



Federal Trade Commission

PRESCREENING UNDER THE FAIR CREDIT REPORTING ACT
AND OTHER CURRENT ISSUES THAT AFFECT CREDIT BUREAUS

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before the

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The views expressed are those of the Commissioner and do not necessarily reflect those of the Federal Trade Commission or the other Commissioners.



I am delighted to be here today to meet with you and to discuss some issues of mutual concern relating to the Fair Credit Reporting Act. Since the FCRA was enacted by Congress in 1970, the consumer credit industry has grown enormously. You are already well-acquainted, of course, with the advancements in computer technology that have led to radical changes in the way personal financial information is gathered, stored, and used by creditors and credit reporting agencies. But the public concerns that prompted enactment of the FCRA -- concerns about privacy and accuracy -- have not changed. They are as valid today as they were twenty years ago.

As you know, the Federal Trade Commission is the primary enforcer of the FCRA, with jurisdiction over the conduct of consumer reporting agencies like yourselves. Our first priority is investigating alleged FCRA violations and enforcing the law against violators. But we also take seriously our duty to educate consumers and the credit industry on their rights and responsibilities under the FCRA. The main reason I am here today is to discuss certain key FCRA enforcement issues -- in particular, prescreening. I also want to tell you about positions the Commission has taken on certain legislation proposing amendments to the FCRA that was introduced in the last Congress, and that may be reintroduced in this Congress. But before I do that, I offer the standard disclaimer, which is that the views expressed in these

remarks are mine, and do not necessarily represent the views of the Commission or of any other Commissioner.

I have been told that you would also be interested in any observations I might make about the overall vigor and direction of the Commission's current consumer protection enforcement program, and I happy to give you my views on that subject. As you probably know, the FCRA is only one of the consumer protection statutes enforced by the Commission. We believe strongly in the benefits of a free-market economy, but we also believe in aggressive enforcement of the laws prohibiting unfair and deceptive practices that harm consumers.

I have served on the Commission for six years now and was a member of our staff for a number of years before that, and I believe the Commission has never been more committed to stopping law violators. Janet Steiger, who became Chairman of the Commission in 1989, has proven to be an outspoken and tireless advocate for consumers, and my other colleagues on the Commission have also been supportive of vigorous law enforcement. Staff morale seems high, in large part because of the Chairman's leadership and the Commission's pro-enforcement attitude. The agency's budget has stabilized, which enables us to focus our attention on prosecuting law violations.

You may be familiar with some of our recent consumer protection enforcement actions, the targets of which range from large food manufacturers who made deceptive health claims for their products, to used car dealers and funeral directors who fail to disclose information required by special regulations governing those industries. We have devoted considerable time and effort to shutting down telemarketers who are guilty of outright fraud in the sale of investment opportunities, vacation packages, and a variety of other goods and services. We seek remedies in such cases that range from prohibitions against future violations to refunds and other forms of consumer redress to civil penalties. Because our enforcement of the FCRA affects your business most directly, I will focus on that topic today. But I will be happy to answer any questions you may have about our other consumer protection activities.

In May of 1990, the Commission published its first Official Commission Commentary on the FCRA to assist consumers and industry members in interpreting the law. The Commentary, which represents the Commission's view of what the FCRA does and does not permit, replaces hundreds of staff and Commission interpretations that had been issued since the FCRA was enacted. The final version of the Commentary was issued only after intensive analysis of the law itself, previous Commission interpretations of the law, and comments the Commission received on a 1988 draft version of the

Commentary. We hope that the Commentary will prove to be a useful source of guidance to the credit industry.

One of the issues that was most hotly debated during the public comment period was the issue of prescreening. Indeed, prescreening and other privacy related issues have received considerable attention in the media and on Capitol Hill as well as at the Federal Trade Commission in the past year. The explosive growth in computer technology has made all types of information more available and more affordable to businesses than ever before. At the same time, competitive pressures in marketing consumer financial services have made information about consumers more valuable than ever. Creditors want as much information as possible about the consumers to whom they will market their products. Consumers, in turn, are increasingly concerned about possible invasions of their privacy. These issues are joined when considering prescreening and privacy under the Fair Credit Reporting Act.

What is "prescreening?" Prescreening is a process in which a credit bureau, either directly or through a third party, provides a creditor with the names of consumers who meet that creditor's credit-granting criteria. In the prescreening process a credit bureau may take a list provided by a creditor and eliminate the names of consumers who do not meet criteria specified by the creditor. More often, it creates a list of those who do meet the

creditor's criteria. Because a prescreened list developed from information in credit bureau files conveys specific information about an individual's creditworthiness, each name on a prescreened list constitutes a consumer report. Because Congress was concerned with protecting consumers from unwarranted invasions of their financial privacy, when enacting the FCRA it stipulated that no one could obtain a consumer report without having a permissible purpose for doing so.

As many of you may know, the Commission has been on record as supporting prescreening, with appropriate controls, for over seventeen years. The first official Commission interpretation on prescreening was issued in early 1973. That interpretation said that prescreening was permissible under the FCRA if the creditor intended to offer credit to everyone on the list produced by the credit bureau. The Commission's 1990 Commentary on the FCRA basically reaffirmed its earlier position. It takes the position that prescreening is permissible as long as the creditor for whom the prescreened list is prepared plans to make an offer of credit to each consumer identified on the list.

The requirement that an offer of credit be made stems from the Commission's conclusion, which I mentioned earlier, that each name and address on a prescreened list constitutes a consumer report. Anyone who wants access to consumer report information must, under Section 604 of the FCRA, have a permissible purpose for

obtaining one. Section 604 states that creditors may obtain a consumer report if they intend "to use the information in connection with a credit transaction involving the consumer on whom the information is to be furnished and involving the extension of credit to, or review or collection of an account of, the consumer." In a prescreening context, clearly the consumer has no intention of entering into a credit transaction with the creditor who seeks the list. Nonetheless, the Commission has taken the position that when the creditor plans to offer credit to the consumers who are identified through prescreening, the requisite intention exists.

I would note here that the Commentary does permit some fine-tuning of the prescreened list. For example, either before or after the credit bureau screens the list, it may be subjected to demographic analysis to focus the credit offer on consumers with specified demographic characteristics. The creditor may also make random deletions from the list if it is too long. The creditor may make such deletions itself or employ a third party to perform this task on its behalf. In addition, the creditor may ask the credit bureau to prepare tiered lists that identify consumers with different creditworthiness characteristics. This procedure enables the creditor to tailor its offer of credit, as it deems appropriate, to different groups of consumers. The key point is that, once the final list is prepared, the creditor must offer credit to all consumers whose names appear on it. It is the offer of credit that validates the creditor's access to consumer report

information about them. Or, put another way, it is the assurance that credit will be offered to these consumers that makes it lawful for the credit bureau to provide a prescreened list to the creditor.

Some creditors have argued that a conditional offer -- one that is contingent on a specified annual income, perhaps -- should suffice. The Commission disagrees. By its terms, a conditional offer signifies that the creditor does not intend to enter into a credit transaction with all consumers on the prescreened list, but only with those who meet the subsequent condition. The position expressed in the Commentary is that prescreening requires a firm offer of credit to those on the list. This means, for example, that a creditor cannot impose a minimum income requirement on the credit application it mails to consumers whose names it has taken from a prescreened list. Nor can the creditor, except in rare and unforeseeable instances, withdraw the offer based on new information it learns about the consumer. In other words, the creditor cannot condition its offer of credit on the consumer remaining as creditworthy several months later as the consumer was when his or her credit report was accessed.

In the period of time that a creditor takes to process its prescreened offers, some consumers' credit histories inevitably will deteriorate and others will improve. Moreover, the creditor may learn that the credit report relied upon originally was not

wholly accurate or complete. These events necessarily occur in a certain predictable percentage of cases, and a creditor who does not offer credit to such consumers clearly never intended to offer credit to all consumers whose names it obtained through prescreening.

This does not mean, however, that creditors must either abandon prescreening or subject themselves to unwarranted risk. When a consumer accepts the credit offer, the creditor has a permissible purpose under the FCRA for obtaining a full credit report on the consumer. If the full report reveals information that raises concerns on the creditor's part, the creditor may flag the account for regular review and, if the consumer does not prove to be creditworthy, close the account. A creditor can limit its liability by offering a modest amount of credit initially and then offering more later if the full credit report confirms the preliminary picture.

Clearly, a creditor may ask for identifying information in its credit offer to be sure that the consumer who responds is the one to whom the creditor intended to extend a credit offer -- i.e., the consumer whose credit file was prescreened. And the creditor may impose a reasonable time limit on the period during which its credit offer remains outstanding. Any consumer who responds beyond that time period may be treated as a credit applicant, and the creditor may obtain a full credit report to evaluate his or her

creditworthiness. We also think it self-evident that creditors may require consumers who accept prescreened offers to be old enough to enter into a binding contract and to sign a credit contract making them legally obligated for the credit being offered.

Finally, we think that the credit offer could be withdrawn if subsequent information were to reveal that the consumer's credit report had been fraudulently altered, or that the consumer had been imprisoned, or that the consumer had moved beyond the creditor's service area so that it became impossible for the creditor to make an extension of credit. Such turns of event are likely to be rare and unforeseeable, and withdrawing the credit offer in these circumstances would not, in our view, negate the creditor's underlying intention to offer credit to all consumers whose names it had obtained through prescreening.

To summarize, then, once a consumer has accepted a creditor's offer of credit, the creditor is free to engage in postscreening by obtaining a full credit report on the consumer. A creditor has a permissible purpose under the FCRA to obtain a credit report at any time to review or collect on a credit account, and the creditor may use the information it thus obtains to protect its financial interests and limit its risk. As long as its original credit offer is not misleading about the terms of the credit offer, a creditor may use postscreening to set different credit terms for different consumers. It may use postscreening to offer better credit risks

additional lines of credit. And it may use postscreening to terminate an account that seems to pose undue risk. The only thing that a creditor may not do under the Commission's Commentary is use the information obtained in the postscreen to rescind the original offer of credit, except in rare circumstances.

Why have I discussed a creditor's obligations under the FCRA in such detail when addressing members of the Associated Credit Bureaus? Because it is credit bureaus who are best situated to ensure compliance with the privacy protections of the FCRA. It is credit bureaus to whom the permissible purposes provisions of the FCRA apply directly, and it is credit bureaus who are directly liable if Section 604 is violated. Credit bureaus are charged with the responsibility of releasing credit history information only to those who have a permissible purpose under the statute. And credit bureaus are required under the FCRA to maintain "reasonable procedures" to ensure that only those with a permissible purpose do, in fact, obtain reports. To meet this standard, I believe that before releasing a prescreened list a credit bureau must, at a minimum, obtain an assurance from the creditor that it will make an offer of credit to all consumers whose names appear on the final list.

We are sometimes asked what else we believe credit bureaus ought to do to ensure that prescreened reports are used properly. There may not be one right answer to that question. The proof is

in the pudding -- a reasonable procedure is one that works in the particular circumstances. You may find that all you need is a clear certification from the user that it intends to send a credit card to each consumer who responds to its offer. Or you may decide that you need to review the user's mailing. Some credit bureaus will no doubt find that certification and a spot check are all that is needed for most customers, but that other users require closer monitoring. In the end, we leave this decision to you. But when we see prescreened credit card solicitations that come with conditions attached, we know that whatever procedures the credit bureau is using are not doing the job.

There may well be some creditors -- particularly banks that issue general purpose credit cards like VISA and MasterCard -- that disagree with the Commission's view of what the law requires. That is, they may believe that a conditional offer of credit provides a lawful basis for obtaining a prescreened report. The bank regulatory agencies, which have enforcement authority over banks that issue credit cards, have not yet stated whether they concur in the Commission's enforcement position. Naturally, the Office of the Comptroller of the Currency's view of what the law requires will be of far greater concern to creditors under its jurisdiction than the FTC's view is. As credit bureaus, however, you are within the Commission's jurisdiction, and the Commission's interpretation of what the FCRA requires of you is directly applicable.

Because some genuine confusion about the Commission's enforcement position has existed previously, we have not yet cracked down on creditors who appear to violate the Commission's prescreening interpretation nor on the credit bureaus that have supplied prescreened lists to these creditors. In effect, we have provided creditors and credit bureaus with a grace period during which to come into compliance with the law. But it has been eight months since the Commission issued its final version of the FCRA Commentary, and this informal grace period is drawing to a close. We now expect you to be in complete compliance with the Commentary. If I had to limit my remarks today to only one sentence, it would be this: if I were you, I would revisit my procedures for ensuring that consumer reports in general and prescreened reports in particular are released only to those with a permissible purpose for receiving them. An ounce of prevention now may save a pound of attorneys' fees later.

Reasonable people can disagree over the extent to which a privacy invasion occurs in the prescreening process as well as over what the FCRA itself requires. For seventeen years, the Commission has interpreted the FCRA in a manner that both permits prescreening and respects the privacy goals of the Act. During the public comment period on the proposed Commission Commentary, many commenters praised the Commission's support for prescreening and urged that the rules governing prescreening be relaxed to permit greater flexibility in its use. On the other side, some groups

have expressed the view that the Commission has gone too far in permitting the use of consumers' personal financial information without the consumer's consent or even knowledge. Even the Congressional Research Service has weighed in with an opinion indicating that the practice of prescreening is not permitted by the FCRA. Last December, the National Association of Attorneys General announced their support of legislation that prohibits prescreening without the consumer's informed affirmative consent.

If there is to be a policy change, Congressional action is the appropriate way to clarify the FCRA's application to prescreening. In the last session of Congress three bills that addressed prescreening were introduced. Two would have banned it outright. The third bill, introduced by Richard Lehman of California, would permit it only when consumers authorized the use of their names and credit histories for prescreening, either directly or through an "opt out" procedure. In its Comments on the proposed legislation the Commission supported Representative Lehman's approach instead of the proposed bans because the Commission recognizes the utility of prescreening and, so long as consumers' privacy is adequately protected, sees no reason to bar its use. Whether these bills will be reintroduced in the new session of Congress remains to be seen. Your organization probably has a better line on that than we do. In the meantime the Commission must continue to interpret and enforce the existing law.

The proposed legislation on prescreening also addressed other aspects of the FCRA. For example, all three bills would have extended the Section 615 notification requirement so that, for example, a landlord who turned down a prospective tenant based on adverse information from a credit report would be required to provide the same disclosures that a creditor must provide when it denies credit. In its testimony on that legislation, the Commission suggested that Congress consider requiring credit bureaus to notify all credit report users of their obligation to provide consumers with Section 615 notifications when they make an adverse decision based on credit history.

The Commission also supported Representative Lehman's proposal to require a report user who denies credit based on adverse information in a credit report not only to identify the credit bureau that provided that report but also to inform the applicant that he or she has the right to a free copy of the report and the right to dispute any erroneous information in the report.

Section 609 of the Act does not requires credit bureaus to disclose medical information to consumers. Both Representative Lehman's bill and Representative Schumer's bill would require that all information -- including medical information -- be made available to consumers as well as to creditors, insurers, and other report users. The Commission supported that proposal because it would allow consumers to review such information for accuracy.

These bills also would require credit bureaus to provide consumers with more specific identifying information on users who had obtained access to their reports. The Commission believed that requirement would assist both consumers and law enforcement agencies in identifying instances of unauthorized access.

All three bills would have required credit bureaus to reinvestigate a disputed item and report back to the consumer within 30 days. As long as some flexibility is permitted for unusually time-consuming investigations, the Commission believes that such a requirement is desirable. Section 611 of the Act currently requires credit bureaus to correct inaccurate information, but does not require them to notify consumers of the outcome of their investigation. Notification may be particularly important where, for example, a creditor erroneously confirms inaccurate information when the credit bureau investigates. Notification in such a case tells the consumer where the problem lies.

Finally, Representative Lehman's bill and Representative Schumer's bill would have required you to provide consumers with one free copy of their credit reports each year, upon request. The Commission did not support that proposal in its testimony because we were not sure that the benefits to consumers of such a requirement outweighed its costs. Offering consumers an

opportunity to review their reports at little or no cost would facilitate their efforts to detect and correct errors, which benefits not only consumers but also creditors and other users of credit reports. But such a requirement could require the credit reporting industry to forego the revenue they currently derive from charges to consumers for copies of their credit reports and to absorb what we understand would be significantly higher costs.

If similar legislation is introduced in the current Congress, the Commission will no doubt be asked to offer its views. No doubt you too will express your opinions on such legislation to your elected representatives. Associated Credit Bureaus has worked with the Commission over the years to make sure that we understand your views on FCRA interpretation and enforcement, and to ensure that you receive up-to-date information on the Commission's enforcement activity. The Commission and its staff presently have a good working relationship with both the credit-reporting and the credit-granting industries. We may not always agree on what the FCRA says or whether it should be amended, but maintaining lines of communication between the Commission and your industry benefits us, benefits you, and benefits consumers.

You should never hesitate to ask our staff for help in understanding the FCRA or the Commission's Commentary on that statute.

One very tangible result of our working relationship with your industry is the excellent consumer education brochure, "Building a Better Credit Record," which the Associated Credit Bureaus helped our consumer protection staff produce. This is the type of private-public cooperation on consumer education that I hope we can extend to the telemarketing fraud area, and it also brings me to the final subject that I want to discuss with you today: credit repair fraud.

You all know about credit repair firms -- the credit "doctors" who claim they can "erase" bad credit histories from consumers' credit reports. They often couple their credit repair promises with pledges to secure bankcards and other sources of new credit for their customers.

As you well know, these people are making promises that they cannot keep and are cheating consumers out of untold millions of dollars annually. But to the extent that they are successful in having accurate information removed from a consumer's file -- and our staff estimates that they are successful in perhaps 10 percent of all cases -- they can do enormous damage to the consumer reporting system.

Why are credit repair operators sometimes successful in removing accurate information? The most common technique of credit repair firms is to file spurious disputes in the hope that some

accurate information will not be confirmed by creditors. Creditors sometimes do not bother to respond to requests for verification. Others are able to verify only recent delinquencies; older adverse information is "off the screen" and no attempt is made to retrieve it. And, of course, if the information is not reverified by the creditor, the law requires the credit bureau to delete it from the credit report.

The second technique is to offer to have the consumer repay amounts long in arrears in exchange for a positive rating. This practice is penny-wise and pound-foolish for creditors. Giving a positive rating to a consumer with a history of serious delinquency sets up the next creditor to take an unwarranted risk that it may well have not taken had it known the truth. Credit grantors rely heavily on the accuracy of the credit reporting industry, and this reliance appears to be growing rather than diminishing. Credit grantors who take care to report accurately, who promptly correct errors when discovered, and who promptly reverify accurate information are the first line of defense against credit repair scams.

Consumers who know their FCRA rights and how to use them are, I think, less likely to be misled by credit repair clinics. That's why I hope you will continue to help us distribute the "Building a Better Credit Record" brochure or otherwise educate consumers about credit repair fraud. I thank Associated Credit Bureaus for

their efforts in this area to date, and I look forward to continued cooperation between the credit reporting industry and the Commission.

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