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Reputation under Regulation

The Fair Credit Reporting Act at 40 and Lessons for the Internet Privacy Debate

by Jim Harper

Executive Summary

More than 40 years ago, Sen. William Proxmire (D-WI) guided the Fair Credit Reporting Act (FCRA) through Congress, seeking to improve the operations of the credit reporting industry. The complexities and tensions in a reputation system like credit reporting are formidable, however, and the FCRA has not satisfied consumer-group demands for accurate, responsive, fair, and confidential credit reporting. In fact, new problems have emerged, such as credit repair fraud and identity fraud.

Credit reporting today is anything but the confidential service Proxmire hoped for. Passed in tandem with a financial surveillance law called the Bank Secrecy Act, the FCRA has been turned toward government and corporate surveillance, providing little or no privacy or control for consumers.

As economic theory predicts, the credit reporting industry appears to have benefited from the ossifying effects of regulation. Though the information and technology environments have changed dramatically over the last four decades, the credit reporting and reputation marketplace has seen little change or innovation. A potential related market for identity services is also stagnant thanks in part to government policies.

When Congress chose to preempt common law remedies for wrongs done by credit bureaus, it withdrew a tool that could have guided credit reporting toward better service to consumers and a more innovative and vibrant marketplace. With uniform national regulations, we cannot know how credit reporting might have evolved for the better.

These 40 years of information regulation under the Fair Credit Reporting Act hold lessons for present-day debates. Foremost: legislators, regulators, and advocates lack the knowledge that it takes to anticipate and guide the direction of technology, privacy, or the information economy. These things should be left to the people and businesses who are together building the future.

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The Fair Credit Reporting Act is a highly complex piece of information regulation.

Introduction

On January 31, 1969, Sen. William Proxmire (D-WI) went to the floor of the U.S. Senate to speak about legislation he was introducing that day. His bill would address problems with credit bureaus, the companies that collect information on individuals' creditworthiness, character, or general reputation and disseminate it to banks, credit card issuers, and others. He discussed his many concerns with credit reporting and his plan to solve them.

"Perhaps the most serious problem in the credit reporting industry," Senator Proxmire said, "is the problem of inaccurate or misleading information. There have been no definitive studies made of just how accurate is the information in the files of credit reporting agencies. . . . Everyone is a potential victim of an inaccurate credit report. If not today, then perhaps tomorrow."[1]

He called his bill the Fair Credit Reporting Act. It proposed a number of requirements for credit bureaus meant to help ensure that the information in credit files would be accurate, relevant, and confidential. To inform people about credit reports, users of them would have to disclose to consumers when credit reports formed the basis for adverse decisions. Credit bureaus would have to allow individuals to correct inaccurate or misleading information. Congress passed Proxmire's bill late the following year, and President Richard Nixon signed the Fair Credit Reporting Act into law.

More than four decades after Proxmire's bill became a law, and after dozens of amendments to it, the Fair Credit Reporting Act is a highly complex piece of information regulation that appears not to have achieved its goals. According to consumer advocates, credit reports are still rife with errors, and credit reporting remains an obscure challenge for many consumers. The Federal Trade Commission is only part way through the study of credit reporting that Proxmire lamented not having in 1969.[2] And under regulation, credit reporting has become nothing like the "confidential" system that Proxmire sought. On the contrary, regulated credit reporting facilitates corporate and government surveillance.

How is it that four decades of federal regulation have not achieved the goals Proxmire sought for credit reporting? Why is a fair and privacy-protective credit reporting industry so elusive? The answers are not obvious, but experience under the FCRA serves as a caution about regulating our information economy top-down from Washington, D.C. This is not because information collection, processing, and use are free of problems, but because regulation is ill-equipped to solve them.

Credit reporting involves deep complexities, including identification issues, contested notions of relevance, and the surprisingly difficult problem of arriving at "fairness." Government regulation of credit reporting has not effectively solved these problems or reconciled the conflicting values that drive them. Meanwhile, the Fair Credit Reporting Act has likely protected the credit reporting industry from competition, denying consumers the benefits of innovation.

When the Fair Credit Reporting Act preempted state common law remedies against credit bureaus, it foreclosed an option that may have resulted in better protection for consumers and better results for the economy and society. Because Congress imposed a national credit reporting rule, we cannot know how this industry might have developed had it been left free to experiment, subject to simple rules against harming consumers.

The lesson of four decades under the Fair Credit Reporting Act is that information regulation—in the name of credit reporting fairness, privacy, or whatever goal—is complex and value-laden. Because the federal government lacks the capacity to foresee how technology, the economy, and society will evolve, it should not regulate information practices. Deviating from our nation's founding principles of freedom is as much a mistake in the information arena as in any other.

With an online world far more advanced and complex than the credit reporting industry of 1969, it is worth examining carefully what we know and what we do not know about the information environment. Despite fulsome good intentions, no expert group or legislative body has the capacity to dictate how the Information Age should take shape. Many in society do not yet understand that they are participants in an information economy, not even the simple, contained part of it known as credit reporting.

What Is Credit Reporting?

A credit report is a record of a person's financial activities intended for use in determining creditworthiness, and also in some employment and insurance decisions. It lists credit card accounts and loans, the balances on those accounts, and how consistently a consumer makes his or her payments. It also shows if any action has been taken against a consumer because of unpaid bills.[3] Firms that lend to consumers provide the data they have collected to credit bureaus, who compile such information from a number of sources, then distribute those compilations back to "data furnishers" and to others.

Credit reporting began in the late 1800s with local merchants pooling information about which customers failed to pay credit accounts.[4] During this period, retailers did much business by extending their own credit, but nowadays credit cards have supplanted store credit. Credit reporting allows retailers to refuse credit sales to deadbeats and to better serve the good credit risks among their customers. In the 1970s there were more than 2,000 credit bureaus, but the inefficiency of their operating separately in an increasingly mobile society was becoming clear. Large credit bureaus emerged in response to increasing mobility in American society and to take advantage of the economies of scale that new computing and communications technologies were creating.

Today there are three major credit bureaus: Experian, TransUnion, and Equifax. Every user of credit in the United States almost certainly has a file with at least one credit bureau, and most probably have files at all three. As of 2005 over two billion items of information were added to the files of the credit bureaus every month, coming from 30,000 lenders and other sources. Credit bureaus issued over three million credit reports every day.[5]

Access to data on a large universe of credit users helps lenders calculate the risk of default on unsecured consumer loans. With large amounts of data, they can develop sophisticated algorithms that enable finer and finer judgments about borrowers. This intelligence lowers credit risk overall, meaning that credit can be offered less expensively to most people, though, of course, the cost of credit may be higher for the relatively small number of people who appear at higher risk of defaulting on loans.[6]

Credit bureaus originally provided only the raw data behind a credit decision, but they have come to do analysis of the data—credit scoring—if the lender wants to purchase it. They do not make the final decision about whether or not to lend or on what terms. Lenders make those decisions.

Credit Reporting as a Reputation System

Though nobody used such lingo in the 1970s, a credit bureau is a type of "reputation system." It is a tool that supports decision-making on a large scale or by a large number of users.

A credit bureau is a type of "reputation system."

Every individual has a reputation within his or her social circle, family, and work environment, of course, but these individual reputations are not useful in remote transactions or in transactions with large, impersonal institutions. The idea of systems that provide reputation information on a large scale has come into its own over the last few years as an adjunct to mass, remote transacting.[7] Credit reporting is probably the original and longest-standing large-scale reputation system.

Reputation systems outside of credit reporting include things like eBay's Feedback Forum, where buyers and sellers rank each other and comment on past transactions.[8] This helps future buyers and sellers gauge the risks of dealing with one another and

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encourages good behavior. EBay users know that the transactions available to them and the prices others will pay them may shrink if they misbehave by misrepresenting the goods they sell, paying slowly, and so on.

A reputation system is a complex social mechanism. It combines two separate concepts, identity and biography, each with its own difficulties.

Take identity. Figuring out precisely who people are is hard to do on a mass scale. Over the last century, changing circumstances have made names like "John Smith" indistinct and obsolete for use as identifiers.[9] There are more people, communications have improved, and mobility has increased. This makes it more likely that two people in the same (now more populous) place will have the same name. Even unusual names may be repeated several times in a country with tens or hundreds of millions of inhabitants. Growth in the size, scope, and complexity of organizations has likewise increased the chance that they will encounter duplication among names.

The response has been to turn to uniform identifiers like the Social Security number. These help institutions such as credit bureaus sort among millions of consumers, the indexing system in the institutional "mind." But the Social Security number is a weak identifier that is not fixed to any individual.[10] It is relatively easy for a person to adopt another's SSN for the purposes of identity fraud. And SSNs are often misreported or incorrectly transcribed, leading to errors in tying data to the right identity.

Then there is biography. Biography would simply be connecting factual information to an identity, but the relevance of given facts to given decisions can be contentious. Determining what factual information goes into a biography that is "right" or "fair" implicates a host of social values and norms.

What is "fairness"? Every child learns about the concept of fairness on the playground, but it remains a complex and elusive concept. The manifold values that go into making any particular decision "fair" are beyond all but the most careful philosophers.

One might say that fairness is some assurance that each person will get his or her due, but that begs the question of what is due. Fairness can include, in different measures, the absence of wrongful bias, consistency of rules, honest administration, and so on. Fairness is not a guarantee of correct decisions in every instance. Fulfilling that goal would raise administrative costs in many decisionmaking systems beyond the value of deciding. Most decisionmaking systems essentially punt. In courts of law, for example, a "fair" trial is one that is merely well calculated to produce the correct outcome. It is not a trial process in which the right result is reached every single time.[11]

Fairness often involves giving the affected party some opportunity to participate in a decision. Thus, constitutional fairness includes giving a criminal defendant a right to participate in his or her trial and to cross-examine witnesses.[12] Important decisions that are not produced with at least some input from an affected party are often rightly criticized as arbitrary. This is not only because a person's participation will favor a correct result. Participation fulfills the ideal that an individual has a measure of autonomy even when he is the object of another's decision.

The question of what is fair and unfair in credit reporting is a matter of ongoing controversy. A single-minded statistician would mine every piece of data about every person to determine the relevance of each item of biography to creditworthiness. The privacy advocate would object to having so much data available, regardless of the purpose. Those who believe in redemption think it is unfair for information from the distant past to haunt one's present. Redistributionists might pursue rules for credit reporting that help people get credit who otherwise wouldn't, making up for some difficulty society has laid before the consumer. All of these interests are represented in the debate about credit reporting.

With all these conflicting dimensions, credit reporting fairness is hard to administer on a mass scale. Challenges come from identity issues, judgments about biography, and the many nuances of fairness. It's no wonder that credit reporting is the subject of complaints and controversy.

What's Wrong with Credit Reporting?

When Senator Proxmire introduced the Fair Credit Reporting Act, he outlined a substantial body of "abuses" he perceived in the credit reporting system.[13] They included

- *Inaccurate Information:* Errors found their way into credit reports in a number of ways, including through confusion with other persons, biased information, malicious gossip and hearsay, computer errors, and incomplete information.
- *Difficulty in Getting Adverse Records Corrected:* Proxmire recounted reasons why it was difficult to correct inaccuracies, including consumers' general unawareness of credit reporting and credit reporting inaccuracy; the costs of correction and roadblocks set up by credit bureaus; and credit bureaus that served as collection agencies, preferring merchants' versions of events.
- *Irrelevant Information*: Proxmire bemoaned the use of information about arrests in the distant past and highly personal information going to "'character,' 'habits,' and 'morals.'"[14]

Proxmire also questioned the confidentiality of credit reporting.[15] When information collected for one purpose—health insurance, for example—is converted to other uses, such as making employment decisions, this may violate privacy by breaching the terms and expectations around its original collection.

Proxmire worried about internal security at credit bureaus.[16] Laxity in the protection of data files could lead to what we today call "data breach." Some credit bureaus would provide credit information to any company under an ambiguous "legitimate business need" standard. Proxmire also wondered aloud whether credit reports should be shared with the government.

Finally, Proxmire lamented how credit reporting systematically excluded "ghetto residents" from credit. He attributed recent riots in these areas to merchants systematically overcharging people who could not get credit from "reputable downtown retailers."[17]

Has the Fair Credit Reporting Act fixed these problems? A systematic comparison between the credit reporting industry of the late 1960s and of today would take volumes, but a survey of contemporary complaints suggests little change from when Proxmire itemized his concerns. Many problems still exist, some problems have gone away, and some new credit reporting problems have emerged.

Inaccurate Information

Proxmire's chief complaint about credit reporting was inaccuracy. Judging by the complaints of consumer advocates, this problem appears not to have been remedied by his legislation. Inaccurate information seems to plague government-regulated credit reporting as much as it did the credit reporting industry of the past.

In 2002, for example, the Consumer Federation of America and the National Credit Reporting Association produced a report titled, "Credit Score Accuracy and Implications for Consumers,"[18] which concluded that tens of millions of consumers were "at risk of being penalized" for incorrect information in their credit reports. Almost one in ten consumers, the report found, risked being excluded from the credit marketplace altogether because of incomplete records, duplicate reports, and mixed files.[19]

In 2004 the U.S. Public Interest Research Group (U.S. PIRG) asked adults in 30 states to order their credit reports and complete a survey on the reports' accuracy.[20] Among other things, their study found that 25 percent of the credit reports surveyed contained serious errors that could result in the denial of credit, such as false delinquencies or accounts that did not belong to the consumer. Fifty-four percent of the credit reports contained

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The Federal Trade Commission is currently studying the accuracy and completeness of credit report information.

personal demographic information that was misspelled, long-outdated, about a stranger, or otherwise incorrect. And almost 8 percent of the credit reports were missing major credit, loan, mortgage, or other consumer accounts that demonstrate the creditworthiness of the consumer.[21] Among the numerous sources of error alleged by U.S. PIRG, some large creditors were reporting incomplete information in an effort to drive their customers' credit scores down so that other lenders would not compete for their business.[22]

The credit reporting industry strongly disputes these findings. Consumer Data Industry Association head Stuart Pratt cited studies by the Government Accountability Office and Federal Reserve Board in 2007 congressional testimony to argue that consumer groups' error statistics are "flawed" and that the proportion of individuals affected by data problems is small.[23] A 1992 Arthur Anderson study commissioned by the industry group, for example, found that 3 percent of applicants denied credit had errors in their reports the correction of which would have resulted in a different outcome.[24] A 2011 study finds that 0.93 percent of consumer credit reports have disputed information the correction of which increases credit scores by 25 points or more. Just 0.5 percent of credit reports move to a higher "credit risk tier," potentially qualifying the subject consumer for better loan terms as a result of a modification.[25]

The Federal Trade Commission is currently studying the accuracy and completeness of credit report information. Under a provision of the Fair and Accurate Credit Transactions Act,[26] it is supposed to complete this study by December 2014. Some 45 years after Proxmire noted the absence of such a study, and 9 years after his death, he may just have it. Perhaps credit reporting accuracy that satisfies consumer advocacy groups will follow on the heels of that report.

Data Correction

Data correction also appears to remain a problem despite 40 years of FCRA regulation. The National Consumer Law Center (NCLC), for example, deplores the state of data correction in no uncertain terms:

> The dispute process mandated by the Fair Credit Reporting Act has become a travesty, with the credit bureaus conducting perfunctory investigations by translating detailed written disputes into two or three digit codes and paying foreign workers as little as $0.57 to process each dispute.[27]

The January 2009 NCLC report[28] does not say how much credit bureaus should spend domestically per dispute. But it does articulate a series of shortcuts that it alleges the credit reporting industry takes, thus denying consumers a fair opportunity to dispute material in their credit reports. The NCLC report notes other impediments to data correction as well: "Many consumers with errors in their reports do not send disputes because of barriers such as lack of time or resources, educational barriers, and not knowing their rights."[29]

A March 2005 Government Accountability Office study on "credit reporting literacy" corroborates the NCLC report.[30] The study found a surveyed population to have general awareness of credit reporting but a lack of knowledge about rights in the error dispute process, particularly among those having less education, lower incomes, and less experience obtaining credit.

There is nascent improvement in error detection and reporting with the rise of "identity monitoring" services, which alert consumers when credit applications are made in their names. This allows consumers to notify lenders that a fraud may be underway. These services are fairly costly, though, given the low risk to the average consumer of being an identity fraud victim.[31]

These were difficulties with credit record correction that Proxmire set out to fix in 1969. In general, they remain in place today.

Irrelevant Information

Some of Proxmire's concerns have been ameliorated. Prior to the passage of the Fair Credit Reporting Act, for example, credit reports often contained "lifestyle" information: things like cleanliness of the home, cohabitation among unmarried adults, and explicit or implicit references to alcohol or drug use. Subjective observations are hard to prove, and the relevance of some such lifestyle information is disputable. An FCRA requirement of "maximum possible accuracy"[32] made it too costly for credit bureaus to retain "lifestyle" information, and it has been phased out.[33] This reflects a societal judgment that allegations about "lifestyle" are too often unfair for mass decisionmaking.

Personal information going to "'character,' 'habits,' and 'morals'" is not actually irrelevant to credit reporting, of course. A nondrinker will often be a better credit risk than an alcohol abuser. A good deal of "socially unacceptable" behavior is also detrimental to financial responsibility, so it is relevant to creditworthiness.

Proxmire was probably interested in scrubbing "prejudicial" information from credit reports as much as irrelevancy. Four decades ago, if a credit applicant was a social outlier—an adult male cohabitating with another adult male, for example—this might have produced adverse credit decisions that were invalid simply because a decisionmaker was prejudiced. Cohabitating adults of the same gender may be gay, and the mere appearance of gayness at the time may have been disqualifying for credit based on anti-gay animus, regardless of the merits.

In fact, being gay may mean that a person is a better credit risk because gays have fewer dependents and higher disposable income. Or it may mean that they are poorer credit risks because they suffer employment discrimination. Or it may have a low bearing on credit risk relative to other indicia.

Today, the likelihood of prejudiced decisions in the credit market has probably dropped because they are largely computerized and data-driven. An invalid assumption that gays are a good or bad credit risk would likely be hounded out of the system by data reflecting actual behavior of this and all other categories of people.[34] Perhaps because of the FCRA, and perhaps because "lifestyle" information is hard to gather reliably and accurately, it no longer has a significant place in credit reporting.

One cost of relying on social judgments rather than statistical ones about what is appropriate for credit reporting is higher overall cost of credit. When lenders do not have all potentially relevant information available to them, they cannot make the best-informed credit judgments. The factors that are predictive of creditworthiness almost certainly go well beyond what is found in today's credit reports, though it is hard to know how much credit access society forgoes because of legal limits on the subject matter within credit reporting. The characteristics that correlate to creditworthiness should be a subject of constant study, as they undoubtedly shift over time.

Treatment of "Ghetto Residents"

Proceeding through Proxmire's goals with the Fair Credit Reporting Act: Are "ghetto residents" being judged on the merits and receiving appropriate offers of credit today? Or are they still systematically excluded? At least one recent study found that they are still excluded from consumer credit.

"Credit Card Redlining," a report published by the Federal Reserve Bank of Boston in 2008,[35] found that individuals in predominantly black neighborhoods receive less consumer credit than individuals in white areas. In spite of similar risks of nonpayment as determined by the credit score, a person living in a black area is less able to access credit.[36] A later paper disputed these findings.[37]

While the jury remains out on Proxmire's concern with the credit reporting situation for blacks, new concerns have formed, such as fraud opportunistic to the regulated credit reporting environment.

New Problems: Credit Repair Fraud, Credit Repair Mills, and Identity Fraud

Once the FCRA obliged credit bureaus to correct information in their reports, a new problem began to emerge: credit repair fraud. This is when a firm claims it can restore consumers' creditworthiness for a fee—often charged up front—using a small array of manipulations of the credit reporting system.

When lenders do not have all potentially relevant information, they cannot make the best-informed credit judgments.

Credit repair organizations are aggressive users of FCRA-mandated processes.

Credit repair outfits—be they legitimate firms or pure scams—often do not deliver.

In the early years of credit repair fraud, many scams claimed that they could permanently remove accurate information from a consumer's credit report. They would attempt to deliver on this promise by "flooding" credit bureaus with disputes. Some credit repair firms today encourage their customers to dispute all items in their credit file. Or they advise consumers to apply for an employer information number (EIN) from the IRS and use it to build fresh credit. These are misuses of the FCRA at best.

Fifteen years ago, Congress had to enact new legislation to address the fraud potential it created with the FCRA. Congress passed the Credit Repair Organizations Act[38] in September 1996, hoping to remedy the opportunistic use of FCRA rights.

Credit repair organizations are still aggressive users of FCRA-mandated processes. As of 2007 one industry estimate held that credit repair organizations are responsible for as much as 30 percent of the disputes that credit bureaus and data furnishers must reinvestigate, at a cost that is substantial in the aggregate.[39]

Credit repair organizations charge consumers for doing what consumers can already do for free under the FCRA. This defies the ideal of the FCRA, which was to make credit reporting easy enough for consumers to handle on their own. One goal of the law has not been met if consumers must pay an intermediary to navigate the credit reporting system for them.

Another problem area, not so clearly produced by the FCRA, but not well ameliorated in credit reporting either, is identity fraud. Identity fraud—often inaccurately called "identity theft"—is the use of personal and financial identifiers to impersonate others. In the most damaging case (and most relevant here), an identity fraudster will open credit accounts in the name of another, run up debt on those accounts, then abandon them. This leaves the person impersonated with potential liability for payment and with a sullied financial reputation.

One reason for the prevalence of identity fraud is its relative ease in the remote-commerce environment. The vast majority of consumer credit transactions today are done without in-person contact between the borrower, lender, or credit bureau. This produces cost savings, but it does open a vulnerability to this kind of fraud.

Identity fraud was within the orbit of the data quality problem Senator Proxmire referred to as inaccuracy and "confusion with other persons." And just as they were 40 years ago, credit bureaus are susceptible to mistaking one person for another. Since that time, identity fraud has grown up to exploit that vulnerability. The FCRA has done little to fix it, and the regulated credit bureaus have not devised effective solutions.

That is not to say that nothing has happened with respect to identity fraud in the FCRA. A lot has. The Fair and Accurate Credit Transactions Act in 2003 added a slew of amendments related to identity fraud, including new rules that allow consumers to place "fraud alerts" on their credit files. When a fraud alert is in place, lenders cannot issue new credit lines, extensions of credit, or new cards, nor allow higher credit limits on existing accounts, in the absence of steps to verify things with the consumer. Credit bureaus are required to block fraudulent trade lines when a consumer has provided them with an identity theft report that has been filed with a law enforcement agency. And identity fraud victims with a police report can get copies of records from businesses where their impersonators opened accounts or obtained goods or services.[40]

But these are elaborate treatments of the symptoms of identity fraud. They do not solve the underlying problem of identifying people suitably for the credit reporting and lending environments. Identification systems suitable for modern financial services delivery have not emerged in the regulated environment, though, of course, this is not exclusively the fault of the FCRA.

While some issues have abated through action of the FCRA, or winnowing that would have occurred anyway, new problems have surfaced or grown, such as credit repair fraud and identity fraud. Credit reporting provides undisputed value to the economy and society, but weaknesses in the credit reporting system make it hard to have confidence that this is a successful, vibrant, and—as the FCRA would have it—fair industry. So how is it doing with privacy?

Privacy

Privacy was one of the values Senator Proxmire tried to advance through the Fair Credit Reporting Act. There is deep tension, of course, between giving individuals control of information about themselves—the heart of privacy—and a reputation system that shares information widely. Proxmire referred to it as "confidentiality," suggesting a relationship in which credit bureaus would hold information as something of a trust for the benefit of the consumer.

As noted above, Proxmire aired four concerns with respect to confidentiality. "Some credit reporting agencies have only a vague policy as to whom they will furnish the information," said the senator.[41] Another concern was use of information beyond the purposes for which it was collected, such as when a person who has bought insurance sees information collected for that purpose used in an employment decision. Senator Proxmire also aired concerns about the internal security of credit bureaus and worried about the sharing of credit information with governmental agencies:

> One can certainly be sympathetic to the problems of the FBI and IRS in meeting their heavy responsibilities. But, nonetheless, their right to investigate is not absolute and is subject to various constitutional restraints including rights guaranteed by the fourth amendment on unreasonable search and seizure. Regardless of whether the individual has any legal control over the information on him in a credit reporting agency's file, I certainly feel he has a moral claim to controlling its use. He should not be entirely dependent upon the policies of the particular credit reporting agencies to protect his basic rights.[42]

When Senator Proxmire introduced the bill, it would have required credit bureaus to "insure [sic] the confidentiality of information," to destroy information after it has become obsolete, and to furnish information only "to persons with a legitimate business need for the information and who intend to use the information in connection with a prospective consumer credit or other transaction with the individual," except when the individual had agreed otherwise in writing.[43] The bill that passed the next year used the concept of "permissible purposes" to delineate with whom information in credit reports could be shared.

Over the years, amendments to the "permissible purposes" section and other FCRA provisions show that the regulated credit reporting industry has not become a repository of data held in trust for consumers. It has become a repository of data for industry and the government to use without consumers' knowledge or interference. Indeed, the story of the FCRA's passage and amendment over 40 years is the story of a tacit collaboration in which a regulated information industry gives government more and more access to Americans' personal financial information.

The regulated credit reporting industry has not become a repository of data held in trust for consumers.

The Fair Credit Reporting Act and Government Financial Surveillance

German military strategist Helmuth von Moltke is credited with having said, "No battle plan survives contact with the enemy." The dynamics are similar when a legislator's ideal plan makes contact with the public policy world. An idea that might make sense in the abstract can change quite dramatically when it encounters the real legislative process, the real regulatory process, and the real-world environment it is supposed to affect.

And it is a long, tortuous path that winds from the ideal that Senator Proxmire held out when he introduced the Fair Credit Reporting Act to the results of his bill today. Among the wrong turns in the path is privacy, or confidentiality. From the moment Proxmire's plan contacted the real world, it began to retreat from privacy protection.

To get the Fair Credit Reporting Act passed, Proxmire joined it to a financial surveillance bill known as the Bank Secrecy Act. In numerous amendments since its original passage, the FCRA has become more and more of a financial surveillance law itself. The law's passage, Supreme Court doctrine that emerged in its wake, and amendments over time show how a law meant to protect privacy has come to give the government entrée to Americans' finances and financial transactions.

On Passage: The FCRA and the Bank Secrecy Act

Having introduced the Fair Credit Reporting Act in January 1969, Senator Proxmire worked throughout that year and the next to get it through Congress. The Senate Committee on Banking and Currency reported the bill on November 5, 1969, and Proxmire oversaw its passage by the Senate the next day. The House never acted on that bill.

In September 1970, though, Proxmire attached the Fair Credit Reporting Act to a related piece of legislation moving through the Senate. He added it as a new title of the bill that would become Public Law 91-508. President Nixon signed the Currency and Foreign Transactions Reporting Act into law on October 26, 1970. That law is better known as the Bank Secrecy Act.

The Bank Secrecy Act of 1970 dragooned U.S. financial institutions into performing surveillance of their customers on behalf of the U.S. government. To this day, it requires financial institutions to keep records of cash purchases of negotiable instruments; to file reports of cash transactions exceeding $10,000; and to report suspicious activity that might signify money laundering, tax evasion, or other criminal activities. The recipient of this information is the Financial Crimes Enforcement Network (FinCEN) in the U.S. Treasury Department.[44]

A law meant to protect privacy has come to give the government entrée to Americans' finances and financial transactions.

The scope of Bank Secrecy Act surveillance has grown over time, going well beyond banks. Casinos and card clubs are required to report to FinCEN. Securities and futures trading is subject to suspicious activity reporting. Insurance companies must report customers' financial activities under the law. Reporting mandates on certain money services businesses came into effect in January 2002. Collectively, these institutions submitted more than 1.2 million reports on Americans' financial transactions during the 2009 calendar year.[45] Under the Supreme Court's current Fourth Amendment doctrine, this mass surveillance system is perfectly constitutional.

Dragnet Surveillance Made Constitutional

How can the government require U.S. businesses to report private financial transactions without violating the Fourth Amendment? A pair of Supreme Court cases litigated after the passage of the Bank Secrecy Act did a two-step around constitutional protection for private financial information.

The first case was *California Bankers Association v. Shultz*.[46] In this 1974 case, bankers challenged the Bank Secrecy Act requirement that they maintain records and file reports with the Treasury Department. The Supreme Court rejected their challenge. Requiring banks to collect information did not mean that anything was disclosed to the government, so the Court denied that it implicates the Fourth Amendment: "[T]he mere maintenance of the records by the banks under the compulsion of the regulations invade[s] no Fourth Amendment right,"[47] said the Court.

As to the reporting requirements, the Court said that bank depositors did not have standing to sue if they could not show that information about their financial transactions had been reported.[48] They had no grounds to complain, according to the Court, if their information had not been handed over to the government.

There were a number of strong dissents. Justice Thurgood Marshall, in particular, presciently criticized the Court's finding that the recordkeeping mandate was not a constitutional seizure when it was clear that the government would acquire the records later. "By accepting the Government's bifurcated approach to the recordkeeping requirement and the acquisition of the records, the majority engages in a hollow charade whereby Fourth Amendment claims are to be labeled premature until such time as they can be deemed too late."[49]

Sure enough, two years later in *United States v. Miller*,[50] the Court did exactly that. It held that a defendant had no Fourth Amendment interest in records maintained pursuant to the Bank Secrecy Act because these records had been compiled by a third party, not the government.[51] The two-step was complete, and the government could access Americans' financial records without a warrant. This is the weak foundation on which Americans' financial privacy still sits.

Surely the ills of the Bank Secrecy Act cannot be laid at the feet of the Fair Credit Reporting Act, though. In the push and pull of the legislative process, the FCRA was the privacy-protective spoonful of sugar that Senator Proxmire demanded to get the Bank Secrecy Act through Congress, was it not?

It was not. Proxmire advocated ably for the Bank Secrecy Act as its Senate manager, speaking of "stock manipulators," "swindlers," and the frustrations of Internal Revenue Service agents unable to get information to convict them.[52] He was a full promoter of mass financial surveillance. Alas, Proxmire's Bank Secrecy Act and the Fair Credit Reporting Act are siblings whose family resemblance has increased over the years.

The FCRA and Government Financial Surveillance

Whatever Proxmire's intentions, the Fair Credit Reporting Act has become a government surveillance tool in parallel with the Bank Secrecy Act. Where the Bank Secrecy Act provides the government millions of reports on people who engage in suspicious behaviors and high-dollar cash transactions, the Fair Credit Reporting Act makes available to the government hundreds of millions of reports on the financial accounts and aggregate financial behavior of everyone else. Amendments to the FCRA since its passage tell the story of how credit reporting has turned to the service of government priorities.

During its first two decades, Congress pretty much left the FCRA alone. But in 1989 Congress expanded the "permissible purposes" for which a credit bureau could furnish a report by allowing federal grand juries to take a look at people's credit files.[53] Modest though it was, that kind of amendment has been a hallmark of amendments to the FCRA since. Among the 23 amendments passed since 1990, Congress has added child support obligations to credit reports,[54] later making disclosure of credit reports to state and local child support agencies a "permissible purpose."[55] In 1996 Congress allowed disclosure of credit report information to the Federal Bureau of Investigation for counterintelligence purposes.[56]

After a heavy revamp of the law's provisions in 1996,[57] Congress in 1997 allowed the use of credit reports for investigations of people related to security clearances,[58] later making sure that holders of security clearances wouldn't enjoy the FCRA rights that are available in other employment contexts.[59]

Terrorism opened credit bureaus' files to the government yet further. In the USA-PATRIOT Act, Congress allowed the release to government officials of consumer reports "and all other information in a consumer's file" for counterterrorism purposes.[60] Congress revamped the FCRA again in 2003[61] and later that year withdrew a reporting requirement that would reveal how often federal agencies used credit reports for security clearance investigations.[62] In the USA-PATRIOT Improvement and Reauthorization Act of 2005, Congress withdrew some of its past excesses, allowing courts to modify or suppress "national security letters" aimed at credit reports. But it did permit the FBI and intelligence agencies to require secrecy about their access to individuals' consumer reports on pain of fines and imprisonment for up to five years.[63]

The Fair Credit Reporting Act has become a government surveillance tool in parallel with the Bank Secrecy Act.

If anyone harbored expectations that federal regulation would substantially fix credit reporting, those expectations have not been met.

In 2006 Congress made it a "permissible purpose" to provide a consumer report to the Federal Deposit Insurance Corporation or the National Credit Union Administration as part of their preparation for appointment as conservator, receiver, or liquidating agent for depository institutions or credit unions.[64] And in 2007 Congress made it a permissible purpose to provide a consumer report to a government agency in connection with the issuance of government-sponsored, individually billed travel charge cards.[65]

Under these amendments to the FCRA, credit bureaus have not become the confidential repositories of financial information that Senator Proxmire envisioned. They are a data source equally serving the consumer credit industry and government investigatory bureaucracies. Credit reporting has many consumer benefits, but credit data is not held in a confidential trust for the consumer.

Meanwhile, few of the other concerns that Proxmire sought to address have been solved. Inaccuracy still allegedly plagues credit reporting. The FCRA-mandated system for disputing credit reporting errors is a disappointment. The FCRA effectively created credit repair fraud, and the law has not effectively handled problems like identity fraud. Forty years of regulation have not solved the problems that go along with credit reporting..

Reputation under Regulation

Why have 40 years of credit bureau regulation under the Fair Credit Reporting Act produced disappointing results? A wag might say that the failure of the FCRA to reach satisfactory results is a product of consumer advocates' resistance to satisfaction. The joke has kernels of truth: Consumer advocates are in the business of complaining. But if anyone harbored expectations that federal regulation would substantially fix credit reporting, those expectations have not been met.

Is It Failed Enforcement?

Among the reasons a traditional consumer advocate would put forward for the FCRA's failure is the lack of enforcement by federal regulatory authorities. It is a common-sense point. At some level of "resources," the Federal Trade Commission would have staff large enough to tightly monitor credit bureau practices, insightful enough to adjudge what is fair in credit reporting, and inquisitive enough to determine once and for all what produces consumer satisfaction in this area.

Unfortunately, the spending needed to produce such an enforcement regime is an unknown. In the last 15 years, the FTC's budget has nearly tripled, from $91 million in fiscal 1995 to $268 million in 2010. (Whether the agency's FCRA work expanded at rates commensurate to its budget is unknown; it may have dedicated these funds to other priorities.) Continuing consumer-group dissatisfaction with credit reporting during this period suggests that funding increases have not produced improvement, though it certainly could be that funding is still so low relative to what is needed that a quarter billion dollars in annual FTC funding does not move the dial.

Funding is only one input into results, of course. Without a profit incentive to drive them, government agencies require oversight from Congress and ultimately the people to keep their focus. Unfortunately, Congress is a chronic underachiever in overseeing executive branch agencies, and those agencies are utterly opaque to the vast majority of people.

The reasonable argument that more funds would produce better results can neither be verified nor falsified. The failure to achieve results at present spending levels is not evidence that more funding would produce better results. But the intuitive idea that more funding, or one more amendment to the law, would produce a satisfactory system keeps many advocates working for the regulation and the regulatory agency that are just around the next corner.

None of this points to some other, easier fix, however. Credit reporting is complex, it involves formidable information-sharing and information-processing problems, and it intersects with a number of challenging societal values. The failure of the Fair Credit Reporting Act to please suggests, but does not dictate, a number of avenues for exploration, starting with our society's curious approach to credit.

There's Something about Credit

The conflicted feelings American society has about credit are fascinating and strange. On one hand, and in some periods, advocates and policymakers treat easy access to credit as an essential of modern living. On the other hand, and at other times, they portray the consumer credit industry as a scourge that preys on the lower classes—"ghetto residents," as Senator Proxmire said.

The FCRA is a clear example of credit promotion: public utility–style regulation of credit reporting meant to fulfill the goal of getting more credit to more Americans. Federal policy has long promoted easy access to credit in other ways, of course. Congress created the Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac) to create a more liquid market for mortgage debt, hoping that more people would then be able to own homes, especially people lower on the socioeconomic ladder.[66]

The Department of Housing and Urban Development (HUD) has consistently promoted homeownership through increased access to credit. In 1995, for example, HUD secretary Henry Cisneros ordered that at least 42 percent of the mortgages Fannie Mae and Freddie Mac purchased must be for "low- to moderate-income families." In 2000 Secretary Andrew Cuomo increased that target to 50 percent. These rules led Fannie and Freddie to increase their purchases of subprime loans by 10 times. In 2004 HUD secretary Alphonso Jackson increased the requirement yet further, to 56 percent. Collectively, these decisions made subprime borrowers a major segment of the mortgage market.[67]

A *New York Times* headline from the fall of 1999 sums up the policy atmosphere at that time: "Fannie Mae Eases Credit to Aid Mortgage Lending."[68] Government policy systematically pushed people toward becoming debtors for many years.

During times of contraction, such as the most recent few years, the media and politicians have portrayed consumer credit markets as exploitative dens of iniquity. A PBS *Frontline* episode on credit that aired in late 2009, for example, provided a comprehensive critique of sharp credit card practices. Its website talks about the "latest snares in the card game" and asks, "Will banks stop their tricks?"[69] In May 2009 Congress and the president passed a new law further regulating credit card practices and creating a new financial services regulator.[70]

Mortgage lending has followed the same path. In contrast to 1999's headline, the *New York Times* of early 2008 captures a new and very different public policy *zeitgeist*: "FBI Opens Investigation into Subprime Lending."[71] The government promotes consumer credit in one decade and exhibits hostility to credit the next.

Rather than this back-and-forth, the best policy would probably be indifference. In credit reporting and lending, just like many consumer markets, imperfection will deny some people what they should ideally have. But credit is not an essential good, and it is not an appropriate financial tool for people who lack the acumen to use it. People should use credit or do without credit as their circumstances—and sometimes dumb luck or error—warrant. Government policy should have nothing to say about it other than to prohibit fraud.

Cartelization, Barriers to Entry, Lost Innovation

The credit reporting industry exhibits some characteristics that are common in regulated industries, such as cartelization, which tends to suppress overall consumer welfare. Economic study over the last few decades has revealed that regulation—no matter how well-intended—is often a mechanism by which special interests use the government to create barriers to entry and other special privileges for themselves. Michael Levine, who worked with legendary economist Alfred Kahn under President Jimmy Carter to dismantle the Civil Aeronautics Board in the mid-1970s, wrote in 1981 about the true role of regulation

> as a device used by relatively small subgroups of the general population, either private corporations or geographic or

People should use credit or do without credit as their circumstances—and sometimes dumb luck or error—warrant.

The market for reputation services is artificially resistant to new entrants who might serve consumers better.

> occupational groups, to produce results favorable to them, which would not be produced by the market. The regulatory services provided were variously described as organization of a cartel, wealth transfers as a form of "taxation," enshrinement of capitalistic class interests, or preservation of congressional and bureaucratic power.[72]

It is well recognized today that the Civil Aeronautics Board cartelized the airline industry, just like the Interstate Commerce Commission had done for the railroad and trucking industries. This insulation of firms from competition enriched business owners inappropriately, and it cost consumers in higher prices and foregone travel and transport. The Federal Communications Commission, particularly in its tight control of electromagnetic spectrum, cartelizes the communications industry today.[73] Occupational licensing creates entry barriers into hundreds of occupations.[74]

Credit reporting is an industry that enjoys network effects, so the economically efficient number of credit bureaus is likely to be small,[75] but the dominance of a small number of credit bureaus over four decades of significant change in the information environment suggests that the market for reputation services is artificially resistant to new entrants who might serve consumers better.

Arguably, ever since the FCRA was passed, the credit reporting industry has served two masters: the financial institutions that furnish information and buy information products, and the government regulators that enforce the FCRA. Consumers—who could be partners in maintaining the data that typically serves them so well—are an afterthought. They enter a confusing maze when they receive adverse credit scores based on bad data, when their files are mixed with other consumers' information, or when their corrected files are re-polluted by data furnishers supplying incorrect information again.

Credit bureaus do provide an important service to a fully modern, remote-commerce economy. Far more often than not, the data aggregation they do helps worthy consumers gain access to financial services, employment, and housing. Credit reporting adds brainpower to our modern economy and makes it far more efficient and responsive to consumer interests.

But credit bureaus have not positioned themselves as a consumer-oriented business, and they have done little to instill in public consciousness the fact that they provide these valuable services. They remain essentially mysterious to the vast majority of people—obscure and shadowy handmaidens of corporate financiers, marketers, and government investigators. They collect information from sources most consumers are unaware of and use this information in ways that most consumers do not understand. The murk surrounding data aggregation prevents consumers from deciding straightforwardly between the material well-being credit reporting offers and the privacy gained by keeping financial and behavioral information private. Consumers are probably worse off for not having a clear choice.

It is up to unhampered markets, of course—not experts or this author—to figure out what serves consumers' interests best in the area of reputation. Given all the data that now courses through our economy, though, it seems strange that economic services like reputation and its close relation, identity, have seen so little innovation over the last 40 years. What might such innovations have been?

As noted earlier, eBay provides its members a reputation service that helps them gauge one another in advance of committing to sales transactions. A system for assessing "tradeworthiness" might easily be ported to credit scoring and creditworthiness. EBay's payment subsidiary, PayPal, seeks to enroll its users as credit card holders, but it does not tap the wealth of information eBay has about them to judge their financial acuity. Doing so would amount to credit reporting, which would probably require eBay/PayPal to provide FCRA rights to consumers with regard to comments and ratings that appear on the eBay feedback system. Credit repair scams might have a new sibling in "feedback repair" scams on eBay.

Other forms of competition have not come into being. In 2006, for example, a start-up called Rapleaf, recognizing the importance of online reputation, sought to build a business in that area, aggregating identity and biography from various Web platforms. The idea was to give people a portable rating they could use in any commerce environment.[76]

Along with competitors' attacks,[77] Rapleaf faced the possibility that it would be treated as a credit bureau under the Fair Credit Reporting Act. This would impose enormous costs relative to the budget of this small start-up and expose the personal information it holds to significant security risks due to the FCRA's access and correction rights. Wisely, Rapleaf's terms and conditions make clear that it is not a credit reporting service, and it forbids users from using it in lieu of obtaining a credit report.[78]

Thus, the FCRA's legal risks and compliance costs ensure that the business of gathering and disseminating data about financial reputation stays with credit bureaus. Reputation services such as Honestly.com and iKarma may be unaware that they could run afoul of the FCRA if information on those sites is used for credit, employment, insurance, or other purposes regulated by the FCRA.

The FCRA does more than just protect against new start-up competitors. The FCRA helps lock in existing business for credit bureaus. Its terms make it very difficult for data furnishers to work around the credit reporting system.

Under the law, users of consumer reports must notify consumers of adverse actions they take based on credit reporting, including information they have gathered from affiliates or third parties.[79] This means that lenders must provide some FCRA rights to consumers if they trade credit report information among themselves, or if they develop some kind of in-house credit report. The result is that gathering creditworthiness information is prohibitively costly even for large financial services providers. Doing so would amount to starting a credit bureau, with legal complexities, 800-number hotlines, and other cost drivers.

This was an outcome that credit bureaus sought in 1969. When the Senate Banking and Currency Committee's Financial Institutions Subcommittee was considering the FCRA, a staffer of Senator Proxmire's touted the credit bureaus' support for language preventing creditors from generating their own information:

> I might point out this . . . provision is strongly supported by the credit bureaus who fear that in its absence creditors might have incentives to bypass credit bureaus and exchange information amongst themselves in order to avoid the disclosure requirements under Section 615.[80]

The FCRA placed responsibilities on users of credit reports not only so there would be uniform coverage for rules about reputation, but at the behest of credit bureaus seeking to ensure that their clients would not develop ways around buying credit reports. Credit bureaus used regulation to lock in their business model.

Credit bureaus used regulation to lock in their business model.

Over time, Rapleaf has turned its concentration away from reputation and toward marketing. As competitors like TARGUSinfo do, it uses the data it collects online to flesh out the customer profiles held by clients. This parallels the move of credit bureaus into the warehousing of marketing data as well. Credit bureau Experian, for example, has business lines that "offer valuable insight on millions of consumers, their behaviors, brand preferences, media usage habits, and more."[81]

These services provide valuable intelligence for marketers, of course, and they help with the fraught process of delivering relevant and timely messages to potential customers—the ultimate goal is getting people things they want and need. But they exemplify the structure of the data environment, preserved in part by the Fair Credit Reporting Act, that is so unsatisfying to so many. Rather than fostering data aggregation into a confidential trust for the benefit of the consumer, the FCRA treats individuals as objects of large organizations' surveillance efforts.

Treating consumers as independent, autonomous, and equal participants would ameliorate many people's concerns with power and privacy in modern, information-fueled commerce. Alternatives are very hard to envision from the vantage of the present day, but it is a historical accident that technical, social, and legal habits around data and surveillance came about as they did.

Historically, computing originated as a government project, largely for war. Deployed next in the administration of large government programs for social measuring and management, such as the census and U.S. Social Security program, managing records about people was its only conceivable use.[82] The early "killer apps" of computing were war-making and surveillance.

The data structures and practices that emerged during the early period of computerized administration have not changed, even though the personal computer has distributed computing power across the society. Credit reporting and online marketing illustrate this. The large organization observes the individual (who has been assigned a small suite of uniform identifiers) rather than the other way around or some variegated arrangement.

Nothing inherent to computing or communications requires that our information society be organized this way. A nascent effort to restructure the personal data environment more amenably to individual power and privacy is the Personal Data Ecosystem, which is pursuing individual control of data and a thriving network of businesses built around "personal data stores."[83]

Nothing inherent to computing or communications requires that our information society be organized this way.

The market for identification services, which is an important component of credit reporting, also remains relatively stagnant. Government dominance of identity provision is probably the chief culprit, not the FCRA, but the credit reporting law is part of a large bulwark against experimentation and dynamism. The U.S. federal government produces the dominant universal identifier, the Social Security number, and state governments control the leading—often mandated—identification system for institutions, the driver's license. These government entities enjoy the advantage of providing identity services with no risk of liability to end users, neither to those identified or to the parties that rely on government-issued identification. Federal policies like the REAL ID Act seek to solidify, strengthen, and centralize government provision of identity services.[84]

Meanwhile, various security-oriented government programs keep the focus of the credit reporting industry on using and strengthening existing identity tools rather than creating new innovations in the identity and credentialing areas. For example, the Department of Homeland Security is currently considering using Equifax for large-scale confirmation of the identities of Americans being vetted through a national background check system called E-Verify.[85] The Transportation Security Administration, with its penchant for identity-based security, has sought to use commercial data for identity verification in the past,[86] though the project raised "real questions" for the Department of Homeland Security's privacy advisory committee.[87] Under returning proposals to have the government examine the backgrounds of American travelers,[88] it may do so again. All this is a far cry from the consumer-focused identity and reputation businesses that could exist, providing people the ability to confirm identity and establish reputation while maintaining privacy consistent with their interests.

The potential identification services marketplace is limited only by the imagination. Government-provided identity artifacts like the Social Security number and driver's license are very rudimentary, and our modernizing economy must eventually move away from them. Credit bureaus and financial services providers have a wealth of information that they can use for consumers' benefit in identity provision. Communications devices and accounts—things like phone numbers, e-mail addresses, and social networking handles—are exceedingly common identifiers that are assigned by telecommunications companies, Internet service providers, and others. These can be made into articulated identity services business lines. Ultimately, the identity marketplace should produce systems that are more useful, more secure, and more privacy protective than SSNs and drivers licenses.

There is no guarantee that diverse and competitive reputation and identification markets would have emerged in the absence of the FCRA and related laws and policies, but the centralized, government-focused status quo did emerge under these policies. That status quo is unsatisfactory in terms of consumer benefits as articulated by consumer advocates, and it is a precarious environment for privacy and civil liberties. It is a government-corporate information system in which it is very difficult for consumers to bargain for privacy protection or—for those who want more disclosure—privacy reduction.

The FCRA has had a role in suppressing the competition and innovation that might have benefited consumers quite a lot. In doing so, it has not solved the problems with credit reporting that Senator Proxmire sought to address when he introduced the legislation. Crucially, the FCRA has also prevented another problem-solving system from operating. It preempted the application of common law remedies to credit bureaus' wrongs. This prevented legal incentives for good credit reporting practices from emerging.

An Alternative Denied: The Common Law

There are many different social mechanisms that husband the behavior of the people and businesses in American society. Federal regulation is just one example. Morality, ethics, and tradition are informal but powerful guides for behavior that also have their influence. Market regulation is a relentless force that requires businesses to hone products and services to satisfy the many dimensions of consumer demand. When businesses fail to meet consumers' desires, market processes quietly but insistently impoverish them and usher them out of existence. There is state regulation, which includes not only sector-specific regulation but general business regulation. (Only one state—Oklahoma—regulated credit bureaus when Congress passed the FCRA.[89]) And there is state common law.

Congress eliminated the influence of the common law on credit bureaus when it passed the Fair Credit Reporting Act. Over the last 40 years, common law might have influenced credit reporting advantageously to consumers, perhaps doing so better than prescriptive regulation.

Congress eliminated the influence of the common law on credit bureaus when it passed the Fair Credit Reporting Act.

What Is Common Law?

Common law is the legal system that came to the American colonies from England. It is distinct from civil law, which dominates on the European continent. Where civil law is written out by experts or legislators, common law is what judges over centuries have "found" to be the law in the common practices of people and in the precedents of other courts. The common law is a slowly evolving set of expectations that courts ratify as much as write.[90] While civil law takes what expertise and erudition is available at a given time and captures it in written rules, common law draws on hundreds of generations of experience, and it adapts old rules to new problems. Fundamental legal regimes such as property, contract, and anti-violence law (assault and battery) are common law.

The law of negligence is a branch of common law that illustrates the balances that common law adjudication strikes over time. Under negligence law, everyone in society owes a duty to every other to keep them safe from harm. A person will be liable to another if (1) his or her activity creates a duty of care—essentially anything that can cause harm creates such a duty; (2) he or she breaches that duty; (3) the breach of duty proximately causes harm; and (4) there is indeed a harm.

The negligence rule causes people to look out for others no matter what they are doing—to "internalize" the costs of their activities, in economic language. A truck driver owes a duty of care, for example, to anyone he or she may hit with the truck. Failing to drive a truck safely enough will make the driver liable to anyone he or she hurts. This is true

Common law tailors legal rules to carrying out the purpose of government, which is to protect each member of society from rights violations committed by others.

no matter what action turns out to endanger others: talking or texting on the phone, speeding, driving on worn tires, failing to get enough sleep, and so on.

Importantly, the negligence rule does most of its work through incentives, not through lawsuits. Most truck drivers drive safely most of the time because of the rule that they would have to pay someone they might injure—not because they have been sued. That means the benefits of the law go to everyone, not just people who can afford to bring a lawsuit. The argument that one has to be able to sue to enjoy the benefits of the common law is invalid. The incentives set up by widespread interest in avoiding lawsuits protect all members of the public.

Common law rules that proscribe harm have an advantage over civil regulation. Barring harm generically, rather than prescribing how to avoid each individual action that may produce harm, allows all actors in society to determine how to act in ways consistent with safety. The freedom to experiment with new ways of acting that are nonharmful distributes the problem of harm-avoidance to many more people than can be involved in writing regulation—crowd-sourcing harm-avoidance techniques, if you will. It also allows for innovation and experimentation that can discover new and better ways of doing things that are consistent with safety.

With the freedom that remains under common law regulation, people and businesses can implement protections more efficiently than they can under prescriptive rules. Common law tailors legal rules more precisely to carrying out the purpose of government, which is to protect each member of society from rights violations committed by others.

Civil law rules meant to achieve the same result are prophylactic. They proscribe specific behaviors that might do harm, not those that in fact result in harm. They also require behaviors that might or might not protect others, such as providing notice about adverse credit decisions. Using civil rules, legislators and regulators often outlaw or require behavior based not on avoiding harm, but on their own moral or social designs for society. Policymakers sometimes indulge in social engineering schemes that are rather sweeping.

Neither system is perfect, of course, and more safety can almost certainly be had through prescriptive regulation. The problem is that such safety can come at a cost higher than its value to society. Forcing truck drivers to move their cargoes at 25 miles per hour, for example, might save some number from dramatic truck-related injuries. But at the same time it might impoverish people and quietly kill them in greater numbers than the number saved. Barring trucks entirely from roadways would brilliantly reduce deaths by truck accident, but that policy would kill many more people than it saved as poverty-related conditions took their toll.

Negligence law avoids these pitfalls. It constantly seeks optimal safety levels by tweaking the rules on duty, breach, causation, and damages. Common law is an intricate and complex, but brilliant, system for balancing societal values. It has not had application in credit reporting for 40 years.

The FCRA Preempted Common Law

The Fair Credit Reporting Act made a clear choice about the law that would apply to credit bureaus. It set aside the inductive reasoning of the common law for a deductive civil law regime. Rather than using courts to accrete knowledge about right and wrong in credit reporting, a political process sought to balance societal values in a credit reporting statute.

There are many very smart people involved in the political process and legislation-writing, but they are not necessarily smart enough to manage complex and value-laden problems like reputation and credit reporting. Self-awareness being in short supply, this did not stop them from assigning themselves the task of commanding an economic sector, as legislatures and regulators prefer to do.[91]

In May 1969 Senator Proxmire held a series of hearings on the Fair Credit Reporting Act. Among his witnesses was Alan Westin, the director of the Center in American Liberties at Columbia University and the author of the book *Privacy and Freedom*.[92] Westin testified about the unsatisfactory legal environment and how common law remedies were failing to meet the problem of credit reporting. Due both to the substantive rules and the costs of suing, Westin found common law insufficiently protective of consumers' fairness and privacy, and too protective of businesses' speech and communication rights:

> The doctrines of qualified privilege and the delays in time that are involved in bringing lawsuits are such that individuals who lose their jobs because of inaccurate, biased, or improper reports by personnel firms can have their careers seriously hampered before they are able to get remedies at law, and the remedies at common law are so saddled over with certain assumptions about the proof of damages and proof of malice or the proof of gross negligence that they don't represent the kind of process that I think we need in the new society of records and dossiers that we are building.[93]

A Library of Congress report largely corroborated Westin's account and assessed the legal landscape around credit reporting at the time.[94] The chief cause of action available to aggrieved consumers was the common law tort of defamation, "an invasion of the interest in reputation and good name, by communication to others which tends to diminish the esteem in which the plaintiff is held, or to excite adverse feelings or opinions again [sic] him."[95] Courts generally denied defamation claims based on a "qualified privilege" for statements made without malice or gross carelessness. At least one court had even denied discovery of the content of credit reports without a showing of malice in advance.

But others denied the qualified privilege entirely. One court in Idaho had written:

> The company that goes into the business of selling news or reports about others should assume the responsibility for its acts, and must be sure that it is peddling the truth. There cannot be two standards of right nor two brands of truth, one for moralizing, and one for business. The law ought to look with a stern, cold eye upon the liar, whether he be incorporated or just an everyday man. If a mercantile agency can safely make false reports about the financial standing and credit of the citizens and destroy his [sic] business, it can then take the next step with equal impunity and destroy his reputation, leaving him shorn and helpless.[96]

The Restatement of Torts, an influential compendium of common law principles, argued at the time that the privilege should give way when the injury to the subject of the report was great and when the gain to the recipient of the information was small.[97] The reasonable thing to do with idle gossip is to go ahead and gossip. The reasonable thing to do when information may affect a person's credit or job prospects is to speak carefully.

Another avenue for aggrieved consumers at the time was to focus not as much on the truth or falsity of credit reports, but on the scope of their publication. University of California, Berkeley, Law School dean William Prosser had argued in a prominent 1960 law review article entitled simply, "Privacy,"[98] that four prongs of common privacy law had emerged: protecting against intrusion onto seclusion, disclosure of embarrassing private facts, publicity placing someone in a false light, or appropriation of one's name or likeness. These had potential application to credit reporting—particularly the "false light" and "disclosure of embarrassing facts" branches—when it came to potentially prejudicial information.

The courts were working on the problem of credit reporting in the 1960s, moving slowly, no question, to assimilate the important and deeply conflicting values involved in that business and its practices. In February 1969 a court in Florida had awarded a druggist $70,000 for a claim that he was libeled in a credit report portraying him as "a deadbeat and a fraud."

The courts were working on the problem of credit reporting in the 1960s.

We cannot know how maintaining the common law in place might have affected credit reporting over the last 40 years.

Consumer attorney Benny L. Kass, speaking at Senator Proxmire's hearings, called this development "a foot in the door."[99]

But consensus in Washington, D.C., formed quickly that clumsy old common law was not up to the task of protecting consumers, and that it should be supplanted with smart, newly written regulation. Indeed, regulation should replace common law. Laying out his vision of a new system for regulating credit reporting, Westin said:

> If such a system is to work, I think it may be necessary for its acceptance that a person who is given access to his file agree in writing not to bring a damage suit against the reporting company if errors are found. This may seem to be immunizing the investigators against responsibility for their mistakes, but I think the primary objective of our society in the deepening age of dossier judgments about individuals is to insure access to files and correction of errors, rather than to continue the traditional "responsibility-through-damage-suit" method.[100]

State tort law was not preempted in the Fair Credit Reporting Act when Senator Proxmire introduced it, but the bill that passed the Congress barred claims against credit bureaus based on state common law.[101] Credit reporting might be very different today if there had been 40 years of common law development in this area. Unfortunately, we cannot know how different.

An Uncontrolled Experiment

Controlled experiments are those where one group of subjects is tested with a new process, and another group, the "control" group, is not subjected to the new process, though it is otherwise maintained in the same conditions as the experimental group. State common law and regulation allow for controlled experiments in public policy. When one jurisdiction, or a small number of them, adopt a rule, the rule's influence and workability can be gauged by comparing it to jurisdictions in which the rule has not been adopted. This idea—of controlled experiments in public policy—prompted Justice Louis Brandeis in 1932 to articulate how states act in our constitutional system as "laboratories of democracy."[102]

Federal legislation and regulation deprive the nation of this learning tool. When there is a federal commercial rule, every business in every state and in every court jurisdiction must obey that one rule. Criticisms of such rules as "one size fits all" or "top-down" may be merited, but they ring hollow while there is no evidence of what gains might come from alternatives. Of course, there is some possibility of comparing circumstances in the United States with other countries, but there are many more variables in such natural experiments than there are in variations among U.S. states.

Accordingly, we cannot know how maintaining the common law in place might have affected credit reporting over the last 40 years. Almost certainly, lawsuits would have continued to attack perceived unfairness in credit reporting. The privilege courts were according to credit bureaus may have given way or weakened in light of the consequences to consumers of flawed information. The "false light" privacy claim may have matured into a protection against erroneous credit reporting. Courts may have approved other causes of action against credit bureaus, such as interference with prospective economic advantage. Almost certainly, any rule limiting discovery of credit reports to where actual malice was already shown would have given way.

It is not entirely certain that credit bureaus would have borne liability, of course. Courts may have found it better placed with users of credit reports. They know better what use they will make of the information credit bureaus supply them, so courts may have found lenders, employers, and other users of credit reports responsible for assessing the veracity of information and reinvestigating decisive facts.

There are worthwhile criticisms of litigation, of course. Class action proceedings produce some efficiencies when issues that are shared by many litigants can be resolved using a minimum of judicial resources. But the class action mechanism also allows cases to be litigated that otherwise would not. The plaintiff's class action bar is rightly accused of chasing "jackpots" in lawsuits about generic slights that might not truly matter. "Wrongs" too trivial for any one litigant to bring before a court routinely become lawsuits with tens or hundreds of millions of dollars at stake, owing to the class action mechanism.

The common law is also slow. Common law rules have been produced over generations, and courts are slow to adapt them to new conditions, as the witnesses before Senator Proxmire effectively illustrated.

Some argue against common law litigation in favor of prescriptive regulation because the costs and delays of litigation are so great and because the diversity of laws in 50 states is a costly impediment to doing businesses in national markets. They believe that having national rules in place is the important prerequisite for progress and efficiency. Regulated entities enjoy certainty under regulation, and they can apportion regulatory costs and burdens among themselves in an efficient way. They can save even more money when the regulation is uniform across the land. These arguments are valid in some ways but not in others, which the Fair Credit Reporting Act helps illustrate.

A credit bureau operating in the 1970s and 1980s did appear to enjoy relative certainty with respect to its legal obligations. The statute was unchanged for most of that period, though regulators tweaked the meaning of the law throughout. But starting in the 1980s, the FCRA has been amended two dozen times—at least two of those being substantial revisions. The Federal Trade Commission has varied its approach to credit reporting under its various chairmanships, generally reflecting the ideological tenor of the presidents appointing its commissioners. These dynamics undercut the certainty that supposedly exists under regulation.

Have credit bureaus been able to find efficiencies in their FCRA compliance? It is certain. But the efficiencies they have found are not available to smaller competitors, which face higher compliance costs per unit of revenue. If the law has excluded new participants in the reputation and identity marketplace, the credit bureaus' gains are the public's losses. And if the national regulatory regime is imperfect, which it almost certainly is, the national rule denying interstate competition and experimentation frustrates a corrective mechanism that could improve the regulatory regime for consumers' benefit as well.

If litigation costs a substantial sum for a period of years while courts work through new problems, such cost is a worthwhile concern. But regulation may cost society 50 times that amount if it forecloses the benefits of innovation and competition. We may have foregone a credit reporting system good enough to redistribute lending decisions back to retailers, for example, dispersing billions of dollars per year from large lenders back to consumers and small businesses. An innovative identity system providing security without surveillance could squeeze payment fraud down to a minimum, returning billions of dollars per year to families and businesspeople. What stability there is in regulation may be penny-wise for incumbent firms and pound-foolish for society as a whole.

If regulation is faster and more efficient, the Fair Credit Reporting Act requires one to ask: "Faster and more efficient at what?" Judging by the discontent that remains around credit reporting, the FCRA arrived at a continuously varying set of nonsolutions to the problems Senator Proxmire meant for it to solve. This suggests another lesson from 40 years of experience with this information regulation.

A Caution against Information Regulation

Senator Proxmire and all who worked on passing the Fair Credit Reporting Act were earnest and assuredly sincere in their intention to help consumers, but their ability to successfully regulate an information marketplace appears to have been lacking. Four decades later,

The FCRA arrived at a continuously varying set of nonsolutions to the problems Senator Proxmire meant for it to solve.

the problems they tried to solve remain largely intact. This provides some lessons for today's debates about the Internet, information practices, and privacy.

Information policy is a challenging field with lots of complications. The values at stake are many and varied. They include control of personal information, fairness, seclusion, security, and liberty. The importance of these values varies from one instance to another. Indeed, from one person to another they are differently prioritized. Some of these values are in tension with one another, in ways of which many people appear surprisingly unaware. And the values that matter to people change over time as society evolves in relation to changing technology.

The technological landscape is a further complication for information regulation. Techniques for gathering data, for transferring it, processing it, and storing it are all under constant revision in the present era. The information policy challenges that Senator Proxmire and his colleagues faced at the end of the 1960s are quaint compared to today's, and technology has changed more quickly than the capacity of most people to understand it. Importantly, legislators and regulators are part of the class who do not know how the interplay of privacy, technology, business, and society should evolve. They do not know how to fix these problems.

Authors of overarching privacy regulation—now a congressional staple for over a decade—claim it would deliver consumers from the various concerns they have with the information economy and the online environment. A release issued by Sen. John Kerry (D-MA) on introduction of a recent privacy bill illustrates:

> Americans have a right to decide how their information is collected, used, and distributed and businesses deserve the certainty that comes with clear guidelines. Our bill makes fair information practices the rules of the road, gives Americans the assurance that their personal information is secure, and allows our information driven economy to continue to thrive in today's global market.[103]

Expressions like these are heavy on good intentions and light on fixed meaning. Appeals to the "fair information practices" (often called "FIPs")[104] are a ceremonial deism of sorts, boilerplate that advocates use when they don't know how to give consumers meaningful notice of information policies, when they don't know when or how consumers should exercise choice about information sharing and use, when they don't know what circumstances justify giving consumers access to data about them, and when they don't know how to describe which circumstances—much less which systems or what levels of spending—make personal data sufficiently "secure."

Senator Kerry's bill,[105] coauthored with Sen. John McCain (R-AZ) and accompanied by a House bill,[106] would assign the Federal Trade Commission the task of writing rules governing businesses that collect, use, or share personal data.[107] It would require such businesses to provide clear disclosures about their information practices and to offer consumers the ability to opt out.

Ideas like these have been tested. Opacity and consumer ignorance of credit reporting is still regarded as a problem in that field 40 years after it came under federal regulation.

The Kerry–McCain legislation requires companies to incorporate "privacy by design" into their policies and procedures. "Privacy by design"—a perfectly good mantra and ideal—would become a vehicle federal regulators use to inject themselves into countless technology and business decisions were it to become a federal government mandate. Innovation and competition among information businesses could be as deadened as it is in credit reporting.

The Kerry–McCain legislation does not call for a "do-not-track" mechanism, but Sen. John D. Rockefeller IV (D-WV) has introduced a bill to make the latest vogue in the Internet privacy discussion a permanent fixture of federal law.[108] His legislation[109] and a House companion[110] would task the Federal Trade Commission with writing rules to prohibit provid-

Legislators and regulators are part of the class who do not know how the interplay of privacy, technology, business, and society should evolve.

ers of online services from collecting personal information from a consumer once he or she has opted out using a "do-not-track" signal, likely to be sent by Internet browsing software.

Appealing as it sounds to go "untracked," nobody yet knows exactly what that means. Websites and other Internet services must keep usage logs for a variety of reasons, and often the quality of the content they provide turns on having information about visitors. Suppression of some tracking would reduce the value of advertising, potentially shrinking the amount and quality of content available online for free. Legally mandated "do-not-track" is an idea whose time has not come, and whose time may never come,[111] but federal regulators are eager to embark on this information policy experiment.

Experience with the Fair Credit Reporting Act counsels caution with respect to regulating information businesses. The federal legislators, regulators, and consumer advocates who echo Senator Proxmire's earnest desire to help do not necessarily know how to solve these problems any better than he did.

Privacy protection is undoubtedly a more complex problem than credit reporting fairness. It is an "Internet-y" problem that demands "Internet-y" solutions—that is, privacy problems should be distributed to the people best positioned to solve them, which are often consumers themselves. It is very unlikely that today's privacy issues can be fixed with federal legislation and regulation. That is a lesson of Senator Proxmire's attempt to manage a relatively modest swath of the information economy beginning more than 40 years ago.

Conclusion: Information Regulation and the Online World

Credit reporting enters its fifth decade under federal regulation with a new regulatory paradigm coming into place. In July 2010 Congress passed a new law called the Dodd–Frank Wall Street Reform and Consumer Protection Act,[112] which again amended the Fair Credit Reporting Act and transferred the bulk of its implementation to a new Bureau of Consumer Financial Protection.

The bureau will be housed within the Federal Reserve System, its director appointed by the president and subject to Senate confirmation. But its funding will not come from Congress. It will come from the Federal Reserve System, rising to 12 percent of the Fed's operating expenses in fiscal year 2013 and thereafter. These funds will not be subject to annual appropriation by elected representatives in Congress, releasing this agency from an important tie to public accountability.[113]

Along with enforcing the terms of the (again modified) Fair Credit Reporting Act, the bureau will have authority to interdict any and all unfair, deceptive, and abusive practices in the financial services arena, including credit reporting.[114] Unlike "unfair" and "deceptive," which at least have a history in Federal Trade Commission practice, "abusive" is a new term of art and a new avenue for regulatory experimentation. The meaning Congress has suggested for this term—it is unlikely to revisit its work, and courts will give the bureau authority to decide—is utterly open-ended and strange.

"Abusive" is anything that "interferes with the ability of a consumer to understand" a financial service or anything that "takes unreasonable advantage" of consumers' lack of understanding, inability to protect themselves, or reliance on a financial services provider.[115] This is a radical departure from what our society has traditionally seen as "wrong," harmful, or a source of market failure to justify regulation. But it is the law that Congress passed.

Recall that in 1969 Senator Proxmire noted consumers' general unawareness of credit reporting and inaccuracies in the credit reporting system. In 2009 the National Consumer Law Center reported that barriers to data correction for consumers include "lack of time or resources, educational barriers, and not knowing their rights."[116] The bureau could easily conclude that credit reporting itself is "abusive" because of consumer unawareness

Experience with the Fair Credit Reporting Act counsels caution with respect to regulating information businesses.

and indifference. It will not do this because of the political consequences, but over time it will use its authority to take control of more and more elements of credit reporting and the credit reporting industry.

Though the regulatory regime will be that much more intense and intrusive, the next decade of credit reporting regulation is unlikely to produce a reputation system that is any more accurate and relevant. It will certainly not be a confidential system. The Bureau of Consumer Financial Protection itself may be the next government entity enjoying entrée to Americans' financial information through the credit reporting system.

Lawmakers and federal government agencies have limited capacity to resolve the complex information issues, technology issues, and human values at stake in credit reporting. This is a lesson of 40 years under the Fair Credit Reporting Act. The law sought to improve credit reporting along a number of dimensions but has generally failed to do so. Unknown costs have accrued to the public in the form of lost improvements in the consumer credit world and in reputation and identification systems that have failed to emerge from the rigid government-corporate information environment.

By preempting common law remedies, the Fair Credit Reporting Act shut off a mechanism for resolving the tensions in credit reporting. The litigation system is slow and imperfect, but we are worse off for not knowing how the credit reporting industry might have evolved in an atmosphere more conducive to experimentation and discovery.

The Fair Credit Reporting Act should be repealed so that market forces and common law can again play their roles in guiding this industry and protecting consumers. Unfortunately, this is unlikely to happen. Industry and consumer groups form a solid phalanx of support for federal law and regulation; it is a battleground they both perceive as advantageous to their interests.[117] It will take many years' of work to drive new thinking to where it is needed and to dislodge the interests that rely on the status quo.

The place to apply these lessons in the near term is in other information policy debates. The Internet can still be saved from information regulations that lack coherence or a clear purpose in preventing concrete harm to individuals. Proposals for "baseline privacy legislation" or a government-backed "do-not-track" system address problems that are far vaguer than what Senator Proxmire addressed in credit reporting. It is hard to have confidence that such proposals can solve these unarticulated problems.

In 40 years, the challenges of credit reporting have not been addressed well by legislation and regulation. When it comes to contemporary issues like online privacy, lovers of the Internet and of freedom should recognize that combining the two—the Internet and freedom—is the best way to reconcile competing values. Top-down, centralized control of the information economy and society is not the better way forward.

Top-down, centralized control of the information economy and society is not the better way forward.

Notes

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Accuracy and Access to Credit," *Federal Reserve Bulletin* (Summer 2004), p. 297, http://www.federalreserve.gov/pubs/bulletin/2004/summer04_credit.pdf. ("Analysts widely agree that the data enable domestic consumer credit markets to function more efficiently and at lower cost than would otherwise be possible.")

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8. Reputation systems are used not only with people. Google's PageRank algorithm is a proprietary reputation system for Web pages. Digg and Reddit are reputation systems for news stories and other Web content.

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12. U.S. Const., amend VI.

13. See *Congressional Record* 115 (January 31, 1969): 2411–13.

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15. Ibid., 2413.

16. Ibid., 2413.

17. See ibid., 2413–14.

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