

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 7991
November 12, 1976]

REVISED PROPOSAL TO AMEND REGULATION B
Implementing the 1976 Amendments to the Equal Credit Opportunity Act

*To All Member Banks, and Others Concerned,
in the Second Federal Reserve District:*

Our Circular No. 7924, dated July 28, 1976, contained the text of a proposal by the Board of Governors of the Federal Reserve System to revise Regulation B — “Equal Credit Opportunity” — to implement the 1976 amendments to the Equal Credit Opportunity Act. The Board of Governors has now issued for further comment a revised version of its earlier proposal. Enclosed is a copy of the Board’s press release of November 3, 1976, summarizing the new proposal.

The complete text of the Board’s revised proposal appears in the Federal Register of November 8, 1976; a copy of the Federal Register excerpt will be made available by our Bank Regulations Department upon request. Comments on the proposed revision should be submitted by December 3, 1976, and may be sent to that department.

PAUL A. VOLCKER,
President.



FEDERAL RESERVE

press release

For immediate release

November 3, 1976

The Board of Governors of the Federal Reserve System today issued revised proposals for changes in its Regulation B to carry out the 1976 Amendments to the Equal Credit Opportunity Act.

The Board requested comment through December 3, 1976.

The 1976 Amendments to the Act will become effective March 23, 1977. They prohibit discrimination in extensions of credit based on race, color, religion, national origin, age, receipt of income from public assistance programs and good faith exercise of rights under the Consumer Credit Protection Act (which includes the Truth in Lending, Fair Credit Billing, Equal Credit Opportunity, Fair Credit Reporting and Consumer Leasing acts). The original ECOA, which became effective last October 28, prohibited discrimination in credit transactions on the basis of sex or marital status.

The Congress directed the Federal Reserve Board to write implementing rules for both the original and the amended ECOA. The proposed revision of Regulation B will become effective, like the revised Act, next March 23, and will supersede the existing Regulation B in its entirety. The existing regulatory rules, implementing the Act's provisions against discrimination in credit transactions on the basis of sex or marital status, remain in effect until that time.

The revised Regulation will be enforced by the same Federal agencies designated in the Act to enforce the existing Regulation.^{1/}

On July 15, 1976, the Board made initial proposals to revise Regulation B to incorporate the 1976 Amendments to the Act. Changes in the rules as now proposed reflect written comments received from the public and testimony at a hearing on the initial proposals held August 12 and 13.

The principal provisions of Regulation B as now proposed are:

Coverage: The Regulation will apply to all persons who are creditors. A creditor is defined in the proposals as a person who, in the ordinary course of business, regularly participates in decisions whether to extend credit. This does not include a person whose only participation in a credit transaction is honoring a credit card, or who only occasionally extends credit.

Sex and marital status: The provisions of the existing Regulation, dealing only with prohibitions of discrimination in credit transactions based on sex and marital status, remain essentially unchanged.

Applications: To assist small creditors and any others having difficulty designing credit application forms to comply with ECOA requirements the Board proposed to supply model forms that, when properly used,

^{1/} This and other footnotes will be found at the end of this release. Other footnotes chiefly cite principal differences between the Board's present and previous proposals for revision of Regulation B in the light of the 1976 Amendments to the Act. Where no change between the previous and current proposals is noted, there has been no substantial change.

would assure the creditor of being in compliance. Creditors could design their own forms, or revise the model forms, but they would then bear responsibility for being in compliance.

New Proposals:

The Board's proposals included several new draft provisions, not a part of the existing Regulation B or of the proposals the Board made in July. These include:

Discrimination on the basis of permanent residence or immigration status: The Board's proposals would permit creditors to inquire into applicant's permanent residence or immigration status (Section 202.5 (d) (5)) and would permit creditors to consider an applicant's permanent residence or immigration status along with other material relevant to ascertaining the creditor's rights, and ability to secure repayment of the credit requested (Section 202.6 (b) (7)). These are creditworthiness tests, and are not intended to permit creditors to make blanket refusals of credit to non-citizens.

Borrowed credit-scoring systems: As discussed below (in the part of this release on "Age") the Board provided in its current proposals for the temporary use of borrowed systems of credit scoring. (Section 202.2 (3))

Credit related insurance: (Section 202.7 (e)) The Board proposed that a creditor shall not be guilty of violating ECOA or Regulation B if rates charged for credit related casualty insurance or credit life insurance are different for different types of applicants (such as older and younger applicants, male and female applicants).

Liability: Non-governmental creditors not complying with the Act or Regulation are subject to civil liabilities limited to \$10,000 in individual cases and the lesser of \$500,000 or 1 per cent of the creditor's net worth in class actions plus costs and reasonable attorney's fees.

Two proposals that grew out of requests for comment from the public made by the Board in its July proposals -- Data notation for enforcement purposes, and Specialized treatment of some classes of credit transactions -- are discussed later.

Other Proposals:

Adverse action: In accordance with the 1976 Amendments to the Act, the Board proposed to add to Regulation B a new section defining what is and what is not an adverse action on an application for credit. An adverse action would require a creditor to provide the applicant with a statement of reasons for the action, and would trigger the requirements relating to written notice of adverse action, notice of the applicant's rights under ECOA and the requirements of the proposed Regulation concerning the retention of records. As now proposed.^{2/}

1. Adverse action has occurred if:

- a creditor declines to grant credit in substantially the amount or on substantially the terms requested by the applicant;
- the creditor makes a counter offer substantially different in amount and terms than requested, and the applicant does not accept it;
- a creditor makes an unfavorable change in the terms of an account, or terminates an account, in an action that does not apply to all or substantially all of the creditor's accounts;

--a creditor refuses a request by an applicant to increase a credit limit if the request is made according to the creditor's established procedures for learning that an applicant wants a higher limit.

2. An adverse action has not occurred if:

--the terms of an account are changed in agreement with an applicant;

--the creditor takes an action (or forebears from taking an action) concerning an account due to inactivity of the account, or default or delinquency;

--a refusal to grant credit at the point of sale, or denial of a request for a loan, connected with the use of an account when the credit desired would exceed a previously agreed credit limit that has been disclosed to the applicant;

--credit is refused because applicable law does not permit it;

--credit is refused because the creditor does not offer the type of credit requested.

Notification of action, statement of reasons and ECOA notice:

To carry out requirements of the 1976 Amendments to the Act, the Board proposed that, whenever an adverse action has been taken, the applicant should receive notice of the action, a statement of rights under ECOA and a statement of specific reasons for the adverse action (or disclosure of the applicant's right to get such an explanation). The content of all the notices is substantially the same as in the existing regulation, but they are to be provided together in order to enhance public understanding.

A change from the existing regulation is the provision in this proposal that the statement of rights under ECOA should be provided only to

persons against whom an adverse action has been taken, rather than supplying it to all applicants.

The proposal provides a sample notice of ECOA rights (Section 202.9). Unlike the existing Regulation, it need not be used verbatim but may be in language substantially the same as the language of the sample notice. The text of the proposed sample notice is identical to the existing notice, except that the prohibitions of the 1976 Amendments to the Act have been added.

The Board also provided a sample statement of specific reasons for adverse action (Sec. 202.9). This check-list form of reasons for adverse action^{3/} is similar to the form in the existing Regulation, but its title has been changed to indicate that it may be used in all cases of adverse action and not, as at present, only in cases of denial or termination of credit. Creditors who properly use the sample form supplied would be in compliance with the Regulation and the Act.

The Act provides that creditors who received 150 or fewer applications for credit in the preceding year may give the above notices orally.

Retention of Records: Requirements for retention of records in the Board's proposed revision of Regulation B are essentially the same as in the existing Regulation, except that, since the amended Act establishes a statute of limitations of 24 months, the period of retention is 25 months instead of the present 15 months.

Age: For creditors using credit-scoring systems, the Act provides that it is not a discriminatory action to consider age in a credit system based on experiences if the system is demonstrably and statistically sound in accordance with the Board's regulations, so long as the system does not operate to assign the age of an elderly applicant a "negative factor or value."

The Board proposed that creditors using such a scoring system would not be assigning a negative factor or value if the creditor gives elderly applicants the score for age dictated by the creditor's experience, so long as the score is not lower than the highest score the creditor assigns to any age category.

The Board proposed that an empirically derived credit-scoring system be defined as one that predicts, on the basis of a numerical score, an applicant's probable willingness and financial ability to repay the requested credit. The score would be derived from points assigned to key questions determined and weighted in accordance with past experience with applicants for credit.

The Board also proposed standards for what would constitute a demonstrably and statistically sound credit system as one developed by the application of, and in accordance with, generally accepted sampling procedures and principles, having a statistically significant relation to credit risk under accepted standards of analysis, and developed for the purpose of predicting the creditworthiness of applicants in relation to the legitimate business interests of the creditor, such as to minimize bad debt losses and operating expenses. (Section 202.2)

The creditor may use a borrowed system of credit scoring for age which satisfies the general criteria for such systems. If a borrowed system is used, validation from the creditor's own experience must begin within one year.^{4/}

Inquiries may be made concerning age in all cases, but the use of this information would be restricted, under the Board's draft rules, to the assessment of creditworthiness and may not be used arbitrarily to cut off or diminish credit due to an applicant's age.

The proposal would forbid creditors to require a reapplication, change the terms of an account or terminate an account because a person reaches a certain age or retires, if the applicant has not demonstrated unwillingness or inability to repay.

The Board specified that considerations of age would apply only to natural persons, not to businesses.

What information creditors may request: The Board proposed to add to existing rules (relating to sex or marital status) regarding

inquiries creditors may or may not make under ECOA, provisions implementing the 1976 Amendments to ECOA. Under the proposed rules, in general a creditor may not request information on a credit application as to the race, color, religion, or national origin of the applicant, or others associated with the applicant. The creditor may inquire as to the permanent residence or immigration status of the applicant. In specified circumstances, for enforcement purposes, the creditor is required to make inquiries otherwise proscribed. (See Data Notation below)

What use may be made of information creditors obtain: In general, the Board proposed, a creditor may consider any information obtained, so long as the information is not used to discriminate against an applicant on a prohibited basis.^{5/} Details and exceptions are noted in Section 202.6, substantially unchanged from the existing Regulation.

In a footnote to Section 202.6 the Board cautioned against the use of "insufficiently refined general information" not related to determination of creditworthiness, where the effect may be to discriminate against an applicant although discrimination is not intended.

The Board noted that in the legislative history of the amended Act the courts are directed to take account of the "effects" test developed in employment discrimination cases, and added:

"There are...practices...that are not specifically proscribed...that, in certain circumstances, also may have the effect of unlawfully discriminating against applicants if (i) those practices result in adverse credit decisions regarding applicants who are members of a class protected by the Act or

this (Regulation); (ii) such decisions occur at a significantly higher rate than adverse decisions involving applicants who are not members of the protected class, and (iii) the information or evaluation criteria underlying the practice does not have a manifest relationship to the creditor's determination of creditworthiness."

Special Purpose Credit Programs: In general, this proposal would permit otherwise discriminatory actions by creditors who offer certain types of special credit assistance programs intended to achieve social or economic goals. In such circumstances the creditor may refuse to extend such credit solely because an applicant does not qualify under the special requirements of a particular program recognized under the proposed Regulation. These include:

1. Credit assistance programs expressly authorized by Federal or State law for the benefit of an economically disadvantaged class of persons.

2. Credit assistance programs administered by a non-profit organization (as defined by the Internal Revenue Code, Section 501(c) as amended), for the benefit of its members or for the benefit of an economically disadvantaged class of persons.

3. Any special purpose credit program offered by a for-profit organization to meet special social needs that are in accord with the provisions of the regulation regarding such programs.

Data notation for enforcement purposes:^{6/} The Board proposed that creditors be required to inquire as to the sex, marital status, race-national

origin and age of applicants for residential mortgage credit, but that applicants have the right to decline to supply such information if they desire. Creditors would not be required to make their own assessment. Race or national origin categories proposed would be American Indian or Alaskan Native; Asian or Pacific Islander; Black; White; Hispanic and Other (at the applicant's option). The marital status categories would be married, unmarried and separated. Answers could be listed, at the creditor's option, on the application form or on a separate form that refers to the application.

Specialized treatment for certain types of credit:^{7/} The Board proposed exemptions from some of the Regulation B requirements with respect to credit transactions of utilities and other businesses, securities credit, incidental credit and governmental credit. With the addition of governmental credit, these proposed partial exemptions are similar to those in the existing Regulation B. They do not exempt these classes of creditors from the basic nondiscrimination requirements of the Act. Generally, they are exemptions from detailed requirements of Regulation B concerning notifications, furnishing credit information and retention of records and requests for, or use of, information about marital status and sex. In the cases of exemption from requirements concerning notifications and retention of records, applicants can override the exemption by written request. Section 202.3 (b through f) of the proposed Regulation provides details.

Pre-emption of inconsistent State laws:⁸⁻ The Board proposed that only States whose laws against discrimination in the granting of credit are inconsistent with Federal law would be preempted, and then only to the extent of the inconsistency. The proposals provided seven guidelines by which

creditors could assess State laws for the consistency with ECOA and Regulation B. (Section 202.11)

Key provisions of the proposed Regulation not discussed above that are unchanged, or substantially so, from the proposals made in July include:

--The general rule against discrimination. (Section 202.4)

--Notice to married people that they may request that their account be carried under the name of each spouse (except that the present proposals call for both signatures, not just one, on the request). (Section 202.10 (2))

--Provisions for interpretations of the Regulation. (Section 202.1 (d))

--Definition of discrimination as "to treat an applicant less favorably than other applicants." (Section 202.2 (n))

--Requests creditors may make for signatures (reworded without change in substance). (Section 202.7 (d))

FOOTNOTES

1/ Enforcement agencies, the creditors they regulate, and their addresses are:

National Banks

Comptroller of the Currency
Consumer Affairs Division
Washington, D.C. 20219

State Member Banks

Federal Reserve Bank serving the area in which the State member bank is located.

Nonmember Insured Banks

Federal Deposit Insurance Corporation Regional Director for the Region in which the nonmember insured bank is located.

Savings Institutions Insured by the FSLIC and Members of the FHLB System (except for Savings Bank insured by FDIC)

The FHLBB's Supervisory Agent in the Federal Home Loan Bank District in which the institution is located.

Federal Credit Unions

Regional Office of the National Credit Union Administration serving the area in which the Federal Credit Union is located.

Creditors Subject to Civil Aeronautics Board

Director, Bureau of Enforcement
Civil Aeronautics Board
1825 Connecticut Avenue, N.W.
Washington, D.C. 20428

Creditors Subject to Interstate Commerce Commission

Office of Proceedings
Interstate Commerce Commission
Washington, D.C. 20523

Creditors Subject to Packers and Stockyards Act

Nearest Packers and Stockyards Administration area supervisor.

Retail, Department Stores, Consumer Finance Companies, All Creditors not mentioned above and All Nonbank Credit Card issuers (Lenders operating on a local or regional basis should use the address of the F.T.C. Regional Office in which they operate)

Federal Trade Commission
Washington, D.C. 20580

Small Business Investment Companies

U.S. Small Business Administration
1441 L Street, N.W.
Washington, D.C. 20416

Brokers and Dealers
Securities and Exchange Commission
Washington, D.C. 20549

Federal Land Banks, Federal Land Bank Associations, Federal Intermediate
Credit Banks and Production Credit Associations
Farm Credit Administration
490 L'Enfant Plaza, S.W.
Washington, D.C. 20578

2/ The proposals that an adverse action has occurred if a creditor makes a counter offer of credit that the applicant does not accept, and that an adverse action has not occurred when credit is refused on grounds that granting the credit would be illegal were not in the July proposals.

3/ The requirements for reasons for denial are basically the same as in the July proposal, chiefly, that the reasons must be specific. However, they have been expanded, including a requirement to facilitate consumer complaints calling for inclusion in the statement of reasons of the name and address of the supervising Federal agency, and, in the interests of making the statement of reasons specific, inclusion of a greater number of reasons for denial.

4/ Authorization for creditors to make temporary use of a borrowed system of credit scoring for age, and the validation requirement, were not included in the July proposals.

5/ The Board's proposals defined "prohibited basis" as meaning race, color, religion, national origin, sex, marital status, or age (provided that the applicant has the capacity to enter into a binding contract); the fact that all or part of the applicant's income derives from any public assistance program, or the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act (Section 202.2 (y)). A footnote to this paragraph of the proposed Regulation said:

" 'Prohibited basis' ... refers also to the characteristics of individuals with whom the applicant deals. This means, for example, that ... a creditor may not discriminate against a non-Jewish applicant because of that person's business dealings with Jews, or discriminate against an applicant because of the characteristics of persons to whom the extension of credit relates (e.g., the prospective tenants in an apartment complex to be constructed with the proceeds of the credit requested), or because of the characteristics of other individuals residing in the neighborhood where the property offered for collateral is located."

6/ This requirement was not included in the July proposals, which, however, asked for comment on a number of questions concerning the issue whether such data should be collected by creditors in order to provide a basis for assessing compliance with the Act and Regulation B. The Justice Department, the Federal Trade Commission, the Veterans Administration and the Small Business Administration, as well as representatives of women's groups and the heads of the House and Senate Banking Committees urged the Board to require data collection for enforcement purposes.

7/ The July proposals contained a series of requests for public comment on whether certain classes of credit transactions should be exempted from some or all requirements of the Regulation.

8/ The July proposals provided, in effect, that all similar State laws would be assumed to be inconsistent, and would be pre-empted by the Federal law, pending application by the State to the Board for an exemption.