Part Two. Consumer Meets Business: Getting Into the Deal

Assignment 4. Solicitations

In a marketplace, consumers sometimes go looking for businesses, searching for the best provider or for a particular product. Other times, businesses seek out consumers. A company may try to make a consumer aware of its superiority to competitors or to establish in consumers' minds that their lives would be better if they had a good or service. Three distinct processes, listed from most general to most specific, are part of getting consumers to make a purchase. Marketing is the umbrella term for the processes that businesses use to identify customers and to deploy strategies about how to connect with consumers and sell goods or services to them. Advertisements are designed to have a broad appeal to potential customers and be displayed in a public forum (billboards, radio ads, etc.). Solicitations are targeted approaches to potential customers. They may occur in a variety of settings, such as door-to-door or by email, and often reflect a certain amount of personalized knowledge about the consumer.

Consumer law contains several limits on solicitations and advertising. There are at least three broad approaches. First, restrictions try to prevent consumers from being subjected to undue pressure from solicitations or simply overwhelmed by the sheer number of solicitations. In this category are innovations like cooling-off periods after in-home sales and the do-not-call list. Second, laws can mandate statements on advertising or product materials, such as certain kinds of labels or the addition of specified language to advertisements. This is a type of forced speech that alters the businesses advertisements or solicitations in response to legal requirements. Third, laws try to curb unfair or deceptive practices in solicitations or advertising, for example, by forbidding statements that mislead consumers or are untrue. The FTC's action against *Airborne*, in Assignment 1, was an example of this issue.

A. In-Home Solicitations

The oldest form of selling is face-to-face. When this occurs outside of a business establishment, consumers may feel constrained from leaving. Sales presentations that involve a day-long tour of condos, complete with bus transportation to the property so that a consumer cannot drive off, is an example. The pressure to buy to escape the sales pitch is a particular problem when a salesperson comes to a consumer's home. Consumers may feel trapped or intimidated in their homes and be willing to make purchases merely to rid themselves of the intruding seller.

The FTC has promulgated a regulation under the Unfair and Deceptive Practices Act that regulates door-to-door sales. The rule extends to all sales in which the seller "personally solicits the sale, including those in response to or following an invitation by the buyer, and the buyer's agreement or offer to purchase is made at a place other than the place of business of the seller." 16 C.F.R. §429.0(a). Of course, there are exceptions. Three merit particular mention: 1) tent sales, provided that the seller has a permanent place of business, and art fairs, 16 C.F.R. §429.3; 2) sales "actually consummated" in a consumer's home, if they follow prior negotiations at the seller's place of business, Statement of Basis and Purpose, 37 Fed. Reg. 22946 (Oct. 26, 1972); and 3) sales for less than $25. 16 C.F.R. §429.0(a). The exceptions reflect situations in which the consumer is more likely to feel free to exercise free will in deciding whether to purchase.

The federal rule is often called the "cooling-off" law. Its primary substantive provision is that door-to-door transactions must contain a provision giving the buyer the right to cancel the transaction for three business days from the date on which the contract was signed. Failure to put the required language in the contract is an unfair and deceptive act or practice under 15 U.S.C. §45. The federal home sales law also requires that the contract be in the language used to conduct the oral sales presentation. 16 C.F.R. §429.1(a), and that the buyer must be informed orally of the right to cancel. 16 C.F.R. §429.1(e). These are difficult to prove in litigation because they essentially come down to the consumer's testimony against the seller's testimony—and if the seller had a good general business lawyer, a written handbook with policies requiring compliance with these regulations.

Every state also has a law regulating door-to-door sales. *See* National Consumer Law Center, Federal Deception Law, §2.5, n. 220 (2012). State laws that are not "directly inconsistent" with the federal rule are not preempted. 16 C.F.R. §429.2(b). While the state and federal rules may seem straightforward enough, compliance seems to be difficult in practice.

Pinnacle Energy, L.L.C. v. Price

2001 Del. C.P. LEXIS 28 (March 21, 2001)

SMALLS, Chief Judge.

Pinnacle Energy, L.L.C. (hereinafter "Pinnacle") brings this action to recover against Catherine Price and Otis Price for breach of contract. Pinnacle claims $3,950 for items refused, $1,000 in liquidated damages, pre- and post-judgment interest of 24%, costs and attorney's fees. This is the Court's decision after trial on February 12, 2001 and written submissions.

Pinnacle is in the business of selling custom fit windows and doors. Pinnacle employs high school and college age students to "canvass" various areas and schedule sales appointments. Once an appointment is scheduled, a Pinnacle salesman makes sales calls to the potential customer. Pinnacle testified it is their normal business practice to telephone twice, first to confirm an appointment the day before, and secondly, to ensure someone is home the day of the appointment.

In these proceedings Carlo Pinto, co-owner and president of Pinnacle, testified an appointment was scheduled through the Prices' grandson. Pinto stated he called to confirm the sales appointment twice before he went to the Prices' house. The Prices, however, testified their first contact with Pinto occurred when he appeared at their house on the morning of April 17, 1999. They concede they were in the market for new windows and doors, and after negotiations agreed to purchase five new windows and three new doors, to be installed by agents of Pinnacle. A contract was signed between the Prices and Pinnacle, which provided for the purchase and installation of the windows and doors.

Pinto testified their manufacturer, Mid South, went to the Prices' house on April 22, 1999, re-measured the windows, and they were ordered May 3, 1999. The installation was scheduled for June 4, 1999. The installation of the windows and doors was not completed due to the refusal of the Prices on the date of delivery. The Prices testified that no one from Mid South came to measure the windows and the next contact they had with Pinnacle was when they appeared to install the windows and doors. The Prices also testified they made numerous attempts to contact Pinto at Pinnacle to inform him of their desire to cancel the agreement. Pinto claims he never received notice of their efforts to cancel the contract until the day of delivery. Further, Pinnacle relies upon a clause at the bottom of the contract in bold print which purports to give the right to cancel required by the statute.

At the close of the Plaintiff's case-in-chief, Defendants moved for a directed verdict. Defendants argue the contract failed to comply with the Home Solicitation and Sales Act (hereinafter "the Act") 6 Del. C. §§4401-4405. After argument, the Court concluded the contract failed to comply with §4404(1) of the "Home Solicitation Sales Act" which provides the language of how a buyer may cancel the contract be "printed in an ink of conspicuous color other than that used for the rest of the contract and/or receipt." Additionally, the Court now concludes plaintiff failed to prove by a preponderance that the "Notice of Cancellation" form required under §4404(2) and (3) was attached to the contract. While Plaintiff produced a blank copy of the form notice to cancel, there was no signed notice and Plaintiff explained this was merely missing from its file. I find this justification has little merit. I also find unpersuasive Pinnacle's argument that it had numerous contacts with the Prices after the initial contract was signed and the date of delivery.

Pinnacle correctly notes the language of the statute does not provide a specific remedy for failure to comply with notice requirements. The Act merely gives the buyer "remedies…at law or in equity." 6 Del. C. §4407. Therefore, following the Court's decision on the statutory violation, testimony was heard on the timeliness of the Defendant's notice and appropriate remedy.…These issues herein have not been addressed in Delaware, but they have been considered by the states of New Jersey and Maryland. The New Jersey case of Swiss v. Williams, 445 A.2d 486, 489-490 (1982) held the consumer has a "continuing right to rescind until such time as the home repair contractor complies with the statutory requirements by providing [the buyer] with receipt complying with the form set forth in the act." The Maryland Court has taken a slightly different view. In *Crystal v. West & Callahan, Inc.*, 614 A.2d 560, 571. it was held where the seller fails to comply

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with the statutory notice, the buyer has a right to cancel for a reasonable amount of time after the contract date.

The Prices argue the Maryland statute is indistinguishable from Delaware's in that, Maryland's statute provides non-compliance is "an unfair or deceptive trade practice," where Delaware makes such non-compliance an unlawful practice. The Prices further argue that even if the court does not adopt the New Jersey view of actual compliance, under these facts they meet the Maryland "reasonableness" analysis. I note that one of the factors which influenced the Maryland decision was the trial court's finding that the defendants had accepted the work and did not complain of the quality. Further, defendants waited one and one-half years to raise the "notice" defense.

In these proceedings, when concluding at trial that Pinnacle did not comply with the act, the court noted the Delaware statute was remedial. In its declaration of purpose it provides in §4401, that: "This chapter shall be interpreted and administered so as to give the greatest effect to the public policy of this State, which declares that it is a basic right of every Delaware citizen to be free of, and protected from, high-pressure door-to-door sales tactics and the resultant inequities to the consumer found in certain ambiguous or misleading contracts, poor quality merchandise and the quick discounting of evidence of indebtedness."

It is clear that the purpose of the statute is to afford the consumer the greatest protection available. Therefore, I find that the analysis found under Swiss case is more consistent with the Delaware statutory language than that of Crystal. However, I need not go as far as the court in *Swiss* because I conclude the Prices gave notice of cancellation within a reasonable period of time.

During their case-in-chief, both Mr. and Mrs. Price testified that they called Pinnacle and Mr. Pinto to cancel the sale. Further, it is undisputed that on the date Pinnacle scheduled for delivery, the Prices refused delivery and cancelled the contract. Pinnacle alleged, but has not produced an acknowledged copy of the notice of right to cancel, as required by the statute. It is clear that one may not accept products under the contract where there are no complaints regarding quality, and later refuses to pay the cost thereof on the basis of the statute. However, that is not the case in these proceedings. Here, there is evidence of the buyers' efforts to cancel prior to delivery. Therefore, based upon the facts herein and the language set forth in the statute, I hereby find the Prices gave notice of cancellation within a reasonable period, and Pinnacle may not collect under the terms of the contract.

Accordingly, I find for the defendants, with the costs to be paid by the respective parties.

Reading the regulation suggests a three-day window. The case reveals that the right to cancel can actually run for many months or even years after the transaction. The key question is whether the consumer can persuade the factfinder that there was no compliance at the time of the deal. The premise of this extended liability is a theme that will recur in consumer law—people cannot exercise rights that they do not know that they have. The case also illustrates that areas of statutory law require more research. It is not enough to find the statute. One must also find the regulations and the case law interpreting the statute and regulations.

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B. Telephone Solicitations

Telemarketing is a routine strategy to solicit customers in certain industries. The calls are often placed from a call center, which is less charitably described as a "boiler room," a rented space with hundreds of operators calling continuously. "Robo-calling" eliminates the human operator from the process, replacing her with computer-generated dialing or even a prerecorded message that is broadcast to consumers or their answering machines. Telemarketing often involves more than one call or efforts to extend the length of the call, both of which presumably motivate customers to make purchases. While many consumers find the calls are a nuisance and never or rarely purchase, telemarketing continues to be widely used. The reason is that the technology of calling has driven down the costs of solicitation so low that even a small response rate can generate profits. (This is same reason that a decade later, spam emails asking for money wires to Nigeria continue to arrive in your inbox.)

Telemarketing is legal within two boundaries. The first limit, discussed here, is that telemarketers cannot engage in fraud or deceptive practices. The second limit, discussed in the next section, is that there are restrictions on when and how often consumers may be contacted.

1. Telemarketing Fraud

The primary laws regulating telemarketing fraud are the Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. §6101 et seq., and the FTC's Telemarketing Sales Rule, 16 C.F.R. §310.4.

The FTC defines telemarketing as "a plan, program, or campaign which is conducted to induce purchases of goods or services, or a charitable contribution, donation, or gift of money or any other thing of value, by use of one or more telephones and which involves more than one interstate telephone call. The term does not include the solicitation of sales through the mailing of a catalog [under certain limitations, including only receiving calls initiated by customers in response to the catalog]." 16 C.F.R. §310.2(dd). Seller-initiated calls are the main focus. For some industries, consumer-initiated calls are covered, such as calls in response to advertisements or mailings for services such as credit repair or prize promotions. 16 C.F.R. §310.6(b)(5). Calls for these and some other services are subject to additional consumer protection restrictions, many of which are motivated by concern that telemarketers do not deliver the promised services.

The Telemarketing Sales Rule requires disclosures for any covered calls. Most fundamentally, the telemarketer must reveal that the purpose of the call is to sell goods or services and the nature of the goods or services. 16 C.F.R. §310.4(d)(2). Telemarketers must also reveal the total costs, any restrictions or conditions on purchase, and all material terms and conditions of a refund policy, including, if applicable, the lack of any right to a refund. In complying with these disclosure requirements, telemarketers cannot make deceptive statements, for example by misrepresenting the goods or services being sold.

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The following case provides an example of the kinds of behavior that violate the Telemarketing Sales Rule.

Federal Trade Commission v. Bay Area Business Council Inc.

423 F.3d 627 (7th Cir. 2005)

ROVNER, Circuit Judge

In 2002 the Federal Trade Commission ("FTC") initiated an action for injunctive and other equitable relief against several Florida corporations and their officers and directors. The FTC alleged that the following interrelated corporations, run by Peter Porcelli, Bonnie Harris, and Christopher Tomasulo, engaged in deceptive trade practices in violation of section 5(a) of the Federal Trade Commission Act ("FTC Act"), 15 U.S.C. §45(a), and the Telemarketing Sales Rule ("TSR"), 16 C.F.R. §310.1-10.9. Bay Area Business Council, Inc. ("BABC"); Bay Area Business Council Customer Service Corp. ("BABC Customer Service"); American Leisure Card Corp. ("American Leisure"); Bay Memberships, Inc.; Bay Vacations, Inc.; and Sr. Marketing Consultants, Inc. In particular, the FTC alleged that the defendants misled consumers into believing that they would receive a credit card in exchange for a hefty "one-time" fee. The district court granted the FTC's motion for summary judgment against all of the corporate defendants and Porcelli and Harris. The defendants appeal, and we affirm.

I.

The FTC based its action on an alleged telemarketing scheme run primarily out of Largo, Florida. Managing BABC and later American Leisure, Porcelli contracted with a telemarketing company in Utah to call consumers throughout the United States who had recently applied for and been denied consumer credit. Referring to those credit applications, telemarketers opened by saying, "Our records indicate that within the past 12 months, you filed an application for a credit card and you are now eligible to receive your MasterCard." After answering a few short "verification" questions, consumers were told that they were "guaranteed to receive a MasterCard that does not require a security deposit with an initial pay as you go limit of $2,000."

In addition to the "MasterCard," consumers were promised a "fabulous" Florida vacation and a free 30-day trial "BABC membership." These offers, however, did not figure prominently in the script, which focused on the "MasterCard." The card was offered as a way to boost flagging credit ratings, as demonstrated by the following scripted promise: "[N]othing [customer name] looks better on your Equifax credit report than a MasterCard."

This supposed opportunity, however, came at a cost. Telemarketers explained that "like most cards there is a one time processing [fee] of $174.95 plus shipping and handling, which covers the cost of processing the MasterCard order and

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getting the vacation package delivered to you on a priority basis." In order to pay the fee, consumers were required to provide personal account information. After obtaining an account number and securing agreement from the consumer, telemarketers played an automated "disclosure" concluding with, "you agree to everything we spoke about over the phone today, Correct?" Within days of the call, BABC and American Leisure debited customer accounts for anywhere from $199 (including "shipping and handling") to $499.

Some time later, customers received the "MasterCard" and accompanying package from BABC or American Leisure. Instead of a credit card, the package contained an "acceptance form" for a "ChexCard TM MasterCard®." The card stated "Bay Area Business Council" prominently across the top and contained a copy of the MasterCard logo in the lower right-hand corner. The back contained a meaningless painted-on black stripe in place of the customary magnetic strip on credit and debit cards. The explanatory material revealed that the card was a "stored value card" that the customer could receive only after mailing in a $15 activation fee. After the actual card arrived (four to six weeks later), it could only be used if a customer pre-loaded his or her own funds onto it.

In addition to the inoperable "ChexCard," customers received information on redeeming their free vacation (a time share presentation) and on their BABC "membership." The "membership" supposedly entitled consumers to take advantage of numerous "free" goods and services, such as gasoline, nationwide long distance, internet access, voice mail, and film developing. Although this was not mentioned in the materials, the privilege of BABC membership cost the consumer $10 a month. The only notice of the fee was contained in the automated "disclosure" played in the initial sales call, where it was revealed that the $10 would be taken directly from the consumer's account each month.

Not surprisingly, BABC received a host of complaints from customers who thought they had been going to receive a credit card. Incorporated separately but doing business under the name Bay Area Business Council, BABC Customer Service handled customer's complaints and requests for refunds. Special Technologies, Inc. essentially succeeded BABC Customer Service in July 2002. Both operated from a suite in Largo next to the offices of Porcelli and Harris. That suite received all calls placed to the toll free numbers for BABC, American Leisure, Sr. Marketing Consultants, and Bay Memberships, Inc. In addition to calls from disgruntled consumers, corporate records reveal that between November 2001 and July 2002, BABC received over 900 written consumer complaints forwarded from the Better Business Bureau, state attorney generals' offices, and private lawyers.

The remaining corporate defendants also worked in conjunction with BABC. Like BABC Customer Service, Sr. Marketing Consultants, Inc. did business under BABC's name. Sr. Marketing Consultants, however, had only four employees, three of whom were related to Porcelli. They operated from Porcelli's mother-in-law's home in Dunedin, Florida. Sr. Marketing Consultants charged BABC and American Leisure for the "ChexCards," and then, through a series of transactions, gave the proceeds to Harris, who handled most of BABC's finances. At the end of July 2002, Porcelli created Bay Memberships, Inc. as a way to ensure that banks, which had begun refusing to process payments to BABC and American Leisure, would continue to charge customers. In the three weeks that Bay Memberships, Inc. operated, it processed approximately $200,000 in debits from customer accounts. Although

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it is not entirely clear from the record, Bay Vacations, Inc. was apparently another shell corporation doing business for BABC....

On that record, the court granted the FTC's motion for summary judgment. The court concluded that the undisputed facts established that the defendants had violated section 5 of the FTC Act by misleading reasonable consumers into believing they would receive a credit card. See 15 U.S.C. §45(a) (forbidding deceptive practices affecting commerce). This deception, the court concluded, also violated 16 C.F.R. §310.3(a)(2)(iii) (prohibiting misrepresentations about any material aspect of a sales offer) and §310.3(a)(4) (forbidding misleading statements to induce payment for goods). And the court determined that the defendants violated 16 C.F.R. §310.3(a)(1)(i) by failing to tell consumers about the extra $15 fee required to obtain the "ChexCard," id. (requiring clear and conspicuous disclosure of all costs associated with goods offered for sale). Finally, the district court concluded that Porcelli and Harris were individually liable for the corporate defendants' deceptive practices because both had authority to control the corporate defendants and knew about their deceptive practices. The court then entered an order permanently enjoining the defendants from telemarketing, promoting or selling credit-related products, making misleading statements to consumers, failing to comply with the TSR, or disclosing any information about customers except to the FTC. The court also held the corporate defendants, Harris, and Porcelli jointly and severally liable for $12.5 million in consumer redress. See 15 U.S.C. §57b(b) (giving court jurisdiction to authorize consumer redress for a corporation's deceptive trade practices).

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Accordingly, in our de novo review of the court's grant of summary judgment, we consider only those facts in the FTC's Rule 56.1 statement, which is amply supported by citations to the relevant record evidence. Although we accept as true the facts in the FTC's Rule 56.1 statement, we still view them in the light most favorable to the defendants in determining whether there exist disputed issues of material fact. See Fed.R.Civ.P. 56(c); Anderson v. Liberty Lobby Inc., 477 U.S. 242, 255 (1986); Laborers' Pension Fund v. RES Env't Servs. Inc., 377 F.3d 735, 737 (7th Cir. 2004). Although the defendants aver generally that there are disputed issues of fact that make summary judgment improper, nothing they point to undercuts the FTC's undisputed evidence that they engaged in unfair trade practices, see 15 U.S.C. §45(a), and violated multiple provisions of the TSR, see 16 C.F.R. §310.1-10.9.

Section 5 of the FTC Act prohibits "unfair or deceptive acts or practices in or affecting commerce." 15 U.S.C. §45(a)(1). The FTC is empowered to initiate federal court actions to enforce violations of section 5 and seek appropriate equitable relief. Id. §§53(a)-(b), 57b. The FTC may establish corporate liability under section 5 with evidence that a corporation made material representations likely to mislead a reasonable consumer. See FTC v. Tashman, 318 F.3d 1273, 1277 (11th Cir. 2003); FTC v. World Travel Vacation Brokers, Inc., 861 F.2d 1020, 1029 (7th Cir. 1988). The FTC is not, however, required to prove intent to deceive. FTC v. Freecom Communications, Inc., 401 F.3d 1192, 1202 (10th Cir. 2005); FTC v. Amy Travel Serv., Inc., 875 F.2d 564, 573 (7th Cir. 1989); World Travel, 861 F.2d at 1029. Additionally, the omission of a material fact, without an affirmative misrepresentation, may give rise to an FTC Act violation. Amy Travel, 875 F.2d at 573; World Travel, 861 F.2d at 1029. The corporate defendants do not dispute the district court's conclusion that they operated as a "common enterprise" such that they are jointly and

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severally liable for the injuries caused by their violations of the FTC Act and the TSR. We thus consider them collectively when analyzing corporate liability.

Throughout their brief, the defendants maintain that they never sold a credit card. They characterize this issue as a material fact in dispute. The FTC, however, does not dispute that the defendants did not actually sell credit cards. Indeed, their failure to provide a "credit card" lies at the heart of this case. We take the defendants at their word that they never sold a credit card. Unfortunately, they misled consumers into believing that was exactly what they were doing. See Freecom Communications, 401 F.3d at 1202 (in analyzing whether act or practice is deceptive, principal inquiry is the practice's likely effect on mind of ordinary consumer).

One look at the scripts used by telemarketers for BABC and American Leisure confirms that the corporate defendants misled reasonable consumers into believing they would receive a credit card. The script opens by referring to the consumer's recent application for "a credit card." The potential customer is then told, "you are now eligible to receive your MasterCard." It is hard to imagine what consumer would not construe this as an offer for a credit card. Indeed, the entire script is tailored to giving consumers that impression. From calling the card a "MasterCard" to promising that nothing would look better on an Equifax credit report, telemarketers gave consumers the impression that they were going to receive a credit card in the mail. Instead, they received a useless card with a MasterCard logo. From that, a consumer could mail additional funds to receive a functional "ChexCard," which could only be used when the consumer pre-loaded it with her or her own funds. We think it safe to say that no reasonable consumer would pay close to $200 for the opportunity to order this "ChexCard." Any doubt that consumers were misled is dispelled by the number of consumer complaints. BABC Customer Service records reveal that in the two-month window from June to August 2002, over 200 consumers called to complain that they thought they would be getting a credit card. Accordingly, the corporate defendants violated section 5 of the FTC Act. See FTC v. World Media Brokers, 415 F.3d 758 (7th Cir. 2005).

The evidence also establishes multiple violations of the TSR, 16 C.F.R. §310.1-10.9, the FTC's Trade Regulation promulgated to implement the Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. §6101-6108. The FTC alleged that the defendants violated three provisions of the TSR, which we consider in turn.

Section 310.3(a)(1)(i) requires telemarketers to clearly and conspicuously disclose "[t]he total costs to purchase, receive, or use…any goods and services" offered for sale. 16 C.F.R. §310.3(a)(1)(i). Although telemarketers assured consumers that the "MasterCard" had a "one time" fee of $174.95 plus shipping and handling, that was not the case. After a consumer's checking account was debited anywhere from $199 up to $399, he or she received the BABC "membership" materials in the mail. Those materials contained the useless "ChexCard TM MasterCard®" with an accompanying form explaining that it was not a credit card. In order to use the "stored value card" consumers then had to mail an additional, previously undisclosed $15 in certified funds to "SMC Bank Card Offer" (presumably Sr. Marketing Consultants, the four-employee operation run from Porcelli's mother-in-law's home). By failing to provide advance warning of the additional $15 fee, the corporate defendants violated §310.3(a)(1)(i).

Likewise, the defendants violated §310.3(a)(2)(iii), which prohibits telemarketers from misrepresenting any material aspect of the performance of the goods

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or services offered for sale. As our discussion regarding section 5 of the FTC Act makes clear, the corporate defendants misled consumers into believing that they would receive a credit card. We need not linger on the obvious point that the lack of any available credit on the "MasterCard" qualifies as a material aspect of its performance subject to disclosure. Cf. World Media, 415 F.3d 758 (defendants' failure to disclose illegality of sales offer violated related provision of TSR requiring disclosure of all material restrictions on goods or services).

Finally, the defendants violated §310.3(a)(4) by leading consumers to believe that the substantial fee charged would be used to secure a credit card on their behalf. Subsection (a)(4) forbids telemarketers from making a false or misleading statement to induce payment for goods or services. 16 C.F.R. §310.3(a)(4); see also World Media, 415 F.3d 758. In addition to suggesting that consumers would receive a credit card, the telemarketers falsely assured consumers that the card would boost their credit ratings. Despite the promise that "nothing" looked better on an "Equifax credit report than a MasterCard," use of the pay-as-you go "Mastercard" was not reported to credit reporting bureaus like Equifax. No doubt this false promise induced consumers, targeted for their poor credit histories, into paying for the supposed "MasterCard."

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For the foregoing reasons, we affirm the district court's grant of summary judgment in favor of the FTC.

In the case, the FTC relied on its authority to stop practices that involve deception in commerce as well as violations of specific rules. The Telemarketing and Consumer Fraud Abuse Prevention Act does not have separate remedy provisions for the FTC, which is instead directed to sue under the general FTC Act. The Telemarketing statute does, however, empower state Attorneys General to enforce the federal law, 15 U.S.C. §6103, and when the amount in controversy is greater than $50,000, even permits a private person to sue. 15 U.S.C. §6102. This overlapping enforcement scheme illustrates the point of Assignment 3; there are a lot of cooks in the consumer protection kitchen, which can lead to conflict or to inaction, as one regulator defers enforcement in the belief that another entity is the better party to act.

In addition to federal telemarketing regulations, telemarketers must also adhere to separate state regulations. Many states require telemarketers to register with a state regulator and have separate rules covering things like whether calls may be recorded, whether the telemarketer must obtain a consumer's consent to continue with a call, and whether a written contract is required to be sent to make the sale effective.

2. Do-not-call List

The Telephone Consumer Protection Act of 1991 (TCPA), 47 U.S.C. §227, places limits on telemarketing activity, including limits on robo-calling and unsolicited faxes. This law also contains limits on telemarketing that are designed to regulate solicitations, with some duplication with the Telemarketing and Consumer Fraud and Abuse Prevention Act. One important difference is that the TCPA is enforced by the Federal Communications Commission (FCC), rather than the FTC.

The focus of the TCPA is somewhat more on the use of the technology than the FTC's rule. For example, its regulations address both faxes and telephone calls. 47 C.F.R. §64.1200. While the law was passed in 1991, in part to address fax spam, it has evolved with technology. The regulation prohibits uninitiated calling of pagers and cellular telephones, and treats text messages as calls for purposes of regulation. 47 C.F.R. §64.1200(a)(1)(iii). This is a protection for everyone, reflecting one approach to the scope of consumer law. The TCPA also gives extra protection to vulnerable consumers. It bans calls to landlines of consumers who reside in "any guest room or patient room of a hospital, health care facility, elderly home, or similar establishment." 47 C.F.R. §64.1200(a)(1)(ii).

The centerpiece of such efforts is the National Do-Not-Call Registry. In 2003, the FTC and the FCC established a national do-not-call rule. The registry met with immediate challenges, first to the FTC's authority, which was immediately resolved by Congress. *See* An Act to Ratify the Authority of the Federal Trade Commission to Establish a Do-Not-Call Registry, Pub. L. No. 108-82, 117 Stat. 1006 (2003). Then came the constitutional attack.

Mainstream Marketing Services, Inc. v. Federal Trade Commission

358 F.3d 1228 (10th Cir. 2004)

EBEL, Circuit Judge.

I. BACKGROUND

In 2003, two federal agencies the Federal Trade Commission (FTC) and the Federal Communications Commission (FCC) promulgated rules that together created the national do-not-call registry. *See* 16 C.F.R. §310.4(b)(1)(iii)(B) (FTC rule); 47 C.F.R. §64.1200(c)(2) (FCC rule). The national do-not-call registry is a list containing the personal telephone numbers of telephone subscribers who have voluntarily indicated that they do not wish to receive unsolicited calls from commercial telemarketers. Commercial telemarketers are generally prohibited from calling phone numbers that have been placed on the do-not-call registry, and they must pay an annual fee to access the numbers on the registry so that they can delete those numbers from their telephone solicitation lists. So far, consumers have registered more than 50 million phone numbers on the national do-not-call registry.

The national do-not-call registry's restrictions apply only to telemarketing calls made by or on behalf of sellers of goods or services, and not to charitable or political fundraising calls. 16 C.F.R. §§310.4(b)(1)(iii)(B), 310.6(a); 47 C.F.R. 64.1200(c)(2), 64.1200(f)(9). Additionally, a seller may call consumers who have signed up for the national registry if it has an established business relationship with the consumer or if the consumer has given that seller express written permission to call. 16 C.F.R. §310.4(b)(1)(iii)(B)(i-ii); 47 C.F.R. §64.1200(f)(9)(i-ii). Telemarketers generally have three months from the date on which a consumer signs up for the registry to remove the consumer's phone number from their call lists. 16 C.F.R. §310.4(b)(3)(iv); 47 C.F.R. §64.1200(c)(2)(i)(D).

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III. FIRST AMENDMENT ANALYSIS

The national do-not-call registry's telemarketing restrictions apply only to commercial speech. Like most commercial speech regulations, the do-not-call rules draw a line between commercial and non-commercial speech on the basis of content. See Metromedia, Inc. v. City of San Diego, 453 U.S. 490, 504 n.11 (1981) ("If commercial speech is to be distinguished, it must be distinguished by its content."); Bates v. State Bar of Ariz., 433 U.S. 350, 363 (1977) (same). In reviewing commercial speech regulations, we apply the *Central Hudson* test. Central Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of N.Y., 447 U.S. 557, 566 (1980). *Central Hudson* established a three-part test governing First Amendment challenges to regulations restricting non-misleading commercial speech that relates to lawful activity. First, the government must assert a substantial interest to be achieved by the regulation. Central Hudson, 447 U.S. at 564. Second, the regulation must directly advance that governmental interest, meaning that it must do more than provide "only ineffective or remote support for the government's purpose." Id. Third, although the regulation need not be the least restrictive measure available, it must be narrowly tailored not to restrict more speech than necessary. See id.; Board of Trs. of the State Univ. of N.Y. v. Fox, 492 U.S. 469, 480 (1989). Together, these final two factors require that there be a reasonable fit between the government's objectives and the means it chooses to accomplish those ends.

The government bears the burden of asserting one or more substantial governmental interests and demonstrating a reasonable fit between those interests and the challenged regulation. The government is not limited in the evidence it may use to meet its burden. For example, a commercial speech regulation may be justified by anecdotes, history, consensus, or simple common sense. Yet we may not take it upon ourselves to supplant the interests put forward by the state with our own ideas of what goals the challenged laws might serve.

A. Governmental Interests

The government asserts that the do-not-call regulations are justified by its interests in 1) protecting the privacy of individuals in their homes, and 2) protecting consumers against the risk of fraudulent and abusive solicitation. See 68 Fed. Reg. 44144; 68 Fed. Reg. at 4635. Both of these justifications are undisputedly substantial governmental interests.

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In *Rowan v. United States Post Office Dep't*, the Supreme Court upheld the right of a homeowner to restrict material that could be mailed to his or her house. 397 U.S. 728 (1970). The Court emphasized the importance of individual privacy, particularly in the context of the home, stating that "the ancient concept that 'a man's home is his castle' into which 'not even the king may enter' has lost none of its vitality." Id. at 737. In *Frisby v. Schultz*, the Court again stressed the unique nature of the home and recognized that "the State's interest in protecting the well-being, tranquility, and privacy of the home is certainly of the highest order in a free and civilized society." 487 U.S. 474, 484 (1988) (quoting Carey v. Brown, 447 U.S. 455, 471 (1980)). As the Court held in *Frisby*:

> One important aspect of residential privacy is protection of the unwilling listener....[A] special benefit of the privacy all citizens enjoy within their own walls, which the State may legislate to protect, is an ability to avoid intrusions. Thus, we have repeatedly held that individuals are not required to welcome unwanted speech into their own homes and that the government may protect this freedom.

Id. at 484-85 (citations omitted). Likewise, in *Hill v. Colorado*, the Court called the unwilling listener's interest in avoiding unwanted communication part of the broader right to be let alone that Justice Brandeis described as "the right most valued by civilized men." 530 U.S. 703, 716-17 (2000) (quoting Olmstead v. United States, 277 U.S. 438, 478 (1928) (Brandeis, J., dissenting)). The Court added that the right to avoid unwanted speech has special force in the context of the home. Id....

In other words, the national do-not-call registry is valid if it is designed to provide effective support for the government's purposes and if the government did not suppress an excessive amount of speech when substantially narrower restrictions would have worked just as well. See Central Hudson, 447 U.S. at 564-65. These criteria are plainly established in this case. The do-not-call registry directly advances the government's interests by effectively blocking a significant number of the calls that cause the problems the government sought to redress. It is narrowly tailored because its opt-in character ensures that it does not inhibit any speech directed at the home of a willing listener.

1. Effectiveness

The telemarketers assert that the do-not-call registry is unconstitutionally underinclusive because it does not apply to charitable and political callers. First Amendment challenges based on underinclusiveness face an uphill battle in the commercial speech context. As a general rule, the First Amendment does not require that the government regulate all aspects of a problem before it can make progress on any front. United States v. Edge Broad. Co., 509 U.S. 418, 434 (1993). "Within the bounds of the general protection provided by the Constitution to commercial speech, we allow room for legislative judgments." Id. The underinclusiveness of a commercial speech regulation is relevant only if it renders the regulatory framework so irrational that it fails materially to advance the aims that it was purportedly designed to further. See Rubin v. Coors Brewing Co., 514 U.S. 476, 489 (1995).

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In *Rubin*, for example, the Supreme Court struck down a law prohibiting brewers from putting the alcohol content of their product on beer labels, purportedly in an effort to discourage "strength wars." 514 U.S. at 478. However, the law allowed advertisements disclosing the alcohol content of beers, allowed sellers of wines and spirits to disclose alcohol content on labels (and even required such disclosure for certain wines), and allowed brewers to signal high alcohol content by using the term "malt liquor." Id. at 488-89. Under these circumstances, the Court concluded that there was little chance that the beer label rule would materially deter strength wars in light of the "irrationality of this unique and puzzling regulatory framework." Id. at 489....

As discussed above, the national do-not-call registry is designed to reduce intrusions into personal privacy and the risk of telemarketing fraud and abuse that accompany unwanted telephone solicitation. The registry directly advances those goals. So far, more than 50 million telephone numbers have been registered on the do-not-call list, and the do-not-call regulations protect these households from receiving most unwanted telemarketing calls. According to the telemarketers' own estimate, 2.64 telemarketing calls per week or more than 137 calls annually were directed at an average consumer before the do-not-call list came into effect. Cf. 68 Fed. Reg. at 44152 (discussing the five-fold increase in the total number of telemarketing calls between 1991 and 2003). Accordingly, absent the do-not-call registry, telemarketers would call those consumers who have already signed up for the registry an estimated total of 6.85 billion times each year.

To be sure, the do-not-call list will not block all of these calls. Nevertheless, it will prohibit a substantial number of them, making it difficult to fathom how the registry could be called an "ineffective" means of stopping invasive or abusive calls, or a regulation that "furnish[es] only speculative or marginal support" for the government's interests. See also id. (noting the effectiveness of state do-not-call lists in reducing unwanted telemarketing calls)....

The telemarketers asserted before the FTC that they might have to lay off up to 50 percent of their employees if the national do-not-call registry came into effect. See 68 Fed. Reg. at 4631. It is reasonable to conclude that the telemarketers' planned reduction in force corresponds to a decrease in the amount of calls they will make. Significantly, the percentage of unwanted calls that will be prohibited will be even higher than the percentage of all unsolicited calls blocked by the list. The individuals on the do-not-call list have declared that they do not wish to receive unsolicited commercial telemarketing calls, whereas those who do want to continue receiving such calls will not register. Cf. 68 Fed. Reg. at 4632 (under the national do-not-call regulations, "telemarketers would reduce time spent calling consumers who do not want to receive telemarketing calls and would be able to focus their calls only on those who do not object").

Finally, the type of unsolicited calls that the do-not-call list does prohibit, commercial sales calls, is the type that Congress, the FTC and the FCC have all determined to be most to blame for the problems the government is seeking to redress. According to the legislative history accompanying the TCPA, "[c]omplaint statistics show that unwanted commercial calls are a far bigger problem than unsolicited calls from political or charitable organizations." H.R. Rep. No. 102-317, at 16 (1991) (noting that non-commercial calls were less intrusive to consumers' privacy because they are more expected and because there is a lower volume of such calls);

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see also 68 Fed. Reg. at 44153. Similarly, the FCC determined that calls from solicitors with an established business relationship with the recipient are less problematic than other commercial calls. 68 Fed. Reg. at 44154 ("Consumers are more likely to anticipate contacts from companies with whom they have an existing relationship and the volume of such calls will most likely be lower.")....

In sum, the do-not-call list directly advances the government's interests, reducing intrusions upon consumer privacy and the risk of fraud or abuse by restricting a substantial number (and also a substantial percentage) of the calls that cause these problems. Unlike the regulations struck down in Rubin and Discovery Network, the do-not-call list is not so underinclusive that it fails materially to advance the government's goals.

2. Narrow Tailoring

Although the least restrictive means test is not the test to be used in the commercial speech context, commercial speech regulations do at least have to be "narrowly tailored" and provide a "reasonable fit" between the problem and the solution. Whether or not there are "numerous and obvious less-burdensome alternatives" is a relevant consideration in our narrow tailoring analysis. Went For It, 515 U.S. at 632. A law is narrowly tailored if it "promotes a substantial government interest that would be achieved less effectively absent the regulation." Ward v. Rock Against Racism, 491 U.S. 781, 799 (1989). Accordingly, we consider whether there are numerous and obvious alternatives that would restrict less speech and would serve the government's interest as effectively as the challenged law. See Central Hudson, 447 U.S. at 565; Edge Broad., 509 U.S. at 430.

We hold that the national do-not-call registry is narrowly tailored because it does not over-regulate protected speech; rather, it restricts only calls that are targeted at unwilling recipients. Cf. Frisby v. Schultz, 487 U.S. 474, 485 (1988) ("There simply is no right to force speech into the home of an unwilling listener."); Rowan v. United States Post Office Dep't, 397 U.S. 728, 738 (1970) ("We therefore categorically reject the argument that a vendor has a right under the Constitution or otherwise to send unwanted material into the home of another."). The do-not-call registry prohibits only telemarketing calls aimed at consumers who have affirmatively indicated that they do not want to receive such calls and for whom such calls would constitute an invasion of privacy. See Hill v. Colorado, 530 U.S. 703, 716-17 (2000) (the right of privacy includes an unwilling listener's interest in avoiding unwanted communication)....

Like the do-not-mail regulation approved in *Rowan*, the national do-not-call registry does not itself prohibit any speech. Instead, it merely "permits a citizen to erect a wall…that no advertiser may penetrate without his acquiescence." See Rowan, 397 U.S. at 738. Almost by definition, the do-not-call regulations only block calls that would constitute unwanted intrusions into the privacy of consumers who have signed up for the list. Moreover, it allows consumers who feel susceptible to telephone fraud or abuse to ensure that most commercial callers will not have an opportunity to victimize them. Under the circumstances we address in this case, we conclude that the do-not-call registry's opt-in feature renders it a narrowly tailored commercial speech regulation.

The do-not-call registry's narrow tailoring is further demonstrated by the fact that it presents both sellers and consumers with a number of options to make

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and receive sales offers. From the seller's perspective, the do-not-call registry restricts only one avenue by which solicitors can communicate with consumers who have registered for the list. In particular, the do-not-call regulations do not prevent businesses from corresponding with potential customers by mail or by means of advertising through other media.

From the consumer's perspective, the do-not-call rules provide a number of different options allowing consumers to dictate what telemarketing calls they wish to receive and what calls they wish to avoid. Consumers who would like to receive some commercial sales calls but not others can sign up for the national do-not-call registry but give written permission to call to those businesses from whom they wish to receive offers. See 16 C.F.R. 310.4(b)(1)(iii)(B)(i); 47 C.F.R. 64.1200(f)(9)(i). Alternatively, they may decline to sign up on the national registry but make company-specific do-not-call requests with those particular businesses from whom they do not wish to receive calls. See 16 C.F.R. 310.4(b)(1)(iii)(A); 47 C.F.R. 64.1200(d)(3). Therefore, under the current regulations, consumers choose between two default rules either that telemarketers may call or that they may not. Then, consumers may make company-specific modifications to either of these default rules as they see fit, either granting particular sellers permission to call or blocking calls from certain sellers.

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For the reasons discussed above, the government has asserted substantial interests to be served by the do-not-call registry (privacy and consumer protection), the do-not-call registry will directly advance those interests by banning a substantial amount of unwanted telemarketing calls, and the regulation is narrowly tailored because its opt-in feature ensures that it does not restrict any speech directed at a willing listener. In other words, the do-not-call registry bears a reasonable fit with the purposes the government sought to advance. Therefore, it is consistent with the limits the First Amendment imposes on laws restricting commercial speech.

The national do-not-call registry does not apply to telemarketers who solicit charitable donations. 16 C.F.R. §310.6(a). Like commercial telemarketers, however, non-profit callers must maintain a do-not-call list for their organization. The Telemarketing Sales Rule prohibits consumers who have previously asked to be on such a list from being contacted again. The constitutionality of this rule was challenged by non-profit organizations and held to be constitutional. *See Natl'l Federation of the Blind v. Fed. Trade Comm'n*, 420 F.3d 331, 341-42 (4th Cir. 2005).

Although the initial regulations would have required consumers to recommit their number to the registry every five years, the FTC changed this policy near the expiration of the first five-year period and numbers put on the list do not expire. FCC regulations also prohibit telemarketers from using automated dialers to call cell phone numbers. As more people only have mobile phones, it may be getting harder for telemarketers to distinguish cell and landline numbers, making a quick trip to www.ftc.gov/donotcall for cell phones probably worthwhile. (The registry does accept cell phone numbers and has since its inception.)

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A related issue with mobile phones is that people take their phones with them. This is true both for short trips and for longer relocations, such as for years after a cross-country move. Telemarketers must call between 8:00 a.m. and 9:00 p.m. per federal law, 16 C.F.R. §310.4(c), and some state laws impose even shorter hours for operation. With mobile numbers, the telemarketer does not know the consumer's time zone. Query if it would be permissible for a company to use the area code to make an assumption about the consumer's time zone, even in light of the company having an address for the consumer putting them in a different time zone.

Even for those who wish to receive calls and have not put themselves on the registry, consumers find some forms of contact particularly annoying. The laws often regulate such types of contact. For example, federal laws try to limit the incidence of abandoned calls, which occur when a consumer rushes to answer the phone only to find nobody on the line. The FTC Telemarketing Sales Rule requires that each call ring for at least fifteen seconds or four complete rings before disconnecting and places a limit of 3 percent on the permissible incidence of abandoned calls. 16 C.F.R. §310.4(b)(v)(B)(i). The FTC regulations ban robo-calls, which are prerecorded telemarketing calls, unless the telemarketers have obtained "prior express written consent" from the consumer that they wish to receive such calls. 16 C.F.R. §310.4(b)(1)(v). Purely informational calls, such as flight cancellations, school notices, and appointment reminders, are not covered by the ban.

C. Email Solicitations

Federal law attempts to prevent unsolicited emails (a.k.a. “spam”). The title of the law gives you some sense of Congress’ view on commercial email solicitations. *See* Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 (CAN-SPAM), 15 U.S.C. §7701 et seq. The CAN-SPAM Act states that unsolicited commercial email makes up over half of all electronic email traffic, §7701(a)(2). Consensus seems to be that spam continues to grow, and that any perceptions that it is dwindling come from improved filtering and management techniques rather than from diminished sender activity.

The CAN-SPAM Act contains limitations on the content of messages and on the procurement of addresses. At the most basic level, the message must specify that it is a solicitation, and the message headers and subject headings must not be deceptive. 15 U.S.C. §7704(a)(1), (2) and (4). Such messages must inform consumers that they have the right not to receive further messages and must facilitate consumers’ opting out from those messages. To do so, senders must provide a valid physical postal address (presumably so the consumer has another way to contact the company besides relying on email) and a link or return email address that operates for thirty days from the date of transmission that can be used to opt out. 15 U.S.C. §7704(a)(4) and (6). Email addresses should generally be obtained the old-fashioned way, by purchase of such lists, rather than through automated procedures that take best guesses at valid addresses using dictionaries and lists of names.

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Liability under the CAN-SPAM Act is not limited to those who physically cause spam to be transmitted, such as the actual sender, but also extends to those who “procure the origination” of spam, which could include a company that hires a spammer to act on its behalf. 15 U.S.C. §7702(9). The effect seems to have been to deter large and legitimate companies, including exclusively online sellers, from sending unsolicited commercial email; companies who are hard to track down, have few resources and need not fear being sued, or are fly-by-night operations seem to still heavily use spam. Of course, these are the companies that consumers may least want to hear from, leading some to question whether the CAN-SPAM Act is deterring desirable messages without eliminating undesirable ones.

D. Referral Schemes and Other Solicitation Techniques

Word of mouth is great advertising. Referral or pyramid schemes take this one step farther. A person buys goods or services and is promised either a discount on additional purchases or cash income from obtaining other customers for the seller. This entire method of solicitation is illegal in some states. For example, Iowa’s UDAP statute declares as an unlawful practice the “sale, lease, or rental of any merchandise at a price or with a rebate or payment or other consideration to the purchaser which is contingent upon the procurement of prospective customers provided by the purchaser, or the procurement of sales, leases, or rentals to persons suggested by the purchaser." Iowa Code §714.16(2)(b). In other states, a plaintiff may rely on case law interpreting the state UDAP statute in ways that limit referral sales schemes. At a federal level, the FTC pursues referral schemes using the UDAP statute, 15 U.S.C. §45.

Federal Trade Commission v. Skybiz.Com, Inc.

No: 01-CV-396 (N.D. Okl. Aug. 31, 2001)

KERN, Chief Judge.

FINDINGS OF FACT AND CONCLUSIONS OF LAW AND ORDER FOR PRELIMINARY INJUNCTION

On May 30, 2001, Plaintiff filed suit against SkyBiz.com, Inc., World Service Corporation (WSC), WorldWide Service Corporation (WWSC), Nanci Corporation International, James S. Brown, Stephen D. McCullough, Elias F. Masso, Nanci Masso, Kier F. Masso, and Ronald E. Blanton alleging that Defendants: 1) made

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false and misleading earnings claims to consumers; 2) provided others with the means and instrumentalities to make the same deceptive claims; 3) failed to disclose to consumers that SkyBiz's pyramid structure would not allow many of SkyBiz's participants to achieve the benefits promised by Defendants; and 4) were operating a pyramid scheme, all in violation of Section 5 of the FTC Act. [ED. NOTE—This is codified at 15 U.S.C. §45.] After issuing an Order requiring the Defendants to show cause why a preliminary injunction should not issue, the Court held a hearing. Now having considered the complaint, the evidence presented, the exhibits, the proposed Findings of Fact and Conclusions of Law submitted by the parties, and the applicable law, the Court renders the following Findings of Fact and Conclusions of Law with respect to SkyBiz.com, Inc., WSC, and WWSC.

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I. FINDINGS OF FACT

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E. DEFENDANTS' BUSINESS STRATEGY

21. Since its inception in 1998, all of the Defendants have been involved in some way with "The SkyBiz Program."

22. The SkyBiz Program is a MLM [multi-level marketing] scheme which involves

the sale of an Internet product called a Web Pak. The program is promoted as a work-from-home business opportunity whereby interested individuals ("Associates") can sell the Web Pak product and achieve unlimited success if they put forth a reasonable amount of diligence. If an individual does not wish to purchase a Web Pak, he may become a "Compensation Only" Associate and simply receive compensation for participating in the program.

23. The Web Pak is a personal computer-related package which allegedly consists of the tools to create a 35 megabyte Internet website, various tutorials for beginner computer users, and an electronic mail account.

24. SkyBiz sells the Web Pak for $100.00 per year, plus a one-time processing charge of $25.00.

25. Associates buy the Web Pak which entitles them to participate in the SkyBiz Program. In order to earn income, they must recruit new Associates who purchase the SkyBiz Program from Defendants and who, in turn, recruit new Associates who purchase the SkyBiz Program from Defendants, and so on. Once an Associate sells two Web Paks, he is eligible to receive commissions. In this way, each Associate creates a "downline" consisting of all the people sponsored directly or indirectly by that Associate. Once an associate has personally sold nine (9) Web Paks, or has sold nine (9) indirectly through those in his "downline," that Associate receives a commission check from SkyBiz. As long as the Associate's downlines recruit new members, the Associate can earn commissions. A total of twenty-seven (27) sales must be made in an Associate's downline before his initial $125.00 is recouped. (Twenty-seven sales actually amounts to $140.00.)

26. Many new Associates are encouraged to buy more than one Web Pak at the outset because there is greater earning potential.…Some people were even

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convinced to buy more than three. (Ken Klein testimony) (purchased five Web Paks); (Declaration of George Brackenrich) (purchased six Web Paks—two "3PAKs"; later persuaded to buy eight "7PAKs," plus one more Web Pak for a total of sixty-three Web Paks at a total cost of over $7,000.00).

27. The SkyBiz Program is promoted both directly by the Defendants and through their network of recruited Associates. Defendants urge Associates to use word-of-mouth referrals to get potential recruits to attend in-person sales presentations given by SkyBiz officers, corporate-sponsored presenters and more senior Associates.

28. In addition, Defendants sponsor conference calls and prerecorded calls to pitch the SkyBiz Program to prospective Associates. To assist their Associates in recruiting new participants in the SkyBiz Program, Defendants sell CD-ROMs, computer disks, videos, and books promoting the SkyBiz Program, and they provide a PowerPoint presentation that Associates may download.

29. In their live presentations, telephone calls, marketing materials and on their websites, defendants represent that participants are likely to receive substantial

income by participating in the SkyBiz Program.

30. In their marketing materials and at seminars, Defendants have also featured "testimonials" from participants in the SkyBiz Program. In these testimonials, the individuals describe how successful they have become through participation in the SkyBiz Program.

31. Under SkyBiz's structure, approximately 87% of SkyBiz participants at any given time will not be able to qualify for commissions. This same structure also ensures that approximately 94% of SkyBiz's members at any given time will not recoup their investment. These facts are concealed when the SkyBiz program is pitched.

32. SkyBiz Associates and others affiliated with SkyBiz (including at least some of its principals) who market its product made numerous representations to consumers —potential Associates—that by participating in the SkyBiz program, they could earn substantial amounts of money. These representations have come in various forms: verbal representations in-person at live seminars and in visits to individual homes; verbal representations over the phone and in conference calls; and written representations on some Associates' websites. The promotional efforts of SkyBiz are designed to recruit new Associates by promising them the opportunity to achieve fabulous wealth with little or no effort through the recruitment of new Associates.

33. Although SkyBiz claims that its main function is to market the product, the emphasis of the seminars and Associate testimonials is on the earning potential one can realize if they become a SkyBiz Associate. Thus, the emphasis is placed on recruiting more Associates and not on selling the Web Pak.

34. The Receiver [Ed. Note—The FTC had a court-appointed receiver put in place when it filed suit] estimates that there are over 1.9 million Associates enrolled in the SkyBiz program.

35. The Receiver found that, out of all Web Pak sales, there have been only 428 sales of Web Paks to individuals who did not want to participate in the Compensation Plan.

36. In a study prepared in connection with the prosecution of criminal charges against SkyBiz Associates in Canada, the Royal Canadian Mounted Police found that 85% of the assigned websites were never developed. The defense's expert in that

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same proceeding, whose expenses were paid by SkyBiz, testified that 87% of all assigned websites were not developed. Defendants' real product is the right to recruit new members.

37. There is little, if any, evidence that the Web Pak alone is a sought-after product. The parties have a difficult time convincingly demonstrating that there are consumers who have bought the Web Pak without any intention of participating in the MLM scheme. Furthermore, Defendants have presented no evidence that a significant number of purchasers of Web Paks use, maintain or renew their websites. This information is solely within the control or knowledge of Defendants. This notable absence of information clarifies to the Court that the interest in SkyBiz appears to lie in

the opportunity to make money, which comes only with the recruitment of more members.

38. There is sufficient evidence to conclude that the SkyBiz Program is a deceptive marketing scheme.

39. There is sufficient evidence to conclude that individuals associated with the SkyBiz Program made misrepresentations and misleading claims to consumers about the potential for effortlessly earning great amounts of money.

II. CONCLUSIONS OF LAW

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56. The misrepresentations made by Defendants and their Associates led consumers to believe that if they took part in the SkyBiz Program, they could earn substantial amounts of money. It is reasonable to expect that consumers could rely on the express claims of the representatives of the SkyBiz Program. See Five-Star Auto Club, 97 F. Supp. 2d at 528. SkyBiz representatives are aware that consumers will rely on these representations and, it is hoped, become participants.

57. Illegal pyramid schemes "are characterized by the payment by participants of money to the company in return for which they receive (1) the right to sell a product and (2) the right to receive in return for recruiting other participants into the program rewards which are unrelated to sale of the product to ultimate users." In re Koscot Interplanetary, Inc., 86 F.T.C. 1106 (1975). Several courts have adopted the *Koscot* test for pyramid schemes. See, e.g., US. v. Gold Unlimited, Inc., 177 F. 3d 472, 480 (6th Cir. 1999); Webster v. Omnitrition Intern., Inc., 79 F.3d 776, 781-82 (9th Cir. 1996).[3]

58. A lawful multi-level marketing program is distinguishable from an illegal pyramid scheme in the sense that the "primary purpose" of the enterprise and its associated individuals is to sell or market an end-product with end-consumers, and not to reward associated individuals for the recruitment of more marketers or "associates." See Gold Unlimited, 177 F.3d at 483-84 (suggesting that based on a

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statutory survey of state criminal laws against pyramid schemes, this is a difference). See also Ger-Ro-Mar, Inc. v. FTC, 518 F.2d 33, 36 (2d Cir. 1975) (explaining that the distributors profited by earning commissions from their own sales and those of their recruits); In re Amway Corp., 93 F.T.C. 618, 716 (1979) (sponsors do not make money from their recruits' efforts until a newly recruited distributor begins to make wholesale purchases from his sponsor and sales to consumers).

59. Another distinction is that an unlawful pyramid scheme will saturate the market of potential participants to the point where it is unrealistic to expect that such a large number of individuals will become involved and the pyramid must therefore eventually collapse. A legitimate MLM does not have such a propensity for saturation. See Five-Star Auto Club, 97 F. Supp. 2d at 518 (S.D.N.Y. 2000) ("[i]f…each Five Star participant recruited only three new members, Five Star would have 387,000,000

members…exceed[ing] the populations of the United States and Canada"); Gold Unlimited, 177 F.3d at 481; Ger-Ro-Mar, 518 F.2d at 36-38 (if even a small number of individuals are recruited each month by each member, after a year the number of members would exceed the population of the United States); Amway, 93 F.T.C. at 716-17.

60. While the Web Pak product marketed and sold by SkyBiz appears to have some value to customers interested in purchasing it, the Court is not convinced that the primary purpose of SkyBiz is to sell Web Paks and to have its Associates sell Web Paks. Instead, the primary purpose of SkyBiz appears to be recruitment of Associates and to reward its members for that recruitment. In addition, whether SkyBiz's product has inherent value is of little consequence. While the product value could affect the quantum of harm suffered by the consumer, the issue of consumer harm is irrelevant to the Court's inquiry when the FTC brings an enforcement action such as this. See Miller, *supra* at ¶48. Furthermore, simply because a MLM's product has value does not render an unlawful pyramid scheme lawful. The other elements of a legal MLM program must also be present. See Gold Unlimited, Ger-Ro-Mar, and In re Amway, supra, at ¶58.

61. In addition, as pointed out by the FTC's expert, the structure of SkyBiz will ultimately result in the company's collapse. Because SkyBiz does not concentrate its business on sales of its single product, but instead on recruitment of members, the exponential growth which would be required to sustain the incomes anticipated by successful recruiters is impossible to attain and spells eventual collapse, or saturation, of the business.

62. There is good cause to believe that, under the more lenient standard, the FTC will ultimately prevail on the merits of this case and establish that Defendants have violated §5(a) of the FTC Act. The Court is convinced that without the entry of preliminary relief, Defendants will continue to violate §5(a) by making false or misleading representations about the SkyBiz program and its marketing plan which emphasizes potential for success for Associates who take part in the scheme.…

The court issued a preliminary injunction designed to not just to eliminate the sale of the Web Pak product but to restrain all defendants, including the individuals, from operating any pyramid marketing scheme. This remedy takes aim at the problem of individuals beginning a new referral sales company, with a different name and product but the same practices.

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At the other end of the spectrum from referral schemes, which rely on consumers being social beings, are unsolicited goods, which just arrive at one's doorstep without any contact with the company or its representatives. The statutes regulating U.S. mail prohibit sending unordered goods, with the exception of free gifts, which must both be truly free and bear a notice telling consumers they are free. 39 U.S.C. §3009. Violations of this law are per se violations of the FTC Act, and quite often scams that use unordered goods and other deceptive practices, such as enclosing documents that suggest a consumer placed an order for the merchandise or is obligated to pay for return shipping.

Problem Set 4

4.1. Lucy Ling founded an interior decoration company, Lovely Living. She goes directly to people's homes, either having called in advance or without notice, and sells decorating plans. Ronald James has really let his house go since his wife's death two decades ago and was persuaded by Lucy's pitch that she could "bring the house back to life" with simple decorating plans that Ronald could execute "with a couple of trips to big-box retailer House, Home, and Hearth." To design the plan, Lucy followed her usual practices of taking digital photos and asking for a few small items of personal property to make pleasing color matches. Ronald gave her a pillow cushion and signed the contract. The plan's total cost is $500, with $300 payable up-front, which Ronald paid with a personal check. Lucy gave Ronald a copy of the signed contract, with all the blanks filled in neatly. The contract contained a prominent disclosure of right to cancel for three days. On the back of the contract were printed two copies of a lengthy term labeled "NOTICE OF CANCELLATION." Lucy's neighbor, a retired lawyer, wrote that language for her, telling her "it is the exact FTC-required language from the Internet." As fate would have it, Ronald fell instantly in love at a bingo tournament just one week later. His new special lady is herself an interior decorator and is excited about the opportunity to bring her unique touch to Ronald's home. Can Ronald cancel the contract with Lovely Living? *See* 16 C.F.R. §429.1.

4.2. Phijheeta Agrawal works for a telemarketing company, Beaches or Bust, that calls consumers to sell them vacation packages. When she makes her calls, Phijheeta identifies herself as an employee of Beaches or Bust, and states that the purpose of the call is to sell vacation packages that include hotel stays, ground transfers, and tours. She enjoys most aspects of her job, including describing the exotic locations and getting to talk to customers from all over the country. Phijheeta sometimes encounters a hostile caller, including some who demand her name, social security number, employee ID number, date of birth, or other details. In those instances, she usually just gives her name as Ann Smith or Jane Wood, in part because people mispronounce her name making it rhyme with "fajita." She politely refuses to give the other information and reminds the consumer that they may end the call at any time. Is Phijheeta violating the FTC's telemarketing sales rule? *See* 16 C.F.R. §§310.3, 310.4, and 310.5.

4.3. Hunt Hudson is the newly elected governor in a state whose populace is purple on the political spectrum (a perfect blend of "red" (Republicans) and

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"blue" (Democratic) citizens). Like all politicians, he needs initiatives that will be offensive to few and be loved by many. Inspired by his own difficulty in managing the flow of email on his iPhone, he has asked what you think of creating a state-wide "do-not-email" registry that would provide parallel protection to the do-not-call registry for unsolicited phone calls. Could a state enact such a law? What exceptions, if any, might Governor Hudson want to include in his proposed registry for certain kinds of emails? *See* 15 U.S.C. §§7707(b); 7702(2)(A); 7702(17).

4.4. Bethany Smith has a tough job as a receptionist at a law firm. She works long hours and to unwind she finds nothing beats a good massage. A new business called Massage Mates opened on the first floor of the skyscraper where she works. Bethany stopped in and learned that it is a members-only club. The initiation fee is $100 but that can be reduced by $10 for every friend that Bethany brings with her at the time that she joins. The monthly membership fee is $50 and includes one massage per month. Additional massages per month cost $40. The contract lasts for one year. Bethany can bring non-member friends for a one-time massage at a cost of $60. If they join within one month of receiving the massage, Bethany gets $10 off the next month's membership fee. Bethany had a bad experience a few years ago getting out of a gym contract after paying a hefty joining fee. She asks you, the most junior associate at the firm, whether she should join Massage Mates. In answering, consider the following statute:

> With respect to a consumer sale of goods or services, the seller may not give or offer to give a rebate or discount or otherwise pay or offer to pay value to the consumer as an inducement for a sale for the consumer giving the seller the names of prospective buyers, or otherwise aiding the seller in making a sale to another person, IF earning the rebate, discount, or other value is contingent upon the occurrence of an event AFTER the time the consumer agrees to buy.

Assignment 5. Advertising

Advertising can help both consumers and businesses. Consumers benefit from awareness of and information about goods and services, and businesses benefit from new customers and increased product demand. Consumer law curbs advertising when it harms consumers by giving them false information. The usual legal maneuver is to prohibit certain statements on the grounds that they are deceptive. In some situations, however, consumer law affirmatively compels businesses to give information through labeling or other disclosures to counter problems with misinformation in a market.

Legally, advertising is a form of commercial speech. It is entitled to some constitutional protection from government regulation but significantly less than non-commercial speech. *See* Robert C. Post, *The Constitutional Status of Commercial Speech*, 48 U.C.L.A. L. REV. 1 (2010). This assignment touches the constitutional aspects lightly, focusing instead on the way in which accurate advertising improves markets and aids consumers.

A. Unfair and Deceptive Advertising

1. False Advertising

Advertisements that are untrue can be attacked under several legal theories. The common law of fraud or misrepresentation is one such tool, as is rescission of a contract on the ground that it was induced by fraud. These actions often focus on when advertising crosses the line from harmless puffery to false advertising. *See* David Hoffman, *The Best Puffery Article Ever*, 91 IOWA L. REV. 1395 (2006). At both the federal and state level, false advertising may be attacked as a deceptive practice banned under a UDAP statute or may violate a more specific law that targets false advertising. As the following case discusses, the statutes use a lower standard than the common law.

State of Iowa ex rel. Miller, Attorney General of Iowa v. Pace

677 N.W.2d 761 (Iowa 2004)

TERNUS, Justice.

The defendant, Edwin Pace, appeals a district court judgment finding he had violated various state laws in his marketing and sale of payphones, awarding monetary remedies and penalties, and granting injunctive relief....Pace also asserts the State failed to prove he committed unlawful practices under Iowa's consumer fraud law....

I. BACKGROUND FACTS AND PROCEEDINGS.

...Beginning in 1997, but primarily in 1999 and continuing through June of 2000, the defendant sold payphones, known as customer-owned, coin-operated telephones (COCOTS), in Iowa....[T]he investor entered into an agreement to purchase a payphone and then simultaneously leased the payphone to a management company. The payphone was then delivered directly to the management company for placement and operation. During the three- to five-year term of the lease, the investor had no involvement in the day-to-day operation of the payphone; all management rights rested in the management company in exchange for a monthly payment of $75-$82 to the investor....[The] investors were only interested in the sale/leaseback plan because they had no expertise in operating or ability to manage a payphone. Thus,...the only COCOTS actually sold by the defendant were under the sale/leaseback plan.

Pace worked with a number of marketing companies, including Tri-Financial Group, Bee Communications, and ATC, Inc. Each company selling payphones was associated or affiliated with a particular management company. Although Pace claimed only to sell payphones and to have no relationship with the management companies, he would forward a request for lease information directly to the management company upon an investor's decision to go with the sale/leaseback option. Each payphone was sold for $5000 to $7000, and Pace earned a commission of between 10-12% on each sale....

On September 17, 2001, the State filed a petition charging Pace with violations of the Iowa Uniform Security Act, Iowa Code chapter 502, the Iowa Business Opportunity Act, Iowa Code chapter 523B, and the Iowa Consumer Fraud Act, Iowa Code §714.16. At trial, the facts previously reviewed were brought out. In addition, several investors testified about the information given to them by Pace. They said Pace told them they would own the payphones; they could cancel the lease at any time and receive a refund of all or some portion of the purchase price; the management companies were financially strong; there was little risk in this investment and the investors would receive a return of 13-14%; and that COCOTS were legal in Iowa. One witness testified that Pace even told an elderly investor that COCOTS were fully insured by Lloyds of London.

The State also called a financial expert who had reviewed the financial statements of ETS. He testified that it was "obvious" the phone program could not be maintained without the continuous sale of payphones because the only way the lease payments could be made was through proceeds from future payphone sales.

In its subsequent decision, the district court made factual findings consistent with our review of the pertinent facts. The court found that even though material was available to Pace indicating significant legal issues with COCOTS across the country, he continued to represent to prospective purchasers that there were no concerns with selling the product in Iowa. He also repeatedly represented to potential investors that they would realize immediate and significant income

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from the ownership of a COCOT, that the COCOT was a liquid and safe investment, and that the COCOT was recession proof.…

Based on the same representations and omissions, the trial court concluded Pace's conduct constituted an "unfair practice" and "deception" under the consumer fraud provision of chapter 714. See id. §714.16. Because the court found Pace's violations were committed against "older persons," the court held the additional civil penalties of §714.16A applied.

The district court ordered Pace to pay restitution in the amount of $302,000. See id. §§502.501(1) (providing for restitution by person found in violation of chapter 502), 502.604(2)(d) (allowing commissioner of insurance to obtain court order for restitution). It also ordered him to disgorge to the State of Iowa all commissions received from the sale of COCOTS. See id. §502.604(2)(d) (allowing commissioner to obtain order providing for disgorgement by person found in violation of chapter 502). In addition, Pace was enjoined from violating chapters 502 and 523B, as well as §714.16, and from selling unregistered securities and business opportunities in Iowa. The court imposed a civil penalty of $4000 ($1000 for each commission of an unlawful practice), and a civil penalty of $1000 ($250 for each commission of consumer fraud against the elderly). See id. §§714.16(7) (providing for civil penalty of up to $40,000 per violation of §714.16), 714.16A(1) (providing for civil penalty of up to $5000 for each violation of §714.16 committed against an older person). Pace was made responsible for court costs, costs of investigation, and reasonable attorney fees. See id. §714.16(11) (permitting recovery of court costs, investigative costs, and attorney fees).

Pace appealed the trial court's decision. He asserts several grounds for reversal [including]…the State failed to prove the representations made by Pace were untrue; [and] the State failed to prove consumer fraud.

…

V. DID PACE COMMIT AN UNLAWFUL PRACTICE PROHIBITED BY THE CONSUMER FRAUD LAW IN HIS SALE OF COCOTS?

The trial court held that Pace violated Iowa Code §714.16, which provides in relevant part:

> The act, use or employment by a person of an unfair practice, deception, fraud, false pretense, false promise, or misrepresentation, or the concealment, suppression, or omission of a material fact with intent that others rely upon the concealment, suppression, or omission, in connection with the lease, sale, or advertisement of any merchandise…, whether or not a person has in fact been misled, deceived, or damaged, is an unlawful practice.

This statute is not a codification of common law fraud principles. See State ex rel. Miller v. Hydro Mag, Ltd., 436 N.W.2d 617, 622 (Iowa 1989). It permits relief upon a lesser showing that the defendant made a misrepresentation or omitted a material fact "with the intent that others rely upon the…omission." Iowa Code §714.16(2)(a).

In the present case, the trial court found that Pace made the following false, deceptive and misleading representations to consumers in selling

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COCOTS: (1) "an investment in COCOTS was guaranteed and was as safe or safer than bank certificates of deposit, annuity products, and insurance products"; (2) "the COCOTS program he offered was properly registered for sale in Iowa"; (3) the investors "would receive a 14% annual return on their COCOT investment and…they would receive a return of…114% on their money"; (4) the investors "would own an asset in the form of a payphone"; and (5) "the payphone companies were financially strong." In addition, the court found that Pace "failed to share facts [that] would have been material [to investors] in making a decision to invest money in COCOTS." The material, undisclosed facts included: (1) the investment was high risk; (2) the high returns promised by the management companies could not realistically be expected; (3) the program was a Ponzi scheme; (4) the offers were not registered as a security or a business opportunity; (5) Pace was not registered as a securities agent in Iowa; and (6) Pace received significant commissions for each sale and he was required to return his commission should an investor liquidate his or her investment. See generally Goettsch, 561 N.W.2d at 378 (defining a Ponzi scheme).

The court also held these misrepresentations and material omissions constituted securities fraud under §502.401(2). Because the standard of proof is higher under §714.16, we consider Pace's challenge to the court's findings of misrepresentation and material omission only under the consumer fraud provisions of chapter 714.

Pace challenges the trial court's finding of consumer fraud on three bases. He denies making the statements attributed to him by the trial court and contends that even if he did make these representations, they were not shown to be false. He also claims that he acted innocently because he simply passed along the information he received from the marketing companies and had no idea this information was false.

Addressing the last argument first, we point out that it is not necessary for the State to prove that the violator acted with an intent to deceive, as is required for common law fraud. See Miller v. William Chevrolet/GEO, Inc., 326 Ill. App. 3d 642, 762 N.E.2d 1, 12, 260 Ill. Dec. 735 (Ill. App. Ct. 2001) (interpreting identical statutory language and stating, "Nor need the defendant have intended to deceive the [investor]."); Gennari v. Weichert Co. Realtors, 148 N.J. 582, 691 A.2d 350, 365 (N.J. 1997) (interpreting nearly identical statutory language and stating, "an intent to deceive is not a prerequisite to the imposition of liability"). As we noted above, the only intent required by the statute is that the defendant act "with the intent *that others rely*" upon his omissions. Iowa Code §714.16(2)(a) (emphasis added). In addition, there is no requirement under the statute that a violator have knowledge of the falsity of his or her representations. See Gennari, 691 A.2d at 365 ("One who makes an affirmative misrepresentation is liable even in the absence of knowledge of the falsity of the misrepresentation, negligence, or the intent to deceive."). Similarly, the Iowa statute does not require knowledge with respect to the omission or concealment of a material fact. See Miller, 762 N.E.2d at 12 (holding "innocent misrepresentations or material omissions" are actionable under consumer fraud law that included "the concealment, suppression or omission of any material fact" within definition of unlawful practice); *cf.* Gennari, 691 A.2d at 365 (holding "for liability to attach to an omission or failure to disclose,...the plaintiff must show that the defendant acted with knowledge" under statutory definition of unlawful practice that included "*knowing* concealment, suppression, or omission of any material fact" (emphasis added)). Thus, the defendant's contention that he was

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misled by the payphone companies just like his client is immaterial. Our consumer fraud statute places the consequences of being uninformed on the agent, not the investor....

AFFIRMED.

Under federal law, an advertisement is false if it is "misleading in a material respect." 15 U.S.C. §55(a)(1). The definition includes not only representations but also the "extent to which the advertisement fails to reveal facts material in the light of such representations or material with respect to consequences which may result from the use of commodity...." *Id*. The misrepresentation can be found anywhere, including on the product itself or in a separate advertisement.

Kraft, Inc. v. Federal Trade Commission

970 F.2d 311 (7th Cir. 1992)

FLAUM, Circuit Judge.

Kraft, Inc. ("Kraft") asks us to review an order of the Federal Trade Commission ("FTC" or "Commission") finding that it violated the Federal Trade Commission Act ("Act"), 15 U.S.C. §§45, 52. The FTC determined that Kraft, in an advertising campaign, had misrepresented information regarding the amount of calcium contained in Kraft Singles American Pasteurized Process Cheese Food ("Singles") relative to the calcium content in five ounces of milk and in imitation cheese slices. The FTC ordered Kraft to cease and desist from making these misrepresentations and Kraft filed this petition for review. We enforce the Commission's order....

Process cheese food slices, also known as "dairy slices," must contain at least 51% natural cheese by federal regulation. 21 C.F.R. §133.173(a)(5). Imitation cheese slices, by contrast, contain little or no natural cheese and consist primarily of water, vegetable oil, flavoring agents, and fortifying agents. While imitation slices are as healthy as process cheese food slices in some nutrient categories, they are as a whole considered "nutritionally inferior" and must carry the label "imitation." Id. at §101.3(e)....

Kraft Singles are process cheese food slices. In the early 1980s, Kraft began losing market share to an increasing number of imitation slices that were advertised as both less expense and equally nutritious as dairy slices like Singles. Kraft responded with a series of advertisements, collectively known as the "Five Ounces of Milk" campaign, designed to inform consumers that Kraft Singles cost more than imitation slices because they are made from five ounces of milk rather than less expensive ingredients. The ads also focused on the calcium content of Kraft Singles in an effort to capitalize on growing consumer interest in adequate calcium consumption.

The FTC filed a complaint against Kraft charging that this advertising campaign materially misrepresented the calcium content and relative calcium benefit of Kraft

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Singles. The FTC Act makes it unlawful to engage in unfair or deceptive commercial practices, 15 U.S.C. §45, or to induce consumers to purchase certain products through advertising that is misleading in a material respect. Id. at §§52, 55. Thus, an advertisement is deceptive under the Act if it is likely to mislead consumers, acting reasonably under the circumstances, in a material respect. In implementing this standard, the Commission examines the overall net impression of an ad and engages in a three-part inquiry: (1) what claims are conveyed in the ad; (2) are those claims false or misleading; and (3) are those claims material to prospective consumers.

Two facts are critical to understanding the allegations against Kraft. First, although Kraft does use five ounces of milk in making each Kraft Single, roughly 30% of the calcium contained in the milk is lost during processing. Second, the vast majority of imitation slices sold in the United States contain 15% of the U.S. Recommended Daily Allowance (RDA) of calcium per ounce, roughly the same amount contained in Kraft Singles. Specifically then, the FTC complaint alleged that the challenged advertisements made two implied claims, neither of which was true: (1) that a slice of Kraft Singles contains the same amount of calcium as five ounces of milk (the "milk equivalency" claim); and (2) that Kraft Singles contain more calcium than do most imitation cheese slices (the "imitation superiority" claim).

The two sets of ads at issue in this case, referred to as the "Skimp" ads and the "Class Picture" ads, ran nationally in print and broadcast media between 1985 and 1987. The Skimp ads were designed to communicate the nutritional benefit of Kraft Singles by referring expressly to their milk and calcium content. The broadcast version of this ad on which the FTC focused contained the following audio copy:

Lady (voice over): I admit it. I thought of skimping. Could you look into those big blue eyes and

> skimp on her? So I buy Kraft Singles. Imitation slices use hardly any milk. But Kraft has five ounces per slice. Five ounces. So her little bones get calcium they need to grow. No, she doesn't know what that big Kraft means. Good thing I do.
>
> Singers: Kraft Singles. More milk makes 'em…more milk makes 'em good.
> Lady (voice over): Skimp on her? No way.

The visual image corresponding to this copy shows, among other things, milk pouring into a glass until it reaches a mark on the glass denoted "five ounces." The commercial also shows milk pouring into a glass which bears the phrase "5 oz. milk slice" and which gradually becomes part of the label on a package of Singles. In January 1986, Kraft revised this ad, changing "Kraft has five ounces per slice" to "Kraft is made from five ounces per slice," and in March 1987, Kraft added the disclosure, "one 3/4 ounce slice has 70% of the calcium of five ounces of milk" as a subscript in the television commercial and as a footnote in the print ads.

The Class Picture ads also emphasized the milk and calcium content of Kraft Singles but, unlike the Skimp ads, did not make an express comparison to imitation slices. The version of this ad examined by the FTC depicts a group of school children having their class picture taken, and contains the following audio copy:

> Announcer (voice over): Can you see what's missing in this picture?
>
> Well, a government study says that half the school kids in America don't get all the calcium recommended for growing kids. That's why Kraft Singles are important. Kraft

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> is made from five ounces of milk per slice. So they're concentrated with calcium. Calcium the government recommends for strong bones and healthy teeth!
>
> Photographer: Say Cheese!
>
> Kids: Cheese!
>
> Announcer (voice over): Say Kraft Singles. 'Cause kids love Kraft Singles, right down to their bones.

…

As to the Skimp ads, the Commission found that four elements conveyed the milk equivalency claim: (1) the use of the word "has" in the phrase "Kraft has five ounces per slice"; (2) repetition of the precise amount of milk in a Kraft Single (five ounces); (3) the use of the word "so" to link the reference to milk with the reference to calcium; and (4) the visual image of milk being poured into a glass up to a five-ounce mark, and the superimposition of that image onto a package of Singles. It also found two additional elements that conveyed the imitation superiority claim: (1) the express reference to imitation slices combined with the use of comparative language ("hardly any," "but"); and (2) the image of a glass containing very little milk during the reference to imitation slices, followed by the image of a glass being filled to the five-ounce mark during the reference to Kraft Singles. The Commission based all of these findings on its own impression of the advertisements and found it unnecessary to resort to extrinsic evidence; it did note, however, that the available extrinsic evidence was consistent with its determinations.

The Commission then examined the Class Picture ads—once again, without resorting to extrinsic evidence—and found that they contained copy substantially similar to the copy in the Skimp ads that conveyed the impression of milk equivalency.

...

Kraft makes numerous arguments on appeal, but its principal claim is that the FTC erred as a matter of law in not requiring extrinsic evidence of consumer deception. Without such evidence, Kraft claims (1) that the FTC had no objective basis for determining if its ads actually contained the implied claims alleged, and (2) that the FTC's order chills constitutionally protected commercial speech. Alternatively, Kraft contends that substantial evidence does not support the FTC's finding that the Class Picture ads contain the milk equivalency claim. Finally, Kraft maintains that even if it did make the alleged milk equivalency and imitation superiority claims, substantial evidence does not support the FTC's finding that these claims were material to consumers. We address each contention in turn.

In determining what claims are conveyed by a challenged advertisement, the Commission relies on two sources of information: its own viewing of the ad and extrinsic evidence. Its practice is to view the ad first and, if it is unable on its own to determine with confidence what claims are conveyed in a challenged ad, to turn to extrinsic evidence. Thompson Medical, 104 F.T.C. at 788-89; Cliffdale Assocs., 103 F.T.C. 110, 164-66 (1984); FTC Policy Statement, 103 F.T.C. at 176. The most convincing extrinsic evidence is a survey "of what consumers thought upon reading the advertisement in question," Thompson Medical, 104 F.T.C. at 788-89, but the Commission also relies on other forms of extrinsic evidence including consumer testimony, expert opinion, and copy tests of ads. FTC Policy Statement, 103 F.T.C. at 176 n. 8.

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Kraft has no quarrel with this approach when it comes to determining whether an ad conveys express claims, but contends that the FTC should be required, as a matter of law, to rely on extrinsic evidence rather than its own subjective analysis in all cases involving allegedly implied claims. The basis for this argument is that implied claims, by definition, are not self-evident from the face of an ad. This, combined with the fact that consumer perceptions are shaped by a host of external variables—including their social and educational backgrounds, the environment in which they view the ad, and prior experiences with the product advertised, see Richard Craswell, *Interpreting Deceptive Advertising*, 65 B.U. L. Rev. 658, 672-74, 717 (1985); Richard Pollay, *Deceptive Advertising and Consumer Behavior: A Case for Legislative and Judicial Reform*, 17 U. Kan. L.

Rev. 625, 629-31 (1969)—makes review of implied claims by a five-member commission inherently unreliable. The Commissioners, Kraft argues, are simply incapable of determining what implicit messages consumers are likely to perceive in an ad. Making matters worse, Kraft asserts that the Commissioners are predisposed to find implied claims because the claims have been identified in the complaint, rendering it virtually impossible for them to reflect the perceptions of unbiased consumers.…

While Kraft's arguments may have some force as a matter of policy, they are unavailing as a matter of law. Courts, including the Supreme Court, have uniformly rejected imposing such a requirement on the FTC, see Colgate-Palmolive, 380 U.S. at 391-92, 85 S. Ct. at 1046 (FTC not required to conduct consumer surveys before determining that a commercial has a tendency to mislead); and we decline to do so as well. We hold that the Commission may rely on its own reasoned analysis to determine what claims, including implied ones, are conveyed in a challenged advertisement, so long as those claims are reasonably clear from the face of the advertisement.

Kraft's case for a per se rule…rests on the faulty premise that implied claims are inescapably subjective and unpredictable. In fact, implied claims fall on a continuum, ranging from the obvious to the barely discernible. The Commission does not have license to go on a fishing expedition to pin liability on advertisers for barely imaginable claims falling at the end of this spectrum. However, when confronted with claims that are implied, yet conspicuous, extrinsic evidence is unnecessary because common sense and administrative experience provide the Commission with adequate tools to makes its findings. The implied claims Kraft made are reasonably clear from the face of the advertisements, and hence the Commission was not required to utilize consumer surveys in reaching its decision.

…

Alternatively, Kraft argues that substantial evidence does not support the FTC's finding that the Class Picture ads convey a milk equivalency claim. Kraft claims that the Commission merely extrapolated its analysis from the Skimp ads to the Class Picture ads without considering significant differences between the two. The Commission stated, for example, that the Class Picture ads "contain copy elements substantially similar to the 'Skimp' ad elements that convey the impression of milk equivalency." In re Kraft, Inc., FTC No. 9208, slip op. at 22. Kraft points out that the Class Picture ads contain only one of the four elements of the Skimp ads—the reference to five ounces of milk juxtaposed with a reference to calcium content—that contributed to the FTC's milk equivalence finding. And Kraft adds that the reference to five ounces of milk per slice and to calcium merely states that each

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Because identity theft is often enabled by business' collection of consumer information, it is intertwined with consumer privacy protections. The more information businesses have and the fewer burdens they have to keep it secure and confidential, the greater the opportunity for identity theft. Given the difficulty in prosecutions and remediation, the prevention of identity theft may be the best tactic. How much of a burden should businesses have in verifying someone's identity?

Andrews v. TRW

225 F.3d 1063 (9th Cir. 2000) (rev'd on other grounds, 534 U.S. 19 (2001))

NOONAN, Circuit Judge.

Adelaide Andrews (Andrews) appeals the judgment by the district court in her suit against TRW, Inc. The case involves the rights under the Fair Credit Reporting Act, 15 U.S.C. §§1681-1681u (1994 & Supp. II) (FCRA), and Cal. Bus. & Prof. Code §17200 et. seq. (1996), of a person claiming to be damaged by the disclosure of inaccurate credit information by a consumer credit reporting agency such as TRW....

In June 1993, Andrea Andrews (hereafter the Imposter) obtained the social security number and California driver's license number of Adelaide Andrews (hereafter the Plaintiff). The Imposter did so simply by misusing her position as a doctor's receptionist and copying the information that the Plaintiff, as a patient in that office, supplied to the doctor.

In 1994-1995 the Imposter applied for credit to four companies subscribing to TRW's credit reports. For example, on July 25, 1994, to First Consumers National Bank (FCNB), the Imposter applied as Andrea A. Andrews, 3993-1/2 Harvard Blvd., Los Angeles, CA, 90062, phone 213-312-0605, employed at Spensor-Robbyns Products, Los Angeles. The Imposter gave the birth date and social security number of the Plaintiff.

In this application the only misinformation was the Imposter's use of the Plaintiff's social security number and date of birth. On October 28, 1994 to Express Department Stores the Imposter made a comparable credit application, using her own identity except for the Plaintiff's social security number. Again, in January 1995, to Commercial Credit the Imposter applied for credit, using her own identity, except for Plaintiff's social security number and a clumsy misspelling of her first name as "Adeliade."

TRW responded to the credit inquiries of the three companies by treating the applications as made by the Plaintiff. TRW furnished the information in its file on the Plaintiff and added the three inquiries to the Plaintiff's file.

Each of the credit applications applied for by the Imposter was turned down by the company getting the TRW report. In addition, the Imposter applied for cable service to a public utility, Prime Cable of Las Vegas, which was required by law to provide cable services but nonetheless asked for a TRW report. The Imposter applied as Andrea Andrews, 4201 S. Decatur #2202, Las Vegas, NV, 89103, Phone 248-6352. The

Imposter used the social security number of the Plaintiff, which was the only stolen item of identity provided. This account became delinquent and was referred to a collection agency.

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The Plaintiff, however, became aware of the Imposter only on May 31, 1995, when she sought to refinance the mortgage on her home. The bank from which the financing was sought received a report from Chase Credit Research, not a party to this case, whose report combined information from TRW and two other credit reporting agencies. Now aware of the fraud, Andrews contacted TRW and requested deletion from her file of all reference to the Imposter's fraudulent activities. TRW complied.

On October 21, 1996, the Plaintiff filed this suit in the district court. In her first claim she alleged that TRW had furnished credit reports without "reasonable grounds for believing" that she was the consumer whom the credit applications involved, contrary to 15 U.S.C. §§1681b and 1681e(a), and that as a consequence she had suffered damages including an expenditure of time and money and "commercial impairment, inconvenience, embarrassment, humiliation, and emotional distress including physical manifestations." In her second claim, she alleged that TRW had violated §1681e by not maintaining the "reasonable procedures" required by that statute in order "to assure maximum possible accuracy of the information concerning the individual about whom the report relates." 15 U.S.C. §1681e(b). She alleged the same damages. She asserted that both violations were willful and that both also violated Cal. Bus. & Prof. Code §17200 et. seq. [Ed. Note—California's version of UDAP statute.] She sought actual and punitive damages and an injunction requiring TRW to comply with the Fair Credit Reporting Act by "requiring a sufficient number of corresponding points of reference" before disseminating an individual's credit history or attributing information to an individual's credit file.

[Ed. Note—The district court ruled that the disclosures to Express and Commercial were made for a purpose permissible under §1681b(a)(3)(A), because the Plaintiff, even against her will, was "involved" in the credit transaction initiated by the Imposter. Any other rule, the court said, would place "too heavy a burden on credit reporting agencies." The court also held that TRW had used "reasonable procedures" as required by §1681e(a) to limit disclosures. For these several reasons, the court granted summary judgment to TRW on the Plaintiff's first claim. The other claims went to a jury, which returned a verdict in favor of TRW.]

...

Disclosure Without Reasonable Belief. Under §1681b TRW could only furnish a report on a consumer to a customer which it had "reason to believe" intended to use the information in connection with "a credit transaction involving the consumer on whom the information is to be furnished." 15 U.S.C. §1681b(a)(3). Did TRW have a reasonable belief that the Plaintiff was the consumer involved in the credit transactions as to which the four companies sought a report from TRW? As the district court observed, there are 250,000,000 persons in the United States (not all of them having Social Security numbers) and 1,000,000,000 possibilities as to what any one Social Security number may be. The random chance of anyone matching a name to a number is very small. If TRW could assume that only such chance matching would occur, it was reasonable as a matter of law in releasing the Plaintiff's file when an application matched her last name and the number. But we do not live in a world in which such matches are made only by chance.

We take judicial notice that in many ways persons are required to make their social security numbers available so that they are no longer private or confidential

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but open to scrutiny and copying. Not least of these ways is on applications for credit, as TRW had reason to know. In a world where names are disseminated with the numbers attached and dishonest persons exist, the matching of a name to a number is not a random matter. It is quintessentially a job for a jury to decide whether identity theft has been common enough for it to be reasonable for a credit reporting agency to disclose credit information merely because a last name matches a social security number on file.

In making that determination the jury would be helped by expert opinion on the prevalence of identity theft, as the district court would have been helped if it had given consideration to the Plaintiff's witnesses on this point before giving summary judgment.

The reasonableness of TRW's responses should also have been assessed by a jury with reference to the information TRW had indicating that the Imposter was not the Plaintiff. TRW argues that people do use nicknames and change addresses. But how many people misspell their first name? How many people mistake their date of birth? No rule of law answers these questions. A jury will have to say how reasonable a belief is that let a social security number trump all evidence of dissimilarity between the Plaintiff and the Imposter.

The district court held that the Plaintiff was involved in the transaction because her number was used. The statutory phrase is "a credit transaction involving the consumer." 15 U.S.C. §1681b(a)(3)(A). "Involve" has two dictionary meanings that are relevant: (1) "to draw in as a participant" or (2) "to oblige to become associated." The district court understood the word in the second sense. We are reluctant to conclude that Congress meant to harness any consumer to any transaction where any crook chose to use his or her number. The first meaning of the statutory term must be preferred here. In that sense the Plaintiff was not involved.

Another consideration for the district court was that a different rule would impose too heavy a cost on TRW. The statute, however, has already made the determination as to what is a bearable cost for a credit reporting agency. The cost is what it takes to have a reasonable belief. In this case that belief needed determination by a jury not a judge.

We reinstate the Plaintiff's first claim together with her request for punitive damages based upon it.

Under federal law, creditors do not need consumers' consent to obtain reports. In California, and several other states, consumers can request that their credit reports remain confidential unless the requesting party has obtained the consumer's express authorization. Cal. Civ. Code §1785.11.2. This "security freeze" must be affirmatively requested in writing by the consumer and contains several exceptions, including for law enforcement, tax collection and child support actions. The initial statute was ruled unconstitutional because the security freeze allowed a consumer to prevent the collection and distribution of information in the public record, such as evictions or bankruptcies. An amendment cured that defect, Cal. Civ. Code §1785.11.2(m), but most Californians remain unaware of this right or have not exercised it. While the security freeze concept was promoted as a way for consumers to take control of their personal information, the low uptake

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suggests an enduring consumer law problem—getting consumers to do the work involved in exercising a legal right.

Another strategy, adopted in California, is to forbid a certain type of user—retail sellers—from furnishing information unless it can provide several pieces of information about the consumer that match information the credit bureau has on file. Cal. Civ. Code §1785.14(a)(1). The weakness of this rule is that in a serious identity theft situation, the thief may well know things such as the consumer's birth date, sex, and social security number. More stringent requirements to verify identity might be imposed in the future, including fingerprints or other forms of biometric identification.

Problem Set 6

6.1. Streams Co. operates a successful online video and e-book business in which consumers pay a fixed $1 fee to watch videos via online streaming or to download e-books. Streams has entered into a partnership with Bellow, a recommender website where people review products and services and can sign up to receive new reviews from people they know. Streams and Bellow will match all their data, creating a merged data set. As part of the partnership, Bellow will display personalized solicitations for each user that will be based on the videos or books that Bellow users' online contacts had seen or read from Streams. For example, on Mother's Day, Bellow plans an advertisement that says "Get to Know Mom: Watch Her Favorite Movie with Her" and will list titles that Streams' data shows that a Bellow user's mother has watched. Does this use of consumer information by Streams and Bellow violate the law? *See* 18 U.S.C. §2710.

6.2. Foreclosure Facts is a start-up trying to capitalize on the real estate downturn. It pays banks for bulk data, which it then reformulates into a searchable database and a foreclosure auction map, which are available to subscribers for $5 per month. Foreclosure Facts' customers are potential buyers at foreclosure sales and journalists who feature homeowners in stories on the foreclosure crisis. The banks sell the following data for each customer's house that is in foreclosure to Foreclosure Facts: the property address, the amount of the mortgage, the tax assessment of the property's value, and the stage of foreclosure process. The banks provide privacy notices as mandated by Gramm-Leach-Bliley, which state, "We do not disclose any nonpublic personal information about our customers or former customers to anyone, except as permitted by law." Are the financial institutions violating Gramm-Leach-Bliley? *See* 15 U.S.C. §6809(4); 16 C.F.R. §§313.3(n-p); 313.10(a)(1).

6.3. Twenty-five years ago, your mother gave you a nice simple name: Mark Zuckerberg. In childhood, you were just one of several million people enjoying the sunshine in California. In the last several years, your name has been causing you considerable headaches. Two weeks ago, your Facebook account was shut down. The notification from Facebook gave no reason at all. You contacted customer service and were told that the reason was "false identity." Your Facebook page used a picture of Mark Zuckerberg, Facebook founder, as a joke. You also chose to "friend" people who may have thought you were Facebook founder, Mark Zuckerberg, responding to the requests with a

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"Be sure to see my *Social Network* movie!" line. Otherwise, your Facebook page made no reference to the "other" Mark Zuckerberg and had photos and posts of you. In creating and maintaining the account, did you violate California law? *See* Cal. Penal Code §528.5. What rights or remedies do you have to get your Facebook account restored?

6.4. You are an intern for a leading consumer rights organization. Tired of fighting about financial regulation and Dodd-Frank, it is turning its attention to advertising and privacy issues. It has asked you to conduct research and make a recommendation about whether it should issue a consumer education bulletin about the site www.AboutTheData.com. Unfortunately, that is all the instruction you have and everyone is away at a conference. Your first step should be visiting the site and poking around. What are your steps in investigating the site? What is your tentative recommendation? Should consumers be encouraged to register at the site? Or warned against it?

Assignment 7. Credit Reporting

Lenders are avid gathers and users of data about consumers. The primary mechanism for disseminating such information is credit reports that are generated by "consumer reporting agencies" (sometimes called bureaus). Creditors, known in this context as "furnishers" because they supply information, contribute data to the agencies. Creditors also are "users" of credit reports when they access reports to collect names for solicitations or to evaluate applicants' creditworthiness. The triangulation between reporting agencies, furnishers, and users creates layers of responsibility for legal compliance. It also produces a tangled statutory framework.

The Fair Credit Reporting Act (FCRA) is the foundation of Title VI of the Consumer Credit Protection Act. 15 U.S.C. §1681 et seq. FCRA was enacted in 1970 when less technology was used in credit reporting and underwriting. Congress has repeatedly amended the law, with substantial amendments in 2003, the Fair and Accurate Credit Transactions Act (FACTA). Most states also have laws governing credit reporting. These are little used because some statutes largely mirror federal law, and several aspects of credit reporting are preempted by FCRA. The law on preemption in this area is a thicket, even by the intimidating standards for consumer law. As a matter of practice, the wisest course for a plaintiff is often to plead violations under FCRA and state law. Correspondingly, savvy defendants will make use of preemption arguments in responding to suits.

Because credit reporting laws are part of "federal consumer law" as identified by the Dodd-Frank Act, the CPFB is now the rule maker and enforcer for FCRA and FACTA. The CFPB also has exercised supervisory authority, including examination power, over the main reporting agencies under the "larger participant" rule. 12 U.S.C. §5514. This assignment has some references to the FTC as a matter of historical record, and because the FTC retains jurisdiction over the use of consumer reports for purposes other than consumer financial products or services (such as landlords or insurance companies). The FTC withdrew its Official Commentary on credit reporting when the CFPB gained responsibility, creating some uncertainty about how the CFPB will apply the law.

A. Content of Consumer Reports

1. Types of Reports

"Credit report," while common parlance, does not accurately describe the content and use of the reports. The law actually uses the more appropriate term "consumer report," 15 U.S.C. §1681a(d)(1), because the reports include

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communications about character, reputation, personal characteristics, and residence, as well as credit data. This definition is so broad that you might think every update or comment on a social network site is a consumer report. However, the law requires that a consumer report be "used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility" for credit or insurance, employment, or any other purpose authorized in FCRA. 15 U.S.C. §1681a(d)(1). It is the purpose of the report that contributes to the "credit report" moniker at least as much as its content.

The law distinguishes between ordinary consumer reports and "investigative" consumer reports. The latter are a subset of consumer reports in which information is "obtained through personal interviews with neighbors, friends, or associates" of the consumer, rather than "specific factual information" obtained from a creditor. 15 U.S.C. §1681a(e). Because of their more invasive process, consumers must be notified in writing within three days of a request for an investigative report. 15 U.S.C. §1681d.

Investigative reports are much less common than the more familiar consumer reports, generated most frequently by three credit reporting agencies: Equifax, Experian, and TransUnion. Over 200 million American adults have a file with these agencies.

2. Data Collected

A consumer report is "any written, oral, or other communication of any information by a consumer reporting agency bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living which is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for (A) credit or insurance to be used primarily for personal family, or household purposes, (B) employment purposes; or (C) any other purposes authorized under section 1681b of this title." 15 U.S.C. §1681a(d). The statute only applies to consumer reporting agencies, and only when such communications are for making certain decisions or for specified purposes. Without these restrictions, a consumer report would be the gossipy conversation around the holiday table about Great Uncle Jeb or Todd or Elmer and their latest shenanigans.

In general, a consumer report may contain any information that is complete, accurate, and not obsolete. When preparing reports, agencies are to follow procedures to assure "maximum possible accuracy." 15 U.S.C. §1681e(b). Furnishers also are required to have reasonable written procedures on the accuracy and integrity of data that they transmit to a consumer reporting agency. 12 C.F.R. §1022.40.

The typical consumer report contains several major categories of information. Most obviously, it includes personal identifiers such as name, current and former addresses, employer, date of birth, and social security number. This information is critical to making sure that information provided by furnishers is inserted into the file of the correct consumer and in providing users with the correct file for the requested person.

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The bulk of a report consists of account-level data for current and past creditors. Mortgages, credit cards, auto loans, student loans and bank lines-of-credit nearly always appear on credit reports. Other routine payments made by households such as rental or utility payments rarely appear, although this is changing as newer market entrants challenge the large actors to use a wider swath of information. The report will flag adverse accounts on which there have been late payments or other types of delinquencies.

Below is an excerpt of the account information from a TransUnion report, with the account numbers blacked out. The "x" marks indicate that information was not provided in certain months, often because there was no account balance or activity in those months. This report was obtained in late 2011; note the dates of some account information. Credit reports have a very long shelf life.

CITICARDS CBNA [redacted]

701 E 60TH ST N
SIOUX FALLS , SD 57104
Phone number not available

Balance:	$0	**Pay Status:**	Paid or Paying as Agreed
Date Updated:	10/2002	**Account Type:**	Revolving Account
Credit Limit:	$2,400	**Responsibility:**	Individual Account
Past Due:	$0	**Date Opened:**	11/1993
		Date Closed:	09/2002

Loan Type: Credit Card
Remark: Account closed by consumer

Late Payments 30 months: 30 – 0, 60 – 0, 90 – 0

Last 24 Months

OK	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	OK	OK	OK	OK
sep	aug	jul	jun	may	apr	mar	feb	'02	dec	nov	oct	sep	aug	jul	jun	may	apr	mar	feb	'01	dec	nov	oct

DIRECT LOAN SVC SYSTEM [redacted]

PO BOX 5609
GREENVILLE , TX 75403-5609
(800) 848-0979

Balance:	$0	**Pay Status:**	Paid or Paying as Agreed
Date Updated:	02/2011	**Account Type:**	Installment Account
High Balance:	$59,705	**Responsibility:**	Individual Account
Past Due:	$0	**Date Opened:**	07/2001
Terms:	$646 for 121 months	**Date Closed:**	02/2011

Loan Type: Student Loan
Remark: Closed

Late Payments 48 months: 30 – 0, 60 – 0, 90 – 0

Last 48 Months

OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK
'11	dec	nov	oct	sep	aug	jul	jun	may	apr	mar	feb	'10	dec	nov	oct	sep	aug	jul	jun	may	apr	mar	feb
OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	X	OK	OK	OK	OK	OK	OK
'09	dec	nov	oct	sep	aug	jul	jun	may	apr	mar	feb	'08	dec	nov	oct	sep	aug	jul	jun	may	apr	mar	feb

Credit reporting agencies also collect information that appears in public records. Examples here include lawsuits, tax liens, bankruptcies, and delinquent child support. If you have no public record section on your report, then that is a good sign as such information is always negative.

Reports also contain data on user inquiries and consumer statements. User inquiries are typically divided into two types. Regular inquiries are those created by a consumer, usually as a result of a consumer applying for loans or employment.

Promotional or account review inquiries are initiated by a creditor without consumer consent. They are used to make decisions about whether to extend credit or change credit terms. Consumer statements are items such as fraud alerts, discussed in Assignment 6 in relationship to identity theft, or other statements that the law permits consumers to require agencies to include in reports, as discussed in the next section.

The credit report system is refreshed on a near-constant basis. Each month the consumer reporting agencies add an estimated 4.5 billion pieces of

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information to their databases. Some of the information in a credit report is used to calculate credit scores, a numerical estimate of a consumer's credit risk. While there is one dominant player in the business of designing score algorithms, the Fair Isaac Co., and people speak of a FICO score to refer to that company, each of the big three credit reporting agencies use slightly different calculations for their scores. Creditors often have in-house algorithms as well, some of which are designed for a particular loan product, or are for more specialized purposes such as Experian and VISA's "BankruptcyPredict" score.

For FICO scores, the Fair Isaac Company says that five categories of information make the following relative contributions to a score: 1) payment history: 35 percent, 2) amounts owed: 30 percent, 3) length of credit history: 15 percent, 4) new credit: 10 percent, and 5) types of credit in use: 10 percent. For any given person and any particularized score, however, the weighting can be different. These different weightings, and many other details, are part of the proprietary "black box" of credit scoring. While companies often urge consumers to monitor their credit scores and aim for a high score, consumer advocates typically focus on the credit report because consumers can only indirectly affect the scores by changing the content of reports.

B. Uses of Credit Reports

The major motivation behind the enactment of FCRA was consumer privacy. To that end, FCRA limits the situations under which an agency may furnish a report. 15 U.S.C. §1681b. The simplest rule is that reports can be furnished "[i]n accordance with the written instructions of the consumer to whom it relates." 15 U.S.C. §1681b(a)(2). In most instances, there is tiny print somewhere in an application that a consumer signs that gives such permission. As with any standard form contract, this generally suffices as consent. Reports also can be obtained for use in several kinds of legal processes, including by grand jury subpoena, court order, or for use in child support enforcement. For the other categories of uses, the agency needs to possess "reason to believe" that a user has a permissible purpose. Users are forbidden from using reports provided by agencies unless the users have a permissible purpose, which is defined by reference back to the permissible purposes for agencies. 15 U.S.C. §1681b(f)(1). The most common purposes are discussed in detail below.

1. Credit

Consumer reports may be furnished and used "in connection with a credit transaction involving the consumer…involving the extension of credit to, or review or collection of an account of, the consumer." 15 U.S.C. §1681b(a)(3)(A). Credit is defined broadly. Other financial transactions are arguably not credit but get swept in under other permissible purposes. One example is a potential investor or insurer who wants to assess and value an

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existing credit obligation. That is, there is already a loan but the company is trying to sell the obligation, buy insurance against its default, or perhaps use it as collateral. These purposes require valuing the loan, which is driven by the borrower's creditworthiness, in part.

Several cases have looked at whether check verification services and merchants' uses of such services are covered by FCRA. In its commentary, the FTC had opined that "bad check lists" were consumer reports, and courts had followed that guidance. *Greenway v. Information Dynamics, Ltd.*, 399 F. Supp. 1092 (D. Ariz. 1974) (holding that lists with check cashing history of potential customers is a consumer report under the FCRA); *Peasley v. Telecheck of Kan., Inc.*, 6 Kan. App. 2d 990, 637 P.2d 437 (1981) (holding that check approval system is a consumer report under Kansas statute that is modeled after the FCRA). Courts had also grappled with whether checks are "extensions of credit" because checks are supposed to be good when written—the money should be in the bank. Some courts got around the issue by finding that payees had a "legitimate business need" to obtain a consumer report to decide whether to accept or reject a check in payment. *Estiverne v. Sak's Fifth Ave.*, 9 F.3d 1171 (5th Cir. 1993).

Once a creditor has made a loan, it can obtain consumer reports to monitor the account and reassess credit risk. After a review of the report, the creditor could change the rate, close the account, or extend additional credit, if such actions are permitted by the loan agreement.

Creditors can also use consumer reports to help them collect from delinquent consumers. In this process, called "skip tracing," the creditor primarily wants the debtor's address information, rather than data on creditworthiness (after all, the consumer is already delinquent—that's some powerful data right there). Some obligations did not begin as credit but fall into that category after a lawsuit is filed and a judgment against the consumer is obtained. At that point, a credit relationship exists, and the business can use a credit report to find the consumer.

2. Insurance

Credit reports may be obtained by users who "intend to use the information in connection with the underwriting of insurance involving the consumer." 15 U.S.C. §1681b(a)(3)(C). Consumer reports are used initially for underwriting but also on an ongoing basis for deciding whether to cancel a policy or adjust terms.

While insurance companies always have had access to credit reports, the practice of calculating and using scores for underwriting is controversial. In 2003, Congress directed the FTC to study the use of credit-based insurance scores and to report on how those scores were calculated and used, particularly their impact on low-income or minority consumers. In July 2007, the FTC issued a 250-page report, Credit-Based Insurance Scores: Impacts on Consumers of Automobile Insurance, focusing solely on auto insurance.

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> The FTC's analysis demonstrates that credit-based insurance scores are effective predictors of risk under automobile insurance policies. Using scores is likely to make the price of insurance conform more closely to the risk of loss that consumers pose, resulting, on average, in higher-risk consumers paying higher premiums and lower-risk consumers paying lower premiums. It has not been clearly established why scores are predictive of risk.
>
> Credit-based insurance scores may benefit consumers overall. Scores may permit insurance companies to evaluate risk with greater accuracy, which may make them more willing to offer insurance to higher-risk consumers. Scores also may make the process of granting and pricing insurance quicker and cheaper, cost savings that may be passed on to consumers in the form of lower premiums. However, little hard data was submitted or available to the FTC to quantify the magnitude of these potential benefits to consumers. Credit-based insurance scores are distributed differently among racial and ethnic groups. The FTC's analysis revealed that the use of scores for consumers whose information was included in the FTC's database caused the average predicted risk for African Americans and Hispanics to increase by 10% and 4.2%, respectively, while it caused the average predicted risk for non-Hispanic whites and Asians to decrease by 1.6% and 4.9%, respectively. These changes in predicted risk are likely to have an effect on the insurance premiums that these groups on average pay.
>
> Credit-based insurance scores predict risk within racial, ethnic, and income groups. Scores have only a small effect as a 'proxy' for membership in racial and ethnic groups in estimating of insurance risk, remaining strong predictors of risk when controls for race, ethnicity and income are included in risk models.

The FTC report drew sharp criticism, including a dissent from one commissioner. One major critique of the report was its reliance on limited industry-supplied data, and its failure to explain why it did not detect racial effects found in studies of consumers with insurance in Texas and Missouri. *See* Dissenting Statement of Commissioner Pamela Jones Harbour (July 2007), at www.ftc.gov/os/2007/07/P044804_facta_dissenting_harbour.pdf. In response to a class-action lawsuit that challenged the permissibility of credit-based scores for homeowner and auto insurance, the Texas Supreme Court upheld the Texas statute that permitted insurers to use scores that were race-neutral (in that they did not include race as a factor), even if the scores had a disparate racial impact on insurance pricing. *See Ojo, et al. v. Farmers Group et al.*, 256 S.W.3d 421 (Tex. 2011).

3. Employment

The Fair Credit Reporting Act says that employment is a permissible purpose for obtaining a consumer report. 15 U.S.C. §1681b(a)(3)(B). Employment purpose is defined to include both evaluations of applicants and of current employees for purposes of promotion, reassignment, or retention. For employment, the user should not procure the report unless it has made a "clear and conspicuous disclosure" to the consumer and obtained written authorization. 15 U.S.C. §1681b(b)(2)(A).

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Kelchner v. Sycamore Manor Health Center

135 Fed. Appx. 499 (3d Cir. 2005) (not precedential)

FUENTES, Circuit Judge.

Petitioner Lisa Kelchner appeals the District Court's order of partial summary judgment dismissing her claims under the Fair Credit Reporting Act, 15 U.S.C. §1681 et seq. ("FCRA" or "the Act"). The District Court held that Kelchner's employer, Sycamore Manor Health Center ("Sycamore"), did not violate the FCRA by requiring Kelchner to sign a blanket authorization entitling Sycamore to obtain Kelchner's credit report in the future. Because such blanket authorizations are not inconsistent with the requirements of the FCRA, we will affirm.

I.

As we write only for the parties, we recite only the essential facts. Kelchner had been employed at Sycamore for about nineteen years when, in February 2001, she and other employees of Sycamore's parent, Presbyterian Homes, Inc. (PHI), were asked to sign an "Annual Statement of Personnel Policy Understanding." [1] When Kelchner refused to sign the Annual Statement she was informed that execution of the Statement was a condition of continued employment and that if she failed to sign the Statement by March 21, 2000, she would be taken off the active schedule. Because she refused to sign, Kelchner's work hours were reduced to zero on March 21, 2001. Kelchner remained on the payroll, however, and on June 12, 2001, PHI sent her a second, revised Annual Statement to be signed by June 19, 2001. The revised Statement sought authorization to obtain "consumer reports" containing information relating to employees' "credit standing, character, general reputation, personal characteristics, or mode of living" for the purposes of investigating "theft from residents, coworkers, or PHI property; potential fraud in insurance claims; or other forms of dishonesty." Kelchner was warned that if she did not sign the revised Statement, PHI would deem her employment "abandoned." Kelchner again refused to sign and her employment at PHI ended on June 30, 2001.

Kelchner claimed that she was wrongfully terminated, and that a class of plaintiffs employed by PHI and its subsidiary Sycamore signed the authorization forms under duress due to threat of termination. The District Court held that blanket authorization forms such as those required by PHI are permissible under the FCRA and certified the issue for interlocutory appeal. Although it had earlier conditionally certified a plaintiffs class of all persons employed by PHI from whom PHI sought authorization to procure consumer reports, the District Court decertified the class when it granted partial summary judgment to the defendants on Kelchner's FCRA claims.

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II.

Kelchner claims that (1) PHI had no valid employment purpose for which it sought her credit report authorization; (2) PHI could not require Kelchner and other employees to sign a blanket, advance authorization form; and (3) that it was improper for PHI to constructively terminate Kelchner upon her refusal to sign the authorization form.[2]...

A.

The Fair Credit Reporting Act provides that, if certain conditions are met, credit reports may be issued to employers for "employment purposes." 15 U.S.C. §1681b(a)(3)(B). The FCRA defines "employment purposes" as those relating to "[evaluation of] a consumer for employment, promotion, reassignment or retention as an employee." 15 U.S.C. §1681a(h). Kelchner's first contention is that, because her retention as an employee was not in question, PHI had no valid employment purpose for procuring her credit report.

Kelchner is right that Congress implicitly recognized employees' privacy interest in avoiding procurement of their credit reports for invalid purposes. But PHI maintains that it needs access to employee credit reports in order to investigate theft, fraud and other dishonesty if and when it arises.[3] PHI claims that it newly imposed the requirement that its employees sign the credit report authorization forms in response to the allegedly broad scope of its protective and investigative duties as an employer, as well as new constraints on its access to information about employees under the FCRA. PHI is persuasive that its ability effectively to investigate allegations pertaining to an employee would be substantially impaired if it had to wait until the investigation was underway before it could obtain authorization from her.

It is important to note that PHI did not actually obtain a credit report on Kelchner. It sought authorization to do so in the future, if and when the need arose. While we do not foreclose the possibility that under certain circumstances an employer may have a valid employment purpose for which to obtain a credit report even before an employee is the subject of internal investigation, here, PHI sought only authorization to procure a report if and when the need arose, and the potential needs it identified clearly qualify as valid employment purposes.

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B.

Kelchner's second contention is that PHI was prohibited from procuring credit reports regarding its employees based on blanket, one-time authorization forms. Under the FCRA, an employer may obtain a credit report for employment purposes if "a clear and conspicuous disclosure has been made in writing to the consumer *at any time before the report is procured* or caused to be procured, in a document that consists solely of the disclosure, that a consumer report may be obtained for employment purposes; and the consumer has authorized in writing...the procurement of the report by that person." 15 U.S.C. §1681b(b)(2)(A)(i) (emphasis added). The consumer-employee must authorize disclosure in writing. See 15 U.S.C. §1681b(b)(2)(A)(ii).

The requirement that an employer obtain authorization "at any time before the report is procured" is unambiguous. The plain language of the statute authorizes the employer to obtain an employee's written authorization at "any time" during the employment relationship. See 15 U.S.C. §1681b(b)(2)(A)(i); see also Valansi v. Ashcroft, 278 F.3d 203, 209 (3d Cir. 2002) ("When the statutory language has a clear meaning, we need not look further.").

C.

We turn to Kelchner's final contention. Kelchner claims that employee authorization under 15 U.S.C. §1681b(b) must be voluntary in that it cannot be compelled as a condition of employment. However, we see nothing in the statute that implies such a limit on an employer's ability to obtain blanket authorization from an employee, at least in the context of an at-will employment relationship. But even if we were to view the statute as ambiguous on this point, we are persuaded by a 1999 advisory opinion letter issued by the FTC, which opined that the FCRA "does not prohibit an employer from taking adverse action against an employee or applicant who refuses to authorize the employer to procure a consumer report." Oct. 1, 1999, FTC Opinion Letter. See also Christensen v. Harris County, 529 U.S. 576, 587 (2000) (holding that an opinion letter by the administering agency is entitled to respect under Skidmore v. Swift & Co., 323 U.S. 134, 140 (1944)). In sum, we agree that an employer is not prohibited from terminating an employee if she refuses to authorize her employer to obtain her consumer credit report.

III.

For all the foregoing reasons, the District Court was clearly correct in its interpretation of the Act and the defendants were entitled to summary judgment on Kelchner's claims under the FCRA. We will affirm.

More employers in recent years are using credit reports and scores, although there remains no clear relationship between these data and employment behavior. In the last decade or so, several states have enacted laws that restrict the use of consumer reports for employment. As of late 2015, the states with restrictions on employer's access to or use of credit information were: California, Colorado, Connecticut, Hawaii, Illinois, Maryland, Nevada, Oregon, Vermont, and Washington. Bills are currently pending in about two dozen other states' legislatures. In the fall of 2015, New York City passed a strong local ordinance against employers' use of consumer reports.

> Except as provided in this subdivision, it shall be an unlawful discriminatory practice for an employer, labor organization, employment agency, or agent thereof to request or to use for employment purposes the consumer credit history of an applicant for employment or employee, or otherwise discriminate against an applicant or employee with regard to hiring, compensation, or the terms, conditions or privileges of employment based on the consumer credit history of the applicant or employee.

New York City Local Law Int. §261-A. The law has relatively few exceptions compared to the similar state bills. Momentum is gathering to prohibit credit checks on employees.

C. Decisions Based on Reports

1. Adverse Action Defined

"Adverse action" is a term of art under FCRA. It describes a decision that is deemed to be unfavorable to the consumer. It is defined separately for insurance, employment, and credit purposes. 15 U.S.C. §1681a(k)(1)(B)(i)-(iv). A denial later always constitutes adverse action, but the term is significantly broader than that, and includes an increase in cost or an otherwise unfavorable change in terms. That is not to suggest that every decision that differentiates among consumers is an adverse action. For example, being excluded from a marketing list constructed from consumer report data may not be an adverse action. After all, how many of us would view it as adverse to get less unsolicited marketing mail?

A vexing issue in the adverse action context has been the treatment of risk-based pricing, which includes granting credit or insurance on terms "materially less favorable than the most favorable terms available to a substantial proportion of consumers." 15 U.S.C. §1681m(h) (requiring notice to be given to a consumer for credit decisions meeting this standard). The Supreme Court recently assessed what constitutes an adverse action in the insurance context.

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Safeco Insurance Co. of America et al. v. Burr et al.

551 U.S. 47 (2007)

SOUTER, Justice.

The Fair Credit Reporting Act (FCRA or Act) requires notice to any consumer subjected to "adverse action…based in whole or in part on any information contained in a consumer [credit] report." 15 U.S.C. §1681m(a). Anyone who "willfully fails" to provide notice is civilly liable to the consumer. §1681n(a). The questions in these consolidated cases are whether willful failure covers a violation committed in reckless disregard of the notice obligation, and, if so, whether petitioners Safeco and GEICO committed reckless violations. We hold that reckless action is covered, that GEICO did not violate the statute, and that while Safeco might have, it did not act recklessly.

I.

A.

Congress enacted FCRA in 1970 to ensure fair and accurate credit reporting, promote efficiency in the banking system, and protect consumer privacy. See 84 Stat. 1128, 15 U.S.C. §1681; TRW Inc. v. Andrews, 534 U.S. 19, 23 (2001). The Act requires, among other things, that "any person [who] takes any adverse action with respect to any consumer that is based in whole or in part on any information contained in a consumer report" must notify the affected consumer. 15 U.S.C. §1681m(a). The notice must point out the adverse action, explain how to reach the agency that reported on the consumer's credit, and tell the consumer that he can get a free copy of the report and dispute its accuracy with the agency. Ibid. As it applies to an insurance company, "adverse action" is "a denial or cancellation of, an increase in any charge for, or a reduction or other adverse or unfavorable change in the terms of coverage or amount of, any insurance, existing or applied for." §1681a(k)(1)(B)(i).

FCRA provides a private right of action against businesses that use consumer reports but fail to comply. If a violation is negligent, the affected consumer is entitled to actual damages. If willful, however, the consumer may have actual damages, or statutory damages ranging from \$100 to \$1,000, and even punitive damages. §1681n(a).

B.

Petitioner GEICO writes auto insurance through four subsidiaries: GEICO General, which sells "preferred" policies at low rates to low-risk customers; Government Employees, which also sells "preferred" policies, but only to government employees; GEICO Indemnity, which sells standard policies to moderate-risk customers; and GEICO Casualty, which sells nonstandard policies at higher rates to high-risk customers. Potential customers call a toll-free number answered by an agent of the four affiliates, who takes information and, with permission, gets the applicant's credit score. This information goes into GEICO's computer system, which

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selects any appropriate company and the particular rate at which a policy may be issued.

For some time after FCRA went into effect, GEICO sent adverse action notices to all applicants who were not offered "preferred" policies from GEICO General or Government Employees. GEICO changed its practice, however, after a method to "neutralize" an applicant's credit score was devised: the applicant's company and tier placement is compared with the company and tier placement he would have been assigned with a "neutral" credit score, that is, one calculated without reliance on credit history.[4] Under this new scheme, it is only if using a neutral credit score would have put the applicant in a lower priced tier or company that GEICO sends an adverse action notice; the applicant is not otherwise told if he would have gotten better terms with a better credit score.

Respondent Ajene Edo applied for auto insurance with GEICO. After obtaining Edo's credit score, GEICO offered him a standard policy with GEICO Indemnity (at rates higher than the most favorable), which he accepted. Because Edo's company and tier placement would have been the same with a neutral score, GEICO did not give Edo an adverse action notice. Edo later filed this proposed class action against GEICO, alleging willful failure to give notice in violation of §1681m(a); he claimed no actual harm, but sought statutory and punitive damages under §1681n(a). The District Court granted summary judgment for GEICO, finding there was no adverse action when "the premium charged to [Edo]…would have been the same even if GEICO Indemnity did not consider information in [his] consumer credit history." Edo v. GEICO Casualty Co., 2004 U.S. Dist. LEXIS 28522, *12 (D. Ore., Feb. 23, 2004).

Like GEICO, petitioner Safeco relies on credit reports to set initial insurance premiums, as it did for respondents Charles Burr and Shannon Massey, who were offered higher rates than the best rates possible. Safeco sent them no adverse action notices, and they later joined a proposed class action against the company, alleging willful violation of §1681m(a) and seeking statutory and punitive damages under §1681n(a). The District Court ordered summary judgment for Safeco, on the understanding that offering a single, initial rate for insurance cannot be "adverse action."

The Court of Appeals for the Ninth Circuit reversed both judgments. In GEICO's case, it held that whenever a consumer "would have received a lower rate for his insurance had the information in his consumer report been more favorable, an adverse action has been taken against him." Reynolds v. Hartford Financial Servs. Group, Inc., 435 F.3d 1081, 1093 (2006). Since a better credit score would have placed Edo with GEICO General, not GEICO Indemnity, the appeals court held that GEICO's failure to give notice was an adverse action.

The Ninth Circuit also held that an insurer "willfully" fails to comply with FCRA if it acts with "reckless disregard" of a consumer's rights under the Act. Id., at 1099. It explained that a company would not be acting recklessly if it "diligently and in good faith attempted to fulfill its statutory obligations" and came to a "tenable, albeit erroneous, interpretation of the statute." Ibid. The court went on to say that "a deliberate failure to determine the extent of its obligations" would not ordinarily escape liability under §1681n, any more than "reliance on creative lawyering that provides indefensible answers." Ibid. Because the court believed that the enquiry into GEICO's reckless disregard might turn on undisclosed circumstances surrounding GEICO's revision of its notification policy, the Court of Appeals remanded the company's case for further proceedings.

In the action against Safeco, the Court of Appeals rejected the District Court's position, relying on its reasoning in GEICO's case (where it had held that the notice requirement applies to a single statement of an initial charge for a new policy). Spano v. Safeco Corp., 140 Fed. Appx. 746 (2005). The Court of Appeals also rejected Safeco's argument that its conduct was not willful, again citing the GEICO case, and remanded for further proceedings.

We consolidated the two matters and granted certiorari to resolve a conflict in the Circuits as to whether §1681n(a) reaches reckless disregard of FCRA's obligations, and to clarify the notice requirement in §1681m(a). We now reverse in both cases.

II.

GEICO and Safeco argue that liability under §1681n(a) for "willfully fail[ing] to comply" with FCRA goes only to acts known to violate the Act, not to reckless disregard of statutory duty, but we think they are wrong. We have said before that "willfully" is a "word of many meanings whose construction is often dependent on the context in which it appears," Bryan v. United States, 524 U.S. 184, 191 (1998) (internal quotation marks omitted); and where willfulness is a statutory condition of civil liability, we have generally taken it to cover not only knowing violations of a standard, but reckless ones as well, see McLaughlin v. Richland Shoe Co., 486 U.S. 128, 132–133 (1988) ("willful," as used in a limitation provision for actions under the Fair Labor Standards Act, covers claims of reckless violation)…The standard civil usage thus counsels reading the phrase "willfully fails to comply" in §1681n(a) as reaching reckless FCRA violations, and this is so both on the interpretive assumption that Congress knows how we construe statutes and expects us to run true to form, see Commissioner v. Keystone Consol. Industries, Inc., 508 U.S. 152, 159 (1993), and under the general rule that a common law term in a statute comes with a common law meaning, absent anything pointing another way, Beck v. Prupis, 529 U.S. 494, 500–501 (2000).

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III.

A.

Before getting to the claims that the companies acted recklessly, we have the antecedent question whether either company violated the adverse action notice requirement at all. In both cases, respondent-plaintiffs' claims are premised on initial rates charged for new insurance policies, which are not "adverse" actions

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unless quoting or charging a first-time premium is "an increase in any charge for…any insurance, existing or applied for." 15 U.S.C. §1681a(k)(1)(B)(i).

In Safeco's case, the District Court held that the initial rate for a new insurance policy cannot be an "increase" because there is no prior dealing. The phrase "increase in any charge for…insurance" is readily understood to mean a change in treatment for an insured, which assumes a previous charge for comparison. See Webster's New International Dictionary 1260 (2d ed. 1957) (defining "increase" as "[a]ddition or enlargement in size, extent, quantity, number, intensity, value, substance, etc.; augmentation; growth; multiplication"). Since the District Court understood "increase" to speak of change just as much as of comparative size or quantity, it reasoned that the statute's "increase" never touches the initial rate offer, where there is no change.

The Government takes the part of the Court of Appeals in construing "increase" to reach a first-time rate. It says that regular usage of the term is not as narrow as the District Court thought: the point from which to measure difference can just as easily be understood without referring to prior individual dealing. The Government gives the example of a gas station owner who charges more than the posted price for gas to customers he doesn't like; it makes sense to say that the owner increases the price and that the driver pays an increased price, even if he never pulled in there for gas before. See Brief for United States as Amicus Curiae 26. The Government implies, then, that reading "increase" requires a choice, and the chosen reading should be the broad one in order to conform to what Congress had in mind.

We think the Government's reading has the better fit with the ambitious objective set out in the Act's statement of purpose, which uses expansive terms to describe the adverse effects of unfair and inaccurate credit reporting and the responsibilities of consumer reporting agencies. See §1681(a) (inaccurate reports "directly impair the efficiency of the banking system"; unfair reporting methods undermine public confidence "essential to the continued functioning of the banking system"; need to "insure" that reporting agencies "exercise their grave responsibilities" fairly, impartially, and with respect for privacy). The descriptions of systemic problem and systemic need as Congress saw them do nothing to suggest that remedies for consumers placed at a disadvantage by unsound credit ratings should be denied to first-time victims, and the legislative histories of FCRA's original enactment and of the 1996 amendment reveal no reason to confine attention to customers and businesses with prior dealings. Quite the contrary. Finally, there is nothing about insurance contracts to suggest that Congress might have meant to differentiate applicants from existing customers when it set the notice requirement; the newly insured who gets charged more owing to an erroneous report is in the same boat with the renewal applicant.[12] We therefore hold that the "increase" required for "adverse action," 15 U.S.C. §1681a(k)(1)(B)(i), speaks to a disadvantageous rate even with no prior dealing; the term reaches initial rates for new applicants.

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B.

Although offering the initial rate for new insurance can be an "adverse action," respondent-plaintiffs have another hurdle to clear, for §1681m(a) calls for notice only when the adverse action is "based in whole or in part on" a credit report. GEICO argues that in order to have adverse action "based on" a credit report, consideration of the report must be a necessary condition for the increased rate. The Government and respondent-plaintiffs do not explicitly take a position on this point.

To the extent there is any disagreement on the issue, we accept GEICO's reading. In common talk, the phrase "based on" indicates a but-for causal relationship and thus a necessary logical condition. Under this most natural reading of §1681m(a), then, an increased rate is not "based in whole or in part on" the credit report unless the report was a necessary condition of the increase.

As before, there are textual arguments pointing another way. The statute speaks in terms of basing the action "in part" as well as wholly on the credit report, and this phrasing could mean that adverse action is "based on" a credit report whenever the report was considered in the rate-setting process, even without being a necessary condition for the rate increase. But there are good reasons to think Congress preferred GEICO's necessary-condition reading.

If the statute has any claim to lucidity, not all "adverse actions" require notice, only those "based…on" information in a credit report. Since the statute does not explicitly call for notice when a business acts adversely merely after consulting a report, conditioning the requirement on action "based…on" a report suggests that the duty to report arises from some practical consequence of reading the report, not merely some subsequent adverse occurrence that would have happened anyway. If the credit report has no identifiable effect on the rate, the consumer has no immediately practical reason to worry about it (unless he has the power to change every other fact that stands between himself and the best possible deal); both the company and the consumer are just where they would have been if the company had never seen the report.[13] And if examining reports that make no difference was supposed to trigger a reporting requirement, it would be hard to find any practical point in imposing the "based…on" restriction. So it makes more sense to suspect that Congress meant to require notice and prompt a challenge by the consumer only when the consumer would gain something if the challenge succeeded.

C.

To sum up, the difference required for an increase can be understood without reference to prior dealing (allowing a first-time applicant to sue), and considering the credit report must be a necessary condition for the difference. The remaining step in determining a duty to notify in cases like these is identifying the benchmark for determining whether a first-time rate is a disadvantageous increase. And in dealing with this issue, the pragmatic reading of “based…on” as a condition necessary to make a practical difference carries a helpful suggestion.

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The Government and respondent-plaintiffs argue that the baseline should be the rate that the applicant would have received with the best possible credit score, while GEICO contends it is what the applicant would have had if the company had not taken his credit score into account (the "neutral score" rate GEICO used in Edo's case). We think GEICO has the better position, primarily because its "increase" baseline is more comfortable with the understanding of causation just discussed, which requires notice under §1681m(a) only when the effect of the credit report on the initial rate offered is necessary to put the consumer in a worse position than other relevant facts would have decreed anyway. If Congress was this concerned with practical consequences when it adopted a "based…on" causation standard, it presumably thought in equally practical terms when it spoke of an "increase" that must be defined by a baseline to measure from. Congress was therefore more likely concerned with the practical question whether the consumer's rate actually suffered when the company took his credit report into account than the theoretical question whether the consumer would have gotten a better rate with perfect credit.

The Government objects that this reading leaves a loophole, since it keeps first-time applicants who actually deserve better-than-neutral credit scores from getting notice, even when errors in credit reports saddle them with unfair rates. This is true; the neutral-score baseline will leave some consumers without a notice that might lead to discovering errors. But we do not know how often these cases will occur, whereas we see a more demonstrable and serious disadvantage inhering in the Government's position.

Since the best rates (the Government's preferred baseline) presumably go only to a minority of consumers, adopting the Government's view would require insurers to send slews of adverse action notices; every young applicant who had yet to establish a gilt-edged credit report, for example, would get a notice that his charge had been "increased" based on his credit report. We think that the consequence of sending out notices on this scale would undercut the obvious policy behind the notice requirement, for notices as common as these would take on the character of formalities, and formalities tend to be ignored. It would get around that new insurance usually comes with an adverse action notice, owing to some legal quirk, and instead of piquing an applicant's interest about the accuracy of his credit record, the commonplace notices would mean just about nothing and go the way of junk mail. Assuming that Congress meant a notice of adverse action to get some attention, we think the cost of closing the loophole would be too high.…

IV.

A.

In GEICO's case, the initial rate offered to Edo was the one he would have received if his credit score had not been taken into account, and GEICO owed him no adverse action notice under §1681m(a).

B.

Safeco did not give Burr and Massey any notice because it thought §1681m(a) did not apply to initial applications, a mistake that left the company in violation of the

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statute if Burr and Massey received higher rates "based in whole or in part" on their credit reports; if they did, Safeco would be liable to them on a showing of reckless conduct (or worse). The first issue we can forget, however, for although the record does not reliably indicate what rates they would have obtained if their credit reports had not been considered, it is clear enough that if Safeco did violate the statute, the company was not reckless in falling down in its duty....Here, there is no need to pinpoint the negligence/recklessness line, for Safeco's reading of the statute, albeit erroneous, was not objectively unreasonable. As we said, §1681a(k)(1)(B)(i) is silent on the point from which to measure "increase." On the rationale that "increase" presupposes prior dealing, Safeco took the definition as excluding initial rate offers for new insurance, and so sent no adverse action notices to Burr and Massey. While we disagree with Safeco's analysis, we recognize that its reading has a foundation in the statutory text, and a sufficiently convincing justification to have persuaded the District Court to adopt it and rule in Safeco's favor.

This is not a case in which the business subject to the Act had the benefit of guidance from the courts of appeals or the Federal Trade Commission (FTC) that might have warned it away from the view it took. Before these cases, no court of appeals had spoken on the issue, and no authoritative guidance has yet come from the FTC...Given this dearth of guidance and the less-than-pellucid statutory text, Safeco's reading was not objectively unreasonable, and so falls well short of raising the "unjustifiably high risk" of violating the statute necessary for reckless liability.

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The Court of Appeals correctly held that reckless disregard of a requirement of FCRA would qualify as a willful violation within the meaning of §1681n(a). But there was no need for that court to remand the cases for factual development. GEICO's decision to issue no adverse action notice to Edo was not a violation of §1681m(a), and Safeco's misreading of the statute was not reckless. The judgments of the Court of Appeals are therefore reversed in both cases, which are remanded for further proceedings consistent with this opinion.

Justice STEVENS, with whom Justice GINSBURG joins, concurring in part and concurring in the judgment.

While I join the Court's judgment and Parts I, II, III-A, and IV-B of the Court's opinion, I disagree with the reasoning in Parts III-B and III-C, as well as with Part IV-A, which relies on that reasoning.

An adverse action taken after reviewing a credit report "is based in whole or in part on" that report within the meaning of 15 U.S.C. §1681m(a). That is true even if the company would have made the same decision without looking at the report, because what the company actually did is more relevant than what it might have done. I find nothing in the statute making the examination of a credit report a "necessary condition" of any resulting increase. The more natural reading is that reviewing a report is only a sufficient condition.

The Court's contrary position leads to a serious anomaly. As a matter of federal law, companies are free to adopt whatever "neutral" credit scores they want. That score need not (and probably will not) reflect the median consumer credit score. More likely, it will reflect a company's assessment of the creditworthiness of a run-of-the-mill applicant who lacks a credit report. Because those who have yet to develop a credit history are unlikely to be good credit risks, "neutral" credit scores

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will in many cases be quite low. Yet under the Court's reasoning, only those consumers with credit scores even lower than what may already be a very low "neutral" score will ever receive adverse action notices.

While the Court acknowledges that "the neutral-score baseline will leave some consumers without a notice that might lead to discovering errors," it finds this unobjectionable because Congress was likely uninterested in "the theoretical question of whether the consumer would have gotten a better rate with perfect credit." The Court's decision, however, disserves not only those consumers with "gilt-edged credit report[s]," but also the much larger category of consumers with better-than-"neutral" scores. I find it difficult to believe that Congress could have intended for a company's unrestrained adoption of a "neutral" score to keep many (if not most) consumers from ever hearing that their credit reports are costing them money. In my view, the statute's text is amenable to a more sensible interpretation.

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2. Duties if Adverse Action Is Taken

Taking adverse action triggers duties for a user. The user must inform the consumer of the adverse action and provide the contact information for the agency that the user relied upon. 15 U.S.C. §1681m(a). The user also must tell the consumer that she has a right to obtain a free copy of the consumer report used in making the decision to take adverse action and that the consumer has a right to dispute the accuracy or completeness of any information in a consumer report furnished by the agency. These disclosures can be made orally, written, or by electronic means. These rules apply to adverse actions taken for all permissible purposes, including insurance, employment, and credit.

For credit transactions for personal, family, or household use, if the creditor relied on information other than from a consumer reporting agency, additional disclosures are required. 15 U.S.C. §1681m(b). The most important of these is that the consumer has a right to request the reason for the adverse action. The consumer has 60 days to make such a request. Upon its receipt, the user must provide the reasons within a reasonable time.

If a user of a report takes an adverse action or makes a risk-based pricing decision, the user must notify the consumer of the actual credit score used in making the decision. 15 U.S.C. §1681m(a)(2) and (h)(5)(E).

D. Accuracy in Credit Reporting

1. Detecting Errors

Given their widespread use and potential consequences, inaccuracies in consumer reports are a serious concern. As one advocate told Congress, "a poor

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credit history is the 'Scarlet Letter' of 20th century America." Fair Credit Reporting Act: How It Functions for Consumers and the Economy: Hearing Before the Subcomm. on Fin. Inst. and Consumer Credit of the H. Comm. On Fin. Servs., 108th Cong. (2003) (statement of Anthony Rodriguez, Staff Attorney, National Consumer Law Center.)

Amendments to FCRA frequently have been motivated by concern about accuracy but empirical estimates of the degree and nature of the problem vary. In 2012, the FTC had 1,000 consumers review their reports from one or more consumer reporting agencies. It found that one in four consumers identified errors on their credit reports that might affect their credit scores. When consumers disputed the information, 80 percent had some modification to their credit reports. Most of these errors did not change consumers' credit scores. However, about one in ten consumers saw a change in their credit score after the disputed information was changed. Most changes were small, but 5 percent of consumers had a score change of more than 25 points. FTC Report to Congress under §310 of the Fair and Accurate Credit Transactions Act of 2002 (2012), https://www.ftc.gov/sites/default/files/documents/reports/section-319-fair-and-accurate-credit-transactions-act-2003-fifth-interim-federal-trade-commission/130211factareport.pdf. Other estimates or errors have been much higher, although these studies are dated. A 2004 study of over 150 consumer files found errors in 79 percent of reports; 25 percent of those were significant enough to cause a potential denial of credit. *See* Alison Cassidy, and Edmund Mierzwinski, *Mistakes Do Happen: A Look at Errors in Consumer Credit Reports*, U.S. PIRG (June 2004). Errors can go in either direction, with the missing or incorrect information either being positive or negative about consumers' past actions. Errors of omission are a particular concern for consumers trying to improve a score. One study found that 78 percent of files were missing a revolving account that was in good standing, and 31 percent of files were missing a mortgage account that had never been delinquent. *See* Consumer Federation of America & National Credit Reporting Ass'n, *Credit Score Accuracy and Implications for Consumers* (Dec., 17, 2002) at http://www.consumerfed.org/pdfs/121702CFA_NCRA_Credit_Score_Report_Final.pdf.

The disparate results of the studies are likely the result of differences in defining what constitutes an inaccuracy, how serious of an inaccuracy is a cause for concern, and improvements in accuracy over time. Even with relatively low percentages of errors, however, the numbers become meaningful. Just a 1 percent error rate would still mean 2 million affected consumers, a large scale problem for law and policy to address.

Several types of errors are of concern. One is that information is added to a report that does not belong to the identified consumer. While this can indicate identity theft, it also results from similar or identical names. A related problem is an agency sending a user a report that may be correct in all its contents, but it is the report of a different person than the person of interest to the user. The major problem is inaccurate information, a category that includes information that is incorrect, information that is incomplete, and information that is missing.

In a follow-up study by the FTC to its 2012 report, the consumers who had completed the FCRA dispute process were provided with new credit reports and

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credit scores in 2014. The new credit reports were then compared to the old reports to assess whether the consumer reporting agencies had modified the reports in response to the disputes. The FTC looked at the "reinsertion rate," meaning the frequency with which previously removed negative information reappeared on a credit report. It found that 70 percent of consumers believed that at least one piece of previously disputed information remained inaccurate. FTC Report to Congress under Section 310 of the Fair and Accurate Credit Transactions Act of 2002 (2015), https://www.ftc.gov/system/files/documents/reports/section-319-fair-accurate-credit-transactions-act-2003-sixth-interim-final-report-federal-trade/150121factareport.pdf.

A key step to improving accuracy is getting consumers to review their reports and to detect errors. To do so, consumers first must obtain their reports. In addition to the disclosure of reports in adverse actions discussed above, FCRA requires "nationwide" agencies to provide consumers with a free copy of their reports one time each year, upon the consumers' requests. This rule effectively means that consumers could make an inquiry every four months, rotating the three major agencies, allowing them to keep fairly close tabs on their reports. The law requires a centralized process for making this request, and the big three agencies operate a website, www.annualcreditreport.com, and a toll-free telephone number for so doing. The free annual credit report does not include the consumer's credit score, giving rise to a thriving trade in selling credit scores and credit monitoring products to consumers. Visit www.freecreditreport.com for an example of such a business.

The second step in improving accuracy is reviewing the included information. The law constrains what may be in the report. 15 U.S.C. §1681c. Even if the information is permissible, it may be inaccurate. Before 1996 when Congress amended FCRA, there were no legal obligations on businesses who furnished information to consumer reporting agencies. A furnisher now has a legal obligation to avoid furnishing any information that it "knows or has reasonable cause to believe is inaccurate." 15 U.S.C. §1681s-2(a)(1). One way a furnisher may learn such information is inaccurate is if a consumer provides it with notice at the furnisher's specified address. However, a furnisher does not have reasonable cause to believe the information is inaccurate solely because of a consumer's allegations. A furnisher who receives notice that a consumer disputes information must pass along the existence of a dispute when it furnishes further information to the consumer reporting agency.

While there is no obligation for any particular business to supply a credit reporting agency with information, once a company does so, it takes on additional obligations under FCRA. Those who "regularly and in the ordinary course of business furnishes information to one or more consumer reporting agencies…and determine [such information] is not complete or accurate, shall promptly notify the consumer reporting agency of that determination and provide to the agency any corrections to that information.…" 15 U.S.C. §1681s-2(a)(2). Furnishers who regularly provide data also must notify credit reporting agencies of the voluntary closure of an account by a consumer. Consumers often rely on their credit reports to verify that a business has closed their account and may be concerned that a failure to report an account as closed lowers a credit score by suggesting access to credit that does not exist. Furnishers that are financial institutions have an additional duty. They must

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notify consumers in writing if they supply negative information to an agency. 15 U.S.C. §1681s-2(a)(7).

Agencies also have a duty to use reasonable procedures to ensure "maximum possible accuracy." 15 U.S.C. §1681e(b). The most commonly used measure of reasonableness that courts have used is a balancing test that weighs "the potential that the information will create a misleading impression against the availability of more accurate information and the burden of providing such information." *Wilson v. Rental Research Serv., Inc.*, 165 F.3d 642 (8th Cir. 1999).

These legal obligations have little meaning unless they are enforced. Under current law, errors do not result in liability. In 2014, the CFPB began to require that major consumer reporting agencies provide "regular accuracy" reports that identify furnishers with the largest number of consumer disputes. This will provide insight into which furnishers, or type of industries that furnish data, are more likely to contribute inaccurate or disputed data.

2. Disputing Information

When consumers believe inaccurate information is in their consumer reports, they can take two actions. First, they can initiate a dispute with the consumer reporting agency that keeps the report. Upon notification of a dispute, the law mandates that the agency "shall, free of charge, conduct a reasonable reinvestigation to determine whether the disputed information is inaccurate and record the current status of the disputed information, or delete the item." The agency has 30 days from receipt of the notice of dispute to conduct its reinvestigation. 15 U.S.C. §1681i(a)(1)(A). (By the way, it is a mystery why it is called a "reinvestigation" because this can be the first investigation of the matter; perhaps the idea is that the consumer has already asked the data furnisher to take action, although the law does not require this.) The agency has five business days from receipt of the consumer's notice to inform the furnisher of the dispute. The agency should pass along all relevant information it received from the consumer about the nature of the dispute. 15 U.S.C. §1681i(a)(2)(A).

Upon review of the dispute notice, the agency may determine that the dispute is "frivolous or irrelevant" and refuse to conduct a reinvestigation. 15 U.S.C. §1681i(a)(3). If it does so, it must tell the consumer of its determination within five business days. The agency also has the option of simply deleting the disputed information; this choice also lets it avoid conducting a reinvestigation. 15 U.S.C. §1681i(a)(1)(A). Note though that deletion of incorrect information may be less helpful to a consumer than correcting information and leaving it in the report. This is particularly true for those with a "thin" file with little information.

If the agency does reinvestigate, it must provide written notice to the consumer of the results. The communication should be sent within 5 business days of completing the reinvestigation and contain the following information:

> (i) a statement that the reinvestigation is completed;

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> (ii) a consumer report that is based upon the consumer's file as that file is revised as a result of the reinvestigation;
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> (iii) a notice that, if requested by the consumer, a description of the procedure used to determine the accuracy and completeness of the information shall be provided to the consumer by the agency, including the business name and address of any furnisher of information contacted in connection with such information and the telephone number of such furnisher, if reasonably available;
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> (iv) a notice that the consumer has the right to add a statement to the consumer's file disputing the accuracy or completeness of the information; and
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> (v) a notice that the consumer has the right to request under subsection (d) that the consumer reporting agency furnish notifications under that subsection.

15 U.S.C. §1681i(a)(6). If its reinvestigation leads the agency to conclude that the information is inaccurate, incomplete, or unverifiable, it must promptly delete or modify that information as appropriate and notify the furnisher of the disputed information of its actions. 15 U.S.C. §1681i(a)(5). Agencies must have procedures to prevent the reappearance of the inaccurate information on the report. For example, the agency must have a certification from the furnisher that the information is complete

and accurate before it can reinsert deleted disputed data. 15 U.S.C. §1681i(a)(5)(B). To prevent the problem from appearing with another consumer reporting agency, the furnisher also has to update the information with all other consumer reporting agencies to which the person furnished the information.

A second avenue for a consumer concerned about inaccurate information is to dispute the information directly with the furnisher, rather than with the agency. To do so, the consumer needs to contact the furnisher at a specified address, explain the basis for the dispute, and include all supporting documentation "required by the furnisher to substantiate the basis of the dispute." 15 U.S.C. §1681s-2(a)(8). This last requirement can be difficult because the consumer may feel that the furnisher is the party in possession of the information to disprove the accuracy of the information. FCRA provides that furnishers can essentially ignore a dispute if it "reasonably determines that the dispute is frivolous or irrelevant" and that failure to provide sufficient information can be the basis for such a determination. 15 U.S.C. §1681s-2(a)(8)(F)(i).

Upon receipt of a dispute, a furnisher has an obligation to conduct an investigation that includes a review of all relevant information provided by the consumer. This investigation must be completed within 30 days and its results reported to the consumer. If the furnisher found an inaccuracy, it must provide the credit reporting agency with information to correct the data. Crucially, there is not a private right of action against a furnisher for failure to comply with the dispute provisions.

The CFPB can bring enforcement actions, however, and has taken some initiatives in this area. For example, the CFPB urged credit card companies to provide free credit scores on monthly bills. It also issued a prominent report showing that half of delinquent/collection items on credit reports are medical debts. In response, the New York Attorney General reached an agreement with the three major consumer reporting agencies to change how they record and

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update medical debt. NPR, *Credit Agencies Agree to Wait Before Adding Medical Debt to Ratings* (March 3, 2015).

3. Credit Repair

The growth in the credit reporting industry has been paralleled by the rise of businesses that claim to help consumers improve their credit. The vast majority of these companies provide little benefit, beyond instructing the consumer how to dispute inaccurate information. In most instances, the only "cure" for bad credit is time.

To address abuses, the Credit Repair Organizations Act, 15 U.S.C. §1679-1679j, regulates credit repair businesses. It gives consumers three days to rescind a contract for credit repair and mandates a notice of this right to cancel. The statute also prohibits credit repair businesses from false or misleading practices, which presumably were already prohibited by the federal and state unfair and deceptive acts. The law does provide for the greater of actual damages or the amount paid to the business, as well as punitive damages. Few suits seem to be filed, however, despite the fact that a quick search of the Internet reveals dozens of companies offering dubious services, many starting at just $49 per month for the first year.

E. Enforcement for FCRA Violations

In addition to dispute provisions, other types of FCRA violations can give rise to both public and private actions. If a violation of FCRA constituted an unfair, deceptive, or abusive practice under a Consumer Financial Protection Bureau rule or an unfair or deceptive practice under state law, the Consumer Financial Protection Bureau or the state attorneys general could bring enforcement proceedings. Public enforcement is crucial in the context of FCRA because private liability actions face some obstacles. First, as discussed above in *Safeco Insurance v. Burr*, there are two recovery provisions: willful noncompliance (§1681n) and negligent noncompliance (§1681o). With willful noncompliance, recovery includes actual damages of not less than $100 and not more than $1,000, punitive damages, court costs, and reasonable attorney's fees. Negligent noncompliance differs in that liability is for "actual damages" without reference to a dollar cap and that punitive damages are unavailable. The problem is that the statutory damages are low (for willful noncompliance) and actual damages can be nonexistent or hard to prove (for negligent noncompliance). Second, it can be difficult to show negligence in any given case. Because several of the substantive provisions of FCRA require parties to have "reasonable procedures," the mere failure to comply with the statute can be overcome by showing procedures were in place that reasonably should have resulted in compliance. Third, FCRA preempted common law actions that were used before its enactment, including defamation, invasion of privacy, and negligence. 15 U.S.C. §1681h(e). These are specific concerns to FCRA, in addition

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to the general issues with private enforcement of consumer law that are the subject of Assignment 24, *infra*.

Problem Set 7

7.1. Harold Weckerly has been feeling old lately, perhaps because he just celebrated his 92nd birthday. His relatives fuss over him constantly and give him unsolicited advice. One of his grandchildren, Marcus, recently "helped" Harold obtain his credit report and is trying to get Harold worked up about its contents. Along with Harold's one active account, a credit card that another grandchild insisted that he needed, the report shows the following: 1) a bankruptcy dated eight years ago; 2) a foreclosure dated seven years ago; 3) a mortgage account that was closed seven years ago while in delinquent status; 4) a revolving account with Sears that was opened in 1971 and closed in 1982, shown paid up in full and closed by consumer; and 5) a criminal conviction for disturbing the peace from 1942 just before Harold entered the Army. Harold has told Marcus that these entries are all accurate, saying that the entries are explained, respectively, by a gambling problem he had a few years ago that led to him telling his relatives that he "sold" his vacation home, his desire for new kitchen appliances in avocado green in the 1970s, and his being a bit of a wild one in his younger years before he got straightened out by World War II. Marcus continues to insist that Harold's character is being unfairly impugned by the consumer reporting agency. Harold has no intention of initiating a dispute. He wonders though if Marcus could be kept occupied by researching the situation, giving him the satisfaction of providing more unwanted "help." Should Harold's report contain the five items listed above? *See* 15 U.S.C. §1681c.

7.2. AutoBarn is a used car dealer specializing in high-mileage hybrid vehicles. It prides itself on its service, promising customers they can complete a car purchase in one hour from when they walk onto the lot. To expedite the process, AutoBarn has a consumer complete a short data form asking for name, address, date of birth, and last four digits of social security number, before it will allow a consumer to take a car out for a test drive. The form also asks the consumer to rate, at that time, the consumer's level of interest from five (very interested) to one (not interested) in closing a sale using Autobarn's "One Hour to Hybrid Happiness" process and contains a place for the consumer's signature. If a consumer indicates a four or five for interest level and signs the form, an employee starts filling out the purchase and financing paperwork, including requesting a credit report and score from a consumer reporting agency, while the consumer is doing the test drive. When the consumer returns, the employee asks the consumer if they wish to purchase the car, and if so, presents them with the partially-complete paperwork, including a finance package for consideration. Does AutoBarn violate FCRA in its practices? *See* 15 U.S.C. §1681b; 1681e(d); 1681m.

7.3. InsureAll is a new entrant to the consumer reporting business. It collects similar data from similar furnishers as do the other large consumer reporting agencies but its business exclusively serves insurance companies as users. InsureAll provides a free copy of their reports to consumers who make a request via a website and toll-free number.

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InsureAll recently received a request from a consumer, Kristine Leung, for a copy of her credit score. InsureAll wrote back it would provide Kristine with her score if she submitted $25. Kristine did so, and received back a short message, stating: "As of the date of this response, the InsureAll RiskScore of Kristine Leung is JJ." Kristine has emailed you, the lawyer who handled her divorce, to ask for your help in understanding this score. What do you tell her? *See* 15 U.S.C. §1681g(c); 15 U.S.C. §1681g(f).

7.4. You are a policy analyst for a presidential candidate. A congressperson has introduced the following bill:

Employment for All Act

(1) GENERAL PROHIBITION—Except as provided in paragraph (3), a person, including a prospective employer or current employer, may not use a

consumer report or investigative consumer report, or cause a consumer report or investigative consumer report to be procured, with respect to any consumer where any information contained in the report bears on the consumer's creditworthiness, credit standing, or credit capacity for employment purposes.

(2) SOURCE OF CONSUMER REPORT IRRELEVANT—The prohibition described in paragraph (1) shall apply even if the consumer consents or otherwise authorizes the procurement or use of a consumer report for employment purposes.

(3) EXCEPTIONS—Notwithstanding the prohibitions set forth in this subsection, an employer may use a consumer report with respect to a consumer in the following situations:

- (A) When the consumer applies for, or currently holds, employment that requires national security or FDIC clearance.
- (B) When the consumer applies for, or currently holds, employment with a State or local government agency which otherwise requires use of a consumer report.
- (C) When the consumer applies for, or currently holds, a supervisory, managerial, professional, or executive position at a financial institution.
- (D) When otherwise required by law.

You anticipate your boss will be asked on the campaign trail if she supports this bill. Give her some talking points to explain the issue to potential voters and advise her on the best position for her to take. Be sure to identify how the position she takes may relate to her commitment to job growth and limiting regulations on business.

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Assignment 8. Credit Discrimination

Credit is a major vehicle for economic and social mobility in the United States. Families borrow to buy homes, pay for education, and meet unexpected expenses. Access to loans can help people improve their quality of life and avoid hardships. Because of its roles as a safety net and mechanism for upward opportunity, discrimination in credit can hold back individuals and hurt their life chances.

Consumer laws prohibit discrimination in the credit process based on a statutorily prescribed list of characteristics. While discrimination in other contexts (such as employment or education) is not considered "consumer" law, those laws influence the enforcement and interpretation of credit discrimination laws.

A. History of Credit Discrimination

For much of its history, credit opportunity did not exist in the United States for large swaths of the population. African Americans simply were not served at many financial institutions, single women were denied credit because they lacked husbands that lenders believed were necessary for financial stability, and immigrants were marginalized to specialized lenders.

The government was complicit in credit discrimination. In the 1930s, a federal agency charged with preventing foreclosure, the Home Owners Loan Corporation, created maps to indicate the risks of lending that used race as a negative factor. High-concentration areas of African Americans were outlined in red. Today, the term "redlining" is used to generally describe discriminatory lending practices.

In the wake of the Civil Rights movement, several laws were enacted to prohibit discrimination in credit markets. Borrowing opportunities increased to racial minorities, women, and other groups, such as older Americans and disabled Americans, who may have income from government support. During the 1970s and 1980s, other policy efforts included the expansion of community banks, education to consumers about their rights to be given fair consideration for credit, and the examination of the lending practices of financial institutions for discrimination.

In the late 1990s, the concerns about discrimination morphed from unfair denials of credit to aggressive extensions of high-cost, unfavorable credit terms to minorities and other groups. Advocates and policymakers began to worry about "reverse redlining," a term that encompassed the practices of inundating certain neighborhoods or certain individuals with offers for exploitative loans.

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These loans often featured expensive fees, above-market rates, and unfavorable terms. As a net result, these credit "opportunities" actually harmed, rather than improved, a person's financial situation. Such predatory loans were disproportionately offered to racial minorities and other groups traditionally limited in opportunities for credit, such as non-English speakers or older Americans. The City of Baltimore sued Wells Fargo in 2008 alleging that unfair credit terms in mortgage loans produced a high foreclosure rate that cost the city millions in lost property taxes and public investment. The city's analysis found that in 2006, high-rate loans went to 65 percent of black Baltimore borrowers and 15 percent of white Baltimore borrowers. Wells Fargo contested the charges on the grounds that its loan pricing was based on credit risk. *Mayor of Baltimore v. Wells Fargo Bank*, 631 F. Supp. 2d 702 (D. Md. 2009) (denying bank's motion to dismiss). The Department of Justice took over as plaintiff to resolve questions about the city's standing as a plaintiff; ultimately Wells Fargo settled for $175 million without admitting any wrongdoing.

In the wake of the 2010 Dodd-Frank Act, the pendulum has swung back to worry about a lack of borrowing opportunity. Credit retrenchment can limit opportunities for individuals to build wealth, access education, or start a small business. With a higher rate of denials and more conservative underwriting comes more concern about discrimination in those decisions. Today, the talk is about "expanding the credit box," and in particular to considering how data analytics and credit scoring may disproportionately harm people in protected groups. As the market responds with specialized products for those excluded from mainstream credit by tighter standards, the cycle likely will repeat itself. Both aggressive credit-markups and credit denials—if either reflects discrimination—are potential acts that limit social and economic mobility in troubling ways.

B. Prohibited Bases of Discrimination

The Equal Credit Opportunity Act (ECOA), 15 U.S.C. §1691 et seq., is the most sweeping of the federal laws pertaining to credit discrimination. Several other laws supplement its coverage, either by prohibiting credit decisions on additional bases not covered by ECOA or by providing different remedies. These laws include the Fair Housing Act, the Americans with Disabilities Act, the Federal Civil Rights Act, and a host of equivalent state laws. A related law is the Community Reinvestment Act, 12 U.S.C. §2903 et seq., which requires regulators to monitor the level of service that banks provide to low- and moderate-income communities. It is most frequently used to challenge mergers or sales of financial institutions that might result in the closing of less profitable branches in low-income neighborhoods. Because the Community Reinvestment Act does not give protections to individual consumers, it is not considered further in this Assignment. Its viability as a tool to ensure access to financial services may be weakened by the growth in online and mobile lending, and the corresponding reduction in physical bank branches.

The general approach of credit discrimination laws is to prohibit any consideration of certain factors in credit applications and decisions. It is not a defense that the factor might bear a statistically provable correlation with credit risk; the creditor's reasonableness is irrelevant. If the factor or an obvious proxy for the factor is considered, discrimination has occurred.

1. Sex or Gender

ECOA was enacted in 1974, in the midst of the struggle to pass an Equal Rights Amendment, the widespread adoption of no-fault divorce laws, and rapid growth in women's college enrollment and professional workforce participation. ECOA itself prohibits discrimination based on "sex." Regulation B, which implements ECOA, prohibits creditors from requesting information about an applicant's birth control practices, intention or capacity to bear children, or intention to rear children. 12 C.F.R. §1002.5(b)(2). These were frequent proxies for determining if an applicant was a woman and sometimes were bases for discrimination themselves (on the theory, for example, that a woman would quit working after becoming a mother).

Marital status and familial status are closely related to sex discrimination because historically women were required to be married and to rely on their husbands' incomes to obtain loans. Regulation B sharply limits when marital or familial status may be considered in the credit process. The idea is that a consumer should have control of whether she or he wants the financial institution to rely on assets or income that are tied to the marriage. For example, if joint property is being offered as collateral, a creditor can require both spouses to complete a credit application. 12 C.F.R. §1002.7(d)(1). The general rule is that married women have the right to seek credit independent of their spouses or fathers and to be evaluated as individuals based on the woman's creditworthiness. The following case is dated but offers a lucid explanation of the concerns with regard to sex and marital status that undergirded ECOA.

Markham v. Colonial Mortgage Serv. Co.

605 F.2d 566 (D.C. Cir. 1979)

SWYGERT, Circuit Judge.

The Equal Credit Opportunity Act, 15 U.S.C. §§1691, et seq., prohibits creditors from discriminating against applicants on the basis of sex or marital status. We are asked to decide whether this prohibition prevents creditors from refusing to aggregate the incomes of two unmarried joint mortgage applicants when determining their creditworthiness in a situation where the incomes of two similarly situated married joint applicants would have been aggregated. The plaintiffs in this action, Jerry and Marcia Markham, appeal the judgment of the district court granting defendant Illinois Federal Service Savings and Loan Association's motion for summary judgment. We reverse....

In November 1976, plaintiffs Marcia J. Harris and Jerry Markham announced their engagement and began looking for a residence in the Capitol Hill section of Washington, D.C. One of the real estate firms which they contacted, defendant B.W. Real Estate, Inc., found suitable property for them, and in December 1976, Markham and Harris signed a contract of sale for the property.

Upon the recommendation of B.W. Real Estate, plaintiffs agreed to have defendant Colonial Mortgage Service Co. Associates, Inc. conduct a credit check. Plaintiffs subsequently submitted a joint mortgage application to Colonial Mortgage...[which was eventually submitted] to Illinois Federal.

Plaintiffs and B.W. Real Estate had decided that February 4, 1977 would be an appropriate closing date for the purchase of the Capitol Hill residence. Accordingly, plaintiffs arranged to terminate their current leases, change mailing addresses, and begin utility service at the new property. On February 1, the loan committee of Illinois Federal rejected the plaintiffs' application. On February 3, the eve of the settlement date, plaintiffs were informed through a B.W. Real Estate agent that their loan application had been denied because they were not married. They were advised that their application would be resubmitted to the "investor" who was not identified on February 8, but that approval would be contingent upon the submission of a marriage certificate.

On February 8, the Illinois Federal loan committee reconsidered the plaintiffs' application, but again denied it. A letter was sent that date from Illinois Federal...that the application had been rejected with the statement: "Separate income not sufficient for loan and job tenure."

On February 9, 1977 plaintiffs filed this suit, alleging violation of the Equal Credit Opportunity Act. After the district court separately granted the motions of Illinois Federal and the other defendants for summary judgment on May 25, 1978, plaintiffs brought this appeal.

II.

A.

We address first the appeal from the district court's summary judgment entered in favor of Illinois Federal. The district court concluded as a matter of law that plaintiffs could not state a claim under the Equal Credit Opportunity Act even if they showed that Illinois Federal's refusal to aggregate their incomes resulted, in whole or in part, in the denial of their loan application. This conclusion was based on the premise that creditors need not ignore the "special legal ties created between two people by the marital bond." It was the court's conclusion that under Illinois law the mere fact of marriage provides creditors with greater rights and remedies against married applicants than are available against unmarried applicants. Presumably the district court believed that this excused Illinois Federal under 15 U.S.C. §1691d(b), which allows a creditor to take "(s)tate property laws directly or indirectly affecting creditworthiness" into consideration in making credit decisions.

We fail to see the relevance of any special legal ties created by marriage with respect to the legal obligations of joint debtors. This was not an instance where a single person is applying for credit individually and claiming income from a third

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party for purposes of determining creditworthiness. In such an instance, the absence of a legal obligation requiring continuance of the income claimed by the applicant from the third party would reflect on the credit applicant's creditworthiness. Inasmuch as the Markhams applied for their mortgage jointly, they would have been jointly and severally liable on the debt. Each joint debtor would be bound to pay the full amount of the debt; he would then have a right to contribution from his joint debtor. See 4 A. Corbin, Contracts §§924, 928 (1951). See also Clayman v. Goodman Properties, Inc., 518 F.2d 1026 (1973). While it may be true that judicially-enforceable rights such as support and maintenance are legal consequences of married status, they are irrelevancies as far as the creditworthiness of joint applicants is concerned. Illinois Federal would have had no greater rights against the Markhams had they been married, nor would the Markhams have had greater rights against each other on this particular obligation. Thus, inasmuch as the state laws attaching in the event of marriage would not affect the creditworthiness of these joint applicants, section 1691d(b) may not be used to justify the refusal to aggregate the plaintiffs' incomes on the basis of marital status.

B.

We turn to a consideration of whether the Equal Credit Opportunity Act's prohibition of discrimination on the basis of sex or marital status makes illegal Illinois Federal's refusal to aggregate plaintiffs' income when determining their creditworthiness. Illinois Federal contends that neither the purpose nor the language of the Act requires it to combine the incomes of unmarried joint applicants when making that determination.

We start, as we must, with the language of the statute itself. March v. United States, 506 F.2d 1306, 1313 (1974). 15 U.S.C. §1691(a) provides:

> It shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction
>
> (1) on the basis of…sex or marital status

This language is simple, and its meaning is not difficult to comprehend. Illinois Federal itself has correctly phrased the standard in its brief: The Act forbids discrimination "on the basis of a person's marital status, that is, to treat persons differently, all other facts being the same, because of their marital status.…" Brief for Defendant Illinois Federal at 18. Illinois Federal does not contend that they would not have aggregated plaintiffs' income had they been married at the time. Indeed, Illinois Federal concedes that the law would have required it to do so.[4] Thus, it is plain that Illinois Federal treated plaintiffs differently that is, refused to aggregate their incomes solely because of their marital status, which is precisely the sort of discrimination prohibited by section 1691(a)(1) on its face.

Despite the section's clarity of language, Illinois Federal seeks to avoid a finding of prohibited discrimination by arguing that it was not the Congressional purpose

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to require such an aggregation of the incomes of non-married applicants. It can be assumed, *arguendo*, that one, perhaps even the main, purpose of the act was to eradicate credit discrimination waged against women, especially married women whom creditors traditionally refused to consider apart from their husbands as individually worthy of credit. But granting such an assumption does not negate the clear language of the Act itself that discrimination against *any* applicant, with respect to *any* aspect of a credit transaction, which is based on marital status is outlawed. When the plain meaning of a statute appears on its face, we need not concern ourselves with legislative history, see Caminetti v. United States, 242 U.S. 470 (1917), especially when evidence of the legislation's history as has been presented to us does not argue persuasively for a narrower meaning than that which is apparent from the statutory language. See Boston Sand & Gravel Co. v. United States, 278 U.S. 41, 48 (1928). We believe that the meaning of the words chosen by Congress is readily apparent.

Illinois Federal expresses the fear that a holding such as we reach today will require it to aggregate the incomes of all persons who apply for credit as a group. Lest it be misinterpreted, we note that our holding is not itself that far-reaching. It does no more than require Illinois Federal to treat plaintiffs—a couple jointly applying for credit—the same as they would be treated if married. We have not been asked to decide what the effect of the Act would have been had plaintiffs not applied for credit jointly. Nor do we have before us a question of whether the Act's marital status provision in any way applies to a situation where more than two people jointly request credit. We hold only that, under the Act Illinois Federal should have treated plaintiffs an unmarried couple applying for credit jointly the same as it would have treated them had they been married at the time.

C.

Illinois Federal also contends that, regardless of this court's decision on the issue of income aggregation, the judgment of the district court should be affirmed. The premise of this contention is that, even had the incomes of plaintiffs' been combined, Illinois Federal would still not have extended the loan because of lack of sufficient job tenure or credit history. Due to the district court's basis for decision and the state of the record, we are not in position to pass on the validity of this separate issue.…

Although Illinois Federal contends that plaintiffs would remain ineligible regardless of aggregation, plaintiffs assert that they were told the loan would be forthcoming if they produced a marriage certificate. Because we remand the case to the district court, we deem it sufficient to note the appearance of a genuine issue of material fact on this state of the record....

The interpretation in this case limited the ability of creditors to discriminate against same-sex couples applying for credit. And in the wake of *United States v. Windsor*, 133 S. Ct. 2675 (2013), the CFPB clarified that it would treat same-sex married couples identically to opposite-sex married couples. CFPB, *Memorandum on Ensuring Equal Treatment for Same-Sex Married Couples* (June 25, 2014).

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As with other areas of discrimination, however, the law often lags behavior and social norms. Passed over 40 years ago, ECOA does not use the term "gender." It arguably does cover discrimination against transgender persons or gender expression, *see Rosa v. Park West Bank & Trust Co.*, 214 F.3d 213 (1st Cir. 2000), but some states have amended their laws to provide protection, *see* Cal. Civ. Code §51 (defining sex for civil rights laws to include "gender identity" and "gender expression").

2. Race and Color

Race and color are prohibited bases under nearly all laws applying to credit discrimination, including ECOA and the Fair Housing Act. ECOA also protects whites, who either may claim direct discrimination, *see Moore v. U.S. Dep't of Agriculture*, 993 F.2d 1222 (5th Cir. 1993), or because the creditor associates them with a protected group. An example of the latter situation is a denial of credit to a white applicant who lives in a heavily minority neighborhood, *see Cherry v. Amoco Oil Co.*, 481 F. Supp. 727 (N.D. Ga. 1979) (denying defendant's motion for summary judgment because plaintiff stated a claim under ECOA based on creditor using plaintiff's zip code as negative credit factor, given segregated housing pattern). These arguments may fail in their application, however, given the difficulty of proving discrimination. *See Cherry v. Amoco Oil Co.*, 490 F. Supp. 1026, 1031 (1980) (ruling for defendant creditor).

In addition to mortgage lending, where ideas about residential segregation are at play, studies have found a relationship between being African-American and paying more for a car loan. Ian Ayres, *Fair Driving: Gender and Race Discrimination in Retail Car Negotiations*, 104 HARVARD L. REV. 817 (1991); Ian Ayres, *Further Evidence of Discrimination in New Car Negotiations and Estimates of Its Cause*, 94 MICH. L. REV. 109 (1995) (replicating and expanding the initial study). In 2014 and 2015, the CFPB has reached settlements with a number of banks or auto finance companies over allegations of racial discrimination. *See* Jonelle Marte, *Fifth Third Bank Fined for Discriminating Against Minorities Seeking Auto Loans*, Wash. Post (Sept. 28, 2015); Devlin Barrett, *Honda Finance Arm to Pay $25 Million to Settle Discriminatory Lending Allegations*, Wall St. J. (July 14, 2014).

3. National Origin

National origin differs from race or color discrimination in that it focuses on ancestry and life history. This includes discouragement or discrimination based on individuals' surnames being associated with certain places of origin or based on individuals' countries of birth. Discrimination on the basis of immigration status is permitted; for example, creditors may distinguish between people with permanent resident status and student visas, and inquire about the immigration situation of an applicant who seeks credit. 12 C.F.R. §1002.5(e).

Prohibiting discrimination based on national origin can provide some protection from discrimination against non-English speakers, as language

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preference/ability and national origin are often correlated. Regulation B explicitly permits lenders to provide credit contracts and disclosures in languages other than English, 12 C.F.R. §1002.4(e), provided that the disclosures are identical in content to English-language versions. The federal government has taken some enforcement actions against creditors who reject applicants based on English-language ability. For example, the U.S. Department of Justice condemned as "blatant discrimination" the practice of a financial institution of intentionally avoiding marketing credit products to any customer who had indicated a Spanish-language preference or who resided in Puerto Rico. Elizabeth Olsen, *GE Consumer Finance Units Reach Settlement*, N.Y. Times (June 19, 2014). States have enacted laws that require loan documents to be translated or that regulate the use of oral translators in loan negotiations. *See*, *e.g.*, Tex. Fin. Code §341.502(a); Cal. Civ. Code §1632(a).

4. Other Bases

Other characteristics that are prohibited bases of credit discrimination under ECOA are religion, age, receipt of income from a public assistance program, or the applicant's exercise of rights under the entire Consumer Credit Protection Act (which includes ECOA). 15 U.S.C. §1691(a). A number of state and municipal laws ban discrimination based on sexual orientation, *see*, *e.g.*, Cal. Gov't. Code §12955, and less commonly on other characteristics such as military service or political affiliation. Disabled or handicapped people, those with a physical or mental impairment that substantially limits one or more major life activities, may fall under the protection of the anti-discrimination protections in the Americans with Disabilities Act or the Fair Housing Act.

The Fair Housing Act also prohibits discriminating against people who have children under 18 years old in their households. Even if the landlord has an honest belief that children will not be safe in the building, it is illegal to deny the housing on that basis. Some landlords try to steer families to more distant parts of the building (the back or the basement) or impose low-occupancy limits. The latter are set by the Housing and Urban Development department based on square footage to remove landlord discretion. The complaint in *United States v. Twin Oaks Mobile Home Park, Inc.* (14-CV-710, W.D. Wis. Oct. 17, 2014), illustrates conduct that will be challenged as housing discrimination. The Department of Justice alleged that the owner and managers of a 230-unit mobile home community enforced explicit policies making sections of the community unavailable to families with children and prevented the sale of a mobile home to a single mother with a two-year-old child.

The lengthier discussion of certain characteristics in this section reflects the historical importance of these factors in enacting ECOA, with its roots in the civil rights movement and women's movement; it is not a reflection of the scope or harm of such discrimination or the desirability of legal protection. Discrimination is rooted in history and culture, and the protected factors and enforcement activity continue to evolve.

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C. Credit Process

Discrimination can occur at various stages of the credit process. Each of the laws that can be used to combat discrimination has a slightly different scope. Perhaps the most broadly applicable are the federal Civil Rights Acts, which apply to making and enforcing contracts and transactions involving real property. 42 U.S.C. §§1681; 1682. The Fair Housing Act prohibits discriminatory conduct in the rental, sale, or financing of a home. 42 U.S.C. §3604(a). It applies to property owners as well as municipalities.

The Equal Credit Opportunity Act also applies to several stages of a credit transaction. The application and evaluation processes are each considered below.

1. Applications

ECOA liability may exist for creditors' determinations in pre-application stages. Regulation B forbids creditors from discouraging prospective consumers on a prohibited basis. 12 C.F.R. §1002.4(b). In the race context, marketing discrimination may be alleged if advertisements feature only white people, if advertising occurs only in media serving non-minority areas, or if words or symbols are used in advertising or on applications that imply a discriminatory preference.

At the application stage, discrimination can arise from seeking information from protected class applicants that should be irrelevant to credit evaluation or from making protected class applicants provide additional information. 12 C.F.R. §1002.5(b). For example, creditors should not seek to identify the sex or marital status of an applicant by requiring them to indicate a prefix like Mr., Mrs. or Ms. Requests for such information must be marked optional on credit applications. 12 C.F.R. §1002.5(b)(2). The exception to inquiries about race, color, religion, and other protected bases is if the lender is conducting a self-test to monitor its own compliance with ECOA. 12 C.F.R. §1002.5(b)(1).

Discrimination can also occur if a lender provides different levels of support and guidance in the application process based on a prohibited characteristic. This might occur by offering suggestions to white applicants on how to improve their applications without offering similar advice to minority applicants. In 2015, the CFPB and the DOJ reached a settlement with a lender under ECOA that was premised in part on the lender refusing to accept mortgage applications at branches in minority-dominated neighborhoods but accepting them in predominately white neighborhoods.

2. Evaluations

Creditors violate ECOA if they rely on a prohibited basis in "any system of evaluating the creditworthiness of applicants." 12 C.F.R. §1002.6(b). This means that lenders cannot have different underwriting standards based on

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factors such as race, sex, national origin, etc. The same rule applies whether the lender uses a credit scoring model based on data or exercises individualized judgment in assessing applications. Informational barriers make it difficult to prove discrimination in either context. In the wake of ECOA, lenders revised procedures and trained employees to avoid blatant discrimination. Reducing or eliminating subtle or unconscious bias is much more difficult.

The evaluation of applicants consists of not just the denial of credit but also on variation in price and term. Historically, most studies of mortgage lending, where the data availability is greatest, focus on credit denials. In a recent study, however, researchers limited the sample to approved applicants for home loans. Their results suggest that black applicants pay about 29 basis points (1 basis point is 1/100th of a percent), which is more than comparable with white borrowers. Ping Cheng et al., *Racial Discrepancy in Mortgage Interest Rates*, 51 J. REAL ESTATE FIN. & ECON. 1 (2015). Studies also are beginning to explore whether the theory of intersectionality applies in credit discrimination. The above study finds that discrimination is more likely when creditors may believe that a person fits into multiple protected categories. The researchers concluded that while blacks paid higher rates than comparable whites across the credit spectrum, black women at the lower end of creditworthiness suffered the most from higher credit costs.

3. Data Collection

Regulation B imposes record keeping requirements on creditors. Section 1002.12(b) requires the retention of application forms, other information used in evaluating the applicant, written notification of the credit decision, written notification of the specific reasons for adverse action, and any statement submitted by an applicant alleging an ECOA violation. Such records should be kept for 25 months from the notification of the applicant. The time period was justified by the two-year statute of limitations for bringing an ECOA action but Dodd-Frank lengthened to five years the period in which a plaintiff may sue under ECOA. 15 U.S.C. §1691e(f). Creditors also must keep information on how they select customers for pre-screened solicitations and copies of those solicitations. During regulatory exams, creditors are reviewed for fair lending compliance. This typically includes ensuring that a lender has proper policies and procedures and also an audit of selected individual loan-level files.

If the credit is being sought for the purchase or refinance of a home, additional data collection is required. The justification for more records is both the historical problems with discriminatory mortgage lending and also the importance of home purchases to allowing consumers to build wealth, access quality public schools, and have safe, high-quality housing. The Home Mortgage Disclosure Act (HMDA), 12 U.S.C. §2801, requires creditors accepting a mortgage loan application to request information on applicants' ethnicity (using specified categories), sex, marital status, and age. Creditors must also note the geographic location of the home sought to be purchased. The applicant must be told that he or she is not required to provide the information but that the data is being requested by the federal government for the purpose of monitoring

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credit discrimination. If an applicant does not provide the information, creditors are required to note that fact and "to the extent possible" document the ethnicity, race, and sex of the applicant "on the basis of visual observation or surname." 12 C.F.R. §1002.13. HMDA is a major departure from ECOA's approach to discrimination. Recall that creditors are explicitly banned from asking for characteristics such as race, age, and sex.

Another major innovation of HMDA is that institutions are required to disclose loan-level data to the public. 12 U.S.C. §2803. Only large lenders are required to comply with HMDA but they cover a large share of the market. The 2012 data include information on 15.3 million home loan applications (of which nearly 9.8 million resulted in loan originations) and 3.2 million loan purchases, for a total of nearly 18.5 million actions. The usefulness of HMDA data to detect discrimination is expected to improve in future years because the Dodd-Frank Act passed in 2010 requires the collection and disclosure of additional information about applicants' creditworthiness that can be used as a control in statistical models to identify disparate treatment. As of 2015, the CFPB was still in the process of issuing rules under Regulation C to implement the Dodd-Frank provisions.

D. Proving Liability

Case law defining the contours of prohibited application procedures or impermissible evaluation of applicants is very sparse. Aside from a spate of cases in the late 1970s following ECOA's enactment that alleged direct discrimination, litigation is rare. A lack of data and expense are the main barriers in indirect discrimination cases. The problem is particularly acute outside the mortgage context because of the lack of a comparable law to HMDA for non-mortgage lending. *See* Winnie Taylor, *Proving Racial Discrimination and Monitoring Fair Lending Compliance: The Missing Data Problem in Nonmortgage Credit*, 31 Rev. of Banking & Fin. Law 199 (2011). The National Consumer Law Center, which served as co-counsel, described the $1 million expenditure for discovery, computer analysis, and expert review, necessary in its successful trial against an auto lender for ECOA violations, *Borlay v. Primus Automotive Financial Services*, CV 02-0382. Filed in 1998, the cases ended seven years later in a bench ruling that plaintiffs had proved their case. Without sufficient evidence at the start, but unable to front the costs for discovery, plaintiffs may settle or lose on a motion to dismiss for failure to state a claim.

Defendants also have incentives to prevent ECOA claims from going to trial, even if their deeper pockets would permit litigation on the merits. One reason is that if an ECOA violation is established, punitive damages are available under nearly all credit discrimination laws, and may be mandatory under ECOA. 15 U.S.C. §1691e(b). Perhaps equally, or more important, are the reputational effects of being named a plaintiff in a discrimination lawsuit. Public enforcement is much more common than private litigation in credit discrimination cases. Problems of proof make it easier for regulators to obtain, analyze,

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and assemble a prima facie case, although even they face challenges in their efforts to establish facts showing discrimination.

1. Disparate Treatment

Disparate treatment requires a showing of discriminatory motive or intent. The evidence can be direct, showing a specific link between the discriminatory intent and the challenged act. For example, a company policy of giving those with Latino surnames a lower credit limit would be an explicit and unambiguous statement of the lender's intent to treat adversely people protected by ECOA. Such overt discrimination is rare.

A prima facie case alleging an ECOA violation requires proof that a lender rejected or acted unfavorably to a creditworthy applicant in an ECOA-protected group and that the lender approved or acted more favorably to those outside the group. The key is comparative evidence showing that applicants with one protected characteristic were treated better, despite similar creditworthiness. The actions must be intentional, but the evidence of discriminatory intent can be indirect. The plaintiffs can then invoke the burden-shifting framework set forth in the employment discrimination case of *McDonnell Douglas Corp. v. Green*, 411 U.S. 792 (1973), and the lender must present a non-discriminatory justification for its different treatment.

2. Disparate Impact

Disparate impact reduces the plaintiff's evidentiary burden even more than disparate treatment. Even if a plaintiff cannot show a creditor is treating applicants differently, discrimination can be established if there is a discriminatory effect of the creditors' neutral practices. Put another way, a lender engaged in a neutral act without intent could nonetheless be harming a protected group. The focus is on the harm, not the motive. As with disparate treatment, the analysis borrows heavily from the framework used in employment cases. And as with employment discrimination, the legal theory of disparate impact is hotly contested. The case below interprets the Fair Housing Act but likely also will be cited with regard to the availability of disparate impact claims under ECOA.

Tex. Dep't of Housing and Community Affairs, et al. v. The Inclusive Communities Project, Inc., et al.

135 S. Ct. 2507 (2015)

KENNEDY, Justice.

The underlying dispute in this case concerns where housing for low-income persons should be constructed in Dallas, Texas—that is, whether the housing should

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be built in the inner city or in the suburbs. This dispute comes to the Court on a disparate-impact theory of liability. In contrast to a disparate-treatment case, where a "plaintiff must establish that the defendant had a discriminatory intent or motive," a plaintiff bringing a disparate-impact claim challenges practices that have a "disproportionately adverse effect on minorities" and are otherwise unjustified by a legitimate rationale. Ricci v. DeSteffano, 557 U.S. 557, 577 (2009). The question presented for the Court's determination is whether disparate-impact claims are cognizable under the Fair Housing Act (or FHA), 42 U.S.C. §3601 et seq.

I.

Before turning to the question presented, it is necessary to discuss a different federal statute that gives rise to this dispute. The Federal Government provides low-income housing tax credits that are distributed to developers through designated state agencies. 26 U.S.C. §42. Congress has directed States to develop plans identifying selection criteria for distributing the credits. §42(m)(1). Those plans must include certain criteria, such as public housing waiting lists, §42(m)(1)(C), as well as certain preferences, including that low-income housing units "contribut[e] to a concerted community revitalization plan" and be built in census tracts populated predominantly by low-income residents. §§42(m)(1)(B)(ii)(III), 42(d)(5)(ii)(I). Federal law thus favors the distribution of these tax credits for the development of housing units in low-income areas.

In the State of Texas these federal credits are distributed by the Texas Department of Housing and Community Affairs (Department). Under Texas law, a developer's application for the tax credits is scored under a point system that gives priority to statutory criteria, such as the financial feasibility of the development project and the income level of tenants. Tex. Govt. Code Ann. §2306.6710(a)-(b) (West 2008). The Texas Attorney General has interpreted state law to permit the consideration of additional criteria, such as whether the housing units will be built in a neighborhood with good schools. Those criteria cannot be awarded more points than statutorily mandated criteria. Tex. Op. Atty. Gen. No. GA-0208, pp. 2-6 (2004), 2004 WL 1434796, *4-*6.

The Inclusive Communities Project, Inc. (ICP), is a Texas-based nonprofit corporation that assists low-income families in obtaining affordable housing. In 2008, the ICP brought this suit against the Department and its officers in the United States District Court for the Northern District of Texas. As relevant here, it brought a disparate-impact claim under §§804(a) and 805(a) of the FHA. The ICP alleged the Department has caused continued segregated housing patterns by its disproportionate allocation of the tax credits, granting too many credits for housing in predominantly black inner-city areas and too few in predominantly white suburban neighborhoods. The ICP contended that the Department must modify its selection criteria in order to encourage the construction of low-income housing in suburban communities.

The District Court concluded that the ICP had established a prima facie case of disparate impact. It relied on two pieces of statistical evidence. First, it found "from 1999-2008, [the Department] approved tax credits for 49.7% of proposed non-elderly units in 0% to 9.9% Caucasian areas, but only approved 37.4% of proposed non-elderly units in 90% to 100% Caucasian areas." 749 F. Supp. 2d 486, 499 (ND

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Tex. 2010) (footnote omitted). Second, it found "92.29% of [low-income housing tax credit] units in the city of Dallas were located in census tracts with less than 50% Caucasian residents." Ibid.

The District Court then placed the burden on the Department to rebut the ICP's prima facie showing of disparate impact. 860 F. Supp. 2d 312, 322-323 (2012). After assuming the Department's proffered interests were legitimate, id., at 326, the District Court held that a defendant—here the Department—must prove "that there are no other less discriminatory alternatives to advancing their proffered interests," ibid. Because, in its view, the Department "failed to meet [its] burden of proving that there are no less discriminatory alternatives," the District Court ruled for the ICP. Id., at 331.

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II.

The issue here is whether, under a proper interpretation of the FHA, housing decisions with a disparate impact are prohibited. Before turning to the FHA, however, it is necessary to consider two other antidiscrimination statutes that preceded it.

The first relevant statute is §703(a) of Title VII of the Civil Rights Act of 1964, 78 Stat. 255. The Court addressed the concept of disparate impact under this statute in *Griggs v. Duke Power Co.*, 401 U.S. 424 (1971).

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In interpreting §703(a)(2), the Court reasoned that disparate-impact liability furthered the purpose and design of the statute. The Court explained that, in §703(a)(2), Congress "proscribe[d] not only overt discrimination but also practices that are fair in form, but discriminatory in operation." Id., at 431. For that reason, as the Court noted, "Congress directed the thrust of [§703(a)(2)] to the consequences of employment practices, not simply the motivation." Id., at 432. In light of the statute's goal of achieving "equality of employment opportunities and remov[ing] barriers that have operated in the past" to favor some races over others, the Court held §703(a)(2) of Title VII must be interpreted to allow disparate-impact claims. Id., at 429-430.

The Court put important limits on its holding: namely, not all employment practices causing a disparate impact impose liability under §703(a)(2). In this respect, the Court held that "business necessity" constitutes a defense to disparate-impact claims. Id., at 431....

The second relevant statute that bears on the proper interpretation of the FHA is the Age Discrimination in Employment Act of 1967 (ADEA)....The Court first addressed whether [section 4 of the ADEA] allows disparate-impact claims in *Smith v. City of Jackson*, 544 U.S. 228 (2005). There, a group of older employees challenged their employer's decision to give proportionately greater raises to employees with less than five years of experience.

Explaining that *Griggs* "represented the better reading of [Title VII's] statutory text," 544 U.S., at 235, a plurality of the Court concluded that the same reasoning pertained to §4(a)(2) of the ADEA. The *Smith* plurality emphasized that both §703(a)(2) of Title VII and §4(a)(2) of the ADEA contain language "prohibit[ing] such actions that 'deprive any individual of employment opportunities or otherwise

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adversely affect his status as an employee, because of such individual's' race or age." 544 U.S., at 235. As the plurality observed, the text of these provisions "focuses on the effects of the action on the employee rather than the motivation for the action of the employer" and therefore compels recognition of disparate-impact liability. Id., at 236....

Together, *Griggs* holds and the plurality in *Smith* instructs that antidiscrimination laws must be construed to encompass disparate-impact claims when their text refers to the consequences of actions and not just to the mindset of actors, and where that interpretation is consistent with statutory purpose. These cases also teach that disparate-impact liability must be limited so employers and other regulated entities are able to make the practical business choices and profit-related decisions that sustain a vibrant and dynamic free-enterprise system. And before rejecting a business justification—or, in the case of a governmental entity, an analogous public interest—a court must determine that a plaintiff has shown that there is "an available alternative…practice that has less disparate impact and serves the [entity's] legitimate needs." Ricci, supra, at 578. The cases interpreting Title VII and the ADEA provide essential background and instruction in the case now before the Court.

Turning to the FHA, the ICP relies on two provisions. Section 804(a) provides that it shall be unlawful:

> "To refuse to sell or rent after the making of a bona fide offer, or to refuse to negotiate for the sale or rental of, or otherwise make unavailable or deny, a dwelling to any person because of race, color, religion, sex, familial status, or national origin." 42 U.S.C. §3604(a).

Here, the phrase "otherwise make unavailable" is of central importance to the analysis that follows.

Section 805(a), in turn, provides:

> "It shall be unlawful for any person or other entity whose business includes engaging in real

> estate-related transactions to discriminate against any person in making available such a transaction, or in the terms or conditions of such a transaction, because of race, color, religion, sex, handicap, familial status, or national origin." §3605(a).

Applied here, the logic of *Griggs* and *Smith* provides strong support for the conclusion that the FHA encompasses disparate-impact claims. Congress' use of the phrase "otherwise make unavailable" refers to the consequences of an action rather than the actor's intent. See United States v. Giles, 300 U.S. 41, 48 (1937) (explaining that the "word 'make' has many meanings, among them '[t]o cause to exist, appear or occur'" (quoting Webster's New International Dictionary 1485 (2d ed. 1934))). This results-oriented language counsels in favor of recognizing disparate-impact liability. See Smith, supra, at 236. The Court has construed statutory language similar to §805(a) to include disparate-impact liability. See, e.g., Board of Ed. of City School Dist. of New York v. Harris, 444 U.S. 130, 140-141 (1979) (holding the term "discriminat[e]" encompassed disparate-impact liability in the context of a statute's text, history, purpose, and structure).

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A comparison to the antidiscrimination statutes examined in *Griggs* and *Smith* is useful. Title VII's and the ADEA's "otherwise adversely affect" language is equivalent in function and purpose to the FHA's "otherwise make unavailable" language. In these three statutes the operative text looks to results. The relevant statutory phrases, moreover, play an identical role in the structure common to all three statutes: Located at the end of lengthy sentences that begin with prohibitions on disparate treatment, they serve as catchall phrases looking to consequences, not intent. And all three statutes use the word "otherwise" to introduce the results-oriented phrase. "Otherwise" means "in a different way or manner," thus signaling a shift in emphasis from an actor's intent to the consequences of his actions. Webster's Third New International Dictionary 1598 (1971). This similarity in text and structure is all the more compelling given that Congress passed the FHA in 1968—only four years after passing Title VII and only four months after enacting the ADEA.

Further and convincing confirmation of Congress' understanding that disparate-impact liability exists under the FHA is revealed by the substance of the 1988 amendments. The amendments included three exemptions from liability that assume the existence of disparate-impact claims. The most logical conclusion is that the three amendments were deemed necessary because Congress presupposed disparate impact under the FHA as it had been enacted in 1968.

The relevant 1988 amendments were as follows. First, Congress added a clarifying provision: "Nothing in [the FHA] prohibits a person engaged in the business of furnishing appraisals of real property to take into consideration factors other than race, color, religion, national origin, sex, handicap, or familial status." 42 U.S.C. §3605(c). Second, Congress provided: "Nothing in [the FHA] prohibits conduct against a person because such person has been convicted by any court of competent jurisdiction of the illegal manufacture or distribution of a controlled substance." §3607(b)(4). And finally, Congress specified: "Nothing in [the FHA] limits the applicability of any reasonable…restrictions regarding the maximum number of occupants permitted to occupy a dwelling." §3607(b)(1).

The exemptions embodied in these amendments would be superfluous if Congress had assumed that disparate-impact liability did not exist under the FHA. Indeed, none of these amendments would make sense if the FHA encompassed only disparate-treatment claims. If that were the sole ground for liability, the amendments merely restate black-letter law. If an actor makes a decision based on reasons other than a protected category, there is no disparate-treatment liability. See, e.g., Texas Dept. of Community Affairs v. Burdine, 450 U.S. 248, 254 (1981). But the amendments do constrain disparate-impact liability. For instance, certain criminal convictions are correlated with sex and race. See, e.g., Kimbrough v. United States, 552 U.S. 85, 98 (2007) (discussing the racial disparity in convictions for crack cocaine offenses). By adding an exemption from liability for exclusionary practices aimed at individuals with drug convictions, Congress ensured disparate-impact liability would not lie if a landlord excluded tenants with such convictions. The same is true of the provision allowing for reasonable restrictions on occupancy. And the exemption from liability for real-estate appraisers is in the same section as §805(a)'s prohibition of discriminatory practices in real-estate transactions, thus indicating Congress' recognition that disparate-impact liability arose under §805(a). In short, the 1988 amendments signal that Congress ratified disparate-impact liability.

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Recognition of disparate-impact claims is consistent with the FHA's central purpose. The FHA, like Title VII and the ADEA, was enacted to eradicate discriminatory practices within a sector of our Nation's economy. See 42 U.S.C. §3601 ("It is the policy of the United States to provide, within constitutional limitations, for fair housing throughout the United States"); H.R. Rep., at 15 (explaining the FHA "provides a clear national policy against discrimination in housing").

These unlawful practices include zoning laws and other housing restrictions that function unfairly to exclude minorities from certain neighborhoods without any sufficient justification. Suits targeting such practices reside at the heartland of disparate-impact liability. See, e.g., Huntington, 488 U.S., at 16-18 (invalidating zoning law preventing construction of multifamily rental units); Black Jack, 508 F.2d, at 1182-1188 (invalidating ordinance prohibiting construction of new multifamily dwellings); Greater New Orleans Fair Housing Action Center v. St. Bernard Parish, 641 F. Supp. 2d 563, 569, 577-578 (E.D. La. 2009) (invalidating post-Hurricane Katrina ordinance restricting the rental of housing units to only "'blood relative[s]'" in an area of the city that was 88.3% white and 7.6% black)….Recognition of disparate-impact liability under the FHA also plays a role in uncovering discriminatory intent: It permits plaintiffs to counteract unconscious prejudices and disguised animus that escape easy classification as disparate treatment. In this way disparate-impact liability may prevent segregated housing patterns that might otherwise result from covert and illicit stereotyping.

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An important and appropriate means of ensuring that disparate-impact liability is properly limited is to give housing authorities and private developers leeway to state and explain the valid interest served by their policies. This step of the analysis is analogous to the business necessity standard under Title VII and provides a defense against disparate-impact liability. See 78 Fed. Reg. 11470 (explaining that HUD did not use the phrase "business necessity" because that "phrase may not be easily understood to cover the full scope of practices covered by the Fair Housing Act, which applies to individuals, businesses, nonprofit organizations, and public entities"). As the Court explained in *Ricci*, an entity "could be liable for disparate-impact discrimination only if the [challenged practices] were not job related and consistent with business necessity." 557 U.S., at 587. Just as an employer may maintain a workplace requirement that causes a disparate impact if that requirement is a "reasonable measure[ment] of job performance," Griggs, supra, at 436, so too must housing authorities and private developers be allowed to maintain a policy if they can prove it is necessary to achieve a valid interest. To be sure, the Title VII framework may not transfer exactly to the fair-housing context, but the comparison suffices for present purposes.

It would be paradoxical to construe the FHA to impose onerous costs on actors who encourage revitalizing dilapidated housing in our Nation's cities merely because some other priority might seem preferable. Entrepreneurs must be given latitude to consider market factors. Zoning officials, moreover, must often make decisions based on a mix of factors, both objective (such as cost and traffic patterns) and, at least to some extent, subjective (such as preserving historic architecture). These factors contribute to a community's quality of life and are legitimate concerns for housing authorities. The FHA does not decree a particular vision of urban development; and it does not put housing authorities and private developers

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in a double bind of liability, subject to suit whether they choose to rejuvenate a city core or to promote new low-income housing in suburban communities. As HUD itself recognized in its recent rulemaking, disparate-impact liability "does not mandate that affordable housing be located in neighborhoods with any particular characteristic." 78 Fed. Reg. 11476.

In a similar vein, a disparate-impact claim that relies on a statistical disparity must fail if the plaintiff cannot point to a defendant's policy or policies causing that disparity. A robust causality requirement ensures that "[r]acial imbalance…does not, without more, establish a prima facie case of disparate impact" and thus protects defendants from being held liable for racial disparities they did not create.

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Courts must therefore examine with care whether a plaintiff has made out a prima facie case of disparate impact and prompt resolution of these cases is important. A plaintiff who fails to allege facts at the pleading stage or produce statistical evidence demonstrating a causal connection cannot make out a prima facie case of disparate impact. For instance, a plaintiff challenging the decision of a private developer to construct a new building in one location rather than another will not easily be able to show this is a policy causing a disparate impact because such a one-time decision may not be a policy at all. It may also be difficult to establish causation because of the multiple factors that go into investment decisions about where to construct or renovate housing units. And as Judge Jones observed below, if the ICP cannot show a causal connection between the Department's policy and a disparate impact—for instance, because federal law substantially limits the Department's discretion—that should result in dismissal of this case. 747 F. 3d, at 283-284 (specially concurring opinion).

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The Court holds that disparate-impact claims are cognizable under the Fair Housing Act upon considering its results-oriented language, the Court's interpretation of similar language in Title VII and the ADEA, Congress' ratification of disparate-impact claims in 1988 against the backdrop of the unanimous view of nine Courts of Appeals, and the statutory purpose.

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Justice ALITO, with whom THE CHIEF JUSTICE, Justice SCALIA, and Justice THOMAS join, dissenting.

No one wants to live in a rat's nest. Yet in *Gallagher v. Magner*, 619 F.3d 823 (2010), a case that we agreed to review several terms ago, the Eighth Circuit held that the Fair Housing Act (or FHA), 42 U.S.C. §3601 et seq., could be used to attack St. Paul, Minnesota's efforts to combat "rodent infestation" and other violations of the city's housing code. 619 F.3d, at 830. The court agreed that there was no basis to "infer discriminatory intent" on the part of St. Paul. Id., at 833. Even so, it concluded that the city's "aggressive enforcement of the Housing Code" was actionable because making landlords respond to "rodent infestation, missing dead-bolt locks, inadequate sanitation facilities, inadequate heat, inoperable smoke detectors, broken or missing doors," and the like increased the price of rent. Id., at 830, 835. Since minorities were statistically more likely to fall into "the bottom bracket for household adjusted median family income," they were disproportionately affected by those rent increases, i.e., there was a "disparate impact." Id., at 834. The upshot was that even St. Paul's good-faith attempt to ensure minimally acceptable housing for its poorest residents could not ward off a disparate-impact lawsuit.

Today, the Court embraces the same theory that drove the decision in *Magner*. This is a serious mistake. The Fair Housing Act does not create disparate-impact liability, nor do this Court's precedents. And today's decision will have unfortunate consequences for local government, private enterprise, and those living in poverty. Something has gone badly awry when a city can't even make slumlords kill rats without fear of a lawsuit. Because Congress did not authorize any of this, I respectfully dissent.

I.

Everyone agrees that the FHA punishes intentional discrimination. Treating someone "less favorably than others because of a protected trait" is "'the most easily understood type of discrimination.'" Ricci v. DeStefano, 557 U.S. 557, 577 (2009) (quoting Teamsters v. United States, 431 U.S. 324, 335, n.15 (1977). Indeed, this classic form of discrimination—called disparate treatment—is the only one prohibited by the Constitution itself. See, e.g., Arlington Heights v. Metropolitan Housing Development Corp., 429 U.S. 252, 264-265 (1977). It is obvious that Congress intended the FHA to cover disparate treatment.

The question presented here, however, is whether the FHA also punishes "practices that are not intended to discriminate but in fact have a disproportionately adverse effect on minorities." Ricci, supra, at 577. The answer is equally clear. The FHA does not authorize disparate-impact claims. No such liability was created when the law was enacted in 1968. And nothing has happened since then to change the law's meaning.

I begin with the text. Section 804(a) of the FHA makes it unlawful "[t]o refuse to sell or rent after the making of a bona fide offer, or to refuse to negotiate for the sale or rental of, or otherwise make unavailable or deny, a dwelling to any person because of race, color, religion, sex, familial status, or national origin." 42 U.S.C. §3604(a) (emphasis added). Similarly, §805(a) prohibits any party "whose business includes engaging in residential real estate-related transactions" from "discriminat[ing] against any person in making available such a transaction, or in the terms or conditions of such a transaction, because of race, color, religion, sex, handicap, familial status, or national origin." §3605(a) (emphasis added).

In both sections, the key phrase is "because of." These provisions list covered actions ("refus[ing] to sell or rent…a dwelling," "refus[ing] to negotiate for the sale or rental of…a dwelling," "discriminat[ing]" in a residential real estate transaction, etc.) and protected characteristics ("race," "religion," etc.). The link between the actions and the protected characteristics is "because of."

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Without torturing the English language, the meaning of these provisions of the

FHA cannot be denied. They make it unlawful to engage in any of the covered actions "because of"—meaning "by reason of" or "on account of," *Nassar*, supra, at ______—race, religion, etc. Put another way, "the terms [after] the 'because of' clauses in the FHA supply the prohibited motivations for the intentional acts…that the Act makes unlawful." American Ins. Assn. v. Department of

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Housing and Urban Development, 74 F. Supp. 3d 30, 41, n. 20 (D.C. 2014). Congress accordingly outlawed the covered actions only when they are motivated by race or one of the other protected characteristics.

It follows that the FHA does not authorize disparate-impact suits. Under a statute like the FHA that prohibits actions taken "because of" protected characteristics, intent makes all the difference.

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V.

Not only is the decision of the Court inconsistent with what the FHA says and our precedents, it will have unfortunate consequences. Disparate-impact liability has very different implications in housing and employment cases.

Disparate impact puts housing authorities in a very difficult position because programs that are designed and implemented to help the poor can provide the grounds for a disparate-impact claim. As *Magner* shows, when disparate impact is on the table, even a city's good-faith attempt to remedy deplorable housing conditions can be branded "discriminatory." 619 F.3d, at 834. Disparate-impact claims thus threaten "a whole range of tax, welfare, public service, regulatory, and licensing statutes." Washington v. Davis, 426 U.S. 229, 248 (1976).

This case illustrates the point. The Texas Department of Housing and Community Affairs (the Department) has only so many tax credits to distribute. If it gives credits for housing in lower income areas, many families—including many minority families—will obtain better housing. That is a good thing. But if the Department gives credits for housing in higher income areas, some of those families will be able to afford to move into more desirable neighborhoods. That is also a good thing. Either path, however, might trigger a disparate-impact suit.

This is not mere speculation. Here, one respondent has sued the Department for not allocating enough credits to higher income areas. See Brief for Respondent Inclusive Communities Project, Inc., 23. But another respondent argues that giving credits to wealthy neighborhoods violates "the moral imperative to improve the substandard and inadequate affordable housing in many of our inner cities." Reply Brief for Respondent Frazier Revitalization Inc. 1. This latter argument has special force because a city can build more housing where property is least expensive, thus benefiting more people. In fact, federal law often favors projects that revitalize low-income communities. See ante, at 2.

No matter what the Department decides, one of these respondents will be able to bring a disparate-impact case. And if the Department opts to compromise by dividing the credits, both respondents might be able to sue. Congress surely did not mean to put local governments in such a position.

The Solicitor General's answer to such problems is that HUD will come to the rescue. In particular, HUD regulations provide a defense against disparate-impact liability if a defendant can show that its actions serve "substantial, legitimate, nondiscriminatory interests" that "necessar[ily]" cannot be met by "another practice that has a less discriminatory effect." 24 C.F.R. §100.500(b) (2014). (There is, of course, no hint of anything like this defense in the text of the FHA. But then, there is no hint of disparate-impact liability in the text of the FHA either.)

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The effect of these regulations, not surprisingly, is to confer enormous discretion on HUD—without actually solving the problem. What is a "substantial" interest? Is there a difference between a "legitimate" interest and a "nondiscriminatory" interest? To what degree must an interest be met for a practice to be "necessary"? How are parties and courts to measure "discriminatory effect"?

These questions are not answered by the Court's assurance that the FHA's disparate-impact "analysis 'is analogous to the Title VII requirement that an employer's interest in an employment practice with a disparate impact be job related.'" Ante, at 4 (quoting 78 Fed. Reg. 11470). See also ante, at 18 (likening the defense to "the business necessity standard"). The business-necessity defense is complicated enough in employment cases; what it means when plopped into the housing context is anybody's guess. What is the FHA analogue of "job related"? Is it "housing related"? But a vast array of municipal decisions affect property values and thus relate (at least indirectly) to housing. And what is the FHA analogue of "business necessity"? "Housing-policy necessity"? What does that mean?

Compounding the problem, the Court proclaims that "governmental entities…must not be prevented from achieving legitimate objectives, such as ensuring compliance with health and safety codes." Ante, at 21. But what does the Court mean by a "legitimate" objective? And does the Court mean to say that there can be no disparate-impact lawsuit if the objective is "legitimate"? That is certainly not the view of the Government, which takes the position that a disparate-impact claim may be brought to challenge actions taken with such worthy objectives as improving housing in poor neighborhoods and making financially sound lending decisions. See Brief for United States as Amicus Curiae 30, n. 7.

Because HUD's regulations and the Court's pronouncements are so "hazy," Central Bank, 511 U.S., at 188-189, courts—lacking expertise in the field of housing policy—may inadvertently harm the very people that the FHA is meant to help. Local governments make countless decisions that may have some disparate impact related to housing. See ante, at 19-20. Certainly Congress did not intend to "engage the federal courts in an endless exercise of second-guessing" local programs. Canton v. Harris, 489 U.S. 378, 392 (1989).

...

I would interpret the Fair Housing Act as written and so would reverse the judgment of the Court of Appeals.

E. Adverse Action and Data Collection

1. General Notices

ECOA requires that creditors provide a response to all applicants. 15 U.S.C. §1691(d). The purpose of this rule is to prevent creditors from skirting liability by never taking action on applications from individuals with certain

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characteristics. The problem that ECOA sought to solve was not just explicit denials but also a failure to make any decision at all. Both rejection and endless delay have the same harmful effect of reducing access to credit or increasing the cost of credit. If an individual never received a decision from a mainstream lender, the individual then might seek credit from a higher-cost lender or give up entirely.

Regulation B, §1002.9, prescribes the timeframe for making decisions on applications. For a completed application, a creditor has 30 days to respond. For an incomplete application, the same 30-day window applies if the creditor is taking adverse action (discussed in the next section). Alternatively, creditors may respond to an incomplete application by notifying applicants of the information needed and informing them that a failure to respond will result in no further consideration of the application. Creditors may also respond to a credit application by making a counteroffer with credit on different terms that originally sought. The creditor has up to 90 days after extending the counteroffer to provide a withdrawal notice to applicants who have not responded by accepting or using the credit.

2. Adverse Action Notices

ECOA, like FCRA, uses the term "adverse action" to describe unfavorable outcomes from credit determinations. ECOA defines adverse action broadly to include not just a denial or revocation of credit, but also "a change in the terms of an existing credit arrangement, or a refusal to grant credit in substantially the amount or on substantially the terms requested." 12 C.F.R. §1002.2(c)(1). The law has two important exclusions. It is not an "adverse action" to refuse to exceed a firm credit limit (such as a maximum on a credit card or home equity line of credit) that was previously set. Creditors also do not engage in adverse action under ECOA when they do not extend additional credit under an existing credit arrangement to a consumer who is delinquent or in default. Consumers will certainly perceive these decisions as adverse to them, a reminder that the law's technical definitions make it difficult to educate consumers about their rights.

If the creditor is taking adverse action, there are special requirements for notification. First, the notice of adverse action must be in writing. This rule actually helps protect lenders. ECOA compliance has pushed lenders to use form letters to deliver credit decisions, rather than making oral statements that could give rise to perceptions of discrimination and that allow for more variance. Second, the notice must inform the consumer that the ECOA prohibits credit discrimination on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The actual notice given to consumers basically parrots 15 U.S.C. §1691(a), with no effort to explain what the Consumer Credit Protection Act is to consumers. The notice also must provide the applicant with the federal agency that administers compliance, which is the Consumer Financial Protection Bureau.

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Third, creditors must give in writing the "specific reasons" for their having taken adverse action or at least a written disclosure of the applicant's right to obtain a statement of specific reasons by making a request within 30 days of the notice. 15 U.S.C. §1691(d)(2). It will not surprise you that lenders do not list a discriminatory purpose as a specific reason. In fact, they may not provide much helpful information at all.

Williams v. MBNA America Bank, N.A.

538 F. Supp. 2d 1015 (E.D. Mich. 2008)

ROSEN, District Judge.

Plaintiff Kim Williams filed her one-count Equal Credit Opportunity Act ("ECOA") complaint in this action alleging that Defendant MBNA America Bank's letter notifying her of its rejection of her credit card application did not comply with the ECOA's notice requirements. Defendant MBNA now moves to dismiss Plaintiff's Complaint pursuant to Fed. R. Civ. P. 12(b)(6) for failure to state a claim upon which relief can be granted....

The relevant facts are not complex and are not disputed. Plaintiff Kim Williams applied for an MBNA American Express credit card via telephone on May 2, 2006. Plaintiff first spoke with a telemarketer who input identifying and credit information she provided and, by computer, interfaced with Experian Information Services to obtain Plaintiff's credit history. Plaintiff's application was then transferred by the MBNA computer system to a human MBNA credit analyst who personally spoke with Plaintiff.

From Plaintiff and Experian, MBNA was provided with the following information: (i) Plaintiff had a total revolving credit from a variety of sources in the amount of $26,596; (ii) of this amount, she had balances due on such revolving credit in the amount of $13,285; and (iii) although Plaintiff's household had a gross income of $70,000, Plaintiff herself had no income of her own (she was a student). Thus, as of May 2, 2006, Plaintiff had a total amount of unused credit available to her in the amount of $13,311.

MBNA's credit analyst denied Plaintiff's application and informed Plaintiff of the denial during the May, 2, 2006 telephone conversation with her. The credit analyst then assigned two "reason codes" (codes which specified the principal reasons credit was being denied)—1010 and 1020—to Plaintiff's application, and input them into the MBNA system. The reason codes were assigned respectively to the following two reasons (i) "You have sufficient balances on your revolving credit lines;" and (ii) "You have sufficient credit available considering your income." The credit analyst explained these reason codes to Plaintiff during the May 2, 2006 telephone conversation, as well.

The MBNA system then automatically incorporated the text corresponding to the reason codes into a form letter to be sent to Plaintiff denying her application for credit and specifying that these were the principal reasons her credit application was being denied. The letter was dated May 2, 2006 and was mailed to Plaintiff the

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same day or shortly thereafter. Plaintiff does not deny receiving this letter. In fact, the letter is at the heart of Plaintiff's Complaint.

The first page of the May 2, 2006 letter stated as follows:

> After careful review, we are unable to approve your request because you have sufficient balances on your revolving credit lines and you have sufficient credit available considering your income. Our credit decision was based in whole or in part on information obtained in a report from Experian, National Consumer Assistance Center, P.O. Box 2002, Allen, TX 75013-0036, 1-888-297-2472, www.experian.com/reportaccess.
>
> If you have any information that may enable us to reconsider this decision, please write to MBNA, P.O. Box 15023, Wilmington, DE XXXXX-XXXX.
>
> Sincerely,
>
> Don Hamilton, Credit department
>
> Please see the next page of this letter for important information.

The second page of the letter contained various notices and, in relevant part, informed Plaintiff that she had a right to a free copy of her credit report from Experian if she requested it within sixty days from receipt of the letter, and if she discovered any inaccurate or incomplete information in her credit report, she could dispute the matter with Experian.

Plaintiff does not dispute that as of May 2, 2006, she was a student, nor does she dispute that she had a total revolving line of credit from a variety of sources in the amount of $26,596, or that she had balances due on such revolving credit in the amount of $13,285, leaving her $13,311 in available credit. Rather, her dispute with MBNA arises out of the language used by MBNA in its letter. She contends that the reasons provided by MBNA indicating that her American Express credit card application was being denied because she had "sufficient balance on [her] revolving credit lines and [because she had] sufficient credit available considering [her] income" were "incoherent [and] illogical," and, this, she contends, constitutes a violation of the Equal Credit Opportunity Act, 15 U.S.C. §1691(d).

...

The ECOA was originally enacted in 1974 to prohibit discrimination in credit transactions. Treadway v. Gateway Chevrolet Oldsmobile, Inc., 362 F.3d 971, 975 (7th Cir. 2004). The Act's principal purpose is "to eradicate discrimination against women, especially married women whom creditors traditionally refused to consider for individual credit." Midkiff v. Adams County Regional Water District, 409 F.3d 758, 771 (6th Cir. 2005) (citation and internal punctuation omitted). The statute was amended in 1976 to require creditors to furnish written notice of the specific reasons why an adverse action was taken against a consumer. See Fischl v. General Motors Acceptance Corp., 708 F.2d 143 (5th Cir. 1983); 15 U.S.C. §1691(d)(2), (3). As explained in the Senate report accompanying the 1976 amendments to the ECOA, Congress viewed the notice requirement as:

> ...a strong and necessary adjunct to the antidiscrimination purpose of the legislation, for only if creditors know they must explain their decisions will they effectively be

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> discouraged from discriminatory practices. Yet this requirement fulfills a broader need: rejected credit applicants will now be able to learn where and how their credit status is deficient and this information should have a pervasive and valuable educational benefit. Instead of being told only that they do not meet a particular creditor's standards, consumers particularly should benefit from knowing, for example, that the reason for the denial is their short residence in the area, or their recent change of employment, or their already over-extended financial situation. In those cases where the creditor may have acted on misinformation or inadequate information, the statement of reasons gives the applicant a chance to rectify the mistake.

Fischl, supra, 708 F.2d at 146 (quoting S. Rep. No. 94-589, 94th Cong., 2d sess., 1976 U.S. Code Cong. & Admin. News, pp. 408, 406).

ECOA's notice provisions apply to all loan applicants, not only those who claim to have been denied credit due to discrimination. See Jochum v. Pico Credit Corp. of Westbank, 730 F.2d 1041, 1043 n. 3 (5th Cir. 1984) (finding that the plaintiffs did not need to state a claim of discrimination to assert a cognizable claim under §1691(d)); Diaz v. Paragon Motors of Woodside, Inc., 424 F. Supp. 2d 519, 532 n. 22 (E.D.N.Y. 2006)

("The [ECOA] notification requirement extends to all applicants, and does not require specific allegations of discrimination.").

A credit denial is referred to as an "adverse action" under the ECOA. 15 U.S.C. §1691(d)(6). A written letter informing an applicant that credit has been denied is referred to as an "adverse action notice." With regard to the content of adverse action notices, §1691(d) of the ECOA provides as follows:

> (1) Within thirty days (or such longer reasonable time as specified in regulations of the Board for any class of credit transaction) after receipt of a completed application for credit, a creditor shall notify the applicant of its action on the application.
>
> (2) Each applicant against whom adverse action is taken shall be entitled to a statement of reasons for such action from the creditor. A creditor satisfies this obligation by—
>
> > (A) providing statements of reasons in writing as a matter of course to applicants against whom adverse action is taken; or
> >
> > (B) giving written notification of adverse action which discloses (i) the applicant's right to a statement of reasons within thirty days after receipt by the creditor of a request made within sixty days after such notification, and (ii) the identity of the person or office from which such statement may be obtained. Such statement may be given orally if the written notification advises the applicant of his right to have the statement of reasons confirmed in writing on written request.
>
> (3) A statement of reasons meets the requirements of this section if it contains the specific reasons for the adverse action taken.

15 U.S.C. §1691(d).

The regulations which implement the ECOA, "Regulation B," 12 C.F.R. §202.1 et seq., provide only as follows with regard to the content of adverse action notices:

> [(a)] (2) Content of notification when adverse action is taken. A notification given to an applicant when adverse action is taken shall be in writing and shall contain a statement of the action taken; the name and address of the creditor; a statement of the provisions of §701(a) of the Act; the name and address of the federal agency that

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> administers compliance with respect to the creditor; and…(i) A statement of specific reasons for the action taken. 12 C.F.R. §202.9(a)(2)(i).

[ED. NOTE—The CFPB reissued Regulation B with different numbering that begins with §1002. The content is identical to the prior regulations and Official Staff Interpretation from the Federal Reserve Board.]

Paragraph (b) of the regulation further provides with regard to the statement of reasons:

> Statement of specific reasons. The statement of reasons for adverse action required by paragraph (a)(2)(i) of this section must be specific and indicate the *principal reasons* for the adverse action. Statements based on the creditor's internal standards or policies or that the

> applicant, joint applicant, or similar party failed to achieve a qualifying score on the creditor's credit scoring system are insufficient.

12 C.F.R. §202.9(b)(2) (emphasis added). While an Appendix to Regulation B sets forth some sample forms intended for use in notifying an applicant that adverse action has been taken on a credit application, the regulations make clear that "[t]he sample forms are illustrative and may not be appropriate for all creditors. They were designed to include some of the factors that creditors most commonly consider." 12 C.F.R. §202, App. C, ¶2.

The Official Federal Reserve Board interpretations of Regulation B, 12 C.F.R. §202 Supp. I, further make clear that there is no statutory or regulatory prohibition against a creditor's wording of its reasons. With regard to Section 202.9's notification requirements, the Official Staff Interpretation states, "In notifying an applicant of adverse action as defined by §202.2(c)(1), a creditor may use any words or phrases that describe the action taken on the application." 12 C.F.R. §202 Supp. I.

The Official Staff Interpretation further states that "[a] creditor need not describe how or why a factor adversely affected an applicant." Id.

In this case, MBNA's notice to Plaintiff provided her with two principal reasons that her credit application was denied. The first principal reason given was "you have sufficient balances on your revolving line of credit." The statement is a "specific reason for the action taken." Furthermore, as Defendant notes, and Plaintiff does not dispute, the statement is consistent with the information provided by Plaintiff and Experian. Having "sufficient balances on her revolving lines of credit" meant that Plaintiff could have charged additional amounts on her existing credit accounts at any time causing her to max out her existing credit lines, which would be a concern for a lender.

The second principal reason that Plaintiff's credit was denied was "you have sufficient credit available considering your income." This, too, is a "specific reason for the action taken." While Plaintiff indicated in applying for credit that her "household" income was $70,000, Plaintiff personally had no income source; she was a student. Being able to charge additional amounts on her existing lines of credit and to max out on those credit lines without having any personal source of income is legitimate concern for any lender.

Plaintiff, however, finds MBNA's stated reasons to be "incoherent" and "illogical." She argues that Regulation B requires that the stated reasons be "clearly and conspicuously" explained in "reasonably understandable" terms. There is, however, no such requirement in the statute or the regulations. In fact, the only

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mention of "clear and conspicuous" is in Section 202.4(d) of the regulation. §202.4 provides:

> (d) Form of disclosures—
> (1) General rule. A creditor that provides in writing any disclosures or information required by this regulation must provide the disclosures in a clear and conspicuous manner and, except for the disclosures required by §§202.5 [requests for information] and 202.13 [information for

> monitoring purposes], in a form the applicant may retain.

12 C.F.R. §202.4(d). As the Official Staff Interpretations make clear, however, the "clear and conspicuous" requirement set forth in this section deals, not with the content of the notice, but rather with the format:

> 1. Clear and conspicuous. This standard requires that disclosures be presented in a reasonably understandable format in a way that does not obscure the required information. No minimum type size is mandated, but the disclosures must be legible, whether typewritten, handwritten, or printed by computer.

12 C.F.R. §202 Supp. I. The only statutory/regulatory requirement is that the "format" must be "reasonably understandable."

...

In sum, the Court finds that the allegations in Plaintiffs Complaint do not make out a cognizable claim for violation of the ECOA. MBNA's adverse action notice clearly and conspicuously presented the creditor's specific reasons for its denial of Plaintiffs credit card application.

For all of the foregoing reasons, the Court finds that Plaintiff has failed to state a claim upon which relief may be granted.

While the content may be of limited use to consumers, the adverse action notice requirement has surprising reach. It applies even when a creditor grants credit, if there is some possible more favorable type of credit that could be issued, because of the broad definition of adverse action.

ECOA's notice rules protect all consumers, even those who are not alleging discrimination. It provides basic procedural fairness whenever adverse action is taken. In this way, ECOA supplements the rights with regard to credit reporting to give consumers' greater insight into lending decisions.

Problem Set 8

8.1. Sunshine State Bank operates branches in areas that attract a high proportion of "snowbirds," retired Americans who leave their homes each winter. Sunshine offers low-cost accounts to these partial-year residents but profitability has been a problem due to the relatively small balances that people keep in these accounts. To boost profits, Sunshine is proposing charging a fee to any new applicants for checking accounts who wish to obtain debit cards. The fee will only be charged to people 55 years or older because

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Sunshine's records show that these people often have irregular incomes and thus overdraw their accounts, requiring Sunshine to extend overdraft protection. Sunshine's experience is also that snowbirds are unlikely to heavily use debit cards, preferring instead to be served in person at a branch location. Can Sunshine ask applicants for their year of birth to determine if it will impose the fee? 15 U.S.C. §§1691(a)(1); 1691a(d); 12 C.F.R. §§1002.2; 1002.6(b).

8.2. Todd and Allison Smith own a 4-bedroom house that they purchased brand new when it was built in 2006. Like all their neighbors, they are "upside down" on the loan, owing $100,000 more than their house's value. Todd and Allison applied for a loan modification under their mortgage company's program. They carefully completed all forms and submitted all information. Yesterday, they received a letter stating that "we regret to inform you that a loan modification was not granted." The letter gave no reason for the denial but invited them to reapply if their circumstances change. Todd and Allison are devastated and worry they will soon lose their home to foreclosure. They are also furious that the mortgage company required them to submit extensive documentation, to the tune of 100 pages, and yet they received only a one-line denial. Did the mortgage company violate ECOA in its dealings with Todd and Allison? *See* 15 U.S.C. §§1691(d)(6); 1691a.

8.3. Cherokee Credit Tribe is a community organization devoted to serving members of the Cherokee Nation. They provide policymaking expertise on issue affecting Native Americans and operate some direct service programs, including a zero-interest student loan fund for members of the Cherokee Nation. The amount of loan is dependent on the degree of relation to the Cherokee Nation, and applicants are required to submit a family tree with full family names that are verified against tribal records. Financial need is not a factor in determining eligibility for the loan or its amount. Your step-sister, Shanna, is a member of the Sioux tribe; her paternal grandfather was a tribal elder. There is no equivalent organization for members of the Sioux. Shanna is thinking that maybe a lawsuit (with a quick settlement) might also be a way to find funds for college. Is the Cherokee Credit Tribe violating ECOA? *See* 15 U.S.C. §1691; 12 C.F.R. §1002.8.

8.4. Dollars on Demand is an Internet start-up focusing on person-to-person credit extensions. On its website, consumers can post a request for a loan that does not exceed $1,000 for a period of one year or less. The loan seeker can supply additional information, including the desired interest rate, the reason they seek the loan, their financial characteristics, and a picture. Loan suppliers, who are also individual consumers can search or browse these profiles and make any loans they wish to fund. Dollars on Demand takes a cut of the loan and makes money off advertising on its site. To date, over 50,000 loans have been funded. The typical person supplying a loan has done so four times in the last year, lending an average of $400 per transaction.

You are the newly hired in-house counsel for Dollars on Demand. As part of your compliance review, you are checking for consumer law violations. You already have determined there are no problems with false advertising, the Fair Credit Reporting Act, or the Truth in Lending Act and are now ready to consider the Equal Credit Opportunity Act and parallel laws on credit discrimination. Do you have any concerns? Please also identify any information that you might request from the business department as part of your review. *See* 15 U.S.C. §1691a(e); 12 C.F.R. §§1002.2(l); 1002.4.

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3. To date, the Tenth Circuit has not defined, nor has it adopted a definition for, a pyramid scheme. However, the Tenth Circuit defines a "Ponzi Scheme," which is a different sort of fraudulent enterprise than the one at bar, as: an investment scheme in which returns to investors are not financed through the success of the underlying business venture, but are taken from principal sums of newly attracted investments. Typically, investors are promised large returns for their investments. Initial investors are actually paid the promised returns, which attract additional investors. In re Hedged Investments Associates, Inc., 48 F.3d 470, 471 n.2 (10th Cir. 1995).

1. The Annual Statement would authorize PHI to obtain "investigative consumer reports" that "may involve personal interviews with sources such as neighbors, friends, or associates" for "employment related purposes only."

2. Kelchner initially asserted claims under the Employment Retirement Income Security Act of 1874 ("ERISA"), 29 U.S.C. §§1001-1461, as amended by the Consolidated Omnibus Reconciliation Act of 1985 ("COBRA"), 29 U.S.C. §1161, et seq., in addition to her Pennsylvania state law claim of wrongful termination.

We address the issues raised under the FCRA only insofar as they are relevant to determining whether PHI and Sycamore Manor are liable for wrongful termination. See Highhouse v. Avery Transportation, 660 A.2d 1374, 1377 (Pa. Super. 1995) ("An employer's liability for wrongful discharge rests on whether a 'well-recognized facet of public policy is at stake'" and "courts have consistently held that employers violate the public policy of this Commonwealth by discharging employees for exercising legal rights"); see also Nazar v. Clark Distribution Sys. Inc., 46 Pa. D. & C. 4th 28 (Pa. Com. Pl. 2000) (finding discharge violated public policy expressed in federal law). Therefore, our resolution of this case does not rest on any implication that there would be a private right of action to bring a claim for equitable relief directly under the FCRA....

3. PHI's revised disclosure and authorization form also indicated that PHI would obtain driving records for employees assigned regular driving duties. Although those reports would also serve a clear employment purpose, that provision is not applicable to Kelchner.

4. A number of States permit the use of such "neutral" credit scores to ensure that consumers with thin or unidentifiable credit histories are not treated disadvantageously. See, e.g., N.Y. Ins. Law Ann. §§2802(e), (e)(1) (West 2006) (generally prohibiting an insurer from "consider[ing] an absence of credit information," but allowing it to do so if it "treats the consumer as if the applicant or insured had neutral credit information, as defined by the insurer").

12. In fact, notice in the context of an initially offered rate may be of greater significance than notice in the context of a renewal rate; if, for instance, insurance is offered on the basis of a single, long-term guaranteed rate, a consumer who is not given notice during the initial application process may never have an opportunity to learn of any adverse treatment.

13. For instance, if a consumer's driving record is so poor that no insurer would give him anything but the highest possible rate regardless of his credit report, whether or not an insurer happened to look at his credit report should have no bearing on whether the consumer must receive notice, since he has not been treated differently as a result of it.

4. 12 U.S.C. §1735f-5 requires that "every person engaged in making mortgage loans secured by residential real property consider without prejudice the combined income of both husband and wife for the purpose of extending mortgage credit...to a married couple or either member thereof."

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Part Three. Doing the Deal: Terms and Financing

Assignment 9. Unfair or Deceptive Acts or Practices