about that.

I agree with the general concept that consumers should have more control, but there are other potential means of accomplishing that.

Senator CORTEZ MASTO. Do you think that some of the legislation you have heard today gives more of that control to consumers?

Ms. MITHAL. I think there are some very interesting options worth exploring through that legislation.

Senator CORTEZ MASTO. Thank you. I appreciate that.

And let me also then go back to this idea, I agree with my colleague Senator Scott and the concern about too many adults have credit invisible and unscorable credit, and I think that is harmful in so many different ways. But I also understand, Ms. Twohig, from what you said that you are studying the issue or the agency is studying the issue on alternative data. Can you talk a little bit more about that and when you are going to anticipate completion of that study and what your intent is after the study is completed?

Ms. TWOHIG. So I do not have a particular date, and I am not sure there is a particular study. It is just something that the Bureau is very interested in and has requested information so we could learn more about that. I can tell you the Acting Director has created an Office of Innovation with the goal of seeing what the Bureau can do to spur innovation in all kinds of ways, and that would include the use of alternative data and avenues for increasing access to credit.

Senator CORTEZ MASTO. OK. Thank you.

One final question. I know that a number of States just recently announced a consent order last week with Equifax, and I believe these States really took the lead on this and did their necessary investigation. One of the reasons why I have concerns that there needs to be more of this collaboration between States and the Federal Government in this area is because I have seen here, as we have had these hearings, that State oversight is even more necessary now. What I have seen from Director Mulvaney and really the CFPB nominee Kraninger have not shown any willingness to challenge the financial services industry.

So given what I know and what I have seen here, let me ask you this: There is legislation in the House—it is H.R. 3626—and it requires enhancing information sharing between the Federal and State regulators when conducting the TSP exams. Would that be something you would support? And I am asking both of you.

Ms. TWOHIG. So I can say as a general matter that—and I have been with the Bureau since its beginning in the Supervision Program. We have placed a priority on developing relationships with State regulators, and my enforcement colleagues the same for the State Attorneys General, and so we have close and cooperative re-

lationships with those regulators, and the Acting Director has said he wants to improve that even more.

Senator CORTEZ MASTO. That is wonderful to hear. Thank you.

Ms. MITHAL. And I would echo that sentiment, and I just want to also say that I think we have been talking a lot about gaps in the FTC's authority, but I do want to say whatever authority Congress gives us, we exercise very aggressively. So we have brought over 60 data security cases, and we have looked at a variety of sectors. So I did not want to make it sound like we were sitting on our hands.

Senator CORTEZ MASTO. Thank you. And I notice my time is up. Thank you both.

Chairman CRAPO. Thank you.

Senator Jones.

Senator JONES. Thank you, Mr. Chairman, and thank you to the witnesses for coming here today.

I want to mention something about—I want to go back to cybersecurity like so many others, but from a little bit different angle. I appreciate all of the colleagues on this Committee concerned with the Equifaxes of the world and the holders of this information. But, you know, I am an old prosecutor, and when we had a bank robbery, we just did not focus on what happened at the bank. We focused on who got the money and trying to catch those folks. So my question is: We have heard a lot today about Equifax and the CRAs. Is law enforcement involved in that investigation? If they are not, I would like to know why. And if so, can we have an expectation at some point when the investigation is released that there has been an effort and we hopefully can find out who did this? Because I agree with Senator Warner, this problem is not going away, and we need to focus on perpetrators as much as those holding the data. I will give that to both of you.

Ms. MITHAL. So I do not think I could talk about this in the context of a specific nonpublic investigation, but what I can say is that we work very closely with criminal authorities. I think it is a kind of one-two punch type situation where we want to make sure as a civil matter that agencies and companies that are entrusted with consumer data are doing everything they can to protect it, and at the same time we work with criminal law enforcement authorities to catch the bad guys and to try to share information to accomplish that. So I agree it is a very important part of the equation.

Senator JONES. All right.

Ms. TWOHIG. And that would be the same for the Bureau of Consumer Financial Protection in terms of coordinating with criminal law enforcement agencies.

Senator JONES. All right. When this investigation is public, would you expect there to be some element of the report about the culprits in this particular Equifax matter?

Ms. MITHAL. I really cannot speak to that.

Senator JONES. All right. That is fair enough.

The other thing I would like to mention is that a recent study showed that Alabama, my State, ranked third from the bottom in terms of average credit scores, and I know there are a lot of things that impact credit scores. But what seemed clear is that there were also regional differences that have remained kind of static, and one

of the—CFPB and FTC both have tools to educate customers, which I think is as important as anything in trying to get folks to get their scores up. I see TV ads all the time. But that is not the same—you know, trying to get your free credit score is not the same as trying to say get your free credit score up.

So could you both briefly describe some of the tools that your agencies have with regard to education and what you believe could be the most effective way to educate the public about how to maintain a good credit score?

Ms. MITHAL. So I can start with that. We have what I believe is a world-class Office of Consumer and Business Education, and one of the things we do is we put out financial literacy materials, materials about credit scores and how to check your credit reports, and I think what we recognize is that a lot of people will not know the FTC, and so they will feel a lot more comfortable getting this information from their local communities, their churches, their schools, their libraries. And so we do not copyright our information. We put it out there for the local communities to put out in their own communities, and we would be happy to work with your office to get our materials out. We are also members of the Interagency Financial Literacy Task Force. So, again, I think we are trying—I absolutely agree that education is a very important part of what we do, and we need to get the word out to consumers so they can help protect themselves.

Senator JONES. Great. Do you want to address that, Ms. Twohig?

Ms. TWOHIG. Same for the Bureau. Consumer education is a very important part of what we do, and we have materials and education materials about how to create a credit file so consumers can have access to mainstream credit. Our Community Affairs Office is also doing active work in certain communities to try to help the communities understand what they can do locally to help consumers understand how they can create and build their credit files and positive credit history.

Senator JONES. Great. Well, thank you both, and my staff will reach out to you so that we can do some affirmative things in Alabama.

In the remaining moment, I would just like to follow back up with what Senator Scott said about the bill that he and I have introduced on the Credit Access Inclusion Act. And, Mr. Chairman and Senator Brown, I would also urge this Committee to get involved and try to get that bill out. A companion bill that I think is identical passed the House unanimously, and in an era in which the divide over Supreme Court nominations and things like are about to get greater, I do not want a bill that is a truly bipartisan bill to fall through the cracks like this, and I would urge the Committee to take some action and let us get that done. So thank you.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you, Senator Jones.

Senator Van Hollen.

Senator VAN HOLLEN. Thank you, Mr. Chairman and Ranking Member, and thank you both for your testimony here today.

We have talked about a number of things. Two of the categories we have talked about are: one, how do we create more incentives to discourage or prevent or deter credit rating agencies from be-

coming victims of data breaches? Obviously no one has an interest in having a big data breach, but the cost-benefit analysis needs to be changed, and that is what Senators Warner and Warren have been talking about.

The other issue, which Senator Kennedy and Senator Schatz have been talking about, is the accuracy of the information collected by the credit rating agencies, and I want to focus on that for a moment because, yes, I absolutely agree that we should make it easier for consumers to try to get their complaints submitted and processed more quickly. But it still appears to me that when you look at the sort of incentives of the CRAs, when they get it wrong, other than making the consumer whole again or correcting the error, they do not seem to have any penalty applied. So let me know if there is a current penalty that can be applied when they get it wrong. And we already know that in 5 percent of the cases they get it wrong, which represents millions and millions of Americans, which can have a devastating impact on their lives. So it seems to me in addition to making it easier to remedy the situation from the point of view of a consumer, we should also create greater incentives for the CRAs to get it right in the first place so that the burden is on them when they get it wrong, that there is some penalty to be paid for getting it wrong.

Are there any penalties right now that either of you can apply when you just find that they are getting it wrong a lot?

Ms. MITHAL. So we do have the authority to seek civil penalties for companies that do not have reasonable procedures to have maximum possible accuracy. So I have been clarifying that under the FCRA we do not have the authority to get penalties under data security, but for accuracy we do, and we have gotten those civil penalties. But I just want to emphasize the statutory standard is reasonable procedures for accuracy, so it is not that every inaccuracy in a credit report will get a civil penalty.

Senator VAN HOLLEN. Right. Would it make sense to think of those—applying more of a penalty when people get it wrong? In other words, as I understand it right now, if you are a consumer who believes you have bad information that is negatively affecting your credit report, you go through this long process, right? You get on the phone. You may be put on hold. You do what you said. It may take a couple years. At the end of the day, what you, the FTC, determines is whether or not the consumer's complaint was correct, right?

Ms. MITHAL. So we look to see whether the company's procedures were reasonable.

Senator VAN HOLLEN. Oh, you just look at the reasonable nature of that. And if you find that they were unreasonable, what do you do to the company?

Ms. MITHAL. So we have gotten civil penalties against several companies. One was a couple of years ago against a company. We got about a $2.6 million civil penalty. There is another check authorization company; we got about a $3.5 million civil penalty. So, again, it depends on the facts and circumstances, and we look at several statutory factors in determining the appropriate penalty amount.

Senator VAN HOLLEN. Would it be worth looking at greater sort of deterrent mechanisms so that there is more of a burden on the CRAs to get it right in the first place? And if so, what kind of suggestions would you have?

Ms. MITHAL. So I certainly kind of sympathize with the goal of making it easier for consumers to dispute credit report inaccuracy and also to make the whole process easier for consumers. And I think that is a goal worth exploring, and I would be happy to work with your staff and others on this Committee to accomplish that goal.

Senator VAN HOLLEN. All right. Anything else?

Ms. TWOHIG. So, Senator, similarly, the Bureau can get penalties where there has been noncompliance with the FCRA's reasonable procedures provisions. In fact, it brought a case against a consumer reporting agency and got, I believe, about $5 million in penalties for their failure to comply with that part of the law.

More generally, I think I also sympathize with the problems you are pointing out, and that is exactly why we have used this new supervisory authority that has never existed before until the Bureau was created to prioritize looking at the national credit reporting agencies and other consumer reporting agencies to ensure that they are looking at all aspects of accuracy. There are various different components of really what it takes to get a quality data control system. There is the incoming information. There is compiling it, and there is monitoring any indications of problems after the fact. We have broken it down and looked at various aspects and worked through our supervisory authority to require improvements in each part of those pieces of the system.

Senator VAN HOLLEN. Good, because I think until—let us say you are CRA. Until you have to suffer—right now, a consumer goes through this complaint process, and the CRA at the end of the day, OK, they have got to make them whole, right? "Oh, we made a mistake 2 years ago that has affected your life." But there is no other penalty to be applied unless they somehow have a system that you determined has met this—that has been shaky. And even with those systems today, as we know, 5 percent error rate which affects tens of millions of people.

So, anyway, I look forward to working with the Chairman and the Ranking Member and all of you. Thanks.

Senator BROWN [presiding]. Thank you, Senator Van Hollen.

My questions are for both of you. I have a couple of questions. A lot of people, as we know, work hard every day, sometimes people are working multiple jobs to keep up with their bills. If they are injured or if they fall ill, we do not have—many, many, many companies in this country do not have any kind of leave policy. Some do not have good health insurance, so when people are injured or fall ill, huge unexpected medical costs can haunt their credit report for years.

Given this type of debt is generally out of a person's control—they obviously did not choose this—should we not pause medical debt reporting, at least until more Americans have access to affordable insurance? We will start with you.

Ms. TWOHIG. So, Senator, I think it is correct that medical debt is different than other kinds of debt. It can cause special problems

for consumers. They can be subject to medical debt collection when they are just waiting for reimbursement. So I think it is a different kind of debt than regular debt.

Senator BROWN. Go ahead.

Ms. MITHAL. I agree with that, and I think S. 2155 was an excellent start in at least excluding certain medical debt for veterans, and I think that this is an idea worth exploring.

Senator BROWN. But it should be broader than that.

Ms. MITHAL. I think that is an idea worth exploring, yes.

Senator BROWN. Partially a follow-up to Senator Cortez Masto, I mentioned Mariner Finance in my opening statement. It is a company that sends cashable checks to people who might be in financial trouble, but the check is, as we know, a high-cost loan. The industry claims these prescreened offers that are allowed by the FCRA help borrowers get a better deal, but it looks like shady lenders fundamentally are taking advantage of a loophole to target struggling families. Wouldn't consumers be better off and less likely to face predatory lending practices if they had to opt into these offers, had to opt in rather than having to take steps to opt out? We will start with you.

Ms. MITHAL. Sure. So I also read the article, and I was very troubled by the practices. I cannot speak on any particular company, but the types of practices described in the article were very troubling. So under the FCRA, prescreened offers are permitted if they are a firm offer of credit, and so that is something that the statute specifically allows. If Congress were to determine to change that, we would enforce that requirement as well. So that is something that the law currently requires, but, again, we would be ready to work with Congress on any potential changes to that.

Senator BROWN. Ms. Twohig.

Ms. TWOHIG. I would agree with that. Consumers now have a right to opt out, but as you suggest, Senator, that is different than having the default the other way, and we would be happy to work with you to consider whether there is a policy determination you think would be better for consumers.

Senator BROWN. That is mostly yes?

Ms. TWOHIG. We would be happy to work with you to consider the pros and cons of going that direction.

Senator BROWN. So it is not quite a yes.

Ms. TWOHIG. Not quite a yes.

Senator BROWN. OK. The Fair Credit Reporting Act protects companies that provide information to credit bureaus. Consumers cannot take them to court to get fixes. We know that. We have all heard the horror stories of someone trying to fix inaccurate data on a credit report. If consumers were allowed to have their day in court, would providers be more careful ensuring the data they report to credit bureaus as accurate? Ms. Twohig.

Ms. TWOHIG. So there is a private right of action under the Fair Credit Reporting Act, and there are private actions filed by consumers if they believe that their information is inaccurate. So I just want to make sure I understand what you are——

Senator BROWN. There is a private right of action, but that private right of action has been, to put it mildly, diluted by this Congress and by decisions made by Government, correct?

Ms. TWOHIG. I cannot speak to that. What I can say is that we are well aware at the Bureau of our obligation to ensure compliance with the law, which is indeed why we have prioritized supervising and enforcing in that area.

Senator BROWN. I agree with you, and I appreciate that, and I appreciate your service over the years. But don't providers—the credit providers fundamentally know there is not a particularly effective private right of action. Do they not know that?

Ms. TWOHIG. I cannot speak to what they know.

Senator BROWN. Well, yeah, you can. The credit providers know about forced arbitration. The credit providers know how the laws have changed. The credit providers know where the power in this society resides. It is not with consumers. It is not with employees. It is with employers. It is with credit reporting companies. You have had a string of really important jobs. You are obviously a really bright woman. You do recognize that, correct?

Ms. TWOHIG. I recognize that it can be hard for an individual consumer, and that is actually why I have spent my career in public service trying to do what I can do——

Senator BROWN. I get all that, and thank you again for that. But you are not willing to say that the credit providers would be more careful ensuring the data they report to credit bureaus is accurate if the laws were written to give consumers more power in the marketplace?

Ms. TWOHIG. They probably would be more careful if the laws were written that way.

Senator BROWN. Would you like to respond to that, too?

Ms. MITHAL. I agree with what Ms. Twohig said.

Senator BROWN. Which part? The part of——

Ms. MITHAL. That companies would be more likely to shore up their practices if consumers had more power.

Senator BROWN. I guess I do not know why a simple "yes" is not clear there. When credit providers know that the law is mostly—the power of the law is mostly on their side and not on the consumer side. You know, Anatole France said, ah, the majesty of the law. It prohibits rich people as well as poor people from sleeping under bridges. Yeah, it does. Well, that tells you a lot about where the power in society is, and the power more and more is residing with those with more and more power and influence and privilege. And consumers have less and less of that. It is just so clear to me that the credit providers act worse because the law so often is on their side and the power resides in them.

Senator Donnelly.

Senator DONNELLY. Thank you, Mr. Chairman. Thank you to the witnesses.

On May 24th, the Economic Growth, Regulatory Relief, and Consumer Protection Act was signed into law. I negotiated and wrote that legislation along with Chairman Crapo and several of my colleagues here. This new law includes important new consumer protection related to the credit bureaus to benefit servicemembers, veterans, and all Americans. The law provides free credit freezes, credit monitoring for servicemembers, and protections for veterans from VA billing delays.

I would like to highlight these consumer-friendly provisions and receive feedback and updates from you on efforts to oversee the implementation and enforcement.

The new law includes a provision to provide free credit monitoring for active-duty servicemembers. The FTC was provided 1 year to complete the rulemaking which will help shape the credit monitoring services provided.

Ms. Mithal, I expect the FTC to complete its rulemaking as soon as possible so troops can start receiving this important service. What is the FTC's expected timeline for the rulemaking?

Ms. MITHAL. So, Senator, I can assure you we are working as expeditiously as possible to complete the rulemaking, and I am hoping that we would have a Notice of Proposed Rulemaking out by hopefully at least the fall. I do not have complete control over that, but that is what I am committing to.

Senator DONNELLY. Obviously, the sooner the better.

Ms. MITHAL. Absolutely.

Senator DONNELLY. Section 301 of the new law includes a section I authored with Senator Perdue to allow every American to freeze and unfreeze their credit free of charge and set year-long fraud alerts. Additionally, the FTC and the major credit bureaus have to set up web pages where consumers can easily freeze their credit, set a fraud alert, and opt out of prescreened credit offers. These provisions allow Americans to take control of their credit files. The law requires compliance by September 21st. These provisions will make things easier for consumers.

Could you please speak about the provisions generally and your expectation for the level of communication and collaboration that will occur between your agencies and the credit bureaus during implementation to ensure consumers benefit as was intended? If you could each respond.

Ms. TWOHIG. So I can assure you, Senator, that the Bureau is going to work expeditiously to update—to implementation what it needs to do in implementing the Economic Growth, Regulatory Relief, and Consumer Protection Act. That would include updating the summary of rights that goes to consumers so that when they get their credit report, they have the information about these important new protections available to them, as well as educating consumers. We work collaboratively with the FTC and share information about that kind of information, as well as, of course, overseeing the compliance with these new provisions.

Senator DONNELLY. Ms. Mithal.

Ms. MITHAL. And I would say, first of all, I think these are very important rights, and they give important tools to consumers, so thank you for your work on that.

As to our implementation, we have put out some guidance to consumers informing them of the new updates to the law that will take place in September, and we have already begun discussions with the CRAs about creating an online portal to effectuate all those tools for consumers. And so we are hoping to be ready—or we will be ready by September when the law goes into effect.

Senator DONNELLY. OK. Section 302 of the new law is based off the Protecting Veterans Credit Act, which I introduced with Senator Rounds to ensure veterans are not wrongly penalized by med-

ical bill payment delays at the Department of Veterans Affairs. Many veterans had their credit scores damaged when the VA was late to pay medical bills. That will not be a problem any longer due to this new law.

Your agencies, again, have oversight and enforcement authority. Can you speak as to how this provision will ensure that veterans are not wrongly penalized for medical debt that is actually the VA's responsibility? Ms. Twohig.

Ms. TWOHIG. Senator, you can be sure that we will be looking for compliance with those important new provisions.

Senator DONNELLY. Ms. Mithal.

Ms. MITHAL. And, again, I think the provisions provide very important new rights for veterans. I think there have been recent studies showing the lack of predictiveness of medical debt, and so I think that is a very important provision, and we will do everything we can to support it.

Senator DONNELLY. All right. Thank you, Mr. Chairman.

Senator BROWN. Thank you, Senator Donnelly.

I ask unanimous consent to enter into the record a letter from several consumer advocacy groups. Without objection.

Thanks for being the last guy standing.

[Laughter.]

Senator DONNELLY. Ready to help anytime.

Senator BROWN. That concludes the questioning for today. Questions for the record are due from Senators in 1 week, by Thursday, July 19th. We ask the two of you to respond to those questions as quickly as possible.

Thank you for joining us. This concludes the hearing.

[Whereupon, at 11:29 a.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF CHAIRMAN MIKE CRAPO

Today's hearing is entitled "An Overview of the Credit Bureaus and the Fair Credit Reporting Act".

Credit bureaus play a valuable role in our financial system by helping financial institutions assess a consumer's ability to meet financial obligations, and also facilitating access to beneficial financial products and services.

Given this role, they have a lot of valuable personal information on consumers and therefore are targets of cyberattacks.

Last year, Equifax experienced an unprecedented cybersecurity incident which compromised the personal data of over 145 million Americans.

Following that event, the Banking Committee held two oversight hearings on the breach and consumer data protection at credit bureaus.

The first hearing with the former Equifax CEO examined details surrounding the breach, while the second hearing with outside experts examined what improvements might be made surrounding credit reporting agencies and data security.

This Committee also recently held a hearing on cybersecurity and risks to the financial services industry.

These hearings demonstrated bipartisan concern about the Equifax data breach and the protection of consumers' personally identifiable information, as well as support for specific legislative measures to address such concerns.

Some of these were addressed in S. 2155, the Economic Growth, Regulatory Relief and Consumer Protection Act, which included meaningful consumer protections for consumers who become victims of fraud.

For example, it provides consumers unlimited free credit freezes and unfreezes per year.

It allows parents to turn on and off credit reporting for children under 18, and provides important protections for veterans and seniors.

Last month, a *New York Times* article commenting on the bill noted that, "one helpful change . . . will allow consumers to 'freeze' their credit files at the three major credit reporting bureaus—without charge. Consumers can also 'thaw' their files, temporarily or permanently, without a fee."

Susan Grant, director of consumer protection and privacy at the Consumer Federation of America expressed support for these measures, calling them "a good thing."

Paul Stephens, director of policy and advocacy at the Privacy Rights Clearinghouse, similarly noted that the freeze provision "has the potential to save consumers a lot of money."

But there is still an opportunity to see whether more should be done, and today's hearing will help inform this Committee in this regard.

Today, I look forward to learning more from the witnesses about: the scope of the Fair Credit Reporting Act and other relevant laws and regulations as they pertain to credit bureaus; the extent to which the Bureau of Consumer Financial Protection and the FTC, whom the two witnesses represent, oversee credit bureau data security and accuracy; the current state of data security, data accuracy, data breach policy, and dispute resolution processes at the credit bureaus; and what, if any, improvements could be made.

States have begun to react in their own ways to various aspects of the public debate on privacy, data security, and the Equifax data breach.

Two weeks ago, California enacted the California Consumer Privacy Act which will take effect on January 1, 2020.

The Act, which applies to certain organizations conducting business in California, establishes a new privacy framework by creating new data privacy rights, imposing special rules for the collection of minors' consumer data, and creating a damages framework for violations and businesses failing to implement reasonable security procedures.

Many Members are interested in learning more about what California and other States are doing on this front.

Additionally, 2 weeks ago, eight State banking commissioners jointly took action against Equifax in a consent order requiring the company to take various actions regarding risk assessment and information security.

I have long been concerned about data collection and data privacy protections by the Government and private industry.

Given Americans' increased reliance and use of technology where information can be shared by the swipe of a finger, we should ensure that companies and Government entities who have such information use it responsibly and keep it safe.

PREPARED STATEMENT OF PEGGY L. TWOHIG

ASSISTANT DIRECTOR, OFFICE OF SUPERVISION POLICY, DIVISION OF SUPERVISION, ENFORCEMENT, AND FAIR LENDING, BUREAU OF CONSUMER FINANCIAL PROTECTION

JULY 12, 2018

Chairman Crapo, Ranking Member Brown, thank you for the opportunity to testify today about the work of the Bureau of Consumer Financial Protection (Bureau) to address consumer protections in the consumer reporting market. My name is Peggy Twohig, and I am the Assistant Director for Supervision Policy at the Bureau. The Office of Supervision Policy is responsible for developing supervision strategy across bank and nonbank markets and ensuring that policy decisions are consistent across markets, charters, and regions.

Prior to my work at the Bureau, I was Director of the Office of Consumer Protection at the Department of the Treasury (Treasury), where I worked on the proposal to create a new consumer agency as part of financial regulatory reform. Immediately before joining Treasury, I served as Associate Director of the Division of Financial Practices at the Federal Trade Commission (FTC). My 17-year tenure at the FTC focused on enforcement and policy issues related to consumer financial services. I have also worked as a litigator in private practice with the firm of Arnold & Porter in Washington, DC.

Credit Reporting System

The consumer reporting market plays a critical role in the overall consumer financial services market and has enormous reach and impact; over 200 million Americans have credit files with tradelines furnished voluntarily by over 10,000 providers. This information is used by many different types of businesses, including creditors, insurers, landlords, telecommunications providers, and employers, to make decisions about individual transactions with consumers. In particular, creditors rely on the information in consumers' credit files to make decisions as to whether to approve a variety of credit transactions, including mortgages, credit cards, student loans, and auto loans. And, when extending credit, creditors use that information to determine what terms to offer.

Accurate consumer report information is therefore important to creditors and other consumer report users to make good business decisions. For any individual consumer, an accurate consumer report can be even more important, given the significant impact that information can have on the consumer's ability to obtain or pay for financial and other products and services. Despite the impact credit reports can have on a consumer, consumers do not get to choose who collects and sells consumer report information about them.

Because of the importance of consumer report accuracy to businesses and consumers, the structure of the Fair Credit Reporting Act (FCRA) creates interrelated legal standards and requirements to support the policy goal of accurate credit reporting. These requirements anticipate that all reports will not be perfect; instead the FCRA requires that credit reporting agencies (CRAs) have "reasonable procedures to assure maximum possible accuracy" of reports.[1] It also imposes certain accuracy obligations on furnishers.[2] The FCRA also sets forth a dispute and investigation framework, with obligations on both CRAs and furnishers, to ensure potential errors are investigated and corrected promptly, if necessary.[3] This dispute resolution framework is important to the efficient operation of credit markets, as it provides a standard mechanism for identifying and resolving inaccuracies when they occur.

Bureau Authority Over Consumer Reporting Agencies and Furnishers

Congress authorized the Bureau to assess compliance with the requirements of Federal consumer financial laws as part of its supervision of both depository institutions and nondepository institutions. As defined by the Dodd–Frank Wall Street Reform and Consumer Protection Act (Dodd–Frank Act), Federal consumer financial laws include most provisions of the Fair Credit Reporting Act.[4] The FCRA is the primary statute that governs consumer reporting by CRAs, furnishing information to CRAs, and using reports generated by CRAs. Together with its implementing regulation, Regulation V,[5] the FCRA imposes obligations on the compilation, mainte-

[1] FCRA Section 607(b), 15 U.S.C. §1681e(b).
[2] FCRA Section 623(a). 15 U.S.C. §1681s-2(a) .
[3] FCRA Section 611, 15 U.S.C. §1681i; FCRA Section 623(b), 15 U.S.C. §1681s-2(b).
[4] Id. at §5481(14), (12)(F).
[5] 12 CFR part 1022.

nance, furnishing, use, and disclosure of information associated with credit, insurance, employment, and other decisions made about consumers.

Federal consumer financial laws also include substantive provisions of Title X of the Dodd–Frank Act.[6] One of these provisions is the prohibition on a covered person or service provider from engaging in unfair, deceptive, or abusive acts or practices (UDAAP).[7] Many CRAs are "covered persons" under the Dodd–Frank Act because they collect, analyze, maintain, or provide consumer report information or other account information used or expected to be used in connection with decisions regarding the offering or provision of consumer financial products or services and delivered, offered, or provided in connection with a consumer financial product or service.[8] Depending on the facts and circumstances of any given transaction, CRAs might also be considered service providers.[9]

The Bureau has supervisory authority over consumer reporting agencies that are larger participants in the consumer reporting market. In July 2012, the Bureau promulgated the first larger participant rule to define larger participants in the consumer reporting market because of the importance of this function to efficient credit markets.[10] The larger participant rule defines a larger participant of the consumer reporting market as a nonbank covered person with more than $7 million in annual receipts resulting from relevant consumer reporting activities.[11] The Bureau estimated 30 companies that account for about 94 percent of the market's annual receipts met the larger participant threshold.[12]

Participants in this market include nationwide consumer reporting companies, consumer report resellers, and specialty consumer reporting companies.[13] The Bureau reviews the operations of these larger participants for compliance with Federal consumer financial laws, including the FCRA and Regulation V. The Bureau also has supervisory authority over a substantial number of entities that furnish credit information to CRAs. As part of its exercise of this authority, the Bureau reviews compliance with the FCRA's furnishing requirements at other institutions subject to the Bureau's supervisory authority, such as large banks. The Bureau also has enforcement authority over nearly every person, regardless of status as a supervised entity, who violates the FCRA.[14] The Bureau is the first Federal or State agency to have both supervisory and enforcement authority over CRAs and the other participants in the consumer reporting market.

In addition to enforcement and supervisory authority over CRAs, the Bureau has broad authority to promulgate rules "as are necessary to carry out the purposes of" the FCRA.[15] The Bureau's rules are applicable to any person subject to the FCRA, except certain motor vehicle dealers.[16] The Bureau does not, however, have rulemaking authority (or supervisory or enforcement authority) under Sections 615(e) and 628 of the FCRA. These provisions direct the Federal banking agencies, the National Credit Union Administration, the FTC, the Commodity Futures Trading Commission, and the Securities and Exchange Commission to promulgate regulations relating to Red Flags, and Disposal of Records. The FTC used its authority under these provisions of the FCRA to promulgate its ID Theft Red Flags Rule[17] and its Consumer Report Records Disposal Rule.[18] Other agencies have promulgated comparable rules pursuant to these sections.

CRAs and other participants in the consumer reporting market may also be subject to other laws within the Bureau's authority, such as the Gramm–Leach–Bliley Act's (GLBA) notice and opt-out and privacy provisions. GLBA gives the Bureau

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[6] 12 U.S.C. §5481(14).

[7] 12 U.S.C. §§5531, 5536(a).

[8] Id. at §5481(5), (15)(A)(ix).

[9] Id. at §5481(26) (defining "service provider" as "any person that provides a material service to a covered person in connection with the offering or provision by such covered person of a consumer financial product or service . . . ").

[10] *https://www.consumerfinance.gov/policy-compliance/rulemaking/final-rules/defining-larger-participants-consumer-reporting-market/*.

[11] 12 CFR §1090.104.

[12] *https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-to-supervise-credit-reporting/*.

[13] The term "consumer reporting company" means the same as "consumer reporting agency," as defined in the Fair Credit Reporting Act, 15 U.S.C. §1681a(f), including nationwide consumer reporting agencies as defined in Section 1681a(p) and nationwide specialty consumer reporting agencies as defined in Section 1681a(x).

[14] E.g., Section 1029 of the Dodd–Frank Act excludes certain motor vehicle dealers from the Bureau's rulemaking, enforcement, or other authority.

[15] 15 U.S.C. §1681s(e)(1).

[16] 12 CFR §1022.1(b)(2).

[17] 16 CFR Part 681.

[18] 16 CFR Part 682.

rulemaking and enforcement authority over these provisions.[19] (Since these provisions are Federal consumer financial laws they are also within the Bureau's supervisory authority under section 1024 of the Dodd–Frank Act.) The Bureau cannot, however, implement GLBA section 501(b), which requires that financial institutions develop, implement, and maintain comprehensive information security programs that contain administrative, technical, and physical safeguards.[20] The Bureau has no supervisory, enforcement, or rulemaking authority with regard to GLBA section 501 (b) or its implementing rules; that section is excluded from the definition of Federal consumer financial law.[21] Section 501(b) is implemented by rules and guidelines promulgated by the FTC and other agencies and include the FTC's GLBA Customer Information Safeguards Rule.[22]

Bureau Credit Reporting Work

In both its supervision and enforcement work, the Bureau has focused on credit reporting accuracy and dispute handling by both CRAs and furnishers.

In March 2017, the Bureau issued a special edition of its *Supervisory Highlights* publication in which it reported out on the supervisory work undertaken in consumer reporting.[23] As discussed in the report, the Bureau has focused its supervisory work on the key elements underpinning accuracy. As a result of these reviews, the Bureau directed specific improvements in data accuracy and dispute resolution at one or more CRA, including:

- improved oversight of incoming data from furnishers;
- institution of quality control programs of compiled consumer reports;
- monitoring of furnisher dispute metrics to identify and correct root causes;
- enhanced oversight of third-party public records service providers;
- adherence to independent obligation to reinvestigate consumer disputes, including review of relevant information provided by consumers; and
- improved communication to consumers of dispute results.

In addition, the Bureau directed both bank and nonbank furnishers, consistent with the FCRA's requirements, to develop reasonable written policies and procedures regarding accuracy of the information they furnish and to take corrective action when they furnished information they determined to be inaccurate. The Bureau also found that furnishers foiled to either conduct investigations or send results of dispute investigations to consumers and demanded that these furnishers bring their dispute handling practices into compliance with legal requirements.

In addition to supervisory work, the Bureau has brought enforcement actions and entered into settlements related to institutions' violation of the FCRA's accuracy and dispute investigation requirements.[24] The Bureau will continue to examine and investigate CRAs and furnishers, using the authority and tools provided by the Dodd–Frank Act and other statutes.

The Bureau is also focused on educating consumers by providing consumers with tools and information to help them know what to do when they encounter a problem, or how to avoid problems in the first place. For example, we provide information to consumers about how they can obtain access to their credit reports to check their accuracy and dispute any information they believe to be incorrect.[25]

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[19] 15 U.S.C. §§6804(a)(1)(A) and 6805(a)(8). The Bureau's GLBA authority does not extend to certain motor vehicle dealers. 12 CFR §1016.1(b)(1).

[20] 15 U.S.C. §6801(b).

[21] 15 U.S.C. §5481(12), (14).

[22] 16 CFR Part 314.

[23] *https://www.consumerfinance.gov/documents/2774/201703-cfpb-Supervisory-Highlights-Consumer-Reporting-Special-Edition.pdf.*

[24] See, e.g., *http://files.consumerfinance.gov/f/201510_cfpb_consent-order_general-information-serviceinc.pdf; http://files.consumerfinance.gov/f/201512_cfpb_consent-order_clarity-services-inc-timothy-ranney.pdf; https://files.consumerfinance.gov/f/documents/bcfp_security-group-inc_consent-order_2018-06.pdf; https://files.consumerfinance.gov/f/documents/201701_cfpb_CitiFinancial-consent-order.pdf.*

[25] For information about how to access your credit reports and how to dispute errors: *https://www.consumerfinance.gov/consumer-tools/credit-reports-and-scores/*; For information about obtaining credit reports: *https://www.consumerfinance.gov/ask-cfpb/how-do-i-get-a-copy-of-my-credit-reports-en-5/*; For information about how to dispute errors: *https://www.consumerfinance.gov/ask-cfpb/how-do-i-dispute-an-error-on-my-credit-report-en-314/*; For information about common credit issues: *https://www.consumerfinance.gov/about-us/blog/3-common-credit-issues-and-what-you-can-do-fix-them/*.

Data Security

CRAs hold a tremendous amount of information about consumers, including sensitive financial information. If CRAs do not protect this data, it may lead to data breaches and other unauthorized access to it. Unauthorized access to data at consumer reporting agencies creates the risk of substantial harm to consumers, including the risk of identity theft. Because of these risks, since the Equifax breach, the Bureau has increased its attention to data security issues in our supervisory and enforcement activities.

The Bureau has the authority to conduct data security investigations and examinations at nonbanks over which it has supervisory authority, including CRAs.

Data security reviews conducted by the Bureau are comprised of three specific inquiries, consistent with the three prongs of the Bureau's general examination authority.[26] First, the Bureau assesses the facts and circumstances to determine whether a nonbank's data security practices and policies constitute violations of Federal consumer financial law, including violations of the Dodd–Frank Act's prohibition against unfair, deceptive or abusive acts and practices (UDAAP)[27] and of the Fair Credit Reporting Act.[28] Second, the Bureau obtains information about compliance management systems and procedures relating to data security practices. Third, the Bureau detects and assesses risks posed by potential data security lapses to consumers and to markets for consumer financial products and services.

In addition to this work, the Bureau website has a list of resources and information for consumers about data breaches to help consumers understand what steps or actions they can take to protect their personal information.[29] The Bureau also provides resources to help consumers protect themselves from identity theft,[30] to help military personnel and their families secure their identities,[31] and specific resources on the Top 10 ways to protect yourself in the wake of the Equifax data breach.[32] In addition, the Bureau's online tool, Ask CFPB, has provided consumers with answers to frequently asked questions about a variety of topics, including identity theft, credit freezes, fraud alerts, and credit and identity monitoring.[33]

Conclusion

Large breaches call for a coordinated response, and the Bureau will continue to coordinate with other Federal and State agencies. We will also continue to exercise our authority to examine and investigate credit reporting companies and furnishers of information, and to educate consumers about important consumer financial issues. Consumers should have confidence that their credit reports comply with all applicable legal requirements.

Thank you again for the opportunity to testify today at this important hearing. I would be happy to answer your questions about the Bureau's work related to credit reporting.

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[26] Section 1024 of the Dodd–Frank Act grants the Bureau the authority to conduct examinations of certain nonbank financial institutions, including larger participants in the consumer reporting market, under its risk-based supervision program for the purposes of: (a) assessing compliance with the requirements of Federal consumer financial law; (b) obtaining information about the activities and compliance systems or procedures of such person; and (c) detecting and assessing risks to consumers and to markets for consumer financial products and services. 15 U.S.C. §5514.

[27] Both courts and executive branch agencies have found that, in certain circumstances, insufficient data security can constitute an unfair or deceptive practice. FTC v. Wyndham Worldwide Corp., 799 F.3d 236 (3d Cir. 2015); FTC v. AshleyMadison.com, No. 1:16-cv-02438 (D.D.C. filed Dec. 14, 2016); available at *https://www.ftc.gov/enforcement/cases-proceedings/152-3284/ashley-madison.*

[28] FCRA Section 607(a), 15 U.S.C. 1681e.

[29] *https://www.consumerfinance.gov/equifaxbreach.*

[30] *https://www.consumerfinance.gov/about-us/blog/identity-theft-protection-following-equifax-data-breach/.*

[31] *https://www.consumerfinance.gov/about-us/blog/servicemembers-should-secure-their-identity-after-equifax-data-breach/.*

[32] *https://www.consumerfinance.gov/about-us/blog/top-10-ways-protect-yourself-wake-equifax-data-breach/.*

[33] Available at *http://www.consumerfinance.gov/askcfpb/search/?selected-facets=tag-exact%3Aidentity+theft.*

PREPARED STATEMENT OF MANEESHA MITHAL

ASSOCIATE DIRECTOR, DIVISION OF PRIVACY AND IDENTITY PROTECTION, BUREAU OF CONSUMER PROTECTION, FEDERAL TRADE COMMISSION

JULY 12, 2018

Introduction

Chairman Crapo and Members of the Committee, my name is Maneesha Mithal, and I am the Associate Director for the Division of Privacy and Identity Protection at the Federal Trade Commission (Commission or FTC).[1] I appreciate the opportunity to appear before you today to discuss the Fair Credit Reporting Act, credit bureaus, and data security.

Congress enacted the Fair Credit Reporting Act[2] (FCRA) in 1970, recognizing the importance of "fair and accurate credit reporting" to maintain "the efficiency of the banking system" and "the public[']s confidence" in that system, while at the same time balancing 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."[3] The FCRA helps to (1) prevent the misuse of sensitive consumer report information by limiting recipients to those who have a legitimate need for it; (2) improve the accuracy and integrity of consumer reports; and (3) promote the efficiency of the Nation's banking and consumer credit systems. Since the FCRA's passage, Congress has amended the statute to address developments in the consumer reporting system and the marketplace and to increase consumers' rights and protections with respect to the collection and use of their data.[4]

The Commission has played a key role in the implementation, enforcement, and interpretation of the FCRA since its enactment.[5] In the last decade, the Commission has brought over 30 actions to enforce the FCRA against consumer reporting agencies (CRAs), users of consumer reports, and furnishers of information to CRAs. As the consumer reporting system evolves and new technologies and business practices emerge, vigorous enforcement of the FCRA continues to be a top priority for the Commission, as well as consumer and business education concerning applicable rights and responsibilities under the statute.

This testimony first provides background on the FCRA. Next, it discusses marketplace developments related to credit report accuracy. It then discusses the Commission's work to enforce the accuracy provisions of the FCRA and educate consumers and businesses about their respective rights and responsibilities under the statute. Finally, it discusses the data security requirements applicable to credit bureaus and the FTC's efforts to promote data security in this sector.

Background on the FCRA

CRAs assemble or evaluate consumer data for third parties to use to make critical decisions about the availability and cost of various consumer products and services, including credit, insurance, employment, and housing.[6] These consumer reports are often used to evaluate the risk of future nonpayment, default, or other adverse events. For example, complete and accurate consumer reports enable creditors to

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[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 or any individual Commissioner.

[2] 15 U.S.C. §§1681-1681x.

[3] Id. §1681(a).

[4] The Consumer Credit Reporting Reform Act of 1996, Title II, Subtitle D, Chapter 1, of the Omnibus Consolidated Appropriations Act for Fiscal Year 1997 (Public Law No. 104-208, Sept. 30, 1996), made extensive revisions to the FCRA, including expanding the duties of consumer reporting agencies, increasing obligations on users of consumer reports, and adding furnishers of information to consumer reporting agencies as a category of entities with statutory obligations. There were a number of more modest revisions over the next 7 years, the most significant of which was a 1999 amendment that specifically authorized the Federal financial agencies to promulgate regulations for the banks and other entities subject to their jurisdiction. The Fair and Accurate Credit Transactions Act of 2003, Public Law No. 108-159 (Dec. 4, 2003) (FACT Act), added several sections to assist consumers and businesses in combating identity theft and reduce the damage to consumers. The Commission, often in conjunction with the Federal financial agencies, issued numerous rules to implement the various FACT Act provisions.

[5] As enacted, the FCRA established the Commission as the primary Federal enforcement agency, with wide jurisdiction over entities involved in the consumer reporting system; the primary exceptions to the Commission's jurisdiction are federally regulated financial institutions. See 15 U.S.C. §1681s(a)-(b). Pursuant to the Consumer Financial Protection Act of 2010 (CFPA), Title X of Public Law 111-203, 124 Stat. 1955 (July 21, 2010) (The Dodd–Frank Wall Street Reform and Consumer Protection Act), the Commission shares its FCRA enforcement role with the Bureau of Consumer Financial Protection (Bureau) in many respects.

[6] 15 U.S.C. §1681a(d) and (f).

make informed lending decisions, benefiting both creditors and consumers. Errors in consumer reports, however, can cause consumers to be denied credit or other benefits or pay a higher price for them. Errors in consumer reports can also cause credit issuers to make inaccurate decisions that result in declining credit to a potentially valuable customer or issuing credit to a riskier customer than intended.

The FCRA imposes a number of obligations on CRAs. For example, to protect the privacy of sensitive consumer report information, CRAs must take reasonable measures to ensure that they provide such information only to those who have a statutorily specified "permissible purpose" to receive it.[7] CRAs must also comply with requirements to help ensure the accuracy of consumer reports, including requirements that CRAs (1) maintain reasonable procedures to ensure the "maximum possible accuracy" of consumer reports[8] and (2) maintain procedures through which consumers can dispute and correct inaccurate information in their consumer reports.[9]

Under the FCRA, if a consumer disputes the completeness or accuracy of information contained in his or her file, the CRA must complete a reasonable investigation within 30 days. The CRA must notify the furnisher of the disputed information within five business days. If a disputed item is found to be inaccurate or incomplete or cannot be verified, the CRA must delete or modify the information and notify the furnisher. In general, the CRA must provide the consumer with written notice of the results of the investigation in accordance with the procedures set forth in the statute within 5 business days after the completion of the investigation.

In addition, the FCRA imposes obligations on those who furnish information about consumers to CRAs, such as entities extending credit. For example, furnishers have a duty to report accurate information and investigate consumer disputes of inaccurate information.[10]

Users of consumer reports have obligations under the statute as well. For example, if a user of a consumer report takes an adverse action against a consumer—such as a denial of credit or employment—based on information in a consumer report, the user must provide an adverse action notice to the consumer, which explains how the consumer can obtain a free copy of the report and dispute any inaccurate information in the report.[11]

Credit Report Accuracy

In 2012, the Commission published a study of credit report accuracy mandated by the FACT Act, which amended the FCRA.[12] It was the first major study that looked at all of the primary groups that participate in the credit reporting and scoring process—consumers, furnishers (e.g., creditors, lenders, debt collection agencies), the Fair Isaac Corporation (which develops FICO credit scores), and the national credit bureaus.[13] To implement the study, researchers worked with approximately 1,000 consumers to review their free credit reports from the three major credit bureaus. The researchers helped consumers identify and dispute possible errors on their credit reports. According to the study findings, 25 percent of consumers identified errors on their credit reports that might affect their credit scores and 80 percent of these consumers who filed disputes experienced some modification to their credit reports. Overall, 13 percent of consumers experienced a change in their credit scores after a dispute and 5 percent of consumers experienced an increase in their credit scores such that their credit risk tier decreased and the consumer may be more likely to be offered a lower loan interest rate.

There have been significant changes in the marketplace aimed at increasing credit report accuracy since the Commission published its study. For example, the Bureau has been exercising its supervisory authority over the nationwide credit bureaus and it periodically publishes Supervisory Highlights describing its findings. Last year, it published an edition focused on accuracy issues in credit reporting and the

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[7] Id. §1681b(a), (c). Permissible purposes under the FCRA include, but are not limited to, the use of a consumer report in connection with a determination of eligibility for credit, insurance, or a license; in connection with the review of an existing account; and for certain employment purposes.

[8] Id. §1681e(b).

[9] Id. §1681i(a)–(d)(1).

[10] Id. §1681s-2(a)–(b).

[11] Id. §1681m(a). The adverse action notice also must include a statement that the CRA that supplied the consumer report did not make the decision to take the adverse action and cannot give the consumer any specific reasons for the decision. Id. §1681m(a)(2)(B).

[12] Public Law No. 108-159 (Dec. 4, 2003).

[13] Section 319 of the Fair and Accurate Credit Transactions Act of 2003: Fifth Interim Federal Trade Commission Report to Congress Concerning the Accuracy of Information in Credit Reports (Dec. 2012), available at *https://www.ftc.gov/reports/section-319-fair-accurate-credit-transactions-act-2003-fifth-interim-federal-trade.*

handling and resolution of consumer disputes, and it pointed to several specific improvements it directed in these areas.[14]

In addition, in 2015, the nationwide credit bureaus announced a Nationwide Consumer Assistance Plan (NCAP) as a result of a settlement with over 30 State attorneys general, with a number of provisions designed to improve the accuracy of credit reports.[15] These provisions include requiring all data furnishers to use the most current reporting format; removing any previously reported medical collections that have been paid or are being paid by insurance; requiring debt collectors to regularly update the status of unpaid debts and remove debts no longer being pursued for collection; and implementing an enhanced dispute resolution process for consumers that are victims of fraud or identity theft or are involved in mixed files (where two consumer files are mistakenly mixed together). NCAP contained a phased implementation plan scheduled to be completed this year.

FTC Activities To Promote Credit Report Accuracy

Law Enforcement

FCRA enforcement continues to be a top priority for the Commission. With the advent in 2011 of the Bureau's supervisory authority over the nationwide credit bureaus and the coordination efforts between the agencies, the FTC has focused its FCRA law enforcement efforts on other entities in the credit reporting area and other aspects of the consumer reporting industry more broadly.

For example, the FTC settled cases against furnishers that allegedly had inadequate policies and procedures for reporting accurate credit information to CRAs. In Credit Protection Association, LP, the Commission alleged that a debt collector failed to have adequate policies and procedures to handle consumer disputes, did not have a policy requiring notice to consumers of the outcomes of investigations about disputed information, and in numerous instances failed to inform consumers of the outcome of disputes.[16] The settlement included $72,000 in civil penalties.[17] And, in Tricolor Auto Acceptance, LLC, the Commission alleged that the loan-servicing department of an auto dealer failed to have written policies and procedures designed to ensure that the credit information it reported to CRAs was accurate and failed to properly investigate consumer disputes regarding the accuracy of credit information.[18] The settlement included $82,000 in civil penalties.

In addition, the FTC has settled cases against background screening CRAs that compile background reports on consumers that may include driving records, employment and education history, eviction records, and criminal records for use in making employment and housing decisions. These settlements include allegations relating to inaccuracies in consumer reports, as well as failures to protect the privacy of consumer reports by ensuring permissible use. For example, in InfoTrack Information Services, Inc., the Commission alleged that a background screening CRA failed to have reasonable procedures to ensure the maximum possible accuracy of consumer report information and, as a result, provided inaccurate information suggesting that job applicants potentially were registered sex offenders.[19] The settlement included $1 million in civil penalties, which was suspended upon payment of $60,000 based on inability to pay. In Instant Checkmate, Inc., the Commission alleged that the CRA compiled public record information into background reports and marketed its services to landlords and employers but failed to comply with several FCRA provisions, including failing to maintain reasonable procedures to ensure the accuracy of its reports, failing to have reasonable procedures to ensure that those using its re-

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[14] See Supervisory Highlights Consumer Reporting Special Edition (Mar. 2, 2017), available at *https://www.consumerfinance.gov/data-research/research-reports/supervisory-highlights-consumer-reporting-special-edition/*.

[15] See, e.g., National Consumer Assistance Plan, News Release (Jun. 9, 2016), available at *http://www.nationalconsumerassistanceplan.com/news/news-release/*.

[16] U.S. v. Credit Protection Association, LP, No. 3:16-cv-01255-D (N.D.Tex. filed May 9, 2016), available at *https://www.ftc.gov/enforcement/cases-proceedings/142-3142/credit-protection-association.*

[17] As specified by the Federal Civil Penalty Inflation Adjustment Act of 1990, 28 U.S.C. §2861, as amended by the Debt Collection Improvements Act of 1996, Public Law 104-134, §31001(s)(1), 110 Stat. 1321-373, in relevant part, civil penalties under the FCRA are capped at $3,500 per violation for violations occurring before August 1, 2016, $3,756 per violation for violations occurring between that date and January 23, 2017, and $3,817 for violations occurring on or after January 24, 2017.

[18] U.S. v. Tricolor Auto Acceptance, LLC, No. 3:15-cv-3002 (N.D.Tex. filed Sept. 16, 2015), available at *https://www.ftc.gov/enforcement/cases-proceedings/142-3073/tricolor-auto-acceptance-llc.*

[19] U.S. v. Infotrack Information Services, Inc., No. 1:14-cv-02054 (N.D.Ill. filed Apr. 9, 2014), available at *https://www.ftc.gov/enforcement/cases-proceedings/122-3092/infotrack-information-services-inc-et-al.*

ports had permissible purposes for accessing them, and providing reports to users that it did not have reason to believe had a permissible purpose to receive them.[20] The settlement included $525,000 in civil penalties.

The FTC has also brought cases against check authorization CRAs for failing to comply with their accuracy obligations. Check authorization companies compile consumers' personal information and use it to help retail merchants throughout the United States determine whether to accept consumers' checks. In its settlements with Telecheck[21] and Certegy,[22] two of the Nation's largest check authorization companies, the Commission charged these companies with failing to follow FCRA accuracy procedures, failing to follow proper procedures for consumer disputes, and failing to establish and implement reasonable written policies regarding the accuracy of information the companies furnish to other CRAs. The FTC obtained $3.5 million in civil penalties against each company.

Business Guidance and Consumer Education

The Commission also continues to educate consumers and businesses on their consumer reporting rights and obligations under the FCRA. The FTC has published guidance for employment and tenant background screening companies regarding their obligations under the FCRA, including with respect to accuracy and consumer disputes.[23] For furnishers, the FTC publication *Consumer Reports: What Information Furnishers Need To Know* provides an overview of obligations under the FCRA.[24] Similarly, for users of consumer reports, FTC guidance includes publications for employers, landlords, insurers, and creditors, as well as guidance on secure disposal of consumer information for all businesses.[25]

The FTC also has a number of user-friendly resources for consumers designed to inform them of their rights under the FCRA and assist them with navigating the consumer reporting system. The publication *Credit and Your Consumer Rights* provides an overview of credit, explains consumers' legal rights, and offers practical tips to help solve credit problems.[26] The FTC also has publications that explain how consumers can obtain their free annual credit reports from each of the nationwide consumer reporting agencies[27] and use the FCRA's dispute procedures to ensure that information in their consumer reports is accurate.[28] For consumers seeking employment or housing, the FTC has materials on employment background

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[20] U.S. v. Instant Checkmate, Inc., No. 3:14-cv-00675-H-JMA (S.D.Cal. filed Apr. 9, 2014), available at *https://www.ftc.gov/enforcement/cases-proceedings/122-3221/instant-checkmate-inc.*

[21] U.S. v. TeleCheck Services, Inc., No. 1:14-cv-00062 (D.D.C. filed Jan. 16, 2014), available at *https://www.ftc.gov/enforcement/cases-proceedings/112-3183/telecheck-services-inc.*

[22] U.S. v. Certegy Services, Inc., No. 1:13-cv-01247 (D.D.C. filed Aug. 15, 2013), available at *https://www.ftc.gov/enforcement/cases-proceedings/112-3183/telecheck-services-inc.*

[23] See "What Employment Background Screening Companies Need To Know About the Fair Credit Reporting Act" (Apr. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/what-employment-background-screening-companies-need-know-about*; "What Tenant Background Screening Companies Need To Know About the Fair Credit Reporting Act" (Oct. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/what-tenant-background-screening-companies-need-know-about-fair.*

[24] See *Consumer Reports*: "What Information Furnishers Need To Know" (Nov. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/consumer-reports-what-information-furnishers-need-know.*

[25] See *Consumer Reports*: "What Employers Need To Know" (Oct. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/using-consumer-reports-what-employers-need-know*; *Consumer Reports*: "What Landlords Need To Know" (Oct. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/using-consumer-reports-what-landlords-need-know*; *Consumer Reports*: "What Insurers Need To Know" (Nov. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/consumer-reports-what-insurers-need-know*; "Using Consumer Reports for Credit Decisions: What To Know About Adverse Action and Risk-Based Pricing Notices" (Nov. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/using-consumer-reports-credit-decisions-what-know-about-adverse*; "Disposing of Consumer Report Information? Rule Tells How" (Jun. 2005), available at *https://www.ftc.gov/tips-advice/business-center/guidance/disposing-consumer-report-information-rule-tells-how*.

[26] "Credit and Your Consumer Rights" (June 2017), available at *https://www.consumer.ftc.gov/articles/pdf-0070-credit-and-your-consumer-rights.*

[27] "Free Credit Reports" (Mar. 2013), available at *https://www.consumer.ftc.gov/articles/0155-free-credit-reports.*

[28] See "Disputing Errors on Credit Reports" (Feb. 2017), available at *https://www.consumer.ftc.gov/articles/0151-disputing-errors-credit-reports.*

checks[29] and tenant background checks.[30] The Commission continues to update and expand its materials as new issues arise.

Data Security

The FTC is committed to protecting consumer privacy and promoting data security in the private sector. The Commission is the Nation's primary data security regulator and enforces several statutes and rules that impose data security requirements on companies across a wide spectrum of industries, including credit bureaus. Since 2001, the Commission has undertaken substantial efforts to promote data security in the private sector through enforcement of Section 5 of the FTC Act, which prohibits unfair or deceptive acts or practices, such as businesses making false or misleading claims about their data security procedures, or failing to employ reasonable security measures.[31] The Commission is also the Federal enforcement agency for the Children's Online Privacy Protection Act (COPPA), which requires reasonable security for children's information collected online.[32]

Further, the Commission's Safeguards Rule, which implements the Gramm–Leach–Bliley Act (GLB Act), sets forth data security requirements for financial institutions within the Commission's jurisdiction, which includes credit bureaus.[33] The Safeguards Rule requires financial institutions, or companies that are significantly engaged in offering consumer financial products or services, to develop, implement, and maintain a comprehensive information security program for handling customer information. The plan must be appropriate to the company's size and complexity, the nature and scope of its activities, and the sensitivity of the customer information it handles. The FTC has exclusive enforcement authority with respect to nonbank consumer financial services providers.

Finally, the FCRA requires consumer reporting agencies to use reasonable procedures to ensure that the entities to which they provide consumer reports have a permissible purpose for receiving that information[34] and also requires the secure disposal of consumer report information.[35] This section describes the FTC's efforts to enforce these laws, educate consumers and businesses, and develop policies in this area.

Law Enforcement

The Commission has brought over 60 law enforcement actions against companies that allegedly engaged in unreasonable data security practices. Last year, the Commission took the unusual step of publicly confirming its investigation into the Equifax data breach due to the scale of public interest in the matter.

The FTC has significant experience with enforcing data security laws against CRAs. In 2006, the FTC brought the seminal Choicepoint case against a CRA that sold consumer reports to identity thieves who did not have a permissible purpose to obtain the information under the FCRA, as well as failed to employ reasonable measures to secure the personal information it collected and misrepresented its security practices under Section 5 of the FTC Act.[36] The complaint alleged that ChoicePoint failed to monitor subscribers even after receiving subpoenas from law enforcement authorities alerting it to fraudulent activity. The settlement included injunctive relief, as well as $10 million in civil penalties—the largest FCRA civil penalty in FTC history—and $5 million in consumer redress. A few years later, the FTC settled another action against the company when it suffered a data breach be-

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[29] See "Background Checks" (Mar. 2018), available at *https://www.consumer.ftc.gov/articles/0157-background-checks.*

[30] See FTC Consumer Blog, "Renting an Apartment? Be Prepared for a Background Check" (Nov. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/disposing-consumer-report-information-rule-tells-how.*

[31] 15 U.S.C. §45(a). If a company makes materially misleading statements or omissions about a matter, including data security, and such statements or omissions are likely to mislead reasonable consumers, they can be found to be deceptive in violation of Section 5. Further, if a company's data security practices cause or are likely to cause substantial injury to consumers that is neither reasonably avoidable by consumers nor outweighed by countervailing benefits to consumers or to competition, those practices can be found to be unfair and violate Section 5.

[32] 15 U.S.C. §§6501-6506; see also 16 CFR Part 312 (COPPA Rule).

[33] 16 CFR Part 314, implementing 15 U.S.C. §6801(b).

[34] 15 U.S.C. §1681e.

[35] Id. §1681w. The FTC's implementing rule is at 16 CFR Part 682.

[36] U.S. v. Choicepoint, Inc., No. 1:06-cv-00198-GET (N.D.Ga. filed Jan. 30, 2006), available at *https://www.ftc.gov/enforcement/cases-proceedings/052-3069/choicepoint-inc.*

cause it turned off a key electronic security tool used to monitor access to one of its databases, in violation of the Commission's order.[37]

The Commission has also brought actions against companies for failing to dispose of consumer report information securely. For example, in the PLS Financial Services, Inc. case, the FTC alleged that the company violated the FCRA Disposal Rule by failing to take reasonable steps to protect against unauthorized access to credit reports in the improper disposal of the consumer information, violated the Safeguards Rule requirements for financial institutions to develop and use safeguards to protect consumer information, and violated the FTC Act by misrepresenting that it had implemented reasonable measures to protect sensitive consumer information.[38] The settlement included injunctive relief and $101,500 in civil penalties.

Business Guidance and Consumer Education

In addition to law enforcement, the FTC provides extensive business guidance on data security. The agency's goal is to provide information to help businesses protect the data in their care and understand what practices may violate the laws the FTC enforces. The FTC provides general business education about data security issues, as well as specific guidance on emerging threats.

In 2015, the FTC launched its Start with Security initiative, which includes a guide for businesses,[39] as well as 11 short videos,[40] that discuss 10 important security topics and give advice about specific security practices for each. In 2016, the FTC published a business advisory on how the National Institute of Standards and Technology Cybersecurity Framework applies to the FTC's data security work[41] and released an update to "Protecting Personal Information: A Guide for Business", which was first published in 2007.[42] Last year, the FTC published its Stick with Security blog series offering additional insights into the Start with Security principles, based on the lessons of recent law enforcement actions, closed investigations, and experiences companies have shared about data security in their business.[43]

In addition to data security guidance, the FTC provides business guidance related to data breaches. In September 2016, the FTC released *Data Breach Response: A Guide for Business*,[44] and a related video, which describes immediate steps companies should take when they experience a data breach, such as taking breached systems offline, securing physical areas to eliminate the risk of further harm from the breach, and notifying consumers, affected businesses, and law enforcement. The guide also includes a model data breach notification letter businesses can use to get started.

The FTC also provides businesses with specific guidance on emerging threats. For example, most recently the FTC released a staff perspective and related blog post to help businesses prevent phishing scams.[45] Following a workshop,[46] the FTC published a blog post describing ransomware,[47] how to defend against it, and essential

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[37] U.S. v. Choicepoint, Inc., No. 1:06-cv-00198-JTC (N.D.Ga. filed Oct. 19, 2009), available at *https://www.ftc.gov/enforcement/cases-proceedings/052-3069/choicepoint-inc.*

[38] U.S. v. PLS Financial Services, Inc., No. 112-cv-08334 (N.D.Ill. filed Oct. 17, 2012), available at *https://www.ftc.gov/enforcement/cases-proceedings/1023172/pls-financial-services-inc-et-al.*

[39] "Start With Security: A Guide for Business" (June 2015), available at *https://www.ftc.gov/tips-advice/business-center/guidance/start-security-guide-business.*

[40] "Start With Security: Free Resources for Any Business" (Feb. 19, 2016), available at *https://www.ftc.gov/news-events/audio-video/business.*

[41] FTC Business Blog, "The NIST Cybersecurity Framework and the FTC" (Aug. 31, 2016), available at *https://www.ftc.gov/news-events/blogs/business-blog/2016/08/nist-cybersecurity-framework-ftc.*

[42] "Protecting Personal Information: A Guide for Business" (Oct. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/protecting-personal-information-guide-business.*

[43] FTC Business Blog, "Stick With Security: A Business Blog Series" (Oct. 2017), available at *https://www.ftc.gov/tips-advice/business-center/guidance/stick-security-business-blog-series.*

[44] "Data Breach Response: A Guide for Business" (Oct. 2016), available at *https://www.ftc.gov/tips-advice/business-center/guidance/data-breach-response-guide-business.*

[45] FTC Staff Perspective, "Businesses Can Help Stop Phishing and Protect Their Brands Using Email Authentication" (Mar. 2017), available at *https://www.ftc.gov/reports/businesses-can-help-stop-phishing-protect-their-brands-using-email-authentication-ftc-staff*; FTC Business Blog, "Want To Stop Phishers? Use Email Authentication", Mar. 3, 2017, available at *https://www.ftc.gov/news-events/blogs/business-blog/2017/03/want-stop-phishers-use-email-authentication.*

[46] Fall Technology Series: "Ransomware" (Sept. 7, 2016), available at *https://www.ftc.gov/news-events/events-calendar/2016/09/fall-technology-series-ransomware.*

[47] Ransomware is malicious software that infiltrates computer systems or networks and uses tools like encryption to deny access or hold data "hostage" until the victim pays a ransom.

steps to take if businesses become victims.[48] Further, the FTC develops targeted guidance for companies in specific industries. For example, staff developed specific security guidance for debt buyers and sellers.[49]

The Commission also educates consumers on security. For example, the FTC has provided guidance for consumers on securing their home wireless networks, a critical security step for protecting devices and personal information from compromise. These resources are accessible on the FTC's consumer guidance website, *consumer.ftc.gov*. The FTC also assists consumers affected by data breaches through its *identitytheft.gov* website that allows consumers who are victims of identity theft to quickly file a complaint with the FTC and get a free, personalized guide to recovery that helps streamline many of the steps involved. In the wake of the announcement of the Equifax data breach last year, the agency published numerous materials and created a dedicated page on its website, *ftc.gov/Equifax*, with resources to educate consumers about fraud alerts, active duty alerts, credit freezes and locks, credit monitoring, and how to reduce the risk of identity theft.

Policy Initiatives

The FTC engages in a variety of policy initiatives to enhance data security. The FTC has hosted workshops and issued reports to highlight the privacy and security implications of new technologies. For example, last year the FTC hosted a workshop to examine consumer injury in the context of privacy and data security and various issues related to the injuries consumers suffer when information about them is misused.[50] Most recently, the Commission announced plans to hold a series of public hearings on the impact of market developments on competition and consumer protection enforcement, including the Commission's remedial authority to deter unfair and deceptive conduct in privacy and data security matters.[51]

Conclusion

Thank you for the opportunity to provide the Commission's testimony on credit report accuracy and security. We look forward to continuing to work with Congress and this Committee on these important issues.

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[48] FTC Business Blog, "Ransomware—A Closer Look" (Nov. 10, 2016), available at *https://www.ftc.gov/news-events/blogs/business-blog/2016/11/ransomware-closer-look.*

[49] "Buying or Selling Debts? Steps for Keeping Data Secure" (Apr. 2015), available at *https://www.ftc.gov/tips-advice/business-center/guidance/buying-or-selling-debts-steps-keeping-data-secure.*

[50] Informational Injury Workshop (Dec. 12, 2017), available at *https://www.ftc.gov/news-events/events-calendar/2017/12/informational-injury-workshop.*

[51] Press Release, "FTC Announces Hearings on Competition and Consumer Protection in the 21st Century" (June 20, 2018), available at *https://www.ftc.gov/news-events/press-releases/2018/06/ftc-announces-hearings-competition-consumer-protection-21st.*

RESPONSES TO WRITTEN QUESTIONS OF SENATOR SCOTT FROM MANEESHA MITHAL

Q.1. I greatly appreciated the FTC's guidance and technical assistance as I authored legislation, the Protecting Children From Identity Theft Act (S. 2498), to stamp out synthetic ID fraud. Your team has long been a leading voice on this issue. Thanks to Chairman Crapo, the legislation was included in the Economic Growth, Regulatory Relief, and Consumer Protection Act (Section 215 of S. 2155) and enacted into law this May.

Please answer the following with specificity:

For the benefit of this Committee, could you explain what synthetic ID fraud is and who predominantly falls victim to this crime?

A.1. Synthetic identify theft is a technique used by some identity thieves in which they apply for credit using a mixture of real, verifiable information of an existing person with fictitious information, thus creating a "synthetic" identity. Often these identity thieves use real Social Security numbers (SSNs) of people they know are unlikely to have existing credit files, such as children or recent immigrants. Using a consumer's SSN to apply for loans, utility accounts, property accounts, driver's licenses, and vehicle registrations can have long-term consequences that can leave victims burdened with unauthorized debt and a flawed credit history. This type of identity theft has been on the rise in recent years and was a topic of discussion at the Federal Trade Commission's 2017 Identity Theft conference.

Q.2. How exactly will the Protecting Children From Identity Theft Act cut down on synthetic ID fraud?

A.2. Synthetic identity theft often happens because there is no convenient mechanism to ensure that an SSN matches with other information provided by an applicant for credit or other services. Currently, the SSA's Consent-Based Social Security Number Verification system—while created to fight synthetic identity theft and other fraud—requires financial institutions to obtain a physical written signature from a consumer before making a request to verify an SSN with the SSA. This requirement has been time consuming and has undermined the effectiveness of the verification system. In an era where many consumers expect instant access to credit, financial institutions will be more likely to take verification measures when the process is quick and efficient.

The Protecting Children From Identity Theft Act, which was incorporated into Section 215 of the Economic Growth, Regulatory Relief, and Consumer Protection Act, allows certain financial institutions, including credit reporting agencies (CRAs), to receive customers' consent by electronic signature to verify their name, date of birth, and Social Security number with the Social Security Administration (SSA). It also directs SSA to modify their databases to allow for the financial institutions, including CRAs, to electronically and quickly request and receive accurate verification of consumer data. These measures will result in a quicker and more efficient verification process that will help reduce synthetic identity fraud.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

STATEMENTS AND LETTERS SUBMITTED BY CHAIRMAN CRAPO

July 12, 2018

Senator Mike Crapo, Chairman
Senator Sherrod Brown, Ranking Member
Senate Committee on Banking, Housing & Urban Affairs
U.S. Senate
Washington, DC 20510

Re: S. 2362, the Control Your Personal Credit Information Act of 2018

Dear Senator Crapo and Senator Brown:

The undersigned consumer groups write in support of S. 2362, the Control Your Personal Credit Information Act of 2018. S. 2362 would amend the Fair Credit Reporting Act to give consumers, not credit bureaus or banks, the ultimate decisionmaking power over our credit reports. It addresses a paradox repeatedly pointed out in the aftermath of the Equifax data breach – that the credit bureaus hold vast amounts of sensitive information about hundreds of millions of American consumers, which they sell for hefty profits, yet we have very little control over how this information is used or disseminated. S. 2362 provides this control to consumers.

S. 2362 requires that credit bureaus first obtain the consumers' permission in order to release their credit reports and scores to lenders, insurers, and others. Requiring permission to access credit reports is neither new nor overly burdensome. For decades, the FCRA has required employers to obtain consumers' permission to use credit and consumer reports for employment purposes. The State of Vermont requires lenders to obtain consumers' permission to access reports, and credit appears not to have been hampered in that state.

As an additional measure to prevent identity theft, S.2362 requires the common-sense step of requiring consumers to provide proof of identity to the credit bureau when granting permission to access a credit report or score, using the standard in Section 610(a) of the FCRA, 15 U.S.C. § 1681h(a). This is the same section of the FCRA that establishes the proof of identity requirements when consumers order their own credit reports, such as through www.annualcreditreport.com, and the same type of proof would be required. Given that consumers must provide proof of identity to obtain their own credit report, it is illogical and unreasonable for the CRAs to argue that it is too burdensome to require this same documentation to prove their identity when credit or insurance is being sought. The goal is the same – to protect the security of the consumer's credit report information and prevent identity theft.

As for claims that this would make unavailable web-enabled credit and insurance applications, that is simply not true. Authentication can all be done online, the same way consumers can order their credit report online through www.annualcreditreport.com. If it's good enough for consumers ordering their own reports, it's good enough for them in order to prevent identity theft when applying for credit or insurance online. As for instant retail credit and auto financing, these are in-person transactions where identity validation could be conducted using actual identity documents, such as a driver's license. Finally, we expect that the credit bureaus would

develop new authentication measures to make the process more seamless, just as they have developed credit "locks" as a new measure.

As for the proposed revision to FCRA Section 604(c)(3), this is also intended to give consumers more control over their own information. Currently, the ability of lenders and insurers to use credit reports for marketing "firm offers" of credit - which are not very firm at all, being little more than advertising – has resulted in huge amounts of unwanted junk mail generated using personal private information. Switching from an opt-out to an opt-in system with affirmative written consent doesn't limit options; it gives consumers the right and ability to decide whether to accept use of their credit reports and scores for marketing.

Thank you for your attention. If you have any questions about this letter, please contact Chi Chi Wu (cwu@nclc.org or 617-542-8010).

Sincerely,

Americans for Financial Reform
Consumer Action
Consumer Federation of America
Consumers Union
National Association of Consumer Advocates
National Consumer Law Center (on behalf of it low-income clients)
Public Citizen
U.S. PIRG

cc: Senator Jack Reed

July 12, 2018

The Honorable Mike Crapo, Chairman
Banking, Housing & Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20515

The Honorable Sherrod Brown, Ranking Member
Banking, Housing & Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20515

Dear Chairman Crapo and Ranking Member Brown:

The National Multifamily Housing Council (NMHC) and National Apartment Association (NAA) applaud the Committee for calling a hearing entitled "An Overview of the Credit Bureaus and the Fair Credit Reporting Act." As an industry that relies heavily on accurate consumer and credit reporting, we appreciate the Committee exploring these issues.

For more than 20 years, the National Multifamily Housing Council (NMHC) and the National Apartment Association (NAA) have partnered on behalf of America's apartment industry. Drawing on the knowledge and policy expertise of staff in Washington, D.C., as well as the advocacy power of more than 160 NAA state and local affiliated associations, NAA and NMHC provide a single voice for developers, owners and operators of multifamily rental housing. One-third of all Americans rent their housing, and 39 million of them live in an apartment home.

There has been a fundamental change in our nation's housing dynamics as changing demographics and lifestyle preferences have driven more people away from the typical suburban house and towards the convenience of renting. Fueled by a growing population, demand for rental housing by younger Americans, immigration trends, and Baby Boomers and other empty nesters trading in single-family houses for apartments, apartment renter demand keeps growing: 2017 saw the biggest pickup in apartment renting since 2000.

Apartment owners and operators have long called for policymakers and the consumer reporting industry, together, to better enable our nation's renters the ability to build a financial profile that allows them to attain the many benefits that come with it. Historically, credit reporting agencies have not captured a complete picture of the financial performance of renters. Existing credit scoring models that drive approvals, interest rates and other terms of apartment leases, car loans, insurance products, home mortgages and other financial products often do not accurately reflect the creditworthiness of renters. Apartment living now attracts a wide variety of Americans and will continue to do so making it all the more important that credit reports and scoring models are modernized and adopted so as not to prevent our nations renters from being put at a financial disadvantage.

In fact, in a study released in 2015 by the Consumer Financial Protection Bureau, over 45 million consumers were either credit invisible or were unscorable by existing credit models.[1] This disparity has drawn the attention of the financial industry and regulators who began to seek ways

[1] Data Point: Credit Invisibles, The CFPB Office of Research, May 2015, page 6

to incorporate more financial data into credit decisions. As an example, as part of the 2015 and 2016 Enterprise Scorecards the Federal Housing Finance Administration (FHFA) has directed Fannie Mae and Freddie Mac to begin looking for ways to evaluate and underwrite a mortgage when a borrower does not have a credit score. In another example from 2013, Experian created Rent Bureau, a credit reporting system targeted to the multifamily industry whereby apartment owners can voluntarily report rental payment information for its residents and allow a more complete financial profile to be built.

Today more credit reporting agencies and central data aggregators are collecting alternative data such as rental payments, medical payments, utility payments and other payment records. The credit reporting industry has migrated towards collecting the required information to create a deeper financial picture of the broader population. The limitation that remains today is that the most widely used credit scoring model- FICO Classic - does not incorporate this additionally reported data. Credit scoring models are evolving to include this new data as well as to update their existing algorithms for evaluating credit decisions. NMHC/NAA applaud this movement as it will improve and inform credit decisions regarding renters who may have been credit invisible, unscorable or whose payments may not have been recognized previously in existing credit scoring models.

NMHC/NAA urge policymakers to recognize the many benefits of alternative credit scoring models that incorporate a broader and more complete financial picture of renters. Again, we thank you for holding this important hearing and for the opportunity to present the views of the multifamily industry.

Sincerely,

Douglas M. Bibby
President
National Multifamily Housing Council

Robert Pinnegar, CAE
President & CEO
National Apartment Association

July 12, 2018

The Honorable Mike Crapo, Chairman
Banking, Housing & Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20515

The Honorable Sherrod Brown, Ranking Member
Banking, Housing & Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20515

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There has been a fundamental change in our nation's housing dynamics as changing demographics and lifestyle preferences have driven more people away from the typical suburban house and towards the convenience of renting. Fueled by a growing population, demand for rental housing by younger Americans, immigration trends, and Baby Boomers and other empty nesters trading in single-family houses for apartments, apartment renter demand keeps growing: 2017 saw the biggest pickup in apartment renting since 2000.

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to incorporate more financial data into credit decisions. As an example, as part of the 2015 and 2016 Enterprise Scorecards the Federal Housing Finance Administration (FHFA) has directed Fannie Mae and Freddie Mac to begin looking for ways to evaluate and underwrite a mortgage when a borrower does not have a credit score. In another example from 2013, Experian created Rent Bureau, a credit reporting system targeted to the multifamily industry whereby apartment owners can voluntarily report rental payment information for its residents and allow a more complete financial profile to be built.

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NMHC/NAA urge policymakers to recognize the many benefits of alternative credit scoring models that incorporate a broader and more complete financial picture of renters. Again, we thank you for holding this important hearing and for the opportunity to present the views of the multifamily industry.

Sincerely,

Douglas M. Bibby
President
National Multifamily Housing Council

Robert Pinnegar, CAE
President & CEO
National Apartment Association

STATEMENT FOR THE RECORD

FROM THE

CONFERENCE OF STATE BANK SUPERVISORS

TO THE

SENATE BANKING, HOUSING AND URBAN AFFAIRS'

HEARING ON

"OVERVIEW OF THE CREDIT BUREAUS AND THE FAIR CREDIT REPORTING ACT"

JULY 12, 2018

Conference of State Bank Supervisors (CSBS) is the nationwide organization of banking and financial regulators from all 50 states, American Samoa, the District of Columbia, Guam, Puerto Rico, and the U.S. Virgin Islands. The mission of CSBS is to support the leadership role of state banking supervisors in advancing the state banking system; ensuring safety and soundness; promoting economic growth and consumer protection; and fostering innovative state regulation of the financial services industry.

State regulators charter and supervise 79 percent of all banks in the United States. In addition, state regulators license and supervise a variety of non-bank financial services providers, including fintech, mortgage lending, money transmission, and consumer finance. CSBS, on behalf of state regulators, also operates the Nationwide Multistate Licensing System (NMLS) to license and register those engaged in mortgage, money transmission, and other non-bank financial services industries.

CSBS appreciates the opportunity to submit this statement for the record on recent efforts by state regulators related to credit bureaus. The recent special multi-state examination demonstrates the responsiveness of the state financial regulatory system working together to protect confidential personal information.

Consent Order with Equifax

On June 25, 2018, state financial regulatory agencies entered into a Consent Order with Equifax Inc., requiring the company to take specific action to protect confidential consumer information in the wake of an extensive security breach last year. Equifax, one of the country's three major credit reporting agencies, disclosed in September 2017, that a vulnerability in one of its websites was exploited by criminal hackers in May 2017 to gain access to the personal information of an

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estimated 146 million U.S. consumers. Data accessed through this cybercrime event included individual customer names, Social Security numbers, birth dates, addresses, and related personally identifiable information.

In response to this breach, an examination team composed of state financial regulators from Alabama, California, Georgia, Maine, Massachusetts, New York, North Carolina, and Texas initiated a multi-state examination of the company in November 2017 to evaluate the company's information security and cybersecurity controls. The states' examination evaluated the company's cybersecurity, internal audit, risk management and controls.

In the Consent Order, Equifax agreed to improve how it protects personally identifiable information. The company will undertake a restructuring of its risk management processes, strengthening of internal controls and processes, and enhanced oversight by the Board of Directors on the information security program. The corrective actions will apply to Equifax's operations nationwide. Compliance with the consent order will be subject to regulator approval and follow-up reports are required from the company. Additionally, the consent order preserves the right of individual states to bring additional actions.

The order requires the Equifax Board and/or Management to:

- Review and approve a written information security risk assessment.
- Improve the oversight of their audit function by establishing a formal and documented internal audit program that effectively evaluates IT controls.
- Approve a consolidated written Information Security Program and review and an annual report on the adequacy of that program.
- The Board must enhance its oversight of the company's information security program.
- Improve oversight of critical vendors consistent with the guidance from the Federal Financial Institutions Examination Council's (FFIEC) "Outsourcing Technology Services IT Examination Handbook" and in the "Payment Card Industry Data Security Standards."
- Improve standards and controls for supporting the patch management function and implement an effective patch management program to reduce the number of unpatched systems and instances of extended patching time frames.
- Enhance oversight of disaster recovery and business continuity.
- Submit a list of all remediation projects planned or in process in response to the 2017 breach to the Multi-state Regulatory Agencies.
- Require an independent third party to validate all such remediation projects and provide notice to the Multi-state Regulatory Agencies.
- Provide progress reports on a quarterly basis to the Multi-state Regulatory Agencies.

As part of required ongoing supervision, the company is required to file written reports with state bank regulators detailing progress with the various provisions of the order on a quarterly basis, and quarterly written progress report submissions will continue until the regulators release the provision.

Amendment to Bank Service Company Act

Moving forward, CSBS encourages enactment of H.R 3626, the Bank Service Company Examination Coordination Act. This legislation will enhance state and federal regulators' ability to coordinate examinations of and share information on banks' technology vendors in an effective and efficient manner. Banks partner with third-party technology service providers (TSPs) to outsource a wide variety of critical banking services. The Bank Service Company Act (BSCA) authorizes federal regulators to examine TSPs to assess the potential risks they pose to individual client banks and the broader banking system. Currently, 38 states have similar authority under state law. The BSCA is silent regarding authorities and/or roles of state banking regulators, limiting the ability of federal and state regulators to share information on TSPs. Amending the BSCA to appropriately reflect states' authority to examine TSPs will improve state-federal coordination and information sharing and promote more efficient supervision of TSPs that provide critical services to a broad range of banks.

We look forward to working to with the Committee on these issues, another other issues vital to the financial services industry.

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REPORTS AND LETTERS SUBMITTED BY SENATOR SCOTT

9 July 2018

The Honorable Mike Crapo
Chairman
Committee on Banking, Housing
& Urban Affairs
U.S. Senate
Washington, DC 20510

The Honorable Sherrod Brown
Ranking Member
Committee on Banking, Housing
& Urban Affairs
U.S. Senate
Washington, DC 20510

Re: S. 3040, the Credit Access and Inclusion Act

Dear Chairman Crapo and Ranking Member Brown:

On behalf of the nearly 50 million Credit Invisible Americans—largely comprised of Millennials, elderly Americans, lower income earners, members of minority communities, and legal immigrants—we write to thank you for your continued leadership on the problem of Credit Invisibility. Those without a credit history, or for whom no score can be generated owing to a lack of sufficient predictive data, face daunting challenges when trying to secure affordable sources of mainstream credit.

Mainstream lenders, unable to assess an applicant's risk, automatically reject Credit Invisibles, forcing them to have their real credit needs met by high-priced alternative financial services providers (AFSPs). Many among the 50 million are never able to break out from the "Credit Catch 22," that in order to qualify for credit you have to already have credit. Consequently, the dream of homeownership or owning a small business remains just that—a dream and not a reality.

Worse still, non-financial service creditors are able and do today report late payment data—defaults, charge offs, delinquencies, and collections—to nationwide consumer reporting agencies, directly or indirectly through collection agencies. What's missing is timely payment data—the overwhelming majority of total payment data. As a result, people are being punished for their credit transgressions, but not receiving any benefit for their good credit behavior.

The Credit Access and Inclusion Act recognizes the seriousness of the problem of Credit Invisibility, and seeks to rectify the terrible economic injustice from reporting negative data but not positive data. By clarifying that the Fair Credit Reporting Act permits non-financial service creditors—energy utilities, telecommunications and media firms, landlords and property management firms—to fully report customer payment data to nationwide consumer reporting agencies, including positive payment data, a significant first step is being taken to end this problem for the 50 million Credit Invisibles.

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RESULTS AND SOLUTIONS

There are abundant reasons why we support this bill, and why we urge all members of Congress to get behind this important piece of legislation. Key reasons include:

- The solution—clarifying that non-financial payment data is already permitted under the Fair Credit Reporting Act and thereby eliminating evident regulatory uncertainty—is a pen-stroke solution that will cost the American taxpayer exactly nothing to implement;
- The solution is supported by over a decade of empirical research on millions of Americans lucky enough to have had this data fully reported at one or more nationwide consumer reporting agencies. For any given default rate, more credit is extended—resulting in sustained economic growth and job creation.
- The largest net beneficiaries from the solution included in S. 3040 are the Credit Invisibles, who are overwhelmingly comprised of lower income Americans (as many as 40% of whom would qualify for some form of prime credit), members of minority communities (African Americans and Hispanics experience a 21% and 22% increase in access to mainstream credit), Millennials and the above 66 populations (14% increase in mainstream credit access), and lower income persons (24% for those earning less than $20,000 and 15% for those earning $20,000 to $29,999 annually).

This solution has been used in more than 90 countries as diverse as Britain, China, Colombia, Germany, and New Zealand. In some cases, non-financial payment data has been used in credit reports for more than a half-century to great success. In fact, the World Bank even endorses the inclusion of fully-reported non-financial payment data in their *General Principles for Credit Reporting*.[1]

In summary, S. 3040 offers consumers a powerful tool to build and/or rebuild their good credit history, enabling dramatically improved access to affordable sources of mainstream credit. This will empower individuals with the necessary resources to build assets and generate wealth by owning a home or a small business. The scourge of Credit Invisibility will be nearly eliminated, and tens of millions of deserving and hard working Americans will finally escape the "Credit Catch 22."

There is a research consensus around this solution.[2] Now is not the time to further study the transformative power of alternative data on Credit Invisibility. Instead, Congress must act forcefully and authoritatively in support of S. 3040.

Sincerely,

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[1] Available for download at http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/Credit_Reporting_text.pdf

[2] See http://www.perc.net/wp-content/uploads/2015/03/ResearchConsensus.pdf

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RESULTS AND SOLUTIONS

Michael A. Turner, Ph.D.
President and CEO

ORGANIZATIONS SUPPORTING USE OF ALTERNATIVE DATA IN CREDIT REPORTS

180 Degrees, Minneapolis, Minnesota
Asian Economic Development Association, Minnesota
Association for Enterprise Opportunity
The Abilities Fund, Florida
Ashoka: Innovators for the Public, Washington DC
Asset Builders of America, Inc., Wisconsin
Asset Building Policy Project (The Michigan Asset Building Coalition), Michigan
BMO Harris Bank, Illinois
Bread for the World, Washington DC
Community and Shelter Assistance Corp (CASA) of Oregon, Oregon
Capital Area Asset Builders, Washington DC
Center for Financial Services Innovation (CFSI), Illinois
Collaborative Support/Community Enterprises, New Jersey
Colorado Community Action Association, Colorado
Community Economic Development Association of Michigan (CEDAM), Michigan
Community Financial Resources, California
Connecticut Voices for Children, Connecticut
Council on Crime and Justice, Minneapolis, Minnesota
Credit Builders Alliance, Washington DC
CRIF Lending Solutions, Atlanta, Georgia
Doorways to Dreams (D2D) Fund, Massachusetts
Dun & Bradstreet Pty Ltd., New Jesey
EARN, California
ECDC, Virginia
Experian, California
Financial Services Innovation Coalition Consortium, Washington, D.C.
Financial Services Roundtable, Washington DC
The Family Conservancy, Kansas
Good Work Network, Louisiana

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RESULTS AND SOLUTIONS

Heartland Alliance for Human Needs & Human Rights, Illinois
Hope Communities, Inc., Colorado
IDA and Asset Building Collaborative of NC, North Carolina
Insight Center for Community Economic Development, California
Jewish Community Action, Minnesota
Kansas Action for Children, Kansas
Minnesota Credit Union Association
Michigan IDA Partnership / OLHSA, Michigan
Micro Mite, Florida
Mission Asset Fund, California
The Midas Collaborative, Massachusetts
National Association of Home Builders, Washington DC
National Association of Realtors, Washington DC
National Black Caucus of State Legislators
National Coalition for Asian Pacific American Community Development
National Consumer Reporting Association, Illinois
Neighborhood Partnerships, Oregon
Asset Building Program of the New America Foundation, Washington DC
NewWell Fund, Virginia
Okanogan County Community Action Council, Washington
OnTrack Financial Education & Counseling, North Carolina
Opportunity Finance Network, Pennsylvania
Policy and Economic Research Council (PERC), North Carolina
PolicyLink, New York
Prosper, California
Prosperity Now, Washington DC
RAISE Kentucky, Kentucky
RAISE Texas, Texas
RentBureau, Georgia
Rural Dynamics Inc., Montana
Sunrise Banks, Minnesota
SVT Group, California
TransUnion LLC, Illinois
United Way of Forsyth County, North Carolina
U.S. Bancorp, Minnesota
Washington Asset Building Coalition
The Women's Center, Washington DC

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Five Ways Alternative Data Can Expand Credit Access

By Rep. Keith Ellison (D-MN)

Millions of Americans lack credit scores or have scores that are too low to gain access to affordable credit. This problem disproportionately affects young people, African-Americans, Latinos and immigrants, many of whom can't establish a credit score without taking on debt. Congress can help address this issue by providing companies with affirmative permission to thicken credit reports with predictive alternative data.

According to the Consumer Financial Protection Bureau, at least 45 million Americans cannot access affordable mainstream sources of credit because they either have no credit report or have insufficient credit histories to be scored. These Americans are known as "credit invisibles." They encounter difficulties when trying to rent an apartment or to take out a loan to obtain low-cost consumer credit.

But there is a solution. Many credit invisibles regularly make payments on their gas, water, electric, heating oil, cable TV, broadband, wireless cellphone bills and pay rent on their apartments or homes. These payments are recognized as credit and predictive of risk. However, this payment information is typically reported to a credit bureau when the customer is in collection, not when people pay their bills on time.

Reporting this alternative payment data would substantially reduce credit invisibility and enable an estimated 40% of credit invisibles to qualify for some variant of prime credit. According to research by the Policy and Economic Research Council and the Brookings Institution, using a sample of more than four million actual credit reports with fully reported nonfinancial payment data, simulations showed that the inclusion of the nonfinancial data would enable credit acceptance to increase 22% for Hispanics, 21% for African-Americans, 21% for the lowest income households, and 14% for people under 25 years old and those over 66.

While these increases seem large, one should consider that the CFPB has found that 28% of Hispanics and African-Americans and 45% of individuals in the lowest-income census tracts are unscoreable with traditional credit scores and data. Credit reports that take into account when people pay their bills on time help the Americans who need credit the most.

I am now championing legislation in Congress which would clarify that energy utility firms, telecommunications companies and property management firms and landlords can report on-time payment data to nationwide credit reporting agencies. While such reporting is not illegal, regulatory uncertainty has hindered its practice.

My bill, the Credit Access and Inclusion Act of 2015, enables the addition of positive payments. There is nothing in the bill that would require or incentivize utility companies to start reporting late payment differently.

A recent op-ed by Chi Chi Wu published in American Banker cautioned that there may be pitfalls to using alternative data to help credit invisibles. However, my proposal would greatly benefit underserved Americans. Here are five substantiated and incontrovertible facts about how alternative data can help promote access to credit.

Fact #1: The status quo harms credit invisibles. Credit invisibles currently have their credit needs met by pawnshops, payday lenders and check-cashing services. These Americans pay an estimated $4 billion per year in fees, further entrenching their financial difficulties.

Fact #2: Credit scoring has made lending fairer and more inclusive. Study after study shows that automated underwriting better predicts risk than manual underwriting, and is more inclusive for traditionally underserved populations.

Fact #3: Reporting bills paid on time makes the system more forgiving and more inclusive. The nature of the problem is not that credit reporting and credit scoring are inherently discriminatory and promote exclusion, but rather that our national credit bureaus only have information on people who are already banked. Therefore credit scores are limited as a tool for promoting financial inclusion. In short, the problem is one of data, not discrimination.

Fact #4: Having a low score is better than no score. If you are a credit invisible, you will almost always be denied access to affordable credit. In this context, having any score —even a low one —is superior to having none at all. The notion that having no score may somehow be helpful in finding an apartment or employment or getting a more affordable insurance rate is also highly contestable. When applying for insurance, an apartment and a job, a credit report is one piece of information considered among many others.

Fact #5: Predatory and subprime lenders already seek data on credit invisibles. It is mainstream lenders who tend to overlook this population for prime offers and in traditional underwriting. To create a two-tiered system in which alternative data is used only for the otherwise unscoreable, as suggested in Wu's op-ed, is a bad idea. One tier would be reserved for mainstream lenders offering competitive loans serviced by the main credit bureau databases. Another tier would be designated for higher-priced niche lenders that use special databases to market to the credit invisibles. Not only would this segregate society, it also would result in consumer confusion and erode important consumer rights and protections. Therefore we should strive to bring all consumers into the same mainstream lending system where possible.

For all of these reasons, it is important that Congress provide affirmative permission to add on-time utility and telecommunications payment data to credit reports and scores. This would open up credit, housing and employment opportunities for tens of millions of Americans and make our current credit system more inclusive and accurate.

Rep. Keith Ellison is a member of the House Financial Services Committee.

Data Point: Credit Invisibles

The CFPB Office of Research

cfpb Consumer Financial Protection Bureau

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This is another in an occasional series of publications from the Consumer Financial Protection Bureau's Office of Research. These publications are intended to further the Bureau's objective of providing an evidence-based perspective on consumer financial markets, consumer behavior, and regulations to inform the public discourse.

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1. Introduction

Consumers with limited credit histories reflected in the credit records maintained by the three nationwide credit reporting agencies (NCRAs) face significant challenges in accessing most credit markets.[1] NCRA records are often used by lenders when making credit decisions. In particular, lenders often use credit scores, such as one of the FICO or VantageScore scores, that are derived entirely from NCRA records when deciding whether to approve a loan application or in setting a loan's interest rate. If a consumer does not have a credit record with one of the NCRAs or if the record contains insufficient information to assess her creditworthiness, lenders are much less likely to extend credit. As a result, consumers with limited credit histories can face substantially reduced access to credit.

In broad terms, consumers with limited credit histories can be placed into two groups. The first group is comprised of consumers without NCRA credit records. We refer to this group as "credit invisibles." The second group includes consumers who, while they have NCRA credit records, have records that are considered "unscorable," meaning they contain insufficient credit histories to generate a credit score. Generally speaking, a credit record may be considered unscorable for two reasons: (1) it contains insufficient information to generate a score, meaning the record either has too few accounts or has accounts that are too new to contain sufficient payment history to calculate a reliable credit score; or (2) it has become "stale" in that it contains no recently reported activity. The exact definition of what constitutes "insufficient" or "stale" information differs across credit scoring models, as each model uses its own proprietary definition. Our analysis is based on a commercially-available credit scoring model that we believe uses a relatively narrow definition of a "scorable" credit record, but one that we believe is consistent with most credit scores used today. We refer to these records as "unscored" rather

[1] The three NCRAs are Equifax, Experian, and TransUnion.

than "unscorable" to reflect the fact that other credit scoring models might generate scores for these records. Nevertheless, we believe our estimates of the population with unscored credit records accurately reflect the circumstances faced by consumers with limited credit histories.

The challenges that credit invisibles and consumers with unscored records face in accessing credit markets has generated considerable attention from researchers and industry participants. Several studies have explored the potential of various types of "alternative data" to supplement the information contained in the NCRA credit records and allow credit scores to be generated for these consumers.[2] Stakeholders have debated the implications of doing so for those with limited credit history as well as those with scorable files whose credit profiles might change with the addition of such data. Several industry participants have also developed scoring products that are aimed specifically at these populations.[3]

Despite all of this attention, very little is known about the number or characteristics of credit invisibles or consumers with unscored credit records. This Data Point documents the results of a research project undertaken by Staff in the Office of Research of the Consumer Financial Protection Bureau (CFPB) to better understand how many consumers are either credit invisible or have unscored credit records and what the demographic characteristics of such consumers are.

This analysis was conducted using the CFPB's Consumer Credit Panel (CCP), a 1-in-48 longitudinal sample of de-identified credit records purchased from one of the NCRAs and representative of the population of consumers with credit records. This dataset contains information on almost 5 million consumer credit records. While these data contain no direct-identifying information (such as name, address, or Social Security Number), for each credit

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[2] For example, see Turner, *et al.* (2006), Experian (2014), and Schneider and Schutte (2007) for utility payments, Experian RentBureau (2014) for rental payments, and CFPB (2014) for remittances.

[3] For example, FICO recently announced that it is launching a pilot project that extends the number of consumers whose records can be scored using alternative data on utility and telecommunication bill payments and property record data (FICO, 2015). LexisNexis has also introduced a credit scoring model, RiskView, that uses alternative data to expand the number of credit records that can be scored (Feinstein, 2013). The new version of the VantageScore, version 3.0, uses alternative data when it is available on a credit record to expand the number of consumers whose records can be scored (VantageScore, 2013). For other examples, see Jacob and Schneider (2006).

record we observe the consumer's census tract, year of birth, and a commercially-available credit score.

We use these data from December 2010 to estimate the number of credit invisibles in each tract by taking the difference between the number of adults living in the tract according to the 2010 Decennial Census and the number of credit records in each tract, as estimated from the CCP. Since the 2010 Census publishes data on population by age, and since the CCP contains year of birth, we estimate the number of credit invisibles in each tract for each of thirteen different age groups. For each of these age groups, we also calculate the number of consumers with unscored credit records in each tract using the CCP. Then using variation across census tracts in the racial and ethnic composition of the population and their household incomes, which we take from the 2008-2012 American Community Survey, we estimate how the incidence of being credit invisible or having an unscored credit record differs across these demographic characteristics.

Key findings of this report include:

- As of 2010, 26 million consumers in the United States were credit invisible, representing about 11 percent of the adult population. An additional 19 million consumers, or 8.3 percent of the adult population, had credit records that were treated as unscorable by a commercially-available credit scoring model. These records were about evenly split between those that were unscored because of an insufficient credit history (9.9 million) and because of a lack of recent history (9.6 million).
- There is a strong relationship between income and having a scored credit record. Almost 30 percent of consumers in low-income neighborhoods are credit invisible and an additional 15 percent have unscored records. These percentages are notably lower in higher-income neighborhoods. For example, in upper-income neighborhoods, only 4 percent of adults are credit invisible and another 5 percent have unscored credit records.
- Blacks and Hispanics are more likely than Whites or Asians to be credit invisible or to have unscored credit records. About 15 percent of Blacks and Hispanics are credit invisible (compared to 9 percent of Whites and Asians) and an additional 13 percent of Blacks and 12 percent of Hispanics have unscored records (compared to 7 percent of Whites). These differences are observed across all age groups, suggesting that these differences materialize early in the adult lives of these consumers and persist thereafter.

2. Data

2.1 Data Sources

The data used in this study come from three sources. The first is the CFPB's Consumer Credit Panel (CCP), a longitudinal sample of approximately 5 million de-identified credit records that is nationally representative of the credit records maintained by one of the NCRAs. This study primarily uses data from December 2010; however, as described below, we also use information for these same consumers from December 2014 in cleaning the data.

For each time period, the entire credit record is supplied in the CCP, excluding any direct-identifying personal information (such as name, address, or Social Security Number). In addition to the credit records, the CCP includes a commercially-available credit score, which we use to indicate which records were scored and which were not. For each unscored record, an "exclusion code" is provided indicating why the record could not be scored using the model for the commercially-available credit score.

Like most credit scoring models, the model that generated the scores in the CCP was built to predict future credit performance (that is, the likelihood, relative to other borrowers, that a consumer will become 90 or more days past due on a credit obligation in the following two years).[4] In some cases, the model builders will determine that a credit record does not contain enough information to make a suitably reliable prediction. During score development, these records are excluded and are unscored by the model going forward.

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[4] This is a generic definition of "credit performance" used in credit scoring models. The exact definition used will vary from one credit scoring model to another. For more information on measures of performance in credit scoring models, see Board of Governors of the Federal Reserve System (2007).

There are two types of unscored records in the CCP.[5] The first, "insufficient unscored" records, do not contain enough information to generate the score, meaning either that the record contained too few reported accounts or accounts that did not have a sufficiently long credit history. The second type, "stale unscored" records, do not contain any recently reported information. Our analysis examines these two types of unscored credit records separately.

When available, a year of birth is included in the CCP for each record.[6] We use this information to calculate the age of each consumer at the end of 2010. This allows us to examine how the incidence of being credit invisible or having an unscored credit record varies with age. Though credit records in the CCP do not include address information, each consumer's census tract using 2010 census definitions is provided. This allows us to measure how credit records are distributed across the country.

The second source of data used in this study is the 2010 Decennial Census, conducted by the U.S. Census Bureau. The Decennial Census indicates the number of consumers in each census tract. It also provides information on the racial and ethnic mix of each tract. In our analysis, we focus on four different racial or ethnic groups: Hispanics or Latinos ("Hispanics"), Non-Hispanic Asians ("Asians"), Non-Hispanic Blacks or African Americans ("Blacks"), and non-Hispanic Whites ("Whites"). All other non-Hispanic racial groups, which include American Indians or Alaska Natives, Native Hawaiians or Other Pacific Islanders, or multi-racial individuals, are included in a category labelled "Other."

The third source of data comes from the 2008-2012 American Community Survey (ACS), which is also conducted by the U.S. Census Bureau. Among other information, the ACS includes the median household income in each tract, county, and Metropolitan Statistical Area (MSA). We use this information to calculate the "relative income" of each tract. Relative income is defined as the ratio between the median household income of the tract and the median household income of the surrounding area, which is the MSA for urban tracts or the county for rural tracts. Following the definitions used in the Community Reinvestment Act, we then characterize each

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[5] Credit records in the CCP will also be unscored if the record belongs to a deceased consumer. Our analysis focuses on living consumers whose records will only be unscored for these two reasons.

[6] Though credit records also contain the month and day of birth for consumers, the CCP does not include this information to help maintain the privacy of the consumers in our sample.

tract as low, moderate, middle, or upper income, depending on whether the tract's relative income is below 50 percent, between 50 and 80 percent, between 80 and 120 percent, or above 120 percent.

2.2 Dataset Creation

Estimating the number of credit invisibles is complicated by the fact that almost no data exists specifically for this population. Some datasets that collect data on a representative sample of the entire population, like the Survey of Consumer Finances or the ACS, certainly include information on credit invisibles, but do not collect information that allows one to determine which sample observations are credit invisible. Datasets like the CCP generally have good information about consumers with credit records but by definition cannot include consumers without credit records.

Our approach is to estimate the number of credit invisibles by comparing the adult population in the U.S. from the 2010 Decennial Census with an estimate of the number of adults who have a credit record at the NCRAs. While this may seem straightforward, it is actually a complex undertaking. The reason is that many consumers have multiple credit records within the data of the NCRAs. As a result, comparing the number of credit records maintained by the NCRAs with the U.S. population would be misleading. For example, the CCP in 2010 contained 4.91 million credit records. Given the 1-in-48 sampling rate used by the CCP, this implies that there were about 236 million credit records at the NCRA, more than the 235 million adults in the U.S. according to the Census. By itself, this would suggest that there are no consumers without credit records.

The reason that some consumers have multiple credit records is the existence of "fragment files." These are credit records containing a portion of a consumer's credit history that exist outside of the consumer's primary file. Take for example a consumer with a credit record who opens a new credit card. When the lender or servicer first reports the account, the NCRA attempts to match it with the correct credit record using a proprietary algorithm. If, based on that algorithm, the NCRA is unable to find any credit records that match, or is unable to find a unique match, perhaps reflecting erroneous or incomplete information reported with the new account, then the newly reported credit card will be placed in its own credit record. Most of these fragment files are temporary. Over time, as more information comes in, the NCRA may determine that the credit record is a fragment and that the accounts in the record belong to a

consumer with an existing credit record. When this happens, the information in the fragment file gets subsumed in the consumer's primary credit record and the fragment file ceases to exist.

Fragment files present an interesting challenge for estimating the number of consumers who have credit records at the NCRAs. An accurate measurement requires pruning from the data those records that are likely to be fragment files; otherwise, we will overestimate the number of consumers with a credit record and underestimate the number of credit invisibles. For example, as discussed above, without any pruning the CCP (or other data based on credit records) would imply that all Americans have credit records or, possibly, that there are more records than people.

Our process of cleaning the data involves the following exclusions. First, since we are comparing credit records to the U.S. population, we exclude credit records that indicate the consumer was living outside of the fifty states. Second, we exclude the credit records of consumers who appear to be deceased in December 2010.

We then use hindsight to identify fragment files. We discard any credit record from December 2010 that does not appear in the December 2014 data as well, suggesting that the record had been purged from the database or merged into another record during this time. Finally, we exclude any credit record that had no reported year of birth in either December 2010 or December 2014. Birth dates tend to be an important characteristic in matching accounts to credit records. Accounts that lack this information are less likely to be (uniquely) matched to an existing credit record and are more likely to be placed into a fragment file. Any CCP record that was missing year-of-birth information for four years should also have been missing date-of-birth information in the records maintained by the NCRA over this period, which suggests that these records are fragments containing accounts that could not be linked.[7] We discuss these exclusions in more detail in Appendix A.

Once we have removed the likely fragment files, we estimate the number of credit invisibles in each tract as the difference between the tract's adult population according to the 2010 Decennial

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[7] This is further supported by the prevalence of authorized user accounts in these files. Authorized users are people who are permitted to use a revolving account, like a credit card, without being legally liable for any of the charges that are incurred. Lenders generally do not require a lot of detail on these consumers and, based on our conversations with industry participants, their accounts often end up in fragment files as a result. For more information on authorized user accounts and the issues involved, see Brevoort, Avery, and Canner (2012).

Census and our estimate of the number of consumers in the tract who have a credit record. Since the 2010 Decennial Census provides tract-level information on population by age, we are able to calculate the number of credit invisibles for each of thirteen different age groups: Eleven age groups are defined using five-year spans of ages from 20 through 74 (i.e, 20 to 24, 25 to 29) and the remaining two contain 18-to-19 year olds and those 75 or older. We also estimate the number of consumers with insufficient-unscored and stale-unscored credit records from the CCP for each tract at each of the 13 age groups.

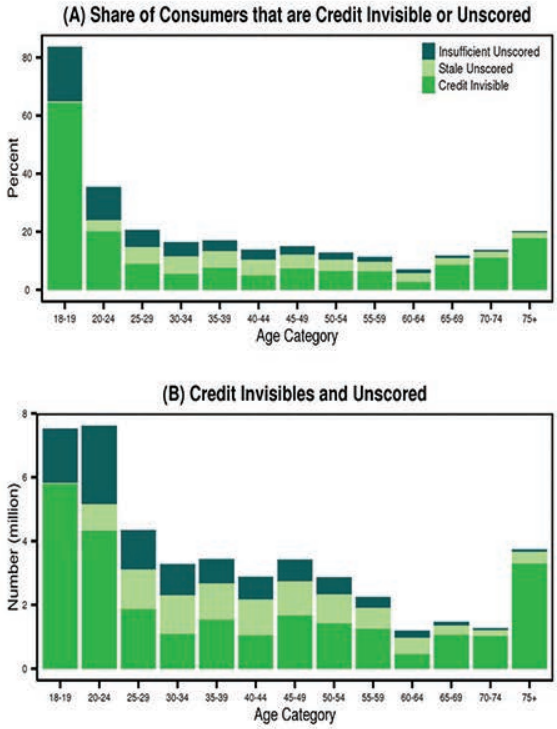
These estimates of the number of credit invisibles and consumers with unscored credit records depend crucially on the exclusions described earlier in this section. To the extent that some of the excluded credit records may have been the primary records of consumers, our estimates of the number of credit invisibles will be overstated and the number of consumers with a credit record (scored or unscored) will be understated. In contrast, if we have failed to exclude some credit records that are fragment files, then our estimates will tend to understate the number of credit invisibles and potentially overstate the number of consumers with credit records. One exclusion that we considered imposing, but decided against, was removing consumers whose only item on their credit record was a third-party debt collection or public record (such as a tax lien). While some of these are likely fragment files, our analysis suggested that removing these would likely exclude too many primary files. As a result, we believe that our estimate of the number of credit invisibles is likely low and our estimate of the number of consumers with unscored credit records likely overstated slightly since debt-collection-only or public-record-only credit records tend to be unscored. We provide additional detail on the consequences of each of these exclusions for our estimates of the number of credit invisibles and consumers with unscored records in Appendix A.

3. How Many Americans Have Limited Credit Histories?

Our estimates suggest that approximately 188.6 million Americans have credit records at one of the NCRAs that can be scored by the commercially-available model that informs our analysis. This represents over 80 percent of the adult population. An additional 19.4 million Americans, representing 8.3 percent of the adult population, have credit records that cannot be scored. These are almost evenly split between consumers with credit records that are insufficient unscored (9.9 million) and those that are stale unscored (9.6 million). The remaining 11 percent of adults, or about 26 million Americans, are credit invisible.

Credit history is something that consumers establish over the course of a lifetime. As a result, one would expect the problem of limited credit history to be more concentrated among the young. This pattern is observed in the data. Panel (A) of figure 1 shows the share of consumers in each age group that are credit invisible, have unscored records because of insufficient information, or have unscored records because of a lack of recently reported information. As shown, over 80 percent of 18 or 19 year olds are credit invisible or have unscored records. This percentage drops substantially for older consumers, falling below 40 percent in total for the 20 to 24 year old age group. After age 60, the number of consumers that are credit invisible or that have an unscored record increases with age. With our existing data, it is difficult to determine to what extent this reflects an age effect (a greater tendency of credit histories to shrink or become stale with age), a cohort effect (in which people born earlier than 1950 had thinner credit histories over the course of their lives, possibly reflecting less credit reporting during the periods of their lives when they were actively using credit), or some combination.

FIGURE 1: INCIDENCE AND NUMBER OF CONSUMERS THAT ARE CREDIT INVISIBLE OR HAVE RECORDS THAT ARE UNSCORED



The data shown in panel (A) also indicate that the causes of an unscored credit record differ substantially by age. The share of consumers with an unscored credit record because of an insufficient credit history declines with age. Only a small percentage of consumers aged 65 or older have records that are unscored because of an insufficient history; instead, most of the unscored records for these older consumers are the result of a lack of recent information. Interestingly, having a stale-unscored credit record is not strongly related to age. In fact, the

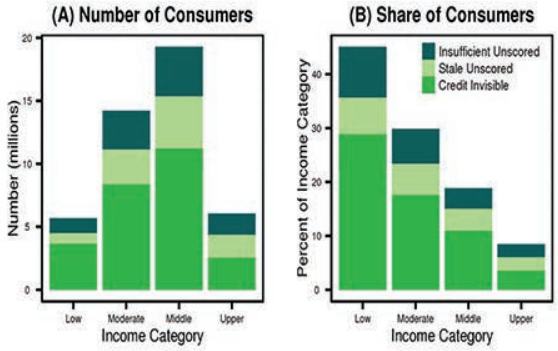
incidence of a stale unscored record is higher for consumers aged 25 to 49 than it is for consumers older than 50.

As this suggests, most consumers that are credit invisible or that have an unscored credit record are young. Panel (B) of figure 1 shows the distribution of the number of consumers who are credit invisible or have unscored records. Over 10 million of the estimated 26 million credit invisibles are younger than 25. Consumers in this age group also account for a disproportionate share of insufficient-unscored credit records. In contrast, most consumers with stale-unscored records are middle aged. Consumers aged between 25 and 50 account for over half of stale-unscored credit records.

Other characteristics besides age may also affect the likelihood of being credit invisible or having an unscored credit record. Among these is income. If higher-income consumers have an easier time qualifying for traditional credit, even without credit histories, then they may be more likely than lower-income consumers to open credit cards, auto loans, or other forms of credit that are frequently reported to the NCRAs. Relatedly, if lower-income consumers have a more difficult time qualifying for traditional credit and, as a result, rely on non-traditional sources like payday or auto-title lenders, then this will exacerbate the differences by income as these non-traditional sources of credit generally do not report information to the NCRAs.

Exploring the relationship between income and the incidence of being credit invisible or having an unscored record is complicated by the fact that credit records do not contain income information. As a result, we do not know the income levels of the consumers whose credit records are in the CCP and, thus, rely on the relative income of each census tract as an alternative measure. Panel (A) of figure 2 shows the number of consumers that are credit invisible or have an unscored credit record who live in census tracts with each of the four relative income levels: low, moderate, middle, or upper. As shown, middle-income tracts account for a larger portion of the credit invisible and unscored population than any of the three other income groups. Consumers from low- and upper-income neighborhoods, in particular, make up a notably smaller share of the credit invisible and unscored population.

FIGURE 2: NUMBER AND INCIDENCE OF CONSUMERS THAT ARE CREDIT INVISIBILE OR HAVE AN UNSCORED CREDIT RECORD BY CENSUS TRACT INCOME LEVEL



By and large, these numbers reflect varying population sizes in each income category. There are many more consumers in middle-income tracts than in low-income tracts, so it is not surprising that so many of these invisible and unscored consumers come from middle-income tracts. Instead, if we look at the share of consumers who are credit invisible or have an unscored credit record at each of these income levels, shown in panel (B), we see a very different pattern. Almost 50 percent of consumers in low-income tracts appear to either lack a credit record entirely or have an unscored credit record (mostly because of an insufficient credit history). At higher-income levels, this incidence falls sharply. In comparison, fewer than 10 percent of consumers in upper-income tracts are credit invisible or have unscored records. So while low-income tracts appear to comprise a relatively small share of the credit invisible or unscored population (about 5 million of the total 45 million consumers), this represents a significant share of the population in those tracts.

4. Patterns of Limited Credit History by Race and Ethnicity

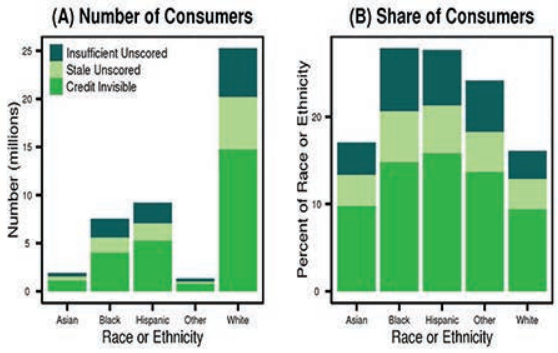
4.1 Patterns by Race or Ethnicity

Another characteristic that has been mentioned in connection with consumers that are credit invisible or have unscored credit records is race or ethnicity. As with income, credit records do not contain any information about the race or ethnicity of the consumer. As a result, we do not observe this information for the consumers whose credit records are in the CCP and, unlike income, we cannot easily segment census tracts into different racial or ethnic groups. This analysis, therefore, requires a different approach than we used in the previous section.

To explore how the incidence of being credit invisible or having an unscored record varies with race or ethnicity, we examine cross-tract variation in the racial composition of census tracts and in the number of consumers who are credit invisible or have unscored records. Specifically, for each tract, we estimate the number of consumers in each of the thirteen age groups who are credit invisible. We then use the racial mix of the tract in each age group from the 2010 Decennial Census to estimate the racial or ethnic mix of credit invisibles, assuming for these purposes that the distribution of credit invisibles in any given tract is proportionate to the racial and ethnic composition of the tract (i.e., that members of each racial or ethnic group in a given tract have an equal chance of being credit invisible). For example, if we find that a tract has 100 credit invisibles in a given age group, and that tract's population in that age group is 15 percent Black, 10 percent Hispanic, 5 percent Asian, and 70 percent White, then we would assume that 15 of these credit invisibles were Black, 10 were Hispanic, 5 were Asian, and the remaining 70 were White. We make this calculation for each tract, at each age level, and aggregate the

numbers nationally. We estimate the racial and ethnic mix of consumers with unscored records using the same method.

FIGURE 3: NUMBER AND INCIDENCE OF CONSUMERS THAT ARE CREDIT INVISIBILE OR HAVE AN UNSCORED CREDIT RECORD BY RACE OR ETHNICITY



The results of these aggregations are shown in figure 3. Panel (A) shows our estimate of the distribution of consumers who are credit invisible or have unscored records across the five different racial or ethnic groups used in this study. The patterns are largely consistent with the overall shares of these racial or ethnic groups in the population at large. Most consumers who are credit invisible or have unscored credit records are White. Minorities account for a smaller share of the population that is credit invisible or has an unscored record, largely reflecting the fact that minorities make up a smaller portion of the overall U.S. population.

Panel (B) shows the percentage of consumers from each of the five racial or ethnic groups who, using our estimates, are credit invisible or have an unscored credit record. Whites are the least likely racial or ethnic group to be credit invisible or to have an unscored credit record, though the rates for Asians are almost identical. Blacks and Hispanics, as well as those included in the "Other" racial category, are notably more likely to be credit invisible or to have an unscored

record than Whites. Though Hispanics are slightly more likely than Blacks to be credit invisible, Blacks appear to be more likely than Hispanics to have unscored records.[8]

In calculating these estimates of the racial and ethnic mix of consumers with limited credit histories, we assumed that, within each census tract, consumers of each race or ethnicity had an equal likelihood of being credit invisible or having an unscored record. Our results suggest that consumers in census tracts with relatively more Blacks or Hispanics are more likely to be credit invisible or have an unscored credit record. Since we observe this pattern across tracts, it is likely that a similar pattern holds within tracts as well. If true, our estimate of the number of Blacks or Hispanics who are credit invisible or have an unscored credit record is likely underestimated and the number of Whites or Asians overestimated.

4.2 Racial or Ethnic Patterns by Age

The results by race or ethnicity suggest that minority populations, other than Asians, are generally more likely to be credit invisible or have unscored credit records. As shown in the previous section, the incidence of these forms of minimal credit history is strongly correlated with age. To better understand how these differences across racial or ethnic groups emerge over the course of a lifetime, we also compare the incidence of being credit invisible or having an unscored record by age across the different racial or ethnic groups. Because we do not observe how credit records change with age, we are unable to disentangle the effects of age from cohort effects, such as the different macroeconomic environments that consumers in different age groups have faced. Nevertheless, while not conclusive, the results of this analysis may provide some evidence about whether these differences emerge at young ages and, if so, whether they tend to dissipate with age.

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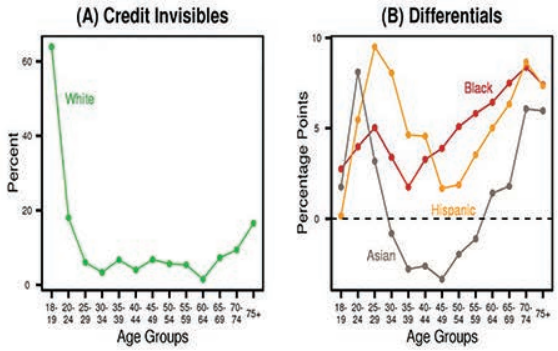
[8] One factor that may distort these figures is the undercounting of minorities (and overcounting of Whites) in the 2010 Decennial Census. The Census Bureau's post-enumeration survey for the 2010 Census found that, while the 2010 Census was the most accurate to date, the White population may have been overcounted by 0.85 percent. Blacks may have been undercounted by 2.1 percent and Hispanics by 1.5 percent (Mule, 2012). These results would suggest that we are overcounting the number of White credit invisibles and undercounting the number of Black or Hispanic credit invisibles. These changes would not have had a notable effect on the number of consumers with unscored records, though the percentage of Blacks and Hispanics unscored records would be slightly smaller.

FIGURE 4: INCIDENCE OF BEING CREDIT INVISIBLE BY AGE AND RACE OR ETHNICITY



The share of consumers in each age group who are credit invisible is shown for four racial or ethnic groups in figure 4.[9] For most racial or ethnic groups, the age patterns are very similar, so we present the results slightly differently to sharpen the contrasts. The graph on the left, panel (A), shows the results for Whites, which we use as the baseline group. The results suggest that the incidence of being credit invisible is very high for 18-19 year olds, but then falls sharply. The share holds relatively steady after age 25, until it begins to increase with age after 60.

The graph on the right, panel (B), which is shown at a magnified scale, shows the results for Asians, Blacks, and Hispanics relative to the pattern for Whites. For example, among consumers who are aged 25-29, Blacks are 5 percentage points more likely than Whites in the same age group to be credit invisible. From the left graph, panel (A), we can see that about 6 percent of Whites are credit invisible, which means that 11 percent of Blacks are credit invisible at this age.

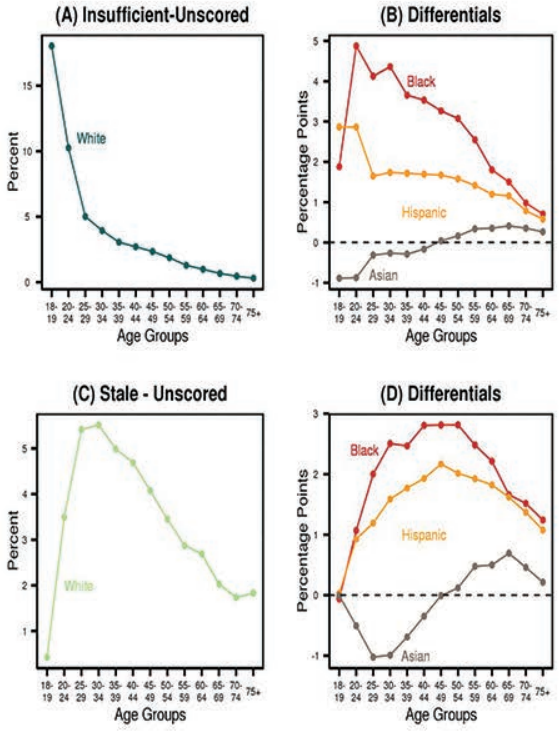
[9] Results for the "Other" racial group are omitted from the remaining graphs of this section to reduce the amount of clutter; however, they are provided in the tables in Appendix B.

The patterns in this graph indicate that Blacks and Hispanics are more likely than Whites to be credit invisible at almost every age. While we are unable to determine with our existing data whether these reflect age or cohort effects, these patterns suggest that the relatively higher incidences of being credit invisible for Blacks and Hispanics emerge at young ages and tend to persist over time. The difference between Whites and Asians is much less consistent across ages. Like Blacks and Hispanics, Asians younger than 30 or older than 60 are more likely to be credit invisible than are Whites; however, Asians aged 30 to 59 have a lower incidence of being credit invisible. This suggests that the relative equality between Whites and Asians in terms of the aggregate incidences of being credit invisible (shown earlier in table panel (b) of figure 3) conceals significant differences across ages.

Figure 5 shows a similar analysis for the incidence of unscored credit records. The left panels show the incidence for Whites of having an unscored record because of an insufficient credit history, panel (A), or a lack of recent history, panel (C). The right panels, (B) and (D), show the patterns by age for the other three racial or ethnic groups relative to Whites for these two types of unscored records, respectively.

The results indicate that the share of Whites with a credit record that is unscored because of an insufficient credit history declines steadily by age, as shown in panel (A). Blacks and Hispanics have consistently higher likelihoods of having an insufficient unscored credit record (panel (B)). The differences are largest at younger ages. While they decline for older consumers, Blacks and Hispanics of all ages are more likely than Whites to have an insufficient-unscored credit record. While young Asians are less likely, and older Asians more likely, than Whites to have an insufficient-unscored credit record, the gap between Asians and Whites remains less than one percentage point across all age groups.

FIGURE 5: INCIDENCE OF HAVING AN INSUFFICIENT-UNSCORED OR STALE-UNSCORED CREDIT RECORD BY AGE AND RACE OR ETHNICITY

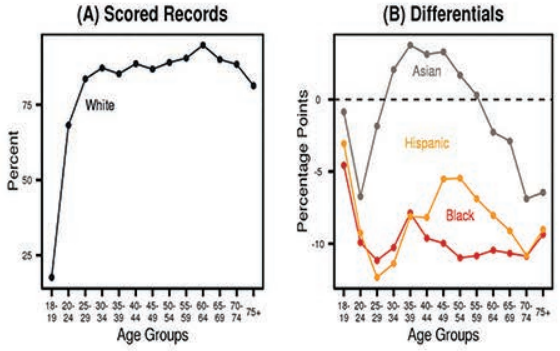


The patterns by age for records that are stale-unscored are somewhat different. For Whites, the likelihood of having a stale-unscored record increases with age until around 25-34 (panel (C)). It then declines with age thereafter. The share of Black or Hispanic consumers who have a stale-unscored record is consistently higher than Whites at almost all age levels (the exception being 18-19 years of age, when the likelihood of having a stale unscored record is near zero for all consumers). This gap increases with age until the mid-40s and declines thereafter. While the gap with Whites declines at older ages, Blacks and Hispanics appear to be consistently more likely to have a stale-unscored credit record.

Like the pattern observed for insufficient-unscored credit records, young Asians are less likely, and older Asians more likely, than Whites to have stale-unscored credit records. Again, however, the gap between Asians and Whites remains within 1 percentage point at all age levels, suggesting that the patterns for Asians and Whites are similar.

Taken together, these results suggest that Blacks and Hispanics are more likely to be credit invisible or to have unscored credit records. These differences are observed for all age groups, which suggests that these differences emerge at young ages and persist over the lifetimes of these consumers.

FIGURE 6: INCIDENCE OF HAVING A SCORED CREDIT RECORD BY AGE AND RACE OR ETHNICITY



The combined effects of being credit invisible or having an unscored credit record are shown in figure 6, which depicts the share of consumers at each age with a scored credit record. Again, the left panel shows the pattern by age for Whites and the right panel shows the relative patterns for Asians, Blacks, and Hispanics.

Panel (A) of this figure shows that the share of Whites with a scored credit record increases sharply with age up to around age 30 and then increases more gradually through age 60. At older ages, the incidence of having a scored credit record decreases somewhat with age. Blacks and Hispanics, shown in panel (B), are less likely than Whites to have a scored credit record at very early ages. This gap widens with age, becoming greater than 10 percentage points for ages 25-29 for both groups, and remains large thereafter, though it does narrow (particularly for Hispanics around 50 years of age, though this narrowing is not observed at older ages). As our earlier results would suggest, the pattern for Asians is somewhat different. At early ages, they are less likely to have scored credit records than are Whites; however, this gap shrinks during their 20s and disappears in their 30s to 50s, during which time they are more likely to have a scored credit record than Whites in the same age group. Asians older than 54, however, are less likely to have credit records than Whites.

Overall, these patterns suggest that the problem of limited credit history affects all racial or ethnic groups. Nevertheless, Blacks and Hispanics appear more likely to be credit invisible or have an unscored record. These differences are observed across all age levels.

5. Conclusions

The three NCRAs have traditionally been the sole source of information used to calculate credit scores like the scores produced by FICO or VantageScore. Consumers with limited credit histories established in the records of the three NCRAs generally have a harder time obtaining credit as a result because many lenders do not extend credit to consumers without a scored credit record or do so only in quite narrow circumstances. While there has been a lot of attention paid to the problem of limited credit history and to various forms of alternative data that might mitigate it, very little is known about the number of consumers who are affected and even less is known about their demographic characteristics.

This report uses data from the CFPB's Consumer Credit Panel and aggregate information from the 2010 Decennial Census and 2008-2012 American Community Survey, both conducted by the U.S. Census Bureau, to construct estimates of the number of consumers with limited credit histories. Our results suggest that there are 26 million adults in the United States without a credit record. This amounts to 11 percent of U.S. adults. Additionally, our results suggest that another 19 million adults (about 8 percent) have credit records that are considered "unscorable" by the commercially-available credit scoring model used in this analysis. These records are almost evenly split between those that are unscored because of an insufficient credit history (too few accounts) and those that are unscored because of a lack of recently reported credit history.

Our results also suggest that there is a strong relationship between income and having a credit record. Almost 30 percent of consumers in low-income neighborhoods are credit invisible and an additional 16 percent have unscored records. These percentages are notably lower in higher-income neighborhoods. For example, in upper-income neighborhoods, only 4 percent of the population is credit invisible and another 5 percent has an unscored record.

Additionally, our results suggest that there are significant differences in the incidence of having a limited credit history across racial and ethnic groups. While Whites and Asians are almost equally likely to be credit invisible or have an unscored record, the shares of Blacks and Hispanics with limited credit history are much larger. About 15 percent of Blacks and Hispanics

are credit invisible (compared to 9 percent of Whites and Asians) and an additional 13 percent of Blacks and 12 percent of Hispanics have unscored records (compared to 7 percent of Whites). This elevated incidence of being credit invisible or having an unscored credit record is observed across ages, suggesting that these differences across racial and ethnic groups materialize early in the adult lives of these consumers and persist thereafter. These results suggest that the problems that accompany having a limited credit history are disproportionally borne by Blacks, Hispanics, and lower-income consumers.

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APPENDIX A:

Effect of Fragment File Exclusions

Estimates of the number of credit invisibles or consumers with unscored credit records depend crucially on the decisions about which credit records in the sample to identify as likely fragment files. In this Appendix, we provide detail about the exclusions that were applied in pruning the data of likely fragment files and the effects that these had on our results.

Before identifying likely fragment files, we excluded credit records for consumers living outside of the United States. Most of these were credit records for consumers living in Puerto Rico and other U.S. territories. About 44,000 records were excluded for this reason. We also excluded credit records that indicated the consumer was deceased in 2010. These exclusions were necessary to focus on the population of interest and make the credit record population as comparable to the Census data as possible.

Once these exclusions were made, this left a sample with 4.7 million credit records. From these we removed two groups of credit records that we believed were most likely fragment files. The first of these groups included credit records that disappeared between December 2010 and December 2014. In total, there were 242,727 records excluded for this reason. These records were split into two subgroups. The first subgroup included 138,152 credit records that were identified as having been consolidated into existing credit records, which is a direct identifier of a fragment file. The second subgroup included an additional 104,575 credit records that, while we could find no record of having been consolidated into an older credit record disappeared during the four years.

The second group included the credit records of consumers whose credit records were missing year-of-birth information in both December 2010 and December 2014. There were 153,152 records excluded for this reason. Date of birth is an important factor used by the NCRAs in matching reported account information to credit records. The fact that these files had no year-of-birth information in the CCP indicates that the credit record maintained by the NCRA did not

have a date of birth and suggests that these files contain account information that the NCRA was unable to uniquely match to a primary file. Consistent with this, most of these credit records contain authorized user accounts.

In addition to these exclusions, our estimates were also affected by records that were not excluded, but that might have contained a large share of fragment files. In particular, we considered excluding those credit records that only contained information reported by third-party debt collectors or information from public records. Based on conversations with industry participants, we believe that NCRAs have a more difficult time finding unique matches for information from these sources. This suggests that these types of records may contain a large number of fragment files. Nevertheless, we believe that excluding all such records would have excluded too many primary credit records and chose to include these records in our estimates.

Table 1 shows the effect that each of these exclusions and inclusions had on our estimates of the number of consumers who are credit invisible or have an unscored credit record. The first line of the table shows our estimate presented in the body of this Data Point. The following lines show the effect that each exclusion or inclusion had on the overall estimate. For example, the decision to exclude credit records that were missing in 2014 because they likely were fragment files had the effect of decreasing our estimate of the number of scored records by 4.3 million and increasing our estimate of the number of credit invisibles by 11.7 million. Similarly, our decision to include credit records that contained only third-party debt collection accounts increased our estimate of the number of consumers with a scored credit record by 0.1 million and decreased our estimate of the number of credit invisibles by 2.1 million.

TABLE 1: EFFECTS OF SAMPLE EXCLUSIONS AND INCLUSIONS

	Scored Records	Credit Invisibles	Stale-Unscored	Insufficient-Unscored
Baseline Estimate	188.6	26	9.6	9.9
Exclusions:				
Missing in 2014 (Total)	-4.3	+11.7	-1.7	-5.7
Observed Merge	-3.0	+6.6	-1.2	-2.4
Disappeared	-1.2	+5.0	-0.5	-3.3
Missing Age	-6.5	+7.4	-0.4	-0.5
Inclusions:				
Debt Collection Only	+0.1	-2.1	+0.09	+1.9
Public Record Only	+0.01	-0.4	+0.01	+0.3

APPENDIX B:

Data Used in Figures

This Appendix provides the underlying data used to produce each of the figures in the text.

TABLE 2: SHARE OF CONSUMERS THAT ARE CREDIT INVISIBLE OR UNSCORED, DATA FOR FIGURE 1(A)

Age Group	Credit Invisible	Stale-Unscored	Insufficient-Unscored
18 to 19 years	64.5	0.4	18.9
20 to 24 years	20.2	3.8	11.5
25 to 29 years	8.9	5.9	5.9
30 to 34 years	5.5	6.1	4.9
35 to 39 years	7.6	5.6	3.9
40 to 44 years	5.1	5.4	3.4
45 to 49 years	7.4	4.7	3.0
50 to 54 years	6.4	4.0	2.4
55 to 59 years	6.3	3.4	1.7
60 to 64 years	2.7	3.1	1.3
65 to 69 years	8.6	2.3	0.9
70 to 74 years	11.1	2.0	0.6
75 years and over	17.8	2.0	0.4

TABLE 3: THE NUMBER OF CONSUMERS THAT ARE CREDIT INVISIBLE OR HAVE AN UNSCORED CREDIT RECORD BY AGE, DATA FOR FIGURE 1(B)

Age Group	Credit Invisible	Stale-Unscored	Insufficient-Unscored
18 to 19 years	5.8	0.0	1.7
20 to 24 years	4.3	0.8	2.5
25 to 29 years	1.9	1.2	1.2
30 to 34 years	1.1	1.2	1.0
35 to 39 years	1.5	1.1	0.8
40 to 44 years	1.1	1.1	0.7
45 to 49 years	1.7	1.1	0.7
50 to 54 years	1.4	0.9	0.5
55 to 59 years	1.2	0.7	0.3
60 to 64 years	0.5	0.5	0.2
65 to 69 years	1.1	0.3	0.1
70 to 74 years	1.0	0.2	0.1
75 years and over	3.3	0.4	0.1

TABLE 4: NUMBER OF CONSUMERS THAT ARE CREDIT INVISIBLE OR HAVE AN UNSCORED CREDIT RECORD BY CENSUS TRACT INCOME LEVEL, DATA FOR FIGURE 2(A)

Income Group	Credit Invisible	Stale-Unscored	Insufficient-Unscored
Low	3.7	0.9	1.2
Moderate	8.4	2.8	3.1
Middle	11.2	4.1	3.9
Upper	2.6	1.8	1.7

TABLE 5: INCIDENCE OF BEING CREDIT INVISIBLE OR HAVING AN UNSCORED CREDIT RECORD BY CENSUS TRACT INCOME LEVEL, DATA FOR FIGURE 2(B)

Income Group	Credit Invisible	Stale-Unscored	Insufficient-Unscored
Low	28.9	6.8	9.5
Moderate	17.6	5.8	6.5
Middle	11.0	4.1	3.8
Upper	3.6	2.5	2.4

TABLE 6: NUMBER OF CONSUMERS THAT ARE CREDIT INVISIBLE OR HAVE AN UNSCORED CREDIT RECORD BY RACE OR ETHNICITY, DATA FOR FIGURE 3(A)

Race or Ethnicity	Credit Invisible	Stale-Unscored	Insufficient-Unscored
Black	4.0	1.6	2.0
Hispanic	5.3	1.8	2.1
Asian	1.1	0.4	0.4
Other	0.7	0.3	0.3
White	14.7	5.5	5.1

TABLE 7: INCIDENCE OF BEING CREDIT INVISIBLE OR HAVING AN UNSCORED CREDIT RECORD BY RACE OR ETHNICITY, DATA FOR FIGURE 3(B)

Race or Ethnicity	Credit Invisible	Stale-Unscored	Insufficient-Unscored
Black	14.8	5.8	7.2
Hispanic	15.8	5.5	6.4
Asian	9.8	3.6	3.7
Other	13.7	4.6	5.9
White	9.4	3.5	3.2

TABLE 8: INCIDENCE OF BEING CREDIT INVISIBLE BY AGE AND RACE OR ETHNICITY, DATA FOR FIGURES 4(A) AND 4(B)

Age Group	White	Black	Hispanic	Asian	Other
18 to 19 years	63.9	66.6	64.0	65.6	65.3
20 to 24 years	18.0	22.0	23.5	26.1	21.0
25 to 29 years	6.0	11.1	15.5	9.2	9.3
30 to 34 years	3.3	6.7	11.4	2.5	5.5
35 to 39 years	6.7	8.4	11.3	3.9	7.3
40 to 44 years	4.0	7.3	8.6	1.4	5.6
45 to 49 years	6.8	10.7	8.5	3.4	9.5
50 to 54 years	5.6	10.7	7.5	3.7	7.9
55 to 59 years	5.3	11.2	8.9	4.2	8.1
60 to 64 years	1.5	8.0	6.6	3.0	4.6
65 to 69 years	7.3	14.8	13.6	9.1	10.2
70 to 74 years	9.4	17.8	18.0	15.5	13.4
75 years and over	16.5	23.9	23.9	22.5	20.0

TABLE 9: INCIDENCE OF HAVING AN INSUFFICIENT-UNSCORED CREDIT RECORD BY AGE AND RACE OR ETHNICITY, DATA FOR FIGURE 5(A) AND 5(B)

Age Group	White	Black	Hispanic	Asian	Other
18 to 19 years	18.0	19.9	20.9	17.1	18.9
20 to 24 years	10.3	15.1	13.1	9.4	12.4
25 to 29 years	5.0	9.1	6.7	4.7	6.3
30 to 34 years	3.9	8.3	5.7	3.7	5.2
35 to 39 years	3.1	6.7	4.8	2.8	4.4
40 to 44 years	2.7	6.2	4.4	2.5	4.1
45 to 49 years	2.3	5.6	4.0	2.4	3.5
50 to 54 years	1.9	4.9	3.4	2.0	3.0
55 to 59 years	1.3	3.8	2.7	1.6	2.2
60 to 64 years	1.0	2.8	2.2	1.3	1.8
65 to 69 years	0.7	2.2	1.8	1.1	1.4
70 to 74 years	0.5	1.4	1.3	0.8	1.0
75 years and over	0.3	1.0	0.9	0.6	0.8

TABLE 10: INCIDENCE OF HAVING A STALE-UNSCORED CREDIT RECORD BY AGE AND RACE OR ETHNICITY, DATA FOR FIGURE 5(C) AND 5(D)

Age Group	White	Black	Hispanic	Asian	Other
18 to 19 years	0.4	0.4	0.5	0.4	0.4
20 to 24 years	3.5	4.6	4.4	3.0	3.9
25 to 29 years	5.4	7.4	6.6	4.4	6.1
30 to 34 years	5.5	8.0	7.1	4.5	6.4
35 to 39 years	5.0	7.5	6.8	4.3	6.0
40 to 44 years	4.7	7.5	6.6	4.3	5.8
45 to 49 years	4.1	6.9	6.2	4.1	5.2
50 to 54 years	3.5	6.3	5.5	3.6	4.7
55 to 59 years	2.9	5.4	4.8	3.3	3.9
60 to 64 years	2.7	4.9	4.5	3.2	3.7
65 to 69 years	2.0	3.7	3.7	2.7	2.9
70 to 74 years	1.7	3.3	3.1	2.2	2.3
75 years and over	1.8	3.1	2.9	2.0	2.3

TABLE 11: INCIDENCE OF HAVING A SCORED CREDIT RECORD BY AGE AND RACE OR ETHNICITY, DATA FOR FIGURE 6(A) AND 6(B)

Age Group	White	Black	Hispanic	Asian	Other
18 to 19 years	17.7	13.1	14.6	16.8	15.4
20 to 24 years	68.2	58.3	59.0	61.5	62.7
25 to 29 years	83.6	72.4	71.2	81.7	78.3
30 to 34 years	87.2	76.9	75.8	89.3	82.8
35 to 39 years	85.3	77.4	77.2	89.0	82.3
40 to 44 years	88.6	79.0	80.4	91.7	84.5
45 to 49 years	86.8	76.8	81.3	90.1	81.8
50 to 54 years	89.0	78.1	83.6	90.7	84.4
55 to 59 years	90.5	79.6	83.6	90.8	85.8
60 to 64 years	94.8	84.3	86.7	92.5	89.9
65 to 69 years	90.0	79.3	80.9	87.1	85.5
70 to 74 years	88.4	77.5	77.6	81.5	83.3
75 years and over	81.3	72.0	72.3	74.9	77.0

GIVE CREDIT WHERE CREDIT IS DUE

Increasing Access to Affordable Mainstream Credit Using Alternative Data

Political and Economic Research Council
The Brookings Institution Urban Markets Initiative

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GIVE CREDIT WHERE CREDIT IS DUE:

Increasing Access to Affordable Mainstream Credit Using Alternative Data

POLITICAL AND ECONOMIC RESEARCH COUNCIL & THE BROOKINGS INSTITUTION URBAN MARKETS INITIATIVE © 2006

EXECUTIVE SUMMARY

Despite the vast accomplishments of the American credit system, approximately 35 million to 54 million Americans remain outside the credit system. For a variety of reasons, mainstream lenders have too little information on them to evaluate risk and thereby extend credit. As a result, those in most need of credit often turn to check cashing services and payday loan providers, with effective interest rates as high as 500 percent. The lack of reliable credit places them at a great disadvantage in building assets (such as homes, small businesses, or loans for education) and thereby improving their lives.

This study offers a feasible market solution to bring those outside the mainstream credit fold within it. Mainstream lenders can use "alternative" or "nontraditional" data, including payment obligations such as rent, gas, electric, insurance, and other recurring obligations, to evaluate the risk profile of a potential borrower.[1] Our findings indicate that alternative data, if widely incorporated into credit reporting, can bridge the information gap on financial risk for millions of Americans. More concretely, considering that many of these millions outside the credit mainstream are poorer, less advantaged Americans, the information can direct markets toward a faster alleviation of poverty in this country.

We examined a sample of approximately 8 million TransUnion credit files with a strong focus on consumers outside of the credit mainstream. The consumers include populations with thin credit files (fewer than three sources of payment information, or trade lines) on payment timeliness, as well as "unscoreable" segments whose risk cannot be determined owing to insufficient information. The credit report files, which contained alternative or nontraditional utility and telecommunications payment information, were applied to models used by lenders to make a variety of credit decisions. The scores, or predictions, of these models were then compared with payment/bankruptcy outcomes observed during the following year.

Key findings include:

- ***Those outside the credit mainstream have similar risk profiles as those in the mainstream when including nontraditional data in credit assessments.*** The evidence suggests that most individuals in this segment are not at high risk in terms of lending. Using nontraditional data lowered the rate of serious default by more than 20 percent among previously unscoreable populations. The risk profile of the thin-file/unscoreable population—after energy utility and telecommunications data sets are included in their credit files—is similar to that of the general population (as measured by credit score distribution).

- ***Nontraditional data make extending credit easier.*** Including energy utility data in all consumer credit reports increases the acceptance rate by 10 percent, and including telecommunications data increases the acceptance rate by 9 percent, given a 3 percent target default rate.

• *Minorities and the poor benefit more than expected from nontraditional data.*

Including alternative data was especially beneficial for members of ethnic communities and other borrower subgroups. For instance, Hispanics saw a 22 percent increase in acceptance rates. The rate of increase was 21 percent for Blacks; 14 percent for Asians; 14 percent for those aged 25 or younger; 14 percent for those aged 66 older; 21 percent for those who earn $20,000 or less annually; and 15 percent for those earning between $20,000 and $29,999. In addition, renters (as opposed to homeowners) saw a 13 percent increase in their acceptance rate, and those who prefer Spanish as their primary language saw a 27 percent increase in their acceptance rate.

• *Nontraditional data decrease credit risk and increase access.*

The addition of the alternative data moves 10 percent of the analysis sample from being unscoreable to scoreable. Sizable segments would see their credit scores improve—22.4 percent in the utility sample and 11 percent in the telecommunications sample. Most remarkable is that two-thirds of both the thin-file utility sample (60.3 percent) and the thin-file telecommunications sample (67.7 percent) become scoreable when alternative data are included in their credit files. Preliminary evidence strongly suggests that the inclusion of alternative trade lines in conventional credit reports improves access to mainstream sources of consumer credit. In a one-year observation period, 16 percent of thin-file borrowers whose credit report included nontraditional data opened a new credit account compared with only 4.6 percent of thin-file borrowers with only traditional data in their credit reports.

• *Nontraditional data have little effect on the credit mainstream.*

One worry is that including nontraditional data will be counterproductive, harming more in the mainstream that helping those now excluded. The results of simulations reported here suggest that little will change for the mainstream population.[2]

• *More comprehensive data can improve scoring models.*

This migration greatly affects the performance of examined scoring models. For example, in our study, in one set of calculations we assume that creditors interpret little or no credit information as the highest risk. As a result, when fully reported utility or telecommunications trade lines are added to credit reports, we see a significant rise in the KS statistic—an industry gauge to measure the model performance. Specifically, we see a 300 percent rise for a sample of thin-file consumers, and a nearly 10 percent rise for the general sample. In the most conservative case, in which the general sample is used but unscoreable credit files are excluded from the calculations, we still find a modest 2 percent improvement in model performance with the addition of alternative data.

• *More data can reduce bad loans.*

Including fully reported energy utility and telecommunications trade lines (i.e., different accounts) in traditional consumer credit reports measurably improves the performance of loans for a target acceptance rate. For example, by integrating fully reported energy utility data, a lender's default rate (percentage of outstanding loans 90 days or more past due) declines 29 percent, given a 60 percent target acceptance rate. Similarly, adding telecommunications data reduces the default rate by 27 percent. These reductions allow lenders to make more capital available and improves their margins, capital adequacy, and provisioning requirements. Such improvements could have further positive economywide effects.

In summary, nontraditional data promise to bring millions into the credit mainstream and improve their chances of building assets. Although using alternative data in consumer credit reports affects how the data appear in a host of credit scoring models, nothing about the data subjects has changed. What has changed is the availability of information. Whenever an information gap exists, markets fail to thrive. The use of alternative data in consumer (and commercial) credit reports can close an information gap that has negatively affected the lives of millions of thin-file and unscoreable Americans who reside in urban areas and elsewhere.

The benefits of using nontraditional data will not be instantaneous. Information must first be gathered and implemented, new models optimized for such data must be built and old models modified. Some models must be altered to not treat utilities and telecommunications accounts as a financial trade. The steps, while few, are important. Simply bringing the information online will spur many of the steps; without it, there is no incentive to take them. Public officials can play a positive role by removing barriers to reporting where they exist. ■

OVERVIEW

- **Section I** provides a brief overview of the impact of the U.S. credit system, those left behind, and the role of information in bringing those outside the credit mainstream into accessible, affordable credit channels.
- **Section II** describes the objectives, data sources, and methodology of the study.
- **Section III** shows how the addition of utility and telecommunications trades has affected consumers' credit profiles, focusing on the number of consumers who can be scored and the resulting distribution of credit scores.
- **Section IV** compares the number and size of new accounts that were opened by consumers with an existing utility or telecommunications trade (the "analysis" sample) to the number and size of new accounts that were opened by otherwise similar consumers without such trades (the "validation" sample).
- **Section V** examines the impact of utility and telecommunications trades on the predictive power of several scoring models and the implications for both the cost and availability of credit.
- **Section VI** examines the demographic groups that would most likely be affected by a more systematic reporting of utility and telecommunications data.
- **Section VII** summarizes the empirical results and concludes with a discussion of their implications for public policy.
- **Section VIII** offers directions for future research.

Appendix A describes the analysis sample in more detail and assesses the extent of potential biases. **Appendix B** presents the complete results of our model simulations. ■

I. INTRODUCTION

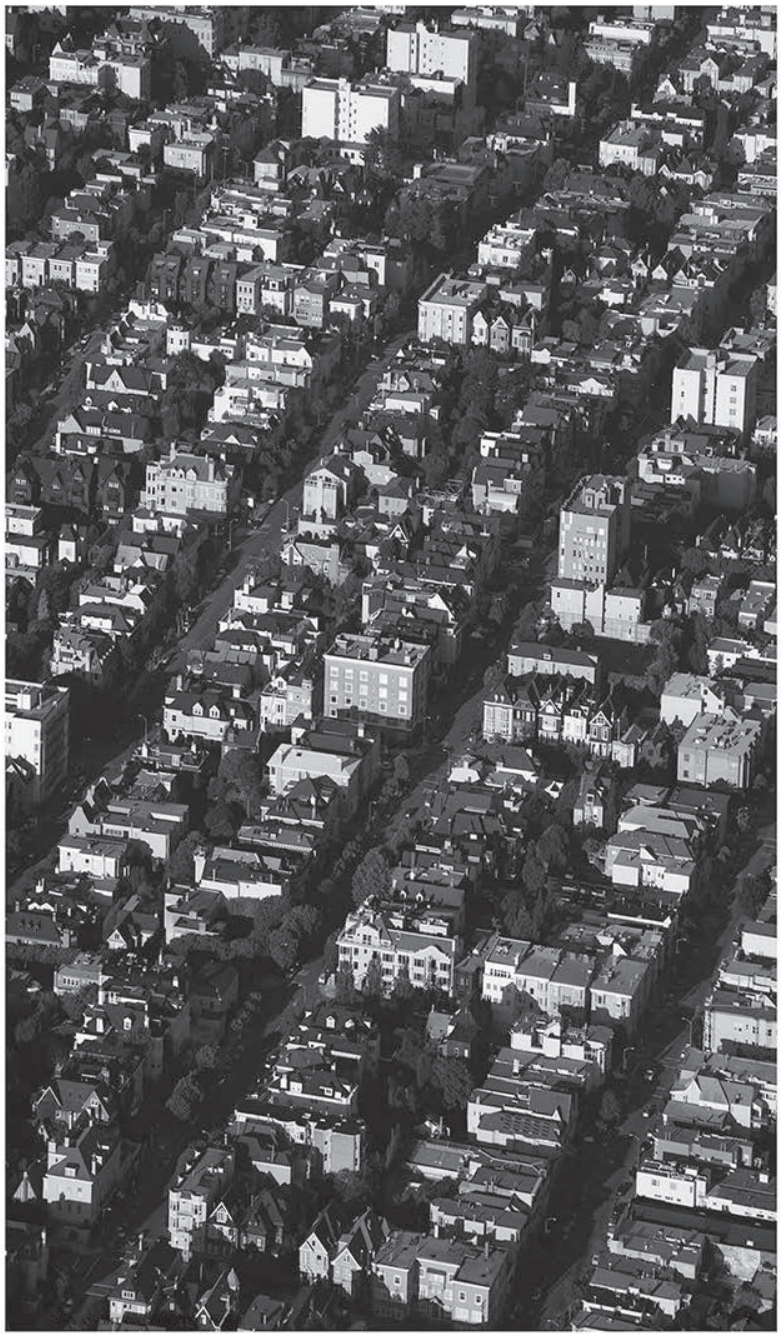
EXCLUDED FROM THE MIRACLE

The American credit system is in many ways the envy of the world.

The steady development of information-sharing, automated credit scoring, and easy entry by new competitors have extended credit to tens of millions of Americans. In the years since the financial services industry began using standardized payment information for scoring, homeownership rates have grown and credit has become available to those for whom credit was reserved for the elite.

The national credit reporting system has become the basis for "automated underwriting," a practice that has become so successful that former Federal Trade Commission Chairman Tim Muris referred to it as "the miracle of instant credit." The former Federal Reserve Board Chairman Alan Greenspan said that such a system and technologies using it had "a dramatic impact...on consumers and households and their access to credit in this country at reasonable rates." This success ranges from those applying for a home mortgage loan or refinancing an existing mortgage to those applying for a credit card or a retail store card. Thus, the national credit reporting system touches the lives of millions of Americans each day. The robust and full-file data maintained by consumer reporting agencies have contributed to a significant expansion in consumer and small-business lending without increasing risk in the national credit system.

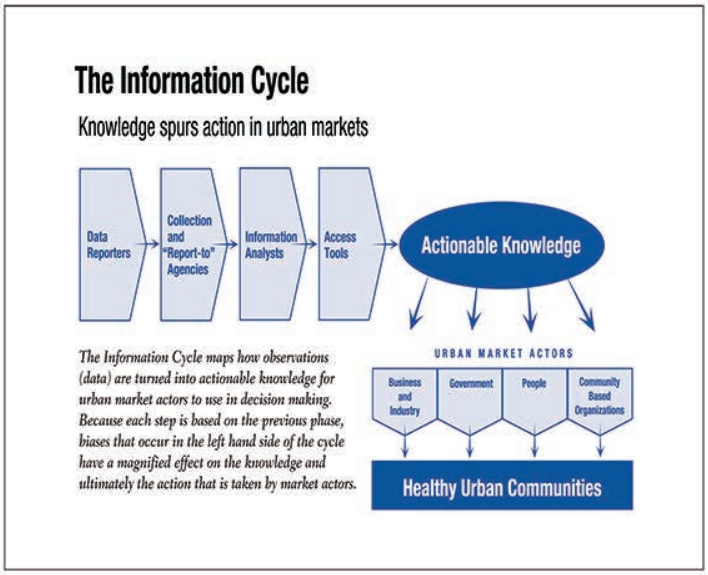
Despite the impressive track record of the national credit system under the Fair Credit Reporting Act—record homeownership, fairer lending across all segments of society, a democratization of access to credit—an estimated 35 million to 54 million Americans remain outside of the mainstream national credit system. This group is excluded from instant credit because there is little or no credit information in their credit files. As a result, mainstream lenders, lacking sufficient information for automated underwriting tools, equate a lack of information with unacceptably high credit risk.



THE INFORMATION CYCLE

In one sense, those outside the mainstream credit system are trapped in a catch-22 by their lack of a credit history: how does one build a credit history when denied access to credit? Lenders currently lack the right tools to adequately assess the credit risk, credit capacity, and credit-worthiness of tens of millions of "thin-file" (that is, those with little credit history) and "unscoreable" Americans. The lack of tools stems from a gap in adequate information on which to make credit decisions about these individuals.

Identifying information gaps, developing solutions to bridge them, and educating decision makers in new ways to better understand underserved credit markets requires a clear understanding of the process of knowledge creation, or the information cycle.[3] Although decision makers begin with raw data, they must analyze it, or add value to it, to make it useful *information*. Prior to 1970, lenders gained information by assessing the capacity, collateral, credit, and character of borrowers. In today's world of automated credit underwriting, data are turned into information by external consultants—consumer credit bureaus. Consumer credit bureaus have become powerful information sources and "translators" of the potential of consumer credit markets.



The Information Cycle maps how observations (data) are turned into actionable knowledge for urban market actors to use in decision making. Because each step is based on the previous phase, biases that occur in the left hand side of the cycle have a magnified effect on the knowledge and ultimately the action that is taken by market actors.

In credit decisions, lender's analytic teams and modeling capabilities provide a customized understanding of the market context to use in turning the information they receive into *knowledge* on which to act. Although automation has enabled a deeper penetration of some markets, it customarily overlooks the thin-file and unscoreable populations. The lack of data and information on these populations can lead to "knowing-doing" gap: the gap between a lender's perception of a particular individual's potential and the reality of his or her credit risk, credit capacity, and credit-worthiness.[4] Many lenders, who are aware that this is not the case, are often forced to treat these borrowers as excessively risky simply for want of better information.

NONTRADITIONAL DATA CAN BRIDGE THE INFORMATION GAP

One potential solution to the credit Catch-22 is pervasive reporting of nontraditional or alternative data in consumer credit reports.[5] In this study, PERC singled out energy utilities (gas, electric, heating oil, water) and telecommunications as the most promising data sets to help bring consumer outliers into the fold. These two data sets ranked highest along three metrics—coverage, concentration, and being credit-like. They were also likely to yield results for a large segment of the 35 million to 54 million thin-file/unscoreable individuals, as the penetration rates for these services are frequently 90 percent or more. The utility and telecommunications industries are relatively concentrated, making data collection more feasible. Finally, exchanges in these two industries involve "credit-like" transactions—that is, a good or service is provided in advance of a payment, and the payments are made in regular installments.

Other alternative data sets—such as auto insurance, remittance payments, and rental data—did not score as highly as utility and telecommunications data. These sets may have value, but their near-term promise for the thin-file/unscoreable population is not as evident. For simplicity's sake, throughout the course of this study, the terms "alternative data" and "nontraditional data" refer exclusively to utility and telecommunications data, unless otherwise specified.

This study tests the hypothesis that including utility and telecommunications data in consumer credit reports can achieve the following results:

(1) Increased ability of mainstream lenders to adequately assess credit risk, credit capacity, and credit-worthiness of the thin-file/unscoreable population;

(2) Increased access to affordable mainstream credit for thin-file/unscoreable population;

(3) Thin-file/unscoreable individuals will derive the greatest benefit from including alternative data, while the credit effects on "thicker-file" individuals will be less evident; and,

(4) Increased fairness in lending, especially for minority communities and younger borrowers.

THE CRITICAL ROLE OF CREDIT FILES

Information contained in consumers' credit files plays a critical role in determining both the amount and the terms of credit that they receive. Behind this simple fact is an issue of considerable importance, for the claim can be extended to "and thereby shape the ability of individuals to build assets and thus alter their life chances." The use of information in credit decisions, especially via automated models, has extended credit to millions, increasing homeownership rates, access to education, and small business formation. This payment information therefore plays a significant role in shaping the social fortunes of individual Americans. In general, consumers who have demonstrated a history of timely payments on several different accounts, or trade lines, are more likely to be granted credit at more favorable terms than those with spotty payment records or with little, if any, established credit.

Unfortunately, those with *no* credit histories and those with *poor* credit are often treated similarly. The net effect is that millions of Americans remain outside the credit mainstream and are consequently handicapped in their ability to access credit and improve their lives. Moreover, many are forced to turn to providers who charge as effective rates as high as 500 percent.

Alternative or nontraditional data offer one possible solution to the problems posed by no credit histories. The financial services industry has long recognized the need to find alternative ways of evaluating the creditworthiness of thin-file consumers. For example, some in the mortgage industry now accept a "nontraditional credit report" based on the consumer's demonstrated performance in meeting such ongoing obligations as rent, utilities, and telephone bills.[6] Although such payments are not credit obligations in the traditional sense, they are generally believed to reflect a consumer's willingness and ability to repay credit-like obligations.

A recent report by the Information Policy Institute examined the feasibility of collecting these and other types of nontraditional credit data on a widescale basis. Of the different sources considered, utility and telecommunications trades again appeared to be most promising, for among other reasons, the concentration of the data. Relatively few data furnishers must be engaged, unlike with rental information, which is widely dispersed among diverse landlords. Although some utility and telecommunications companies currently report data to credit bureaus, the majority do not. In fact, in some states, the reporting of such data is prohibited by law or regulation, and in many others, uncertainty about the reaction of regulators inhibits utilities from reporting.

None of this is to suggest that other types of alternative payment information—auto insurance, rents, and so forth—are of less value, just that utility and telecommunications data may be one effective way of folding in those outside the credit mainstream. From a standpoint of practicality, utility and telecommunications payment data may be the fastest way to extend credit to underserved communities.

The promise is that new data sources can help tens of millions of Americans take a step toward asset formation. Considering that many of these millions are poorer, less advantaged Americans, the information can help alleviate poverty in this country. That is, it promises a market solution to problems of credit access. What follows is an attempt to measure that promise.

II. METHODS

OBJECTIVES

This report examines the impact that the broader reporting of telecommunications and utility trades could have on consumers' access to different types of credit. In our analysis, "utility" trades include payments for electricity, gas, and heating oil, while "telecommunications" trades refer to traditional telephone service (i.e., land lines) and mobile phones. Although precise statistics are difficult to assemble, the number of consumers who would likely be affected by the reporting of these trades is undoubtedly very large, as the consumption of these services is nearly universal.

It should be noted that there have been previous attempts to encourage the utilities to report to the credit bureaus. Yet, to date, the scale of the impact remained one without measurement. This study aims to fill that gap and to provide clear estimates of the impact of reporting. In doing so, industry and policy makers can assess what is at stake and chart viable courses to assist those who have poor or no access to mainstream credit.

Increasing the reporting of utility and telecommunications trades could affect consumers in at least two different ways:

- ***First, it would increase the number of consumers who can be scored, and who thereby can access credit.*** Although the industry has developed several alternative approaches for evaluating the credit-worthiness of thin-file borrowers, many traditional scoring models require at least one valid trade. All of the models used in this study require just one trade to produce a score. Nonetheless, using a representative sample of credit files, we found, 13 percent of credit files had no payment histories, and 19.4 percent had only one or two payment trade lines. Because the systematic reporting of utility and telecommunications data should add one or more trade lines to the credit profile of the typical consumer, the number of potential borrowers with thin credit files should be reduced. By increasing the number of trade lines that can be used to score consumers, the predictive power of scoring models should be improved, which in turn should lead to higher acceptance rates, lower costs, or a combination of the two.

- ***Second, the systematic reporting of utility and telecommunications trades could affect the distribution of credit scores.*** Depending on the consumer's payment record and overall credit profile, the impact on an individual's score could be positive or negative. Although the impact on consumers with well-established credit histories would likely be minimal, the impact on consumers with little or no established credit could be large.

To the extent that this information leads to better lending, we might also expect reductions in the average price of credit. We do not, however, undertake a direct measure of this expected reduction, but rather estimate changes in the performance of portfolios, which

Table 2.1. Distribution of Consumers by Number of Telecommunications and Utility Trades: 2005 Analysis Sample

Number of Trades	Consumers with Utility Trades		Consumers with Telecom Trades	
	No.	%	No.	%
1	5,076,811	67.5	545,826	92.4
2	1,414,501	18.8	38,127	6.5
3	608,502	8.1	5,025	0.9
4+	419,206	5.6	1,817	0.3
Total	7,519,020	100.0	590,795	100.0

are a major component of loan pricing. The research presented in this report has been designed to estimate the probable magnitude of these different effects and to identify the types of consumers who are most likely to be affected.

Although not quantified in this study, another benefit of including alternative data in consumer credit reports is that the uncertainty associated with a given credit score should decline. For example, a lender deciding whether to extend credit to two individuals with identical credit scores—the first of which uses alternative data in addition to traditional credit data—will be more likely to lend to the first applicant, all else equal, because the additional data reduces uncertainty about the credit score. The lender may even prefer to extend credit to an individual with a more accurate but lower credit score than to an individual with a less accurate but higher credit score. As is evidenced in this and other studies, adding predictive information to a credit scoring model reduces the uncertainty of credit scores. It is therefore reasonable to expect that lenders would extend credit more deeply[281] than the estimates generated in this study. This may be particularly true for those with thin credit files. A lender may be more likely to lend (and at better rates) to an individual of a given risk level if they know that risk level with greater certainty.

THE DATA FOR THE SIMULATIONS

Our analysis uses a data set constructed by TransUnion from the detailed credit reports of two mutually exclusive samples of consumers:

- An analysis sample of approximately 8.1 million consumers with at least one "fully reported" utility (gas, electric, or fuel) or telecommunications trade (wireless or land line) as of March 31, 2005.
- A validation sample of approximately 4 million randomly selected individuals designed to represent the broader population of consumers with no fully reported utility or telecommunications trades on March 31, 2005.

"Fully reported" trade lines include information on the timely payment of bills as well as any derogatories (e.g., delinquent accounts referred to collection agencies.) Although most utility and telecommunications companies routinely report collections, the reporting of *timely* payments is far less common.

Table 2.1 shows the number and distribution of consumers in the analysis file by the number of utility and telecommunications trades. As shown in the chart, most of the records in the analysis file have a utility as opposed to a telecommunications trade. Just over 7.5

million consumers in the analysis file have at least one fully reported utility trade, and about one-third have more than one (for example, consumers who use a combination of gas and electricity in their homes.) In contrast, only 591,000 consumers in the analysis file have a fully reported telecommunications trade, and only 8 percent have more than one. Because there is relatively little overlap between the two groups (only about 1,500 records have both a utility and a telecommunications trade), they are treated separately throughout this report.

We collected detailed information from the consumers' credit reports for both the analysis and the validation samples at two points in time: March 31, 2005 (the date that was used to generate the samples) and March 31, 2006. The intervening year is the "performance period," during which the predictions of the model were evaluated. We augmented the credit bureau data in two ways:

- We used a variety of credit scoring models to score each consumer in the sample with and without his or her utility and telecommunications data.
- We sent the data to an independent service provider, who appended information on the individual's race, ethnicity, age, and household income.[9]

The resulting data set contains a wealth of information on the credit profiles of consumers, their demographic characteristics, and the effect of any reported utility and telecommunications trades on a variety of credit scores.

We took deliberate steps to ensure the privacy and confidentiality of individual consumers. Specifically, the data contain no identifying information of individual consumers (that is, no names, addresses, social security numbers, or account numbers). Once the demographic data were merged with the credit reports, we purged all identifying information from the file.

APPROACH

This study examines the impact of including alternative data in consumer credit reports on credit scoring models and on credit access by various communities. Specifically, the analysis focuses predominantly on the 35–54 million Americans outside the credit mainstream. Attention is paid to the credit profiles and score distributions of this group as well as access to credit with and without alternative data. Then credit scoring model performance, as measured by the Kolmogorov-Smirnov (K-S) statistic, is examined. Several commercial grade scoring models were analyzed to determine model predictiveness. Finally, credit access is probed through a comparative analysis of new accounts opened by those with and without alternative data and an examination of acceptance rates for various communities.

The next step in the analysis examined the impact of removing the telecommunications and utility trades on the consumer's credit score. This analysis used a "VantageScore," a generic scoring model recently introduced by the three national credit bureaus (Experian, Equifax, and TransUnion). We used the model to derive a credit score for each consumer, with and without the utility or telecommunications trades. We then compared the distribution of these hypothetical scores with the score based on the consumer's existing credit file (that is, including the telecommunications and utility trades).[10]

The third step in the analysis focused on the impact that utility and telecommunications data would have on consumers' access to credit. We also compare the actual experiences of the consumers in the analysis and the validation files over a 12-month time period: March 31, 2005 (the date that the samples were drawn) and March 31, 2006 (the end of the performance period.) In particular, we compared the number and size of new accounts that were opened by consumers with an existing utility or telecommunications trades (the analysis sample) with the number and size of new accounts opened by otherwise similar consumers without such trades (the validation sample.)

That is, does this information impact credit behavior?

We then examined how the reporting of utility and telecommunications trades would affect the predictive power of several generic and industry-specific scoring models, and estimated the impact that this would have on both the availability and cost of credit.[11] Credit scores are the principal means by which credit is allocated in the United States to consumers. The scoring models considered in this report include:

- VantageScore, which predicts the probability that a consumer will have at least one 90-day delinquency on a new or existing account over a two-year period;
- TransRisk New Account, which predicts the probability that a consumer will have at least one 90-day delinquency on a new account over a two-year period;
- Two separate bankruptcy scores (one from a large financial institution and one from TransUnion[12]), which predict the probability that a consumer will declare bankruptcy in a two-year period; and
- A mortgage screening model developed by a major lender that exclusively relies on credit bureau data and predicts the probability that a consumer will have at least one 60-day delinquency on a mortgage account over a two-year period.[13]

We used these different models to score consumers with and without their utility and telecommunications trade line(s), and test the extent to which the resulting scores accurately predict consumer performance over a 12-month period: April 1, 2005 to March 31, 2006.[14] In general, if the presence of utility and telecommunications trades helps to improve the models' accuracy, this should ultimately lead to higher acceptance rates, lower delinquency rates, or a combination of the two.

The final step in the analysis explored how different demographic groups are likely to be affected. We first estimated the relative importance of energy utility and telecommunications trades for different demographic groups by examining each group's share of total trades. We next estimated the probable impact of such trades on acceptance rates within each group. The impact on acceptance rates again reflects the extent to which the predictive power of scoring models improves with the addition of utility and telecommunications trades.

LIMITATIONS

The analysis has a few limitations that should be noted. Most relate to the underlying characteristics of the analysis sample and the scoring models.

SAMPLING ISSUES

Because of the local nature of both utility and telecommunications providers, we knew from the start that the analysis sample would not be representative. In fact, 84 percent of our data on consumers with utility trades is concentrated in the three states—Illinois, Wisconsin, and Pennsylvania—where several large local utilities have begun to report their data. Likewise, 81 percent of the records with telecommunications data were from Pennsylvania and Texas.

The validation sample was designed to test the extent to which the analysis file is representative in other ways, for example, the number of trades in the consumer's files *excluding* telecommunications and utilities. The results of this analysis are presented in Appendix A. As discussed there, the analysis file appears to be broadly representative of all consumers in terms of their overall credit profiles and demographic mix. In general, however, consumers with utility or telecommunications trades seem to have stronger credit profiles than the general population, although this is less true for consumers with telecommunications trades.

The analysis sample is also limited in two other respects. The analysis file is necessarily restricted to consumers with either a utility or telecommunications trade. As a result, the findings they cannot be used to make inferences to the broader population, which includes an unknown number of consumers with neither a utility nor a telecommunications account. In addition, consumers in our analysis file are unlikely to have *all* of their utility and telecommunications trades reported. Despite the fact that many consumers pay both a utility and telephone bill, there is relatively little overlap between the two trade accounts in our sample. Furthermore, the telecommunications data are dominated by wireless accounts and may therefore underestimate the full effects of reporting both land lines and cell phone accounts. As a result, our analysis will likely underestimate the potential impact of full reporting.

MODELING ISSUES

It is important to recognize that many of our findings are based on the current versions of existing scoring models. In the event that utility and telecommunications data were more broadly reported, many scoring models would undoubtedly be optimized to reflect this important change. However, on the basis of an earlier analysis of a similar issue,[14] we believe that any biases introduced by this simplification will not affect our overall conclusions regarding the probable impact of full reporting. This limitation likely means our findings will tend to err on the side of caution, attenuating the actual impact we would expect with increased reporting of alternative trades.[16] ■

III. IMPACT ON CONSUMERS' CREDIT PROFILES

The full reporting of utility and telecommunications data would clearly affect the credit profiles of most consumers by adding one or more trade lines to their files. Logically, consumers with little, if any, "traditional" forms of credit would have the most to gain. (Simulations below suggest that this is in fact the case.) This section details the results of our estimation of the potential magnitude of these effects by examining the impact of the utility and telecommunications trades on the consumer's total number of trade lines as well as their credit score.

Table 3.1 compares the distribution of consumers by their total number of trade lines, with and without any utility or telecommunications trades.[17] The first two columns refer to the sample of 7.5 million consumers with an existing utility trade. Column 1 shows the distribution of these consumers on the basis of the total number of trades that currently appear in their credit files (that is, including any utilities.) Column 2 presents the counterfactual, the distribution of these same consumers when their utility trades are excluded. The last two columns present comparable information for the sample of 590,795 consumers with at least one fully reported telecommunications trade. Column 3 shows the distribution of these consumers based on the information currently appearing in their files (i.e., including any telecommunications), while column 4 illustrates what this distribution would have looked like had the telecommunications trades not been reported.

As shown in Table 3.1, the reporting of both utility and telecommunications trades has a sizable impact on the credit profiles of the consumers in our sample. For example, when utilities are included in consumers' credit reports (column 1), about 12 percent of the sample can be classified as having a thin credit file (fewer than three established trades). However, when the utility trades are removed from their credit records (column 2), the proportion of thin-file borrowers rises to 17 percent, and about 10 percent of the sample have no reported trade lines at all.[19]

The impact of adding the telecommunications trades is similar, although the impact on the share of consumers with no established trade lines is more pronounced. For example, when their telecommunications trades are reported (column 3), about 18 percent of the sample would be classified as having a thin credit file. However, when their telecommunications trades are removed (column 4), the share rises to 23 percent, and 14 percent of the sample would have had no established trades.

Table 3.1. Impact of Utilities and Telecom Trades on Total Number of Trades[21]

	Consumers with Utility Trades		Consumers with Telecom Trades	
Total Number of Trades	Including Utilities (#1) (%)	Excluding Utilities (#2) (%)	Including Telecoms (#3) (%)	Excluding Telecoms (#4) (%)
Thin-File				
0	-	9.6	-	14.0
1	7.7	4.0	13.4	4.9
2	4.1	3.4	5.0	4.1
Thick-File				
3	3.5	3.2	4.1	3.7
4	3.2	3.1	3.8	3.5
5	3.1	3.1	3.5	3.3
6	3.1	3.1	3.4	3.2
7+	75.2	70.5	66.8	63.3
All Consumers	100.0	100.0	100.0	100.0
Sample Size	7,519,020	7,519,020	590,795	590,795

Data Source: March 31, 2005 Credit Files for Analysis sample.

Differences in the impact of telecommunications and utility trades most likely reflect underlying differences in the populations with such trades. For example, a comparison of the underlying credit profiles of the two groups of consumers (columns 2 and 4) suggests that consumers with telecommunications trades have a smaller number of traditional trade lines than consumers who are responsible for utility payments. In this respect, consumers with telecommunications trades appear to be more similar to the general population than do consumers with utility trades (see Appendix A). Because it is easier to get a cell phone than to rent or buy a home, this pattern makes sense.

Figures 3.2c and 3.2d show the impact of adding the utility and telecommunications trades to the consumer's VantageScore. (This score ranges from 501 to 990, with higher scores signifying lower credit risks). Figures 3.2a and 3.2b show the distribution of consumers by the change they experience when adding their utility and telecommunications trade lines to their scores. In general, a change of more than 25 points in the VantageScore, or a change from an "unscoreable" to a "scoreable" situation, should be viewed as a significant change. Where along the score range the change occurs is also important. For instance, a consumer gaining 50 points and moving from 900 to 950 may gain little in practical terms relative to a consumer also gaining 50 points but moving from 650 to 700.

One would expect the reporting of utility and telecommunications data to increase the number of consumers who could be scored by increasing the their trade lines. However, there is no a priori reason to expect that the reporting of utility or telecommunications data will change a consumer's existing credit score in one direction as opposed to another. Although a good payment history on a larger number of trades will tend to increase a consumer's score, a poor payment history on additional trades would most likely reduce it.

Figure 3.2. Impact of Utilities and Telecommunications Trades on VantageScore
All Consumers

Figure 3.2a Impact of Utility Trades on VantageScore Change

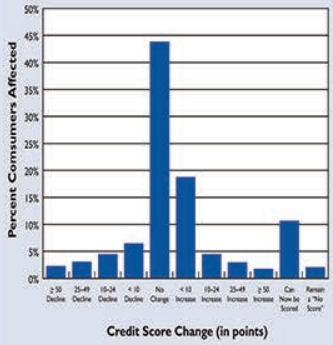


Figure 3.2c Impact of Utility Trades on VantageScore

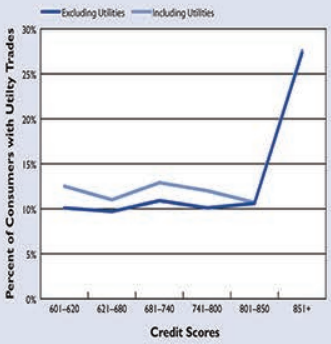


Figure 3.2b Impact of Telecom Trades on VantageScore Change

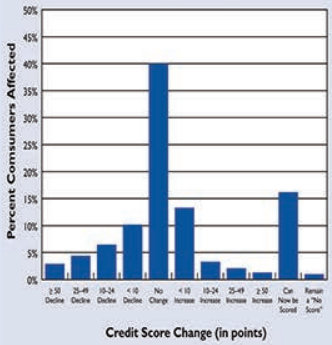
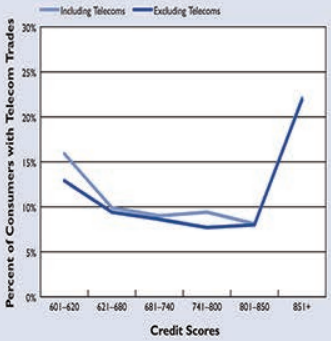


Figure 3.2d Impact of Telecom Trades on VantageScore



Source: March 31, 2005 Credit Files for Analysis sample.

"The impact of adding utility and telecommunications trades is considerably greater for thin-file consumers than for the population at large."

Adding utility data to the consumer's credit report decreases the proportion of consumers who cannot be scored, from about 12 percent to 2 percent. However, among consumers who could be scored without their utility trade lines, the share whose score increased by more than 25 points with the addition of the utility trades (4.6 percent) was about the same as the share whose score decreased by more than 25 points (5.2 percent). In fact, the inclusion of the utility data had little or no significant effect on about 69 percent of the sample, resulting in no change or changes less than 10 points. It should be kept in mind that lenders often place unscoreable consumers among the highest risk. That is, a share of the 12 percent would be treated as belonging to the lowest-risk tiers, given that they have little on which to base their decisions. (Some lenders of course will attempt to collect information to get a better sense of the applicant's risk, but this track is far more costly.)

Figure 3.3. Impact of Utilities and Telecommunications Trades on VantageScore Consumers with Less than 3 Traditional Trades

Figure 3.3a Impact of Utility Trades on VantageScore Change (Consumers with Less than 3 Traditional Trades)

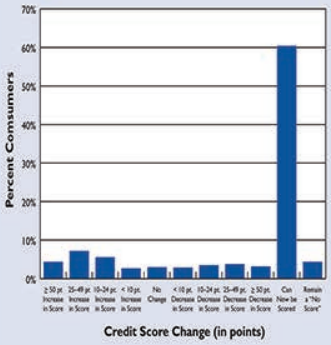


Figure 3.3c Impact of Utility Trades on VantageScore

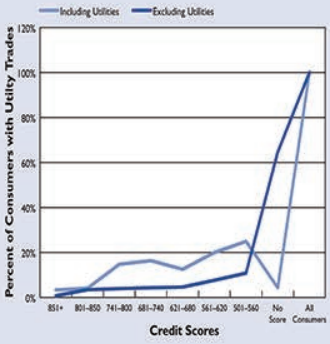


Figure 3.3b Impact of Telecom Trades on VantageScore Change (Consumers with Less than 3 Traditional Trades)

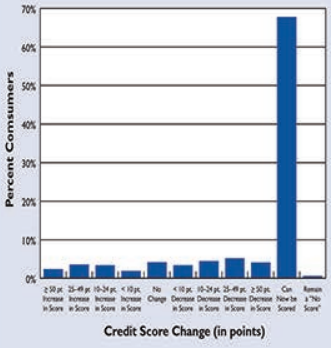
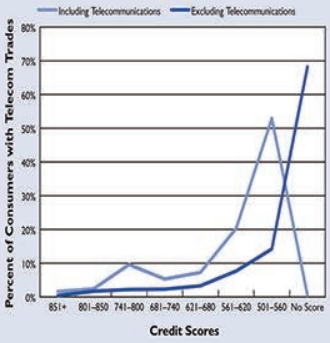


Figure 3.3d Impact of Telecom Trades on VantageScore



Source: March 31, 2005 Credit Files for Analysis sample.

Roughly comparable patterns can be observed in the sample of consumers with telecommunications data. Again, the primary impact of including telecommunications data appears to be on the proportion of consumers who cannot be scored, which drops from 17 percent to 1 percent. However, among the consumers who could be scored without their telecommunications data, the share who experienced an increase of more than 25 points in their score (3.2 percent) was only about one-half the proportion of consumers who experienced a decline (7.1 percent.) Although the number significantly affected was higher than it was for the utility data, telecommunications data had little or no effect on the credit scores of about 63 percent of the population.

Figure 3.3 presents comparable statistics for borrowers with less than three traditional trades (or more precisely, less than three trades, excluding any telecommunications and utility accounts.) This segment represents the population of most interest, as many of these borrowers have difficulty accessing mainstream credit. As expected, the impact of adding utility and telecommunications trades is considerably greater for thin-file consumers than for the population at large, and the primary effect is to increase the percentage of consumers who can be scored. For example, adding utility data reduced the percentage of thin-file consumers who could not be scored from about 65 percent to just 4 percent. The reporting of telecommunications data had an even greater effect, declining from 68 percent to less than 1 percent. ■

"The primary effect [of using alternative data] is to increase the percentage of consumers who can be scored"

IV. OBSERVED DIFFERENCES IN ACCESS TO CREDIT

All else equal, one would expect that the full reporting of utility and telecommunications data would increase access to credit by reducing the proportion of consumers with thin credit files and increasing the proportion of consumers who can be scored. Although we the impact on consumers with a well-established credit history is relatively modest, the impact on consumers with less than three traditional trades was quite pronounced.

To estimate the potential impact of the utility and telecommunications trades on the consumer's access to credit, we compare the actual experiences of consumers in the analysis and validation files over a 12-month period beginning April 1, 2005 and ending on March 31, 2006. Because consumers in the validation sample have no reported utility and telecommunications trades, they provide a convenient, although imperfect "control" for assessing the potential effects of full reporting.[20]

The results of this analysis are presented in Table 4.1. In addition to comparing the proportion of consumers who opened a new account within this period, we also looked at other indicators of credit use, including the average change in the consumer's total outstanding credit balance (i.e., credit use) and the average change in the consumer's aggregate credit limit. The first three columns in Table 4.1 describe the results for the three populations groups. The last three columns restrict the analysis to thin-file consumers.

Table 4.1. New Credit Accounts Opened February 2005 to January 2006

	All Borrowers			Thin-File (<3 *Traditional* Trades)		
	Consumers with Utility Trades (#1)	Consumers with Telecom Trades (#2)	Validation Sample (#3)	Consumers with Utility Trades (#4)	Consumers with Telecom Trades (#5)	Validation Sample (#6)
Pct with new accounts	50.92%	48.73%	42.21%	16.44%	16.42%	4.61%
Ave. no. trades opened	1.14	1.07	0.93	0.27	0.26	0.05
_ Total outstanding balance	+ $3956	+ $1466	+ $8489	+ $1972	+ $891	- $402
_ Total available credit	+ $6973	+ $3192	+ $12309	+ $2466	+ $1094	- $382
Sample size	6,211,323	504,481	3,785,681	1,036,396	113,240	1,030,357

Data Source: March 31, 2005 and March 31, 2006 Credit Files for Analysis Sample

In general, widespread reporting of utility and telecommunications data increases consumer access to credit. Although the proportion of consumers who opened a new account over the observation period was higher for all consumers with a fully reported utility or telecommunications trade, the impact was significantly greater for thin-file borrowers. For example, only about 5 percent of thin-file borrowers in the validation sample (column 6) opened a new account between April 1, 2005, and March 31, 2006, compared with 16 percent of thin-file consumers who had either a reported utility or telecommunications trade (columns 4 and 5, respectively).

Compared with thin-file consumers without such trades, those with a fully reported utility or telecommunications trades also experienced greater increases in their use of and access to credit. In fact, thin-file consumers with utility and telecommunications data increased their credit limits by about $2,500 and $1,100, respectively, over the 12-month period, while thin-file consumers without such trades experienced a small decline ($382). However, the pattern for all consumers shows the opposite effects, with larger increases observed for consumers in the validation sample. ■

"Thin-file consumers with utility and telecommunications data increased their credit limits"

V. IMPACT ON SCORING MODELS

Another way to assess the probable outcome of full reporting is to examine its impact on the reliability or ability to rank risk within the scoring models. In general, reporting utility and telecommunications trades should affect consumers' access to credit if the additional information provided improves the ability of credit issuers to identify a good credit risk. As shown in prior research, greater accuracy in estimating credit performance should lead to lower credit costs for lenders, higher acceptance rates, or some combination of the two.[21] Moreover, if better performance reflects better capacities of borrowers to pay, it limits over-indebtedness.

IMPACT ON PREDICTIVE POWER

To examine these potential effects, we relied on several commercial scoring models, including the VantageScore model; a generic new account model; two bankruptcy models; and a mortgage screening model Although none of these models specifically distinguishes telecommunications or utility trades from other types of accounts, the scores of each model will be affected by the consumer's performance on all reported trade lines, including any utility or telecommunications accounts.

We began by scoring consumers in the analysis file with and without their reported telecommunications and utility trades. We then used the resulting scores to rank consumers according to their predicted risk, and compared the different rankings with consumers' performance over a 12-month period (April 1, 2005, to March 31, 2006). The accuracy of the various scores was summarized by their Kolmogorov-Smirnov (K-S) statistic, a commonly used metric designed to capture a model's ability to distinguish between two different groups, in this case, performing and nonperforming accounts.[22] The K-S statistic ranges from 0 to 100, with higher values signifying a greater ability to distinguish between good and poor credit risks.

In calculating the KS statistics, we first assumed that consumers who could not be scored would be treated as a higher risk than consumers with the minimum applicable score. In reality, however, some credit issuers, primarily those lending for mortgages, would attempt to validate the credit-worthiness of no-score applicants by examining nontraditional sources of credit. Our analysis, therefore, may oversimplify the decision-making process of credit-issuers in some instances, such as for mortgages, and overstate the benefits that arise when consumers move from unscoreable to scoreable.

Table 5.1. Impact of Utilities and Telecommunications Trades on K-S Statistics: General Population Models

	Consumers with Utility Trades		Consumers with Telecom Trades	
Model	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms (#3)	Excluding Telecoms (#4)
VantageScore	1.098	1.000	1.085	1.000
TransRisk new account	1.051	1.000	1.048	1.000
TransRisk bankruptcy	1.135	1.000	1.214	1.000
Bankruptcy model II	1.138	1.000	1.262	1.000
Sample size	6,211,323	6 ,211,323	504,481	504,481

Data Source: March 31, 2005 and March 31, 2006 Credit Files for analysis sample.

With these caveats in mind, Table 5.1 shows the estimated impact of adding the utility and telecommunications trades on the predictive power of the various models (For reasons described below, the mortgage model has been treated separately.) To protect the proprietary nature of the models, the K-S statistics for each of the models has been scaled to equal 100 when the utility and telecommunications trades are excluded from the consumers' credit files. Values above 100 when the utility or telecommunications trades are included indicate a relative improvement in the model's predictive power.

As shown Table 5.1, adding utility and telecommunications data increases the overall accuracy of the scoring models by a significant amount.[23] For example, adding the data to the VantageScore model increases its overall K-S statistic by 9.8 percent and 8.5 percent, respectively. Results for the other general population models are similar, ranging from a 5 percent increase for the second generic model to nearly a 14 percent increase for the bankruptcy scores in the utility sample and increases of more than 20 percent for the bankruptcy scores in the telecommunications sample.

The improvement in the model's predictive power with the addition of the utility and telecommunications trades appears primarily to be driven by the greater ability to score previously unscoreable consumers, rather than to a better risk-ordering of those who can be scored without the addition of the alternative data. This is evident from comparing the results in Table 5.1 and 7, which are based on calculations from samples composed of only those who can be scored with or without the alternative data, and thus only captures the reordering effect from the addition of the new data. The greater lift (that is, increase in the KS statistic) in Table 5.1 when previously unscoreable consumers are scored and moved out of the greatest risk category. This reflects the fact that the average rate of serious delinquencies among such consumers is relatively low compared with the scoreable consumers at the bottom of the score distribution. Hence, these consumers do not belong (as a group) in the highest-risk category. For example, consumers who were unscoreable without their utility trades had a delinquency rate of 14 percent, which is only slightly greater than the rate observed among consumers with scores in the 680 to 740 range of the VantageScore, and well below the rates observed among consumers with lower scores (whose delinquency rates ranged between 33 percent and 60 percent).

As mentioned, also calculated changes in the K-S statistic for samples of consumers who could be scored with and without the alternative data. These calculations, thus, make no assumptions regarding how those with no score should be classified, but they do exclude those who would most benefit from the inclusion of the alternative data. Nonetheless, it is useful to explore

Table 5.2. Impact of Utilities and Telecommunications Trades on K-S Statistics: Excluding Unscoreables[24]

	Consumers with Utility Trades		Consumers with Telecom Trades	
Model	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms (#3)	Excluding Telecoms (#4)
VantageScore	1.022	1.000	1.012	1.000
TransRisk New Account	1.025	1.000	1.010	1.000
TransRisk Bankruptcy	1.005	1.000	0.987	1.000
Bankruptcy Model II	1.008	1.000	1.003	1.000
Sample Size	5,439,844	5,439,844	421,915	421,915

how the models' performance is affected when including alternative data for those who can be scored without it. These results are shown in Table 5.2.

Table 5.2 makes it clear that for those who can already be scored without the alternative data, we should expect, on average, only a modest improvement in score model performance (at least with current nonoptimized models). This should be expected given that, for instance, more than three-quarters of the consumers in the utility subsample used had seven or more traditional trade lines. Therefore, the addition of another (alternative) trade line for the average consumer should have little effect.

Because the purpose of the study is to determine whether and how the addition of alternative data in credit files can benefit those traditionally underserved by the mainstream financial sector, we now look at model performance for those with little or no traditional trade lines—the thin-file consumers.

As before, we first treated those with no score as the highest-risk consumers (they were placed at the bottom of the score distribution). In the absence of the utility and telecommunications data, only 36 percent and 32 percent, respectively, of such consumers registered a score for the VantageScore model. With the addition of the data, the number of no-scores declined to a minimal amount, and the model's ability to predict the credit performance of thin-file consumers increased dramatically.

As shown in Table 5.3, the K-S statistic for VantageScore model rose by more than a factor of 3 with the addition of the utility data and by more than a factor of 4 with the addition of the telecommunications trades. The results for the other models are roughly the same order of magnitude. These findings underscore the critical nature of such trades in evaluating the credit performance of thin-file borrowers.

Table 5.4 shows the change in model performance when scoring thin-file consumers who are scoreable with and without utility and telecommunications data, that is, when scoring consumers with one or two traditional trade lines. We see a larger average lift with the addition of the alternative data for the thin-file consumers than for the general sample results in Table 5.2, reflecting the greater importance of additional trade lines to consumers (and those trying to estimate their level of risk) with few trade lines. Again, we should expect a lift from adding utility and telecommunications data to the credit files of the thin-file consumers when the scoring models are optimized for such data.

Table 5.3. Impact of Utilities and Telecommunications Trades on K-S Statistics: Thin-File Borrowers Only

	Consumers with Utility Trades		Consumers with Telecom Trades	
Model	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms (#3)	Excluding Telecoms (#4)
VantageScore	3.294	1.000	4.281	1.000
TransRisk New Account	2.932	1.000	4.993	1.000
TransRisk Bankruptcy	3.358	1.000	5.297	1.000
Bankruptcy Model II	3.595	1.000	6.783	1.000
Sample Size	1,280,553	1,280,553	137,256	137,256

Data Source: March 31, 2005 and March 31, 2006 Credit Files for Analysis Sample

Table 5.4. Impact of Utilities and Telecommunications Trades on K-S Statistics: Thin-File Borrowers Only, Excluding Unscoreables

	Consumers with Utility Trades		Consumers with Telecom Trades	
Model	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms (#3)	Excluding Telecoms (#4)
VantageScore	1.078	1.000	1.021	1.000
TransRisk New Account	1.061	1.000	1.024	1.000
TransRisk Bankruptcy	1.035	1.000	0.978	1.000
Bankruptcy Model II	1.050	1.000	0.971	1.000
Sample Size[26]	369,903	369,903	36,506	36,506

These findings are consistent with what one would expect with the addition of alternative data; namely, that (1) the largest impact would be for those who become scoreable after adding the new data; (2) thin-file consumers who were scoreable without the new data would experience a smaller, but noticeable, impact; and (3) consumers with thick files would see relatively little change.

MORTGAGE SCREENING MODEL

Although the results are quite robust for the generic scoring models, applying the same approach to the mortgage screening models proved problematic. Because mortgage screening models are designed to predict the incidence of 60+ days mortgage delinquencies, the samples we used to estimate the K-S statistics were limited to consumers with mortgage trades at the beginning of the performance

period. Not surprisingly, all of the consumers in these subsamples had at least one established traditional trade (their mortgage), and the great majority had thick credit files. For example, 95.6 percent of mortgage holders in the utility sample had seven or more traditional trades (i.e., excluding utility trades), compared with 70.5 percent in an overall sample of consumers. Likewise, fewer than 1 percent of mortgage holders in the utility sample had thin credit files compared with about 17 percent in the overall sample.

Given that including utility and telecommunications data had relatively little impact on a model's ability to predict the performance of thick-file borrowers, it is therefore not surprising that these data had relatively little impact on the K-S statistics of the mortgage screening models, *on the basis of the observed performance of consumers with mortgages.* In fact, the addition of the utility data led to a 0.4 percent decline in the K-S statistic of a mortgage screening model designed for homebuyers, while the telecommunications data led to 0.9 percent decline.[27]

To gain a better understanding about how utility and telecommunications data could enhance a mortgage lender's ability to identify credit-worthy borrowers, we recalculated the K-S statistics for the mortgage screening models using an alternative performance measure: the incidence of any 90+ day delinquency. We based this analysis on the entire sample of consumers, whether or not they had a mortgage trade. The results of this analysis were similar to the generic scoring models. In particular, we found that utility and telecommunications data increased the K-S statistics of the homebuyers model by 13.4 percent and 3.2 percent, respectively. Although these results should be interpreted with caution—mortgage models are specifically designed to predict mortgage performance not performance across all trades—they nevertheless suggest that the improvements observed for the generic credit models are likely to apply to models specifically designed for mortgage loans.

ADDITIONAL RESULTS ON THE PREDICTIVE POWER OF ALTERNATIVE DATA

We would expect that alternative payment data would contain some information useful in predicting future payment outcomes. If an individual has been making his or her utility or telecommunications payments on time for a period of time, we would expect they would be more likely to make timely payments (in the present and the future) on a variety of their obligations compared with someone who had fallen behind on payments. That we see a rise in the K-S statistic in the overall samples or in the thin-file samples, and including or excluding the unscoreable populations, points to this. In addition, and more simply, we could look at the correlations between a serious delinquency on an alternative trade and a serious delinquency on a traditional trade.

Specifically, using the sample of consumers with utility trade lines who also had traditional trade lines, we calculated the correlation between a serious delinquency (90+ days) on a utility trade and on a traditional trade line between March 2004 and March 2005. We similarly calculated serious delinquencies for telecommunications trade lines. The respective correlations were .288 and .292 and, not surprisingly given the very large sample sizes, they were statistically significant.[28] The results indicate that a serious delinquency on either a utility or telecommunications trade is weakly to moderately correlated with a serious delinquency on a traditional trade. These results refute any notion that utility and telecommunications payments are unrelated to traditional payments. The correlation does not, however, explain whether alternative payments are a good predictor of future payments.

Table 5.5. Regression Results, Dependent Variable: Whether a Consumer Had a Serious Delinquency on Any Trade During March 2005 and March 2006 (Standard Errors in Parentheses)

	Consumers with Utility and Traditional Trades		Consumers with Telecom and Traditional Trades	
Variables	(#1)	(#2)	(#3)	(#4)
Constant	.082	.106	.110	.130
	(.0001)	(.0002)	(.0006)	(.0006)
Whether a Traditional (90+ DPD) Delinquency, March 04-March 05	.412	0.511	.424	0.485
	(.0004)	(.0004)	(.0014)	(.0014)
Whether a Utility (90+ DPD) Delinquency, March 04-March 05	.410			
	(.0005)			
Whether a Telecom (90+ DPD) Delinquency, March 04-March 05			.247	
			(.0017)	
R-Squared	0.3009	0.2136	0.2506	0.2143
Sample Size	5,631,146	5,631,146	436,140	436,140

The correlation between having a serious delinquency on a utility trade during March 2004 and March 2005 and having such a delinquency on any trade the following year is 0.42. Such a correlation for telecommunications delinquencies during is 0.32. The correlation for delinquencies on a traditional trade is 0.46. The correlation between a consumer's serious delinquency and serious delinquencies on a traditional trade, a utility trade, or a telecommunications trade are quite similar.

It could be the case that the predictive information alternative trades embody is already captured in the information from traditional trades, and therefore adding such alternative trades to traditional trades may not add any predictive power. To test this, we ran regressions to determine whether adding alternative trade information would improve predictability.

The results in Table 5.5 indicate that with the addition of the utility data, the predictive power or goodness of fit of this admittedly crude model rises by 40% as measured by the R-squared. With the addition of the telecommunications data, the goodness of fit of the model rises by 17% also as measured by the R-squared.[29]

Of course, this is only suggestive of how the addition of utility and telecommunications payment information would affect model fit in a reoptimized commercial-grade scoring model. A commercial model would be more sophisticated, take into account much more detailed information, and do a much better job of predicting. Nonetheless, it appears that utility and telecommunications payment data contain information that could be useful in predicting future payment outcomes.

IMPACT ON DELINQUENCY AND ACCEPTANCE RATES

In a competitive market, consumers could benefit from an increase in the accuracy of scoring models in two different ways. On the one hand, credit issuers could increase their acceptance rates and keep the rates that they charge the same. Increasing their acceptance rate without increasing rates and fees is possible because the default rate associated with a given acceptance rate will necessarily decline with an improvement in the model's predictive power. Alternatively, lenders could maintain their existing acceptance rates but lower their rates and fees. Again, a price reduction would be possible because the default rate that is associated with a given acceptance rate will decline with improvements in the model's predictive power. In short, the trade-off between the size of the lender's market and the performance of their portfolios becomes less steep.

Although it is difficult to predict the market outcome, the types of trade-offs that credit issuers face with full reporting of utility and telecommunications trades are illustrated in Tables 5.6 and 5.7. Although the data in the tables are based on the VantageScore model, results for the other models are generally similar and are presented in Appendix B. As before, we have assumed that lenders would put consumers who cannot be scored in the highest-risk category.[30] This assumes that the unscoreable population is essentially excluded from consideration (given that they are put at the bottom of the risk distribution) but nonetheless count as potential borrowers/consumers (their presence is felt in the numerator of the acceptance rate).

Table 5.6 shows how the performance associated with a given acceptance rate could improve with the addition of utility and telecommunications data.[31] For example, suppose that a credit issuer wished to maintain an acceptance rate of about 50 percent, a rate that is more or less in line with the current acceptance rates among credit card issuers. With this target acceptance rate, serious delinquencies would fall by about 22 percent (from 2.3 to 1.8 percent) with the

Table 5.6. Serious Delinquencies by Target Acceptance Rates: VantageScore Model

	Consumers with Utility Trades		Consumers with Telecom-Telecommunications Trades	
Acceptance Rate	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms-Telecommunications	Excluding Telecoms-Telecommunications
30%	0.90%	1.10%	1.10%	1.30%
40%	1.20%	1.50%	1.70%	2.20%
50%	1.80%	2.30%	3.30%	4.60%
60%	3.00%	4.20%	7.40%	10.10%
70%	5.40%	8.10%	12.40%	16.20%
80%	9.50%	13.80%	15.90%	20.90%
90%	13.80%	17.70%	18.20%	21.60%

addition of utility data, and by about 28 percent (from 4.6 to 3.3 percent) with the full reporting of telecommunications accounts. In a highly competitive market, the savings associated with these declines would ultimately be passed through to consumers in the form of lower rates.

Table 5.7 takes the opposite perspective, and shows what would happen to acceptance rates if issuers wished to maintain their current level of risk (as measured by the incidence of serious delinquencies) and expand their business base. For example, acceptance rates could rise from 54.9 to 60.4 percent with the addition of utility data using a targeted delinquency rate of about 3 percent—the approximate average for credit cards. With the addition of the telecommunications data, acceptance rates could rise from about 44.9 to 49.0 percent without increasing projected losses.

As noted earlier, many credit issuers attempt to create alternative credit histories for thin-file borrowers by turning to non-traditional credit sources. As a result, the findings presented in Tables 5.3 and 5.4 may tend to overestimate the actual impact on acceptance rates, but they may do so only slightly. Nevertheless, our analysis clearly illustrates the potential impact of such reporting, and the value it can bring to underserved markets. ■

Table 5.7. Acceptance Rates by Targeted Delinquency Rates: VantageScore Model

	Consumers with Utility Trades		Consumers with Telecom Trades	
Delinquency Rate %	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms (#1)	Excluding Telecoms (#2)
2	52.4	47.2	43.4	38.8
3	60.4	54.9	49.0	44.9
4	65.4	59.6	52.6	48.4
5	69.1	63.1	55.3	51.0
6	72.0	65.7	57.4	53.3
7	74.5	67.9	59.4	55.0

VI. DEMOGRAPHIC IMPACTS

Figure 6.1 shows how changes in acceptance rates would vary across different demographic groups[32] assuming that the risk tolerance of lenders remains the same. To simplify the presentation, we again present our results for just one model—the VantageScore model— and use a "targeted" delinquency rate (3 percent) that approximates the average for credit cards. However, as before, the results are much the same when other models or risk cut-offs are used.[33]

In general, minorities, lower-income groups, and younger (18 to 25 years old) and older (66+ years) consumers are most affected by the addition of utility and telecommunications data. Again, although the results are roughly similar for the utility and telecommunications trades, the largest impact is associated with the addition of the utility data. The addition of the utility trades would increase acceptance rates for both black and Hispanic borrowers by about 21 percent, more than twice the increase observed for whites (see Figure 6.1a). Likewise, acceptance rates would rise by about 25 percent for consumers earning less than $20,000 per year (see Figure 6.1b), by about 13 percent for consumers under the age of 25, and by 14 percent for those over age 65 (see Figure 6.1c). We were curious whether the 65+ group was evidence of "widow effect," where a widow is left with little credit history because bills had been in her husband's name. We did not, however, find any difference by gender.

Figure 6.1. Impact on Acceptance Rates by Demographic Group:
(assumes 3 percent serious delinquency rate)

Figure 6.1a Consumers by Race with Utility Trades
(Assumes 3 percent Serious Delinquency Rate)

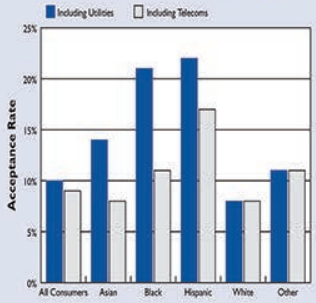


Figure 6.1c Consumers by Age with Utility and Telecom Trades
(Assumes 3 percent Serious Delinquency Rate)

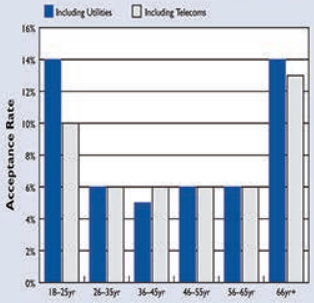


Figure 6.1b Consumers by Income
with Utility Trades
(Assumes 3 percent Serious Delinquency Rate)

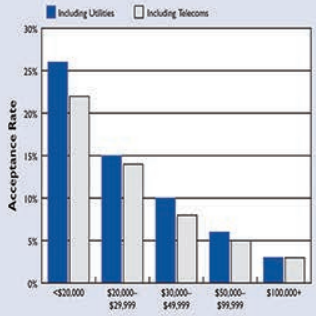


Figure 6.1d Consumers by Homeowner Status
with Utility and Telecom Trades
(Assumes 3 percent Serious Delinquency Rate)

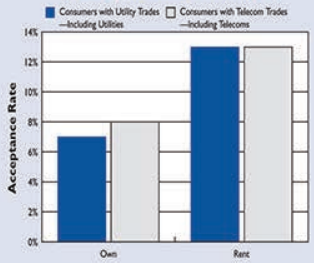
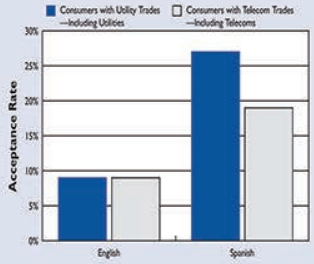


Figure 6.1e Consumers by Language Preference
with Utility and Telecom Trades
(Assumes 3 percent Serious Delinquency Rate)



Source: March 31, 2005 Credit Files for Analysis sample.

Table 6.2. Reported Trades by Borrower Characteristics

	Consumers with Utility Trades			Consumers with Telecom Trades		
	<3 traditional trades (%)	Mean Number of Trades	Utilities as Percent of Total Trades	<3 traditional trades (%)	Mean Number of Trades	Telecoms as Percent of Total Trades
All	17%	17.32	9%	23%	15.04	7%
Race						
Asian	20%	17.02	8%	18%	17.54	6%
Black	28%	12.46	11%	48%	7.91	13%
Hispanic	32%	13.24	11%	40%	10.16	11%
Other	16%	18.12	9%	20%	16.21	7%
White	14%	18.35	9%	19%	16.21	7%
Gender						
F	14%	18.19	9%	22%	15.33	7%
M	12%	18.44	9%	16%	16.74	7%
Age						
18–25	24%	11.11	13%	36%	8.88	12%
26–35	10%	19.19	9%	18%	16.29	7%
36–45	9%	21.57	8%	13%	18.85	6%
46–55	9%	20.81	8%	12%	19.21	6%
56–65	8%	20.19	8%	10%	19.39	6%
66+	18%	13.43	11%	18%	13.25	8%
Income						
<$20,000	31%	11.01	14%	38%	9.13	12%
$20,000–29,999	20%	13.92	11%	24%	12.49	9%
$30,000–$49,999	13%	16.88	9%	16%	15.51	7%
$50,000–$99,999	7%	20.89	8%	8%	20.54	5%
$100,000+	4%	24.22	7%	4%	24.24	5%

"Minorities, lower-income consumers, and the young and the old are more likely to be thin-file borrowers."

Renters, who presumably are less in the financial mainstream than homeowners, saw their acceptance increase at nearly twice rate as homeowners with the addition of the utility data. Renters may also find improving their credit files particularly important if they hope to become eventual homeowners.

Finally, language preference reveals that those who prefer Spanish as their primary language experience a 27 percent increase in their acceptance with the addition of the alternative data. This is probably a better measure than ethnicity of the underserved immigrant population from Latin America. Although similar patterns for all conditions are observed for the telecommunications data, the estimated impact were not as large.

Differences in the estimated impact on different demographic groups reflect differences in their underlying credit profiles. As shown in Table 6.2, minorities, lower-income consumers, and the young and the old are more likely to be thin-file borrowers. As a result, the addition of utility and telecommunications trades to their credit records will have a larger effect on their overall credit profiles. ■

VII. SUMMARY AND POLICY IMPLICATIONS

The results of our analysis lend strong support to the suggestion that the systematic reporting of telecommunications and utility trades would benefit consumers and increase their access to low-cost credit. Assuming that our sample is reasonably representative of all consumers with such trades, the impact is likely to be large.

The primary effect of fully reporting energy utility and telecommunications data appears to be on the number of consumers who could be scored. Based on the tri-bureau VantageScore model, the percentage of unscoreable consumers would decline from 13 percent to 2 percent when adding utility data. Likewise, adding telecommunications data reduces the number of unscoreable consumers from about 17 percent to 1 percent.

Scoring models and credit scores are relatively unaffected by additional information on utility and telecommunications trades for consumers who can be scored without them. In other words, for consumers with a relatively thick credit files, the addition of these trade lines has little, if any, effect—either positive or negative—on their credit scores or their access to credit. As a result, it seems safe to assert that relatively few consumers would be harmed by the full reporting of such data.

In contrast, the impact on otherwise unscoreable consumers would be significant. For example, based on the VantageScore model, we estimate that overall acceptance rates could rise by as much as 10 percent with the full reporting of utility and telecommunications trades. Significantly larger gains would go to minorities, low-income groups, and consumers at the two extremes of the age continuum—the relatively young (18 to 25 years) and the relatively old (over 65).

ENCOURAGING ALTERNATIVE DATA REPORTING

In our view, these findings provide a strong public policy rationale for encouraging the full reporting of utility and telecommunications payment data to consumer reporting agencies. The net result of full reporting should be positive for consumers and business alike. Thin-file consumers would stand to gain by having a more accurate assessment of their credit-worthiness, and credit issuers would stand to gain by enhancing their ability to expand their markets without a concurrent increase in risk.

PERC surveyed the members of the National Association of Regulated Utility Commissions (NARUC) in 2005, and identified four states where the transfer of customer data to third parties was statutorily prohibited. Although these laws were written with other concerns in mind—in most cases they are privacy rules—they clearly preclude sharing customer data with consumer reporting agencies (CRAs). We believe that lawmakers in those states should carefully review those laws in light of the findings reported here. Any privacy concerns should be carefully weighed against the demonstrated social and economic

benefits. Specifically, we encourage state lawmakers in those few states to carve out an exemption in existing law for reporting payment data—not detailed account information such as customer proprietary network information or CPNI—to accredited consumer reporting agencies.

The NARUC survey identified regulatory uncertainty as the primary policy barrier to sharing energy utility and telecommunications data with CRAs. Given that the majority of states have no law on the books either precluding or permitting data sharing with CRAs, and given an environment of heightened sensitivity to data privacy and data security concerns, regulators are unwilling to provide energy utility and telecommunications firms with explicit permission (especially written permission) to share customer payment data with CRAs. In fact, in some cases, despite the absence of a statutory prohibition, some regulators have told inquiring energy utility and telecommunications firms that they were not permitted to share customer payment data with CRAs. In these states, we advocate the passage of a law clearly permitting the sharing of customer data with CRAs.

PRESERVE VOLUNTARY REPORTING

When considering data-sharing legislation, it is important to preserve the voluntary nature of the national credit reporting system. Mandating the reporting of energy utility, telecommunications, or other alternative data will result in a radical and disruptive paradigm change to the world's most successful credit reporting regime. The decision of any energy or telecommunications providers to become a "full file reporter" must ultimately be driven by a combination of each firm's self-interest (in reducing account delinquencies)[34] and by the understanding that doing so helps to promote access to mainstream credit markets for previously underserved groups.

Interestingly, for years, energy utility and telecommunications firms have been major consumers of credit reports from the big three national credit bureaus. Most of these firms, however, either report only negative information (delinquencies, defaults, and collections), or do not report at all. Such an imbalance in using payment history information, but not contributing to it, is particularly costly to those consumers who have no traditional payment histories, given that they will be building no positive payment histories by using the utility or telecommunications services, and they will likely be charged a relatively high deposit because they have no payment history. For some uses of consumer credit files, such as for marketing and prescreening lists, there is a principle of reciprocity, where companies wishing to use the information must have contributed to it. But these benefits may hold little

value to entities, such as utilities, that provide services typically considered necessities and often face little or no competition.

Nonetheless, as the value of consumer payment data from nontraditional sources becomes more evident, efficient market responses may emerge by data aggregators and credit bureaus to bring the nontraditional data online. As potential furnishers of nontraditional data realize how providing payment data not only helps their bottom line, but also their customers, they will likely become more interested in supplying payment data. However, these market responses can happen when statutory prohibitions are removed or amended, and more important, when regulatory and legislative uncertainties surrounding the transfer of such data are cleared up.

Without sufficient credit history, it is impossible to begin the process of asset building and wealth creation.

REPORTING ENHANCES DEVELOPMENT OF COMMUNITIES

The sociodemographic analysis of the thin-file and unscoreable population confirmed beliefs about the characteristics of this group. It is composed largely of members of ethnic minorities, many of whom are economically disadvantaged and are recent immigrants. Many of these individuals reside in "domestic emerging markets"—urban markets and poorer, industrial and rural areas. For those living in such areas, the ability to improve one's life often depends on access to credit. Without sufficient credit history, it is impossible to purchase a car for traveling to work, to secure a student loan for the college of choice, to secure a home mortgage loan or a small business loan to begin the process of asset building and wealth creation.

A recent study analyzed credit scores, credit use, and delinquency patterns for low- to moderate-income individuals (LMIs) for 50 metropolitan areas.[35] Key findings from this analysis of more than 14 million partial credit files during a one-year period indicate high variance across metropolitan areas in credit use, score distribution, and credit management. Most relevant for this study was the finding that the portion of borrowers with extremely weak credit scores (scores lower than 75 percent of the total population) was considerably higher in urban markets than the national average. For low- to moderate-income persons in urban areas, nearly 41 percent have credit scores in the bottom quarter for the nation. Given the concentration of LMI households in most urban areas, and the prevalence of automated underwriting among mainstream lenders, this translates to a substantial barrier to accessing affordable capital to build assets in these urban markets.

The results from this study offer great promise for community development in domestic emerging markets, especially in urban areas. Not only are the credit scores of a majority of thin-file and unscoreable Americans improved by using alternative data, but credit access for LMI borrowers is dramatically improved. Thin-file borrowers with one or more alternative trade lines in their credit files accessed capital at four times the rate of thin-file borrowers without any alternative trade lines. In short, preliminary evidence strongly suggests that using alternative data in consumer credit reports makes a difference in credit access and fairness in lending. Enhanced access to affordable, mainstream credit—albeit just one part of the solution—can greatly assist with the economic development of urban markets.

Given the size of this population, and its risk profile when alternative data are considered, in an environment of pervasive alternative data reporting everything changes. First, if—and this is a big if—alternative data are reported in sufficient quantity in the near term (currently, a small but growing minority of energy utility and telecommunications firms fully report customer payment data to one or more credit bureaus), then credit bureaus, analytics firms, and lenders will have the data necessary to build new alternative scoring models or optimize existing scoring models. In short, lenders will have the tools to process the newly available information to make credit decisions. Empowered with new tools and information, lenders can profitably expand into previously overlooked markets—markets that may even become competitive.

Perhaps most important, millions of credit-worthy borrowers in urban areas who previously had to rely on check-cashing, payday lenders, or other predatory lenders can gain access to affordable mainstream credit. The miracle of instant credit can palpably affect the lives and life chances of millions, making possible the dream of homeownership and the ability to secure a secure a small business loan to launch a new enterprise, two avenues for asset-building. In an environment of pervasive alternative data reporting, the landscape of consumer banking in urban areas should fundamentally change to the benefit of those who live there. This, in turn, can have deep and systematic affects on community development and asset-building, resulting in improved opportunity and quality of life. ■

VIII. FUTURE RESEARCH DIRECTIONS

Evidence presented in this study supports the use of alternative data as one means to help bridge the credit information gap for millions of thin-file and unscoreable Americans. Although alternative data can be held out as a promising potential solution to the problem of too little credit information, it is not an easy solution.

First, there is a chicken-and-egg quality to alternative data. That is, consumer reporting agencies are not actively exhorting energy utility and telecommunications firms to fully report data because their major clients—large financial institutions—are not demanding alternative data and alternative scoring models. Lenders are not demanding alternative data and alternative scoring models because so little alternative data is fully reported. By one estimate, just under 5 percent of all credit files have one or more alternative trade lines, and alternative data composes less than 1 percent of all trade lines in a major credit bureau's database.

There does appear to be interest in using alternative payment data in the market. One example is Payment Reporting Builds Credit (PRBC), which uses self-reported (but verified) alternative payment information, thus sidestepping legal and regulatory barriers and accessing payment information not in standard credit reports. However, the advantage of this model (self-reported data) also likely limits its impact in bringing useful alternative data online.[36] Fair Isaac's Expansion Score and First American's Anthem model are scoring models specifically designed to use alternative payment data. These two models rely on data from

niche aggregators, and remain somewhat of a black box. However, that a small number of important lenders are beginning to use them in credit decision suggests that a demand for alternative scoring models exists. Demand will likely grow as more alternative data come online. For instance, while the reporting of utility and telecommunications payments is far from pervasive, the TransUnion database nonetheless had more than 8 million consumer files with at least one alternative payment reported for at least a year as of March 2005, making this study possible.

It is clear, however, that much more needs to be done to jump-start a cycle of alternative data use and reporting, leading to its broad use. Data furnishers—in this case utility and telecommunications companies—must be convinced that reporting data to CRAs, and assuming Fair Credit Reporting Act data furnisher obligations, is in their best interest. Anecdotal evidence suggests that fully reporting customer data to credit bureaus, and consistently communicating the benefits of reporting to customers, can lead to a dramatic reduction in delinquencies and charge-offs. At a 2005 Brookings Urban Markets Initiative roundtable on alternative data and credit scoring, WE Energies and Verizon stated that fully reporting customer data, directly or in part, led to a substantial reduction in delinquencies.[37] Similarly, Nicor Gas reported a 20 percent reduction in delinquencies one year after it began fully reporting customer data to TransUnion.[38]

Data furnishers—in this case utility and telecommunications companies—must be convinced that reporting data to credit reporting agencies, assuming Fair Credit Reporting Act guidelines, is in their best interest.

A systematic survey of energy utility and telecommunications firms on their experience reporting data to consumer reporting agencies could identify hurdles to reporting. From a policy perspective, the results of such a survey and analysis could serve as the basis for a national outreach program to expedite an environment in which alternative data are pervasively reported. Such an outcome could go a long way toward helping untold millions of thin-file and unscoreable Americans build assets and create wealth in a sustainable fashion. ■

APPENDIX A. SAMPLE CHARACTERISTICS

This appendix compares the characteristics of the analysis file with the characteristics of the validation sample. Table A1 compares the demographic characteristics of the consumers in each sample. Table A2 compares their credit profiles excluding their utility and telecommunications trades. Table A3 presents the distribution of the samples by state. In presenting the statistics on the analysis file, consumers with utility trades are distinguished from those with telecommunications trades. Although there is a small overlap between the two groups, they are essentially separate groups and have been treated as such throughout this report.

DEMOGRAPHIC DIFFERENCES

Table A1 compares the samples based on the race, gender, age and income of the consumer. In general, the three population groups look remarkably similar. While consumers with telecommunications trades tend to have somewhat lower incomes and a higher proportion of males compared to validation sample, their other characteristics are about the same. Likewise, consumers with utility trades tend to have a higher proportion of males, a lower proportion of Hispanics and a higher proportion of blacks than the population at large (as measured by the validation sample), but again, these differences are not pronounced.

CREDIT DIFFERENCES

Table A2 compares the characteristics of the samples on the basis of credit profiles of consumers. In making these comparisons, we removed the utility and telecommunications trade lines from the credit reports of consumers contained in the analysis file. Removing these trade lines enabled us to compare the different samples on an "apples to apples" basis, and assess the extent to our analysis file is representative of the broader population of consumers in terms of their underlying credit profiles.

Again, the three population groups look fairly similar, although some different differences can be observed. In general, consumers with either a utility or telecommunications trades have somewhat stronger credit profiles than the general population as measured by their total number of trades (excluding utilities and telecommunications) as well as their credit scores. Although the differences are relatively modest for consumers with telecommunications trades, they are more pronounced for consumers with a reported utility. This pattern is not surprising given that the latter primarily reflect household heads or individuals living on their own.

Appendix Table A1. Distribution of Samples by Demographic Characteristics

	Consumers with Utility Trades (%)	Consumers with Telecommunications Trades (%)	Validation Sample (%)
Race			
Asian	3.6%	1.7%	4.2%
Black	8.5	5.8	6.3
Hispanic	8.9	11.7	12.1
Other	11.9	10.2	9.5
White	67.1	70.6	68.0
Total	100.0	100.0	100.0
Gender			
F	40.8	46.8	50.4
M	59.2	53.2	49.6
Total	100.0	100.0	100.0
Age			
18–25	1.7	2.3	2.6
26–35	15.5	16.8	14.3
36–45	23.4	24.4	21.3
46–55	24.5	24.1	25.3
56–65	16.1	15.3	17.2
66+	18.8	17.1	19.1
Total	100.0	100.0	100.0
Income			
<$20,000	17.8	25.3	18.6
$20,000–$29,999	9.0	11.5	10.1
$30,000–$49,999	18.9	20.3	20.0
$50,000–$99,999	36.5	30.7	34.0
$100,000+	17.8	12.3	17.3
Total	100.0	100.0	100.0
Sample Size	7,519,020	590,795	3,985,525

GEOGRAPHIC DIFFERENCES

Table A3 presents the distribution of the three population groups by state. As expected, the samples are not representative in terms of their geographic location. Consumers with utility trades are concentrated in Illinois (44 percent), Pennsylvania (16 percent) and Wisconsin (24 percent.) The telecommunications sample is also primarily in Pennsylvania (69 percent) and Texas (13 percent).

Appendix Table A2. Distribution of Samples by Credit Profiles of Consumer: Excluding All Utility and Telecommunications Trades

	Consumers with Utility Trades (%)	Consumers with Telecommunications Trades (%)	Validation Sample (%)
% Distribution by No. of Traditional Trades			
0	9.6	14.0	13.1
1	4.0	4.9	13.9
2	3.4	4.1	5.5
3	3.2	3.7	3.9
4	3.1	3.5	3.4
5	3.1	3.3	3.2
6	3.1	3.2	3.0
7+	70.5	63.3	53.9
All Consumers	100	100	100
% Distribution by VantageScore[a]			
851+	27.3	21.9	20.6
801–850	10.6	8.0	9.4
741–800	10.1	7.7	11.2
681–740	10.9	8.6	12.3
621–680	9.7	9.4	9.4
561–620	10.1	12.9	9.0
501–560	8.7	14.6	6.7
No Score	12.6	16.9	21.4
All Consumers	100	100	100
Sample Size	7,519,020	590,795	3,985,522

a The score was obtained by removing the utility and telecommunications trades from the consumer's credit files

Appendix Table A3. Distribution of Samples by State

State	Consumers with Utility Trades (%)	Consumers with Telecommunications Trades (%)	Validation Sample (%)
Alabama	0.1	0.1	1.6
Alaska	0.0	0.0	0.2
Arizona	2.4	0.2	2.0
Arkansas	0.1	1.4	1.0
California	0.7	0.8	12.7
Colorado	0.2	0.2	1.7
Connecticut	3.6	0.1	1.1
Delaware	0.0	0.1	0.3
DC	0.0	0.0	0.2
Florida	1.0	1.2	6.6
Georgia	0.3	0.4	2.9
Hawaii	0.0	0.0	0.4
Idaho	0.0	0.0	0.4
Illinois	44.6	0.3	3.3
Indiana	0.4	0.9	2.1
Iowa	0.6	0.0	1.0
Kansas	0.1	1.5	1.0
Kentucky	0.1	0.1	1.4
Louisiana	0.1	0.1	1.6
Maine	0.0	0.0	0.5
Maryland	0.2	0.4	1.9
Massachusetts	0.1	0.2	2.0
Michigan	0.7	2.7	3.5
Minnesota	0.8	0.1	1.7
Mississippi	0.1	0.1	1.0
Missouri	0.2	1.9	2.0
Montana	0.0	0.0	0.3
Nebraska	0.0	0.0	0.6
Nevada	0.2	0.1	0.9
New Hampshire	0.0	0.0	0.4
New Jersey	0.2	0.7	2.9
New Mexico	0.1	0.1	0.6
New York	0.3	0.7	6.3
North Carolina	0.3	0.3	3.0
North Dakota	0.0	0.0	0.2
Ohio	0.4	1.3	3.9
Oklahoma	0.1	0.5	1.3
Oregon	0.1	0.1	1.3
Pennsylvania	15.9	68.7	3.7
Rhode Island	0.0	0.0	0.3
South Carolina	1.1	0.1	1.4
South Dakota	0.0	0.0	0.2
Tennessee	0.2	0.1	2.0
Texas	0.6	12.6	8.2
Utah	0.0	0.0	0.8
Vermont	0.0	0.0	0.2
Virginia	0.2	0.3	2.5
Washington	0.2	0.1	2.3
West Virginia	0.1	0.0	0.6
Wisconsin	23.5	1.3	1.3
Wyoming	0.0	0.0	0.2
No Data	0.0	0.0	0.2
Sample Size	7,519,020	590,795	3,985,522

APPENDIX B. DETAILED MODEL RESULTS

Appendix Table B1. Serious Delinquencies by Target Acceptance Rates: VantageScore, Excluding Unscoreables

	Consumers with Utility Trades		Consumers with Telecom Trades	
Acceptance Rate	Including Utilities (#1) (%)	Excluding Utilities (#2) (%)	Including Telecom (#1) (%)	Excluding Telecom (#2) (%)
30	0.9	1.0	0.9	1.1
40	1.1	1.3	1.3	1.5
50	1.5	1.7	2.2	2.4
60	2.4	2.7	4.4	4.7
70	4.2	4.5	9.1	9.1
80	7.8	8.1	14.7	14.5
90	12.9	13.1	18.9	18.8

Source: PERC

Appendix Table B2. Acceptance Rates by Targeted Delinquency Rates: VantageScore, Excluding Unscoreables

	Consumers with Utility Trades		Consumers with Telecom Trades	
Acceptance Rate	Including Utilities (#1) (%)	Excluding Utilities (#2) (%)	Including Telecom (#1) (%)	Excluding Telecom (#2) (%)
2	56.6	53.9	48.3	46.4
3	64.4	62.7	54.8	53.7
4	69.5	68.1	58.8	57.8
5	72.9	72.0	61.8	61.0
6	75.9	75.0	64.2	63.7
7	78.3	77.5	66.3	65.8

Source: PERC

Appendix Table B3. Serious Delinquencies by Target Acceptance Rates: TransRisk New Account Model

	Consumers with Utility Trades		Consumers with Telecom Trades	
Acceptance Rate (%)	All Trade (%)	Excluding Utility Trades (%)	All Trades (%)	Excluding Telecom Trades (%)
	All			
30	0.9	1.1	1.2	1.3
40	1.2	1.5	1.8	2.1
50	1.9	2.3	3.8	4.6
60	3.5	4.1	7.9	10.1
70	5.9	7.9	10.8	15.9
80	9.5	13.2	14.8	20.5
90	13.7	17.6	17.9	21.9
	Excluding Unscoreables			
30	0.9	1.0	1.0	1.1
40	1.1	1.3	1.3	1.5
50	1.5	1.8	2.2	2.5
60	2.4	2.7	4.9	5.0
70	4.4	4.7	9.7	9.7
80	8.2	8.4	14.8	14.7
90	13.1	13.2	19.3	19.0

Source: PERC

Appendix Table B4. Acceptance Rates by Targeted Delinquency Rates: TransRisk New Account Model

	Consumers with Utility Trades		Consumers with Telecom Trades	
Delinquency Rate	All Trade	Excluding Utility Trades	All Trades	Excluding Telecom Trades
	All			
2	50.7	47.2	41.2	38.8
3	57.3	55.0	45.9	44.7
4	62.5	59.7	50.6	48.4
5	66.4	62.9	53.5	50.8
6	70.6	65.8	56.0	53.0
7	73.3	68.1	58.1	54.8
	Excluding Unscoreables			
2	56.8	53.2	48.5	45.7
3	64.0	61.9	54.1	52.7
4	68.5	67.2	57.7	57.1
5	71.6	70.8	60.1	59.9
6	74.5	74.0	62.6	62.5
7	77.0	76.5	64.6	64.7

Source: PERC

Appendix Table B5. Bankruptcies by Target Acceptance Rates: TransRisk Bankruptcy Model

	Consumers with Utility Trades		Consumers with Telecom Trades	
Acceptance Rate (%)	All Trades (%)	Excluding Utility Trades (%)	All Trades (%)	Excluding Telecom Trades (%)
30	0.07	0.06	0.07	0.07
40	0.07	0.06	0.07	0.11
50	0.08	0.09	0.14	0.25
60	0.12	0.19	0.25	0.52
70	0.21	0.38	0.41	0.83
80	0.38	0.74	0.60	1.44
90	0.69	1.28	1.02	1.76
Excluding Unscoreables				
30	0.06	0.06	0.06	0.07
40	0.06	0.06	0.06	0.07
50	0.07	0.07	0.12	0.13
60	0.11	0.11	0.28	0.27
70	0.21	0.22	0.52	0.50
80	0.41	0.41	0.75	0.75
90	0.70	0.74	1.17	1.18

Source: PERC

Appendix Table B6. Acceptance Rates by Targeted Bankruptcy Rates: TransRisk Bankruptcy Model

	Consumers with Utility Trades		Consumers with Telecom Trades	
Bankruptcy Rate (%)	All Trade (%)	Excluding Utility Trades (%)	All Trades (%)	Excluding Telecom Trades (%)
0.25	72.7	63.9	60.6	50.0
0.50	85.0	74.3	74.4	59.1
0.75	90.9	80.0	84.5	67.6
1.00	96.3	84.4	88.7	73.1
Excluding Unscoreables				
0.25	72.1	71.9	58.3	58.9
0.50	83.7	83.5	68.8	69.7
0.75	90.3	90.0	79.5	79.7
1.00	94.8	94.9	86.0	86.2

Source: PERC

Appendix Table B7. Bankruptcy Rates by Target Acceptance Rates: Bankruptcy Model II

	Consumers with Utility Trades		Consumers with Telecom Trades	
Acceptance Rate (%)	All Trades (%)	Excluding Utility Trades (%)	All Trades (%)	Excluding Telecoms Trades (%)
30	0.03	0.03	0.04	0.05
40	0.06	0.06	0.07	0.12
50	0.08	0.11	0.12	0.25
60	0.14	0.21	0.22	0.47
70	0.23	0.39	0.37	0.76
80	0.40	0.69	0.56	1.23
90	0.70	1.29	0.90	1.76
Excluding Unscoreables				
30	0.03	0.03	0.03	0.03
40	0.04	0.04	0.06	0.06
50	0.07	0.07	0.14	0.15
60	0.13	0.13	0.28	0.27
70	0.23	0.24	0.45	0.46
80	0.39	0.40	0.67	0.68
90	0.64	0.66	1.00	1.03

Source: PERC

Appendix Table B8. Acceptance Rates by Targeted Bankruptcy Rates: Bankruptcy Model II

	Consumers with Utility Trades		Consumers with Telecom Trades	
Bankruptcy Rate (%)	All Trades (%)	Excluding Utility Trades (%)	All Trades (%)	Excluding Telecoms Trades (%)
0.25	71	62	62	50
0.50	84	74	77	61
0.75	91	81	86	70
1.00	95	86	92	76
Excluding Unscoreables				
0.25	72	71	58	59
0.50	85	84	73	72
0.75	93	92	83	82
1.00	97	97	90	89

Source: PERC

Appendix Table B9. Impact on Acceptance Rates by Demographic Group (TransRisk New Account): (Assumes 3% Serious Delinquency Rate)

	Consumers with Utility Trades		Consumers with Telecom Trades	
	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms (#1)	Excluding Telecoms (#2)
All Consumers	1.04	1.00	1.03	1.00
Race				
Asian	1.05	1.00	1.02	1.00
Black	1.06	1.00	1.02	1.00
Hispanic	1.08	1.00	1.03	1.00
Other	1.04	1.00	1.03	1.00
White	1.04	1.00	1.03	1.00
Gender				
F	1.04	1.00	1.03	1.00
M	1.04	1.00	1.03	1.00
Age				
18–25	1.08	1.00	1.04	1.00
26–35	1.03	1.00	1.02	1.00
36–45	1.03	1.00	1.02	1.00
46–55	1.03	1.00	1.02	1.00
56–65	1.03	1.00	1.02	1.00
66+	1.05	1.00	1.04	1.00
Income				
<$20,000	1.09	1.00	1.07	1.00
$20,000–$29,999	1.06	1.00	1.05	1.00
$30,000–$49,999	1.05	1.00	1.03	1.00
$50,000–$99,999	1.03	1.00	1.02	1.00
$100,000+	1.02	1.00	1.01	1.00

Source: January 31, 2005 Credit Files for Analysis sample

Appendix Table B10. Impact on Acceptance Rates by Demographic Group (TransRisk Bankruptcy): (Assumes 0.25% Bankruptcy Rate)

	Consumers with Utility Trades		Consumers with Telecom Trades	
	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms (#1)	Excluding Telecoms (#2)
All Consumers	1.14	1.00	1.21	1.00
Race				
Asian	1.19	1.00	1.17	1.00
Black	1.39	1.00	2.67	1.00
Hispanic	1.43	1.00	1.70	1.00
Other	1.12	1.00	1.18	1.00
White	1.10	1.00	1.16	1.00
Gender				
F	1.09	1.00	1.18	1.00
M	1.08	1.00	1.11	1.00
Age				
18–25	1.17	1.00	1.36	1.00
26–35	1.07	1.00	1.13	1.00
36–45	1.06	1.00	1.09	1.00
46–55	1.06	1.00	1.08	1.00
56–65	1.06	1.00	1.07	1.00
66+	1.12	1.00	1.12	1.00
Income				
<$20,000	1.32	1.00	1.51	1.00
$20,000–$29,999	1.16	1.00	1.24	1.00
$30,000–$49,999	1.09	1.00	1.13	1.00
$50,000–$99,999	1.05	1.00	1.06	1.00
$100,000+	1.02	1.00	1.03	1.00

Appendix Table B11. Impact on Acceptance Rates by Demographic Group (Bankruptcy Model II): (Assumes 0.25% Bankruptcy Rate)

	Consumers with Utility Trades		Consumers with Telecom Trades	
	Including Utilities (#1)	Excluding Utilities (#2)	Including Telecoms (#1)	Excluding Telecoms (#2)
All Consumers	1.14	1.00	1.25	1.00
Race				
Asian	1.18	1.00	1.21	1.00
Black	1.32	1.00	2.40	1.00
Hispanic	1.36	1.00	1.69	1.00
Other	1.13	1.00	1.21	1.00
White	1.10	1.00	1.19	1.00
Gender				
F	1.10	1.00	1.24	1.00
M	1.09	1.00	1.14	1.00
Age				
18–25	1.19	1.00	1.58	1.00
26–35	1.08	1.00	1.19	1.00
36–45	1.06	1.00	1.12	1.00
46–55	1.07	1.00	1.10	1.00
56–65	1.07	1.00	1.09	1.00
66+	1.13	1.00	1.14	1.00
Income				
<$20,000	1.29	1.00	1.54	1.00
$20,000–$29,999	1.16	1.00	1.27	1.00
$30,000–$49,999	1.10	1.00	1.17	1.00
$50,000–$99,999	1.06	1.00	1.07	1.00
$100,000+	1.03	1.00	1.04	1.00

Source: PERC

ENDNOTES

1. See Michael Turner, et al., *The Fair Credit Reporting Act: Access, Efficiency and Opportunity.* (Washington, DC: The National Chamber Foundation, June 2003), available at **http://www.infopolicy.org/pdf/fcra_report.pdf**

2. Such changes in the actual value of the scores are short-run effects of bringing new data online. Because the scores represent some probability of default, and the new data would change this probability for each score (consumers would be resorted), the scores would need to be rescaled so that a score of 700 before the addition of the new data meant the same thing as a score of 700 with the new data. To gauge the longer-term effects of bringing new data online, one should focus on the results that show that the addition of the new data helps to better sort consumers by risk. We find that better sorting leads to increased access to credit, particularly among low-income consumers, ethnic minorities, the young, and the old.

3. Pari Sabety and Virginia Carlson, "Using Information to Drive Change: New Ways of Moving Markets" (Washington: Brookings Institution, 2003).

4. Dana Nottingham opening keynote speech at the 2006 UMI Forum

5. Michael A. Turner, "Giving Underserved Consumers Better Access to the Credit System: The Promise of Non-traditional Data." Information Policy Institute. New York City. July 2005.

6. Credit providers and commercial scoring firms have also developed scoring models for thin-file borrowers. For example, Fair Isaacs & Co. (FICO) recently introduced a FICO Expansion Score using nontraditional credit data. According to Fair Isaacs, the score "can effectively predict risk for the growing number of U.S. consumers that fail to receive a traditional FICO score due to non-existent or 'thin' credit histories." Although FICO does not reveal the underlying drivers of its score, nontraditional credit data generally capture the consumer's performance on obligations such as rent-to-own agreements. For more information, see **www.fairisaac.com/fairisaac/solutions/FICO+Expansion+Score/Expansion+Score+Overview**.

7. *Giving Underserved Better Access to the Credit System: The Promise of Non-Traditional Data.* (New York: Information Policy Institute, July 2005)

8. This statistic is based on the credit records of approximately 4 million randomly selected consumers in the validation sample. See Appendix A. Since some consumers are not included in credit bureau files (e.g., they have no established credit and have never been reported by a collection agency), 13 percent is most likely a lower bound estimate.

9. TransUnion and financial institutions providing the scores did not conduct the demographic analysis, and do not have this sort of sociodemographic data in their credit files.

10. None of the models in this study has been optimized specifically for utility or telecommunications data, something that will undoubtedly occur as the reporting of such data increases. The models instead treat these trades as general trades.

11. Our approach was similar to one employed in an earlier Information Policy Institute study, which examined the impact of deleting certain types of derogatory data from consumers' credit files. See "The Fair Credit Reporting Act: Access, Efficiency, and Opportunity" (Washington: Information Policy Institute, June 2003).

12. TransRisk Bankruptcy model.

13. The mortgage screening model is based entirely on data found in the consumer's credit report and contains no information on the characteristics of the mortgage itself (e.g., loan-to-value ratio). It is used as an initial screen to process loans, as opposed to credit decision tool.

14. Although most scoring models use a 24-month performance period, we used a 12 month period to capture a larger number of consumers with an established telecommunications or utility trade at the beginning of the performance period (March 31, 2005.) The number of providers reporting such trades has increased significantly in the past two years, and we wanted to capture as many consumers as possible. Even so, because many wireless companies began reporting in mid- to late 2005, our sample will exclude many individuals who now have a reported utility or telecommunications trade.

15. Giving Underserved Better Access to the Credit System: The Promise of Nontraditional Data (New York: Information Policy Institute, July 2005), available online **www.infopolicy.org/pdf/nontrad.pdf**

16. The nonoptimized models do, generally, a better job separating the good risks from the bad risks with the inclusion of the alternative data. Therefore, we take this performance as the floor of what we should expect from models reoptimized for this data.

17. Some consumers have more than one reported utility or telecommunications trade. Although they are treated as a single category in Table 1, multiple utility or telecommunications accounts are reflected in the consumer's total number of trades.

18. Total number of trades includes both the number of alternative trades and traditional trades.

19. In order to be selected for our sample, a consumer had to have at least one fully reported utility or telecommunications trade. Thus, by definition, their current credit profiles (Columns 1 and 3 in Table 2) will include at least one reported trade line.

20. Ideally, any control sample would be restricted to consumers with an established, but unreported telecommunications or utility trade. However, it was impossible to determine the extent to which consumers in the validation sample have such accounts. If one assumes that consumers who have such accounts have stronger credit profiles than those who do not, our comparisons may overestimate the marginal impact of reporting utility and telecommunications trades.

21. See Michael Turner et al, The Fair Credit Reporting Act: Access, Efficiency & Opportunity Part II. (New York: The Information Policy Institute, September 2002), available at **www.infopolicy.org/pdf/institute_fcra_ptII.pdf**

22. The performance measure used to assess the accuracy of a given model was geared to the specific purpose of that model, although we limited the performance period to 12 months to capture as many consumers as possible in our analysis file. For example, the new account model is designed to predict the probability that a consumer will experience a 90-day delinquency on a new account over a two-year period. In assessing the impact on the model, we based our analysis on the occurrence of at least 90-day delinquency on a new account between April 1, 2005, and March 31, 2006. Likewise, our assessment of two bankruptcy models was based on the number of consumers who experienced a bankruptcy within the observation period. Thus, while our performance period differs, the performance measure used to assess the impact of the utility and the telecommunications trades on a given model was the same as that used to construct the model.

23. In general, increases of more than 10 percentage points in a model's K-S statistic are considered significant by model developers.

24. These calculations are based on subsamples consisting of individuals who had scores with and without the alternative data (utility or telecommunications trades). These subsamples, therefore, consisted of individuals with at least one traditional trade.

25. These sample sizes correspond to the VantageScore model since scoreablity differs across models.

26. These sample sizes correspond to the VantageScore model since scoreablity differs across models.

27. The lender also has screening models designed for refinancing, as well as for thin-file consumers and CRA loans. The results observed for these models are similar to those described in the text.

28. The p-values were less than .001.

29. Because the dependent variable is dichotomous, we also ran a logit regression and found that the goodness-of-fit of the models (Nagelkerke R-Squared) rose by 40 percent and 17 percent, respectively, with the addition of the alternative utilities and telecommunications data.

30. Results when the calculations are limited to consumers who can be scored with or without their utility and telecommunications trades are presented in Appendix B. In general, the marginal impact of the utility and telecommunications trades is considerably smaller when this restriction is imposed.

31. For a given acceptance rate, the rate of serious delinquencies that is observed for consumers with utility trades is lower than it is for consumers with telecommunications trades. This pattern is consistent with our earlier finding that consumers in the utility sample generally have stronger credit profiles than consumers with telecommunications trades.

32. The socio-demographic data appended to the indivdual credit files were generated by Acxiom from a combination of data sources including, self-reported sources, estimates from some of the individual's characteristics, extrapolation from census data, and public record information.

33. See appendix B for results for additional results based on other score models.

34. TransUnion, "TransUnion Case Study: How reporting helped Nicor Gas reduce bad debt." (Chicago, Il: TransUnion, 2002)

35. Matthew Fellowes, "Where is the Asset Building Opportunity?: A Profile of Credit Utilization and Management in 50 Metros." Presented at CFED Asset Building Conference, Phoneix, AZ. Sept. 2006.

36. Its impact is limited by the number of people who utilize its service and by the fact that individuals can choose which payment information they would like to include. It is likely that consumers will want to only include the payment histories which paint them in the best light, thus biasing the picture of themselves they present to users of the information.

37. For a complete transcript of the event, see **www.brookings.edu/metro/umi/events/20051215_paid.htm**

38. TransUnion, "TransUnion Case Study: How Reporting Helped Nicor Gas Reduce Bad Debt" (Chicago: TransUnion, 2002).

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LETTER SUBMITTED BY SENATOR REED

July 12, 2018

Senator Mike Crapo, Chairman
Senator Sherrod Brown, Ranking Member
Senate Committee on Banking, Housing & Urban Affairs
U.S. Senate
Washington, DC 20510

Re: S. 2362, the Control Your Personal Credit Information Act of 2018

Dear Senator Crapo and Senator Brown:

The undersigned consumer groups write in support of S. 2362, the Control Your Personal Credit Information Act of 2018. S. 2362 would amend the Fair Credit Reporting Act to give consumers, not credit bureaus or banks, the ultimate decisionmaking power over our credit reports. It addresses a paradox repeatedly pointed out in the aftermath of the Equifax data breach – that the credit bureaus hold vast amounts of sensitive information about hundreds of millions of American consumers, which they sell for hefty profits, yet we have very little control over how this information is used or disseminated. S. 2362 provides this control to consumers.

S. 2362 requires that credit bureaus first obtain the consumers' permission in order to release their credit reports and scores to lenders, insurers, and others. Requiring permission to access credit reports is neither new nor overly burdensome. For decades, the FCRA has required employers to obtain consumers' permission to use credit and consumer reports for employment purposes. The State of Vermont requires lenders to obtain consumers' permission to access reports, and credit appears not to have been hampered in that state.

As an additional measure to prevent identity theft, S.2362 requires the common-sense step of requiring consumers to provide proof of identity to the credit bureau when granting permission to access a credit report or score, using the standard in Section 610(a) of the FCRA, 15 U.S.C. § 1681h(a). This is the same section of the FCRA that establishes the proof of identity requirements when consumers order their own credit reports, such as through www.annualcreditreport.com, and the same type of proof would be required. Given that consumers must provide proof of identity to obtain their own credit report, it is illogical and unreasonable for the CRAs to argue that it is too burdensome to require this same documentation to prove their identity when credit or insurance is being sought. The goal is the same – to protect the security of the consumer's credit report information and prevent identity theft.

As for claims that this would make unavailable web-enabled credit and insurance applications, that is simply not true. Authentication can all be done online, the same way consumers can order their credit report online through www.annualcreditreport.com. If it's good enough for consumers ordering their own reports, it's good enough for them in order to prevent identity theft when applying for credit or insurance online. As for instant retail credit and auto financing, these are in-person transactions where identity validation could be conducted using actual identity documents, such as a driver's license. Finally, we expect that the credit bureaus would

develop new authentication measures to make the process more seamless, just as they have developed credit "locks" as a new measure.

As for the proposed revision to FCRA Section 604(c)(3), this is also intended to give consumers more control over their own information. Currently, the ability of lenders and insurers to use credit reports for marketing "firm offers" of credit - which are not very firm at all, being little more than advertising – has resulted in huge amounts of unwanted junk mail generated using personal private information. Switching from an opt-out to an opt-in system with affirmative written consent doesn't limit options; it gives consumers the right and ability to decide whether to accept use of their credit reports and scores for marketing.

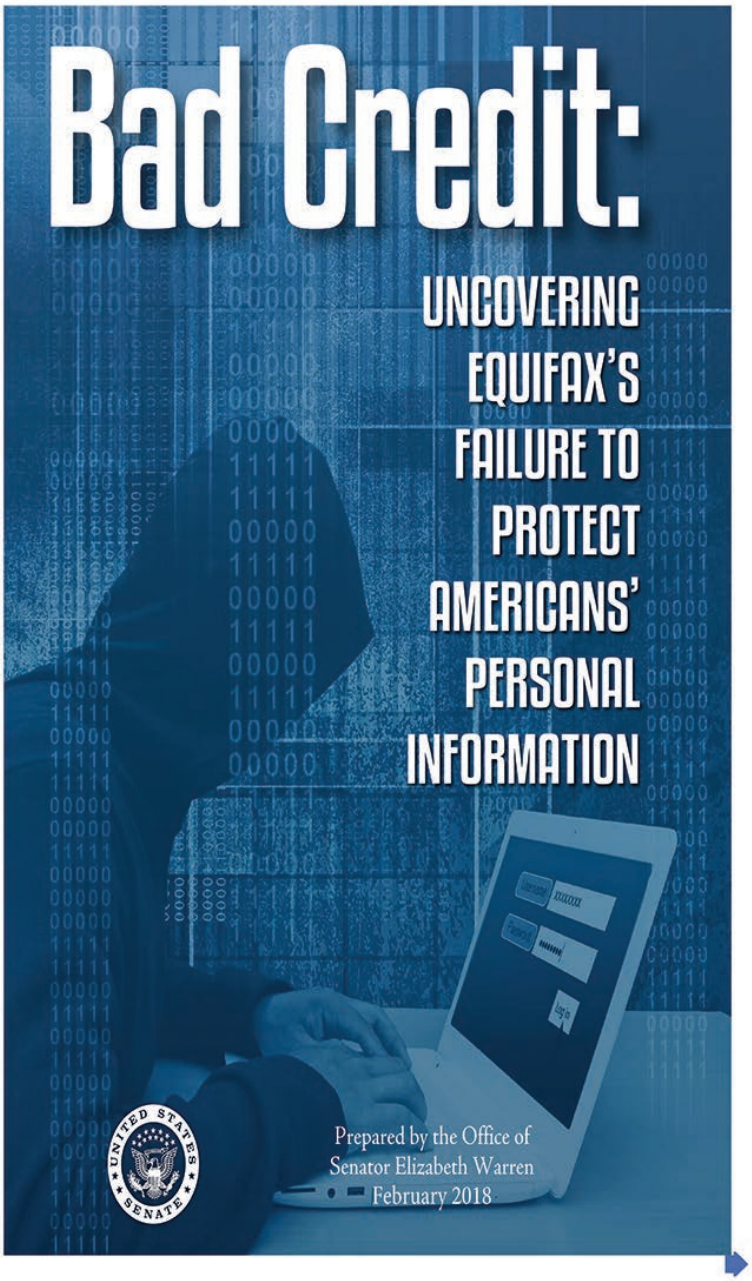
Thank you for your attention. If you have any questions about this letter, please contact Chi Chi Wu (cwu@nclc.org or 617-542-8010).

Sincerely,

Americans for Financial Reform
Consumer Action
Consumer Federation of America
Consumers Union
National Association of Consumer Advocates
National Consumer Law Center (on behalf of it low-income clients)
Public Citizen
U.S. PIRG

cc: Senator Jack Reed

REPORT SUBMITTED BY SENATOR WARREN



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Executive Summary

Equifax, one of the nation's largest credit reporting agencies, revealed on September 7, 2017, that the company had allowed an extraordinary breach of personal information. Sensitive information belonging to over 145 million Americans was exposed as a result of the breach – one of the largest and most significant data security lapses in history.

One week after Equifax revealed the breach, Senator Elizabeth Warren opened an investigation into the causes, impacts, and response to the exposure of millions of Americans' personal data. She questioned Equifax executives in Senate hearings, consulted outside experts, and sent letters containing dozens of questions to Equifax, to federal regulators, and to other credit rating agencies. The information they provided, and information obtained from additional sources, allowed the staff to reach a series of robust and important findings. This report presents the results of Senators Warren's Equifax investigation. It finds that:

- **Equifax Set up a Flawed System to Prevent and Mitigate Data Security Problems.** The breach was made possible because Equifax adopted weak cybersecurity measures that did not adequately protect consumer data. The company failed to prioritize cybersecurity and failed to follow basic procedures that would have prevented or mitigated the impact of the breach. For example, Equifax was warned of the vulnerability in the web application software Apache Struts that was used to breach its system, and emailed staff to tell them to fix the vulnerability – but then failed to confirm that the fixes were made. Subsequent scans only evaluated part of Equifax's system and failed to identify that the Apache Struts vulnerability had not been remediated.

- **Equifax Ignored Numerous Warnings of Risks to Sensitive Data.** Equifax had ample warning of weaknesses and risks to its systems. Equifax received a specific warning from the Department of Homeland Security about the precise vulnerability that hackers took advantage of to breach the company's systems. The company had been subject to several smaller breaches in the years prior to the massive 2017 breach, and several outside experts identified and reported weaknesses in Equifax's cyber defenses before the breach occurred. But the company failed to heed – or was unable to effectively heed – these warnings.

- **Equifax Failed to Notify Consumers, Investors, and Regulators about the Breach in a Timely and Appropriate Fashion.** The breach occurred on May 13, 2017, and Equifax first observed suspicious signs of a problem on July 29, 2017. But Equifax failed to notify consumers, investors, business partners, and the appropriate regulators until 40 days after the company discovered the breach. By failing to provide adequate information in a timely fashion, Equifax robbed consumers of the ability to take precautionary measures to protect themselves, materially injured investors and withheld market-moving information, and prevented federal and state governments from taking action to mitigate the impacts of the breach.

- **Equifax Took Advantage of Federal Contracting Loopholes and Failed to Adequately Protect Sensitive IRS Taxpayer Data.** Soon after the breach was announced, Equifax and the IRS were engulfed in controversy amid news that the IRS was signing a new $7.2 million contract with the company. Senator Warren's investigation revealed that Equifax used contracting loopholes to force the IRS into signing this "bridge" contract, and the contract was finally cancelled weeks later by the IRS after the agency learned of additional weaknesses in Equifax security that potentially endangered taxpayer data.

- **Equifax's Assistance and Information Provided to Consumers Following the Breach was Inadequate.** Equifax took 40 days to prepare a response for the public before finally announcing the extent of the breach – and even after this delay, the company failed to respond appropriately. Equifax had an inadequate crisis management plan and failed to follow their own procedures for notifying consumers. Consumers who called the Equifax call center had hours-long waits. The website set up by Equifax to assist consumers was initially unable to give individuals clarity other than to tell them that their information "may" have been hacked – and that website had a host of security problems in its own right. Equifax delayed

their public notice in part because the company spent almost two weeks trying to determine precisely which consumers were affected by the breach – but then failed to provide consumers with any specific information to determine if their data was breached. And while Equifax continues to publicly state only that data was "accessed," the company has confirmed that the data was exfiltrated – stolen – from their systems and downloaded by the hackers. Equifax appeared to be more focused on using the breach as a profit-making opportunity for other company services rather than providing redress to consumers.

- **Federal Legislation is Necessary to Prevent and Respond to Future Breaches.** Equifax and other credit reporting agencies collect consumer data without permission, and consumers have no way to prevent their data from being collected and held by the company – which was more focused on its own profits and growth than on protecting the sensitive personal information of millions of consumers. This breach and the response by Equifax illustrate the need for federal legislation that (1) establishes appropriate fines for credit reporting agencies that allow serious cybersecurity breaches on their watches; and (2) empowers the Federal Trade Commission to establish basic standards to ensure that credit reporting agencies are adequately protecting consumer data.

I. INTRODUCTION

On September 7, 2017, the massive credit reporting company Equifax publicly revealed a breach of the company's computer systems – described as "one of the largest risks to personally sensitive information in recent years" – that exposed data from over 145 million Americans to criminal hackers.[1] The company indicated that a vast trove of sensitive data – including social security numbers, credit card numbers, passport numbers, and driver's license numbers – may have been compromised. The incident was the fifth recent data breach of Equifax or its subsidiaries that endangered American's personal information.[2]

A subsequent internal investigation released by Equifax revealed additional information: that the company first became aware of the breach in July 2017; that the first breach occurred months earlier, in May 2017; and that the cause of the breach was a vulnerability in a web-application software, Apache Struts, that was used by Equifax and many other companies.[3]

Equifax announced a series of actions when the company publicly revealed the breach or soon thereafter, including monitoring of consumer credit files; the ability to access, review, and lock Equifax credit files; an insurance policy that covers out-of-pocket expenses stemming from identity theft; and ongoing review for misuse of consumers' social security numbers.[4] The company also announced on September 15, 2017, that two top executives responsible for the company's cybersecurity were immediately "retiring,"[5] and on September 26, 2017, announced the retirement of CEO Richard F. Smith.

Consumer concerns about the Equifax breach were particularly stark because the company – along with the two other large credit reporting agencies, Experian and TransUnion – occupy a unique place in the financial world: they obtain and use massive amounts of data on millions of consumers, but consumers have little to no power over how this data is collected, how it is used, or how it is kept safe.

As a result of these concerns, Senator Warren opened an investigation into the causes of, response to, and impact of the Equifax data breach. She sent several letters to Equifax seeking information; she questioned the former Equifax CEO in a Senate hearing; she wrote to Experian and TransUnion seeking information on their cybersecurity practices; she wrote to federal regulators seeking information on their authority to prevent and respond to cybersecurity breaches; she wrote to the Internal Revenue Service with Senator Ben Sasse to get information and answers surrounding the agency's decision to award a contract to Equifax to verify taxpayer identities; her staff reviewed internal investigations of the Equifax breach conducted by the cybersecurity firm Mandiant; and her staff consulted with independent cybersecurity experts.[6] This report presents the results of Senator Warren's detailed investigation of the Equifax cybersecurity breach.

II. FINDINGS

A. Equifax Failed to Take Adequate Steps to Prevent the Data Breach

1. Equifax Set up a Flawed System to Prevent and Mitigate Data Security Problems

This investigation finds that the breach was made possible because Equifax adopted weak cybersecurity measures that failed to protect consumer data – a symptom of what appeared to be the low priority afforded cybersecurity by company leaders. The CEO at the time of the breach, Richard Smith, testified that despite record profits in recent years, Equifax spent only a fraction of its budget on cybersecurity – approximately 3 percent of its operating revenue over the last three years.[7] In contrast, Equifax paid nearly twice as much in dividends to shareholders.[8]

Cybersecurity experts consulted by Senator Warren staff indicated that a large company that holds sensitive data, such as Equifax, should have multiple layers of cybersecurity. Equifax should have had (1) frequently updated tools to prevent hackers from breaching their systems; (2) controls that limited hackers' ability to move throughout their systems in the event of an initial breach; (3) restrictions on hackers' ability to access sensitive data in the event of an initial breach; and (4) procedures to monitor and log all unauthorized access in order to stop the intrusion as quickly as possible. Despite collecting data on hundreds of millions of Americans without their permission, Equifax failed to fully and effectively adopt any of these four security measures.

This investigation identified the following weaknesses in Equifax's cybersecurity:

- **Faulty Patch Management Procedures:** For many vulnerabilities that arise in its software and applications, Equifax only has to deploy a software "patch" that will fix the vulnerability and restrict access to the susceptible system. It's like putting a Band-Aid on a cut – simple, effective, and cheap. Yet Equifax let numerous software vulnerabilities sit un-patched for months at a time, leaving weaknesses through which hackers could gain access.[9] The failure to fully deploy a free Apache Struts patch led directly to the breach that compromised the data of millions of Americans.[10] Equifax failed to effectively use these simple, low-cost patches to protect consumer data.[11] In a briefing provided to Banking Committee staff, Equifax explained how this happened: they were warned of the vulnerability, and emailed staff to fix it.[12] But not all staff received this email, meaning not all necessary updates were in place – and Equifax failed to perform appropriate checks that would have identified this egregious error.[13] A subsequent security scan only covered part of Equifax's system, missing that the Apache Struts vulnerability was still present.[14]

- **Feeble Monitoring of Endpoint and Email Security:** Hackers often exploit weaknesses in the security of individual users of a system – for example, with spear phishing attacks over e-mail. In order to detect attacks on its system, Equifax must monitor laptops and other network devices that have access to its systems. But Equifax failed to adopt strict endpoint and email security measures.[15] While Equifax has now indicated that they are making improvements to their cybersecurity measures, it is too late to prevent the breach that put over 145 million Americans at risk.

- **Exposure of Sensitive Information:** In addition to adopting weak external security measures that allowed hackers to breach its systems, Equifax also failed to effectively secure sensitive consumer information.[16] When a bank locks its doors at night, it doesn't leave the money on the front counter in the assumption that nobody will break in. It locks the cash in the vault. Equifax, on the other hand, retained sensitive consumer information on easily accessible systems. Once the hackers exploited the Apache Struts vulnerability and gained access to Equifax's system, they found a treasure trove of consumer information at their fingertips.

- **Weak Network Segmentation:** Equifax also failed to put security measures in place that would prevent hackers from jumping from insecure, internet-facing systems to backend databases that contain more valuable data.[17] In other words, putting your valuables in a vault doesn't do much good if you forget to lock it. Equifax's network

segmentation measures failed to keep hackers from accessing consumer information because the company did not adopt adequately strict measures to protect valuable data.[18]

- **Inadequate Credentialing:** Equifax's cybersecurity failures extended to their internal security. Each user on Equifax's system receives a set of privileges. Under a strict security standard, Equifax would limit access to the most critical databases to just a handful of necessary users. This would protect the company from internal attacks and further bolster the company's overall data security regime. After gaining access to Equifax's system, hackers then acquired user credentials – a username and password – and accessed a huge quantity of sensitive information using just those credentials.[19] The company did not adopt adequately strict security measures to properly restrict user access to sensitive data.[20]

- **Logging:** Equifax neglected the use of robust logging techniques that could have allowed the company to expel the hackers from their systems and limited the size and scope of the data breach.[21] Logging is a simple but crucial cybersecurity technique in which companies monitor their systems, continuously logging network access in order to identify unauthorized users. Logging cannot necessarily prevent a breach, but just as a security camera can monitor access to a bank and allow a quick response when a break-in is identified, a robust monitoring system can identify and catch a hacker more quickly, allowing security to shut down the system and prevent future access. Equifax allowed hackers to continuously access sensitive data for over 75 days, in part because the company failed to adopt effective logging techniques and other security measures.[22]

Equifax was making huge profits but failing to protect consumers' data safety and security. Equifax adopted ineffective cybersecurity measures for sensitive data belonging to millions of Americans. As a company that has "data on approaching a billion people," and "manage[s] massive amounts of very unique data," as CEO Rick Smith put it two weeks after learning of the breach, Equifax failed to take the necessary efforts to protect that data.[23] While Equifax has found no evidence that this information has been sold, their actions put millions at risk of identity theft for the rest of their lives.[24] Equifax's goal, as stated by its CEO just weeks before he disclosed the breach, was to go from "$4 billion in revenue to $8 billion" in approximately 5 years.[25] Equifax prioritized growth and profits – but did not appear to prioritize cybersecurity.

2. Equifax Ignored Numerous Warnings of Risks to Sensitive Data

The Equifax data breach did not come out of the blue. The company had ample warning of potential risks to its systems and potential weaknesses. Equifax was subject to several smaller breaches in the years prior to the massive 2017 breach and received a specific warning from the Department of Homeland Security about the Apache Struts vulnerability that was used by the hackers to breach the company's systems. But Equifax failed to heed – or was unable to effectively heed – these warnings.

Equifax received the first notification of the Apache Struts vulnerability via a specific warning from the Department of Homeland Security U.S. Computer Emergency Readiness Team (CERT) on March 8, 2017.[26] Richard F. Smith, former Equifax CEO, testified that the company disseminated the U.S. CERT warning the next day, "requesting that applicable personnel... upgrade their software... within a 48 hour time period."[27] One week later, the company ran a series of internal scans that "should have identified any systems that were vulnerable" to that weakness.[28] These scans did not reveal any problems. The unpatched vulnerability remained for two months, until hackers used it to breach Equifax's network on May 13.[29] Equifax later admitted that the company failed to close the loop and confirm whether the fixes were made, and revealed that the subsequent scans only evaluated part of Equifax's systems.[30]

Equifax had other warnings of potential problems. Prior to the breach revealed in September 2017, there were four different instances when company data was accessed by hackers between 2013 and 2017. Hackers accessed credit-report data held by Equifax between April 2013 and January 2014; Equifax discovered "that it mistakenly exposed consumer data as a result of a technical error that occurred during a software change in 2015"; a breach compromised information on consumers' W-2 forms that were stored by Equifax units in 2016 and 2017; and Equifax reported in

February 2017 that a technical issue "compromised credit information of some consumers who used identity-theft protection services from a customer."[31]

Press reports also revealed that four independent analyses of Equifax cybersecurity, conducted either before or immediately after the breach, identified important weaknesses.

(1) In April 2017 – the month before the breach – Cyence, a cyber-risk analysis firm, "rated the danger of a data breach at Equifax during the next 12 months at 50%. It also found the company performed poorly when compared with other financial-services companies."[32]

(2) SecurityScorecard, another security monitoring firm, identified the precise weakness that was used by the hackers to breach the Equifax system, reporting that "Equifax used older software – such as the Apache Struts tool kit… and often seemed slow to install patches."[33]

(3) An outside review by the Fair Isaac Corp. rated Equifax's "enterprise security score" based on three elements: hardware, network security, and web services. The score declined from 550 out of 800 at the beginning of the year to 475 in mid-July when the breach had already occurred. According to reports, "By July, 14 public-facing websites run by Equifax had expired certificates, errors in the chain of certificates, or other web-security issues."[34]

(4) A fourth independent review released just after the breach was revealed identified significant problems with Equifax cybersecurity. This report by BitSight Technologies gave the company an "'F' in application security and a 'D' for software patching."[35]

B. Equifax Failed to Notify Consumers, Investors, and Regulators about the Breach in a Timely and Appropriate Fashion

Equifax was first warned about the vulnerability that led to the breach on March 8, 2017; the breach occurred on May 13, 2017, and Equifax first observed suspicious network traffic on July 29; Equifax's CEO first learned of the suspicious activity on July 31; and Equifax engaged a cybersecurity consulting firm, retained a law firm, and contacted the Federal Bureau of Investigation on August 2.[36] Equifax knew of the major breach, and knew it was significant, but spent almost two weeks trying to identify precisely which customers were affected – all while saying nothing to regulators or the public.[37] By August 11, Equifax knew that hackers likely accessed "a database table containing a large amount of consumers' PII.[38]" Equifax failed to notify consumers, investors, business partners, and other regulators until September 7, 40 days after the company initially discovered the breach.[39]

In addition, Equifax has publicly stated on numerous occasions that data was "accessed" – leaving it unclear if hackers merely obtained access to, or actually stole the data. But in a December 11 Banking Committee staff briefing, Equifax officials confirmed that, in fact, data tables were "exfiltrated" – stolen – by the hackers.[40]

By failing to provide adequate information about the breach – either publicly, or privately to regulators and other business partners – Equifax robbed consumers of the ability to take precautionary measures to protect themselves; materially injured investors and withheld market-moving information; and prevented the federal government from taking action to remedy the situation and cut ties with Equifax in other contracts. Equifax failed to notify the following parties in a timely fashion:

- **Consumers:** Equifax exposed the sensitive personal information of over 145 million individuals, yet the hackers that stole this information had more than a month to take advantage of consumers who had no idea they were at risk. Equifax did not give consumers a chance to obtain credit freezes, cancel their credit cards, place fraud alerts or credit monitoring on their accounts, or take any number of precautionary measures to ensure their financial safety. Furthermore, Equifax failed to disclose the fact that the hackers gained access to consumers' passport numbers.[41] And four months after the breach, Equifax still has not affirmatively notified all individual consumers that were impacted by the breach.[42]

- **Investors:** According to the SEC's cybersecurity guidance, Equifax has a duty to disclose information that a "reasonable investor would consider important to an investment decision."[43] This includes "costs or other consequences" of a breach, including the potential costs of remediation, protection, lost revenues, and reputational harm.[44] After first learning of suspicious activity on its network, Equifax waited 40 days to inform investors – filing an 8-K form with the SEC on the same day it made a public announcement.[45] And Equifax missed other key opportunities to inform investors of risks.

  In particular, Equifax held an investor presentation on August 16, more than two weeks after the initial discovery and one day after Equifax CEO Rick Smith learned that consumer personally identifiable information had been stolen in the breach.[46] Equifax neglected their duty to investors by failing to inform them of the breach during that presentation, and continued to withhold material information that had a large impact on the company for more than three weeks.

- **Government Regulators:** The Federal Trade Commission (FTC) and the Consumer Financial Protection Bureau (CFPB) regulate Equifax. The FTC has primary authority to enforce the Gramm-Leach Bliley Act, which provides data security requirements for non-bank financial institutions. The FTC and the CFPB have concurrent authority to enforce the Fair Credit Reporting Act, which requires credit reporting agencies to maintain "reasonable procedures" to protect consumer data, but are not specifically designed to address cybersecurity threats.[47] And while the FTC can bring lawsuits against companies that have allowed data to be compromised, the agency does not have authority to provide ongoing supervision of company practices.[48] The Department of Homeland Security also addresses cybersecurity threats, and warned Equifax about the vulnerability that hackers eventually utilized to breach the company's networks and access consumer data. Yet Equifax failed to notify its regulators for more than a month after first learning of suspicious activity, leaving them behind the curve in helping consumers deal with the consequences. The FTC, the CFPB, and DHS only learned of the breach when it was disclosed to the public.[49]

  The FTC was forced to hastily address the regulatory and public interest concerns rather than having time to prepare a response. The FTC released an advisory to consumers after Equifax's public announcement of the breach that eventually became the most viewed webpage in the federal government.[50] If Equifax had informed the agency sooner, the FTC could have worked to make sure consumers were prepared and protected, and advised them immediately following Equifax's announcement.

  Equifax also failed to inform state agencies and Attorneys General of the breach, delaying action at the state level under appropriate state laws.[51]

- **Federal Contractors:** Equifax also failed to inform government agencies with which the company holds federal contracts of the breach. For example, Equifax did not notify the IRS of its data breach for 40 days after first learning of suspicious activity.[52] Although reviews conducted by the IRS after the breach indicated that there was no consumer tax data exposed to hackers, Equifax's delay potentially placed this data at risk.

C. Equifax took advantage of federal contracting loopholes and failed to maintain adequate protections for sensitive IRS taxpayer data

Over the last decade, Equifax has been awarded 2,106 Federal contracts worth over $120 million.[53] These contracts have been awarded by dozens of agencies, including the General Services Administration, the Department of Justice, the Department of Homeland Security and the Equal Employment Opportunity Commission.[54]

Equifax was involved in the exposure of consumer data in several instances while it was performing Federal contracts. In some cases, these contracts involved particularly sensitive personal information. For example, in 2013, the Center for Medicare and Medicaid services awarded a five year, $329 million contract to Equifax to verify income and employment information for Americans who applied for subsidies under the Affordable Care Act.[55]

A recent controversial contract was awarded to Equifax in 2015[56] by the Internal Revenue Service (IRS) to verify taxpayers' identities in an online portal that allows taxpayers access to their tax documents.[57] This contract – and the IRS – became the subject of intense criticism when it was announced that it would be renewed soon after Equifax revealed the breach in September 2017.[58] Several weeks later, the IRS reversed itself and suspended the contract on October 12, 2017.[59]

This investigation reveals that Equifax used loopholes in Federal procurement law to obtain this extension, gouging taxpayers in the process and placing data at risk. In response to a request, the IRS provided Senator Warren's staff with a briefing on this matter. In this briefing, staff learned that the IRS suspended this contract after the agency learned of a number of additional flaws in how Equifax was handling sensitive taxpayer data.[60]

In June 2017, the IRS asked companies to bid for a contract to verify taxpayers' identities on its online portal.[61] Equifax had won the previous contract in 2015 and bid again, but Experian underbid Equifax, asking for less than a third of Equifax's bid – a savings of more than $1.7 million in taxpayer dollars to provide the same services.[62] But barely a week after the contract was awarded to Experian in late June, Equifax protested the award.[63] Federal procurement law gives the Government Accountability Office 100 days to resolve the dispute.[64] Even after it announced the massive security breach, Equifax continued its protest.[65] And because of the protest, the IRS couldn't start the 2-3 month process of integrating Experian into its system as the new contractor.[66]

Because of this delay, the IRS was forced to seek a "bridge contract" to keep the online portal open during the appeal, when victims of Hurricanes Harvey and Maria were relying on the portal to get access to financial documents they had lost. Equifax took advantage of the IRS during this period by raising their price for the bridge contract.[67] In fact, the total bridge contract, which included a three-month contract with two additional three month options, would cost taxpayers $7.3 million – more than nine times as much as Experian will charge for a full year of service ($795,000).[68] This bridge contract was awarded on September 29.[69]

The IRS found out about the breach at the same time as the American public.[70] Within a day, the IRS was on the phone with Equifax, and within two weeks IRS staff was on the ground checking the Equifax systems to make sure no taxpayer information had been compromised.[71] The IRS determined that no data was compromised in this case – but the six-week delay in informing the IRS of the breach could have left taxpayers vulnerable to hackers.[72]

On October 13, a little over one week after announcing the bridge contract, the IRS reversed itself and announced that it was suspending the bridge contract with Equifax.[73] This was because Equifax announced new information that put taxpayer information at risk.[74]

There is no indication that any IRS data was exposed in the breach. But because of the delays, the IRS was forced to give Equifax an expensive bridge contract, and belatedly discovered – weeks after they should have been warned – that Equifax was not able to effectively protect taxpayer data to IRS standards.

D. Equifax's assistance to consumers following the breach was sorely inadequate

On September 7, 2017, when Equifax publicly announced the breach, then-CEO Richard Smith wrote that "[w]e…are focused on consumer protection and have developed a comprehensive portfolio of services to support all U.S. consumers, regardless of whether they were impacted by this incident."[75]

But after failing to prevent the breach, the company then failed to effectively respond to it and provide adequate assistance to the millions of Americans put at risk. Equifax did not have an adequate crisis management plan in place, and the company failed to follow the procedures they did have in place for notifying consumers affected by the breach.[76] From the start, the victims of the breach were faced with an obstacle course riddled with traps and frustrations. In fact, as of November 21, 2017, the CFPB handled "over 7,500 complaints" related to the breach, and "a large number of complaints involved specific problems with Equifax's post-breach response."[77] According to the CFPB, "Consumers described difficulty in reaching Equifax's call centers and in accessing their security freeze PIN when adding a freeze online.

Consumers mentioned lengthy hold times, dropped calls, agents not calling back as promised, and call centers that were not helpful."[78] These failures occurred despite the fact that Equifax had 40 days after learning of the breach to prepare their public response.

1. Failure to Adopt or Follow an Effective Breach Response Plan

Equifax confirmed, in response to questions from Senator Warren, that the company has "several plans and procedure guides that address cybersecurity incidents," including the company's Security Incident Handling Procedure Guide, Security Incident Response Team Plan, and Security and Safety Crisis Action Team Plan.[79] While Equifax provided my office with a 150-page Corporate Crisis Management Plan,[80] including a full chapter on Security Incident Handling Policy & Procedures, there are a number of problems with this plan.

The Security Incident procedures are dated October 2014, indicating that they have not been updated in over three years.[81] Moreover, this Crisis Management Plan appears to place little emphasis on protecting the well-being of the millions of individuals whose data are used by Equifax, and often appears more focused on physical security threats and shareholder value [82] than protecting the victims of cybersecurity breaches. For example, the three key overarching principles listed in the Crisis Management Plan are to "Place the highest priority on Life Safety...protect our assets and preserve our ability to operate and supply our customers, [and] maintain a strong Equifax reputation through ethically and socially aware behaviors that ultimately preserve shareholder value." These principles say nothing about protecting sensitive consumer data that earn Equifax hundreds of millions in revenue per year.

The specific "Unauthorized Access Incident Handling Checklist" in the Equifax Security Incident Handling Policy & Procedures does not include informing customers of potential access to their personal data.[83] Instead, these procedures are listed separately in the crisis response handbook – and even then, are not appropriately detailed. For example, there is no clear required deadline or timeline to inform customers about a breach that places their personal data at risk – perhaps explaining why Equifax did not inform the public until over 40 days after the incident.

Finally, it appears that Equifax failed to follow its own procedures for informing the public of breaches. These procedures require that notice be provided to affected customers "in a clear and conspicuous manner, either by telephone or in writing."[84] But according to information provided to Senator Warren's staff, Equifax provided such notice only to 2.5 million affected consumers – the remaining 140 million-plus consumers received notice of the breach only if they went to the company website on their own volition.

2. Problems with the Equifax Call Center

From the start, the Equifax call center had major problems. Consumers sometimes waited up to an hour, if not more, to speak to a representative.[85] Equifax took advantage of the hold time to advertise for various Equifax products.[86] When Equifax representatives eventually got on the phone, they were unable to give consumers even the most basic information about whether their data had been compromised. Callers who wanted to put a fraud alert on or freeze their account were also out of luck – or at least in for a merry-go-round of additional toll-free numbers and dropped calls that even if successful, cost consumers hours of time and aggravation.[87] The CFPB received numerous complaints describing "difficulty in reaching Equifax's call centers and in accessing their security freeze PIN[,]" as well as "lengthy hold times, dropped calls, [and] agents not calling back as promised."[88]

3. Problems with EquifaxSecurity2017.com

Equifax set up a website, EquifaxSecurity2017.com, and instructed consumers to visit to determine whether their data were compromised and to learn about the products the company was presumably providing to help them protect themselves from the effects of the hack.[89] But the website asked consumers for some of the very same information that Equifax had already left vulnerable to hackers, including the last six digits of consumers' social security numbers.[90] Then it misled consumers, telling *most* visitors the same thing: that their information *may* have been compromised, and instructing them to enroll in the Equifax credit monitoring program at some later date.[91]

And to make matters worse, according to cybersecurity experts consulted by Senator Warren's staff, EquifaxSecurity2017.com had major security vulnerabilities: the site Equifax took weeks to put up to handle inquiries and allow consumers to sign up for services that could protect their financial futures, was itself vulnerable. The main problem was that the site's design and web address made it easy for others to impersonate and collect consumers' information.[92] To demonstrate this, a cybersecurity expert created a website with a nearly identical web address – www.securityequifax2017.com – which looked so similar to the actual website's link that Equifax directed consumers to the fake site multiple times.[93]

In addition, experts consulted by Senator Warren's staff identified numerous other technical flaws in the website design. They reported that the website was set up to run on a stock installation of Wordpress, which didn't include the necessary security features to protect the sensitive information consumers submitted, and that the[94] website's Transport Layer Security certificate also did not perform proper revocation checks, which would have ensured that it was establishing a secure connection and protecting a user's data. And then, on October 12, Equifax was forced to take down a web-page where people could learn how to get a free credit report when a security analyst reported that the site's visitors were targeted by malicious pop-up ads.[95] After failing to protect consumer data, Equifax subsequently set up a website that put their customers in even greater danger.

4. Equifax Forced Arbitration Requirements

In the wake of the breach, Equifax urged all consumers to sign up for one year of free credit monitoring from TrustedID Premier, a product Equifax owned. But to sign up for this service, Equifax initially required consumers to sign a forced arbitration agreement and give up their right to go to court if Equifax cheated them in the future.[96] And deep in the fine print of the agreement was a provision that allowed Equifax to charge customers if they didn't cancel the service within a year.[97] Equifax ultimately eliminated both requirements by September 10, after a public outcry.[98]

5. Equifax Used the Breach as a Moneymaking Opportunity

Rather than acting solely to help customers after the breach, Equifax instead used it as a moneymaking opportunity, attempting to profit off of their own failures. Equifax initially charged consumers to freeze their credit.[99] A credit freeze prevents a credit reporting agency from providing a consumer's credit file to a third party that does not already have the consumers as a customer, and is often the best tool for consumers to protect themselves against identity theft. At first, Equifax was charging customers the full amount allowed – up to $30.95 per credit bureau – to freeze their credit in the wake of the breach.[100] Equifax was raking in these fees until the public backlash forced it to provide free freezes – but only until it releases a new "credit lock" product in 2018, which provides some of the same services without the legal protections.[101] Equifax controls its own credit lock product, which means it can control what services the product provides, whether customers are able to sue if Equifax provides data notwithstanding the lock, and whether it remains free after the public attention dissipates.

The problem for consumers is that risks will continue until well after Equifax's free service ends, and if they want to fully protect themselves, they may have little choice but to sign up for the new product. According to the FTC, "if certain types of information – such as Social Security numbers – are exposed due to a breach, the risks to consumers could certainly continue for longer than one year. ...Given that Equifax has chosen to provide free credit monitoring for only one year, some consumers may choose to pay for credit monitoring services after that period."[102]

Equifax also made money on other companies' products after the breach. Frustrated customers who were fed up by Equifax's customer service or didn't trust Equifax's protection flocked to other companies like Lifelock, which reported a tenfold increase in enrollment during the month after the Equifax breach.[103] As Former Equifax CEO Rick Smith confirmed under questioning by Senator Warren, Lifelock uses Equifax to monitor its customers' credit and pays Equifax on a per customer basis for use of its services.[104]

Former Equifax CEO Richard Smith said in August – after Equifax had discovered the breach – that fraud "is a huge opportunity" for Equifax.[105] Equifax sells products to businesses and governments to help them prepare for and recover from data breaches.[106] They also sell credit monitoring products to help mitigate damages when breaches happen. As Senator Warren pointed out during a Banking Committee Hearing on October 4, 2017, "So far, 7.5 million people have signed up for free credit monitoring through Equifax since the breach. If just 1 million of them buy just one more year of monitoring through Equifax at the standard rate of $17 a month, that is more than $200 million in revenue for Equifax because of this breach."[107]

E. Federal Legislation is Necessary to Protect Consumers

Equifax and other credit reporting agencies collect consumer data without permission, and consumers have no way to prevent their data from being collected and held by the company.[108] Equifax recently confirmed to Senator Warren that the company "will not offer consumers the opportunity to delete their personally identifiable information..." [109] Equifax adopted weak cybersecurity measures that did not do enough to protect that data. This investigation conducted in the aftermath of the recent massive security breach reveals that the company failed to safeguard consumer data and was unable or unwilling to address persistent weaknesses in their system, even when notified by multiple parties, including the Department of Homeland Security. After hackers took advantage of one of these weaknesses to access the personal data of over 145 million consumers, Equifax caused consumers, investors, and the federal government even more problems by waiting 40 days to notify interested parties. And after finally announcing the breach, Equifax abandoned consumers once again by offering shoddy, unreliable assistance that failed to fix their problems and, in some cases, increased their risk.[110]

Individual companies have a responsibility to protect personal information. But federal legislation is necessary to give regulators and consumers the tools they need to ensure that credit reporting agencies, including Equifax, put consumer financial safety above their bottom-line. Legislation should:

- **Impose Appropriate Penalties in the Event of a Breach of Consumer Data**

The federal government cannot presently issue fines against credit reporting agencies when they fail to protect personal information and put consumer safety and financial security at risk – even when, like Equifax, they do so despite having ample warning of problems. In fact, the FTC has requested legislation that would "allow the FTC to seek civil penalties," because these penalties would "help ensure effective deterrence" of cybersecurity breaches." [111] The CFPB also supports such legislation, claiming that "federal laws that are applicable to data security have not kept pace with technological and cybersecurity developments... it is imperative for Congress to take steps to ensure that the regulatory framework is adequate to meet" the challenges posed by cybersecurity threats, and adding that "federal laws...have not kept pace with...cybersecurity developments."[112] There have been breaches at all three credit reporting agencies in the last several years, and hundreds of millions of consumers have been impacted.[113] When credit reporting agencies collect personal data without consumer permission, the burden should be on them to protect that data. If they fail to protect that data, they should be punished.

Consumer lawsuits do not provide adequate deterrence for companies like Equifax. While the average consumer recovers less than $2 through civil lawsuits in response to data breaches, Equifax is actually set to make money off their recent breach. If our laws don't punish companies like Equifax for their failure to protect sensitive consumer data, these companies will continue to adopt sub-standard security measures.

- **Set Strict Cybersecurity Standards and Empower the FTC to Update and Monitor these Standards**

No single agency currently has the appropriate authority to both establish basic cybersecurity requirements and monitor companies' adherence to those standards. The FTC itself has stated that "additional tools are necessary."[114] Equifax didn't just fall victim to a sophisticated attacker; Equifax failed to provide basic security for the personal information belonging to millions of Americans. Congress should empower the FTC to establish requirements

for fundamental cybersecurity measures at credit reporting agencies.

The FTC should also have supervisory authority to monitor credit reporting agencies and ensure they are following these standards. If they aren't, the FTC should be able to obtain an injunction requiring them to update their security procedures. If a company like Equifax has a breach and the FTC finds that they weren't following the appropriate standards, the penalties should be increased for every consumer exposed in the breach. That is the only way to make sure credit reporting agencies take the security of consumer data seriously.

Equifax and other credit reporting agencies have taken advantage of consumers for years, collecting their data without permission and turning a huge profit while failing to adequately protect that data. These practices won't change without federal legislation that forces Equifax and its peers to put appropriate emphasis on protecting consumer data.

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