Dēmos
AN EQUAL SAY AND AN EQUAL CHANCE FOR ALL

Establish a Public Credit Registry

AMY TRAUB
Associate Director, Policy & Research, Dēmos

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About Demos

Dēmos is a public policy organization working for an America where we all have an equal say in our democracy and an equal chance in our economy.

Our name means "the people." It is the root word of democracy, and it reminds us that in America, the true source of our greatness is the diversity of our people. Our nation's highest challenge is to create a democracy that truly empowers people of all backgrounds, so that we all have a say in setting the policies that shape opportunity and provide for our common future. To help America meet that challenge, Dēmos is working to reduce both political and economic inequality, deploying original research, advocacy, litigation, and strategic communications to create the America the people deserve.

demos.org
80 Broad St., 4th Fl.
New York, NY 10004

Media Contact
media@demos.org

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SUMMARY

Demos proposes establishing a public credit registry as a key part of a larger effort to reshape our rules around debt and lending in order to reduce racial wealth inequality. This publicly run credit registry would gradually replace the current for-profit corporate system and is designed to be responsive to consumer needs and equity concerns rather than the corporate bottom line. A public credit registry would develop algorithms that diminish the impact of past discrimination, deliver transparent credit scoring, provide greater data security and offer a publicly accountable way to resolve disputes. The use of credit information for non-lending purposes, such as employment, housing, and insurance will be curtailed.

THE BIG PICTURE: DEBT AND RACIAL WEALTH INEQUALITY

When Americans of all races and backgrounds have access to affordable credit on fair terms, borrowing can help households, communities, and our broader economy flourish. Credit enables families to afford significant purchases like a home or a car, smooth out ups-and-downs in household finances, manage emergencies when they occur, and create opportunities for the future, for example, by helping to launch a small business. To achieve this vision, our rules around lending, credit reporting, debt collection, and bankruptcy must serve the public interest—not the interest of greedy banks, fringe lenders, credit reporting companies that cash in on our personal data, or speculators who grow rich draining wealth from our communities. A fair consumer credit system should be part of a larger financial system that operates like a utility, distributing risk and resources so that we can all share in the prosperity that we help generate.

Yet the reality of debt and lending in America today is far from this vision. Credit reporting companies issue reports riddled with errors and unavoidable medical debt that compel home buyers to pay thousands of dollars in additional interest; predatory lenders target struggling families for deceptive and exploitative loans; debt collectors hound consumers about loans they paid off long ago or never took out in the first place. Most harmfully, our credit system is built on—and continues to reinforce and expand—deep racial inequities. Public policymakers institutionalized the discriminatory lending that established much of America's continuing racial wealth inequality: for example, starting in the late 1930s the Federal Housing Administration redlined entire black neighborhoods, marking them as bad credit risks and effectively discouraging home mortgage lending in these areas, even as black home buyers continued to be excluded from white neighborhoods.[1] The patterns of segregation and inequality established by redlining policy persist to this day.[2] And because redlining and similar discriminatory public policies and corporate practices systematically excluded (and continue to exclude) black, Latino/a, and other families of color from wealth-building opportunities that benefit white families, households of color today have substantially less wealth than their white counterparts, even when controlling for factors like age and education.

As a result, families of color remain less likely to have sufficient savings to fall back on to handle an emergency, buy a car, attend college, pay a medical bill, start a business, or make a down payment on a home.[3] The lack of wealth and greater need for credit to meet these needs disproportionately exposes communities of color, as well as low-wealth white communities, to new waves of predatory lending and other forms of high-cost credit. In a vicious cycle, high-cost credit strips additional resources from families and communities, further reducing the quality of their credit and increasing their reliance on borrowing in the future. Our system of credit and lending automatically increases racial wealth inequality and causes racial economic disadvantage to persist and spread.

To disrupt the cycle of racial economic disadvantage, policymakers must change the rules around credit and debt, remaking the credit system to serve the public. Policymakers must also improve jobs and public services, so that borrowing is less central to Americans' ability to thrive economically. Therefore, we propose an innovative policy solution: establish a public credit registry to replace for-profit credit reporting corporations—and endorse a suite of additional policies that would move the nation towards our vision of fair and equitable credit for all. These policies include:

- **Establish a public credit registry.** Congress should establish a publicly run credit registry, housed in the Consumer Financial Protection Bureau, that would gradually replace the for-profit corporate system. The public credit registry would be responsive to consumer needs and equity concerns rather than the corporate bottom line. A public credit registry would develop algorithms that diminish the impact of past discrimination, deliver transparent credit scoring, provide greater data security and offer a publicly accountable way to resolve disputes. The public registry would also restrict the use of personal credit information for non-credit purposes, for example prohibiting employment credit checks.

- **Ban predatory lending.** Congress should enact a set of national usury limits which are indexed to a federal rate, and tiered based on the credit product (for example, auto loans, payday loan, or credit cards); cap lender fees; and require lenders to evaluate a borrower's ability to repay all loans. In no case should the annual interest rate on any type of loan exceed 36 percent, the rate researchers have found establishes a cycle of debt that is difficult for borrowers to escape.

- **Reform debt collection practices.** Congress should reform the Fair Debt Collection Practices Act and the Consumer Credit Protection Act to prevent abuses by creditors and collection agencies. Priorities include broadening the law to cover *anyone* collecting on a debt, reining in threats and harassment (including the use of arrest warrants in debt collection cases), and mandating that debt collectors fully verify information about a debt before attempting collection. Congress should modernize outdated rules on the amount of wages that can be garnished and assets that can be seized to repay debt and should clarify that consumers have the right to sue to halt unfair practices.

- **Ensure fairness in bankruptcy.** Congress should reform bankruptcy law to enable Americans in severe financial distress to get a fresh start. Key reforms include permitting consumers to discharge student loans in bankruptcy, allowing bankruptcy courts to modify unfordable mortgages and ensuring that the bankruptcy process as a whole works effectively for people of color.

- **Prohibit forced arbitration.** Congress should ban the forced arbitration clauses that appear in the fine print of many financial contracts. These clauses deprive consumers of their right to a day in court and force them into an arbitration process that is tilted in favor of companies, allowing corporations to dodge accountability for violating the law and cheating consumers.

- **Defend the Consumer Financial Protection Bureau (CFPB).** Congress should oppose the Trump administration's efforts to weaken the authority of the CFPB and should instead bolster the agency's independence and authority to protect consumers by investigating the consumer finance industry, supervising financial companies, enacting and enforcing financial regulations.

- **Improve jobs and public services.** Struggling families often take on debt when wages are not sufficient to make ends meet; when public services do not address critical public needs such as health care, higher education, transportation, or child care; or when a disaster strikes and safety net programs are inaccessible or insufficient to sustain people. To reduce families' need to resort to debt in the first place, Congress should act to raise job standards, expand and improve public services, and strengthen safety net programs.

POLLING DATA: AMERICANS STRONGLY SUPPORT STRONGER RULES ON CREDIT AND LENDING

- Americans overwhelmingly agree there should be more government regulation of financial companies, such as Wall Street banks, mortgage lenders, payday lenders, debt collectors, and credit card companies.[4] Overall, 71 percent of Americans say there should be more regulation of financial companies, including 87 percent of Democrats, 73 percent of Independents, and 52 percent of Republicans. Only 17 percent of Americans think financial companies should be less regulated.
- Following the Equifax data breach, nearly 8 in 10 Americans say companies that do a bad job protecting customer data should face more severe legal penalties. That view cuts across party lines: 81 percent of Democrats and independents and 79 percent of Republicans agreed.[5]
- Americans strongly support the mission of the CFPB to mission to "prevent deceptive, unfair and abusive lending and collection practices by banks and other companies."[6]
- 77 percent of Americans say it is "very" or "somewhat concerning that the CFPB is cutting back on work to prevent racial discrimination in lending and "ending efforts to curb discrimination in lending based on data showing that borrowers of color pay more for loans"[7]

SIGNATURE POLICY: ESTABLISH A PUBLIC CREDIT REGISTRY

The Problem

Credit reports and scores directly impact Americans' economic security and opportunity. Credit history can affect the way Americans are treated by lenders, landlords, utility companies, hospitals and employers.[8] Having a poor credit history or a "thin file" with insufficient credit information to generate a credit score can mean a consumer will end up paying more for loans and insurance (or have trouble even getting them in the first place). Misguided uses of credit history are prevalent and harmful: job seekers can be denied work based on their credit history[9] and the Trump administration has even proposed using credit history to determine whether immigrants should be eligible for permanent residency.[10] And generations of discrimination in employment, lending, education and housing have produced significant racial disparities in credit history. Past discrimination is baked in to current determinations of creditworthiness: Credit scores and other lending algorithms disproportionately represent black and Latino loan applicants as "riskier" customers.[11] Black and Latino consumers are also more likely to be "credit invisible" – to lack a robust credit history at all.[12] As a result, decisions drawing on credit data reproduce and spread existing racial inequality, making it harder to achieve true economic equity.

America's credit reporting system is controlled by three big, for-profit companies—Experian, Transunion, and Equifax—which collect lending and payment data on 220 million Americans without consumers' permission or approval, and there is no way for consumers to opt out from having personal financial data collected. Recent security breaches at one of the "big three" companies illustrate how unreliable and unaccountable to consumers these companies are. The algorithms that determine our credit worthiness are not publicly available and consumers must pay to access their own credit reports and scores (beyond one free report from each company per year). Errors are common, and people of color experience higher error rates than white households.[13] Meanwhile these errors are notoriously difficult to correct, as credit reporting companies have failed to make the investments necessary to investigate disputed items.[14] It is lenders—not American consumers—who are the customers of these companies. Our consumer data is their product, thus these corporations are not accountable to consumers. The companies have no incentive to be concerned about racial equity or fairness.

Credit reports and scores were designed as tools for lenders to evaluate whether a would-be borrower would be a good credit risk, using a consumers' past behavior to predict how responsibly they will use credit in the future. Yet the high rate of errors and the reality that consumers handle different types of debt differently may make credit scores and reports significantly *less* predictive than they are purported to be. Consider unpaid medical bills, which tarnish the credit reports of nearly 1 in 5 consumers.[15] Unlike a student loan or a mortgage, medical debt is often involuntary and unplanned and patients seldom know how much doctors and hospitals will charge them for medical care beforehand. A Federal Reserve study noted that even credit evaluators—the employees at banks and other lending institutions who evaluate applicants' reports for creditworthiness—have concerns about the appropriateness of including medical debt on credit reports, noting that they "may be of questionable value in predicting future payment performance."[16] Predatory and deceptive financial products represent a similar difficulty: a consumer's inability to repay an abusive loan (such as the shoddy mortgages that lenders aggressively marketed in communities of color during the run-up to the 2008 financial crisis) reveals little about how the same borrower would handle credit provided on fair terms.[17] Yet millions of Americans who have unfavorable credit reports and scores as a result of medical debt and/or predatory loans must pay more to access conventional loans and insurance as a result. At the same time, families making regular rent payments and utility payments—which could provide evidence that they are responsible consumers—are unable to have this positive payment history reflected on their credit reports or used to improve their credit scores.[18]

If credit information is a flawed tool for its intended function of lending, it is even less appropriate when used for other common purposes like employment screening or insurance. Nearly half of U.S. employers check job applicants' credit as part of the hiring process.[19] Credit reporting companies have promoted their product as a way to discern a prospective employee's character or even whether they are likely to commit fraud or steal from an employer. Yet there is scant evidence that personal credit history can reveal any of this.[20] Instead, misusing credit data for employment purposes can shut out otherwise qualified job seekers because of medical debt, student loans, a layoff, divorce, predatory loans, or the ubiquitous credit reporting errors. Employment credit checks have a disproportionate impact on people of color, as they reproduce historic discriminatory practices. People with disabilities[21] and survivors of domestic abuse[22] also face discrimination as a result of employment credit checks. By screening out job applicants who have imperfect credit, employers are effectively judging a prospective employee on the basis of economic disadvantage, and then multiplying that disadvantage by denying a job. A similar process may be at work when home and car insurers charge more to insure people with low credit scores, claiming that people with poor credit are more likely to make an insurance claim.[23] However, this propensity might reflect unfair factors such as wealth or income. The "mission creep" of credit information is the predictable result of a for-profit industry seeking new markets for its existing products—regardless of their applicability or the impact on people's well-being.

Why fairer credit reporting cannot completely eliminate racial disparities in credit

A more fair credit reporting system could minimize disparate racial impact, but could not, by itself, eliminate it. This is because the function of credit reporting is to provide information about a borrowers' past actions to predict future behavior, so that lenders can appropriately price risk that a loan will not be repaid. Since a borrowers' past actions result of from unequal resources and opportunities shaped by an ongoing legacy of structural racism there is no way to produce a credit reporting system that is entirely free of disparate racial impact until other elements of structural racism are dismantled. By minimizing racial disparities, a fair credit reporting system can be part of the effort to eliminate racial wealth inequality.

Policy Solution

Establish a public credit registry, housed in the Consumer Financial Protection Bureau, to gradually replace the for-profit, corporate credit reporting system. The public credit registry will improve equity, transparency, accuracy, accountability, appropriateness, security and public awareness of credit information through the following mechanisms:

- **Equity:** The public credit registry will develop new algorithms for predicting creditworthiness with a goal of minimizing disparate racial impact. New credit reporting algorithms could draw on alternative data sources (beyond lending), when these data have been shown to be predictive and to minimize racial disparities. Data sources could include allowing consumers to opt into reporting bank account data, rental payments, or utility data in order to have a more full credit file. It is important that these data sources be opt-in rather than mandatory because of equity considerations relating to each source of data.[24] Some lenders are already experimenting with alternative data, often without robust considerations of equity or fairness. In addition to drawing on new data sources, the public credit registry will research proposals to exclude certain adverse credit data from credit reports and scores, for example medical debt or payment delinquencies on credit products determined to be predatory. The public credit registry will reduce the amount of time that adverse credit information remains on a credit report from 7 years to 4 years.

- **Transparency:** The algorithms used to determine creditworthiness will be publicly available with clear explanations of what consumers can do to improve their credit. Credit reports and scores will be free to consumers at any time.

- **Accuracy:** Lenders and other companies that furnish consumer credit data to the public credit registry will be held accountable for providing accurate information. The CFPB will impose fines on companies found to consistently furnish inaccurate or incomplete information. At the same time, the public credit registry will use the most robust methods available to ensure that credit information is accurate and to avoid mixed files (cases where one person's credit accounts are mixed into someone else's file).

- **Accountability:** Consumers will have a right to dispute inaccurate information on their credit report and will be provided free copies of any documents used by the public credit registry to ascertain the accuracy of a disputed item. Consumers will have the right to appeal the results of a dispute and provide additional evidence. As a last resort, consumers will have the right to sue the public credit registry for a failure to fulfill its responsibilities.

- **Appropriateness:** Credit information will only be used for lending purposes, not employment, housing, or insurance. The federal government may not use credit information to make decisions about immigration status or for any purpose other than lending and credit information will not be shared with any other government agency.

- **Security:** While no electronic data is 100 percent secure, the public credit registry's ultimate accountability to American consumers will provide a greater incentive to enhance data security compared to the private credit reporting agencies (CRAs), which so far have faced very light consequences for data breaches.[25] Americans already trust their government with extensive personal financial information through the Internal Revenue Service, which has a strong record of data security. As an additional safeguard against fraud and identity theft, all personal credit information will be frozen by default, meaning that prospective lenders will be unable to access consumer credit data without prior authorization from a consumer. There will be no charge to consumers for removing credit freezes or placing a new one on their credit information.

- **Public awareness:** The public credit registry will fulfill the CFPB's mission of educating consumers about credit products and how to develop and maintain a good credit score. The public credit registry will also provide free or low-cost credit counseling and credit rehabilitation services, through contracts with licensed non-profit organizations that already provide these services.

THE TRANSITION TO THE PUBLIC CREDIT REGISTRY

The public credit registry will be established as a function of the Consumer Financial Protection Bureau. Over a period of 7 years, all consumer credit reporting will shift from the private credit reporting agencies (CRAs) to the public credit registry. The 7-year transition period allows the public credit registry to amass sufficient data on consumers to fully replace the private, for-profit CRAs. As soon as the public credit registry is launched, any furnisher of data that currently reports to any private CRA will also be required to report data to the public agency. Consumers will be able to immediately opt out of having their credit data furnished to private CRAs. Private CRAs and furnishers of credit data will be required to report the age of all accounts to the public credit registry, so that the positive credit history of long-time payers can be reflected in the public registry's records. During the transition period, prospective lenders seeking credit information could continue to consider data from the private CRAs in making lending decisions, but lenders would not be permitted to discriminate against prospective borrowers who have opted out of reporting to the private CRAs. After the public credit registry has collected consumer credit data for 7 years, lenders will *only* be permitted to consider data from the public credit registry to make lending decisions—lenders will no longer be allowed to consider data from private CRAs or any other private source.

Many countries in Asia and Europe have public credit registries, although these are primarily oriented toward ensuring the stability of lenders, not the benefit of consumers. The United States will be a pioneer in establishing a consumer-oriented public credit registry that also benefits lenders through its greater accuracy, predictiveness, and public perceptions of fairness.

How to Talk About the Public Credit Registry

The messaging ideas in this section derive from best practices developed by communications and messaging experts.[26] General principles include:

- Start with an appeal to values and the vision of a better future.
- Include an up-front discussion of race and of the *causes* of racial disparities in wealth, credit, and debt.
- Highlight credit and debt as systemic issues, rather than exclusively personal failings.
- Emphasize the concrete, lived consequences of credit and debt disparities for people (being denied a job, paying more every month for a car loan) and the concretely better outcomes for people that would be a result of good policy.
- Offer a clear villain, in this case unaccountable private credit reporting companies.

Why we need a public credit registry: When Americans of all races and backgrounds have access to affordable credit on fair terms, borrowing can help households and communities flourish. Families need fair access to credit in order to rent or buy a home or car, start a business or attend college, and manage emergencies when they occur. But today, the credit reports and scores required to get credit are controlled by three big, for-profit companies that collect and sell our personal financial information with little concern for fairness or accuracy, and no accountability to consumers. We need a public credit registry to ensure that credit benefits people and communities, not corporations that profit from selling our private information.

How a public credit registry advances racial equity: Our nation is at its best when every American enjoys full and equal opportunity to participate in the economy. Yet our nation's policies and practices have historically shut families of color out of opportunities to fairly access credit and accrue wealth. Those generations of discrimination continue to push up the costs families of color pay today for car loans, mortgages, credit cards and other types of borrowing. By providing fairer and more equitable access to credit, a public credit registry opens the doorway to more affordable credit for families experiencing the harms of discrimination and a fairer system for *all* Americans.

Why we need credit and lending reform as a whole: Our lending and credit system should operate like a public utility, distributing risk and resources so that we can all share in the prosperity that we help generate. To do this, our rules around lending, credit reporting, debt collection, and bankruptcy must change to serve the public interest – not the interest of greedy banks or fringe lenders, credit reporting companies that cash in on our personal data, or speculators who grow rich draining wealth from our communities.

More Resources

- Demos Discrediting America
- National Consumer Law Center An Overview of the Credit Reporting System
- Federal Trade Commission Follow-Up Study on Credit Report Accuracy
- Demos and the Institute on Assets an Social Policy at Brandeis University The Racial Wealth Gap: Why Policy Matters
- National Consumer Law Center How Credit Scores and Other Analytics "Bake In" and Perpetuate Past Discrimination

WRAP-AROUND POLICY: BAN PREDATORY LENDING

The Problem

When Americans of all races and backgrounds have access to affordable credit on fair terms, borrowing can help households and communities flourish. Yet risky, high-interest debt can profoundly undermine communities, draining resources and destabilizing family finances. In the 1990s, politicians loosened rules on the financial sector, enabling lenders to prey on Americans struggling to make ends meet. Unscrupulous lenders cashed in on predatory loans of all types, from the deceptive mortgages that triggered the Great Recession to credit cards full of tricks and traps hidden from reasonable borrowers. While regulators reined in some of these abusive practices, others continue to flourish: Payday lenders and car-title lenders multiplied, promising quick and easy money while trapping borrowers in a cycle of debt. Because communities of color have historically been shut out of opportunities to fairly access credit and accrue wealth, black, Latino, and other communities of color are particular targets of abusive lending practices today, further expanding racial wealth inequality.

Twelve million Americans take out payday loans each year, spending more than $9 billion on loan fees.[27] Payday and car-title lenders disproportionately target low-income neighborhoods with high populations of people of color, promoting quick-fix loans with annual interest rates of nearly 400 percent a year on average. These short-term loans also carry high fees, so that most borrowers ultimately pay more in fees than they originally obtained in credit.[28] The loans are designed so that the vast majority of borrowers will have to roll over or renew their loans within 2 weeks, incurring new fees and additional interest. Car-title loans operate on a similar business model of repeat loans, with 1 in 5 consumers ultimately losing their vehicle through repossession.[29] While the predatory lenders make millions, low-income borrowers often end up in financial wreckage, because they are less able to pay their mortgage, rent, and other bills.

Policy Solution

Protect consumers from high-interest debt.

- **Enact a set of national usury limits**. The limits are floating, indexed to a federal rate, and potentially tiered based on the credit product (for example, auto loans or credit cards). In no case should the annual interest rate on any type of loan exceed 36 percent, the rate researchers have found establishes a cycle of debt that is difficult for borrowers to escape.
- **Require all lenders to evaluate a borrower's ability to repay all loans.**
- **Cap lender fees.** Limit late fees and charges for borrowers who fail to make a payment on or before the due date.

How Banning Predatory Lending Works

- Today 14 states and the District of Columbia have effective caps on loan interest, essentially banning payday lenders from preying on 90 million Americans.
- People living in states without payday and car-title loans save an estimated $5 billion a year in fees annually—$2.2 billion from payday lending, plus another $2.8 billion from car-title lending.[30]
- The Military Lending Act prohibits active-duty service members from being charged interest greater than 36 percent; however, loopholes have undermined the law.[31]
- The Credit CARD Act of 2009 protects consumers from excessive and unfair credit card fees, and has saved consumers more than $16 billion in fees since it went into effect.[32] Although credit card issuers warned that limiting fees would choke off access to consumer credit, available credit increased and the cost of credit declined.

More Resources

- Americans For Financial Reform consumer finance resource page
- The Center for Responsible Lending resource page
- StopTheDebtTrap.org campaign page on payday lending

WRAP-AROUND POLICY: REFORM DEBT COLLECTION PRACTICES

The Problem

Debt collection enables credit markets to operate, giving creditors a recourse if consumers are unwilling or unable to fully repay money they owe. Yet policymakers have permitted debt collection to grow into a predatory industry, with unscrupulous collections companies using underhanded tactics to squeeze profits from struggling families. Americans are harassed, have their paychecks garnished and assets stripped—and may even be jailed—for debts they may never have owed in the first place. Nationally, 1 in 3 American adults has a debt in collections on their credit report.[33] Under current law, a debt reported as being in collections can remain on a credit report for as long as 7 years, although debt collectors often use deceptive tactics to make even older debts appear current.[34] Debts in collections include not only auto, credit card, payday and other loans but also unpaid bills for services like medical care, legal services, utilities, rent, or even traffic tickets.

When a consumer becomes late on a bill, creditors frequently sell the past due debt to a debt collection company for pennies on the dollar. Although debt collectors purchase the debt at a steeply discounted rate, they aggressively seek to collect the full amount, and may add inflated interest charges, penalty fees, and attorney's fees. Although some states and cities have strong protections around debt collection, a lack of robust federal oversight allows the spread of predatory debt collection practices such as threatening or harassing phone calls and efforts by debt collectors to contact the employer or relatives of a person with debt. In addition, debt collectors routinely sue Americans for even small consumer debts. Debt collection lawyers may file hundreds of lawsuits each day: in many cases, the alleged debtors are unaware they have been sued and received no notice to appear in court.[35] Even if they have little evidence that a debt is actually owed, debt collectors win judgments that allow them to seize a significant portion of a person's pay or assets, even when this exposes the consumer to severe economic hardship. In some states, courts issue arrest warrants for people who fail to appear in court to deal with debt judgments: people already unable to pay bills may wait in jail until they can arrange to pay bail, creating a *de facto* debtors' prison.[36] The injustice is compounded by the fact that debt is frequently sold with incomplete or inaccurate information about who owes the debt, whether some portion has already been paid, whether the statute of limitations on the debt has passed and who genuinely has the right to collect on it. A survey by the Consumer Financial Protection Bureau found that 53 percent of consumers contacted by a debt collector reported receiving collection attempts that were incorrect because the debt was not theirs or was the wrong amount.[37]

While debts in collection are widespread, they are far from evenly distributed. Researchers at the Urban Institute find that debt collections are concentrated in neighborhoods experiencing greater financial distress, including higher rates of unemployment, lower household incomes, lower rates of health insurance coverage, lower housing values and homeownership rates, and more delinquent and underwater mortgages.[38] They also find that debt in collections is more prevalent in predominantly African American and Latino neighborhoods. As a result of generations of discrimination, black households and other households of color have access to dramatically fewer resources than their white counterparts to fall back on in a time of need. As a result, black families are more likely to face financial stress, resorting to unsustainable levels of debt or leaving certain bills unpaid. A ProPublica analysis of court judgments in three major metropolitan areas revealed that even after accounting for income, residents of predominantly black neighborhoods had twice as many judgments for unpaid debt as residents of mostly white neighborhoods.[39]

Policy Solution

Congress should reform the Fair Debt Collection Practices Act and the Consumer Credit Protection Act to prevent abuses by creditors and collection agencies. The National Consumer Law Center's Model Family Financial Protection Act, while drafted as a state bill, provides an excellent set of principles for federal legislation. The following recommendations build on that model:

- Ensure that consumer protections apply regardless of who is attempting to collect on a debt, including both creditors and third-party debt collectors.
- Curtail debt collectors' use of threats and harassment to collect on debt, prohibiting arrest warrants in all debt collection cases, including for unpaid criminal justices fines and fees. Debt collectors must obey a consumer's request to stop calling and cannot leave messages with friends, neighbors, or

employers.

- Mandate that debt collectors fully document and verify information about a debt, the consumer who owes it, the original creditor, any previous payments or collection efforts, and the ownership of the debt before attempting collection.
- Prohibit attempts to collect debt that is beyond the statute of limitations.
- Require debt collectors to provide consumers with written notice of their intent to file any lawsuit or arbitration claim at least 30 days in advance so that consumers have adequate notice to defend themselves. The notice must include full documentation of the debt as described above as well as name and contact information for the debt collector.
- Require debt collectors to respond to consumers' disputes about debt.
- Reduce the amount of wages that creditors and debt collectors can garnish from workers' pay and restrict assets that can be seized, including the amount of money that can be seized from bank accounts. At minimum, debtors should retain the ability to work (including protecting a vehicle or money for commuting), live in their homes, and preserve and income capable of supporting their families. The value of income and assets exempted from debt collection should automatically adjust based on the consumer price index.
- Limit attorneys' fees, interest rates on unpaid debt, and other charges to reasonable levels.
- Clarify that consumers have the right to sue debt collectors and creditors to halt unfair practices. Increase statutory damages and class relief provisions and adjust them automatically for inflation, so that they are a genuine deterrent to violators and offer real compensation to consumers who have been wronged. Encourage courts to consider awarding damages per violation for egregious activities by debt collectors.
- Ensure that people facing debt collections are informed of their rights and can access programs designed to help low-income debtors.

How Reforming Debt Collection Works

In the late 2009 and 2011 respectively, North Carolina and Maryland enacted strong new state rules to curb abuses by debt buyers and collectors.

- Both states raised standards for substantiating and verifying debt, increasing the documentation debt buyers and collectors needed to show to in order to obtain a legal judgment against consumers.
- The debt-buying industry claimed that the regulations would result in less credit being made available, particularly to consumers with below-prime credit scores. However, a thorough study by the Center for Responsible Lending found that after the new rules were in place, credit availability in North Carolina and Maryland reflected larger national trends in credit rather than being impacted by the new rules.[40]
- Further, North Carolina and Maryland consumers seeking new credit cards generally fared better than consumers in peer states, according to the study.[41]
- Sub- and near-prime consumers in North Carolina and Maryland fared at least as well as those nationally and in peer states regardless of debt-buying reforms.[42]

More Resources

- National Consumer Law Center Model Family Financial Protection Act
- ACLU A Pound of Flesh: The Criminalization of Private Debt
- Center for Responsible Lending Debt Collection resource page
- ProPublica Debt Collection Lawsuits Squeeze Black Neighborhoods

WRAP-AROUND POLICY: ENSURE FAIRNESS IN BANKRUPTCY

The Problem

When Americans are overwhelmed by debt they cannot pay, they should have the opportunity to get a fresh financial start in bankruptcy. The ability to discharge unpayable debts in an orderly way has been such a critical part of the nation's economy from its earliest days that it is enshrined in our nation's founding documents.[43] Yet the bankruptcy system does not treat all types of debt—or all types of debtors—equitably. Under current law, the treatment of home mortgage debt and student loan debt in bankruptcy is particularly problematic, leading struggling families to lose their homes unnecessarily and student borrowers to remain trapped in debt even if the face of severe financial adversity. At the same time, African American consumers are far more likely to experience worse outcomes in bankruptcy cases than their white counterparts.

The home mortgage crisis that began in 2006 was less a problem of borrowers who lived beyond their means than of mortgage brokers and lenders who made irresponsible and often predatory loans while lax government regulators looked the other way. Yet individual homeowners were left to watch their single largest family asset plummet in value. Black and Latino families were frequently targeted by predatory mortgage lenders for destructive home loans and were more likely to have the bulk of their wealth invested in their homes. As a result, the crisis was particularly severe in communities of color: while the median white family lost 16 percent of their wealth in the housing crash and Great Recession, black families lost 53 percent and Latino families lost 66 percent.[44] Black and Latino households were nearly 50 percent more likely to face foreclosure than their white counterparts. At the height of the foreclosure crisis, policymakers proposed allowing bankruptcy judges to modify home mortgage loans to reduce the principal owed, just as they can do for commercial real estate, vacation homes, and even yachts. The policy was never enacted, and millions of families lost their homes. While subsequent regulations curtailed the worst mortgage lending abuses that led to the financial crisis and foreclosure rates have declined, hundreds of thousands of families of all backgrounds still faced foreclosure proceedings in 2018.

As the cost of college has soared, taking on loans is now the only way for most American students to access higher education. More than 44 million Americans, or nearly 1 in 5 adults, now carry student debt, and student loan debt is growing more quickly than borrower incomes.[45] Yet unlike other debt, policymakers have made student loans almost impossible to discharge in bankruptcy, setting up an "undue hardship" standard that is difficult to meet in even the most hopeless of financial circumstances. As a result, wages and even Social Security checks are garnished to pay student loans. Like most people seeking bankruptcy protection, people with student loan burdens have struggled for years to pay their debts by the time they resort to bankruptcy: over one-third of the $1.5 trillion in student loan debt is currently held by Americans age 40 or older.[46] There are over 500,000 senior citizens with a defaulted

student loan.[47] At the same time, because they have fewer family resources to draw on to pay for college, young black households (ages 25-40) are far more likely to have student debt than their white peers and face more challenges in paying off their debt.[48]

As a result of generations of discrimination that have left black households facing greater financial stress with dramatically fewer resources to fall back on, black Americans are more likely than their white counterparts to exhaust their financial options and resort to filing bankruptcy.[49] Yet the evidence suggests that, particularly in certain jurisdictions in the southern United States, black consumers are disproportionately steered into a type of bankruptcy proceeding that fails to serve them well, often resulting in little or no long-term relief from debt.[50] While evaluating the relative merits of Chapter 7 versus Chapter 13 bankruptcy is beyond the scope of this project, it is vital that policymakers consider how to ensure that the bankruptcy process serves its intended purpose in offering a fresh financial start for all Americans—*especially* communities that have long been targets of predatory financial practices.

Policy Solution

Congress should reform the U.S. Bankruptcy Code to ensure that Americans in severe financial distress are able to get a fresh start.

- **Enable consumers to discharge student loans in bankruptcy.** Strike the student loan exception from the Bankruptcy Code so that student loan debt can be discharged just like any other type of unsecured consumer loan, without the often-impossible to meet standard of "undue hardship." Like other forms of debt, attempts to discharge student loan debt would remain subject to provisions of the Bankruptcy Code designed to prevent abuse of the system.

- **Permit bankruptcy courts to restructure the debt on home mortgages**. For homeowners who cannot afford to make mortgage payments and are in danger of foreclosure, bankruptcy judges should be empowered to set interest rates and principal on home mortgages at commercially reasonable market rates and to extend repayment periods. If a bankruptcy court reduced the mortgage's principal to the current fair market value of the property and the value later rose, the mortgage lender would be entitled to receive the net proceeds from a sale of the property.
- **Consider changing the treatment of attorney's fees in bankruptcy.** Research suggests that one significant contributor to racial disparities in bankruptcy outcomes is the availability of "no money down" filings for chapter 13 bankruptcies but not for chapter 7 bankruptcies.[51] The opportunity to file for chapter 13 bankruptcy without paying a fee upfront may disproportionately turn African American consumers away from chapter 7 bankruptcy even when chapter 7 would better address their financial circumstances. Congress should study proposals to permit people filing for bankruptcy to pay attorneys' fees in installments during chapter 7 bankruptcy cases, as they can already do under chapter 13.
- **Study additional ways to ensure that the bankruptcy process works effectively for people of color and for all Americans.**

How Ensuring Fairness in Bankruptcy Works

- Enabling consumers to discharge student loan debt in bankruptcy would provide relief to the estimated 140,000 Americans with student debt whole file for bankruptcy protection each year.[52] Americans who are not weighed down by student loan debt are more likely to own homes,[53] save for retirement[54] and report a higher sense of well-being[55] than those with student loan debt. Further, relieving workers from the burden of student debt could increase their ability to open and grow small businesses.
- Relieving student loan debt, and the specter of wage or benefit garnishment, will enable struggling households to pay bills, save for the future, and participate more productively in the economy, since student debt has a chilling effect on the ability to build financial assets, especially for African-American and Latino households.
- An analysis of legislation to let bankruptcy judges restructure and write down home mortgage debt estimated that the proposal would have prevented 600,000 families from losing their homes to foreclosure and saved $89 billion in wealth for families who would otherwise see their property values fall as a result of living near a

foreclosed home.[56] Many homeowners would see benefits without filing for bankruptcy, since the availability of modification in bankruptcy would give lenders greater incentives to consider loan workouts before foreclosing. An analysis by Credit Suisse found that the measure would not impact the availability or cost of mortgage loans.[57]

More Resources

- Demos No Recourse: Putting an End to Bankruptcy's Student Loan Exception
- *The Nation* Why a Mortgage Cramdown Bill Is Still the Best Bet to Save the Economy
- ProPublica How the Bankruptcy System Is Failing Black Americans

WRAP-AROUND POLICY: PROHIBIT FORCED ARBITRATION

The Problem

When a bank, payday lender, or loan servicer cheats or deceives its customers, consumers have a right to hold the lawbreaker accountable in a court of law. The American justice system is often the last line of defense against underhanded corporate practices and policies that strip families and entire communities—particularly communities of color—of their wealth. Yet over the last 25 years, corporations advanced a low-profile effort to prevent consumers, workers, and small businesses that are harmed by corporate wrongdoing from attaining justice or even getting into the courthouse door. To block accountability, corporations bury forced arbitration agreements in the fine print of contracts that consumers must sign to conduct transactions such as opening a bank account, taking out a loan or even buying a cell phone plan.[58] People frequently do not realize that just by purchasing a product or service, they are giving up their right to go to court if the company cheats them, and will instead be forced to submit to a private system of justice where there is no judge, jury, or opportunity to appeal an unfair decision.[59] Arbitration rules largely benefit the businesses that are repeat customers of the arbitration firm. In fact, consumers win just 9 percent of disputes with banks and other financial institutions that go to arbitration.[60] In many cases, consumers are forced to pay thousands of dollars to the bank they originally alleged defrauded *them*. A system that prevents workers and consumers from holding companies accountable for discriminatory treatment, negligence, defective products or fraud effectively makes employee and consumer protections unenforceable and gives corporations free rein to drain wealth from communities of color.

Policy Solution

Congress should enact the Forced Arbitration Injustice Repeal (FAIR) Act to prohibit forced arbitration clauses for employment, consumer, antitrust, or civil rights disputes. The bill would not ban all arbitration in these cases, but would provide an opportunity for people to have a meaningful choice about whether or not to pursue arbitration after a dispute has arisen. Pre-dispute mandatory arbitration would be permitted to continue in business-to-business agreements and in collective bargaining agreements.

How Prohibiting Forced Arbitration Works

If forced arbitration were prohibited, consumers would once again have the ability to hold financial services companies accountable in a court of law, including joining together in class action lawsuits against financial institutions. The Economic Policy Institute analyzed the outcomes of arbitration cases against financial institutions compared to consumer class actions, finding that:

- In an average year, 6.8 million consumers receive cash relief in class action lawsuits, compared with just 16 consumers who obtain cash relief in arbitration.[61]
- Consumers recover *at least* $440,000,000 in class actions, in an average year *after* deducting all attorneys' fees and court costs—compared with a *total* of $86,216 in arbitration.[62]
- Arbitration is only slightly faster than a class action lawsuit: Consumers typically wait 150 days for a decision in arbitration, compared with a typical wait of around 215 days for a conclusion in most class actions.
- Permitting class action lawsuits does not increase consumer prices or reduce consumers' access to credit: Consumers saw *no increase* in price after Bank of America, JPMorgan Chase, Capital One, and HSBC dropped their arbitration clauses as a result of court-approved settlements, and mortgage rates *did not increase* after Congress banned forced arbitration in the mortgage market.[63]
- Class action lawsuits can bring systematic change to a financial institution's unfair practices, preventing future abuses, including wealth stripping on a broad scale. Arbitration, which is individual and secret, does not have this potential.

More Resources

- Fair Arbitration Now resource page
- Public Citizen fair arbitration resource page
- Economic Policy Institute forced arbitration resource page

WRAP-AROUND POLICY: DEFEND THE CONSUMER FINANCIAL PROTECTION BUREAU (CFPB)

The Problem

The Consumer Financial Protection Bureau was created in the aftermath of the financial crisis to defend Americans from being cheated and misled by predatory banks, loan servicers, debt collectors and other financial services companies. In its first 6 years of its existence, the agency handled more than 1.2 million consumer complaints and helped more than 29 million people harmed by abusive financial practices to recover nearly $12 billion in relief.[64] Polls have consistently shown strong bipartisan support for the CFPB's mission of regulating financial services and products to make sure they are fair for consumers.[65] The CFPB's work against financial practices that cheat, exclude, or discriminate against people of color is particularly critical for combating the growth of racial wealth inequality. For example, the agency implemented mortgage rules that prevent brokers and lenders from steering African-American and Latino borrowers into deceptive, high-cost loans; developed regulations to tame the abuses of payday lenders that target communities of color and drain their wealth; and enforced laws against discriminatory lending, winning millions of dollars in restitution for borrowers of color who had been defrauded.[66]

Yet financial corporations—which could increase profits significantly if the CFPB didn't stand in their way—have continuously sought to limit and weaken the agency. Under Trump appointee Mick Mulvaney, financial companies have largely prevailed, as Mulvaney reduced supervision of industry and relaxed enforcement in numerous ways. Among other measures, Trump's CFPB has watered down rules that would have curbed predatory payday lenders, weakened oversight of companies that service student loans, undermined financial protections for military service members, and stripped enforcement powers from the office tasked with combating lending discrimination.[67] For the CFPB to fulfill its mandate to ensure a fair financial marketplace for American consumers—including halting the abusive financial practices that strip wealth from communities of color—the agency's independence and authority must be strengthened and defended.

Policy Solution

Congress should enact the Consumers First Act to bolster the CFPB's authority to protect consumers. The bill reestablishes full supervisory and enforcement powers of the CFPB's fair lending office, restores the agency's dedicated student loan office, promotes cooperation between the CFPB and other federal agencies, limits political appointees, mandates adequate staffing to fulfill the CFPB's responsibilities under the law, and requires that the agency's consumer complaint database be kept publicly accessible, among other measures. Congress should act to prevent any further efforts to weaken the CFPB or deflect it from its primarily mission of defending financial consumers.

How the CFPB Works

Americans for Financial Reform compiled the following list of some of the major CFPB enforcement actions that penalized financial companies for stripping wealth from communities of color.[68] The CFPB:

- Obtained a settlement with Ally Financial over discriminatory auto loan pricing. Ally had charged the average African-American car buyer receiving an Ally loan paying more than $300 in extra interest over the course of the loan above the amount paid by white borrowers with similar qualifications. Ally was ordered to pay $80 million in damages to African-American, Hispanic, and Asian and Pacific Islander borrowers in addition to $18 million in penalties.
- Resolved the largest redlining case in history against Hudson City Savings, which will pay nearly $33 million in direct loan subsidies, funding for community programs and outreach, and a civil penalty for structuring its business to avoid (and discourage mortgage access for) residents of majority-Black-and-Hispanic neighborhoods in New York, New Jersey, Connecticut, and Pennsylvania.
- Worked with the Justice Department to force the Mississippi-based BancorpSouth to pay $10.6 million in penalties and borrower relief after an undercover investigation in which the Bureau used black and white "mystery shoppers" with similar credit records to document a pattern of discriminatory lending.

- Joined in a fair-lending lawsuit against National City Bank (an Ohio bank since merged with PNC) that led to payments of over $35 million to tens of thousands of African-American and Hispanic borrowers who had been charged higher prices on their mortgage loans.

More Resources

- Americans for Financial Reform CFPB issue page
- USPIRG Defend the Consumer Bureau page
- Center for American Progress Communities of Color Cannot Afford a Weakened CFPB

BIGGER PICTURE POLICY: IMPROVE JOBS AND PUBLIC SERVICES TO REDUCE THE NEED TO BORROW

If every employer in the United States structured jobs to pay a living wage, offered stable schedules with sufficient work hours, and provided paid sick time and other basic benefits, working Americans would have dramatically reduced need to borrow to keep up with everyday expenses. If the federal government established universal health coverage that kept costs genuinely affordable, medical debt—a burden faced for over half of adults without health insurance (and 20 percent of those who were insured)[69]—would no longer upend the finances of families already coping will illness and injury. If states and the federal government invested in public colleges and universities to lower the cost of higher education, students would be able to earn a degree and embark on their futures without taking on a crushing weight of student loans. If local governments raised revenue through broad-based, progressive taxes, they would no longer rely on fines and fees to fund government operations—and people without the resources to pay local fines and fees would no longer be forced into debt.[70] Policymakers investing in improved and expanded public transit would give millions of people the choice not to take out an auto loan. Guaranteeing affordable child care and paid family leave would free parents who rely on debt to perform the otherwise impossible balancing act of caring for children while also earning enough to support them.

Finally a stronger public safety net, with greater access to and more adequate benefit levels for programs including Supplemental Nutrition Assistance Program (SNAP), unemployment insurance, housing vouchers, home heating assistance, and other critical public support programs would reduce the need for struggling families to depend on an ad-hoc “plastic safety net” of credit. In sum, if policymakers raised job standards and provided the public investments needed to make borrowing less necessary to survive and get ahead, Americans would not need to resort to debt as frequently: having good credit (and the credit reports and scores that quantify it) would be less important in determining people’s life chances.

This report has emphasized the ways that racial wealth inequality—created and reinforced by generations of public policies and private practices—increases the need for families of color to borrow to meet expenses that white families are more likely to have the resources to handle without taking on significant debt. Racially inequitable policies in every in every part of the nation’s credit system, from credit reporting to lending, debt collection, and bankruptcy, compound the historical injustice and deepen inequality. Even in a country with family-sustaining jobs and universal, high-quality public services, Americans would sometimes choose to borrow, and these facets of the credit system would need reform. Yet policies that improve jobs and public services are also critical to addressing racial wealth inequality, especially when benefits are targeted to communities that continue to struggle with discrimination and marginalization.

Demos' federal policy briefing book, *Everyone's Economy* collects a wide range of policy solutions for achieving improved jobs and public services with considerations of racial equity at the forefront. The briefing book is available for free download on our website. Since many of these policies require substantial public investment to achieve greater equity and improve people's lives and our nation's long-term prosperity, Demos also offers a memo with guidance on how to respond when asked, *"How Are You Going to Pay for That?"*

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