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CREDIT REPORTS AND THE FAIR CREDIT REPORTING ACT

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The purpose of this Article is to explain how credit reports are compiled in the context of the extension and rejection of credit by mortgage companies, national banks, and thrift institutions. All national banks, mortgage companies, and thrifts are not created equal. They do not operate using the same criteria. Consequently, what has emerged is a somewhat disorganized process that is used to make decisions to extend credit for residential mortgage purposes.

Credit reporting agencies, often called credit bureaus, gather information on credit users. These agencies sell this information to banks, finance companies, and retailers. In addition, the credit reporting agencies maintain records on all consumers. This information shows the accounts a consumer has, how a consumer has made payments on those accounts, how much the consumer owes, whether the accounts are up to date or are overdue, whether action has been taken against a consumer, and whether a consumer has been assigned for collection purposes.

Credit agencies or bureaus cooperate with each other. Thus, if a consumer moves to a different city, the credit agency which maintained that consumer's records will transfer those records to another agency located near the consumer. The agencies typically transfer files via computer tape although they can use some other form of data transfer. Sometimes the transfer process is corrupted because the agencies do not always validate the accuracy of the records prior to transfer. Although the credit bureaus keep information about consumers, the bureaus do not track all aspects of the consumer's personal life or evaluate credit applications.

There are three main credit bureaus throughout the country. The first bureau is called Equifax and is based in Atlanta.[1]

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1. Carrie Teegardin, *One Man's Tale from Credit-Bureau Hell*, ATLANTA J. & CONST., June 5, 1994, at A1.

Equifax is a publicly owned company whose 1993 revenues were $1.2 billion.[2] Equifax will offer the consumer a free credit report if the consumer was denied credit or denied an extension of credit.[3] Otherwise, it will charge the consumer $8.[4] Equifax has a toll free line that the consumer may call to request a copy of his or her credit report if he or she has been denied credit.[5] Otherwise, they prefer that the consumer communicates with them via mail, identifying himself or herself by address and social security number to gain access to his or her credit file.[6]

The second agency is TRW, headquartered in Cleveland.[7] It is also a publicly owned company.[8] TRW's credit reports are free once a year for all consumers and free upon request whenever the consumer has been denied an extension of credit.[9] The third major credit bureau is Transunion, a privately held company headquartered in Chicago.[10] Transunion will issue free reports to persons who are denied credit.[11] Otherwise, the cost is $8.[12]

There are more than 1,100 credit and mortgage reporting companies in the United States. There are more than 450 million credit files on American consumers. One in three people who view their credit report end up disputing the information. Seventy-five percent of the disputes are corrected with some sort of protracted negotiation and/or discussion.[13] The federal Fair Credit Reporting Act governs the collection, distribution, reporting, and correction of errors on credit reports.[14]

A variety of information appears in credit reports. The first item is identification and employment data: the consumer's name, birth date, address, and social security number. The agencies can determine where the consumer has lived or where he or she was born through his or her social security number. The credit agencies also provide other information, such as employment history, home ownership, income, previous address, payment history, other creditors and the amount of credit extended, method of repay-

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2. *Id.*
3. *Id.*
4. *Id.*
5. *Id.*
6. *Id.*
7. *Id.*
8. *Id.*
9. *Id.*
10. *Id.*
11. *Id.*
12. *Id.*
13. *But see TRW Plans to Offer Free Credit Reports to Consumers Once a Year*, COLUMBUS DISPATCH, Oct. 15, 1991, at B1 (discussing the errors in credit reports and the denial by the credit bureaus of any severe problems with the accuracy of credit reports).
14. 15 U.S.C. § 1681 (1992).

ment, and whether a borrower's account has ever been referred to a collection agency.

Credit bureaus are required to maintain a record of all potential creditors that have requested a consumer's credit history within the past six months. However, in many instances inquiries are made on consumers that are neither authorized nor known to those consumers. Those inquiries are held against the consumer when he or she applies for a residential mortgage because that is one of the factors that is used to determine credit worthiness. Credit bureaus also compile information that is a matter of public record, such as information related to bankruptcies, foreclosures, and tax liens.

Under the Fair Credit Reporting Act, credit bureaus can report most negative information for no more than seven years.[15] The seven year period runs from the date of the last regularly scheduled payment that was made before the account became delinquent, unless the creditors took a later action on the account, such as charging it off or obtaining a judgment for the amount owed.[16] There are exceptions to the seven year rule. Bankruptcies may be reported for ten years.[17] Also, negative credit history information may be reported indefinitely in three circumstances: (1) credit transactions involving $50,000 or more;[18] (2) underwriting of a life insurance policy with a face amount of $50,000 or more;[19] or (3) employment of an individual for an annual salary of $20,000 or more.[20]

TRW, Equifax and Transunion do not maintain the same data on consumers. If a consumer were to obtain a credit report from each of these entities, the consumer would find that the reports contain different information about the same individual.

Besides providing information about the consumer, a credit report also identifies the lender and loan type. In addition, the report identifies the borrower, including maiden name, if applicable. The report not only lists the borrower's present and former address during the past two years, but also, the employers of each consumer borrower as well as the dates of employment. All accounts listed on the original application for mortgage credit should be included on the credit report.

Adverse credit listed on the credit report should be identified and investigated by the borrower. Adverse credit is primarily delinquency. All accounts listed on the original application should

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15. § 1681c(a)(2)-(6).
16. § 1681(c)(a)(2)-(6).
17. § 1681c(a)(1).
18. § 1681c(b)(1).
19. § 1681c(b)(2).
20. § 1681c(b)(3).

be included on the credit report. The reports are typically issued from an independent consumer reporting agency.[21] All information in the report should be obtained from and verified by sources other than the borrower. The reporting agency will contact at least two national repositories of accumulative credit records for each locality in which the borrower has lived during the most recent two year period. Repositories are one of the big three: Transunion, TRW or Equifax. When co-borrowers have individually obtained credit, separate repository inquiries are often necessary, e.g., a maiden name check. The results of reports on a borrower and co-borrower may be combined into one report if the report clearly indicates that this has been done. The reporting agency should verify in writing or by telephone the borrower's current employment and, if possible, the borrower's income.[22] If the borrower has been employed for less than two years, the reporting agency must verify previous employment. When the consumer agency has incomplete information or when it discovers undisclosed credit or public records, the agency should interview the borrower to obtain the additional information needed to issue a quality report.[23] The credit report must present all data in a format that is easy to read.[24] The report must contain all discovered credit and legal information for the past seven years.[25] The report should also indicate the dates the accounts were last updated. Each account balance must have been checked with the creditor within ninety days of the report. The agency must respond to items on the report such as any inability to verify or an employer's refusal to verify. The report must be an original report with no erasures, "white-outs" or alterations. The report must contain the full name, address and phone number of the reporting agency. The report must be delivered to the office of the lender who requested it or the office of the requesting lender.[26]

The report which is provided to the national bank, thrift or mortgage company is not the same report which will be provided to the consumer. This is important for litigators because they need to know that they are not on an even playing field with the lenders. When the consumer is denied credit, the lender will not provide the consumer with a copy of the credit report. Instead, the lender might inform the consumer that they are prohibited from doing so. Generally, the lender will give the consumer the name and address of the repository who issued the report, and tell the

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21. *See* § 1681b(f).
22. *See* § 1681b(d).
23. *See* § 1681e(b).
24. *See generally* § 1681e(b).
25. § 1681c(a)(6).
26. *See generally* § 1681.

consumer to obtain a copy of the report by contacting the repository. The lender may or may not sit down with the consumer once he or she obtains the report and compare the lender's report with the consumer's report.

The report must include all available public records such as judgments, foreclosures, tax liens, and bankruptcies for the past seven years.[27] For each debt listed, the report must give the creditor's name, the date the account was opened, the amount of the highest credits, the unpaid balance, the current status of the account, and the required payment amount.[28] The report must also show the payment history, including the historical status of the account and a list of the items paid late. It is not acceptable just to reflect "satisfactory" or "paid as agreed."[29]

In addition, there are some things that the three main credit bureaus consider a liability. A revolving charge account is considered a liability because the borrower could exceed the credit limit after the creditor extends credit, which would affect the front and back ratios and the borrower's ability to carry the loan to term. Other items that are considered a liability are installment loans, real estate loans, term loans, debts from previous marriages, outstanding past due accounts, and debts from inquiries.

There is a system in the marketplace called credit scoring. Financial institutions claim that credit scoring allows for objectivity and standardization of the process of granting credit by using quantitative analysis. A credit scoring system involves converting information or characteristics from the credit application or the credit bureau report into numbers or score weights which are added to produce a score. The resulting scores are ranked and a cut off is selected to separate loan approval and rejection based on risk. The scoring system is based on application information and credit bureau information. The application information used to determine an applicant's credit score is: time at residence, time at employment, total credit score, loan amount requested, number of payments, estimated monthly payment, cash price, percentage of down payment, collateral value of the property, loan to value, total monthly income, total monthly payment present, the total monthly payment future, debt ratios present, and debt ratios future.

The credit bureau information may or may not be accurate. The consumer should obtain a copy of the credit report before applying for a mortgage loan. The information that could be held against the consumer includes: number of inquiries, whether the borrower represented previous approvals or denials, number of

27. *See generally* § 1681c(a).
28. *See generally* § 1681(b).
29. *See generally id.*

satisfactory accounts, number of minor derogatory references, number of major derogatory references, outstanding installment balances, outstanding revolving balances, total revolving balances, sum of revolving payments, and sum of installment payments. Each one of these factors is given a weight that could be considered against the consumer. Generally, a chief underwriter or a committee (known as a "processor") makes the decision whether or not to approve the loan. Once the information is gathered, and the consumer is denied credit, it is very difficult to change the decisionmaker's mind. However, if there is a system in place, it is not impossible to do so.

It is probably not possible for an attorney who represents a person denied a loan to get around the issue of credit reports, inasmuch as they play a vital role in the extension of credit. In order to attack the process, the attorney may argue that the enumerated factors used in the decision-making process do not accurately predict who constitutes an acceptable credit risk. The attorney will probably have to attack the accuracy of the report and the process in which information was acquired. Thus, litigators have to learn to navigate whatever landscape has been created by each respective financial institution. Often the starting point is simply inquiring what it takes to complete a deal. For instance, it is not unusual for people with tax liens, judgments and garnishments to be issued mortgage loans.

The attorney should look for the "skinny, thick file." This is an accurate description because the thick files are filled with a lot of work done to overcome any negatives that a prospective borrower may have encountered early in the process. These persons are instructed to close certain accounts, pay off certain debts, get some "mattress money," borrow some money, or have a balance in the account to reflect some sort of liquidity. Other persons will have a slim file because they have not been told how to correct their deficiencies.

The attorney must also seek the automated notepad maintained by the institution to find out what calls were made, what was said, and what was received and transmitted during the loan processing. Litigators may have to attack the predictive value of the criteria and the tools used to evaluate credit. This will require engaging an expert to discuss what criteria is really predictive and therefore, acceptable.

Credit plays an important, if not crucial, role in why someone is not given a mortgage. Attorneys who represent persons who have been denied a loan must be prepared to give the credit report strict scrutiny.