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California Law Which Allows Consumer To Place Freeze On Credit Report Is Unconstitutional As Applied To Credit Reporting Agency That Provides Reports Based On Public Records

Issue

A California Court of Appeal recently addressed the issue of whether California Civil Code section 1785.11.2, which allows California consumers to prevent dissemination of their credit reports, is unconstitutional. The Court of Appeal found that section 1785.11.2 is not unconstitutional on its face, but is unconstitutional as applied to a credit reporting agency that provides consumer credit reports to landowners and property managers because the agency provides reports drawn mostly from public records. (*U.D. Registry, Inc. v. State of California*, (2006 WL 3059937, Cal.App. 2 Dist., Oct. 30, 2006 (Nos. B179653, B186012).)

Facts

U.D. Registry ("U.D.") is a credit reporting agency that issues consumer credit reports. U.D. collects credit-related data contained in public records including information related to unlawful detainer actions, foreclosures, bankruptcies, and tax liens. U.D. sells consumer credit reports to landowners and property managers who use the information to decide whether to lease to prospective tenants. U.D. also resells credit reports from the three major U.S. credit reporting agencies that contain employment and credit histories.

U.D. brought a lawsuit against the State of California seeking to enjoin it from enforcing section 1785.11.2. The trial court permanently enjoined the State from enforcing section 1785.11.2 both generally

and against U.D. to the extent that the statute prevents credit reporting agencies from disseminating information contained in the public records.

Decision

Section 1785.11.2 provides, in part, "A consumer may elect to place a security freeze on his or her credit report by making a request in writing by certified mail to a consumer credit reporting agency." Section 1785.11.2 further explains that a "security freeze" is a notice placed on a consumer's credit report which prohibits a reporting agency from releasing a report or information from it without express authorization from the consumer. Section 1785.11.2 was enacted to help address the problem of identity theft.

U.D. asserted that its dissemination of public records and other credit-related information is protected by the United States and California Constitutions and that section 1785.11.2 violates its right to free speech. The First Amendment to the United States Constitution protects commercial speech that "is truthful, concerns lawful activity, and is not misleading," and the protection provided by the California Constitution is at least as broad as that offered by the First Amendment. Commercial speech, however, is entitled to less protection under the First Amendment than other forms of expression. The Court of Appeal noted that other courts have treated credit reports as commercial speech. However, the Court determined that it need not definitively decide if credit reports are in

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fact commercial speech. The Court concluded that, if the State's restriction on the dissemination of credit reports could not pass the level of scrutiny used to examine the constitutionality of restrictions placed on commercial speech, the restriction could not pass the more stringent level of scrutiny applied when a government attempts to regulate other forms of expression.

The government may restrict commercial speech only if it can demonstrate that the speech at issue concerns lawful activity; the interest of the government in regulating the speech is substantial; the regulation directly and materially advances the interest asserted; and the regulation is not more extensive than is necessary to serve the government's interest. The Court found that U.D.'s credit reports "neither relate to unlawful activity nor are misleading." The Court further found that there is no dispute that the interest advanced by the State in enacting section 1785.11.2, to protect consumers from identity theft, is a substantial government interest. As to the question of whether section 1785.11.2 directly and materially advances the State's interest in protecting consumers from identity theft, the Court stated that there was no evidence that a single credit report prepared by U.D. led to a single case of identity theft. However, the Court assumed for the purposes of its discussion that section 1785.11.2 directly advances the State's interest in protecting consumers.

As to the requirement that the restriction on speech must not be excessive, the Court held that section 1785.11.2 is too restrictive as applied to U.D. because it "sweeps more

broadly than is necessary to serve the government's interest in protecting consumers from identity theft." Section 1785.11.2 prevents the disclosure of data that is contained in and secured from court records. U.D. obtains information about unlawful detainer, bankruptcy, tax liens, and foreclosures from public court records. The public has access to these same records. The Court concluded that preventing U.D. "from disseminating *all* of the public record information does not serve the asserted state interest." The knowledge that a consumer has been the subject of one of the above described court actions does not, the Court concluded, facilitate identity theft. The Court opined that, even if the information could be used by a potential identity thief, he or she could obtain the information without resort to a report prepared by U.D.

Accordingly, the Court held section 1785.11.2 is unconstitutional as applied to U.D. The Court also held that section 1785.11.2 can not be judicially reformed so as to permit the statute to apply to U.D. The Court declined, however, to find that section 1785.11.2 is invalid on its face. The Court found that "section 1785.11.2 can validly apply if there are fraudulent misrepresentations in a credit report as there is no First Amendment right to use commercial speech to make fraudulent or misleading statements." If such a case arises, section 1785.11.2 can be used to prevent the release of a report. Because situations exist where section 1785.11.2 does not conflict with the First Amendment, the Court held that the statute is not unconstitutional on its face.

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