



FEDERAL RESERVE BANK  
OF DALLAS

ROBERT D. McTEER, JR.  
PRESIDENT  
AND CHIEF EXECUTIVE OFFICER

June 27, 1995

DALLAS, TEXAS  
75265-5906

**Notice 95-59**

**TO:** The Chief Executive Officer of each member bank and others concerned in the Eleventh Federal Reserve District

**SUBJECT**

**Final Revisions to the  
Official Staff Commentary to Regulation B  
(Equal Credit Opportunity)**

**DETAILS**

The Board of Governors of the Federal Reserve System has published final revisions to the official staff commentary to Regulation B (Equal Credit Opportunity).

The revisions, which were effective June 5, 1995, provide guidance on several issues including disparate treatment, special purpose credit programs, credit scoring systems, and marital status discrimination.

**ATTACHMENT**

A copy of the Board's notice as it appears on pages 29965-69, Vol. 60, No. 109, of the Federal Register dated June 7, 1995, is attached.

**MORE INFORMATION**

For more information, please contact Eugene Coy at (214) 922-6201. For additional copies of this Bank's notice, please contact the Public Affairs Department a (214) 922-5254.

Sincerely yours,

*Robert D. McTeer, Jr.*

## FEDERAL RESERVE SYSTEM

### 12 CFR Part 202

[Regulation B; Docket No. R-0865]

#### Equal Credit Opportunity

**AGENCY:** Board of Governors of the Federal Reserve System.

**ACTION:** Final rule; official staff interpretation.

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**SUMMARY:** The Board is revising its official staff commentary to Regulation B (Equal Credit Opportunity). The commentary applies and interprets the requirements of Regulation B and is a substitute for individual staff interpretations. The revisions to the commentary provide guidance on several issues including disparate treatment, special purpose credit programs, credit scoring systems, and marital status discrimination.

**EFFECTIVE DATE:** June 5, 1995.

**FOR FURTHER INFORMATION CONTACT:** Jane Jensen Gell, Sheilah Goodman, Natalie E. Taylor, or Manley Williams, Staff Attorneys, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, at (202) 452-3667 or 452-2412; for the hearing impaired only, contact Dorothea Thompson, Telecommunications Device for the Deaf, (202) 452-3544.

#### SUPPLEMENTARY INFORMATION:

##### I. Background

The Equal Credit Opportunity Act (ECOA), 15 U.S.C. 1691-1691f, makes it unlawful for creditors to discriminate in any aspect of a credit transaction on the basis of sex, marital status, age, race, national origin, color, religion, receipt of public assistance, or the exercise of rights under the Consumer Credit Protection Act. The Board's Regulation B (12 CFR Part 202) implements this statute. In addition, the Board's official staff commentary (12 CFR Part 202 (Supp. I)) interprets the regulation. The commentary provides general guidance in applying the regulation to various credit transactions and is updated periodically.

## II. Summary of Revisions to the Commentary

In December 1994 (59 FR 67235, December 29, 1994), the Board proposed amendments to the staff commentary to Regulation B. The Board received nearly 100 letters on the proposal. After reviewing the comment letters and upon further analysis, the Board is adopting final amendments to the staff commentary.

### Section 202.2—Definitions

#### 2(c)(1)(i) Application for Extension of Credit

The Board proposed a new comment 2(c)(2)(iii)-2 to address court decisions that misapplied portions of that section. Commenters suggested that to the extent the comment defined types of adverse action, it more clearly fit under section 202.2(c)(1)(i). The Board agrees. The Board is adopting comment 2(c)(1)(i)-1 to clarify that the refusal to refinance or extend the term of a business or other loan is adverse action if the applicant applied in accordance with the creditor's procedures.

#### 2(c)(2)(iii) Application for Increase in Available Credit

The Board proposed comment 2(c)(2)(iii)-2 to clarify that a denial of an application to increase available credit or for a change in terms is adverse action. Many commenters expressed concern that the phrase "change in terms" was overly broad, requiring a creditor to provide an adverse action notice in a variety of situations in which it is not now required. The Board has changed the comment heading and has narrowed its scope to refer only to applications to increase credit.

#### 2(p) Empirically Derived and Other Credit Scoring Systems

The Board has adopted comment 2(p)-3, regarding pooled data scoring systems, as proposed.

The proposed comment 2(p)-4 clarified that a credit scoring system—even if "empirically derived, demonstrably and statistically sound"—is subject to review under the ECOA and Regulation B. When a scoring system is used in conjunction with individual discretion, disparate treatment could still occur. In addition, a system could have a disparate impact on a prohibited basis, and could be challenged. Whether such a challenge would be successful depends on a variety of factors, as commenters noted.

More generally, commenters questioned how the standards set out in the proposed comment related to the discussion of disparate impact in

comment 6(a)-2. Commenters believed that the proposal's reference to disparate impact was attempting to describe a highly complex area of law in a condensed manner. The Board has deleted the proposed reference to the standards of proof and burdens of persuasion the parties must meet, and instead has added a reference to comment 6(a)-2.

### Section 202.4—General Rule Prohibiting Discrimination

Comment 4-1 addresses the legal concept known as "disparate treatment," which is a particular type of discrimination. The proposed amendment clarified that disparate treatment might be found even absent a conscious will to discriminate. Some commenters expressed concern that the proposal meant that "intent," as that term has been interpreted by courts in discrimination cases, is not an element of disparate treatment. The Board has revised the comment to clarify that treating individuals differently is not unlawful *per se*. However, treating individuals differently on a prohibited basis is unlawful discrimination ("disparate treatment") if there is no credible, nondiscriminatory reason that explains the difference in treatment. In the examples given, the differential treatment would constitute disparate treatment if the creditor lacked a legitimate nondiscriminatory reason for its action, or if the asserted reason was found to be a pretext for discrimination.

### Section 202.5a—Rules on Providing Appraisal Reports

#### 5a(a) Providing Appraisals

The Board proposed comment 5a(a)-1 to clarify that section 202.5a applies to applications for credit to be secured by a dwelling, whether the credit is for a business or a consumer purpose. Commenters generally supported the proposed comment. It was suggested that the Board should eliminate a reference to the "consumer's" dwelling, given the definition of "dwelling" used in sections 202.5a(a) and (c). It was noted that "consumer's dwelling" could be read as both more limited than "dwelling" (including only transactions that involve a consumer's dwelling, as "consumer" is defined elsewhere) and more expansive (any dwelling, not limited to one-to-four family dwellings). The Board has revised the comment accordingly.

The Board proposed comment 5a(a)-2 to clarify that section 202.5a applies to a request for renewal of an existing extension of credit secured by a dwelling if the creditor obtains and uses

a new appraisal report in evaluating the request.

Section 202.5a does not apply if a consumer requests renewal of existing credit and the creditor does not obtain a new appraisal. Commenters supported this clarification.

#### 5a(a)(2)(i) Notice

The Board proposed comment 5a(a)(2)(i)-1 to clarify the rule for credit involving more than one applicant, which parallels the rule in section 202.9 concerning notices of action taken where there is more than one applicant. Commenters supported this clarification.

#### 5a(a)(2)(ii) Delivery

The Board proposed a new comment 5a(a)(2)(ii)-1 to clarify that in all cases creditors may seek reimbursement for photocopy and postage costs incurred in providing the copy of the appraisal report unless prohibited by state or other law, or unless the consumer has already paid for the report.

The proposal provided that if the creditor does not otherwise charge for the report, as in "no closing cost" loans, the creditor may not require payment solely from those consumers who request a copy of the report. Commenters were divided on this issue. Some noted that these loans benefit consumers by reducing the upfront costs of applying for credit. Several commenters believed that a prohibition on reimbursement for an appraisal report for "no closing cost" loans would have a chilling effect on creditors' willingness to offer these products. Commenters said that for no-cost loans that close, creditors who waive closing costs (including the cost of an appraisal) recover those costs over the term of the loan; they do not recover the cost of the appraisal for no-cost loans that are denied or withdrawn. Commenters requested that in such cases, the Board allow creditors to charge for the cost of the appraisal when applicants ask for a copy of the report.

The statute gives a creditor the right to require an applicant to reimburse the creditor for the cost of the appraisal. Upon further analysis, the Board believes that creditors may collect the costs of an appraisal unless the consumer has already paid for the report.

#### 5a(c) Definitions

New comments 5a(c)-1 and 5a(c)-2 address the scope of the term "appraisal report." Under the proposal, publicly available listings of valuations for dwellings, such as published home sales prices or mortgage amounts, are not

covered. The appraisal rules guard against discriminatory evaluations of a dwelling's value. The Board believes that publicly available reports of home sales prices or tax assessments, among others, are unlikely to be influenced by the type of subjectivity the law is intended to eliminate.

Commenters generally supported the clarifications to the definitions. The Board has adopted the comments as proposed.

**Section 202.6—Rules Concerning Evaluation of Applications**

**6(a) General Rule Concerning Use of Information**

The Board did not propose commentary under this section. In addressing the issue of disparate impact under proposed comment 2(p)-4, however, many commenters discussed comment 2 to this section. The commenters uniformly expressed concern, in regard to this comment and comment 2(p)-4, about the Board's articulation of the standards of proof and burdens of persuasion under a disparate impact analysis (sometimes referred to as the effects test). The Board recognizes that this is an evolving area of law, one in which creditors and consumers alike would benefit from more specificity. However, given that the Board did not propose any amendments to this section of the commentary, the only change to the existing commentary is the addition of a reference to the Civil Rights Act of 1991, which codifies the standards used for disparate impact under Title VII. The Board will consider addressing these issues further in future commentary proposals.

**6(b)(1) Prohibited Basis—Marital Status**

The Board proposed to revise comment 6(b)(1)-1 to clarify that if a creditor chooses to offer joint credit, the creditor generally may not take the applicants' marital status into account in credit evaluations, except to the extent necessary for determining rights and remedies under state law. Commenters generally supported this clarification.

A few commenters requested clarification on how the commentary applied to other parties such as cosigners or guarantors. Creditors are not required to combine the debts and incomes of two parties when one of them is a cosigner or guarantor for the other. (Comment 7(d)(5)-1 provides guidance on standards that creditors may use in requesting additional parties.)

**Section 202.8—Special-Purpose Credit Programs**

**8(a) Standards for Programs**

The Board proposed comments 8(a)-5 and -6 to clarify the requirements that for-profit organizations must meet to establish special-purpose credit programs under section 202.8(a).

Commenters generally supported both comments. In response to some commenters' concerns, the Board has added language to comment 8(a)-5 clarifying that the program can be designed to benefit a class of people who would otherwise receive credit on less favorable terms, as well as those who would be denied credit.

Two issues have been clarified in comment 8(a)-6. First, some commenters were concerned about the statement that the plan should specify the length of time that it will be in effect and that it be reevaluated after that time. Some commenters said that this added regulatory burden. The Board believes that because special purpose credit programs are designed to fulfill a particular need, they must be reevaluated periodically to determine if there is a continuing need for the program. The comment has been amended to reflect this position. Second, the reference to avoiding a negative effect on individuals who are not in the class the program was designed to benefit, by denying them rights or opportunities they might otherwise have, has been deleted because it is not clear precisely how this condition applies in the credit context.

**Section 202.9—Notifications**

The Board proposed comment 9-5 to address when a creditor must send a notice of action taken under prequalification, preapproval, and similar programs. The comment clarified that the guidance provided in the commentary to section 202.2(f), addressing applications and inquiries, applies to all types of inquiries, including prequalification and preapproval programs. Thus, if a creditor—in giving information to a consumer about a prequalification or preapproval program—decides it will not grant credit, and communicates this to the consumer, the creditor has treated the inquiry as an application (by virtue of having made a credit decision) and must comply with the notification rules in § 202.9. Commenters generally supported the guidance provided in the proposal.

**Appendix C of Supplement I to Part 202—Sample Notification Forms**

The Board proposed a comment to Appendix C to provide examples of additions that may be made to Model Form C-9. The commenters supported the comment and the Board has adopted it as proposed.

**List of Subjects in 12 CFR Part 202**

Aged, Banks, banking, Civil rights, Credit, Federal Reserve System, Marital status discrimination, Penalties, Religious discrimination, Reporting and recordkeeping requirements, Sex discrimination.

For the reasons set forth in the preamble, the Board is amending 12 CFR part 202 as set forth below:

**PART 202—EQUAL CREDIT OPPORTUNITY (REGULATION B)**

1. The authority citation for part 202 continues to read as follows:

**Authority:** 15 U.S.C. 1691-1691f.

2. In Supplement I to Part 202, Section 202.2—Definitions, is amended as follows:

a. Under 2(c) Adverse action., preceding 1. Move from service area., a new paragraph heading 2(c)(1)(i), a new paragraph 1., and a new paragraph heading 2(c)(1)(ii) are added;

b. Under Paragraph (2)(c)(2)(iii), a new paragraph 2. is added; and

c. Under 2(p), the paragraph heading for 2(p) is revised and new paragraphs 3. and 4. are added.

The additions and revision read as follow:

**Supplement I to Part 202—Official Staff Interpretations**

**Section 202.2 Definitions**  
**2(c) Adverse action.**

**Paragraph 2(c)(1)(i)**

1. Application for credit. A refusal to refinance or extend the term of a business or other loan is adverse action if the applicant applied in accordance with the creditor's procedures.

**Paragraph 2(c)(1)(ii)**

1. Move from service area. \* \* \*

**Paragraph 2(c)(2)(iii)**

2. Application for increase in available credit. A refusal or failure to authorize an account transaction at the point of sale or loan is not adverse action, except when the refusal is a denial of an application, submitted in accordance with the creditor's procedures, for an increase in the amount of credit.



2(p) Empirically derived and other credit scoring systems.

3. Pooled data scoring systems. A scoring system or the data from which to develop such a system may be obtained from either a single credit grantor or multiple credit grantors. The resulting system will qualify as an empirically derived, demonstrably and statistically sound, credit scoring system provided the criteria set forth in paragraph (p)(1) (i) through (iv) of this section are met.

4. Effects test and disparate treatment. An empirically derived, demonstrably and statistically sound, credit scoring system may include age as a predictive factor (provided that the age of an elderly applicant is not assigned a negative factor or value). Besides age, no other prohibited basis may be used as a variable. Generally, credit scoring systems treat all applicants objectively and thus avoid problems of disparate treatment. In cases where a credit scoring system is used in conjunction with individual discretion, disparate treatment could conceivably occur in the evaluation process. In addition, neutral factors used in credit scoring systems could nonetheless be subject to challenge under the effects test. (See comment 6(a)-2 for a discussion of the effects test).

3. In Supplement I to part 202, under Section 202.4—General Rule Prohibiting Discrimination, four new sentences are added at the end of paragraph 1. To read as follows:

Section 202.4—General Rule Prohibiting Discrimination

1. Scope of section. \*\*\* Disparate treatment on a prohibited basis is illegal whether or not it results from a conscious intent to discriminate. Disparate treatment would be found, for example, where a creditor requires a minority applicant to provide greater documentation to obtain a loan than a similarly situated nonminority applicant. Disparate treatment also would be found where a creditor waives or relaxes credit standards for a nonminority applicant but not for a similarly situated minority applicant. Treating applicants differently on a prohibited basis is unlawful if the creditor lacks a legitimate nondiscriminatory reason for its action, or if the asserted reason is found to be a pretext for discrimination.

4. In Supplement I to part 202, a new Section 202.5a, is added in numerical order to read as follows:

Section 202.5a—Rules on Providing Appraisal Reports

5a(a) Providing appraisals. 1. Coverage. This section covers applications for credit to be secured by a lien on a dwelling, as that term is defined in § 202.5a(c), whether the credit is for a business purpose (for example, a loan to start a business) or a consumer purpose (for example, a loan to finance a child's education).

2. Renewals. If an applicant requests that a creditor renew an existing extension of credit, and the creditor obtains a new appraisal report to evaluate the request, this section applies. This section does not apply to a renewal request if the creditor uses the appraisal report previously obtained in connection with the decision to grant credit.

5a(a)(2)(i) Notice. 1. Multiple applicants. When an application that is subject to this section involves more than one applicant, the notice about the appraisal report need only be given to one applicant, but it must be given to the primary applicant where one is readily apparent.

5a(a)(2)(ii) Delivery. 1. Reimbursement. Creditors may charge for photocopy and postage costs incurred in providing a copy of the appraisal report, unless prohibited by state or other law. If the consumer has already paid for the report—for example, as part of an application fee—the creditor may not require additional fees for the appraisal (other than photocopy and postage costs).

5a(c) Definitions. 1. Appraisal reports. Examples of appraisal reports are:

- i. A report prepared by an appraiser (whether or not licensed or certified), including written comments and other documents submitted to the creditor in support of the appraiser's estimate or opinion of value.
- ii. A document prepared by the creditor's staff which assigns value to the property, if a third-party appraisal report has not been used.

- iii. An internal review document reflecting that the creditor's valuation is different from a valuation in a third party's appraisal report (or different from valuations that are publicly available or valuations such as manufacturers' invoices for mobile homes).

2. Other reports. The term "appraisal report" does not cover all documents relating to the value of the applicant's property. Examples of reports not covered are:

- i. Internal documents, if a third-party appraisal report was used to establish the value of the property.
- ii. Governmental agency statements of appraised value.
- iii. Valuations lists that are publicly available (such as published sales prices or mortgage amounts, tax assessments, and retail price ranges) and valuations such as manufacturers' invoices for mobile homes.

5. In Supplement I to Part 202, Section 202.6—Rules Concerning Evaluation of Applications, is amended as follows:

a. Under 6(a) General rule concerning use of information., the first sentence in paragraph 2. is revised; and

b. Under Paragraph 6(b)(1), three new sentences are added at the end of paragraph 1.

The additions and revision read as follow:

Section 202.6—Rules Concerning Evaluation of Applications

6(a) General rule concerning use of information.

2. Effects test. The effects test is a judicial doctrine that was developed in a series of employment cases decided by the Supreme Court under Title VII of the Civil Rights Act of 1964 (42 U.S.C. 2000e et seq.), and the burdens of proof for such employment cases were codified by Congress in the Civil Rights Act of 1991 (42 U.S.C. 2000e-2). \*\*\*

Paragraph 6(b)(1)

1. Prohibited basis—marital status. \*\*\* Except to the extent necessary to determine rights and remedies for a specific credit transaction, a creditor that offers joint credit may not take the applicants' marital status into account in credit evaluations. Because it is unlawful for creditors to take marital status into account, creditors are barred from applying different standards in evaluating married and unmarried applicants. In making credit decisions, creditors may not treat joint applicants differently based on the existence, the absence, or the likelihood of a marital relationship between the parties.

6. In Supplement I to Part 202, Section 202.8—Special Purpose Credit Programs, under 8(a) Standards for programs., new paragraphs 5. and 6. are added to read as follows:

Section 202.8—Special Purpose Credit Programs

(8)(a) Standards for Programs

5. Determining need. In designing a special-purpose program under § 202.8(a), a for-profit organization must determine that the program will benefit a class of people who would otherwise be denied credit or would receive it on less favorable terms. This determination can be based on a broad analysis using the organization's own research or data from outside sources including governmental reports and studies. For example, a bank could review Home Mortgage Disclosure Act data along with demographic data for its assessment area and conclude that there is a need for a special-purpose credit program for low-income minority borrowers.

6. Elements of the program. The written plan must contain information that supports the need for the particular program. The plan also must either state a specific period of time for which the program will last, or contain a statement regarding when the program will be reevaluated to determine if there is a continuing need for it.

7. In Supplement I to Part 202, Section 202.9—Notifications, a new paragraph 5. is added to read as follows:

Section 202.9—Notifications

5. *Prequalification and preapproval programs.* Whether a creditor must provide a notice of action taken for a prequalification or preapproval request depends on the creditor's response to the request, as discussed in the commentary to section 202.2(f). For instance, a creditor may treat the request as an inquiry if the creditor provides general information such as loan terms and the maximum amount a consumer could borrow under various loan programs, explaining the process the consumer must follow to submit a mortgage application and the information the creditor will analyze in reaching a credit decision. On the other hand, a creditor has treated a request as an application, and is subject to the adverse action notice requirements of § 202.9 if, after evaluating information, the creditor decides that it will not approve the request and communicates that decision to the consumer. For example, if in reviewing a request for prequalification, a creditor tells the consumer that it would not approve an application for a mortgage because of a bankruptcy in the consumer's record, the creditor has denied an application for credit.

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8. In Supplement I to Part 202, a new Appendix C—Sample Notification Forms is added at the end to read as follows:

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#### **Appendix C—Sample Notification Forms**

*Form C-9.* Creditors may design their own form, add to, or modify the model form to reflect their individual policies and procedures. For example, a creditor may want to add:

- i. A telephone number that applicants may call to leave their name and the address to which an appraisal report should be sent.
- ii. A notice of the cost the applicant will be required to pay the creditor for the appraisal or a copy of the report.

By order of the Board of Governors of the Federal Reserve System, acting through the Secretary of the Board under delegated authority, June 1, 1995.

**William W. Wiles,**  
*Secretary of the Board.*

[FR Doc. 95-13862 Filed 6-6-95; 8:45 am]

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