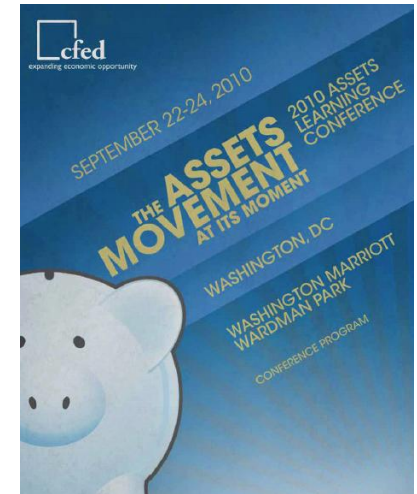


Policy & Economic Research Council

To Report or Not to Report...

Evaluating the Inclusion of Utility Payment Data in Credit Reports



By Michael Turner, Ph.D.

September 23, 2010

Utility Reporting: Solution to the Problem of Credit Access

- **30 Million** Americans with *no* payment histories (PERC)
 - No credit score possible; little access to low priced mainstream credit
- **75 Million** with *two or fewer* payment histories (PERC)
 - Too few tradelines = reduced credit score, if scoreable; pay more than should for credit
- **120 Million** could benefit from the inclusion of one or more non-reported accounts (Trycera Financial)
 - Could change score band



What is Credit? Who is a Creditor?

MORTGAGE APPLICATION

3

Name _____
Driver's License Number (with state) _____
Home Phone _____

1.	Present	Reason for moving
	Previous	Reason for moving
	First time	Reason for moving

2. Employment
Employer Name _____
Address _____
City _____ State _____ Zip _____
Employment Dates From _____ To _____
Job Title _____
Annual Salary _____
Employment Status (Full-time, Part-time, Seasonal) _____

3. Name of Bank _____
Branch Name _____
Branch Address _____
City _____ State _____ Zip _____
Account Number _____
Type of Account (Checking, Savings, etc.) _____

4. In case of co-borrower, joint, or second mortgage:
Borrower Name _____
Address _____
City _____ State _____ Zip _____
Employment _____
Annual Salary _____
Employment Status _____

5. Social Security No. _____
Date of Birth (Month, Day, Year) _____
Email _____

Business Phone	City	Zip	Owner or Mgr	Phone	From	To
_____	_____	_____	_____	_____	_____	_____

Prior Occupation _____
Present Occupation _____
Type of Loan _____
Account Number _____
Mortgage No. _____
Mortgage Type _____
Mortgage Amount _____
Mortgage Date _____
Mortgage Status _____

What is Credit? Who is a Creditor?

The Equal Opportunity Credit Act (ECOA) and the Fair Credit Reporting Act (FCRA) define credit and creditor as:

The term "**credit**" means the right granted by a creditor to a debtor to defer payment of debt or to incur debts and defer its payment *or to purchase property or services and defer payment therefor.*

The term "**creditor**" means any person who regularly extends, renews, or continues credit;

What is Credit? Who is a Creditor?

- **Utilities *are* creditors**
- **Utility payments *are* credit payments**

Clearly, utilities *can* report consumer utility payments to CRAs (and several utilities do currently report)

Q: Are Utility Payments Used in Lending?

- A: Utility payments are used in lending

It is non-controversial and advisable to use a complete picture of a borrower's obligations and payment history when underwriting and assessing capacity and risk.

- **Use of utility payments is common in alternative scores and underwriting**

- Fannie Mae
- Freddie Mac
- FHA



To report or not to report...

That is the question

- *How do consumer's fare if utility and telecom information are included in credit file?*
- *What is the benchmark? What are we comparing?*

Relevant Caveats and Misconceptions About Reporting?

Metro 2 is a flexible reporting format:

- Not limited to 30-, 60- 90, 180+ day “buckets”, can be done in days
- Provides furnisher choice (within parameters) on how to report
 - Needn't report defaults below a certain dollar value; and
 - needn't report special status of individuals on deferred payment plans or LIHEAP recipients

FICO's reporting system weighs mild negatives mildly and only serious negatives seriously:

- Score effects on 30 and 60 day delinquencies are generally mild and recovered from within a moderate timeframe?
- 90 day delinquencies are effective predictors or default/ measures of whether one can afford a loan

To Report or Not to Report...



Q: Are Low-income Consumers Hurt When Their Utility Payments Are Fully Reported?

A: NCLC shows that 85% of lowest income quintile did not pay their utility bills late in 1998

Are Low-income Consumers Hurt When Their Utility Payments Are Fully Reported?



Q: But....would scores fall much for that 15% that paid late?

A: That depends on many factors:

- How late were they?
- Did they have utility collections reported?
- Did they have many other payment histories?
- Were they late on other payments reported?

Are Low-income Consumers Hurt When Their Utility Payments Are Fully Reported?

The best way to determine the impact on low-income consumers is *not via speculation* but empirical testing with:

- Real low-income consumers
- Real credit files
- Real credit scores

Then compare outcomes when utility payment data is and is not fully reported.

....we did just that.

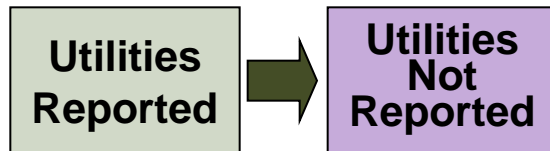
What Does the Test Do?

Helps us to compare 2 scenarios and measure:

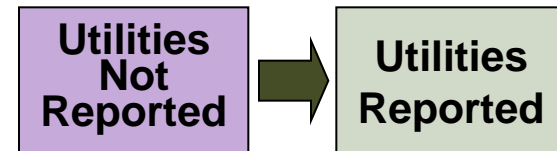
- Score changes: increases v. decreases
- Accuracy, reliability of scores

So, 2 scenarios--both are real,

Scenario 1



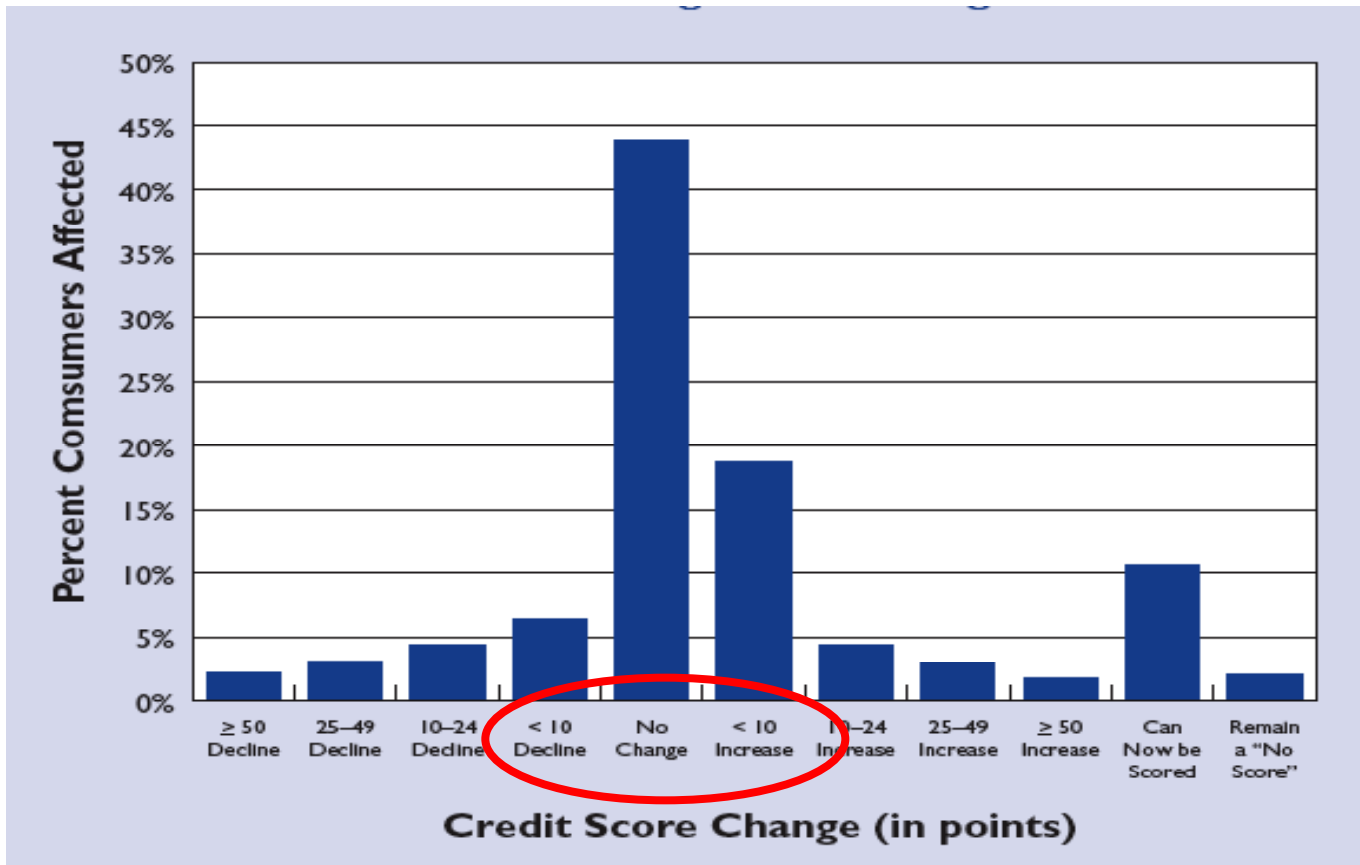
Scenario 2



- **In that many utilities do currently report.**
- **Undoing reporting also entails score change**

Original Finding: Little Effect on Scores

Change in Credit Score with the Addition of Utility Payment
Data (Statics from March 2005)



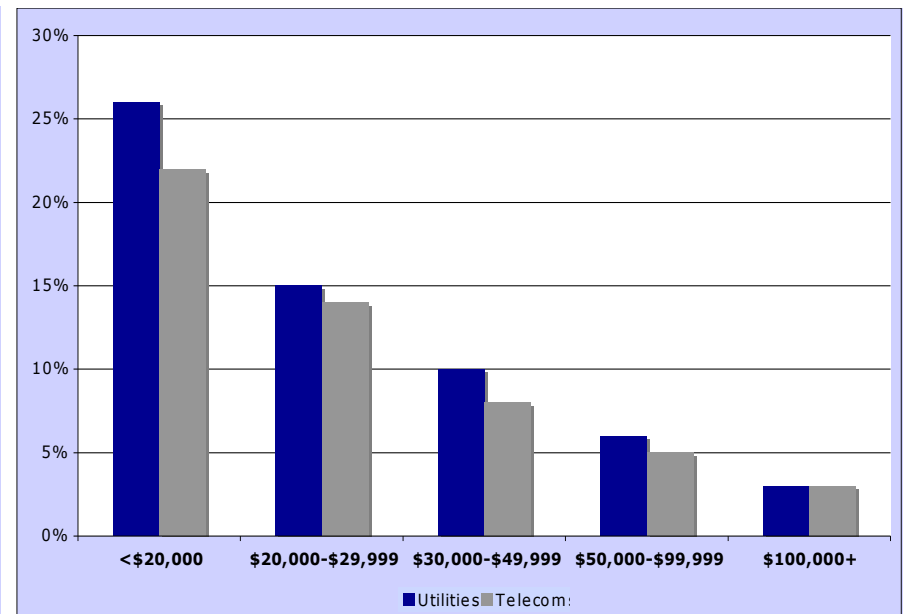
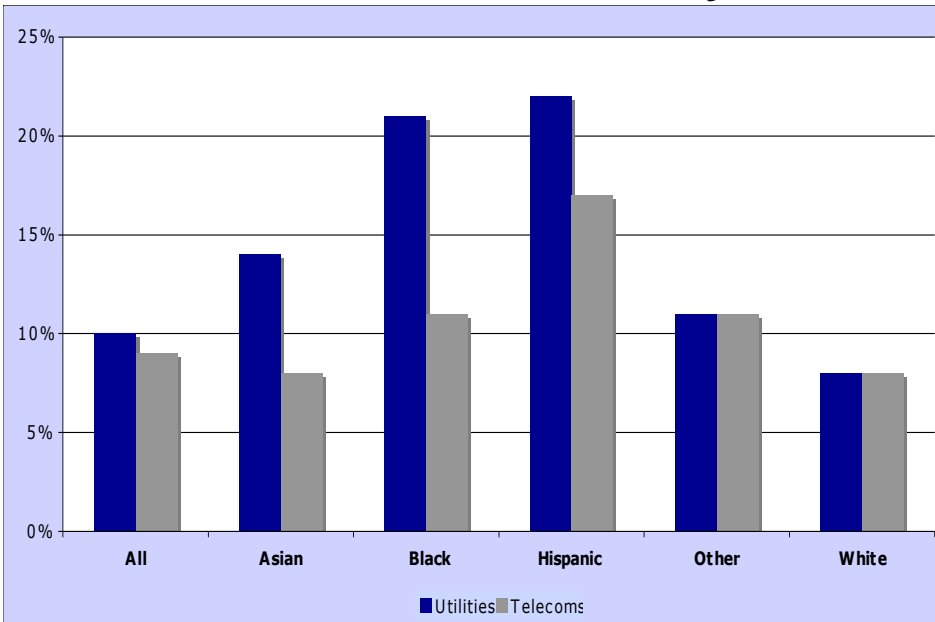
Key metric: 66% scores had little or no change in score

Key Findings: Increased Access for Underprivileged Social Segments

Change in Acceptance Rates at 3% Delinquency Target by

Race/Ethnicity

Income

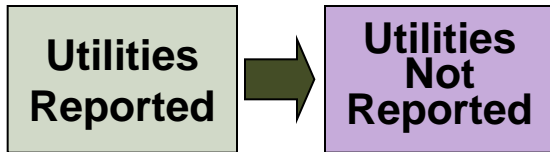


Key metric: 20%+ of African American and Latino segments able to now get mainstream credit

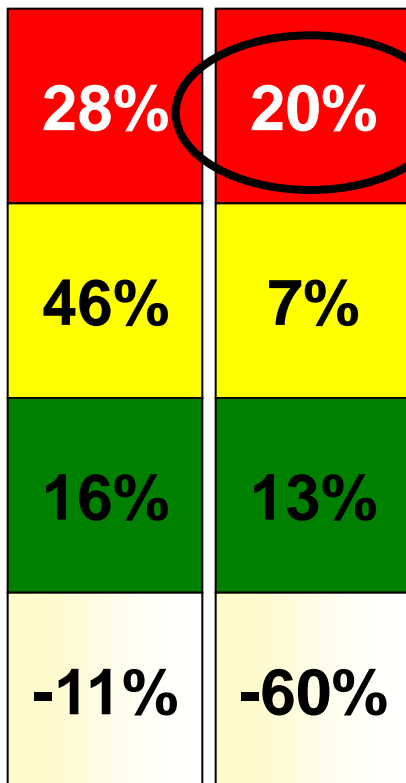
Key metric: 25%+ of households earning < \$20K able to now get mainstream credit

Comparing Scenarios: National Study 2005/2006

Scenario 1



All Thin file



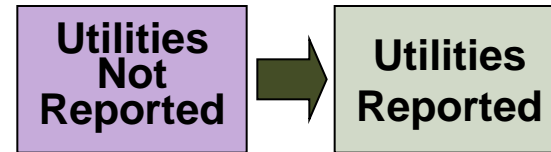
Share whose scores are worse than at starting scenario

Share whose scores don't change

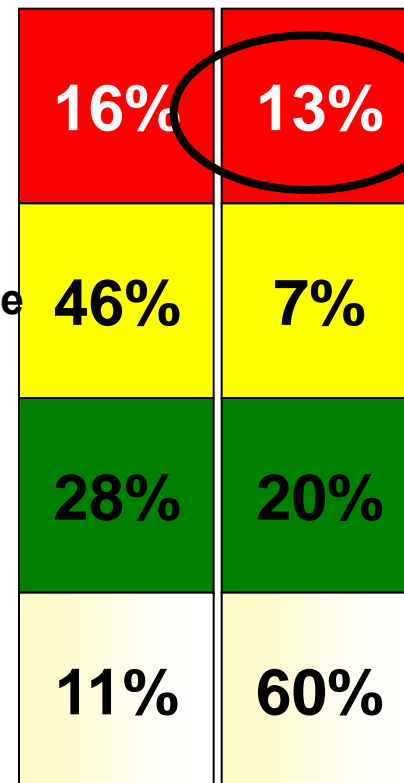
Share whose scores get better

Share that become scoreable

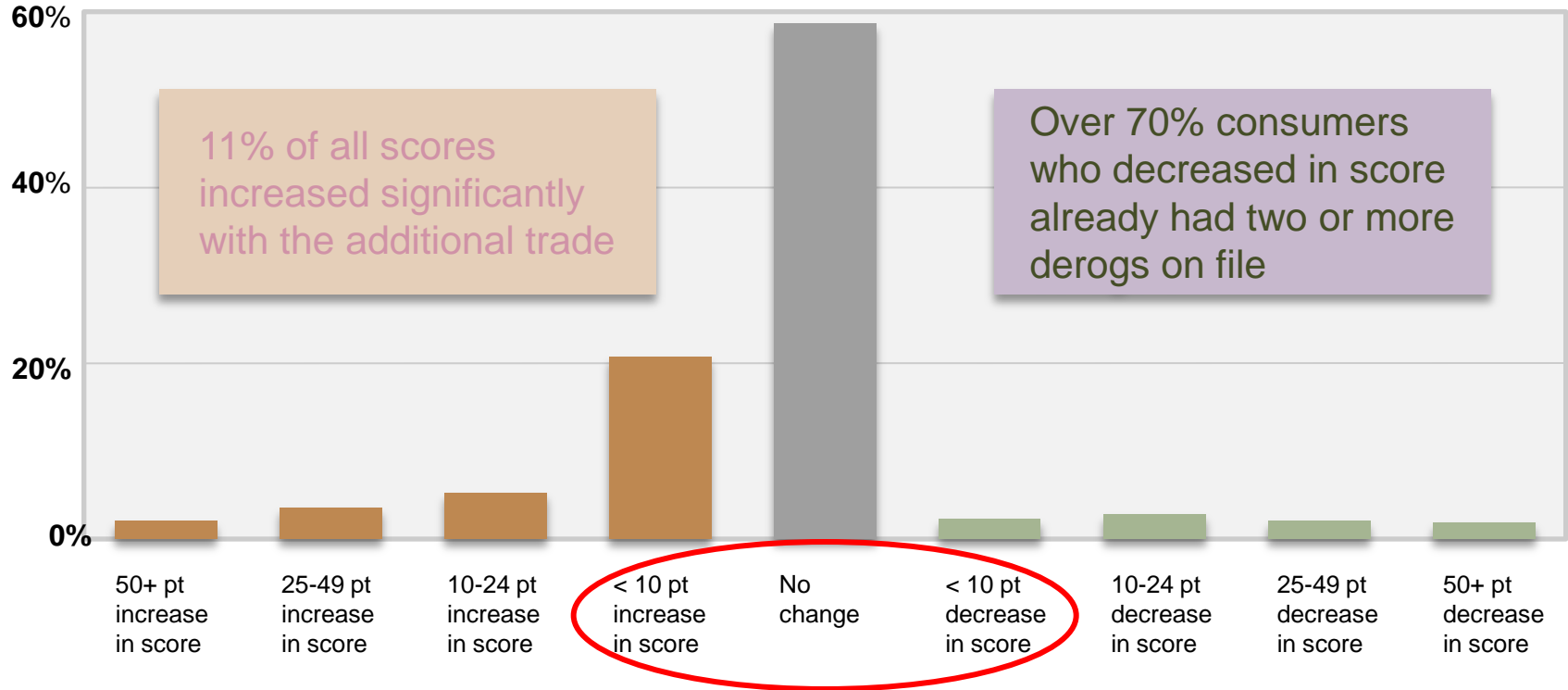
Scenario 2



All Thin file



Case Study #1: VantageScore® Changes (all customers)

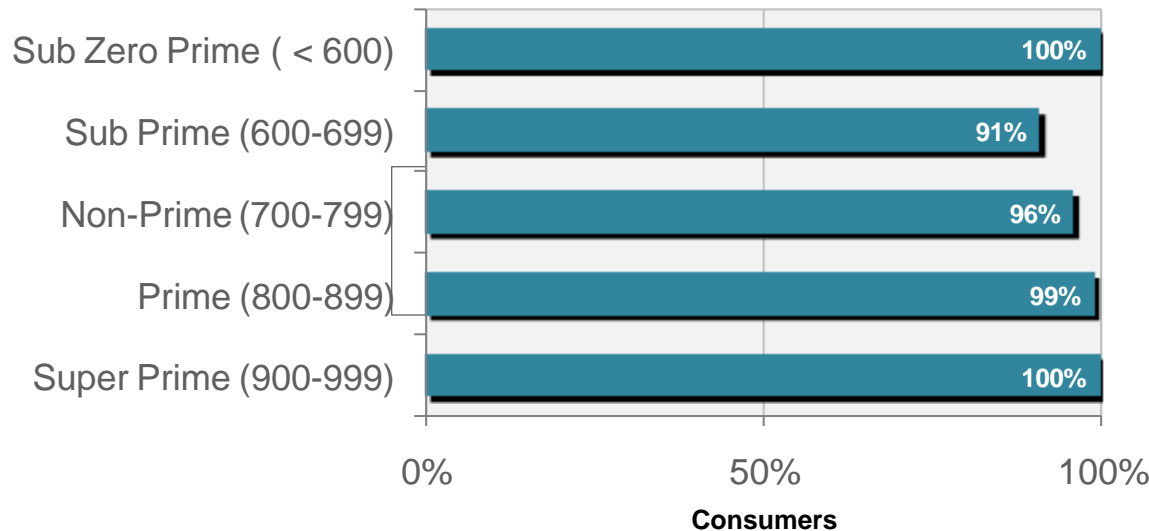


81% scores had little or no change in score

Source: Experian 2010

Case Study #1

Scoreband changes (all customers)



Very little change due to the addition of a utility trade

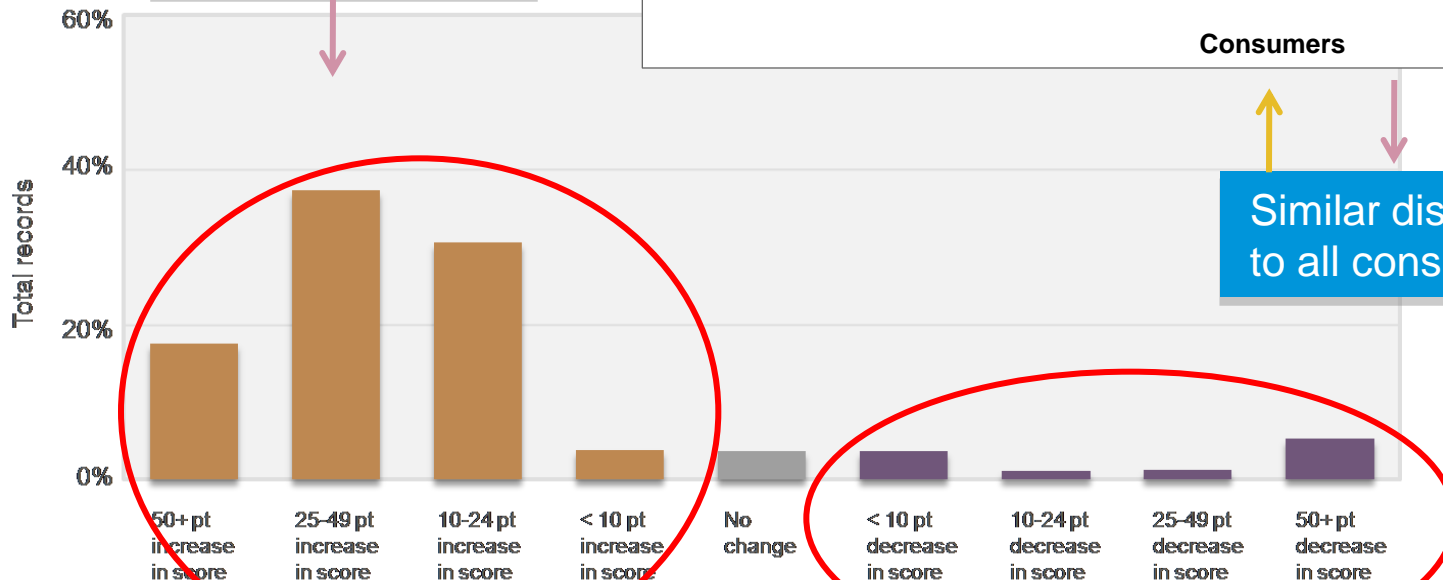
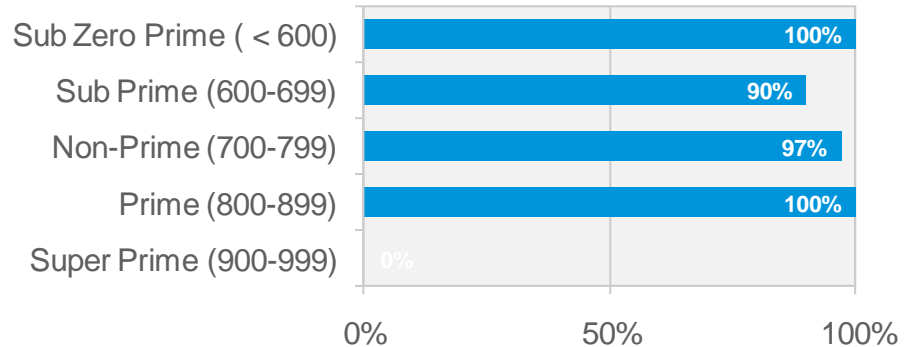
Key findings

- ▶ Over 91% either stay within the same band or move to a higher band
- ▶ 84% of the tradelines that declined were already in a negative scoreband

Case Study: Vantagescore® Scoreband Changes (Thin File)

Generally positive impact to thin file consumers with the additional utility trade

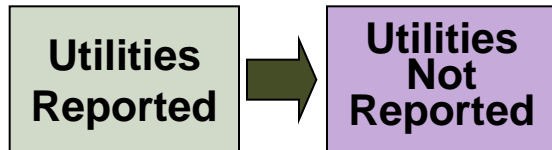
Positive scoreband changes – Thin file consumers



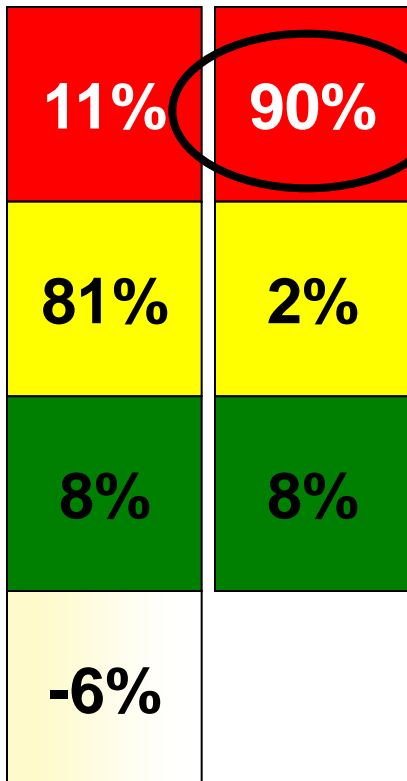
Similar distribution to all consumers

Comparing Scenarios: Recent, Post-Crisis Case Study

Scenario 1



All Thin file



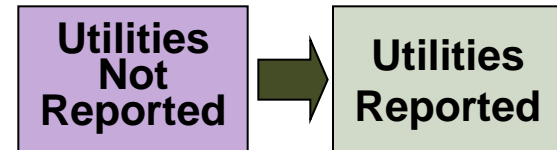
Share whose scores are worse than at starting scenario

Share whose scores don't change

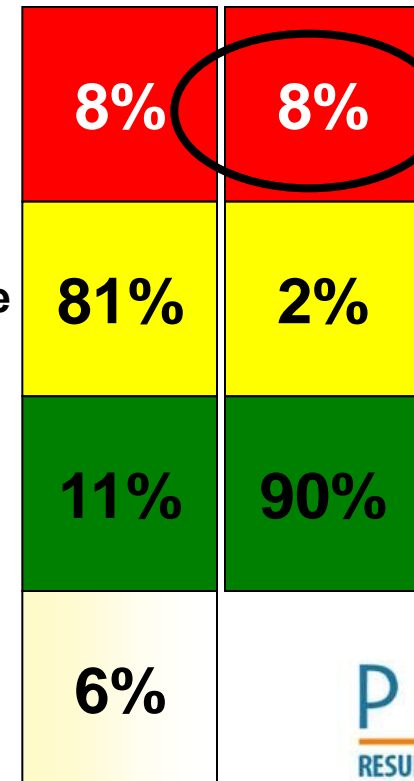
Share whose scores get better

Share that become scoreable

Scenario 2



All Thin file



Summary of Effects

Reporting improves scores for most (for whole population and thin-files)

- Whole population: 28% (when reported) compared to 16% (when not reported)
- Thin-file population: 20% (when reported) compared to 13% (when not reported)

How do we compare impact of non-reporting to impact of reporting?

- Number of people positively affected--points *to* reporting
- Number of people negatively affected--points *to* reporting
- Accuracy of score--points *to* reporting
- Minimizing harms

What is “Harm”?

The objective of credit reporting is...

- An accurate assessment of risk, meaning, associated harms
 - Low-risk borrowers are not mistaken for high-risk ones
 - High-risk borrowers are not mistaken for low-risk ones
 - Denial of credit to those who can afford it (leaving high priced credit options)
 - Provision of credit to those who cannot afford it (overindebtedness)

Effective underwriting = reduction of harm

What Does it Mean to Say That a Score “Harms” You?

What is a credit score?

- A prediction based on a set of credit and other transaction behavioral factors
 - Credit history
 - Indebtedness levels
 - Payment behavior
 - Etc.
- Harm--two conceptions of how a score can harm you?
 - Lower score vs. a score that does reflects risk poorly
 - *Is a lower score a harm if it more accurately reflects your risk than a higher score?*

Given “Harm”, What are the Choices Before US?

Return to two scenario results

- Scenario 1: we exclude utility data
 - 13% of consumer will have scores increased
 - 7% of consumers will have scores unchanged
 - **20% to perhaps as much as 90% of consumers will have scores decreased**
- Scenario 2: we include utility data
 - 20% of consumer will have scores increased
 - 7% of consumers will have scores unchanged
 - **13% of consumers will have scores decreased-
-perhaps fewer, 8%**

With reporting, more people have increasing scores and fewer people have decreasing scores...because the vast majority of people, including lower income segments, pay bills on time

Given “Harm”, By What Standard Can We Evaluate Choice?

Credit scores make accurate assessments of risk, so;

Better scores are more accurate scores

This means that utility payment data is a ***good predictor of the consumer's risk***

Score or No Score?



Q: Is it better to have a moderate or low score or no score?

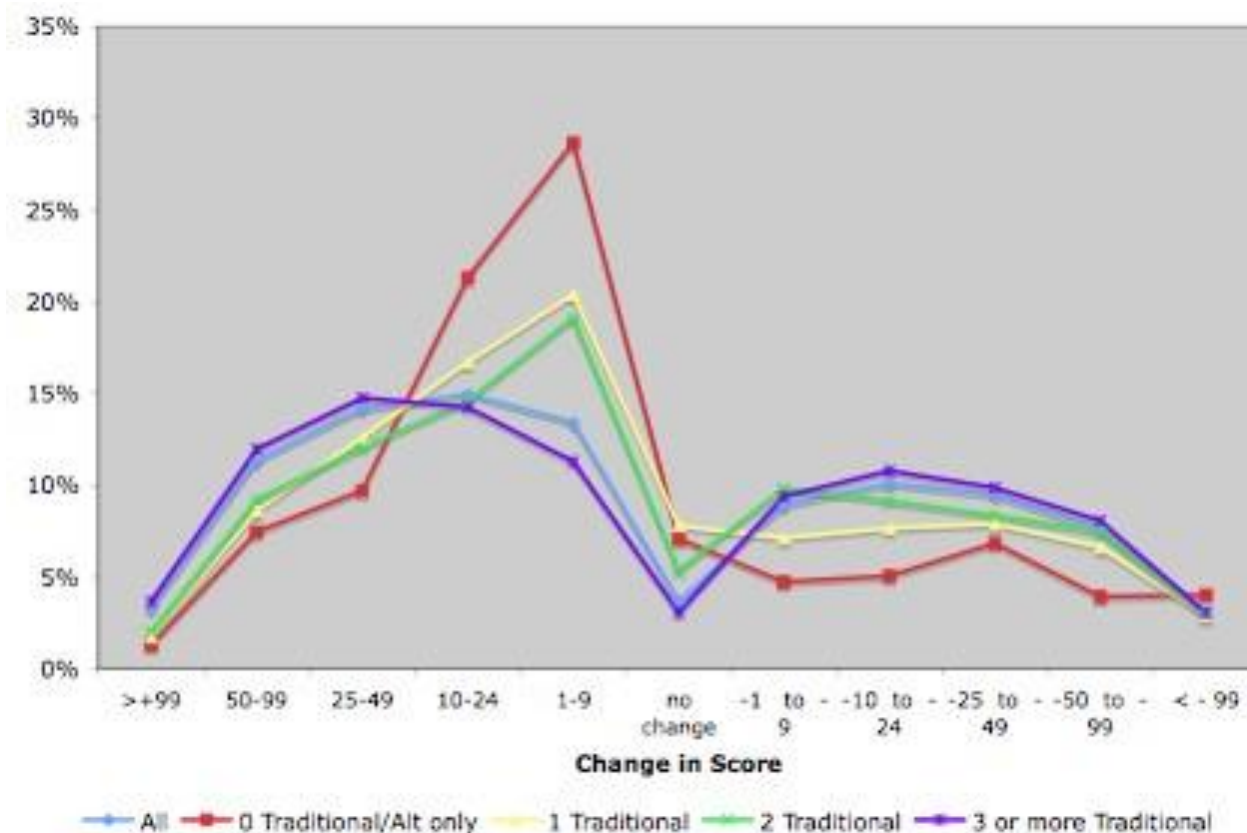
A: No score consumers are treated as highest risk; Low and moderate scores allow entry into mainstream markets

Most thin-file, no file segments have moderate to high scores.

- Score distribution similar to that of thick file population, excluding “super primes” (which require thicker credit histories)
- No evidence that access leads to overindebtedness, above what is witnessed with thick file segments

Key Findings

Changes in Score for Consumers with Alternative Data Over a 1-year Period, by Number of Trade Lines (from March 2005 to March 2006)



Scores increased for consumers by a larger degree than they decreased over the year-long period

Key Findings

This means that including alternative data can actually *allow more people to enter the credit mainstream*



Testimonial: Rose Marie and Grandville



“

I actually didn't even have a credit score for a number of years, I guess because, once again, I didn't buy a lot on credit.

I like to say you have to play the game.

I don't think they have records that show that you paid good cash.”

Research Canards I

Beware of:

Generalizations

- E.g., “lower income people will have lower credit scores” if utility data is included, when...
- **More low income consumer see score increases with inclusion than score decreases**

Beware of contextless facts that affect inferences

- “collections are increasing, therefore there are more people with delinquencies so more people will have lower credit scores,” when...
- **Collections will be reported no matter what.**
- **Scores are dynamic odds ratios.**
 - The odds of being 90+ days late or more today are quadruple of four years ago.
 - Late payments are more heavily discounted during economics down times



Research Canards I

Beware of:

Substantiated assertions — ask whether a statement has empirical support.

- Utility rates vary across states, and therefore, credit scores are determined by geography. But,
- Wage, income, taxes, housing, rent, food, and many other variables vary across regions
- Should we not report mortgage or credit card payments because of interest rate differences?

Kitchen sink approaches.

- Where multiple arguments are offered each with thin or no evidence
- **Lots of weak arguments do not make a strong one**



Support for PERC/CFED's ADI

The Abilities Fund, Florida
ACORN Institute, Louisiana
Ashoka: Innovators for the Public, Washington DC
Asset Builders of America, Inc., Wisconsin
Asset Building Policy Project (The Michigan Asset Building Coalition), Michigan
Baja Group Consultants, Canada
Biroul de Credit SA, Romania
Bread for the World, Washington DC
Community and Shelter Assistance Corp (CASA) of Oregon, Oregon
Capital Area Asset Builders, Washington DC
Center for Financial Services Innovation (CFSI), Illinois
Center for Microfinance Studies, Brazil
Collaborative Support/Community Enterprises, New Jersey
Colorado Community Action Association, Colorado
Community Economic Development Association of Michigan (CEDAM), Michigan
Community Financial Resources, California
Connecticut Voices for Children, Connecticut
Corporation for Enterprise Development (CFED), Washington DC
Doorways to Dreams (D2D) Fund, Massachusetts
Dun & Bradstreet Pty Ltd.
EARN, California
ECDC, Virginia
Experian, California
The Family Conservancy, Kansas
Good Work Network, Louisiana
Heartland Alliance for Human Needs & Human Rights, Illinois
Hope Communities, Inc., Colorado
IDA and Asset Building Collaborative of NC, North Carolina
Insight Center for Community Economic Development, California

Insight Center for Community Economic Development, California
Jewish Community Action, Minnesota
Kansas Action for Children, Kansas
Michigan IDA Partnership / OLHSA, Michigan
Micro Mite, Florida
The Midas Collaborative, Massachusetts
National Association of Consumer Advocates, Washington DC
National Bureau of Commercial Information, Oman
Neighborhood Partnerships, Oregon
Asset Building Program of the New America Foundation, Washington DC
NewWell Fund, Virginia
Okanogan County Community Action Council, Washington
OnTrack Financial Education & Counseling, North Carolina
Opportunity Finance Network, Pennsylvania
PKU-ACOM Financial Information Research Center, China
Policy and Economic Research Council (PERC), North Carolina
Prosper, California
RAISE Kentucky, Kentucky
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