

FEDERAL RESERVE BANK
OF NEW YORK

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*To All Depository Institutions in the Second Federal Reserve
District, and Others Maintaining Sets of Board Regulations:*

Enclosed is a copy of the Official Staff Commentary on Regulation B, "Equal Credit Opportunity," effective September 30, 1996.

The revised pamphlet supersedes the previous printing of this Commentary and any subsequent amendments thereto.

This pamphlet has been punched with an additional hole so that it can be inserted into our two-volume 8-1/2 x 11 size binders.

Public Information Department

Official Staff Commentary on Regulation B Equal Credit Opportunity

As amended effective September 30, 1996



Any inquiry relating to Regulation B should be addressed to the Federal Reserve Bank of the District in which the inquiry arises.

November 1996

Contents

	<i>Page</i>		<i>Page</i>
Introduction	1	Section 202.8—Special-purpose credit programs	14
Section 202.1—Authority, scope, and purpose	1	Section 202.9—Notifications	16
Section 202.2—Definitions	1	Section 202.10—Furnishing of credit information	19
Section 202.3—Limited exceptions for certain classes of transactions	5	Section 202.11—Relation to state law ...	19
Section 202.4—General rule prohibiting discrimination	5	Section 202.12—Record retention	20
Section 202.5—Rules concerning taking of applications	6	Section 202.13—Information for monitoring purposes	21
Section 202.5a—Rules on providing appraisal reports	7	Section 202.14—Enforcement, penalties, and liabilities	22
Section 202.6—Rules concerning evaluation of applications	8	Appendix B—Model application forms ...	22
Section 202.7—Rules concerning extensions of credit	11	Appendix C—Sample notification forms .	23

Official Staff Commentary on Regulation B

As amended effective September 30, 1996

Following is an official staff interpretation of Regulation B issued under authority delegated by the Federal Reserve Board to officials in the Division of Consumer and Community Affairs. References are to sections of the regulation or the Equal Credit Opportunity Act (15 USC 1601 et seq.).

INTRODUCTION

1. *Official status.* Section 706(e) of the Equal Credit Opportunity Act protects a creditor from civil liability for any act done or omitted in good faith in conformity with an interpretation issued by a duly authorized official of the Federal Reserve Board. This commentary is the means by which the Division of Consumer and Community Affairs of the Federal Reserve Board issues official staff interpretations of Regulation B. Good faith compliance with this commentary affords a creditor protection under section 706(e) of the act.

2. *Issuance of interpretations.* Under appendix D to the regulation, any person may request an official staff interpretation. Interpretations will be issued at the discretion of designated officials and incorporated in this commentary following publication for comment in the *Federal Register*. Except in unusual circumstances, official staff interpretations will be issued only by means of this commentary.

3. *Status of previous interpretations.* Interpretations of Regulation B previously issued by the Federal Reserve Board and its staff have been incorporated into this commentary as appropriate. All other previous Board and staff interpretations, official and unofficial, are superseded by this commentary.

4. *Footnotes.* Footnotes in the regulation have the same legal effect as the text of the regulation, whether they are explanatory or illustrative in nature.

5. *Comment designations.* The comments are designated with as much specificity as possible according to the particular regulatory provision addressed. Each comment in the com-

mentary is identified by a number and the regulatory section or paragraph that it interprets. For example, comments to section 202.2(c) are further divided by subparagraph, such as comment 2(c)(1)(ii)-1 and comment 2(c)(2)(ii)-1.

SECTION 202.1—Authority, Scope, and Purpose

1(a) Authority and Scope

1. *Scope.* The Equal Credit Opportunity Act and Regulation B apply to all credit—commercial as well as personal—without regard to the nature or type of the credit or the creditor. If a transaction provides for the deferral of the payment of a debt, it is credit covered by Regulation B even though it may not be a credit transaction covered by Regulation Z (Truth in Lending). Further, the definition of creditor is not restricted to the party or person to whom the obligation is initially payable, as is the case under Regulation Z. Moreover, the act and regulation apply to all methods of credit evaluation, whether performed judgmentally or by use of a credit scoring system.

2. *Foreign applicability.* Regulation B generally does not apply to lending activities that occur outside the United States. The regulation does apply to lending activities that take place within the United States (as well as the Commonwealth of Puerto Rico and any territory or possession of the United States), whether or not the applicant is a citizen.

3. *Board.* The term “Board,” as used in this regulation, means the Board of Governors of the Federal Reserve System.

SECTION 202.2—Definitions

2(c) Adverse Action

Paragraph 2(c)(1)(i)

1. *Application for credit.* A refusal to refi-

nance 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.* If a credit card issuer terminates the open-end account of a customer because the customer has moved out of the card issuer's service area, the termination is "adverse action" for purposes of the regulation unless termination on this ground was explicitly provided for in the credit agreement between the parties. In cases where termination is adverse action, notification is required under section 202.9.

2. *Termination based on credit limit.* If a creditor terminates credit accounts that have low credit limits (for example, under \$400) but keeps open accounts with higher credit limits, the termination is adverse action and notification is required under section 202.9.

Paragraph 2(c)(2)(ii)

1. *Default—exercise of due-on-sale clause.* If a mortgagor sells or transfers mortgaged property without the consent of the mortgagee, and the mortgagee exercises its contractual right to accelerate the mortgage loan, the mortgagee may treat the mortgagor as being in default. An adverse-action notice need not be given to the mortgagor or the transferee. (See comment 2(e)-1 for treatment of a purchaser who requests to assume the loan.)

2. *Current delinquency or default.* The term "adverse action" does not include a creditor's termination of an account when the account-holder is currently in default or delinquent on that account. Notification in accordance with section 202.9 of the regulation generally is required, however, if the creditor's action is based on a past delinquency or default on the account.

Paragraph 2(c)(2)(iii)

1. *Point-of-sale transactions.* Denial of credit at point of sale is not adverse action except under those circumstances specified in the reg-

ulation. For example, denial at point of sale is not adverse action in the following situations:

- A credit cardholder presents an expired card or a card that has been reported to the card issuer as lost or stolen.
- The amount of a transaction exceeds a cash advance or credit limit.
- The circumstances (such as excessive use of a credit card in a short period of time) suggest that fraud is involved.
- The authorization facilities are not functioning.
- Billing statements have been returned to the creditor for lack of a forwarding address.

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.

Paragraph 2(c)(2)(v)

1. *Terms of credit versus type of credit offered.* When an applicant applies for credit and the creditor does not offer the credit terms requested by the applicant (for example, the interest rate, length of maturity, collateral, or amount of downpayment), a denial of the application for that reason is adverse action (unless the creditor makes a counteroffer that is accepted by the applicant) and the applicant is entitled to notification under section 202.9.

2(e) Applicant

1. *Request to assume loan.* If a mortgagor sells or transfers the mortgaged property and the buyer makes an application to the creditor to assume the mortgage loan, the mortgagee must treat the buyer as an applicant unless its policy is not to permit assumptions.

2(f) Application

1. *General.* A creditor has the latitude under the regulation to establish its own application process and to decide the type and amount of information it will require from credit applicants.

2. *"Procedures established."* The term refers to the actual practices followed by a creditor for making credit decisions as well as its stated application procedures. For example, if a creditor's stated policy is to require all applications to be in writing on the creditor's application form, but the creditor also makes credit decisions based on oral requests, the creditor's established procedures are to accept both oral and written applications.

3. *When an inquiry becomes an application.* A creditor is encouraged to provide consumers with information about loan terms. However, if in giving information to the consumer the creditor also evaluates information about the applicant, decides to decline the request, and communicates this to the applicant, the creditor has treated the inquiry as an application and must then comply with the notification requirements under section 202.9. Whether the inquiry becomes an application depends on how the creditor responds to the applicant, not on what the applicant says or asks.

4. *Examples of inquiries that are not applications.* The following examples illustrate situations in which only an inquiry has taken place:

- When a consumer calls to ask about loan terms and an employee explains the creditor's basic loan terms, such as interest rates, loan-to-value ratio, and debt-to-income ratio.
- When a consumer calls to ask about interest rates for car loans, and, in order to quote the appropriate rate, the loan officer asks for the make and sales price of the car and the amount of the downpayment, then gives the consumer the rate.
- When a consumer asks about terms for a loan to purchase a home and tells the loan officer her income and intended downpayment, but the loan officer only explains the creditor's loan-to-value ratio policy and other basic lending policies, without telling the consumer whether she qualifies for the loan.
- When a consumer calls to ask about terms for a loan to purchase vacant land and states his income and the sale price of the property to be financed, and asks whether

he qualifies for a loan, and the employee responds by describing the general lending policies, explaining that he would need to look at all of the applicant's qualifications before making a decision, and offering to send an application form to the consumer.

5. *Completed application—diligence requirement.* The regulation defines a completed application in terms that give a creditor the latitude to establish its own information requirements. Nevertheless, the creditor must act with reasonable diligence to collect information needed to complete the application. For example, the creditor should request information from third parties, such as a credit report, promptly after receiving the application. If additional information is needed from the applicant, such as an address or telephone number needed to verify employment, the creditor should contact the applicant promptly. (But see comment 9(a)(1)-3, which discusses the creditor's option to deny an application on the basis of incompleteness.)

2(g) Business Credit

1. *Definition.* The test for deciding whether a transaction qualifies as business credit is one of primary purpose. For example, an open-end credit account used for both personal and business purposes is not business credit unless the primary purpose of the account is business-related. A creditor may rely on an applicant's statement of the purpose for the credit requested.

2(j) Credit

1. *General.* Regulation B covers a wider range of credit transactions than Regulation Z (Truth in Lending). For purposes of Regulation B, a transaction is credit if there is a right to defer payment of a debt—regardless of whether the credit is for personal or commercial purposes, the number of installments required for repayment, or whether the transaction is subject to a finance charge.

2(l) Creditor

1. *Assignees.* The term "creditor" includes all persons participating in the credit decision. This may include an assignee or a potential

purchaser of the obligation who influences the credit decision by indicating whether or not it will purchase the obligation if the transaction is consummated.

2. Referrals to creditors. For certain purposes, the term “creditor” includes persons such as real estate brokers who do not participate in credit decisions but who regularly refer applicants to creditors or who select or offer to select creditors to whom credit requests can be made. These persons must comply with section 202.4, the general rule prohibiting discrimination, and with section 202.5(a), on discouraging applications.

2(p) Empirically Derived and Other Credit Scoring Systems

1. Purpose of definition. The definition under section 202.2(p)(1)(i) through (iv) sets the criteria that a credit system must meet in order for the system to use age as a predictive factor. Credit systems that do not meet these criteria are judgmental systems and may consider age only for the purpose of determining a “pertinent element of creditworthiness.” (Both types of systems may favor an elderly applicant. See section 202.6(b)(2).)

2. Periodic revalidation. The regulation does not specify how often credit scoring systems must be revalidated. To meet the requirements for statistical soundness, the credit scoring system must be revalidated frequently enough to ensure that it continues to meet recognized professional statistical standards. To ensure that predictive ability is being maintained, creditors must periodically review the performance of the system. This could be done, for example, by analyzing the loan portfolio to determine the delinquency rate for each score interval, or by analyzing population stability over time to detect deviations of recent applications from the applicant population used to validate the system. If this analysis indicates that the system no longer predicts risk with statistical soundness, the system must be adjusted as necessary to reestablish its predictive ability. A creditor is responsible for ensuring its system is validated and revalidated based on the creditor’s own data when it becomes available.

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).

2(w) Open-End Credit

1. Open-end real estate mortgages. The term “open-end credit” does not include negotiated advances under an open-end real estate mortgage or a letter of credit.

2(z) Prohibited Basis

1. Persons associated with applicant. “Prohibited basis” as used in this regulation refers not only to characteristics—the race, color, religion, national origin, sex, marital status, or age—of an applicant (or officers of an applicant in the case of a corporation) but also to the characteristics of individuals with whom an applicant is affiliated or with whom the applicant associates. This means, for example, that under the general rule stated in section 202.4, a creditor may not discriminate against an applicant because of that person’s personal or business dealings with members of a certain religion, because of the national origin of any persons associated with the extension of credit (such as the tenants in the apartment

complex being financed), or because of the race of other residents in the neighborhood where the property offered as collateral is located.

2. *National origin.* A creditor may not refuse to grant credit because an applicant comes from a particular country but may take the applicant's immigration status into account. A creditor may also take into account any applicable law, regulation, or executive order restricting dealings with citizens (or the government) of a particular country or imposing limitations regarding credit extended for their use.

3. *Public assistance program.* Any federal, state, or local governmental assistance program that provides a continuing, periodic income supplement, whether premised on entitlement or need, is "public assistance" for purposes of the regulation. The term includes (but is not limited to) Aid to Families with Dependent Children, food stamps, rent and mortgage supplement or assistance programs, Social Security and Supplemental Security Income, and unemployment compensation. Only physicians, hospitals, and others to whom the benefits are payable need consider Medicare and Medicaid as public assistance.

SECTION 202.3—Limited Exceptions for Certain Classes of Transactions

1. *Scope.* This section relieves burdens with regard to certain types of credit for which full application of the procedural requirements of the regulation is not needed. All classes of transactions remain subject to the general rule given in section 202.4, barring discrimination on a prohibited basis, and to any other provision not specifically excepted.

3(a) Public-Utilities Credit

1. *Definition.* This definition applies only to credit for the purchase of a utility service, such as electricity, gas, or telephone service. Credit provided or offered by a public utility for some other purpose—such as for financing the purchase of a gas dryer, telephone equipment, or other durable goods, or for insulation or other home improvements—is not excepted.

2. *Security deposits.* A utility company is a creditor when it supplies utility service and bills the user after the service has been provided. Thus, any credit term (such as a requirement for a security deposit) is subject to the regulation.

3. *Telephone companies.* A telephone company's credit transactions qualify for the exceptions provided in section 202.3(a)(2) only if the company is regulated by a government unit or files the charges for service, delayed payment, or any discount for prompt payment with a government unit.

3(c) Incidental Credit

1. *Examples.* If a service provider (such as a hospital, doctor, lawyer or retailer) allows the client or customer to defer the payment of a bill, this deferral of a debt is credit for purposes of the regulation, even though there is no finance charge and no agreement for payment in installments. Because of the exceptions provided by this section, however, these particular credit extensions are excepted from compliance with certain procedural requirements as specified in the regulation.

3(d) Government Credit

1. *Credit to governments.* The exception relates to credit extended to (not by) governmental entities. For example, credit extended to a local government by a creditor in the private sector is covered by this exception, but credit extended to consumers by a federal or state housing agency does not qualify for special treatment under this category.

SECTION 202.4—General Rule Prohibiting Discrimination

1. *Scope of section.* The general rule stated in section 202.4 covers all dealings, without exception, between an applicant and a creditor, whether or not addressed by other provisions of the regulation. Other sections of the regulation identify specific practices that the Board has decided are impermissible because they could result in credit discrimination on a basis prohibited by the act. The general rule covers, for example, application procedures, criteria

used to evaluate creditworthiness, administration of accounts, and treatment of delinquent or slow accounts. Thus, whether or not specifically prohibited elsewhere in the regulation, a credit practice that treats applicants differently on a prohibited basis violates the law because it violates the general rule. 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.

SECTION 202.5—Rules Concerning Taking of Applications

5(a) Discouraging Applications

1. *Potential applicants.* Generally, the regulation's protections apply only to persons who have requested or received an extension of credit. In keeping with the purpose of the act—to promote the availability of credit on a nondiscriminatory basis—section 202.5(a) covers acts or practices directed at potential applicants. Practices prohibited by this section include—

- a statement that the applicant should not bother to apply, after the applicant states that he is retired
- use of words, symbols, models or other forms of communication in advertising that express, imply, or suggest a discriminatory preference or a policy of exclusion in violation of the act
- use of interview scripts that discourage applications on a prohibited basis.

2. *Affirmative advertising.* A creditor may affirmatively solicit or encourage members of

traditionally disadvantaged groups to apply for credit, especially groups that might not normally seek credit from that creditor.

5(b) General Rules Concerning Requests for Information

1. *Requests for information.* This section governs the types of information that a creditor may gather. Section 202.6 governs how information may be used.

Paragraph 5(b)(2)

1. *Local laws.* Information that a creditor is allowed to collect pursuant to a “state” statute or regulation includes information required by a local statute, regulation, or ordinance.

2. *Information required by Regulation C.* Regulation C generally requires creditors covered by the Home Mortgage Disclosure Act (HMDA) to collect and report information about the race or national origin and sex of applicants for home-improvement loans and home-purchase loans, including some types of loans not covered by section 202.13. Certain creditors with assets under \$30 million, though covered by HMDA, are not required to collect and report these data; but they may do so at their option under HMDA, without violating the ECOA or Regulation B.

3. *Collecting information on behalf of creditors.* Loan brokers, correspondents, or other persons do not violate the ECOA or Regulation B if they collect information that they are otherwise prohibited from collecting, where the purpose of collecting the information is to provide it to a creditor that is subject to the Home Mortgage Disclosure Act or another federal or state statute or regulation requiring data collection.

5(d) Other Limitations on Information Requests

Paragraph 5(d)(1)

1. *Indirect disclosure of prohibited information.* The fact that certain credit-related information may indirectly disclose marital status does not bar a creditor from seeking such in-

formation. For example, the creditor may ask about—

- the applicant's obligation to pay alimony, child support, or separate maintenance
- the source of income to be used as the basis for repaying the credit requested, which could disclose that it is the income of a spouse
- whether any obligation disclosed by the applicant has a co-obligor, which could disclose that the co-obligor is a spouse or former spouse
- the ownership of assets, which could disclose the interest of a spouse

Paragraph 5(d)(2)

1. *Disclosure about income.* The sample application forms in appendix B to the regulation illustrate how a creditor may inform an applicant of the right not to disclose alimony, child support, or separate maintenance income.

2. *General inquiry about source of income.* Since a general inquiry about the source of income may lead an applicant to disclose alimony, child support, or separate maintenance, a creditor may not make such an inquiry on an application form without prefacing the request with the disclosure required by this paragraph.

3. *Specific inquiry about sources of income.* A creditor need not give the disclosure if the inquiry about income is specific and worded in a way that is unlikely to lead the applicant to disclose the fact that income is derived from alimony, child support, or separate maintenance payments. For example, an application form that asks about specific types of income such as salary, wages, or investment income need not include the disclosure.

5(e) Written Applications

1. *Requirement for written applications.* The requirement of written applications for certain types of dwelling-related loans is intended to assist the federal supervisory agencies in monitoring compliance with the ECOA and the Fair Housing Act. Model application forms

are provided in appendix B to the regulation, although use of a printed form of any kind is not required. A creditor will satisfy the requirement by writing down the information that it normally considers in making a credit decision. The creditor may complete the application on behalf of an applicant and need not require the applicant to sign the application.

2. *Telephone applications.* A creditor that accepts applications by telephone for dwelling-related credit covered by section 202.13 can meet the requirements for written applications by writing down pertinent information that is provided by the applicant(s).

3. *Computerized entry.* Information entered directly into and retained by a computerized system qualifies as a written application under this paragraph. (See the commentary to section 202.13(b), *Applications through electronic media* and *Applications through video*.)

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 section 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.

Paragraph 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 appli-

cant, but it must be given to the primary applicant where one is readily apparent.

Paragraph 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

SECTION 202.6—Rules Concerning Evaluation of Applications

6(a) General Rule Concerning Use of Information

1. *General.* When evaluating an application for credit, a creditor generally may consider any information obtained. However, a creditor may not consider in its evaluation of creditworthiness any information that it is barred by section 202.5 from obtaining.

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 USC 2000e et seq.), and the burdens of proof for such employment cases were codified by Congress in the Civil Rights Act of 1991 (42 USC 2000e-2). Congressional intent that this doctrine apply to the credit area is documented in the Senate Report that accompanied H.R. 6516, No. 94-589, pp. 4-5; and in the House Report that accompanied H.R. 6516, No. 94-210, p. 5. The act and regulation may prohibit a creditor practice that is discriminatory in effect because it has a disproportionately negative impact on a prohibited basis, even though the creditor has no intent to discriminate and the practice appears neutral on its face, unless the creditor practice meets a legitimate business need that cannot reasonably be achieved as well by means that are less disparate in their impact. For example, requiring that applicants have incomes in excess of a certain amount to qualify for an overdraft line of credit could mean that women and minority applicants will be rejected at a higher rate than men and nonminority applicants. If there is a demonstrable relationship between the income requirement and creditworthiness for the level of credit involved, however, use of the income standard would likely be permissible.

6(b) Specific Rules Concerning Use of Information

Paragraph 6(b)(1)

1. *Prohibited basis—marital status.* A creditor may not use marital status as a basis for de-

termining the applicant's creditworthiness. However, a creditor may consider an applicant's marital status for the purpose of ascertaining the creditor's rights and remedies applicable to the particular extension of credit. For example, in a secured transaction involving real property, a creditor could take into account whether state law gives the applicant's spouse an interest in the property being offered as collateral. 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.

2. *Prohibited basis—special-purpose credit.* In a special-purpose credit program, a creditor may consider a prohibited basis to determine whether the applicant possesses a characteristic needed for eligibility. (See section 202.8.)

Paragraph 6(b)(2)

1. *Favoring the elderly.* Any system of evaluating creditworthiness may favor a credit applicant who is age 62 or older. A credit program that offers more favorable credit terms to applicants age 62 or older is also permissible; a program that offers more favorable credit terms to applicants at an age lower than 62 is permissible only if it meets the special-purpose credit requirements of section 202.8.

2. *Consideration of age in a credit scoring system.* Age may be taken directly into account in a credit scoring system that is "demonstrably and statistically sound," as defined in section 202.2(p), with one limitation: applicants 62 years old or older must be treated at least as favorably as applicants who are under age 62. If age is scored by assigning points to an applicant's age category, elderly applicants must receive the same or a greater number of points as the most favored class of nonelderly applicants.

i. *Age-split scorecards.* A creditor may segment the population into scorecards based on the age of an applicant. In such a system, one card covers a narrow age range (for example, applicants in their twenties or younger) who are evaluated under attributes predictive for that age group. A second card covers all other applicants who are evaluated under the attributes predictive for that broad class. When a system uses a card covering a wide age range that encompasses elderly applicants, the credit scoring system does not score age. Thus, the system does not raise the issue of assigning a negative factor or value to the age of elderly applicants. But if a system segments the population by age into multiple scorecards, and includes elderly applicants in a narrower age range, the credit scoring system does score age. To comply with the act and regulation in such a case, the creditor must ensure that the system does not assign a negative factor or value to the age of elderly applicants as a class.

3. *Consideration of age in a judgmental system.* In a judgmental system, defined in section 202.2(t), a creditor may not take age directly into account in any aspect of the credit transaction. For example, the creditor may not reject an application or terminate an account because the applicant is 60 years old. But a creditor that uses a judgmental system may relate the applicant's age to other information about the applicant that the creditor considers in evaluating creditworthiness. For example:

- A creditor may consider the applicant's occupation and length of time to retirement to ascertain whether the applicant's income (including retirement income) will support the extension of credit to its maturity.
- A creditor may consider the adequacy of any security offered when the term of the credit extension exceeds the life expectancy of the applicant and the cost of realizing on the collateral could exceed the applicant's equity. (An elderly applicant might not qualify for a 5 percent down, 30-year mortgage loan but might qualify with a larger downpayment or a shorter loan maturity.)
- A creditor may consider the applicant's age to assess the significance of the length of

the applicant's employment (a young applicant may have just entered the job market) or length of time at an address (an elderly applicant may recently have retired and moved from a long-term residence).

As the examples above illustrate, the evaluation must be made in an individualized, case-by-case manner; and it is impermissible for a creditor, in deciding whether to extend credit or in setting the terms and conditions, to base its decision on age or information related exclusively to age. Age or age-related information may be considered only in evaluating other "pertinent elements of creditworthiness" that are drawn from the particular facts and circumstances concerning the applicant.

4. Consideration of age in a reverse mortgage. A reverse mortgage is a home-secured loan in which the borrower receives payments from the creditor and does not become obligated to repay these amounts (other than in the case of default) until the borrower dies, moves permanently from the home, or transfers title to the home, or upon a specified maturity date. Disbursements to the borrower under a reverse mortgage typically are determined by considering the value of the borrower's home, the current interest rate, and the borrower's life expectancy. A reverse mortgage program that requires borrowers to be age 62 or older is permissible under section 202.6(b)(2)(iv). In addition, under section 202.6(b)(2)(iii), a creditor may consider a borrower's age to evaluate a pertinent element of creditworthiness, such as the amount of the credit or monthly payments that the borrower will receive, or the estimated repayment date.

5. Consideration of age in a combined system. A creditor using a credit scoring system that qualifies as "empirically derived" under section 202.2(p) may consider other factors (such as a credit report or the applicant's cash flow) on a judgmental basis. Doing so will not negate the classification of the credit scoring component of the combined system as "demonstrably and statistically sound." While age could be used in the credit scoring portion, however, in the judgmental portion age may not be considered directly. It may be used only for the purpose of determining a "pertinent

element of creditworthiness." (See comment 6(b)(2)-3.)

6. Consideration of public assistance. When considering income derived from a public assistance program, a creditor may take into account, for example—

- the length of time an applicant will likely remain eligible to receive such income
- whether the applicant will continue to qualify for benefits based on the status of the applicant's dependents (such as Aid to Families with Dependent Children or Social Security payments to a minor)
- whether the creditor can attach or garnish the income to assure payment of the debt in the event of default

Paragraph 6(b)(5)

1. Consideration of an individual applicant. A creditor must evaluate income derived from part-time employment, alimony, child support, separate maintenance, retirement benefits, or public assistance (all referred to as "protected income") on an individual basis, not on the basis of aggregate statistics, and must assess its reliability or unreliability by analyzing the applicant's actual circumstances, not by analyzing statistical measures derived from a group.

2. Payments consistently made. In determining the likelihood of consistent payments of alimony, child support, or separate maintenance, a creditor may consider factors such as whether payments are received pursuant to a written agreement or court decree; the length of time that the payments have been received; whether the payments are regularly received by the applicant; the availability of court or other procedures to compel payment; and the creditworthiness of the payor, including the credit history of the payor when it is available to the creditor.

3. Consideration of income. A creditor need not consider income at all in evaluating creditworthiness. If a creditor does consider income, there are several acceptable methods, whether in a credit scoring or a judgmental system:

- A creditor may score or take into account

the total sum of all income stated by the applicant without taking steps to evaluate the income.

- A creditor may evaluate each component of the applicant's income, and then score or take into account reliable income separately from income that is not reliable, or the creditor may disregard that portion of income that is not reliable before aggregating it with reliable income.
- A creditor that does not evaluate all income components for reliability must treat as reliable any component of protected income that is not evaluated.

In considering the separate components of an applicant's income, the creditor may not automatically discount or exclude from consideration any protected income. Any discounting or exclusion must be based on the applicant's actual circumstances.

4. *Part-time employment, sources of income.*

A creditor may score or take into account the fact that an individual applicant has more than one source of earned income—a full-time and a part-time job or two part-time jobs. A creditor may also score or treat earned income from a secondary source differently than earned income from a primary source. However, the creditor may not score or otherwise take into account the number of sources for protected income—for example, retirement income, Social Security, alimony. Nor may the creditor treat negatively the fact that an applicant's only earned income is derived from a part-time job.

Paragraph 6(b)(6)

1. *Types of credit references.* A creditor may restrict the types of credit history and credit references that it will consider, provided that the restrictions are applied to all credit applicants without regard to sex, marital status, or any other prohibited basis. However, on the applicant's request, a creditor must consider credit information not reported through a credit bureau when the information relates to the same types of credit references and history that the creditor would consider if reported through a credit bureau.

Paragraph 6(b)(7)

1. *National origin—immigration status.* The applicant's immigration status and ties to the community (such as employment and continued residence in the area) could have a bearing on a creditor's ability to obtain repayment.

Accordingly, the creditor may consider and differentiate, for example, between a noncitizen who is a long-time resident with permanent resident status and a noncitizen who is temporarily in this country on a student visa.

2. *National origin—citizenship.* Under the regulation, a denial of credit on the ground that an applicant is not a United States citizen is not per se discrimination based on national origin.

SECTION 202.7—Rules Concerning Extensions of Credit

7(a) Individual Accounts

1. *Open-end credit—authorized user.* A creditor may not require a creditworthy applicant seeking an individual credit account to provide additional signatures. However, the creditor may condition the designation of an authorized user by the account holder on the authorized user's becoming contractually liable for the account, as long as the creditor does not differentiate on any prohibited basis in imposing this requirement.

2. *Open-end credit—choice of authorized user.* A creditor that permits an account holder to designate an authorized user may not restrict this designation on a prohibited basis. For example, if the creditor allows the designation of spouses as authorized users, the creditor may not refuse to accept a nonspouse as an authorized user.

3. *Overdraft authority on transaction accounts.* If a transaction account (such as a checking account or NOW account) includes an overdraft line of credit, the creditor may require that all persons authorized to draw on the transaction account assume liability for any overdraft.

7(b) Designation of Name

1. *Single name on account.* A creditor may require that joint applicants on an account designate a single name for purposes of administering the account and that a single name be embossed on any credit card(s) issued on the account. But the creditor may not require that the name be the husband's name. (See section 202.10 for rules governing the furnishing of credit history on accounts held by spouses.)

7(c) Action Concerning Existing Open-End Accounts

Paragraph 7(c)(1)

1. *Termination coincidental with marital status change.* When an account holder's marital status changes, a creditor generally may not terminate the account unless it has evidence that the account holder is unable or unwilling to repay. But the creditor may terminate an account on which both spouses are jointly liable, even if the action coincides with a change in marital status, when one or both spouses—

- repudiate responsibility for future charges on the joint account
- request separate accounts in their own names
- request that the joint account be closed

2. *Updating information.* A creditor may periodically request updated information from applicants but may not use events related to a prohibited basis—such as an applicant's retirement, reaching a particular age, or change in name or marital status—to trigger such a request.

Paragraph 7(c)(2)

1. *Procedure pending reapplication.* A creditor may require a reapplication from a contractually liable party, even when there is no evidence of unwillingness or inability to repay, if (1) the credit was based on the qualifications of a person who is no longer available to support the credit and (2) the creditor has information indicating that the account holder's income by itself may be insufficient to support the credit. While a reapplication is

pending, the creditor must allow the account holder full access to the account under the existing contract terms. The creditor may specify a reasonable time period within which the account holder must submit the required information.

7(d) Signature of Spouse or Other Person

1. *Qualified applicant.* The signature rules ensure that qualified applicants are able to obtain credit in their own names. Thus, when an applicant requests individual credit, a creditor generally may not require the signature of another person unless the creditor has first determined that the applicant alone does not qualify for the credit requested.

2. *Unqualified applicant.* When an applicant applies for individual credit but does not alone meet a creditor's standards, the creditor may require a cosigner, guarantor or the like—but cannot require that it be the spouse. (See commentary to section 202.7(d)(5) and (6).)

Paragraph 7(d)(1)

1. *Joint applicant.* The term "joint applicant" refers to someone who applies contemporaneously with the applicant for shared or joint credit. It does not refer to someone whose signature is required by the creditor as a condition for granting the credit requested.

Paragraph 7(d)(2)

1. *Jointly owned property.* If an applicant requests unsecured credit, does not own sufficient separate property, and relies on joint property to establish creditworthiness, the creditor must value the applicant's interest in the jointly owned property. A creditor may not request that a nonapplicant joint owner sign any instrument as a condition of the credit extension unless the applicant's interest does not support the amount and terms of the credit sought.

i. *Valuation of applicant's interest.* In determining the value of an applicant's interest in jointly owned property, a creditor may consider factors such as the form of ownership

and the property's susceptibility to attachment, execution, severance, or partition; the value of the applicant's interest after such action; and the cost associated with the action. This determination must be based on the form of ownership prior to or at consummation, and not on the possibility of a subsequent change. For example, in determining whether a married applicant's interest in jointly owned property is sufficient to satisfy the creditor's standards of creditworthiness for individual credit, a creditor may not consider that the applicant's separate property may be transferred into tenancy by the entirety after consummation. Similarly, a creditor may not consider the possibility that the couple may divorce. Accordingly, a creditor may not require the signature of the nonapplicant spouse in these or similar circumstances.

ii. *Other options to support credit.* If the applicant's interest in jointly owned property does not support the amount and terms of credit sought, the creditor may offer the applicant other options to provide additional support for the extension of credit. For example—

- A. requesting an additional party (see section 202.7(d)(5));
- B. offering to grant the applicant's request on a secured basis (see section 202.7(d)(4)); or
- C. asking for the signature of the joint owner on an instrument that ensures access to the property in the event of the applicant's death or default, but does not impose personal liability unless necessary under state law (e.g., a limited guarantee). A creditor may not routinely require, however, that a joint owner sign an instrument (such as a quitclaim deed) that would result in the forfeiture of the joint owner's interest in the property.

2. *Need for signature—reasonable belief.* A creditor's reasonable belief as to what instruments need to be signed by a person other than the applicant should be supported by a thorough review of pertinent statutory and decisional law or an opinion of the state attorney general.

Paragraph 7(d)(3)

1. *Residency.* In assessing the creditworthiness of a person who applies for credit in a community property state, a creditor may assume that the applicant is a resident of the state unless the applicant indicates otherwise.

Paragraph 7(d)(4)

1. *Creation of enforceable lien.* Some state laws require that both spouses join in executing any instrument by which real property is encumbered. If an applicant offers such property as security for credit, a creditor may require the applicant's spouse to sign the instruments necessary to create a valid security interest in the property. The creditor may not require the spouse to sign the note evidencing the credit obligation if signing only the mortgage or other security agreement is sufficient to make the property available to satisfy the debt in the event of default. However, if under state law both spouses must sign the note to create an enforceable lien, the creditor may require them to do so.

2. *Need for signature—reasonable belief.* Generally, a signature to make the secured property available will only be needed on a security agreement. A creditor's reasonable belief that, to ensure access to the property, the spouse's signature is needed on an instrument that imposes personal liability should be supported by a thorough review of pertinent statutory and decisional law or an opinion of the state attorney general.

3. *Integrated instruments.* When a creditor uses an integrated instrument that combines the note and the security agreement, the spouse cannot be required to sign the integrated instrument if the signature is only needed to grant a security interest. But the spouse could be asked to sign an integrated instrument that makes clear—for example, by a legend placed next to the spouse's signature—that the spouse's signature is only to grant a security interest and that signing the instrument does not impose personal liability.

Paragraph 7(d)(5)

1. *Qualifications of additional parties.* In es-

tablishing guidelines for eligibility of guarantors, cosigners, or similar additional parties, a creditor may restrict the applicant's choice of additional parties but may not discriminate on the basis of sex, marital status or any other prohibited basis. For example, the creditor could require that the additional party live in the creditor's market area.

2. Reliance on income of another person—individual credit. An applicant who requests individual credit relying on the income of another person (including a spouse in a non-community property state) may be required to provide the signature of the other person to make the income available to pay the debt. In community property states, the signature of a spouse may be required if the applicant relies on the spouse's separate income. If the applicant relies on the spouse's future earnings that as a matter of state law cannot be characterized as community property until earned, the creditor may require the spouse's signature, but need not do so—even if it is the creditor's practice to require the signature when an applicant relies on the future earnings of a person other than a spouse. (See section 202.6(c) on consideration of state property laws.)

3. Renewals. If the borrower's creditworthiness is reevaluated when a credit obligation is renewed, the creditor must determine whether an additional party is still warranted and, if not, release the additional party.

Paragraph 7(d)(6)

1. Guarantees. A guarantee on an extension of credit is part of a credit transaction and therefore subject to the regulation. A creditor may require the personal guarantee of the partners, directors, or officers of a business, and the shareholders of a closely held corporation, even if the business or corporation is creditworthy. The requirement must be based on the guarantor's relationship with the business or corporation, however, and not on a prohibited basis. For example, a creditor may not require guarantees only for women-owned or minority-owned businesses. Similarly, a creditor may not require guarantees only from

the married officers of a business or married shareholders of a closely held corporation.

2. Spousal guarantees. The rules in section 202.7(d) bar a creditor from requiring a signature of a *guarantor's spouse* just as they bar the creditor from requiring the signature of an *applicant's spouse*. For example, although a creditor may require all officers of a closely held corporation to personally guarantee a corporate loan, the creditor may not automatically require that spouses of married officers also sign the guarantee. If an evaluation of the financial circumstances of an officer indicates that an additional signature is necessary, however, the creditor may require the signature of a spouse in appropriate circumstances in accordance with section 202.7(d)(2).

7(e) Insurance

1. Differences in terms. Differences in the availability, rates, and other terms on which credit-related casualty insurance or credit life, health, accident, or disability insurance is offered or provided to an applicant does not violate Regulation B.

2. Insurance information. A creditor may obtain information about an applicant's age, sex, or marital status for insurance purposes. The information may only be used, however, for determining eligibility and premium rates for insurance, and not in making the credit decision.

SECTION 202.8—Special-Purpose Credit Programs

8(a) Standards for Programs

1. Determining qualified programs. The Board does not determine whether individual programs qualify for special-purpose credit status, or whether a particular program benefits an "economically disadvantaged class of persons." The agency or creditor administering or offering the loan program must make these decisions regarding the status of its program.

2. Compliance with a program authorized by federal or state law. A creditor does not violate Regulation B when it complies in good

faith with a regulation promulgated by a government agency implementing a special-purpose credit program under section 202.8(a)(1). It is the agency's responsibility to promulgate a regulation that is consistent with federal and state law.

3. *Expressly authorized.* Credit programs authorized by federal or state law include programs offered pursuant to federal, state, or local statute, regulation or ordinance, or by judicial or administrative order.

4. *Creditor liability.* A refusal to grant credit to an applicant is not a violation of the act or regulation if the applicant does not meet the eligibility requirements under a special-purpose credit program.

5. *Determining need.* In designing a special-purpose program under section 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.

8(b) Rules in Other Sections

1. *Applicability of rules.* A creditor that rejects an application because the applicant does not meet the eligibility requirements (common characteristic or financial need, for example) must nevertheless notify the applicant of action taken as required by section 202.9.

8(c) Special Rule Concerning Requests and Use of Information

1. *Request of prohibited information.* This section permits a creditor to request and consider certain information that would otherwise be prohibited by sections 202.5 and 202.6 to determine an applicant's eligibility for a particular program.

2. *Examples.* Examples of programs under which the creditor can ask for and consider information related to a prohibited basis are—

- energy conservation programs to assist the elderly, for which the creditor must consider the applicant's age
- programs under a Minority Enterprise Small Business Investment Corporation, for which a creditor must consider the applicant's minority status

8(d) Special Rule in the Case of Financial Need

1. *Request of prohibited information.* This section permits a creditor to request and consider certain information that would otherwise be prohibited by sections 202.5 and 202.6, and to require signatures that would otherwise be prohibited by section 202.7(d).

2. *Examples.* Examples of programs in which financial need is a criterion are—

- subsidized housing programs for low- to moderate-income households, for which a creditor may have to consider the applicant's receipt of alimony or child support, the spouse's or parents' income, etc.
- student loan programs based on the family's financial need, for which a creditor may have to consider the spouse's or parents' financial resources

3. *Student loans.* In a guaranteed student loan program, a creditor may obtain the signature of a parent as a guarantor when required by federal or state law or agency regulation, or when the student does not meet the creditor's standards of creditworthiness. (See sections 202.7(d)(1) and (5).) The creditor may not require an additional signature when a student has a work or credit history that satisfies the creditor's standards.

SECTION 202.9—Notifications

1. *Use of the term "adverse action."* The regulation does not require that a creditor use the term "adverse action" in communicating to an applicant that a request for an extension of credit has not been approved. In notifying an applicant of adverse action as defined by section 202.2(c)(1), a creditor may use any words or phrases that describe the action taken on the application.

2. *Expressly withdrawn applications.* When an applicant expressly withdraws a credit application, the creditor is not required to comply with the notification requirements under section 202.9. (The creditor must, however, comply with the record-retention requirements of the regulation. See section 202.12(b)(3).)

3. *When notification occurs.* Notification occurs when a creditor delivers or mails a notice to the applicant's last known address or, in the case of an oral notification, when the creditor communicates the credit decision to the applicant.

4. *Location of notice.* The notifications required under section 202.9 may appear on either or both sides of a form or letter.

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 section 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.

9(a) Notification of Action Taken, ECOA Notice, and Statement of Specific Reasons*Paragraph 9(a)(1)*

1. *Timing of notice—when an application is complete.* Once a creditor has obtained all the information it normally considers in making a credit decision, the application is complete and the creditor has 30 days in which to notify the applicant of the credit decision. (See also comment 2(f)-5.)

2. *Notification of approval.* Notification of approval may be express or by implication. For example, the creditor will satisfy the notification requirement when it gives the applicant the credit card, money, property, or services requested.

3. *Incompletion application—denial for incompleteness.* When an application is incomplete regarding matters that the applicant can complete and the creditor lacks sufficient data for a credit decision, the creditor may deny the application giving as the reason for denial that the application is incomplete. The creditor has the option, alternatively, of providing a notice of incompleteness under section 202.9(c).

4. *Incomplete application—denial for reasons other than incompleteness.* When an application is missing information but provides sufficient data for a credit decision, the creditor may evaluate the application and notify the applicant under this section as appropriate. If credit is denied, the applicant must be given the specific reasons for the credit denial (or notice of the right to receive the reasons); in this instance the incompleteness of the application cannot be given as the reason for the denial.

5. *Length of counteroffer.* Section 202.9(a)(1)(iv) does not require a creditor to hold a counteroffer open for 90 days or any other particular length of time.

6. *Counteroffer combined with adverse-action*

notice. A creditor that gives the applicant a combined counteroffer and adverse-action notice that complies with section 202.9(a)(2) need not send a second adverse-action notice if the applicant does not accept the counter offer. A sample of a combined notice is contained in form C-4 of appendix C to the regulation.

7. Denial of a telephone application. When an application is conveyed by means of telephone and adverse action is taken, the creditor must request the applicant's name and address in order to provide written notification under this section. If the applicant declines to provide that information, then the creditor has no further notification responsibility.

Paragraph 9(a)(3)

1. Coverage. In determining the rules in this paragraph that apply to a given business-credit application, a creditor may rely on the applicant's assertion about the revenue size of the business. (Applications to start a business are governed by the rules in section 202.9(a)(3)(i).) If an applicant applies for credit as a sole proprietor, the revenues of the sole proprietorship will determine which rules in the paragraph govern the application. However, if an applicant applies for business-purpose credit as an individual, the rules in paragraph 9(a)(3)(i) apply unless the application is for trade or similar credit.

2. Trade credit. The term "trade credit" generally is limited to a financing arrangement that involves a buyer and a seller—such as a supplier who finances the sale of equipment, supplies, or inventory; it does not apply to an extension of credit by a bank or other financial institution for the financing of such items.

3. Factoring. Factoring refers to a purchase of accounts receivable and thus is not subject to the act or regulation. If there is a credit extension incident to the factoring arrangement, the notification rules in section 202.9(a)(3)(ii) apply, as do other relevant sections of the act and regulation.

4. Manner of compliance. In complying with the notice provisions of the act and regulation, creditors offering business credit may follow

the rules governing consumer credit. Similarly, creditors may elect to treat all business credit the same (irrespective of revenue size) by providing notice in accordance with section 202.9(a)(3)(i).

5. Timing of notification. A creditor subject to section 202.9(a)(3)(ii)(A) is required to notify a business credit applicant, orally or in writing, of action taken on an application within a reasonable time of receiving a completed application. Notice provided in accordance with the timing requirements of section 202.9(a)(1) is deemed reasonable in all instances.

9(b) Form of ECOA Notice and Statement of Specific Reasons

Paragraph 9(b)(1)

1. Substantially similar notice. The ECOA notice sent with a notification of a credit denial or other adverse action will comply with the regulation if it is "substantially similar" to the notice contained in section 202.9(b)(1). For example, a creditor may add a reference to the fact that the ECOA permits age to be considered in certain credit scoring systems, or add a reference to a similar state statute or regulation and to a state enforcement agency.

Paragraph 9(b)(2)

1. Number of specific reasons. A creditor must disclose the principal reasons for denying an application or taking other adverse action. The regulation does not mandate that a specific number of reasons be disclosed, but disclosure of more than four reasons is not likely to be helpful to the applicant.

2. Source of specific reasons. The specific reasons disclosed under section 202.9(a)(2) and (b)(2) must relate to and accurately describe the factors actually considered or scored by a creditor.

3. Description of reasons. A creditor need not describe how or why a factor adversely affected an applicant. For example, the notice may say "length of residence" rather than "too short a period of residence."

4. Credit scoring system. If a creditor bases the denial or other adverse action on a credit

scoring system, the reasons disclosed must relate only to those factors actually scored in the system. Moreover, no factor that was a principal reason for adverse action may be excluded from disclosure. The creditor must disclose the actual reasons for denial (for example, "age of automobile") even if the relationship of that factor to predicting creditworthiness may not be clear to the applicant.

5. Credit scoring—method for selecting reasons. The regulation does not require that any one method be used for selecting reasons for a credit denial or other adverse action that is based on a credit scoring system. Various methods will meet the requirements of the regulation. One method is to identify the factors for which the applicant's score fell furthest below the average score for each of those factors achieved by applicants whose total score was at or slightly above the minimum passing score. Another method is to identify the factors for which the applicant's score fell furthest below the average score for each of those factors achieved by all applicants. These average scores could be calculated during the development or use of the system. Any other method that produces results substantially similar to either of these methods is also acceptable under the regulation.

6. Judgmental system. If a creditor uses a judgmental system, the reasons for the denial or other adverse action must relate to those factors in the applicant's record actually reviewed by the person making the decision.

7. Combined credit scoring and judgmental system. If a creditor denies an application based on a credit evaluation system that employs both credit scoring and judgmental components, the reasons for the denial must come from the component of the system that the applicant failed. For example, if a creditor initially credit scores an application and denies the credit request as a result of that scoring, the reasons disclosed to the applicant must relate to the factors scored in the system. If the application passes the credit scoring stage but the creditor then denies the credit request based on a judgmental assessment of the ap-

plicant's record, the reasons disclosed must relate to the factors reviewed judgmentally, even if the factors were also considered in the credit scoring component.

8. Automatic denial. Some credit-decision methods contain features that call for automatic denial because of one or more negative factors in the applicant's record (such as the applicant's previous bad credit history with that creditor, the applicant's declaration of bankruptcy, or the fact that the applicant is a minor). When a creditor denies the credit request because of an automatic-denial factor, the creditor must disclose that specific factor.

9. Combined ECOA-FCRA disclosures. The ECOA requires disclosure of the principal reasons for denying or taking other adverse action on an application for an extension of credit. The Fair Credit Reporting Act requires a creditor to disclose when it has based its decision in whole or in part on information from a source other than the applicant or from its own files. Disclosing that a credit report was obtained and used to deny the application, as the FCRA requires, does not satisfy the ECOA requirement to disclose specific reasons. For example, if the applicant's credit history reveals delinquent credit obligations and the application is denied for that reason, to satisfy section 202.9(b)(2) the creditor must disclose that the application was denied because of the applicant's delinquent credit obligations. To satisfy the FCRA requirement, the creditor must also disclose that a credit report was obtained and used to deny credit. Sample forms C-1 through C-5 of appendix C of the regulation provide for the two disclosures.

9(c) Incomplete Applications

Paragraph 9(c)(2)

1. Reapplication. If information requested by a creditor is submitted by an applicant after the expiration of the time period designated by the creditor, the creditor may require the applicant to make a new application.

6-196.8

Paragraph 9(c)(3)

1. Oral inquiries for additional information.

If the applicant fails to provide the information in response to an oral request, a creditor must send a written notice to the applicant within the 30-day period specified in section 202.9(c)(1) and (c)(2). If the applicant does provide the information, the creditor shall take action on the application and notify the applicant in accordance with section 202.9(a).

9(g) Applications Submitted Through a Third Party

1. *Third parties.* The notification of adverse action may be given by one of the creditors to whom an application was submitted. Alternatively, the third party may be a noncreditor.

2. *Third-party notice—enforcement agency.* If a single adverse action notice is being provided to an applicant on behalf of several creditors and they are under the jurisdiction of different federal enforcement agencies, the notice need not name each agency; disclosure of any one of them will suffice.

3. *Third-party notice—liability.* When a notice is to be provided through a third party, a creditor is not liable for an act or omission of the third party that constitutes a violation of the regulation if the creditor accurately and in a timely manner provided the third party with the information necessary for the notification and maintains reasonable procedures adapted to prevent such violations.

SECTION 202.10—Furnishing of Credit Information

1. *Scope.* The requirements of section 202.10 for designating and reporting credit information apply only to creditors that furnish credit information to credit bureaus or to other creditors. There is no requirement that a creditor furnish credit information on its accounts.

2. *Reporting on all accounts.* The requirements of section 202.10 apply only to accounts held or used by spouses. However, a creditor has the option to designate all joint accounts (or all accounts with an authorized user) to reflect the participation of both parties, whether or not the accounts are held by persons married to each other.

3. *Designating accounts.* In designating accounts and reporting credit information, a creditor need not distinguish between accounts on which the spouse is an authorized user and accounts on which the spouse is a contractually liable party.

4. *File and index systems.* The regulation does not require the creation or maintenance of separate files in the name of each participant on a joint or user account, or require any other particular system of recordkeeping or indexing. It requires only that a creditor be able to report information in the name of each spouse on accounts covered by section 202.10. Thus, if a creditor receives a credit inquiry about the wife, it should be able to locate her credit file without asking the husband's name.

10(a) Designation of Accounts

1. *New parties.* When new parties who are spouses undertake a legal obligation on an account, as in the case of a mortgage-loan assumption, the creditor should change the designation on the account to reflect the new parties and should furnish subsequent credit information on the account in the new names.

2. *Request to change designation of account.* A request to change the manner in which information concerning an account is furnished does not alter the legal liability of either spouse upon the account and does not require a creditor to change the name in which the account is maintained.

SECTION 202.11—Relation to State Law

11(a) Inconsistent State Laws

1. *Preemption determination—New York.* Effective November 11, 1988, the Board has determined that the following provisions in the state law of New York are preempted by the federal law:

- Article 15, Section 296a(1)(b)—Unlawful discriminatory practices in relation to credit on the basis of race, creed, color, national

origin, age, sex, marital status, or disability. This provision is preempted to the extent that it bars taking a prohibited basis into account when establishing eligibility for certain special-purpose credit programs.

- Article 15, Section 296a(1)(c)—Unlawful discriminatory practice to make any record or inquiry based on race, creed, color, national origin, age, sex, marital status, or disability. This provision is preempted to the extent that it bars a creditor from requesting and considering information regarding the particular characteristics (for example, race, national origin, or sex) required for eligibility for special-purpose credit programs.

2. *Preemption determination—Ohio.* Effective July 23, 1990, the Board has determined that the following provision in the state law of Ohio is preempted by the federal law:

- Section 4112.021(B)(1)—Unlawful discriminatory practices in credit transactions. This provision is preempted to the extent that it bars asking or favorably considering the age of an elderly applicant; prohibits the consideration of age in a credit scoring system; permits without limitation the consideration of age in real estate transactions; and limits the consideration of age in special-purpose credit programs to certain government-sponsored programs identified in the state law.

SECTION 202.12—Record Retention

12(a) Retention of Prohibited Information

1. *Receipt of prohibited information.* Unless the creditor specifically requested such information, a creditor does not violate this section when it receives prohibited information from a consumer reporting agency.

2. *Use of retained information.* Although a creditor may keep in its files prohibited information as provided in section 202.12(a), the creditor may use the information in evaluating

credit applications only if permitted to do so by section 202.6.

12(b) Preservation of Records

1. *Copies.* A copy of the original record includes carbon copies, photocopies, microfilm or microfiche copies, or copies produced by any other accurate retrieval system, such as documents stored and reproduced by computer. A creditor that uses a computerized or mechanized system need not keep a written copy of a document (for example, an adverse action notice) if it can regenerate all pertinent information in a timely manner for examination or other purposes.

2. *Computerized decisions.* A creditor that enters information items from a written application into a computerized or mechanized system and makes the credit decision mechanically, based only on the items of information entered into the system, may comply with section 202.12(b) by retaining the information actually entered. It is not required to store the complete written application, nor is it required to enter the remaining items of information into the system. If the transaction is subject to section 202.13, however, the creditor is required to enter and retain the data on personal characteristics in order to comply with the requirements of that section.

Paragraph 12(b)(3)

1. *Withdrawn and brokered applications.* In most cases, the 25-month retention period for applications runs from the date a notification is sent to the applicant granting or denying the credit requested. In certain transactions, a creditor is not obligated to provide a notice of the action taken. (See, for example, comment 9-2.) In such cases, the 25-month requirement runs from the date of application, as when—

- an application is withdrawn by the applicant
- an application is submitted to more than one creditor on behalf of the applicant, and the application is approved by one of the other creditors

SECTION 202.13—Information for Monitoring Purposes

13(a) Information to Be Requested

1. *Natural person.* Section 202.13 applies only to applications from natural persons.

2. *Principal residence.* The requirements of section 202.13 apply only if an application relates to a dwelling that is or will be occupied by the applicant as the principal residence. A credit application related to a vacation home or a rental unit is not covered. In the case of a two- to four-unit dwelling, the application is covered if the applicant intends to occupy one of the units as a principal residence.

3. *Temporary financing.* An application for temporary financing to construct a dwelling is not subject to section 202.13. But an application for both a temporary loan to finance construction of a dwelling and a permanent mortgage loan to take effect upon the completion of construction is subject to section 202.13.

4. *New principal residence.* A person can have only one principal residence at a time. However, if a person buys or builds a new dwelling that will become that person's principal residence within a year or upon completion of construction, the new dwelling is considered the principal residence for purposes of section 202.13.

5. *Transactions not covered.* The information-collection requirements of this section apply to applications for credit primarily for the purchase or refinancing of a dwelling that is or will become the applicant's principal residence. Therefore, applications for credit secured by the applicant's principal residence but made primarily for a purpose other than the purchase or refinancing of the principal residence (such as loans for home improvement and debt consolidation) are not subject to the information-collection requirements. An application for an open-end home equity line of credit is not subject to this section unless it is readily apparent to the creditor when the application is taken that the primary purpose of the line is for the purchase or refinancing of a principal dwelling.

6. *Refinancings.* A refinancing occurs when

an existing obligation is satisfied and replaced by a new obligation undertaken by the same borrower. A creditor that receives an application to refinance an existing extension of credit made by that creditor for the purchase of the applicant's dwelling may request the monitoring information again but is not required to do so if it was obtained in the earlier transaction.

7. *Data collection under Regulation C.* See comment 5(b)(2)-2.

13(b) Obtaining of Information

1. *Forms for collecting data.* A creditor may collect the information specified in section 202.13(a) either on an application form or on a separate form referring to the application.

2. *Written applications.* The regulation requires written applications for the types of credit covered by section 202.13. A creditor can satisfy this requirement by recording in writing or by means of computer the information that the applicant provides orally and that the creditor normally considers in a credit decision.

3. *Telephone, mail applications.* If an applicant does not apply in person for the credit requested, a creditor does not have to complete the monitoring information. For example:

- When a creditor accepts an application by telephone, it does not have to request the monitoring information.
- When a creditor accepts an application by mail, it does not have to make a special request to the applicant if the applicant fails to complete the monitoring information on the application form sent to the creditor.

If it is not evident on the face of the application that it was received by mail or telephone, the creditor should indicate on the form or other application record how the application was received.

4. *Applications through electronic media.* If an applicant applies through an electronic medium (for example, the Internet or a facsimile) without video capability that allows the credi-

tor to see the applicant, the creditor may treat the application as if it were received by mail or telephone.

5. *Applications through video.* If a creditor takes an application through a medium that allows the creditor to see the applicant, the creditor treats the application as taken in person and must note the monitoring information on the basis of visual observation or surname, if the applicant chooses not to provide the information.

6. *Applications through loan-shopping services.* When a creditor receives an application through an unaffiliated loan-shopping service, it does not have to request the monitoring information for purposes of the ECOA or Regulation B. Creditors subject to the Home Mortgage Disclosure Act should be aware, however, that data collection may be called for under Regulation C, which generally requires creditors to report, among other things, the sex and race or national origin of an applicant on brokered applications or applications received through a correspondent.

7. *Inadvertent notation.* If a creditor inadvertently obtains the monitoring information in a dwelling-related transaction not covered by section 202.13, the creditor may process and retain the application without violating the regulation.

13(c) Disclosure to Applicant(s)

1. *Procedures for providing disclosures.* The disclosures to an applicant regarding the monitoring information may be provided in writing. Appendix B contains a sample disclosure. A creditor may devise its own disclosure so long as it is substantially similar. The creditor need not orally request the applicant to provide the monitoring information if it is requested in writing.

13(d) Substitute Monitoring Program

1. *Substitute program.* An enforcement agency may adopt, under its established rulemaking or enforcement procedures, a program requiring creditors under its jurisdiction to collect information in addition to that required by this section.

SECTION 202.14—Enforcement, Penalties, and Liabilities

14(c) Failure of Compliance

1. *Inadvertent errors.* Inadvertent errors include, but are not limited to, clerical mistake, calculation error, computer malfunction, and printing error. An error of legal judgment is not an inadvertent error under the regulation.

2. *Correction of error.* For inadvertent errors that occur under sections 202.12 and 202.13, this section requires that they be corrected prospectively only.

APPENDIX B—Model Application Forms

1. *FHLMC/FNMA form—residential loan application.* The uniform residential loan application form (FHLMC 65/FNMA 1003), including supplemental form (FHLMC 65A/FNMA 1003A), prepared by the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association and dated May 1991 may be used by creditors without violating this regulation even though the form's listing of race or national origin categories in the "Information for Government Monitoring Purposes" section differs from the classifications currently specified in section 202.13(a)(1). The classifications used on the FNMA-FHLMC form are those required by the U.S. Office of Management and Budget for notation of race and ethnicity by federal programs in their administrative reporting and statistical activities. Creditors that are governed by the monitoring requirements of Regulation B (which limits collection to applications primarily for the purchase or refinancing of the applicant's principal residence) should delete, strike, or modify the data-collection section on the form when using it for transactions not covered by section 202.13(a) to ensure that they do not collect the information. Creditors that are subject to more extensive collection requirements by a substitute monitoring program under section 202.13(d) or by the Home Mortgage Disclosure Act (HMDA) may use the form as issued, in compliance with that substitute program or HMDA.

2. *FHLMC/FNMA form—home-improvement loan application.* The home-improvement and energy loan application form (FHLMC 703/FNMA 1012), prepared by the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association and dated October 1986, complies with the requirements of the regulation for some creditors but not others because of the form's section "Information for Government Monitoring Purposes." Creditors that are governed by section 202.13(a) of the regulation (which limits collection to applications primarily for the purchase or refinancing of the applicant's principal residence) should delete, strike, or modify the data-collection section on the form when using it for transactions not covered by section 202.13(a) to ensure that they do not collect the information. Creditors that are subject to more extensive collection requirements by a substitute monitoring program under sec-

tion 202.13(d) may use the form as issued, in compliance with that substitute program.

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

