ISSUE BRIEF

CREDIT SCORING

Under the terms of the Equal Credit Opportunity Act,[1] financial institutions may use credit scores—numerical values arrived at by looking at such details as a borrower's credit history and income level—to help determine a borrower's creditworthiness. This score is formed using information contained in a consumer's credit report, which is one of the principal tools used by lenders to determine the risk involved in a making a loan.

The Fair and Accurate Credit Transactions Act of 2003 (FACT Act or FACTA)[2] updated the Fair Credit Reporting Act[3] and installed numerous new provisions into federal law. The FACT Act provides for consumers to receive free annual credit reports, increases the standard for the accuracy of information furnished to credit reporting agencies, strengthens adverse action notices, and creates a right to a credit score from a credit reporting agency for a reasonable fee.

The FACT Act also requires a lender or broker who is considering a home loan application to provide a credit score without a fee, and adds certain rights for identity theft victims and measures intended to prevent identity theft, including a duty on creditors to take certain steps before granting credit when a fraud alert is contained in a credit file or accompanies a credit score. States retain significant authority to continue to protect their residents, including from identity theft, particularly in areas untouched by the federal act. States also retain the right to supplement most federal identity theft provisions.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010[4] included the Fair Access to Credit Scores Act (FACS Act), which mandates situations in which a lender must disclose a potential borrower's credit score; for example, in cases in which the applicant is denied credit based on their credit score.

AFSA'S POSITION

AFSA believes that a robust credit scoring and reporting system serves both borrowers and creditors. The use of credit scores gives lenders a much better understanding of risk, giving them the confidence to offer credit to more people. With more credit available, the cost of credit for borrowers generally decreases.

Automated credit processes, including credit scoring, also make the credit system more efficient and thus less costly for lenders, who pass savings on to their customers. In addition, lenders can more effectively control their losses using credit scoring, again, allowing them to offer lower overall rates.

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[1] Equal Credit Opportunity Act, 15 U.S.C. § 1691.
[2] Fair and Accurate Credit Transactions Act of 2003, Pub. L. No. 108-159, 111 Stat. 1952.
[3] Fair Credit Reporting Act, 15 U.S.C. § 1681 et seq.
[4] Dodd-Frank Wall Street Reform and Consumer Protection Act § 1100F, 15 U.S.C. § 1681m.