

Unscoreable: How the Credit Reporting Agencies Exclude Latinos, Younger Consumers, Low-Income Consumers, and Immigrants

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Who's Keeping Score? Holding Credit Bureaus Accountable and Repairing a Broken System

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INTRODUCTION

UnidosUS, formerly the National Council of La Raza, is the largest national Hispanic* civil rights and advocacy organization in the United States. For 50 years, we have worked to advance opportunities for low-and moderate-income Latino families so that they can achieve economic stability and build wealth. In this capacity, UnidosUS with its network of nearly 300 Affiliates— local, community-based organizations in 35 states, the District of Columbia, and Puerto Rico— provides education, health care, housing counseling, workforce development, and financial coaching programs to millions of citizens and immigrants in the United States annually.

UnidosUS’s work with our network of community-based financial and housing counseling providers helps inform our understanding of Latinos’ financial challenges and opportunities. The UnidosUS Wealth and Housing Alliance (UWHA) (formerly the National Homeownership Network, or NHN) is the nation’s largest network of community-based organizations working to empower Latino wealth-building through homeownership. The UWHA develops effective programs that blend research, advocacy, and direct housing and financial counseling. The UWHA is a HUD-approved housing counseling intermediary and trains hundreds of housing counselors emphasizing individual, culturally competent counseling. Established in 1997, the UWHA includes 50 independent community-based organizations that support more than 60,000 families a year.

We are further informed of the credit needs of Latinos through our own small-dollar loan program. In 2016, UnidosUS developed a loan program to increase access to small-dollar lines of credit for Latino immigrants who needed assistance in paying for the costs associated with naturalization. Our program, Fuente Crédito (“credit source” in Spanish), helps community-based service providers connect underserved Latinos and immigrants to credit unions, community banks, and Community Development Financial Institutions (CDFIs), which offer safe and affordable loan products to build credit and finance small-dollar expenses. Several lenders that participate in Fuente Credito obtain credit scores from the big three traditional credit reporting agencies— Equifax, Experian, and TransUnion—in addition to alternative data bureaus, such as Clarity and LexisNexis, to help supplement credit history for Latino applicants who have a thin credit history or none at all.

For more than two decades, UnidoUS has published reports, testimony, and engaged in advocacy on issues that focus on supporting strong fair housing and fair lending laws, increased access to financial services for low-and moderate-income individuals, and has promoted homeownership in the Latino community. Additionally, UnidosUS has conducted its own original community-based research on the experiences of low-and moderate-income (LMI) communities of color in using financial services and products including: [Latino Financial Access and Inclusion in California](#) (2013), [Banking in Color: New Findings on Financial Access for Low- and Moderate-Income Communities](#)

* The terms “Hispanic” and “Latino” are used interchangeably by the U.S. Census Bureau and throughout this document to refer to persons of Mexican, Puerto Rican, Cuban, Central and South American, Dominican, Spanish, and other Hispanic descent; they may be of any race.

(2014), [Small Dollars for Big Change](#) (2017), and a forthcoming follow-up to *Banking in Color* with PolicyLink.

This written statement focuses on how the credit scoring system is biased against low-income consumers, consumers of color, younger consumers, and immigrants through information and stories from our Affiliates. It also focuses on how this bias excludes or extremely limits these same consumers from accessing credit, in addition to affecting their ability to obtain employment, rent an apartment, turn on their utilities, or access health insurance. In short, it discusses how the current credit scoring system affects almost every economic aspect of the lives of everyday Americans, especially Latinos.

BACKGROUND

“Credit bureaus are the original gangsters because they have their own system.”
—55-year-old woman from Philadelphia, Pennsylvania

For most of modern history, there was no such thing as a credit score. Lending decisions were made by loan officers at banks who relied on experience and subjective assessments of credit risk, including the applicant’s race or ethnic background.¹ For example, the Federal Housing Administration’s first Chief Economist and the co-author of its first underwriting manual—Homer Hoyt—established a ranking system in 1933 that listed groups based on their perceived benefits or detrimental effects on property valuation and borrower risk. “English,” “Germans,” “Scotch,” “Irish,” and “Scandinavians” were the most beneficial groups, while “Negroes” and “Mexicans” were the most detrimental groups and were the riskiest to lenders and communities.² There were two major problems with this model of lending. First, it relied up on an individual loan officer’s subjective judgment, and second, it was discriminatory.

Credit scores were first introduced in the United States during World War II, when banks lost their loan officers to the war effort. Standardized credit scorecards were then developed to provide bank employees with clear instructions on how to decide credit applications.³ Credit scores were then developed into a statistical instrument by Bill Fair and Earl Issac, who founded Fair, Issac, and Company (FICO) in 1956. Credit scoring was not adopted on a large scale by the financial services industry until after the passage of the Equal Credit Opportunity Act of 1974 (ECOA).⁴ In implementing ECOA, the Federal Reserve stipulated that lenders who used empirically derived, demonstrably and statistically sound credit scores to make loan decisions would be immune to discrimination suits.⁵ The three national credit reporting agencies (Equifax, Experian, and TransUnion) followed suit in 1989 and developed their own proprietary generic credit history scores.⁶

The credit reporting agencies collect information about consumers from many sources and organize this information into reports that are sold to businesses to make decisions about consumers. These are proprietary products designed to make profits for their creators. Thus, the way that these scores are calculated are not public. Each credit scoring company uses their own

formula—so an individual’s score can vary from lender to lender. Additionally, the information that is fed into these calculations is obtained from a variety of sources. Again, the sources used vary between companies. According to FICO, 35% of an individual’s score is based on on-time payments, and the rest of the score is based on factors such as having a low balance on credit cards compared to the credit limit, how many years a consumer has had credit, and a “good mix” of credit including a mortgage.⁷

Even though these generic credit scoring systems are a vast improvement from the subjective assessments behind lending decisions made prior to 1974, they still reflect longstanding disparities in U.S. credit infrastructure. The incorporation of these disparities into credit scoring models results in communities of color, low-income individuals, young adults, and immigrants having disproportionately low credit scores, high rates of credit invisibility, or thin credit files.

This is especially true for Latinos. Today, Latinos number 58.9 million and compose 18% of the U.S. population. Yet, Latinos have had longstanding challenges connecting to mainstream financial institutions and obtaining credit, similar to other communities of color. As the youngest and fastest-growing segment of the nation’s population, Latinos’ economic opportunities will have a significant role in shaping the nation’s economic future. Increased credit scores and credit visibility are important components of ensuring that Latinos can unlock these opportunities.

“I feel discriminated against because I don't have credit. Whenever I am trying to do anything it gets so frustrating and I feel that it affects many aspects of my life. One example is how the gas company and the power company need to check my credit history in order for me to receive their service. Since I don't have credit history, my only option was to give a down payment of \$500. That's a lot of money. As a new renter I had to give the first and last month rent and give a down payment to have gas. It is too much for one person.”

—Henry from California

CREDIT SCORES

“[A] high credit score opens the door; a low credit score, they take away the keys.”

—A 55-year-old woman from Philadelphia, Pennsylvania

Credit scores are supposed to be an objective measure of an individual’s creditworthiness—free from the racial and gender bias that has historically determined who can, and cannot, access credit and on what terms.* Yet, credit scores are still largely correlated with income and wealth,⁸ exacerbating longstanding wealth disparities between different racial and ethnic groups, and perpetuating the racial wealth gap.⁹

* Under the Equal Credit Opportunity Act (ECOA), it is unlawful for a lender to discriminate against a credit applicant on a prohibited basis, including race; color; religion; sex; and national origin, in any aspect of a credit transaction.

A study by Experian in 2018 found that there was a correlation between an individual's income and their credit score. They found that higher-income consumers, on average, have higher credit scores. For example, the average FICO 8 score for individuals with an income of \$15,000 or less was 652, while individuals with incomes in excess of \$200,000 had an average score of 739.¹⁰ Data from the Financial Clinic's Change Machine, a nonprofit organization that works with poor Americans to build financial security, shows that in 2017, individuals with an excellent credit score over 750 had an average asset balance of \$15,559, while those with poor scores of lower than 650 had an average asset balance of \$1,343.*

Numerous studies have shown that communities of color have lower credit scores than their White counterparts. A 2007 report by the Federal Reserve Board mandated by the Fair and Accurate Credit Transactions Act of 2003 (FACTA) found that the average credit score of Black Americans was approximately half of that of Whites, and the average credit score of Latinos was more than one-third less than Whites.¹¹ A 2010 study by the Woodstock Institute found that in predominantly Black ZIP codes in Illinois, more than 54.2% of the individuals had a credit score of less than 620, which are considered subprime. In ZIP codes that were primarily Latino, 31.4% of individuals had a credit score of less than 620, and only 47.3% had a credit score greater than 700, or prime. In predominantly White ZIP codes, 67.3% of residents had a credit score of 700 or greater and only 16.8% of individuals had a credit score of less than 620.¹² A 2012 study by the Consumer Financial Protection Bureau (CFPB) found that the median FICO score for consumers in majority-minority ZIP codes was in the 34th percentile, while ZIP codes with low minority populations was in the 52nd percentile.¹³ The Urban Institute found that in 2013, only 41% of Latinos and 33% of Black consumers have a FICO score of 750 or higher, while more than 64% of Whites had a score of 750 or higher.¹⁴

"I have a job, and a bank account with direct deposit. My bank won't extend me credit. The financial system is not here for us.....I don't think they're here for any of us. I feel like they're here for the big people."
—A 31-year-old from San Diego, California

CREDIT INVISIBILITY

"My experience with not having credit has been bad and sad. When I went to the car dealership to try to purchase a new vehicle, I was denied a car loan because I don't have credit. I was not able to purchase the vehicle because my other option was to provide a big down payment and at the time I didn't have that kind of money. Since I don't have a Social Security Number, I have tried to build my credit by using my [Individual Taxpayer Identification Number] but not all lenders accept it or can't see the history of my activities. When I ask lenders why is it that not all lenders can see my activities, they don't know how to answer my question. I feel

* These numbers are from the Financial Clinic's social enterprise software Change Machine. They represent figures for coaching customers in the system that reported credit scores and assets at their first meeting.

that my work and work history should be the factor that determines if I get a loan; if I have income coming in at the end of the day I will be able to make the loan payments.”

—Miguel from California

According to the Consumer Financial Protection Bureau (CFPB), 26 million American consumers or one-in-ten (11%) adults are credit “invisible.”¹⁵ Credit invisibility means that they do not have credit information that has been reported to the major credit repositories.¹⁶ An additional 8.3% or 19 million American consumers have “unscorable” credit files, meaning that they have a “thin” or insufficient credit files (approximately 9.9 million individuals) or they have “stale” credit files and lack any recent credit history (9.6 million individuals).¹⁷ In total, approximately 45 million American consumers, or 19.3%, are credit invisible, have thin credit files, or lack a recent credit history.

Credit invisibility occurs most frequently in communities of color, in low-income neighborhoods, in younger populations, and among foreign-born communities. Black and Latino consumers are almost twice as likely to be credit invisible or have unscorable credit records than Whites or Asians in the United States. For example, 30% of Black and Hispanic consumers are credit invisible or are unscorable, compared to 17% of Whites.¹⁸

Consumers in low-income neighborhoods are disproportionately credit invisible and are also more likely to have unscorable credit files.¹⁹ The CFPB found that almost 30% of consumers in low-income neighborhoods are credit invisible and an additional 15% have unscorable records, while only 4% of adults in higher-income neighborhoods are credit invisible and 5% have unscorable credit records.²⁰

Younger consumers are more likely to be credit invisible, compared to older consumers. With few exceptions, children under the age of 18 generally do not have credit reports, and 64–67% of all consumers between 18 and 19 years of age are credit invisible. The CFPB found that while only 6% of White consumers between the ages of 25 and 29 are credit invisible, Latinos are more than twice as likely to be credit invisible at 15.5%, and Black Americans are almost twice as likely to be credit invisible at 11.1% in that same age range.²¹

Foreign-born individuals and recent immigrants, who make up nearly 44.5 million individuals or 13.7% of the total U.S. population, including 13.2 million non-U.S. citizens with lawful permanent resident status, are often credit invisible. Recent immigrants, including refugees, asylum applicants, and newly arrived visa-holders are most likely credit invisible or have thin credit files. Additionally, immigrants who hold an Individual Taxpayer Identification Number (ITIN), face additional challenges in obtaining credit and are more often credit invisible or have thin credit files.

Among the factors that contribute to the prevalence of credit invisibility for these populations is that mainstream credit scoring models rely on formulas and algorithms that fail to consider cultural norms, such as a reluctance to accumulate debt, reliance on cash, credit history from other countries, or failure to account for other methods of making on-time payments—which keep these individuals out of the financial mainstream. Thus, communities of color, low-income consumers, young consumers, and immigrants are left out or left behind by the credit scoring models.

“I have tried to build my credit with my ITIN but banks don't accept it. Since me and my family want to purchase a home one day, we have gone to several banks to get guidance, but our dreams have been shut down. The banks told us that since we don't have a Social Security Number, we will not be able to get a home loan.”

—Amparo from California

CONSEQUENCES OF CREDIT INVISIBILITY

Credit scores were originally intended to be used by lenders to assess whether to approve a consumer for credit. Today, however, credit scores or credit histories are used for many non-lending purposes. These purposes include applications for employment, housing, utility services, and even health insurance. This “mission creep” means that a group of for-profit companies, making decisions based on proprietary formulas, now have tremendous power over every person in the United States. These companies determine whether a person can obtain a job, put a roof over their head, stay warm in the winter or cool in the summer, or secure health care for individuals and their families.

Use of Credit Scores in Employment

10 states;^{*} the District of Columbia; and the cities of Chicago, New York City, and Philadelphia have passed laws restricting the use of credit reports for employment purposes. Yet, the Society for Human Resources Management (SHRM) found that 47% of employers conduct credit checks on job applicants.²² This practice is not limited to management positions or positions that require a security clearance. The think tank Demos found that employers required credit checks for jobs as diverse as maintenance work, telephone support, office assistants, delivery drivers, selling insurance, working as a home care aide, supervising a stockroom, and even serving frozen yogurt. They also found that some employers also conduct credit checks on existing employees when they are considering them for a promotion. In a survey they conducted in 2014, Demos found that one-in-ten survey respondents who were unemployed were informed that they would not be hired for a job due to information contained in their credit report, and one-in-seven job applicants with blemished credit histories were advised that they were not being hired because of their credit.²³

^{*} California, Colorado, Connecticut, Hawaii, Illinois, Maryland, Nevada, Oregon, Vermont and Washington.

Use of Credit Scores in Housing and Utilities

Landlords have at their disposal rental screening services offered by several hundred companies, which provide landlords with four types of rental information: residential history, criminal background checks, civil litigation (including eviction cases), and credit reports. Even landlords who do not use these services are likely to check the credit records of prospective renters and use these credit records as a measure of the likelihood of renting to a “problem tenant.” TransUnion offers their own tenant scoring based on an individual’s credit records; Equifax sells additional information with credit reports to landlords as a package; while Experian has its own rental screening operation and claims to not only predict rental behavior, but also provides rental payment data as part of its report.²⁴ Credit reports and credit scores are also used as screeners for federally subsidized housing. The U.S. Department of Housing and Urban Development’s (HUD) guidebook to owners and managers of housing units states that “the applicant should have a neutral or good record for a recommendation of admission” but also plainly states that “lack of a credit history will not have a bearing on eligibility.”²⁵ The use of credit records can result in a denial of housing, higher deposit requirements, and higher rents charged for substandard properties. Additionally, paying more for housing can exacerbate the financial difficulties that many communities of color, low-income individuals, younger individuals, or immigrants face daily.

Many Americans have utility bills, including those for their power, water, phone, internet, and natural gas. Although utilities are not traditionally included on a credit report, they are still considered a credit account because they provide service in advance of payment. Individuals without a credit score or with a poor credit score when they attempt to establish an account with a utility company may be denied service, required to provide a co-applicant, or asked to provide a deposit to establish service.

Use of Credit Scores in Health Insurance

To purchase health insurance plans from the federally facilitated marketplace (FFM), individuals must undergo an identity verification process run by Experian to perform its electronic identity proofing function. Using Experian’s database and the individual’s credit history, Experian generates a series of questions that the consumer must answer correctly to verify his or her identity, including questions about an existing or previous credit line, mortgage, or personal loan. If a consumer does not answer the question correctly, or if Experian does not have enough credit history to generate questions, the consumer is not allowed to proceed with the online application process and they must then validate their identity with a property deed or title, or a driver’s license by mail, delaying enrollment.²⁶ This process disproportionately impacts communities of color, low-income consumers, younger consumers, and immigrants, who are more likely to be credit invisible or have a thin or unverifiable credit file.

CONCLUSION

We hope this testimony provides the committee with information on the ways in which the current credit rating system has left entire populations—including communities of color, low-income individuals, younger individuals, and immigrants—underserved and adversely impacted by its structure. For Latinos, who represent 18% of the population, it is important that our credit rating system serve them in a fair and inclusive manner. If we continue to rely on credit bureaus as gatekeepers who determine access to housing, employment, and health coverage, in addition to making lending decisions, the credit rating system will need to reflect a more accurate and transparent depiction of the credit-worthiness of these underserved populations. We look forward to further discussions on improving our credit system, and will be happy to respond to any questions raised by this testimony.

¹ Board of Governors of the Federal Reserve System. “Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit.” August 2007. <https://www.federalreserve.gov/boarddocs/rptcongress/creditscore/creditscore.pdf>. (accessed February 21, 2019).

² Hoyt, Homer. 1933. *One Hundred Years of Land Values in Chicago*. Chicago: University of Chicago Press.

³ Rona-Tas, Akos. “The Off-Label Use of Consumer Credit Ratings.” *Journal of Historical Social Research* 42, no. 1 (2017): 52-67. (accessed February 20, 2019).

⁴ 15 U.S.C. 1691 (2006).

⁵ Rona-Tas, Akos. “The Off-Label Use of Consumer Credit Ratings.” *Journal of Historical Social Research* 42, no. 1 (2017): 52-67. (accessed February 20, 2019).

⁶ Board of Governors of the Federal Reserve System. “Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit.” August 2007. <https://www.federalreserve.gov/boarddocs/rptcongress/creditscore/creditscore.pdf>. (accessed February 20, 2019).

⁷ MyFICO. “Understanding FICO Scores.” https://www.myfico.com/Downloads/Files/myFICO_UYFS_Booklet.pdf. (accessed February 20, 2019).

⁸ Albanesi, Stephania, Giacomo DeGiorgi, and Jaromir Nosal. “Credit Growth and the Financial Crisis: A New Narrative.” 2017. https://www.jaromirnosal.net/uploads/6/0/7/5/60756213/newnarrative_september_2017.pdf. (accessed February 20, 2019).

⁹ Chetty, Raj, et al. “Race and Economic Opportunity in the United States: An Intergenerational Perspective.” NBER Working Paper No. 24441. 2018. <https://www.nber.org/papers/w24441>. (accessed February 20, 2019).

¹⁰ Experian. “Can You Make Minimum Wage and Still Have a Maximum Credit Score?” January 12, 2018. <https://www.experian.com/blogs/ask-experian/can-you-make-minimum-wage-and-still-have-a-maximum-credit-score/>. (accessed February 21, 2019).

¹¹ Board of Governors of the Federal Reserve System. “Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit.” August 2007. <https://www.federalreserve.gov/boarddocs/rptcongress/creditscore/creditscore.pdf>. (accessed February 20, 2019).

¹² Woodstock Institute. “Bridging the Gap: Credit Scores and Economic Opportunity in Illinois Communities of Color.” <http://www.woodstockinst.org/research/reports/bridging-gap-credit-scores-and-economic-opportunity-illinois-communities-color/>. (accessed February 21, 2019).

¹³ Consumer Financial Protection Bureau. “Analysis of Differences between Consumer- and Creditor-Purchased Credit Scores” September 2012. https://files.consumerfinance.gov/f/201209_Analysis_Differences_Consumer_Credit.pdf. (accessed February 20, 2019).

¹⁴ Li, Wei. “Weaker Credit or Racial Discrimination: The Data are Unclear.” 2014. <https://www.urban.org/urban-wire/weaker-credit-or-racial-discrimination-data-are-unclear>. (accessed February 20, 2019).

¹⁵ Consumer Financial Protection Bureau. “Who Are the Credit Invisibles?” December 2016. https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201612_cfpb_credit_invisible_policy_report.pdf. (accessed February 21, 2019).

¹⁶ Ibid.

¹⁷ Ibid.

¹⁸ Ibid.

¹⁹ Ibid.

²⁰ Ibid.

²¹ Ibid.

²² Society for Human Resource Management. “Background Checking-The Use of Credit Background Checks in Hiring Decisions.” May 19, 2017. <https://www.shrm.org/hr-today/trends-and-forecasting/research-and-surveys/pages/creditbackgroundchecks.aspx>. (accessed February 21, 2019).

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