

An hourglass-shaped graphic with a globe in the top bulb and another globe in the bottom bulb. The top bulb is dark blue, and the bottom bulb is light blue. The hourglass is light gray. The globe in the top bulb is dark blue, and the globe in the bottom bulb is light blue. The hourglass is centered on the page.

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Report RL32008

*A Consumers Access to a Free Credit Report: A Legal and  
Economic Analysis*

Loretta Nott, Government and Finance Division; and Angie A. Welborn, American Law Division

December 16, 2003

**Abstract.** This report offers one approach to assessing the potential costs of requiring credit reporting agencies to provide an annual free credit report upon request. It is shown that the additional costs of such a policy proposal can vary significantly depending on three factors: (1) the number of consumers who decide to exercise their option; (2) the number of consumers who dispute information in their files; and (3) the processing and dispute costs for a credit reporting agency.

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# CRS Report for Congress

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## **A Consumer's Access to a Free Credit Report: A Legal and Economic Analysis**

**Updated December 16, 2003**

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# A Consumer's Access to a Free Credit Report: A Legal and Economic Analysis

## Summary

The Fair Credit Reporting Act (FCRA) is the federal law that regulates the collection, use and disclosure of consumer credit information. With key provisions of the FCRA set to expire at the end of 2003,<sup>1</sup> the 108<sup>th</sup> Congress conducted a series of extensive hearings on the FCRA and how it pertained to a number of consumer-related issues, such as identity theft and the credit granting process. The legislation that resulted was the Fair and Accurate Credit Transactions (FACT) Act of 2003, which was signed by the President on December 4, 2003, and became Pub. L. 108-159.<sup>2</sup>

One of the key issues during the debate was the accuracy of credit reports and a consumer's access to the information in his or her file. In an effort to increase the accuracy of reports and provide greater transparency for consumers, there were several bills introduced during the 108<sup>th</sup> Congress to require consumer reporting agencies to provide an annual free credit report upon the consumer's request. The recently enacted FACT Act includes such a provision.

This report provides a brief legal analysis of the FACT Act provision requiring annual free credit reports to be disclosed on request, and from an economic perspective, offers one approach to assessing the potential costs of this requirement to the credit reporting industry. It is shown that the additional costs of this policy can vary significantly depending on three factors: (1) the number of consumers who decide to exercise their option; (2) the number of consumers who dispute information their files; and (3) the processing and dispute costs for a credit reporting agency.

This report will not be updated.

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<sup>1</sup> 15 U.S.C § 1681t, section 624. For a detailed description of these preemptive provisions, see CRS Report RS21449, *Fair Credit Reporting Act: Preemption of State Law*, by Angie A. Welborn.

<sup>2</sup> For a detailed summary of the key provisions in the FACT Act, see CRS Report RL32121, *Fair Credit Reporting Act: A Side-By-Side Comparison of House, Senate and Conference Versions*, by Angie A. Welborn and Loretta Nott.

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# Consumer's Access to a Free Credit Report: A Legal and Economic Analysis

## Introduction

The Fair Credit Reporting Act (FCRA) is the federal law that regulates the collection, use and disclosure of consumer credit information. With key provisions of the FCRA set to expire at the end of 2003,<sup>3</sup> the 108<sup>th</sup> Congress conducted a series of extensive hearings on the FCRA and how it pertained to a number of consumer-related issues, such as identity theft and the credit granting process. The legislation that resulted was the Fair and Accurate Credit Transactions (FACT) Act of 2003, which was signed by the President on December 4, 2003, and became Pub. L. 108-159.<sup>4</sup>

A key issue that emerged during the debate was the degree to which consumer credit files are complete and accurate, and to what extent the accuracy of the information affects the ability of consumers to access credit at reasonable rates. The empirical research suggests that there can be significant inconsistencies, omissions, and/or errors in consumer credit files.<sup>5</sup> For example, a Federal Reserve Board study found that “[a]bout 70 percent of the consumers in the sample had a missing credit limit on one or more of their revolving accounts.”<sup>6</sup> In these cases, the highest balance is typically used in place of the credit limit to measure a consumer’s credit utilization, which can lead to a “higher perceived level of credit risk for affected consumers.”<sup>7</sup>

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<sup>3</sup> 15 U.S.C § 1681t, section 624. For a detailed description of these preemptive provisions, see CRS Report RS21449, *Fair Credit Reporting Act: Preemption of State Law*, by Angie A. Welborn.

<sup>4</sup> For a detailed summary of the key provisions in the FACT Act, see CRS Report RL32121, *Fair Credit Reporting Act: A Side-By-Side Comparison of House, Senate and Conference Versions*, by Angie A. Welborn and Loretta Nott.

<sup>5</sup> See Robert B. Avery, Paul S. Calem, and Glenn B. Canner, “An Overview of Consumer Data and Credit Reporting,” *Federal Reserve Bulletin*, February 2003. Also, see “Credit Score Accuracy and Implications for Consumers,” a study by the Consumer Federation of America and the National Credit Reporting Association, Dec. 17, 2002, at [[http://www.consumerfed.org/121702CFA\\_NCRA\\_Credit\\_Score\\_Report\\_Final.pdf](http://www.consumerfed.org/121702CFA_NCRA_Credit_Score_Report_Final.pdf)], visited Dec. 16, 2003. For a more detailed overview of the empirical research on credit reporting accuracy, see Robert Hunt, “The Development and Regulation of Consumer Credit Reporting in America,” Federal Reserve Bank of Philadelphia, Working Paper No. 02-21, Nov. 2002.

<sup>6</sup> Avery, Calem, and Canner, “An Overview of Consumer Data and Credit Reporting,” p. 71.

<sup>7</sup> *Ibid.*, p. 71.

However, it is unclear to what extent these inaccuracies affect a consumer's ability to access credit at reasonable rates. A study by Arthur Andersen and Company concluded that "in only two-tenths of one percent of the over 15,000 cases studied, were consumers denied a benefit based on an error in their credit report."<sup>8</sup> In contrast, a study by the Consumer Federation of America (CFA) demonstrated that data discrepancies across the three nationwide credit data repositories<sup>9</sup> can lead to significant variations in a consumer's credit score, which can seriously affect the terms and conditions of a loan. For example, it found that "approximately 20 percent of all consumers—about 40 million Americans—are at risk for misclassification into the subprime mortgage market because their scores are near the 620 pricing cutoff point and vary significantly."<sup>10</sup> As Travis B. Plunkett, the legislative director for the CFA, noted in his June 12, 2003 testimony before the House Subcommittee on Financial Institutions and Consumer Credit, the interest rates on subprime mortgages "can be more than 3.25% higher than prime loans."<sup>11</sup>

In an effort to address these concerns, there were several bills introduced in the 108<sup>th</sup> Congress that would require consumer reporting agencies to provide an annual free credit report upon the consumer's request.<sup>12</sup> Six states had already enacted similar laws.<sup>13</sup> The recently enacted FACT Act includes such a provision.

During the legislative debate, consumer advocates strongly supported proposals that required credit bureaus to provide an annual free credit report upon a consumer's request.<sup>14</sup> They argued that empowering "consumers with more and better

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<sup>8</sup> See Consumer Data Industry Association (CDIA) press release, March 12, 1998, at [<http://www.cdiaonline.org/mediaroomdocs/readtext.cfm?ID=4>], visited Dec. 16, 2003.

<sup>9</sup> The three nationwide credit bureaus are Equifax, Experian, and TransUnion.

<sup>10</sup> Prepared testimony of Consumer Federation of America Legislative Director Travis B. Plunkett, in U.S. Congress, House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit, *The Role of the Fair Credit Reporting Act in the Credit Granting Process*, hearings, 108<sup>th</sup> Congress, 1<sup>st</sup> sess., June 12, 2003, p. 4, at [<http://financialservices.house.gov/media/pdf/061203tp.pdf>], visited Dec. 16, 2003.

<sup>11</sup> Prepared testimony of Consumer Federation of America Legislative Director Travis B. Plunkett, p. 4.

<sup>12</sup> The bills were H.R. 2622, H.R. 2546, H.R. 2035, H.R. 2796, S. 22, S. 223, and S. 1753. It is also important to note that some credit data inaccuracies may result from an act of identity theft. Thus, the proposal to require credit reporting agencies to provide an annual free credit report upon a consumer's request is also considered a means of improving consumer awareness and empowering the consumer to spot potential fraudulent data.

<sup>13</sup> Maryland, Massachusetts, Colorado, Vermont and New Jersey all require reporting agencies to provide one free credit report a year upon the request of the consumer, while Georgia allows consumers to request two free credit reports a year.

<sup>14</sup> In addition to an annual free credit report, many consumer groups also advocate the disclosure of the consumer's credit score with the report. A credit score is a derived statistical measure, based on credit bureau data, which ranks applicants according to their relative credit quality and quantifies the likelihood that a given applicant will become delinquent or default on a loan. H.R. 2546 is currently the only bill introduced during the

(continued...)

information is the key to improving the accuracy and fairness of the credit reporting system.”<sup>15</sup>

Although the consumer reporting industry agreed with this general thesis, it did not support any legislative initiative that would allow *all* credit-using individuals to request one free credit report a year.<sup>16</sup> Given the difficulties in predicting how many consumers would exercise their right to receive a free credit report each year, the industry asserted that the potential increased costs from such a policy could “pose tremendous burdens”<sup>17</sup> on credit reporting agencies.

This report provides a brief legal analysis of the FACT Act provision requiring annual free credit reports to be disclosed on request, and from an economic perspective, offers one approach to assessing the potential costs of this requirement to the credit reporting industry. The report is divided in two distinct sections. The first section provides a legal analysis of the current federal and state laws regarding free credit reports, including the recently enacted FACT Act. The second section develops a general economic framework which could be used to assess the potential costs to the credit reporting industry, and then calibrates the model using industry-supplied data to calculate different cost scenarios.

## A Legal Analysis

### The FCRA and Free Credit Report Disclosure

**Free Reports under the FACT Act.** The FACT Act, *inter alia*, amends the FCRA to allow a consumer to request one free copy of his or her credit report from each nationwide consumer reporting agency once during a twelve month period.<sup>18</sup>

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<sup>14</sup> (...continued)

108<sup>th</sup> Congress that also requires an annual free disclosure of a consumer’s credit score.

<sup>15</sup> Prepared testimony of Consumer Federation of America Legislative Director Travis B. Plunkett, p. 9.

<sup>16</sup> U.S. Congress, Senate Banking Committee, *The Growing Problem of Identity Theft and Its Relationship to the Fair Credit Reporting Act*, hearings, 108<sup>th</sup> Congress, 1<sup>st</sup> sess., June 19, 2003 (Washington: Federal News Service, 2003).

<sup>17</sup> Prepared testimony from Consumer Data Industry Association CEO and President Stuart Pratt, *Fair and Accurate Credit Transactions Act of 2003*, hearing on H.R. 2622, 108<sup>th</sup> Congress, 1<sup>st</sup> sess., July 9, 2003, p. 11-12, at [http://financialservices.house.gov/media/pdf/070903sp.pdf], visited Dec. 16, 2003.

<sup>18</sup> Pub. L. 108-159, Sec. 211(a). The law makes a distinction between nationwide consumer reporting agencies in general and what are referred to as nationwide specialty consumer reporting agencies. Nationwide specialty consumer reporting agencies are defined as consumer reporting agencies that compile and maintain files on consumers on a nationwide basis relating to (1) medical records or payments; (2) residential or tenant history; (3) check writing history; (4) employment history; or (5) insurance claims.

(continued...)

Requests for free credit reports must be made through a centralized source to be established pursuant to regulations to be promulgated by the Federal Trade Commission.<sup>19</sup> The centralized source for placing requests must allow the consumer to place a single request by calling a toll-free telephone number, or by using a standardized form either through the mail or through an Internet web site, in order to receive a free report from each nationwide consumer reporting agency.<sup>20</sup> The reports must be provided to the consumer no later than fifteen days after the date on which the request was received.<sup>21</sup>

Under the new provisions, a consumer may also request a free copy of his or her credit report after having a fraud alert placed in his or her file.<sup>22</sup> These reports must be provided to the consumer not later than three business days after the request is made.<sup>23</sup> If an extended fraud alert is requested, the consumer may request two free copies of his or her credit report during the twelve month period beginning on the date the alert is placed.<sup>24</sup>

**Additional Free Reports Available under the FCRA.** Additional free credit reports may be available under certain special circumstances as provided under existing provisions within the FCRA. Each of these special situations is discussed below.

Following an adverse action by a user of a consumer report, the consumer may, upon request, obtain a free copy of his or her report.<sup>25</sup> In order to receive a free report on this ground, the consumer must request the report within 60 days of receiving notice from a user indicating that an adverse action has been taken, or within 60 days after receiving a notification from a debt collection agency affiliated with a consumer

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<sup>18</sup> (...continued)

Both the FACT Act and the FCRA use the term “consumer report” rather than “credit report.” While “consumer report” may in certain circumstances encompass more information than what is in a typical “credit report,” the latter is the commonly used term for the type of information that is the subject of this report. In fact, the legislative history uses the term “credit report” when referring to the free access provisions and courts have also used the terms interchangeably. For example, see H. Report 108-263, p. 47; *Hasbun v. County of Los Angeles*, 323 F.3d 801 (9<sup>th</sup> Cir. 2003).

<sup>19</sup> *Id.* at Sec. 211(d). The process for requesting free reports from nationwide specialty consumer reporting agencies differs from this process. The Federal Trade Commission is required to prescribe regulations applicable to these types of consumer reporting agencies to require the establishment of a streamlined process for consumers to request free reports, which must include, at a minimum, the establishment by each such agency of a toll-free telephone number for such requests. Sec. 211(a).

<sup>20</sup> *Id.* at Sec. 211(d).

<sup>21</sup> *Id.* at Sec. 211(a).

<sup>22</sup> *Id.*

<sup>23</sup> *Id.* at Sec. 112(a).

<sup>24</sup> *Id.*

<sup>25</sup> 15 U.S.C. 1681j(b).



reporting agency from which the report is being requested stating that the consumer's credit rating may be or has been adversely affected.<sup>26</sup> The consumer may be entitled to a free report under such circumstances even if the basis for the adverse action was that the consumer had supplied credit references that were too few in number or too new to appear on the report.<sup>27</sup> It is unclear whether the consumer only has a right to a free credit report from the agency whose report was used in the determination that led to the adverse action.<sup>28</sup>

A consumer may also, upon request, receive a free copy of his or her credit report if he or she is unemployed and seeking employment.<sup>29</sup> Free reports may be obtained under such circumstances once during a 12-month period if the consumer certifies in writing that he or she is unemployed and intends to apply for employment in the 60-day period beginning on the date on which the certification is made. Presumably, this free disclosure is intended to help consumers avoid losing employment opportunities due to inaccurate information in consumer reporting agency files.<sup>30</sup>

Free credit reports are also available to recipients of public welfare assistance.<sup>31</sup> A recipient of public welfare assistance may, upon request, receive a free copy of his or her credit report once during a 12-month period.<sup>32</sup> The consumer must certify in writing that he or she is a recipient of such benefits, but the law does not require public agency confirmation or certification of the basis of the consumer's request. The law does not state whether the consumer can make the request of more than one consumer reporting agency during the 12-month period, but has been interpreted so as to allow requests to more than one agency.<sup>33</sup>

Finally, under federal law, a consumer may receive a free copy of his or her credit report once during a 12-month period if he or she has reason to believe that the file on record with the consumer reporting agency contains inaccurate information due to fraud.<sup>34</sup> The consumer must provide written certification of this belief, but the

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<sup>26</sup> *Id.* For more information on the adverse action notice requirements, see 15 U.S.C. 1681m.

<sup>27</sup> FTC Official Staff Commentary § 612 item 1, reprinted in *Fair Credit Reporting, 5<sup>th</sup> ed.*, National Consumer Law Center (2002), Appendix C.

<sup>28</sup> *Fair Credit Reporting, 5<sup>th</sup> ed.*, National Consumer Law Center (2002), p. 93.

<sup>29</sup> 15 U.S.C. 1681j(c)(1).

<sup>30</sup> *Fair Credit Reporting, 5<sup>th</sup> ed.*, National Consumer Law Center (2002), p. 93.

<sup>31</sup> The term "public welfare assistance" is not defined in the Fair Credit Reporting Act, but could presumably include "family welfare benefits to low-income children and households, Social Security benefits to elder Americans and SSI benefits to others, state and federal food stamp programs, workers compensation benefits, fuel assistance benefits, Medicare and Medicaid coverage, and other state and federal and local benefit programs." *Fair Credit Reporting, 5<sup>th</sup> ed.*, National Consumer Law Center (2002), p. 94.

<sup>32</sup> 15 U.S.C. 1681j(c)(2).

<sup>33</sup> *Fair Credit Reporting, 5<sup>th</sup> ed.*, National Consumer Law Center (2002), p. 94.

<sup>34</sup> 15 U.S.C. 1681j(c)(3).

law does not require the consumer to explain or provide details as to the basis of the belief. A consumer's report may be inaccurate due to fraud resulting from identity theft, fraudulent telemarketing scams, lending abuses, fraudulent sales, or the intentional furnishing of misleading information to a consumer reporting agency.

## Related State Laws

Prior to the enactment of the FACT Act, several states enacted laws allowing citizens of the state to obtain free copies of their credit reports. Generally, the new federal law preempts state laws related to the provision of free annual credit reports. However, state laws enacted prior to the enactment of the FACT Act are explicitly exempt from this general preemption.<sup>35</sup>

Pursuant to state law, residents of Colorado, Maryland, Massachusetts, New Jersey and Vermont can receive one free copy of their credit report per calendar year.<sup>36</sup> Georgia residents are entitled to two free copies per year.<sup>37</sup>

In addition to the free annual reports provided by some states, a state may also require the provision of free credit reports under certain special circumstances. For example, consumers in Colorado may obtain free copies of their credit reports upon notification from a consumer reporting agency that the agency has received eight credit inquiries pertaining to the consumer, or the agency has received a report that would add negative information to the consumer's file.<sup>38</sup> The consumer reporting agency is required to notify the consumer when either of these events occurs and must provide the consumer with a toll-free number to call to request a free copy of the report under such circumstances. Statutes of this type do not appear to be preempted under the general preemption discussed above.

In addition to the states that require the provision of free reports, a number of states limit the amount that a consumer reporting agency may charge a consumer for disclosure of his or her credit report. Federal law places a cap on what consumer reporting agencies may charge for the disclosure of a consumer's report, but does not require the imposition of a charge, thus states are free to enact laws limiting the charges allowed. For example, residents of Connecticut pay \$5 for the first copy and \$7.50 for each additional copy of their credit report requested during a 12-month period.<sup>39</sup> In Maine, residents pay only \$2 for copies of their credit reports, while in Minnesota the maximum charge is \$3.

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<sup>35</sup> Pub. L. 108-159, Sec. 212(e).

<sup>36</sup> Colorado, C.R.S. § 12-14.3-104(2)(e); Maryland, Md. Commercial Law Code Ann. § 14-1209(a)(1); Massachusetts, Mass. Gen. Laws Ann. ch. 93, § 59; New Jersey, N.J. Stat. § 56:11-37(a); Vermont, Vt. Stat. Ann. tit. 9, § 2480c.

<sup>37</sup> Ga. Code Ann. §§ 10-1-392, 10-393(29).

<sup>38</sup> C.R.S. § 12-14.3-104(2)(a).

<sup>39</sup> Conn. Gen. Stat. § 36a-696(b).

## An Economic Analysis

### The Consumer's Decision Tree

By requiring credit reporting agencies to provide an annual free credit report upon the request of a consumer, the FACT Act mandates these agencies to, in effect, provide consumers a free option which they can choose to exercise or not. If a consumer chooses not to exercise this option, there will be no cost incurred by the credit bureau. If, however, a consumer does choose to exercise the option, the consumer may find data inaccuracies and decide to dispute the information contained in the report. In this case, the cost to the credit reporting agency of issuing the option will be dependent on the consumer's decision path. **Figure 1** illustrates the different paths of possible consumer decisions.

As can be seen from **Figure 1**, the cost to the credit reporting agency of providing the option for consumers to request a free credit report will depend on three major factors:

#### 1. The proportion of consumers who exercise their option (P).

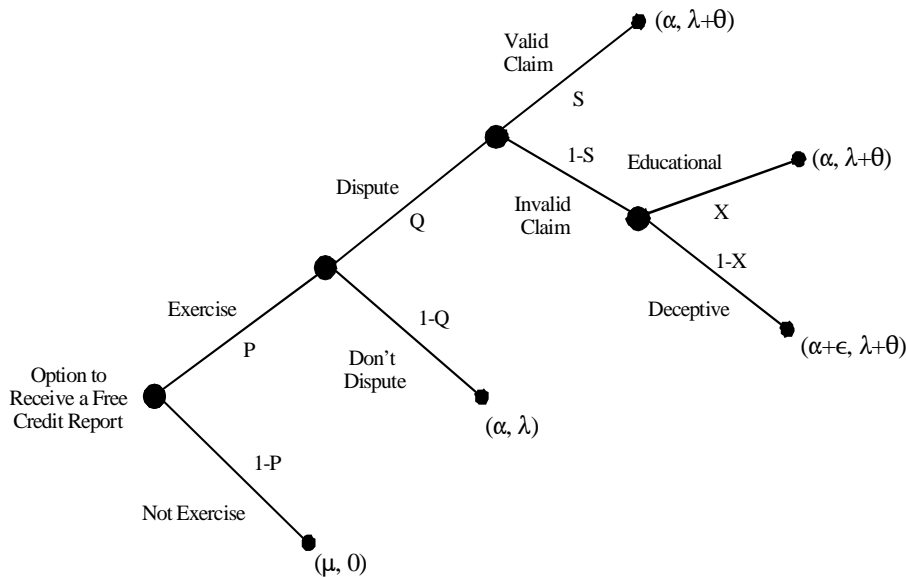
Consumers will choose to exercise their option when the marginal benefit of receiving the report ( $\alpha$ ) exceeds the hassle of taking the time and effort to request the report ( $\mu$ ). For each consumer, the value derived from the peace of mind of knowing that his/her credit data are accurate will depend on the individual's particular characteristics and circumstances. For example, the marginal benefit of requesting a credit report will likely be higher prior to the consumer's application for credit. Or, if a consumer is particularly concerned about the possibility of identity theft, the consumer may derive significant peace of mind from reviewing his/her credit report once a year. The credit reporting industry has also suggested consumers may request a copy of their report following a security breach notice.<sup>40</sup>

For many consumers, however, the perceived hassle of taking the time to request the report may simply not be worth the effort to exercise the option. This will be especially true for those consumers who are not well informed about the importance of accurate credit data or the risk of identity theft. As consumers become more aware of these issues, the proportion of consumers who choose to exercise their option will likely increase.

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<sup>40</sup> Prepared testimony from Consumer Data Industry Association CEO and President Stuart Pratt, *Fair and Accurate Credit Transactions Act of 2003*, hearing on H.R. 2622, 108<sup>th</sup> Congress, 1<sup>st</sup> sess., July 9, 2003, p. 11-12, at [<http://financialservices.house.gov/media/pdf/070903sp.pdf>], visited Dec. 16, 2003. Credit card companies may send security breach notices when their customer databases have been compromised either internally or by an outside source. These notices generally include the type of information that may have been compromised and the steps the company is taking to resolve the breach and insure that customer information is not used in an inappropriate manner. Such notices may also encourage consumers to check their credit reports for inaccuracies resulting from the breach.

**Figure 1**  
**The Consumer's Decision Tree**



Legend:

- P = proportion of consumers who exercise their right to receive a free credit report
- Q = proportion of consumers who decide to dispute the information contained in the credit report
- S = proportion of disputed claims that are valid errors and need to be corrected
- X = proportion of invalid claims that are actually consumers calling in with questions
- $\mu$  = opportunity cost of requesting a free report for the consumer (the "hassle" factor)
- $\alpha$  = benefit to the consumer of an error-free report (the "peace of mind" factor)
- $\lambda$  = cost to the credit bureau for issuing a report (includes cost of processing and delivery)
- $\theta$  = cost to the credit bureau of investigating a dispute (includes personnel and training costs)
- $\epsilon$  = benefit to the consumer from getting adverse data incorrectly removed (the "gaming the system" factor)

**Source:** Congressional Research Service

**2. The proportion of consumers who dispute (Q).** Of those consumers who decide to exercise their option, there will be some proportion (Q) who decide to dispute the information contained in their credit reports. Some of these disputes will be valid (S) in the sense that the errors are legitimate and the credit reporting agency is responsible for correcting them. There will, however, also be some invalid claims. Of this type of claim, some proportion (X) will be educational. In other words, a consumer has a question or suspects there may be erroneous information in his/her report, when in fact, it is correct. The remainder of invalid claims (1-X) can be categorized as deceptive. For instance, the industry states that, according to the FTC, credit repair agencies "are notorious for submitting false claims of inaccuracies with the sole intention of deleting accurate information off of credit files."<sup>41</sup> Thus, the proportion of consumers who dispute (Q) will depend on the frequency of credit

<sup>41</sup> Prepared testimony from the Consumer Data Industry Association (CDIA) CEO and President Stuart Pratt, *The Accuracy of Credit Report Information and the Fair Credit Reporting Act*, hearings, 108<sup>th</sup> Congress, 1<sup>st</sup> sess., July 10, 2003, p. 14, at [http://banking.senate.gov/03\_07hr/071003/pratt.pdf], visited Dec. 16, 2003. For more information on credit repair agencies, see the Federal Trade Commission website at [http://www.ftc.gov/bcp/conline/edcams/repair/index.html], visited on Dec. 16, 2003.

data inaccuracies, the credit report literacy of consumers, and the prevalence of credit repair activities.

### 3. A credit bureau's processing and investigation costs ( $\lambda+\theta$ ).

Providing consumers the option to receive a free credit report is costless to a consumer reporting agency if no consumers exercise their right (i.e. if  $P=0$ ). For every consumer who does exercise the option, the minimum cost that the credit bureau will incur is the cost of processing and delivering the credit report ( $\lambda$ ). This cost will vary depending on the mode of delivery (mail vs. electronic) and the length of the report. Once the report is received, if the consumer chooses to dispute, there will be an additional cost ( $\theta$ ), which represents the personnel and training costs associated with handling each dispute.<sup>42</sup>

## A Practical Application to the Credit Reporting Industry

Given this general model, data from the credit reporting industry can be used to calibrate different cost scenarios.<sup>43</sup> Although there exists a lack of publicly available data, the following information has been collected from recent testimony and conversations with industry representatives:

- Each of the three nationwide credit repositories (Experian, Equifax, and TransUnion) maintains 190 million credit files.<sup>44</sup>
- 16 million credit reports are issued to consumers each year. In other words, 8.4% of credit-using consumers request a copy of their credit report.<sup>45</sup>
- Of those 16 million reports, nearly 95% or 15.2 million consumers receive the report for free.<sup>46</sup>
- A breakdown of the 16 million reports by reason of request shows that 84% were disclosed due to adverse action, 11.5% were due to fraud claim, 5.25% were due to curiosity, 0.4% were to due to being

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<sup>42</sup> For simplicity, the model assumes that dispute costs are the same regardless of the type of dispute. In reality, however, it is likely that the cost of answering consumer questions is less than the cost of conducting a full reinvestigation process.

<sup>43</sup> CRS uses industry reported data in this analysis as it is the only available data on these costs.

<sup>44</sup> See the CDIA website at [<http://www.cdiaonline.org/about.cfm>], visited on Dec. 16, 2003.

<sup>45</sup> Prepared testimony from CDIA CEO and President Stuart Pratt, *Fair and Accurate Credit Transactions Act of 2003*, p.10.

<sup>46</sup> *Ibid.*, p. 10. Also, Harry Gambill, CEO of TransUnion, testified on June 12, 2003 before the House Subcommittee on Financial Institutions and Consumer Credit that it issues approximately 8 million free credit reports each year. For more details on Harry Gambill's testimony, see U.S. Congress, House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit, *The Role of the Fair Credit Reporting Act in the Credit Granting Process*, hearings, 108<sup>th</sup> Congress, 1<sup>st</sup> sess., June 12, 2003, Q&A session following official proceedings (Washington: Federal News Service, 2003).

unemployed and seeking employment and 0.1% were due to a consumer being on public assistance.<sup>47</sup>

- TransUnion estimates that in the 44 states that do not have a law requiring credit bureaus to provide an annual free credit report upon request, the consumer request rate ranges between 1.5% and 2%. In Georgia, Massachusetts, New Jersey, Maryland and Vermont, the request rate ranges between 3.5 to 4%. In Colorado, where consumers are notified that they may receive a free credit report under two specific circumstances, the request rate jumps to between 10 and 11%.<sup>48</sup>
- Fewer than half or just under 8 million consumers dispute after receiving a copy of their credit report.<sup>49</sup>
- As much as 50% of call backs to a credit reporting agency are of an educational nature, where consumers simply have questions about their reports.<sup>50</sup>
- The industry estimates that disputes submitted by credit repair agencies represent as much as one-third of all disputes.<sup>51</sup>
- Large lenders are charged approximately \$0.37 when a credit report is issued to them.<sup>52</sup> The cost to a credit reporting agency of issuing a credit report to a consumer can range between \$1.00 and \$2.00.<sup>53</sup>
- The industry estimates that the average cost of issuing a consumer credit report that results in a reinvestigation is \$10.<sup>54</sup>

By applying these industry figures to the general economic model outlined above, it can be shown how the cost estimates can vary significantly depending on

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<sup>47</sup> Prepared testimony from CDIA CEO and President Stuart Pratt, *The Accuracy of Credit Report Information and the Fair Credit Reporting Act*, p. 8.

<sup>48</sup> These figures were provided to Representative Darlene Hooley's office after she requested this information from TransUnion's CEO, Harry Gambill, during a June 12<sup>th</sup> hearing before the House Subcommittee on Financial Institutions and Consumer Credit. During the Senate Banking Committee hearing on July 10, 2003, however, one Senator offered figures provided by a credit reporting agency that suggested that the request rate ranged between 2.21% and 6.14%.

<sup>49</sup> Prepared testimony from CDIA CEO and President Stuart Pratt, *The Accuracy of Credit Report Information and the Fair Credit Reporting Act*, p. 12.

<sup>50</sup> *Ibid.*, p. 12.

<sup>51</sup> *Ibid.*, p. 14.

<sup>52</sup> U.S. Congress, House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit, *The Role of the Fair Credit Reporting Act in the Credit Granting Process*, hearings, 108<sup>th</sup> Congress, 1<sup>st</sup> sess., June 12, 2003, Q&A session following official proceedings (Washington: Federal News Service, 2003).

<sup>53</sup> Based on conversations with the CDIA's CEO and President Stuart Pratt on July 9, 2003.

<sup>54</sup> Based on conversations with the CDIA's CEO and President Stuart Pratt on June 17, 2003.

the assumptions for P and Q. **Table 1** (attached at the end) illustrates the range of possible cost estimates under different scenarios.<sup>55</sup>

The benchmark case assumes the industry's estimate for the number of consumers who are receiving free credit reports under the current federal provisions. As can be seen from the table, if it is true that approximately half of these consumers call back with either a question or a dispute, the model estimates that it is likely costing the industry anywhere between \$83.6 million and \$91.2 million.

If credit bureaus were required to provide an annual free credit report to all credit-using consumers who request one, the industry estimates that there could be as much as a fourfold increase in the number of consumers who request a free report.<sup>56</sup> Under this scenario, the table shows that the costs to the industry could range anywhere from \$66.3 million to \$608.0 million, depending on the number of consumers who decide to dispute and the unit cost of issuing a consumer report. If one assumes that roughly half of these consumers will dispute, then the cost could range from \$334.4 million to \$364.8 million. Thus, under this assumption, the model estimates that the additional cost of the policy could cost the industry anywhere from \$250.8 million to \$273.6 million, which is roughly in line with the industry's assessment of a quarter billion.<sup>57</sup>

However, given the request rates reported by TransUnion and other credit bureaus for states that already require annual free credit reports, the data suggest it is more likely that there will be a twofold or a threefold increase in the number of free reports requested. Once again assuming that approximately 50% of those consumers will dispute, the cost to the credit reporting industry could range between \$167.2 million and \$273.6 million. Thus, under these assumptions, the additional cost of the policy to the credit reporting industry could be anywhere from \$83.6 million to \$182.4 million.<sup>58</sup>

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<sup>55</sup> The estimates presented in Table 1 assume that a consumer requests a free credit report from only one of the three nationwide credit bureaus. The calculations would clearly be higher if one assumed that a consumer requested a free report from all three credit repositories.

<sup>56</sup> U.S. Congress, House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit, *Fair and Accurate Credit Transactions Act of 2003*, hearing on H.R. 2622, 108<sup>th</sup> Congress, 1<sup>st</sup> sess., July 9, 2003, Q&A session following official proceedings (Washington: FDCH Political Transcripts, 2003).

<sup>57</sup> *Ibid.*

<sup>58</sup> On September 9, 2003, the Congressional Budget Office (CBO) published its own estimate of the cost to consumer reporting agencies for providing mandatory annual free credit reports upon request. CBO assumed a threefold increase in the number of consumers requesting a free credit report each year and estimated that the issuance cost (or direct cost) would range from \$30 million to \$60 million per year. To estimate the secondary effect of reinvestigations, the agency assumed that approximately half of those individuals would dispute the information. In accordance to CBO industry sources, the cost per reinvestigation is likely to range between \$7.00 and \$8.00, not \$10.00, so the total cost of the secondary effect would range from \$110 million to \$125 million per year. For more information, see (continued...)

Theoretically, however, all credit-using individuals could decide to request a free credit report. If approximately half of these consumers dispute, the model estimates that the cost to the credit reporting industry could range between \$1.045 billion to \$1.140 billion. Subtracting these costs from the benchmark scenario, the additional cost of the policy to the credit reporting industry could theoretically range between \$961.4 million to \$1.0488 billion.

It is important to note that the calculations presented in this report are based on information that was publicly available in July 2003, collected from hearing testimonies and conversations with industry representatives. More accurate estimates of the cost to the credit reporting industry could be derived using the general model with more detailed data on the unit cost of issuance and the cost for different types of disputes. Furthermore, the calculations do not reflect the possibility of greater efficiencies or economies of scale over time.

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<sup>58</sup> (...continued)

the CBO web site at [<http://www.cbo.gov/showdoc.cfm?index=4547&sequence=0>], visited on Dec. 16, 2003.



**Table 1. Potential Cost Scenarios for the Credit Reporting Industry**  
(in thousands of dollars)

(Q, λ)	P=0.08 or 15.2 million (Benchmark Case)		P=0.16 or 30.4 million (Twofold Increase)		P=0.24 or 45.6 million (Threefold Increase)		P=0.32 or 60.8 million (Fourfold Increase)		P=1 or 190 million (Theoretical Max)	
	\$1.00	\$2.00	\$1.00	\$2.00	\$1.00	\$2.00	\$1.00	\$2.00	\$1.00	\$2.00
0.01	16,568	31,616	33,136	63,232	49,704	94,848	66,272	126,464	207,100	395,200
0.10	28,800	42,560	57,760	85,120	86,640	127,680	115,520	170,240	361,000	532,000
0.25	49,400	60,800	98,800	121,600	148,200	182,400	197,600	243,200	617,500	760,000
0.50	83,600	91,200	167,200	182,400	250,800	273,600	334,400	364,800	1,045,000	1,140,000
0.75	117,800	121,600	235,600	243,200	353,400	364,800	471,200	486,400	1,472,500	1,520,000
1.00	152,000	152,000	304,000	304,000	456,000	456,000	608,000	608,000	1,900,000	1,900,000

Note:

These estimates are calculated from the following formula based on the model:

$$\text{Cost} = [\# \text{ of consumer credit files} * P] * [(1-Q) * \lambda + Q * (\lambda + \theta)]$$

where

# of consumer credit files = 190 million

λ+θ = \$10

P = proportion of consumers who exercise their option

Q = proportion of consumers who dispute

λ = the cost of processing and delivering the credit report

The Q=0.50 row is highlighted since the industry estimates that approximately half of consumers dispute.