

- Which of the borrower's principals are required to provide a personal guarantee and the type of guarantee required based on different ownership structures for the business. The letter also clarifies what constitutes an associated borrower.
- The documentation you will need to submit and standards you will need to meet to request and qualify for a waiver.
- New NCUA procedures intended to streamline the process for obtaining waivers for credit unions buying a participation interest in an MBL.

I appreciate hearing constructive views that help NCUA improve the clarity of our rules and guidance.

If your credit union makes or plans to make MBLs, I encourage you to review the attached supervisory guidance. It will not only help you understand the MBL waiver process, it also contains guidance on sound risk management practices that will aid you in maintaining a safe and sound MBL portfolio.

Adhering to these risk management principles will help you tailor loans to meet the specific needs and financial capabilities of your members with small businesses.

If you have any questions related to this letter, please contact NCUA's Office of Examination and Insurance at 703-518-6360 or EIMail@ncua.gov.

Sincerely,

/s/

Debbie Matz
Chairman



Office of Consumer Protection
Fair Lending Guide

March 2013

National Credit Union Administration Fair Lending Guide

Table of Contents

| | |
|--|----|
| Using this Guide | 2 |
| Introduction | 3 |
| Equal Credit Opportunity Act (Regulation B) | |
| Overview | 6 |
| Operational Requirements | 9 |
| Review Considerations..... | 12 |
| Checklist..... | 18 |
| Definitions | 24 |
| Fair Housing Act | |
| Overview | 29 |
| Operational Requirements | 32 |
| Review Considerations..... | 33 |
| Checklist..... | 37 |
| Definitions | 38 |
| Home Mortgage Disclosure Act (Regulation C) | |
| Overview | 40 |
| Operational Requirements | 43 |
| Review Considerations..... | 45 |
| Checklist..... | 48 |
| Definitions | 51 |

Using this Guide

This guide is intended for use by a credit union's board of directors and management, compliance officers, and others having responsibility for fair lending compliance as part of their duties. While the guide covers federal fair lending laws and regulations that affect federal credit unions, it does not address all federal consumer protection laws or any state laws.

This fair lending guide is divided into five sections:

- **Overviews** – provide a brief description of what is covered in each fair lending law and regulation, what the regulations require of credit unions, and some potential risks.
- **Operational requirements** – denote specific requirements covered in each fair lending law and regulation and possible administrative actions for noncompliance.
- **Review Considerations** – contain various areas management should consider when evaluating fair lending compliance issues or developing compliance policies.
- **Checklists** – can be used to test compliance with the various fair lending laws and regulations, or as a starting point in developing a policy for compliance with the various regulations. The questions are written so that a “yes” answer indicates compliance with the regulation, and a “no” answer indicates a potential problem area
- **Definitions** – defines terms used in the narrative sections of this guide as well as terms used in each fair lending law and regulation.

While the content of this guide was carefully reviewed for applicability and accuracy, changes occur in the wording and interpretation of consumer compliance regulations. If a situation arises where this guide becomes inconsistent with the provisions of applicable laws or regulations, the requirement of the law or regulation will prevail.

Introduction

Overview of Fair Lending Laws and Regulations

This overview provides a basic and abbreviated discussion of federal fair lending laws and regulations. It is adapted from the Interagency Policy Statement on Fair Lending issued in March 1994.

The Equal Credit Opportunity Act (ECOA) prohibits discrimination in any aspect of a credit transaction. It applies to any extension of credit, including extensions of credit to small businesses, corporations, partnerships, and trusts.

The ECOA prohibits discrimination based on:

- Race or color
- Religion
- National origin
- Sex
- Marital status
- Age (provided the applicant has the capacity to contract)
- The applicant's receipt of income derived from any public assistance program
- The applicant's exercise, in good faith, of any right under the Consumer Credit Protection Act

Regulation B, found at 12 CFR part 1002, implements the ECOA. Regulation B describes lending acts and practices that are specifically prohibited, permitted, or required. Official staff interpretations of the regulation are found in Supplement I to 12 CFR part 1002.

The Fair Housing Act (FH Act) prohibits discrimination in all aspects of "residential real-estate related transactions," including but not limited to:

- Making loans to buy, build, repair or improve a dwelling
- Purchasing real estate loans
- Selling, brokering, or appraising residential real estate
- Selling or renting a dwelling

The FH Act prohibits discrimination based on:

- Race or color
- National origin
- Religion

- Sex
- Familial status (defined as children under the age of 18 living with a parent or legal custodian, pregnant women, and people securing custody of children under 18)
- Handicap

U.S. Department of Housing and Urban Development (HUD) regulations implementing the FH Act are found at 24 CFR Part 100. Because both the FH Act and the ECOA apply to mortgage lending, lenders may not discriminate in mortgage lending based on any of the prohibited factors in either list.

Under the ECOA, it is unlawful for a lender to discriminate on a prohibited basis in any aspect of a credit transaction, and under both the ECOA and the FH Act, it is unlawful for a lender to discriminate on a prohibited basis in a residential real-estate-related transaction. Under one or both of these laws, a lender may not, because of a prohibited factor:

- Fail to provide information or services or provide different information or services regarding any aspect of the lending process, including credit availability, application procedures, or lending standards
- Discourage or selectively encourage applicants with respect to inquiries about or applications for credit
- Refuse to extend credit or use different standards in determining whether to extend credit
- Vary the terms of credit offered, including the amount, interest rate, duration, or type of loan
- Use different standards to evaluate collateral
- Treat a borrower differently in servicing a loan or invoking default remedies
- Use different standards for pooling or packaging a loan in the secondary market.

A lender may not express, orally or in writing, a preference based on prohibited factors or indicate that it will treat applicants differently on a prohibited basis. A violation may still exist even if a lender treated applicants equally.

A lender may not discriminate on a prohibited basis because of the characteristics of:

- An applicant, prospective applicant, or borrower
- A person associated with an applicant, prospective applicant, or borrower (for example, a co-applicant, spouse, business partner, or live-in aide)
- The present or prospective occupants of either the property to be financed or the characteristics of the neighborhood or other area where property to be financed is located.

Finally, the FH Act requires lenders to make reasonable accommodations for a person with disabilities when such accommodations are necessary to afford the person an equal opportunity to apply for credit.

National Credit Union Administration (NCUA) Enforcement of Fair Lending Laws

NCUA implemented its fair lending examination program in 1999. With the exception of those federally insured credit unions with assets over \$10 billion, which are under the authority of the Consumer Financial Protection Bureau, NCUA enforces ECOA and Regulation B in federal credit unions and the Home Mortgage Disclosure Act (HMDA) and Regulation C in all federally insured credit unions.

NCUA's fair lending examination program also assesses compliance with the FH Act, but HUD and the U.S. Department of Justice (DOJ) enforce the FH Act. NCUA reports violations of the FH Act to HUD or DOJ. NCUA conducts fair lending examinations at and supervisory contacts with federal credit unions to assess compliance with fair lending laws using the Federal Financial Institutions Examination Council (FFIEC) Interagency Fair Lending Examination Procedures (August 2009).

EQUAL CREDIT OPPORTUNITY ACT (REGULATION B) OVERVIEW

The Equal Credit Opportunity Act (ECOA), implemented by Regulation B (12 CFR 1002), promotes availability of credit to all creditworthy applicants without regard to race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to contract), receipt of public assistance, or good faith exercise of any rights under the Consumer Credit Protection Act.

The basic rule of Regulation B, as found in §1002.4, is:
"A creditor shall not discriminate against any applicant on a prohibited basis with respect to any aspect of a credit transaction."

Prohibited basis refers not only to the characteristics of the applicant, but also to the characteristics of individuals with whom the applicant is affiliated or associates. Therefore, a credit union may not discriminate against a member-applicant based on a prohibited basis characteristic of an associated individual. For example, a credit union cannot discriminate against an applicant because of the race of the residents in the neighborhood where the collateral property is located.

Credit transaction means every aspect of an applicant's dealings with a credit union regarding an application for credit or an existing extension of credit including, but not limited to, information requirements, investigation procedures, standards of creditworthiness, terms of credit, furnishing of credit information, revocation, alteration, or termination of credit, and collection procedures.

Regulation B also requires credit unions to do the following:

- Notify applicants of the credit decision within 30 days of receiving a completed application.
- Retain records of credit applications for 25 months after notifying the member of its credit decision.
- Collect information about the applicant's race and other personal characteristics in applications for certain dwelling-related loans.
- Provide applicants with copies of appraisal reports used in connection with credit transactions.

Credit Applications

Regulation B prevents credit unions from discouraging prospective applicants from making or pursuing an application.

Credit unions are encouraged to use industry standard form applications. A credit union choosing to use a non-standard credit application form should obtain a legal opinion stating the forms comply with the applicable legal requirements.

The application may request any information, except for information about the member's:

- Spouse, unless the spouse will use or is contractually liable on the account or the applicant relies on the spouse's income
- Marital status when applying for unsecured credit when applying for secured credit, the application may use only the terms married, unmarried, or separated
- Sex, race, color, religion, and national origin
- Childrearing or childbearing, such as birth control practices, intentions, or capability to bear children

A credit union may consider any information obtained in the credit application provided it does not use the information to discriminate against an applicant on a prohibited basis. An exception to this rule relates to the consideration of age in determining an applicant's creditworthiness.

Self-Test for Compliance

On April 15, 2003, Regulation B was amended to address the collection of applicants' personal characteristics in connection with non-mortgage credit. The mandatory compliance date was April 15, 2004.

This exception allows creditors to collect personal characteristics in a self-test for compliance with the ECOA in order to allow creditors to develop compliance programs that utilize applicant data in a controlled and targeted manner. A self-test is a program, practice, or study designed and used by a creditor specifically to determine compliance with the ECOA. The creditor must take corrective action when the results of the self-test indicate that "it is more likely than not" that a violation occurred.

Creditors that conduct a self-test and request information about personal characteristics must disclose to applicants that:

- Providing the information is optional
- It is being collected to monitor for compliance with the ECOA
- It will not be used in making the credit decision
- If applicable, information may be noted based on visual observation or surname

Effects Test

While not specifically mentioned in the ECOA, the legislative history of the ECOA indicates Congress intended an “effects test” concept to apply to a credit union’s determination of creditworthiness. The effects test refers to a credit practice that appears facially neutral, but has a disproportionately negative effect on a prohibited basis, even though the credit union has no intent to discriminate. This type of practice is discriminatory, in effect, unless the credit union can demonstrate the practice meets a legitimate business need that cannot be reasonably achieved by means less disparate in impact.

Answering the following questions should assist in determining if the credit union’s credit practices result in a potential violation of the effects test:

1. Does a particular credit practice have a statistically disproportionate impact on a protected group (those covered under the prohibited basis definition)?
2. If so, can the credit union show that the practice serves a genuine business need?
3. If so, is there a less discriminating way to meet that business need?

Appraisals

Currently, federal credit unions are subject to the appraisal requirements outlined in Section 701.31(c)(5) and Part 722 of the NCUA Rules and Regulations.

Effective January 18, 2014, federal credit unions will be subject to Section 1002.14 (Rules on providing appraisals and other valuations) of Regulation B. Refer to Operational Requirements section for more information.

Associated Risks

- Compliance risk can occur when the credit union fails to implement the necessary controls to comply with the ECOA.
- Reputation risk can occur when the credit union incurs fines and penalties or receives negative publicity or declined membership confidence as a result of failure to comply with ECOA.

Additional Information

The Consumer Financial Protection Bureau’s website contains additional information at <http://www.consumerfinance.gov/>.

Please note the ECOA and the Fair Housing Act should be read together in order to fully understand the scope of a credit union’s fair lending obligations.

EQUAL CREDIT OPPORTUNITY ACT (REGULATION B) OPERATIONAL REQUIREMENTS

Disclosures / Notices

Appraisal Reports [Section 1002.14]

Effective January 18, 2014, Section 1002.14 will:

- Require creditors to notify applicants within three business days of receiving an application of their right to receive a copy of appraisals developed.
- Require creditors to provide applicants a copy of each appraisal and other written valuation promptly upon their completion or three business days before consummation (for closed-end credit) or account opening (for open-end credit), whichever is earlier.
- Permit applicants to waive the timing requirement for providing these copies. However, applicants who waive the timing requirement must be given a copy of all appraisals and other written valuations at or prior to consummation or account opening, or if the transaction is not consummated or the account is not opened, no later than 30 days after the creditor determines the transaction will not be consummated or the account will not be opened.
- Prohibit creditors from charging for the copy of appraisals and other written valuations, but permits creditors to charge applicants reasonable fees for the cost of the appraisals or other written valuation unless applicable law provides otherwise.

Notification of Action Taken [Section 1002.9(a)]

The creditor must notify an applicant of the action taken on a credit application, in accordance with the requirements of Section 1002.9. The notification must be in writing and must include a statement of the action taken, the name and address of the creditor, a statement of the provisions of Section 701(a) of the ECOA (see Section 1002.9(b)), the name and address of the creditor's federal regulator, and a statement of the specific reasons for the action or the disclosure of the right to obtain such reasons. Generally, the notice must be provided within 30 days after receipt of a completed application. The notification requirements for business credit applicants may vary somewhat as described in Section 1002.9(a)(3).

ECOA Notice [Section 1002.9(b)]

When providing a notification of action taken in connection with the requirements of Section 1002.9(a), the creditor must provide a statement of the provisions of Section 701(a) of the ECOA that is substantially similar to the language contained in Section 1002.9(b).

Monitoring Information [Section 1002.13]

A creditor must inform applicant(s) for a home mortgage loan that the federal government requests information on ethnicity, race, sex, marital status, and age for monitoring purposes. The creditor must also inform the applicant(s) that if they choose not to provide the information, the creditor is required to note the ethnicity, race, and sex on the basis of visual observation or surname.

Equal Housing Lender Poster [NCUA Rules and Regulations Sections 701.31(d)(2)]

Federal credit unions engaging in real estate-related lending must display a notice of nondiscrimination. The notice (with the prescribed logo and language) must be placed in the public lobby of the credit union and in the public areas of each office where such loans are made and must be clearly visible to the general public.

Written Programs / Documentation

Written Applications [Section 1002.4(c)]

A creditor must take written applications for the types of credit covered by Section 1002.13(a), i.e., applications for credit related to the purchase or refinancing of a principal residence secured by the residence.

Recordkeeping

Record Retention [Section 1002.12]

Applications, supporting information, and required notifications generally must be retained for 25 months (12 months for business credit) from the date of the notice of action taken. A longer retention period may apply if an investigation or enforcement proceeding is underway.

Creditors must retain for 25 months certain records related to prescreened solicitations, such as the list of criteria used to select potential customers.

Advertising

No Discouraging Applications on a Prohibited Basis [Section 1002.4(b)]

A credit union must not make any oral or written statement that discourages applicants or prospective applicants on a prohibited basis from making or pursuing an application.

Nondiscriminatory Advertising [NCUA Rules and Regulations Section 701.31(d)]

No federal credit union may engage in any form of advertising of real estate-related loans that indicates the credit union discriminates on a prohibited basis. Advertisements must not contain any words, symbols, models, or other forms of communication that suggest a discriminatory preference or policy of exclusion.

Advertisements of real estate products must include a facsimile of the prescribed equal housing lender logo (for written advertisements) or prescribed language (for oral advertisements).

Reports

Reporting Credit Information [Section 1002.10]

If a credit union reports credit information to a consumer reporting agency or in response to a credit inquiry, and the account reflects the participation of both spouses, the credit union must furnish the information in a manner that enables access to or provides the information for the particular spouse in question.

Enforcement / Liability

Administrative Enforcement Authority [Section 704 of the ECOA]

The Consumer Financial Protection Bureau has responsibility for enforcement at credit unions with greater than \$10 billion in assets. The National Credit Union Administration has responsibility for enforcement at federal credit unions with less than \$10 billion in assets. The Federal Trade Commission enforces Regulation B at state-chartered credit unions with less than \$10 billion in assets.

Penalties and Liabilities [Section 1002.16(b)]

Regulation B provides for actual damages, as well as for punitive damages of up to \$10,000 in individual lawsuits and up to the lesser of \$500,000 or one percent of the institution's net worth in class action suits. Court costs and reasonable attorney fees may also be awarded to an aggrieved applicant in a successful action.

EQUAL CREDIT OPPORTUNITY ACT (REGULATION B) REVIEW CONSIDERATIONS

All reviews need not be full-scope but may be focused to the areas posing the most risk to the credit union.

| Review Area | Requirements / Recommendations |
|---|--|
| Policies / Procedures | Ensure the policy for implementing ECOA (Regulation B) does not tolerate discrimination in any aspect of the credit transaction process. |
| No Discrimination on a Prohibited Basis | Ensure employees do not discriminate on a prohibited basis regarding any aspect of a credit transaction. Prohibited bases: race, color, religion, national origin, sex, marital status, age (provided the applicant has capacity to contract), receipt of public assistance, or exercise of rights under the Consumer Credit Protection Act. |
| No Discouraging of Applications | Ensure employees do not discourage applicants or prospective applicants on a prohibited basis from making or pursuing an application. |
| Inquiries Concerning a Spouse | Ensure employees do not request information concerning the spouse or former spouse except when the spouse has rights of access to the account, is liable on the account, or the applicant is relying on spousal income, support, or property as a basis for repayment. |
| Inquiries Concerning Marital Status | Ensure employees do not inquire about the marital status of an applicant who is applying for individual unsecured credit. For applicants residing in a community property state or relying on property located in such a state, limit applicant marital status information to the categories: married, unmarried, and separated. |
| Inquiries Concerning Other Income | Ensure employees do not inquire whether income stated in application is derived from alimony, child support, or separate |

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| | <p>maintenance payments unless applicant is given a choice as to whether such information is to be considered in the determination of creditworthiness.</p> |
| Inquiries Concerning Applicant's Sex | <p>Ensure employees do not inquire about the applicant's sex; however, an applicant can be requested to designate a title (such as Ms., Miss, Mr., or Mrs.), if the form discloses that such a designation is optional.</p> |
| Inquiries on Childbearing, Childrearing | <p>Ensure employees do not inquire about childbearing or rearing or about birth control practices. Information about dependents may be requested if sought from all applicants.</p> |
| Written Applications | <p>Written applications must be taken for credit related to the purchase or refinancing of a principal residence secured by the residence. (Note: these are the same types of credit for which monitoring information must be collected.)</p> |
| Rules on Use of Information | <p>Creditors are not permitted to take the following into account when evaluating an applicant's creditworthiness:</p> <ol style="list-style-type: none"> 1. Any prohibited basis, except as provided by the ECOA and Regulation B; 2. Age or receipt of public assistance (with exceptions noted in Section 1002.6(b)(2)); 3. Assumptions or statistics related to childbearing or childrearing; or 4. Telephone listing in name of applicant. <p>Also note the following limits on the use of information:</p> <ol style="list-style-type: none"> 1. Income – no discounting/exclusion of income if derived from part-time employment, annuity, pension, public assistance, alimony, or child support. 2. Credit History – consider accounts that |

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| | <p>the applicant and the applicant’s spouse use or on which they are contractually liable. Also consider information offered by applicants concerning inaccuracies in their credit history.</p> <p>3. Immigrant Status – may consider applicant’s immigration status as it relates to rights/remedies regarding repayment.</p> |
| Credit Scoring Systems: Use of Age | <p>Use of a credit scoring system that scores age as a predictive variable is permissible only when it is empirically derived and is demonstrably and statistically sound. The age of an elderly applicant may not be assigned a negative factor or value.</p> |
| Self-test | <p>Use information gathered in a controlled and targeted manner to specifically determine compliance with the ECOA.</p> <p>The following must be disclosed to applicants:</p> <ul style="list-style-type: none"> • Providing the information is optional. • It is being collected to monitor for compliance with the ECOA. • It will not be used in making the credit decision. • If applicable, information may be noted based on visual observation or surname. |
| Action on Open-End Accounts | <p>Creditors are restricted from terminating, changing account terms, or requiring reapplications for open-end accounts on the basis of changes of age or retirement status. Reapplications may not be required for a change of marital status (where spouse had no liability and spousal income had no impact on credit decision).</p> |
| Spousal Signatures | <p>Creditors are restricted from requiring the signature of an applicant’s spouse or other person on any credit instrument if the applicant qualifies for the amount and terms of credit requested.</p> |

| | |
|-------------------------------|--|
| Insurance | Creditors may not refuse to extend credit and may not terminate an account because credit life, health, accident, disability, or other credit-related insurance is not available based on the applicant's age. |
| Furnishing Credit Information | Creditors reporting credit information must abide by requirements enabling separate tracking of spouses and their individual and/or joint credit histories. |
| Providing Appraisals | <p>Currently, federal credit unions are subject to the appraisal requirements outlined in Section 701.31(c)(5) and Part 722 of the NCUA Rules and Regulations.</p> <p>Effective January 18, 2014, federal credit unions will be subject to Section 1002.14 (Rules on providing appraisals and other valuations) of Regulation B. Refer to Operational Requirements for more information.</p> |
| Notification of Action Taken | <p>Creditors must provide written notice of action taken on credit applications that include a statement of specific reasons for the action (or disclosure of right to obtain such reasons), name and address of creditor, and name and address of creditor's federal regulatory agency. The notice must also contain a statement of the provisions of Section 1002.9(b).</p> <p>There are special provisions concerning:</p> <ul style="list-style-type: none"> • Notification to business credit applicants (Section 1002.9(a)(3)) • Incomplete applications (Section 1002.9(c)) • Applications submitted through a third party (Section 1002.9(g)) |
| Monitoring Information | In connection with applications for the purchase or refinancing of a principal residence secured by the residence, the application must request information |

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| | <p>regarding the applicant(s) ethnicity, race, sex, marital status, and age.</p> <p>If the applicant(s) chooses not to provide some or all of the information, the creditor should note that fact and, to the extent possible, should also note the ethnicity, race, and sex of the applicant(s) based on visual observation or surname.</p> <p>See also additional information that must be disclosed to applicants concerning the collection and use of the monitoring information. (Section 1002.13(c).)</p> |
| Record Retention | <ul style="list-style-type: none"> • Preserve applications, monitoring information, information used in evaluating the application, and required notifications. Generally, required for 25 months after date of notice of action taken. • Retain records relating to prescreened solicitations for 25 months. |
| Self-Testing | <p>Institutions have a legal privilege in information developed as a result of self-tests that they voluntarily conduct to determine their compliance with the ECOA and Regulation B. The privilege applies only if the definition of self-test is met and the creditor takes appropriate corrective actions as described in Section 1002.15.</p> |
| Training | <p>Provide training to all employees involved in any aspect of taking, evaluating, acting on a credit application, or furnishing/maintaining credit information. In addition, persons involved in marketing and credit operations should receive appropriate instruction relative to their responsibilities.</p> |
| Monitoring, Internal Review, Audit | <p>Monitor the various phases of the credit application process on a periodic basis, including taking and evaluating applications, providing appraisal reports, and reporting credit histories. This process</p> |



should focus on the credit union's compliance with the substantive nondiscrimination requirements as well as its adherence to the technical provisions of the ECOA and Regulation B.

An internal or external audit should be conducted at least annually to assess overall compliance.

EQUAL CREDIT OPPORTUNITY ACT (REGULATION B) CHECKLIST

| | Yes | No |
|--|-------|-------|
| 1. Does the credit union prohibit its employees from making statements that would discourage, on a prohibited basis, applicants from making or pursuing an application? [§1002.4(b)] | _____ | _____ |
| 2. Does the credit union refrain from requesting information concerning the applicant's spouse or former spouse unless such person will be permitted to use or be contractually liable, or the applicant is relying on community property, the spouse's income, alimony, child support, or maintenance payments for repayment of the debt? [§1002.5(c)(2)] | _____ | _____ |
| 3. Regarding applications for individual unsecured loans, does the credit union refrain from inquiring as to the marital status of the loan applicant (unless community property is involved)? [§1002.5(d)(1)] | _____ | _____ |
| 4. For secured loans, are inquiries into marital status limited to the terms "married," "unmarried," or "separated?" [§1002.5(d)(1)] | _____ | _____ |
| 5. When income derived from alimony, child support, or maintenance payments is disclosed, is there evidence that the credit union properly informed the applicant that such income need not be revealed? [§1002.5(d)(2)] | _____ | _____ |
| 6. When a title such as Ms., Miss, Mrs., or Mr. is shown on the application, does the form appropriately disclose that such designation is optional? [§1002.5(b)(2)] | _____ | _____ |
| 7. Are requests for information relative to birth control, childbearing, or rearing intentions of applicants prohibited? [§1002.5(d)(3)] | _____ | _____ |
| 8. If the credit union considers age or the fact that an applicant's income is derived from a public assistance | | |

program, does it do so only to determine a pertinent element of creditworthiness? [§1002.6(b)(2)(iii)] _____

9. If the age of an elderly applicant is considered, is such age used only to favor the elderly applicant? [§1002.6(b)(2)(iv)] _____

10. When evaluating the applicant's creditworthiness, does the credit union refrain from considering aggregate statistics or assumptions relative to the likelihood of bearing or rearing children? [§1002.6(b)(3)] _____

11. Does the credit union refrain from discounting or excluding income on a prohibited basis or because the income is derived from part-time employment, or a retirement benefit? [§1002.6(b)(5)] _____

12. Does the credit union consider income from alimony, child support, or maintenance payments to the extent it is likely to be consistently received? [§1002.6(b)(5)] _____

13. When considering an applicant's credit history, does the credit union consider:

a. all accounts designated as accounts that the applicant and applicant's spouse are permitted to use or for which both are contractually liable? [§1002.6(b)(6)(i)] _____

b. at the applicant's request, any information the applicant may present regarding past credit performance which indicates that such performance does not accurately reflect the applicant's willingness to pay? [§1002.6(b)(6)(ii)] _____

c. at the applicant's request, any credit information in the name of the applicant's spouse or former spouse which demonstrates the applicant's willingness to pay? [§1002.6(b)(6)(iii)] _____

14. Does the credit union grant loans to creditworthy applicants regardless of sex, marital status, or membership in any other protected group? [§1002.7(a)] _____

15. Does the credit union allow the granting of loans in maiden names or combinations of maiden and married names? [§1002.7(b)] _____

16. When the credit union requires cosigners, is the requirement based on factors other than the applicant's sex, marital status, or other prohibited basis of discrimination? (State law may be considered when determining the necessity for cosigners.)
[Commentary to §1002.7(d)(5)]

17. Are restrictions on spousal signatures observed?
[§1002.7(d)]

18. If a loan can only be approved with a cosigner, could an applicant volunteer any other person and not be limited to a spouse? [§1002.7(d)(5)]

19. Is business credit available separately to principals of corporations, partners, and proprietors without requiring spouses' signatures?
[Commentary to §1002.7(d)(6)]

20. Does the credit union refrain from refusing credit because credit life, health, accident, disability, or other credit-related insurance is not available due to the applicant's age? [§1002.7(e)]

21. Does the credit union notify applicants of action taken within:

a. 30 days of receipt of a completed application?
[§1002.9(a)(1)(i)]

b. 30 days after taking adverse action on an incomplete application? [§1002.9(a)(1)(ii)]

c. 30 days after taking adverse action on an existing account? [§1002.9(a)(1)(iii)]

d. 90 days after notifying the applicant of a counteroffer if the applicant does not expressly accept or use the credit offered? [§1002.9(a)(1)(iv)]

e. a reasonable period, not more than 30 days, after an oral request to complete an incomplete application?
[§1002.9(c)]



22. Are notices of adverse action: [§1002.9(a)(2)]

a. in writing? _____

b. do they contain the name and address of the credit union? _____

c. do they contain an accurate statement of action taken? _____

d. do they contain a statement of the provisions of Section 701(a) of the Equal Credit Opportunity Act in a form substantially similar to that contained in §1002.9(b)(1) of the regulation? _____

e. do they contain the name and address of the credit union's federal regulator? _____

f. do they contain an accurate statement of specific reasons for the action taken or disclosure of the applicant's right to such a statement as specified in §1002.9(a)(2)? _____

23. Do statements of specific reasons for adverse action contain the principal, specific reasons for such actions? [§1002.9(b)(2)] _____

24. Has the credit union established procedures for the identification, and designation as such, of existing and future loans upon which both spouses are or will be contractually liable? [§1002.10(a)] _____

25. When furnishing credit information on designated accounts to a consumer reporting agency, does the credit union report the designation and furnish the information in a manner that provides access to such information in the name of each spouse? [§1002.10(b)] _____

26. When furnishing credit information regarding a designated account in response to an inquiry regarding a particular applicant, is the information furnished in the name of such applicant? [§1002.10(c)] _____

27. Does the credit union retain for 25 months after notice of action taken or notice of incompleteness: [§1002.12(b)] _____
- a. the application and all supporting material? _____
 - b. all information obtained for monitoring purposes? _____
 - c. the notification of action taken? _____
 - d. a statement of specific reasons for adverse action? _____
 - e. discrimination complaints under Regulation B? _____
28. Is all information relative to an investigative action retained until final disposition of the matter? [§1002.12(b)(4)] _____
29. If the credit union engages in a special purpose credit program, is it in compliance with Section 1002.8 of the Regulation? _____
30. Has the credit union adopted procedures to comply with notification and record retention requirements on business credit? [§1002.9(a)(3)] and [§1002.12] _____
31. Does the credit union make available a copy of the appraisal used in connection with the member's real estate-related loan application? [701.31(c)(5), §1002.14 effective January 18, 2014] _____
32. Does the credit union include in its advertisements of real estate-related loans, that such loans are made without regard to race, color, religion, national origin, sex, handicap, or familial status? [701.31(d)(1)] _____
33. If the credit union makes real estate-related loans, does it display a notice of nondiscrimination in the public lobby of the credit union and in the public area of each office where such loans are made? [701.31(d)(2)] _____
34. Does the credit union collect monitoring information (ethnicity, race, sex, marital status, age) as required by §1002.13? _____



35. If the credit union collects data in a self-test for compliance with the ECOA, does it disclose to the applicants that providing the information is optional, that it is being collected to monitor for compliance with the ECOA, that it will not be used in making the credit decision, and, where applicable, that information may be noted based on visual observation or surname? [§1002.5(b)(1)]

36. Is the self-test designed and used specifically to determine compliance with the ECOA? [§1002.15(b)(1)(i)]

37. Does the credit union retain records related to a self-test for 25 months? [§1002.12(b)(6)]

38. Does the credit union retain records related to prescreened solicitations for 25 months? [§1002.12(b)(7)]

EQUAL CREDIT OPPORTUNITY ACT (REGULATION B) DEFINITIONS

Definitions (Section 1002.2)

For the purposes of Regulation B, unless the context indicates otherwise, the following definitions apply.

Account

An extension of credit. When employed in relation to an account, the word use refers only to open-end credit.

Act

The Equal Credit Opportunity Act (Title VII of the Consumer Credit Protection Act).

Adverse action

(1)(i) a refusal to grant credit in substantially the amount or on substantially the terms requested in an application unless the creditor makes a counteroffer (to grant credit in a different amount or on other terms) and the applicant uses or expressly accepts the credit offered;

(ii) a termination of an account or an unfavorable change in the terms of an account that does not affect all or a substantial portion of a class of the creditor's accounts; or,

(iii) a refusal to increase the amount of credit available to an applicant who has made an application for an increase.

(2) Adverse action does not include:

(i) a change in the terms of an account expressly agreed to by an applicant;

(ii) any action or forbearance relating to an account taken in connection with inactivity, default, or delinquency as to that account;

(iii) a refusal or failure to authorize an account transaction at a point of sale or loan, except when the refusal is a termination or an unfavorable change in the terms of an account that does not affect all or a substantial portion of a class of the creditor's accounts, or when the refusal is a denial of an application for an increase in the amount of credit available under the account;

(iv) a refusal to extend credit because applicable law prohibits the creditor from extending the credit requested; or,

(v) a refusal to extend credit because the creditor does not offer the type of credit or credit plan requested.

(3) An action that falls within the definition of both paragraphs (1) and (2) is governed by paragraph (2).

Age

Refers only to the age of natural persons and means the number of fully elapsed years from the date of an applicant's birth.

Applicant

Any person who requests or who has received an extension of credit from a creditor, and includes any person who is or may become contractually liable regarding an extension of credit. For purposes of Section 1002.7(d), the term includes guarantors, sureties, endorsers, and similar parties.

Application

An oral or written request for an extension of credit that is made in accordance with procedures established by a creditor for the type of credit requested. The term does not include the use of an account or line of credit to obtain an amount of credit that is within a previously established credit limit. A completed application means an application in connection with which a creditor has received all the information that the creditor regularly obtains and considers in evaluating applications for the amount and type of credit requested (including, but not limited to, credit reports, any additional information requested from the applicant, and any approvals or reports by governmental agencies or other persons that are necessary to guarantee, insure, or provide security for the credit or collateral). The creditor shall exercise reasonable diligence in obtaining such information.

Business credit

Refers to extensions of credit primarily for business or commercial (including agricultural) purposes, but excluding extensions of credit of the types described in Section 1002.3(a), (b), and (d).

Consumer credit

Credit extended to a natural person primarily for personal, family, or household purposes.

Contractually liable

Expressly obligated to repay all debts arising on an account by reason of an agreement to that effect.

Credit

The right granted by a creditor to an applicant to defer payment of a debt, incur debt and defer its payment, or purchase property or services and defer payment therefore.

Credit card

Any card, plate, coupon book, or other single credit device that may be used from time to time to obtain money, property, or services on credit.

Creditor

A person who, in the ordinary course of business, regularly participates in the decision of whether or not to extend credit. The term includes a creditor's assignee, transferee, or subrogee who so participates. For purposes of Sections 1002.4 and 1002.5(a) the term also includes a person who, in the ordinary course of business, regularly refers applicants or prospective applicants to creditors, or selects or offers to select creditors to whom requests for credit may be made. A person is not a creditor regarding any violation of the act or this regulation committed by another creditor unless the person knew or had reasonable notice of the act, policy, or practice that constituted the violation before becoming involved in the credit transaction. The term does not include a person whose only participation in a credit transaction involves honoring a credit card.

Credit transaction

Every aspect of an applicant's dealings with a creditor regarding an application for credit or an existing extension of credit (including, but not limited to, information requirements; investigation procedures; standards of creditworthiness; terms of credit; furnishing of credit information; revocation, alteration, or termination of credit; and collection procedures).

Discriminate against an applicant means to treat an applicant less favorably than other applicants.

Elderly

Age 62 or older.

Empirically derived and other credit scoring systems

(1) A credit scoring system is a system that evaluates an applicant's creditworthiness mechanically, based on key attributes of the applicant and aspects of the transaction, and that determines, alone or in conjunction with an evaluation of additional information about the applicant, whether an applicant is deemed creditworthy. To qualify as an empirically derived, demonstrably and statistically sound, credit scoring system, the system must be:

- (i) based on data that are derived from an empirical comparison of sample groups or the population of creditworthy and non-creditworthy applicants who applied for credit within a reasonable preceding period of time;
- (ii) developed for the purpose of evaluating the creditworthiness of applicants with respect to the legitimate business interests of the creditor utilizing the system (including, but not limited to, minimizing bad debt losses and operating expenses in accordance with the creditor's business judgment);
- (iii) developed and validated using accepted statistical principles and methodology; and,
- (iv) periodically revalidated by the use of appropriate statistical principles and methodology and adjusted as necessary to maintain predictive ability.

(2) A creditor may use an empirically derived, demonstrably and statistically sound, credit scoring system obtained from another person or may obtain credit experience from which to develop such a system. Any such system must satisfy the criteria set forth in paragraph (1) (i) through (iv) of this section; if the creditor is unable during the development process to validate the system based on its own credit experience in accordance with paragraph (1) of this section, the system must be validated when sufficient credit experience becomes available. A system that fails this validity test is no longer an empirically derived, demonstrably and statistically sound, credit scoring system for that creditor.

Extend credit and extension of credit

The granting of credit in any form (including, but not limited to, credit granted in addition to any existing credit or credit limit; credit granted pursuant to an open-end credit plan; the refinancing or other renewal of credit, including the issuance of a new credit card in place of an expiring credit card or in substitution for an existing credit card; the consolidation of two or more obligations; or the continuance of existing credit without any special effort to collect at or after maturity).

Good faith

Honesty in fact in the conduct or transaction.

Inadvertent error

A mechanical, electronic, or clerical error that a creditor demonstrates was not intentional and occurred notwithstanding the maintenance of procedures reasonably adapted to avoid such errors.

Judgmental system of evaluating applicants

Any system for evaluating the creditworthiness of an applicant other than an empirically derived, demonstrably and statistically sound, credit scoring system.

Marital status

The state of being unmarried, married, or separated, as defined by applicable state law. The term "unmarried" includes persons who are single, divorced, or widowed.

Negative factor or value, in relation to the age of elderly applicants, means utilizing a factor, value, or weight that is less favorable regarding elderly applicants than the creditor's experience warrants or is less favorable than the factor, value, or weight assigned to the class of applicants that are not classified as elderly and are most favored by a creditor on the basis of age.

Open-end credit

Credit extended under a plan under which a creditor may permit an applicant to make purchases or obtain loans from time to time directly from the creditor or indirectly by use of a credit card, check, or other device.

Person

A natural person, corporation, government or governmental subdivision or agency, trust, estate, partnership, cooperative, or association.

Pertinent element of creditworthiness, in relation to a judgmental system of evaluating

applicants, means any information about applicants that a creditor obtains and considers and that has a demonstrable relationship to a determination of creditworthiness.

Prohibited basis

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 or any state law upon which an exemption has been granted by the Bureau.

State

Any state, the District of Columbia, the Commonwealth of Puerto Rico, or any territory or possession of the United States.

FAIR HOUSING ACT OVERVIEW

The Fair Housing Act (FH Act) provides for fair housing throughout the United States. In particular, FH Act makes it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap, or familial status.

The FH Act works in conjunction with the Equal Credit Opportunity Act (ECOA) to prohibit discrimination by anyone who is in the business of providing loans for housing. The U.S. Department of Housing and Urban Development (HUD) has primary FH Act regulatory and enforcement authority over credit unions. HUD's FH Act regulations are located at 24 CFR Parts 100, 103, and 110, and guidance on discriminatory advertising practices is located on the HUD's website. Federal credit unions must also comply with NCUA Rules and Regulations Section 701.31, 12 CFR Section 701.31.

Non-Discrimination in Lending

A credit union may not deny a loan or other financial assistance for the purpose of purchasing, constructing, improving, repairing, or maintaining a dwelling, nor may it discourage an application for such a loan, on the basis of the race, color, religion, handicap, familial status (having children under the age of 18), national origin, or sex of:

- The loan applicant or joint applicant
- Any person associated with the loan applicant or joint applicant
- The present or prospective owners, lessees, tenants, or occupants of other dwellings in the vicinity of the dwelling

It is unlawful to discriminate because of race, color, religion, handicap, familial status, national origin, or sex in determining the:

- Amount
- Interest rate
- Duration, or
- Other credit terms

Consideration of the following factors is not necessary to a federal credit union's business, generally has a discriminatory effect, and is therefore prohibited:

- Age or location of the dwelling
- Zip code of the applicant's current residence

- Previous home ownership
- Age or location of dwellings in the neighborhood of the subject dwelling
- Income level of residents in the neighborhood of the dwelling

A credit union may not rely on an appraisal that it knows or should know is based upon any prohibited bases or factors listed above.

Legal Interpretations

Because the FH Act was broadly written by Congress, the courts have ruled a wide variety of lending practices illegal under the Act, including some that the Act itself does not specifically mention but which the courts determined are illegal because they violate implicit requirements and prohibitions. Examples of some prohibited practices include:

- Redlining on a racial basis. "Redlining" is the practice of denying loans for housing in certain neighborhoods even though the individual applicant may be otherwise eligible for credit.
- Making excessively low appraisals in relation to purchase prices, based on prohibited considerations (closely akin to redlining).
- Discouraging applications for credit on prohibited bases, as well as outright denials. Taken together, the FH Act and ECOA produce a strong statutory prohibition against prescreening or discouraging applicants by housing sellers or lenders, even to the point of ensuring that their advertising policies do not have that effect.
- The use of excessively burdensome qualification standards for the purpose, or with the effect, of denying housing to protected applicants.
- Applying differing standards or procedures in administering foreclosures, late charges, penalties, or reinstatements, or other collection procedures.
- Racial notation or code on appraisal forms or loan forms (other than the information which §1002.13 of Regulation B requires the credit union to retain for monitoring purposes).
- Use by initial interview personnel of scripts designed to discourage protected applications.
- Patterns of significantly greater or exclusive use of insured or guaranteed loan programs by protected groups or in certain areas. This may indicate illegal "steering" to this type of lending by the credit union.

Advertising

Credit unions may not directly or indirectly engage in any form of advertising of real estate related loans that implies or suggests the credit union discriminates.

Any credit union that advertises real estate related loans must prominently indicate in the advertisement, in a manner appropriate to the advertising medium and format used,

that it makes such loans without regard to the prohibited bases. Additionally, every credit union engaged in real estate lending must provide a notice of nondiscrimination in its lobby and in each office where such loans are made. The notice must be clearly visible to the general public and must contain the Equal Housing Lender logo and language appearing in HUD's FH Act guidelines on advertising or NCUA Rules and Regulations Section 701.31(d)(3) for federal credit unions.

Associated Risks

The following risk areas apply to the compliance area:

- Compliance risk can occur when the credit union fails to implement the necessary controls to comply with the FH Act.
- Reputation risk can occur when the credit union receives negative publicity or declined membership confidence as a result of failure to comply with the FH Act.

Additional Information

Please refer to Section 701.31(e) of the NCUA Rules and Regulations for additional guidelines concerning nondiscrimination in lending. In addition, information is available on HUD's website at <http://www.hud.gov>.

Please note the ECOA and the Fair Housing Act should be read together in order to fully understand the scope of a credit union's fair lending obligations. For example, the bases of discrimination prohibited by the ECOA are similar, but not identical, to those prohibited by the FH Act.

FAIR HOUSING ACT OPERATIONAL REQUIREMENTS

Enforcement / Liability

Administrative Enforcement Authority [Section 810 of the FH Act]

The U.S. Department of Housing and Urban Development (HUD) has responsibility for administrative enforcement for both federal and state-chartered credit unions.

Enforcement Mechanisms [Sections 810, 812, 813, and 814 of the FH Act]

The Attorney General may bring a civil court action directly when reasonable cause exists to believe persons or entities are engaged in a pattern or practice of FH Act violations. In addition, a person who claims to have been discriminated against may:

- 1) file a private civil action directly in federal court; or
- 2) file a complaint with HUD. HUD will investigate the complaint and it may attempt to resolve the grievance by means of conference, conciliation, and persuasion. If it finds a FH Act violation, HUD may take administrative action against the violator or, when reasonable cause exists to believe that persons or entities are engaged in a pattern or practice of violations, may refer the case to the Attorney General for action in federal court.

Penalties and Liabilities [Sections 812, 813, and 814 of the FH Act]

Administrative remedies available to HUD include permanent or temporary injunctions, restraining orders, or other relief including monetary damages and civil penalties. In civil court actions, the court may grant relief as it deems appropriate, including monetary damages, permanent or temporary injunctions, temporary restraining orders, or other similar remedy. Court-awarded monetary damages may include both punitive and actual damages.

It is unlawful to coerce, intimidate, threaten, or interfere with any person in the exercise of, or because they have exercised, rights granted by certain sections of FH Act [Section 818 of the FH Act].

FAIR HOUSING ACT REVIEW CONSIDERATIONS

| Review Area | Requirements / Recommendations |
|--|---|
| Policies / Procedures | Ensure the policy for implementing FH Act does not tolerate prohibited discrimination in any aspect of a residential real estate-related transaction. |
| Nondiscrimination in Residential Lending | <p>Ensure employees do not discriminate against any person in setting or exercising the terms or conditions of such a loan or discourage an application on the basis of race, color, religion, national origin, sex, handicap, or familial status (having children under the age of 18).</p> <p>Note: The use of the term residential real estate-related transaction means (1) the making or purchasing of loans for the purchase, construction, improvement, repair, or maintenance of a dwelling secured by residential real estate or (2) the selling, brokering, or appraising of a dwelling.</p> |
| Nondiscrimination in Appraisals | <p>Do not rely on an appraisal of a dwelling if one knows or should know that the appraisal is based upon consideration of race, color, national origin, religion, sex, handicap, or familial status.</p> <p>Do not rely upon an appraisal of a dwelling if one knows or should know that the appraisal is based upon consideration of a criterion which has the effect of discriminating on the basis of race, color, national origin, religion, sex, handicap, or familial status.</p> <p>Do not rely upon an appraisal that one knows or should know is based upon consideration of any of the following</p> |

| | |
|----------------------------------|--|
| | <p>criteria, which generally have a discriminatory effect, and are not necessary to a federal credit union's business:</p> <ul style="list-style-type: none"> • The age or location of the dwelling • The age or location of dwellings in the neighborhood of the dwelling • The income level of the residents in the neighborhood of the dwelling <p>Note: See NCUA Rules and Regulations Section 701.31 regarding guidelines concerning possible exceptions or guidelines concerning the consideration of location factors.</p> |
| Providing Appraisals | <p>Creditors must provide a copy of the appraisal report used in connection with an application for credit to be secured by a lien on a dwelling.</p> |
| Nondiscrimination in Advertising | <p>Do not engage in any form of advertising of real estate-related loans that indicate the credit union discriminates on the basis of race, color, religion, national origin, sex, handicap, or familial status in violation of the FH Act.</p> <p>Ensure advertisements do not contain any words, symbols, models, or other forms of communication that suggest a discriminatory preference or policy of exclusion in violation of the FH Act or the Equal Credit Opportunity Act.</p> <p>Ensure real estate-related loan advertisements prominently indicate, in a manner appropriate to the advertising medium and format used, that the credit union makes such loans without regard to race, color, religion, national origin, sex, handicap, or familial status. (Federal credit unions see NCUA Rules and</p> |

| | |
|------------------------------------|--|
| | Regulations Section 701.31; state chartered credit unions see HUD guidance on advertising.) |
| HUD Regulations | Ensure compliance with all HUD regulations implementing the FH Act and NCUA Nondiscrimination regulations relating to residential real estate lending. (HUD regulations applicable to all credit unions are located at 24 CFR Parts 100, 103, and 110; and NCUA regulations applicable to federal credit unions are located at 12 CFR Section 701.31.) |
| Equal Housing Lender Poster | Display the Equal Housing Lender poster in the public lobby of the credit union and in the public area of each office where such loans are made, and it must be clearly visible to the general public. |
| Self-testing | <p>Credit unions have a legal privilege in information developed as a result of self-tests that they would voluntarily conduct to determine their compliance with the FH Act. The privilege only applies if the definition of self-test is met and the credit union takes appropriate corrective action as described in the HUD implementing regulations, 24 CFR Part 100, Subpart C.</p> <p>Note: Data or factual information that is available or can be derived from credit or application files is not privileged. Data collection required by law or any government authority is not a voluntary self-test.</p> |
| Training | Provide training to all employees involved in any aspect of residential real estate, including the financing, selling, renting, advertising, brokering, and appraising of housing. All employees should be provided with training on the basic principles and core requirements of FH Act, along with other relevant fair lending laws and regulations. |
| Monitoring, Internal Review, Audit | Conduct periodic monitoring of the credit |

| | |
|--|--|
| | <p>union's compliance with the requirements of the FH Act, as well as other relevant fair lending laws and regulations.</p> <p>An internal or external audit should be conducted at least annually to assess overall compliance with the FH Act and to ensure the credit union's practices conform to its policies and procedures.</p> |
|--|--|



FAIR HOUSING ACT CHECKLIST

| | Yes | No |
|--|-------|-------|
| 1. Does the credit union avoid the follow actions based on race, color, religion, sex, handicap, familial status, or national origin: [§805(a)] | | |
| • Refuse to make a mortgage loan | _____ | _____ |
| • Refuse to provide information regarding loans | _____ | _____ |
| • Impose different terms or conditions on a loan | _____ | _____ |
| • Discriminate in appraising property | _____ | _____ |
| • Refuse to purchase a loan | _____ | _____ |
| • Set different terms or conditions for purchasing a loan | _____ | _____ |
| 2. Does the credit union avoid any statements or advertisements that indicates a limitation or preference based on race, color, religion, sex, handicap, familial status, or national origin? | _____ | _____ |
| 3. Does the credit union include in its advertisements of real estate-related loans, that such loans are made without regard to race, color, religion, sex, handicap, familial status, or national origin? [§701.31(d)(1)] | _____ | _____ |
| 4. If the credit union makes real estate-related loans, does it display a notice of nondiscrimination in the public lobby of the credit union and in the public area of each office where such loans are made? [§701.31(d)(2)] | _____ | _____ |

FAIR HOUSING ACT DEFINITIONS

Definitions (Section 802)

As used in this title (Title 42 of the United States Code)

Secretary

The Secretary of Housing and Urban Development.

Dwelling

Any building, structure, or portion thereof which is occupied as, or designed or intended for occupancy as, a residence by one or more families, and any vacant land which is offered for sale or lease for the construction or location thereon of any such building, structure, or portion thereof.

Family

Includes a single individual.

Person

Includes one or more individuals, corporations, partnerships, associations, labor organizations, legal representatives, mutual companies, joint-stock companies, trusts, unincorporated organizations, trustees, trustees in cases under Title 11 of the United States Code, receivers, and fiduciaries.

To rent

Includes to lease, to sublease, to let and otherwise to grant for a consideration the right to occupy premises not owned by the occupant.

Discriminatory housing practice

An act that is unlawful under Section 3604, 3605, 3606, or 3617 of this title.

State

Any of the several States, the District of Columbia, the Commonwealth of Puerto Rico, or any of the territories and possessions of the United States.

Handicap

with respect to a person-

- (1) a physical or mental impairment which substantially limits one or more of such person's major life activities,
- (2) a record of having such an impairment, or

(3) being regarded as having such an impairment, but such term does not include current, illegal use of or addiction to a controlled substance (as defined in Section 802 of Title 21 of the United States Code).

Aggrieved person

Includes any person who-

- (1) claims to have been injured by a discriminatory housing practice; or
- (2) believes that such person will be injured by a discriminatory housing practice that is about to occur.

Complainant

The person (including the Secretary) who files a complaint under Section 3610 of this title.

Familial status

One or more individuals (who have not attained the age of 18 years) being domiciled with-

- (1) a parent or another person having legal custody of such individual or individuals; or
- (2) the designee of such parent or other person having such custody, with the written permission of such parent or other person.

The protections afforded against discrimination on the basis of familial status shall apply to any person who is pregnant or is in the process of securing legal custody of any individual who has not attained the age of 18 years.

Conciliation

The attempted resolution of issues raised by a complaint, or by the investigation of such complaint, through informal negotiations involving the aggrieved person, the respondent, and the Secretary.

Conciliation agreement

A written agreement setting forth the resolution of the issues in conciliation.

Respondent

- (1) the person or other entity accused in a complaint of an unfair housing practice; and
- (2) any other person or entity identified in the course of investigation and notified as required with respect to respondents so identified under Section 3610(a) of this title.

Prevailing party

Has the same meaning as such term has in Section 1988 of this title.

HOME MORTGAGE DISCLOSURE ACT (REGULATION C) OVERVIEW

The Home Mortgage Disclosure Act (HMDA), implemented by Regulation C (12 CFR 1003), requires financial institutions, including credit unions, to compile and disclose data about home purchase loans, home improvement loans, and refinancings that it originates or purchases, or for which it receives applications. Data to be recorded on reportable transactions include:

- Application or loan number
- Date application received
- Loan type
- Property type
- Purpose
- Owner occupancy status
- Loan amount
- Request for preapproval
- Type of action taken and date
- Property location (by metropolitan statistical area, state, county, and census tract)
- Applicant information (ethnicity, race, sex, and gross annual income)
- Type of purchaser of loan
- Reasons for denial (optional)
- Rate spread (effective January 1, 2004)
- Home Ownership and Equity Protection Act of 1994 (HOEPA) status (effective January 1, 2004)
- Lien status

The purpose of Regulation C is to provide the public with data that can be used to:

- Help determine whether credit unions are serving the housing needs of their communities
- Assist public officials in distributing public-sector investments so as to attract private investment to areas where it is needed
- Assist in identifying possible discriminatory lending patterns and enforcing compliance with anti-discrimination statutes

Regulation C is not intended to encourage unsound lending practices or the allocation of credit.

Exempt Institutions

A credit union is exempt from the requirements of the regulation for a given calendar year if on the preceding December 31st:

- It had neither a home office nor a branch office in a metropolitan statistical area (MSA) or
- Total assets were at or below the threshold established by the Consumer Financial Protection Bureau (CFPB) or
- It made no first-lien home purchase loans (including refinancings of home purchase loans) on one-to-four family dwellings in the preceding calendar year.

The CFPB adjusts the asset threshold based on the year-to-year change in the average of the Consumer Price Index for Urban Wage Earners and Clerical Workers, not seasonally adjusted, for each twelve-month period ending in November, with rounding to the nearest million. NCUA notifies credit unions about the asset threshold change each year in a Regulatory Alert.

Disclosure and Reporting

A non-exempt credit union must maintain a loan/application register (LAR) on which it will enter data about each application received and each loan originated and purchased. The credit union must send the LAR to NCUA HMDA Processing (done by the Federal Reserve Board on behalf of the Federal Financial Institutions Examination Council (FFIEC)) by March 1st following the calendar year for which loan data is compiled.

Using data from the LAR, the FFIEC will prepare and send to the credit union a series of tables that will comprise the public mortgage loan disclosure statement for that credit union. The credit union must make its disclosure statement available to the public at its home office no later than three business days after receiving it. In addition, if a credit union has branch offices in other MSAs, it must make the disclosure statement available using one of two options:

- It can make the disclosure statement available in at least one office in each of those MSAs, within ten business days of receipt from the FFIEC or
- It can send a copy of the disclosure statement if someone makes a written request, within fifteen calendar days of receiving the request. If the credit union chooses this option, it must post the address for requesting copies in each branch office in an MSA.

The disclosure statements need only contain data relating to the metropolitan statistical area for which the request is made.

Enforcement

The CFPB enforces compliance with HMDA for all credit unions with greater than \$10 billion in assets.

NCUA enforces compliance with HMDA for all credit unions with less than \$10 billion in assets. NCUA may impose administrative sanctions for failure to comply, including the imposition of civil money penalties. NCUA does not consider an error in compiling or recording required data a violation of the regulation if it was unintentional and occurred despite the credit union's maintenance of procedures reasonably adapted to avoid such errors.

Associated Risks

- Compliance risk can occur when the credit union fails to implement the necessary controls to comply with HMDA.
- Reputation risk can occur when the credit union incurs fines and penalties as a result of the failure to comply with HMDA or poor publicity as a result of negative trends displayed by the disclosure statement.
- Strategic risk can occur when the credit union fails to perform adequate planning and due diligence in regard to HMDA.

Additional Information

Credit unions engaged in mortgage lending should obtain the publication: *A Guide to HMDA Reporting: Getting it Right!* It is available from the NCUA publications office and can be downloaded from NCUA's website at

<http://www.ncua.gov/Legal/GuidesEtc/Pages/Home-Mortgage-Disclosure-Act-Reporting-Guide.aspx>.

HOME MORTGAGE DISCLOSURE ACT (REGULATION C) OPERATIONAL REQUIREMENTS

Disclosures / Notices

Modified Loan Application Register (LAR) [Sections 1003.5(c) and (d)]

A lender must make its LAR available for public inspection upon request after modifying it to protect the privacy interest of applicants and borrowers by deleting the:

- Application or loan number
- Date of receipt of the application
- Date of action taken

The modified LAR must be available following the calendar year for which the data relates, no later than March 31st for requests received on or before March 1st and within 30 days for requests received after March 1st. The modified register need only contain data relating to the metropolitan statistical area (MSA) for which the request is made. The lender must make its modified register available for a three year period.

Mortgage Loan Disclosure Statement [Section 1003.5(b)]

The disclosure statement, prepared by the Federal Financial Institutions Examination Council (FFIEC), must be made available to the public for inspection and copying at the lender's home office within three business days after receiving it from the FFIEC.

In addition, a lender must do either one of the following:

- Make the statement available in at least one office in each additional MSA where it has offices within ten business days of receipt from the FFIEC or
- Post the address for sending written requests for the statement in the lobby of each branch office in an MSA where it has offices, and mail or deliver a copy of the statement within fifteen calendar days of receipt of a written request.

The lender must make the disclosure statement available to the public for a five year period.

Lobby Notice [Section 1003.5(e)]

The lender must post a general notice about the availability of its HMDA data in the lobby of its home office and of each branch office located in an MSA.

Recordkeeping

Record Retention [Section 1003.5]

A copy of the Loan Application Register (LAR) must be retained for a period of at least three years.

The modified LAR must be available to the public for a period of three years.

The disclosure statement must be available to the public for a period of five years.

Reports

Reporting Requirements [Section 1003.5(a)]

A credit union must submit its complete loan application register (LAR) by March 1st following the calendar year for which the loan data is compiled to the Federal Reserve Board.

Enforcement / Liability

Administrative Enforcement Authority

The CFPB enforces compliance with HMDA for all credit unions with greater than \$10 billion in assets. NCUA enforces compliance with HMDA for all credit unions with less than \$10 billion in assets.

Penalties and Liabilities

Administrative sanctions, including civil money penalties, may result from violations of the regulation.

HOME MORTGAGE DISCLOSURE ACT (REGULATION C) REVIEW CONSIDERATIONS

| Review Area | Requirements / Recommendations |
|--|--|
| General Coverage | <p>Determine whether the credit union is subject to the requirements of HMDA / Regulation C.</p> <p>Credit unions are exempt from reporting requirements for a given year if on the preceding December 31st:</p> <ul style="list-style-type: none"> • The credit union did not have a home or branch office in an MSA or • The credit union's total assets were at or below the asset threshold or • The credit union did not make a first lien home purchase loan (or refinancing) on a one-to-four family dwelling in the preceding calendar year. |
| Policies / Procedures | Ensure policy and procedures for implementing HMDA are in place for collecting and maintaining accurate data of covered loans and applications. |
| Collection of Data | <p>Compile data on applications for, and originations and purchases of, home purchase loan, home improvement loans, and refinancings.</p> <p>The required information must be retained on a loan application register (LAR) in the format prescribed in Appendix A to Regulation C.</p> |
| Data on Ethnicity, Race, Sex, and Income | <p>Ensure information on ethnicity, race, and sex is collected in the manner prescribed in Appendix B to Regulation C.</p> <p>If the applicant chooses not to provide this</p> |

| | |
|------------------------------------|---|
| | <p>information for an application taken in person, the lender must note this fact on the form and note the data based on visual observation or surname, to the extent possible.</p> <p>If the applicant chooses not to provide this information for an application taken by mail, Internet, or telephone, the data need not be provided.</p> <p>Ethnicity, race, sex, and income data may but need not be collected for loans purchased by the credit union.</p> |
| Excluded Data | <p>Ensure certain transactions are excluded from being reported, including:</p> <ul style="list-style-type: none"> • Loans made or purchased in a fiduciary capacity • Loans on unimproved land • Construction and temporary financing loans • Purchase of an interest in a mortgage pool • Purchase of servicing rights • Loans originated prior to the current reporting year and acquired as part of a merger or acquisition |
| Reporting Requirements | <p>Submit the completed HMDA LAR to the Federal Reserve Board by March 1st following the calendar year for which loan data is compiled.</p> |
| Modified Loan Application Register | <p>Ensure the modified register is made available to the public after removing the following information: application or loan number, date the application was received, and date of action taken.</p> |
| Disclosure Statements | <p>Ensure the disclosure statement prepared by the FFIEC is made available to the public for inspection and copying at its home office within three business days of receipt from the FFIEC.</p> |

| | |
|--------------|---|
| | If a credit union has branches in other MSAs, it must make disclosure statements available using one of two options (see Overview section). |
| Lobby Notice | Post a general notice regarding availability of HMDA data in the lobby of its home office and each branch office located in an MSA. |
| Training | Provide training to employees whose duties are impacted by HMDA. |
| Monitoring | Ensure collection of data for the HMDA LAR is being properly recorded within the required timeframes. |

HOME MORTGAGE DISCLOSURE ACT CHECKLIST

| | Yes | No |
|---|-------|-------|
| 1. Did the federally insured credit union originate, in the preceding calendar year, at least one home purchase loan or refinancing of a home purchase loan secured by a first lien on a one-to-four family dwelling? [§1003.2] | _____ | _____ |
| 2. Did the federally insured credit union have a home or branch office in a Metropolitan Statistical Area (MSA) on December 31 st of the preceding year? [§1003.2)] | _____ | _____ |
| 3. Did the federally insured credit union's total assets exceed the established threshold as of December 31 st of the preceding year? [§1003.2] Note: The Consumer Financial Protection Bureau adjusts the asset threshold annually. | _____ | _____ |
| If you answered "Yes" to <u>all</u> three questions, the federally insured credit union is subject to HMDA and the remainder of the checklist should be completed. | | |
| If you answered "No" to <u>any</u> of the three questions, the federally insured credit is exempt from HMDA for the year in question. | | |
| 4. Is the credit union ensuring data regarding applications for, and originations and purchases of, home purchase loans, home improvement loans, and refinancings for each calendar year are properly compiled? [§1003.4(a)] | _____ | _____ |
| 5. Does the credit union maintain the necessary records to compile the required data? | _____ | _____ |
| 6. Is there an adequate audit trail to test the accuracy of the data compiled? | _____ | _____ |
| 7. Is accurate census tract information (2010 census data) available for the compilation of data? | _____ | _____ |
| 8. Are loan/application registers (LARs) completed fully and accurately? [§1003.4(a) and Appendix A] | _____ | _____ |
| 9. Is the credit union properly collecting data on ethnicity, | | |

race, sex, and income? [§1003.4(b) and Appendix B]

If an applicant chooses not to provide information, for applications taken in person, on ethnicity, race, or sex, is this fact noted on the form and is this data noted, based on visual observation or surname, to the extent possible? [§1003.4(b) and Appendix B]

10. Does the credit union avoid reporting data on transactions excluded by the regulation? [§1003.4(d)]

11. If the credit union reports 26 or more entries, is the credit union submitting data in an automated, machine readable, and conforming format no later than March 1st following the calendar year for which data was compiled? [§1003.5(a) and Appendix A]

If the credit union reports 25 or fewer entries on their HMDA LAR and submits reports in paper form, does the credit union submit two copies that are typed or computer printed in the proper format?

12. Are applications and loans recorded on the credit union's LAR within 30 calendar days after the end of the calendar quarter in which final action is taken? [§1003.4(a) and Appendix A]

13. Is the disclosure statement prepared by the FFIEC made available to the public at the credit union's home office no later than 3 business days after receiving it from the FFIEC? [§1003.5(b)(2)]

14. Is the disclosure statement made available to the public, within ten business days of receiving it, in at least one branch office in each other metropolitan statistical area (MSA) where the credit union has offices? [§1003.5(b)(3)(i)] **or**

Does the credit union post the address for sending written requests in the lobby of each branch office in other MSAs where the credit union has offices, and mail or deliver a copy of the disclosure statement within fifteen calendar days of receiving a written request? [§1003.5(b)(3)(ii)]

15. Does the credit union make its modified loan application

register available to the public after removing the application or loan date, the date the application was received, and the date action was taken? [§1003.5(c)]

16. Are the disclosure statements and modified registers available to anyone for inspection and copying during normal public business hours? [§1003.5(d)]

17. Are disclosure statements made available to the public for five years and modified registers made available to the public for three years? [§1003.5(d)]

18. Has the credit union posted a general notice about the availability of its HMDA data in the lobby of its home office and of each branch office located in an MSA? [§1003.5(e)]

19. Are policies, procedures, and training adequate to ensure compliance with HMDA?

20. Does management ensure that affected personnel are aware of the requirements of HMDA?

HOME MORTGAGE DISCLOSURE ACT (REGULATION C) DEFINITIONS

Definitions (Section 1003.2)

Application

(1) In general, an application means an oral or written request for a home purchase loan, a home improvement loan, or a refinancing that is made in accordance with procedures used by a financial institution for the type of credit requested.

(2) Preapproval programs - A request for preapproval for a home purchase loan is an application under paragraph (1) if the request is reviewed under a program in which the financial institution, after a comprehensive analysis of the creditworthiness of the applicant, issues a written commitment to the applicant valid for a designated period of time to extend a home purchase loan up to a specified amount. The written commitment may not be subject to conditions other than:

- (i) Conditions that require the identification of a suitable property;
- (ii) Conditions that require that no material change has occurred in the applicant's financial condition or creditworthiness prior to closing; and
- (iii) Limited conditions that are not related to the financial condition or creditworthiness of the applicant that the lender ordinarily attaches to a traditional home mortgage application (such as certification of a clear termite inspection).

Branch office

(1) Any office of a bank, savings association, or credit union that is approved as a branch by a federal or state supervisory agency¹, but excludes free-standing electronic terminals such as automated teller machines; and

(2) Any office of a for-profit mortgage-lending institution (other than a bank, savings association, or credit union) that takes applications from the public for home purchase loans, home improvement loans, or refinancings.

Dwelling

Residential structure (whether or not attached to real property) located in a state of the United States of America, the District of Columbia, or the Commonwealth of Puerto

¹ There is no law or regulation that requires NCUA approve credit union branch offices established within the United States, and NCUA does not issue such approvals. Accordingly, a domestic credit union branch office may qualify as a HMDA branch office without approval by a federal or state regulatory agency

Rico. The term includes an individual condominium unit, cooperative unit, or mobile or manufactured home.

Financial institution

(1) A bank, savings association, or credit union that:

(i) On the preceding December 31st had assets in excess of the asset threshold established and

published annually by the Consumer Financial Protection Bureau for coverage by the act, based on the year-to-year change in the average of the Consumer Price Index for Urban Wage Earners and Clerical Workers, not seasonally adjusted, for each twelve-month period ending in November, with rounding to the nearest million;

(ii) On the preceding December 31st, had a home or branch office in a metropolitan statistical area (MSA);

(iii) In the preceding calendar year, originated at least one home purchase loan or refinancing of a home purchase loan, secured by a first lien on a one-to-four family dwelling; and

(iv) Meets one or more of the following three criteria:

(A) The institution is federally insured or regulated;

(B) The mortgage loan referred to in paragraph (iii) of this section was insured, guaranteed, or supplemented by a federal agency; or

(C) The mortgage loan referred to in paragraph (iii) of this section was intended by the institution for sale to Fannie Mae or Freddie Mac.

Note: The definition of “financial institution” also includes other provisions covering types of institutions that are not credit unions.

Home-equity line of credit

Open-end credit plan secured by a dwelling as defined in Regulation Z (Truth in Lending), 12 CFR Part 1026.

Home improvement loan

(1) A loan secured by a lien on a dwelling that is for the purpose, in whole or in part, of repairing, rehabilitating, remodeling, or improving a dwelling or the real property on which it is located; and

(2) A non-dwelling secured loan that is for the purpose, in whole or in part, of repairing, rehabilitating, remodeling, or improving a dwelling or the real property on which it is located, and that is classified by the financial institution as a home improvement loan.

Home purchase loan

A loan secured by and made for the purpose of purchasing a dwelling.

Manufactured home

Any residential structure as defined under regulations of the U.S. Department of Housing and Urban Development establishing manufactured home construction and safety standards (24 CFR 3280.2).

Metropolitan statistical area

A metropolitan statistical area as defined by the U.S. Office of Management and Budget.

Refinancing

A new obligation that satisfies and replaces an existing obligation by the same borrower, in which:

(1) For coverage purposes, the existing obligation is a home purchase loan (as determined by the lender, for example, by reference to available documents; or as stated by the applicant), and both the existing obligation and the new obligation are secured by first liens on dwellings; and

(2) For reporting purposes, both the existing obligation and the new obligation are secured by liens on dwellings.

Additional Information

For more information and clarification regarding definitions of terms used, refer to the publication: *A Guide to HMDA Reporting: Getting it Right!* It is available from the NCUA publications office and can be downloaded from NCUA's website at <http://www.ncua.gov/Legal/GuidesEtc/Pages/Home-Mortgage-Disclosure-Act-Reporting-Guide.aspx>.

Fair Lending Compliance Best Practices for Federal Credit Unions

Fair lending laws are designed to provide fair and equal access to credit, based on individual creditworthiness, without regard to a prohibited basis such as race, gender, or national origin.¹ In addition to satisfying legal requirements, fair lending compliance is good business practice, and there can be major consequences for noncompliance. NCUA enforces fair lending laws for federal credit unions.² NCUA developed the following best practices to educate and help ensure that the credit union's lending program complies with fair lending laws and regulations.³

What are fair lending laws? Fair lending laws include the Equal Credit Opportunity Act (Regulation B), Home Mortgage Disclosure Act (Regulation C), and Fair Housing Act,⁴ and federal credit unions must comply with them. The Equal Credit Opportunity Act prohibits discrimination in any aspect of a credit transaction. It applies to any extension of credit, including extensions of credit to small businesses, corporations, partnerships, and trusts. The Home Mortgage Disclosure Act (HMDA) requires financial institutions, including credit unions, meeting certain reporting requirements to compile and disclose loan application data for home purchase loans, home improvement loans, and refinancings that they originate or purchase.⁵ The Fair Housing Act prohibits discrimination in all aspects of residential, real-estate related transactions, including but not limited to: making loans to buy, build, repair or improve a dwelling; purchasing real estate loans; selling, brokering, or appraising residential real estate; and, selling or renting a dwelling.

What practices are prohibited under fair lending laws? Under the Equal Credit Opportunity Act and/or the Fair Housing Act, a lender may not, because of a prohibited factor:

- Fail to provide information or services or provide different information or services regarding any aspect of the lending process, including credit availability, application procedures, or lending standards.
- Discourage or selectively encourage applicants with respect to inquiries about or applications for credit.

¹ The Equal Credit Opportunity Act prohibits discrimination based on race or color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to contract), the applicant's receipt of income derived from any public assistance program, and the applicant's exercise, in good faith, of any right under the Consumer Credit Protection Act. The Fair Housing Act prohibits discrimination based on race or color, national origin, religion, sex, familial status (defined as children under the age of 18 living with a parent or legal custodian, pregnant women, and people securing custody of children under 18), and handicap. Additionally, NCUA regulations contain nondiscrimination requirements that, among other things, prohibit discrimination with regard to real estate-related loans and activities. See 12 CFR § 701.31. The regulation also requires Federal credit unions engaging in real estate-related lending to display a notice of nondiscrimination.

² NCUA's fair lending examination program assesses compliance with the Fair Housing Act, but the U.S. Department of Housing and Urban Development (HUD) and the U.S. Department of Justice (DOJ) enforce the Fair Housing Act. NCUA reports violations of the Fair Housing Act to HUD or DOJ.

³ For additional information about assessing fair lending risks, please refer to the Federal Financial Institutions Examination Council Interagency Fair Lending Examination Procedures at www.ffiec.gov/PDF/fairlend.pdf and www.ffiec.gov/PDF/fairappx.pdf.

⁴ U.S. Department of Housing and Urban Development (HUD) regulations implementing the Fair Housing Act are found at 24 CFR Part 100.

⁵ NCUA Regulatory Alert 13-RA-01 provides the current data collection and filing requirements.

- Refuse to extend credit or use different standards in determining whether to extend credit.
- Vary the terms of credit offered, including the amount, interest rate, duration, or type of loan.
- Use different standards to evaluate collateral.
- Treat a borrower differently in servicing a loan or invoking default remedies.
- Use different standards for pooling or packaging a loan in the secondary market.

It is a violation of fair lending laws to express, orally or in writing, a preference based on prohibited factors or to indicate that the lender will treat applicants differently on a prohibited basis, even if the lender treats applicants equally. A lender may not discriminate on a prohibited basis because of the characteristics of:

- An applicant, prospective applicant, or borrower.
- A person associated with an applicant, prospective applicant, or borrower (for example, a co-applicant, spouse, business partner, or live-in aide).
- The present or prospective residents of the property to be financed.
- The neighborhood or other area where property to be financed is located (e.g., on the basis of the area's racial or ethnic composition. This is known as "redlining.").

What can federal credit unions do to mitigate fair lending risk? Federal credit unions can take several actions to proactively address fair lending risk. These actions include developing written fair lending policies and procedures, performing risk assessments, and ongoing monitoring of compliance with fair lending laws. All of these activities should be appropriate for the size and complexity of the credit union.

First, develop written fair lending policies and procedures. The fair lending policies and procedures should clearly state how the credit union will comply with fair lending laws and enable the credit union to serve the entire field of membership.

The board of directors and senior management should understand and convey to all credit union staff that they are responsible and accountable for complying with the fair lending laws and regulations.

Policies and procedures concerning the approval of credit, loan underwriting, pricing, and servicing standards should be clearly written and understood. Any deviations from these policies and procedures should be explained and documented.

Fair lending training should be provided for all credit union employees and officials involved in the lending process. Include training for employees who take applications, originate loans, service loans, and collect delinquent loans. The supervisory committee and internal audit staff should also incorporate an assessment of compliance with the credit union's fair lending policies as a component of their review procedures.

Second, identify risks by conducting periodic fair lending risk assessments. The risk assessment should evaluate all credit products and services the credit union offers, its organizational structure, advertising or marketing media, and lending channels.

Evaluate credit operations' collections and loss mitigation functions. Determine if borrowers receive consistent treatment for loan modifications and loan workout arrangements.

Third, develop a fair lending program based on the results of the risk assessments. The compliance program should include sufficient internal controls to monitor and reduce fair lending risks at the credit union.

For example, mitigate risk by monitoring pricing decisions. Potential risk factors for pricing include:

- Lack of specific guidelines for pricing, including exceptions.
- Use of risk-based pricing that is not based on objective criteria or that is applied inconsistently.
- Broad pricing discretion, such as through overages, underages, or yield spread premiums.
- Lack of clear documentation of reasons for pricing decisions, including exceptions.
- Lack of monitoring for pricing disparities.
- Financial incentives for loan originators to charge higher prices.
- Pricing policies or practices that treat applicants of a protected class(es) differently or have a disparate impact.
- Loan programs only offered to borrowers of a particular protected class.
- Complaints about pricing by members.

Determine whether the credit union is required to submit HMDA data. If so, the credit union should ensure that verifying the accuracy of HMDA data is an important component of the compliance program. Management should specifically:

- Ensure personnel responsible for maintaining and reporting HMDA data clearly understand the collection and reporting requirements related to all data elements, especially the pricing and government monitoring information fields (ethnicity, race, and gender).
- Establish a verification system to test HMDA data.

Finally, stay current on fair lending developments.

NCUA has created a new Fair Lending Guide, which is available at http://www.ncua.gov/Legal/GuidesEtc/GuidesManuals/OCP_FairLendingGuide.pdf, to assist the credit union in developing or evaluating the fair lending compliance program. The guide includes:

- An overview of fair lending laws and regulations;
- Credit union operational requirements;
- Issues to consider when developing a fair lending compliance program; and
- Checklists for testing compliance with laws and regulations, or developing a compliant fair lending policy.

Additionally, NCUA's Office of Consumer Protection (OCP) hosted a fair lending webinar to provide an overview of NCUA's 2013 fair lending examination program, including:

- An explanation of the fair lending off-site supervision contact process;
- Fair lending tips and best practices that credit unions should consider; and
- Time for questions and answers.

An archive of the webinar presentation can be located by selecting "Videos and Webcasts" from the "News, Media, and Events" tab at www.ncua.gov.

**Office of the Comptroller of the Currency
Federal Deposit Insurance Corporation
Federal Reserve Board
Office of Thrift Supervision
National Credit Union Administration**

**INTERAGENCY FAIR LENDING
EXAMINATION PROCEDURES**

August 2009

CONTENTS

| | |
|---|----|
| INTRODUCTION | i |
| PART I - EXAMINATION SCOPE GUIDELINES | 1 |
| Background | 1 |
| Step One – Develop an Overview | 5 |
| Step Two - Identify Compliance Program Discrimination Risk Factors | 6 |
| Step Three - Review Residential Loan Products | 7 |
| Step Four - Identify Residential Lending Discrimination Risk Factors | 8 |
| Step Five - Organize and Focus Residential Risk Analysis | 12 |
| Step Six - Identify Consumer Lending Discrimination Risk Factors | 12 |
| Step Seven – Identify Commercial Lending Discrimination Risk Factors | 13 |
| Step Eight - Complete the Scoping Process | 13 |
| PART II - COMPLIANCE MANAGEMENT REVIEW | 15 |
| PART III - EXAMINATION PROCEDURES | 17 |
| A. Verify Accuracy of Data | 17 |
| B. Documenting Overt Evidence of Disparate Treatment | 17 |
| C. Transactional Underwriting Analysis - Residential and Consumer Loans | 18 |
| D. Analyzing Potential Disparities in Pricing and Other Terms and Conditions | 22 |
| E. Steering Analysis | 24 |
| F. Transactional Underwriting Analysis - Commercial Loans | 27 |
| G. Analysis of Potential Discriminatory “Redlining” | 29 |
| H. Analysis of Potential Discriminatory Marketing Practices | 38 |
| I. Credit Scoring | 40 |
| J. Disparate Impact Issues | 40 |
| PART IV - OBTAINING AND EVALUATING RESPONSES FROM THE INSTITUTION AND CONCLUDING THE EXAMINATION | 41 |
| APPENDIX | |
| I. Compliance Management Analysis Checklist | |
| II. Considering Automated Underwriting and Credit Scoring | |
| III. Evaluating Responses to Evidence of Disparate Treatment | |
| IV. Fair Lending Sample Size Tables | |
| V. Identifying Marginal Transactions | |
| VI. Potential Scoping Information | |
| VII. Special Analyses | |
| VIII. Using Self-Tests and Self-Evaluations to Streamline the Examination | |

INTRODUCTION

Overview of Fair Lending Laws and Regulations

This overview provides a basic and abbreviated discussion of federal fair lending laws and regulations. It is adapted from the Interagency Policy Statement on Fair Lending issued in March 1994.

1. Lending Discrimination Statutes and Regulations

The Equal Credit Opportunity Act (ECOA) prohibits discrimination in any aspect of a credit transaction. It applies to any extension of credit, including extensions of credit to small businesses, corporations, partnerships, and trusts.

The ECOA prohibits discrimination based on:

- Race or color
- Religion
- National origin
- Sex
- Marital status
- Age (provided the applicant has the capacity to contract)
- The applicant's receipt of income derived from any public assistance program
- The applicant's exercise, in good faith, of any right under the Consumer Credit Protection Act

The Federal Reserve Board's Regulation B, found at 12 CFR part 202, implements the ECOA. Regulation B describes lending acts and practices that are specifically prohibited, permitted, or required. Official staff interpretations of the regulation are found in Supplement I to 12 CFR part 202.

The Fair Housing Act (FHAct) prohibits discrimination in all aspects of "residential real-estate related transactions," including but not limited to:

- Making loans to buy, build, repair or improve a dwelling
- Purchasing real estate loans
- Selling, brokering, or appraising residential real estate
- Selling or renting a dwelling

The FHAct prohibits discrimination based on:

- Race or color
- National origin
- Religion
- Sex
- Familial status (defined as children under the age of 18 living with a parent or legal custodian, pregnant women, and people securing custody of children under 18)
- Handicap

HUD's regulations implementing the FHAct are found at 24 CFR Part 100. Because both the

FHAct and the ECOA apply to mortgage lending, lenders may not discriminate in mortgage lending based on any of the prohibited factors in either list.

Under the ECOA, it is unlawful for a lender to discriminate on a prohibited basis in any aspect of a credit transaction, and under both the ECOA and the FHAct, it is unlawful for a lender to discriminate on a prohibited basis in a residential real-estate-related transaction. Under one or both of these laws, a lender may not, because of a prohibited factor

- Fail to provide information or services or provide different information or services regarding any aspect of the lending process, including credit availability, application procedures, or lending standards
- Discourage or selectively encourage applicants with respect to inquiries about or applications for credit
- Refuse to extend credit or use different standards in determining whether to extend credit
- Vary the terms of credit offered, including the amount, interest rate, duration, or type of loan
- Use different standards to evaluate collateral
- Treat a borrower differently in servicing a loan or invoking default remedies
- Use different standards for pooling or packaging a loan in the secondary market.

A lender may not express, orally or in writing, a preference based on prohibited factors or indicate that it will treat applicants differently on a prohibited basis. A violation may still exist even if a lender treated applicants equally.

A lender may not discriminate on a prohibited basis because of the characteristics of

- An applicant, prospective applicant, or borrower
- A person associated with an applicant, prospective applicant, or borrower (for example, a co-applicant, spouse, business partner, or live-in aide)
- The present or prospective occupants of either the property to be financed or the characteristics of the neighborhood or other area where property to be financed is located.

Finally, the FHAct requires lenders to make reasonable accommodations for a person with disabilities when such accommodations are necessary to afford the person an equal opportunity to apply for credit.

2. Types of Lending Discrimination

The courts have recognized three methods of proof of lending discrimination under the ECOA and the FHAct:

- Overt evidence of disparate treatment
- Comparative evidence of disparate treatment
- Evidence of disparate impact

Disparate Treatment

The existence of illegal disparate treatment may be established either by statements revealing that a lender explicitly considered prohibited factors (overt evidence) or by differences in treatment that are not fully explained by legitimate nondiscriminatory factors (comparative evidence).

Overt Evidence of Disparate Treatment. There is overt evidence of discrimination when a lender openly discriminates on a prohibited basis.

Example: A lender offered a credit card with a limit of up to \$750 for applicants aged 21-30 and \$1500 for applicants over 30. This policy violated the ECOA's prohibition on discrimination based on age.

There is overt evidence of discrimination even when a lender expresses - but does not act on - a discriminatory preference:

Example: A lending officer told a customer, "We do not like to make home mortgages to Native Americans, but the law says we cannot discriminate and we have to comply with the law." This statement violated the FHAct's prohibition on statements expressing a discriminatory preference as well as Section 202.4(b) of Regulation B, which prohibits discouraging applicants on a prohibited basis.

Comparative Evidence of Disparate Treatment. Disparate treatment occurs when a lender treats a credit applicant differently based on one of the prohibited bases. It does not require any showing that the treatment was motivated by prejudice or a conscious intention to discriminate against a person beyond the difference in treatment itself.

Disparate treatment may more likely occur in the treatment of applicants who are neither clearly well-qualified nor clearly unqualified. Discrimination may more readily affect applicants in this middle group for two reasons. First, if the applications are "close cases," there is more room and need for lender discretion. Second, whether or not an applicant qualifies may depend on the level of assistance the lender provides the applicant in completing an application. The lender may, for example, propose solutions to credit or other problems regarding an application, identify compensating factors, and provide encouragement to the applicant. Lenders are under no obligation to provide such assistance, but to the extent that they do, the assistance must be provided in a nondiscriminatory way.

Example: A non-minority couple applied for an automobile loan. The lender found adverse information in the couple's credit report. The lender discussed the credit report with them and determined that the adverse information, a judgment against the couple, was incorrect because the judgment had been vacated. The non-minority couple was granted their loan. A minority couple applied for a similar loan with the same lender. Upon discovering adverse information in the minority couple's credit report, the lender denied the loan application on the basis of the adverse information without giving the couple an opportunity to discuss the report.

The foregoing is an example of disparate treatment of similarly situated applicants, apparently based on a prohibited factor, in the amount of assistance and information the lender provided.

If a lender has apparently treated similar applicants differently on the basis of a prohibited factor, it must provide an explanation for the difference in treatment. If the lender's explanation is found to be not credible, the agency may find that the lender discriminated.

Redlining is a form of illegal disparate treatment in which a lender provides unequal access to credit, or unequal terms of credit, because of the race, color, national origin, or other prohibited characteristic(s) of the residents of the area in which the credit seeker resides or will reside or in which the residential property to be mortgaged is located. Redlining may violate both the FHAct and the ECOA.

Disparate Impact

When a lender applies a racially or otherwise neutral policy or practice equally to all credit applicants, but the policy or practice disproportionately excludes or burdens certain persons on a prohibited basis, the policy or practice is described as having a “disparate impact.”

Example: A lender’s policy is not to extend loans for single family residences for less than \$60,000.00. This policy has been in effect for ten years. This minimum loan amount policy is shown to disproportionately exclude potential minority applicants from consideration because of their income levels or the value of the houses in the areas in which they live.

The fact that a policy or practice creates a disparity on a prohibited basis is not alone proof of a violation. When an Agency finds that a lender’s policy or practice has a disparate impact, the next step is to seek to determine whether the policy or practice is justified by “business necessity.” The justification must be manifest and may not be hypothetical or speculative. Factors that may be relevant to the justification could include cost and profitability. Even if a policy or practice that has a disparate impact on a prohibited basis can be justified by business necessity, it still may be found to be in violation if an alternative policy or practice could serve the same purpose with less discriminatory effect. Finally, evidence of discriminatory intent is not necessary to establish that a lender's adoption or implementation of a policy or practice that has a disparate impact is in violation of the FHAct or ECOA.

These procedures do not call for examiners to plan examinations to identify or focus on potential disparate impact issues. The guidance in this Introduction is intended to help examiners recognize fair lending issues that may have a potential disparate impact. Guidance in the Appendix to the Interagency Fair Lending Examination Procedures provides details on how to obtain relevant information regarding such situations along with methods of evaluation, as appropriate.

General Guidelines

These procedures are intended to be a basic and flexible framework to be used in the majority of fair lending examinations conducted by the FFIEC agencies. They are also intended to guide examiner judgment, not to supplant it. The procedures can be augmented by each agency as necessary to ensure their effective implementation.

While these procedures apply to many examinations, agencies routinely use statistical analyses

or other specialized techniques in fair lending examinations to assist in evaluating whether a prohibited basis was a factor in an institution's credit decisions. Examiners should follow the procedures provided by their respective agencies in these cases.

For a number of aspects of lending -- for example, credit scoring and loan pricing -- the "state of the art" is more likely to be advanced if the agencies have some latitude to incorporate promising innovations. These interagency procedures provide for that latitude.

Any references in these procedures to options, judgment, etc., of "examiners" means discretion within the limits provided by that examiner's agency. An examiner should use these procedures in conjunction with his or her own agency's priorities, examination philosophy, and detailed guidance for implementing these procedures. These procedures should not be interpreted as providing an examiner greater latitude than his or her own agency would. For example, if an agency's policy is to review compliance management systems in all of its institutions, an examiner for that agency must conduct such a review rather than interpret Part II of these interagency procedures as leaving the review to the examiner's option.

The procedures emphasize racial and national origin discrimination in residential transactions, but the key principles are applicable to other prohibited bases and to nonresidential transactions.

Finally, these procedures focus on analyzing institution compliance with the broad, nondiscrimination requirements of the ECOA and the FHAct. They do not address such explicit or technical compliance provisions as the signature rules or adverse action notice requirements in Sections 202.7 and 202.9, respectively, of Regulation B.

PART I

EXAMINATION SCOPE GUIDELINES

Background

The scope of an examination encompasses the loan product(s), market(s), decision center(s), time frame, and prohibited basis and control group(s) to be analyzed during the examination. These procedures refer to each potential combination of those elements as a "focal point." Setting the scope of an examination involves, first, identifying all of the potential focal points that appear worthwhile to examine. Then, from among those, examiners select the focal point(s) that will form the scope of the examination, based on risk factors, priorities established in these procedures or by their respective agencies, the record from past examinations, and other relevant guidance. This phase includes obtaining an overview of an institution's compliance management system as it relates to fair lending.

When selecting focal points for review, examiners may determine that the institution has performed "self-tests" or "self-evaluations" related to specific lending products. The difference between "self tests" and "self evaluations" is discussed in the *Using Self-Tests and Self-Evaluations to Streamline the Examination* section of the Appendix. Institutions must share all information regarding "self-evaluations" and certain limited information related to "self-tests." Institutions may choose to voluntarily disclose additional information about "self-tests." Examiners should make sure that institutions understand that voluntarily sharing the results of self-tests will result in a loss of confidential status of these tests. Information from "self-evaluations" or "self-tests" may allow the scoping to be streamlined. Refer to *Using Self-Tests and Self-Evaluations to Streamline the Examination* in the Appendix for additional details.

Scoping may disclose the existence of circumstances -- such as the use of credit scoring or a large volume of residential lending -- which, under an agency's policy, call for the use of regression analysis or other statistical methods of identifying potential discrimination with respect to one or more loan products. Where that is the case, the agency's specialized procedures should be employed for such loan products rather than the procedures set forth below.

Setting the intensity of an examination means determining the breadth and depth of the analysis that will be conducted on the selected loan product(s). This process entails a more involved analysis of the institution's compliance risk management processes, particularly as it relates to selected products, to reach an informed decision regarding how large a sample of files to review in any transactional analyses performed and whether certain aspects of the credit process deserve heightened scrutiny.

Part I of these procedures provides guidance on establishing the scope of the examination. Part II (Compliance Management Review) provides guidance on determining the intensity of the examination. There is naturally some interdependence between these two phases. Ultimately the scope and intensity of the examination will determine the record of performance that serves as

the foundation for agency conclusions about institutional compliance with fair lending obligations. The examiner should employ these procedures to arrive at a well-reasoned and practical conclusion about how to conduct a particular institution's examination of fair lending performance.

In certain cases where an agency already possesses information which provides examiners with guidance on priorities and risks for planning an upcoming examination, such information may expedite the scoping process and make it unnecessary to carry out all of the steps below. For example, the report of the previous fair lending examination may have included recommendations for the focus of the next examination. However, examiners should validate that the institution's operational structure, product offerings, policies and risks have not changed since the prior examination before condensing the scoping process.

The scoping process can be performed either off-site, onsite, or both, depending on whatever is determined appropriate and feasible. In the interest of minimizing burdens on both the examination team and the institution, requests for information from the institution should be carefully thought out so as to include only the information that will clearly be useful in the examination process. Finally, any off-site information requests should be made sufficiently in advance of the on-site schedule to permit institutions adequate time to assemble necessary information and provide it to the examination team in a timely fashion. (See "Potential Scoping Information" in the Appendix for guidance on additional information that the examiner might wish to consider including in a request).

Examiners should focus the examination based on:

- An understanding of the credit operations of the institution
- The risk that discriminatory conduct may occur in each area of those operations
- The feasibility of developing a factually reliable record of an institution's performance and fair lending compliance in each area of those operations.

1. Understanding Credit Operations

Before evaluating the potential for discriminatory conduct, the examiner should review sufficient information about the institution and its market to understand the credit operations of the institution and the representation of prohibited basis group residents within the markets where the institution does business. The level of detail to be obtained at this stage should be sufficient to identify whether any of the risk factors in the steps below are present. Relevant background information includes:

- The types and terms of credit products offered, differentiating among broad categories of credit such as residential, consumer, or commercial, as well as product

- variations within such categories (fixed vs. variable, etc.)
- Whether the institution has a special purpose credit program, or other program that is specifically designed to assist certain underserved populations
 - The volume of, or growth in, lending for each of the credit products offered
 - The demographics (i.e., race, national origin, etc.) of the credit markets in which the institution is doing business
 - The institution's organization of its credit decision-making process, including identification of the delegation of separate lending authorities and the extent to which discretion in pricing or setting credit terms and conditions is delegated to various levels of managers, employees or independent brokers or dealers
 - The institution's loan officer or broker compensation program
 - The types of relevant documentation/data that are available for various loan products and what is the relative quantity, quality and accessibility of such information. i.e., for which loan product(s) will the information available be most likely to support a sound and reliable fair lending analysis
 - The extent to which information requests can be readily organized and coordinated with other compliance examination components to reduce undue burden on the institution. (Do not request more information than the exam team can be expected to utilize during the anticipated course of the examination.)

In thinking about an institution's credit markets, the examiner should recognize that these markets may or may not coincide with an institution's Community Reinvestment Act (CRA) assessment area(s). Where appropriate, the examiner should review the demographics for a broader geographic area than the assessment area.

Where an institution has multiple underwriting or loan processing centers or subsidiaries, each with fully independent credit-granting authority, consider evaluating each center and/or subsidiary separately, provided a sufficient number of loans exist to support a meaningful analysis. In determining the scope of the examination for such institutions, examiners should consider whether:

- Subsidiaries should be examined. The agencies will hold a financial institution responsible for violations by its direct subsidiaries, but not typically for those by its affiliates (unless the affiliate has acted as the agent for the institution or the violation by the affiliate was known or should have been known to the institution before it became involved in the transaction or purchased the affiliate's loans). When seeking to determine an institution's relationship with affiliates that are not supervised financial institutions, limit the inquiry to what can be learned in the institution and do not contact the affiliate without prior consultation with agency staff.
- The underwriting standards and procedures used in the entity being reviewed are used in related entities not scheduled for the planned examination. This will help examiners to recognize the potential scope of policy-based violations.
- The portfolio consists of applications from a purchased institution. If so, for scoping

purposes, examiners should consider the applications as if they were made to the purchasing institution. For comparison purposes, applications evaluated under the *purchased* institution's standards should not be compared to applications evaluated under the *purchasing* institution's standards.).

- The portfolio includes purchased loans. If so, examiners should look for indications that the institution specified loans to purchase based on a prohibited factor or caused a prohibited factor to influence the origination process.
- A complete decision can be made at one of the several underwriting or loan processing centers, each with independent authority. In such a situation, it is best to conduct on-site a separate comparative analysis at each underwriting center. If covering multiple centers is not feasible during the planned examination, examiners should review their processes and internal controls to determine whether or not expanding the scope and/or length of the examination is justified.
- Decision-making responsibility for a single transaction may involve more than one underwriting center. For example, an institution may have authority to decline mortgage applicants, but only the mortgage company subsidiary may approve them. In such a situation, examiners should learn which standards are applied in each entity and the location of records needed for the planned comparisons.
- Applicants can be steered from the financial institution to the subsidiary or other lending channel and vice versa, and what policies and procedures exist to monitor this practice.
- Any third parties, such as brokers or contractors, are involved in the credit decision and how responsibility is allocated among them and the institution. The institution's familiarity with third party actions may be important, for an institution may be in violation if it participates in transactions in which it knew or reasonably ought to have known other parties were discriminating.

As part of understanding the financial institution's own lending operations, it is also important to understand any dealings the financial institution has with affiliated and non-affiliated mortgage loan brokers and other third party lenders.

These brokers may generate mortgage applications and originations solely for a specific financial institution or may broadly gather loan applications for a variety of local, regional, or national lenders. As a result, it is important to recognize what impact these mortgage brokers and other third party lender actions and application processing operations have on the lending operations of a financial institution. Because brokers can be located anywhere in or out of the financial institution's primary lending or CRA assessment areas, it is important to evaluate broker activity and fair lending compliance related to underwriting, terms and conditions, redlining, and steering, each of which is covered in more depth in sections of these procedures. Examiners should consult with their respective agencies for specific guidance regarding broker activity.

If the institution is large and geographically diverse, examiners should select only as many markets or underwriting centers as can be reviewed readily in depth, rather than selecting

proportionally to cover every market. As needed, examiners should narrow the focus to the Metropolitan Statistical Area (MSA) or underwriting center(s) that are determined to present the highest discrimination risk. Examiners should use Loan Application Register (LAR) data organized by underwriting center, if available. After calculating denial rates between the control and prohibited basis groups for the underwriting centers, examiners should select the centers with the highest fair lending risk. This approach would also be used when reviewing pricing or other terms and conditions of approved applicants from the prohibited basis and control groups. If underwriting centers have fewer than five racial or national origin denials, examiners should not examine for racial discrimination in underwriting. Instead, they should shift the focus to other loan products or prohibited bases, or examination types such as a pricing examination.

However, if examiners learn of other indications of risks that favor analyzing a prohibited basis with fewer transactions than the minimum in the sample size tables, they should consult with their supervisory office on possible alternative methods of analysis. For example, there is strong reason to examine a pattern in which almost all of 19 male borrowers received low rates but almost all of four female borrowers received high rates, even though the number of each group is fewer than the stated minimum. Similarly, there would be strong reason to examine a pattern in which almost all of 100 control group applicants were approved but all four prohibited basis group applicants were not, even though the number of prohibited basis denials was fewer than five.

2. Evaluating the Potential for Discriminatory Conduct

Step One: Develop an Overview

Based on his or her understanding of the credit operations and product offerings of an institution, an examiner should determine the nature and amount of information required for the scoping process and should obtain and organize that information. No single examination can reasonably be expected to evaluate compliance performance as to every prohibited basis, in every product, or in every underwriting center or subsidiary of an institution. In addition to information gained in the process of Understanding Credit Operations, above, the examiner should keep in mind the following factors when selecting products for the scoping review:

- Which products and prohibited bases were reviewed during the most recent prior examination(s) and, conversely, which products and prohibited bases have not recently been reviewed?
- Which prohibited basis groups make up a significant portion of the institution's market for the different credit products offered?
- Which products and prohibited basis groups the institution reviewed using either a voluntarily disclosed self-test or a self evaluation?

Based on consideration of the foregoing factors, the examiner should request information for all residential and other loan products considered appropriate for scoping in the current examination

cycle. In addition, wherever feasible, examiners should conduct preliminary interviews with the institution's key underwriting personnel and those involved with establishing the institution's pricing policies and practices. Using the accumulated information, the examiner should evaluate the following, as applicable:

- Underwriting guidelines, policies, and standards
- Descriptions of credit scoring systems, including a list of factors scored, cutoff scores, extent of validation, and any guidance for handling overrides and exceptions. (Refer to *Part A of the Considering Automated Underwriting and Credit Scoring* section of the Appendix for guidance)
- Applicable pricing policies, risk-based pricing models, and guidance for exercising discretion over loan terms and conditions
- Descriptions of any compensation system, including whether compensation is related to, loan production or pricing
- The institution's formal and informal relationships with any finance companies, subprime mortgage or consumer lending entities, or similar institutions
- Loan application forms
- Home Mortgage Disclosure Act – Loan Application Register (HMDA-LAR) or loan registers and lists of declined applications
- Description(s) of databases maintained for loan product(s) to be reviewed
- Records detailing policy exceptions or overrides, exception reporting and monitoring processes
- Copies of any consumer complaints alleging discrimination and related loan files
- Compliance program materials (particularly fair lending policies), training manuals, organization charts, as well as record keeping, monitoring protocols, and internal controls
- Copies of any available marketing materials or descriptions of current or previous marketing plans or programs or pre-screened solicitations.

Step Two: Identify Compliance Program Discrimination Risk Factors

Review information from agency examination work papers, institutional records and any available discussions with management representatives in sufficient detail to understand the organization, staffing, training, recordkeeping, auditing, policies and procedures of the institution's fair lending compliance systems. Review these systems and note the following risk factors:

- C1. Overall institution compliance record is weak.
- C2. Prohibited basis monitoring information required by applicable laws and regulations is nonexistent or incomplete.
- C3. Data and/or recordkeeping problems compromised reliability of previous examination reviews.
- C4. Fair lending problems were previously found in one or more institution products

- or in institution subsidiaries.
- C5. The size, scope, and quality of the compliance management program, including senior management's involvement, designation of a compliance officer, and staffing is materially inferior to programs customarily found in institutions of similar size, market demographics and credit complexity.
 - C6. The institution has not updated compliance policies and procedures to reflect changes in law or in agency guidance.
 - C7. Fair lending training is nonexistent or weak.

Consider these risk factors and their impact on particular lending products and practices as you conduct the product specific risk review during the scoping steps that follow. Where this review identifies fair lending compliance system deficiencies, give them appropriate consideration as part of the Compliance Management Review in Part II of these procedures.

Step Three: Review Residential Loan Products

Although home mortgages may not be the ultimate subject of every fair lending examination, this product line must at least be considered in the course of scoping every institution that is engaged in the residential lending market.

Divide home mortgage loans into the following groupings: home purchase, home improvement, and refinancings. Subdivide those three groups further if an institution does a significant number of any of the following types or forms of residential lending, and consider them separately:

- Government-insured loans
- Mobile home or manufactured housing loans
- Wholesale, indirect and brokered loans
- Portfolio lending (including portfolios of Fannie Mae/Freddie Mac rejections)

In addition, determine whether the institution offers any conventional "affordable" housing loan programs special purpose credit programs or other programs that are specifically designed to assist certain borrowers, such as underserved populations and whether their terms and conditions make them incompatible with regular conventional loans for comparative purposes. If so, consider them separately.

If previous examinations have demonstrated the following, then an examiner may limit the focus of the current examination to alternative underwriting or processing centers or to other residential products that have received less scrutiny in the past:

- A strong fair lending compliance program
- No record of discriminatory transactions at particular decision centers or in particular residential products
- No indication of a significant change in personnel, operations or underwriting or

- pricing policies at those centers or in those residential products
- No unresolved fair lending complaints, administrative proceedings, litigation or similar factors.
- No discretion to set price or credit terms and conditions in particular decision centers or for particular residential products.

Step Four: Identify Residential Lending Discrimination Risk Factors

- Review the lending policies, marketing plans, underwriting, appraisal and pricing guidelines, broker/agent agreements and loan application forms for each residential loan product that represents an appreciable volume of, or displays noticeable growth in, the institution's residential lending.
- Review also any available data regarding the geographic distribution of the institution's loan originations with respect to the race and national origin percentages of the census tracts within its assessment area or, if different, its residential loan product lending area(s).
- Conduct interviews of loan officers and other employees or agents in the residential lending process concerning adherence to and understanding of the above policies and guidelines as well as any relevant operating practices.
- In the course of conducting the foregoing inquiries, look for the following risk factors (factors are numbered alphanumerically to coincide with the type of factor, e.g., "O" for "overt"; "P" for "pricing", etc.).

NOTE: For risk factors below that are marked with an asterisk (*), examiners need not attempt to calculate the indicated ratios for racial or national origin characteristics when the institution is not a HMDA reporter. However, consideration should be given in such cases to whether or not such calculations should be made based on gender or racial-ethnic surrogates.

Overt indicators of discrimination such as:

- O1. Including explicit prohibited basis identifiers in the institution's written or oral policies and procedures (underwriting criteria, pricing standards, etc.)
- O2. Collecting information, conducting inquiries or imposing conditions contrary to express requirements of Regulation B
- O3. Including variables in a credit scoring system that constitute a basis or factor prohibited by Regulation B or, for residential loan scoring systems, the FHAct. (If a credit scoring system scores age, refer to *Part E* of the *Considering Automated Underwriting and Credit Scoring* section of the Appendix.)
- O4. Statements made by the institution's officers, employees or agents which constitute an express or implicit indication that one or more such persons have engaged or do engage in discrimination on a prohibited basis in any aspect of a credit transaction
- O5. Employee or institutional statements that evidence attitudes based on prohibited

basis prejudices or stereotypes.

Indicators of potential disparate treatment in Underwriting such as:

- U1. *Substantial disparities among the approval/denial rates for applicants by monitored prohibited basis characteristic (especially within income categories)
- U2. *Substantial disparities among the application processing times for applicants by monitored prohibited basis characteristic (especially within denial reason groups)
- U3. *Substantially higher proportion of withdrawn/incomplete applications from prohibited basis group applicants than from other applicants
- U4. Vague or unduly subjective underwriting criteria
- U5. Lack of clear guidance on making exceptions to underwriting criteria, including credit scoring overrides
- U6. Lack of clear loan file documentation regarding reasons for any exceptions to standard underwriting criteria, including credit scoring overrides
- U7. Relatively high percentages of either exceptions to underwriting criteria or overrides of credit score cutoffs
- U8. Loan officer or broker compensation based on loan volume (especially loans approved per period of time)
- U9. Consumer complaints alleging discrimination in loan processing or in approving/denying residential loans.

Indicators of potential disparate treatment in Pricing (interest rates, fees, or points) such as:

- P1. Financial incentives for loan officers or brokers to charge higher prices (including interest rate, fees and points). Special attention should be given to situations where financial incentives are accompanied by broad pricing discretion (as in P2), such as through the use of overages or yield spread premiums.
- P2. Presence of broad discretion in loan pricing (including interest rate, fees and points), such as through overages, underages or yield spread premiums. Such discretion may be present even when institutions provide rate sheets and fees schedules, if loan officers or brokers are permitted to deviate from those rates and fees without clear and objective criteria.
- P3. Use of risk-based pricing that is not based on objective criteria or applied consistently
- P4. *Substantial disparities among prices being quoted or charged to applicants who differ as to their monitored prohibited basis characteristics
- P5. Consumer complaints alleging discrimination in residential loan pricing.
- P6. *In mortgage pricing, disparities in the incidence or rate spreads¹ of higher-priced lending by prohibited basis characteristics as reported in the HMDA data.
- P7. *A loan program that contains only borrowers from a prohibited basis group, or has significant differences in the percentages of prohibited basis groups, especially in the absence of a Special Purpose Credit Program under ECOA.

¹ Regulation C, Section 203.4(a)(12).

Indicators of potential **disparate treatment by Steering** such as:

- S1. Lack of clear, objective and consistently implemented standards for (i) referring applicants to subsidiaries, affiliates, or lending channels within the institution (ii) classifying applicants as “prime” or “sub-prime” borrowers, or (iii) deciding what kinds of alternative loan products should be offered or recommended to applicants (product placement).
- S2. Financial incentives for loan officers or brokers to place applicants in nontraditional products (i.e., negative amortization, “interest only”, “payment option” adjustable rate mortgages) or higher cost products.
- S3. For an institution that offers different products based on credit risk levels, any significant differences in percentages of prohibited basis groups in each of the alternative loan product categories.
- S4. *Significant differences in the percentage of prohibited basis applicants in loan products or products with specific features relative to control group applicants. Special attention should be given to products and features that have potentially negative consequences for applicants (i.e., non-traditional mortgages, prepayment penalties, lack of escrow requirements, or credit life insurance)
- S5. *For an institution that has one or more sub-prime mortgage subsidiaries or affiliates, any significant differences, by loan product, in the percentage of prohibited basis applicants of the institution compared to the percentage of prohibited basis applicants of the subsidiary(ies) or affiliate(s).
- S6. *For an institution that has one or more lending channels that originate the same loan product, any significant differences in the percentage of prohibited basis applicants in one of the lending channels compared to the percentage of prohibited basis applicants of the other lending channel.
- S7. Consumer complaints alleging discrimination in residential loan pricing or product placement.
- S8. *For an institution with sub-prime mortgage subsidiaries, a concentration of those subsidiaries’ branches in minority areas relative to its other branches.

Indicators of potential **discriminatory Redlining** such as:

- R1. *Significant differences, as revealed in HMDA data, in the number of applications received, withdrawn, approved not accepted, and closed for incompleteness or loans originated in those areas in the institution's market that have relatively high concentrations of minority group residents compared with areas with relatively low concentrations of minority residents.
- R2. *Significant differences between approval/denial rates for all applicants (minority and non-minority) in areas with relatively high concentrations of minority group residents compared with areas with relatively low concentrations of minority residents.
- R3. *Significant differences between denial rates based on insufficient collateral for

applicants from areas with relatively high concentrations of minority residents and those areas with relatively low concentrations of minority residents.

R4. * Significant differences in the number of originations of higher-priced loans or loans with potentially negative consequences for borrowers, (i.e., non-traditional mortgages, prepayment penalties, lack of escrow requirements) in areas with relatively high concentrations of minority residents compared with areas with relatively low concentrations of minority residents.

R5. Other patterns of lending identified during the most recent CRA examination that differ by the concentration of minority residents.

R6. Explicit demarcation of credit product markets that excludes MSAs, political subdivisions, census tracts, or other geographic areas within the institution's lending market or CRA assessment areas and having relatively high concentrations of minority residents.

R7. Difference in services available or hours of operation at branch offices located in areas with concentrations of minority residents when compared to branch offices located in areas with concentrations of non-minority residents.

R8. Policies on receipt and processing of applications, pricing, conditions, or appraisals and valuation, or on any other aspect of providing residential credit that vary between areas with relatively high concentrations of minority residents and those areas with relatively low concentrations of minority residents.

R9. The institution's CRA assessment area appears to have been drawn to exclude areas with relatively high concentrations of minority residents.

R10. Employee statements that reflect an aversion to doing business in areas with relatively high concentrations of minority residents.

R11. Complaints or other allegations by consumers or community representatives that the institution excludes or restricts access to credit for areas with relatively high concentrations of minority residents. Examiners should review complaints against the institution filed either with their agency or the institution; the CRA public comment file; community contact forms; and the responses to questions about redlining, discrimination, and discouragement of applications, and about meeting the needs of racial or national origin minorities, asked as part of obtaining local perspectives on the performance of financial institutions during prior CRA examinations.

R12. An institution that has most of its branches in predominantly non-minority neighborhoods at the same time that the institution's sub-prime mortgage subsidiary has branches which are located primarily in predominantly minority neighborhoods.

Indicators of potential **disparate treatment in Marketing** of residential products, such as:

M1. Advertising patterns or practices that a reasonable person would believe indicate prohibited basis customers are less desirable.

M2. Advertising only in media serving non-minority areas of the market.

M3. Marketing through brokers or other agents that the institution knows (or has reason to know) would serve only one racial or ethnic group in the market.

M4. Use of marketing programs or procedures for residential loan products that exclude one or more regions or geographies within the institutions assessment or marketing area that have significantly higher percentages of minority group residents than does the remainder of the assessment or marketing area.

M5. Using mailing or other distribution lists or other marketing techniques for pre-screened or other offerings of residential loan products that:

- Explicitly exclude groups of prospective borrowers on a prohibited basis; or
- Exclude geographies (e.g., census tracts, ZIP codes, etc.) within the institution's marketing area that have significantly higher percentages of minority group residents than does the remainder of the marketing area.

M6. *Proportion of prohibited basis applicants is significantly lower than that group's representation in the total population of the market area.

M7. Consumer complaints alleging discrimination in advertising or marketing loans.

Step Five: Organize and Focus Residential Risk Analysis

Review the risk factors identified in Step 4 and, for each loan product that displays risk factors, articulate the possible discriminatory effects encountered and organize the examination of those loan products in accordance with the following guidance. For complex issues regarding these factors, consult with agency supervisory staff.

- Where overt evidence of discrimination, as described in factors O1-O5, has been found in connection with a product, document those findings as described in Part III, B, besides completing the remainder of the planned examination analysis.
- Where any of the risk factors U1-U9 are present, consider conducting an underwriting comparative file analysis as described in Part III, C.
- Where any of the risk factors P1-P7 are present, consider conducting a pricing comparative file analysis as described in Part III, D.
- Where any of the risk factors S1-S8 are present, consider conducting a steering analysis as described in Part III, E.
- Where any of the risk factors R1-R12 are present, consider conducting an analysis for redlining as described in Part III, G.
- Where any of the risk factors M1-M7 are present, consider conducting a marketing analysis as described in Part III, H.
- Where an institution uses age in any credit scoring system, consider conducting an examination analysis of that credit scoring system's compliance with the requirements of Regulation B as described in Part III, I.

Step Six: Identify Consumer Lending Discrimination Risk Factors

For any consumer loan products selected in Step One for risk analysis, examiners should conduct a risk factor review similar to that conducted for residential lending products in Steps Three through Five, above. Examiners should consult with agency supervisory staff regarding the

potential use of surrogates to identify possible prohibited basis group individuals.

NOTE: The term surrogate in this context refers to any factor related to a loan applicant that potentially identifies that applicant's race, color or other prohibited basis characteristic in instances where no direct evidence of that characteristic is available. Thus, in consumer lending, where monitoring data is generally unavailable, a Hispanic or Asian surname could constitute a surrogate for an applicant's race or national origin because the examiner can assume that the institution (which can rebut the presumption) perceived the person to be Hispanic or Asian. Similarly, an applicant's given name could serve as a surrogate for his or her gender. A surrogate for a prohibited basis group characteristic may be used to set up a comparative analysis with control group applicants or borrowers.

Examiners should then follow the rules in Steps Three through Five, above and identify the possible discriminatory patterns encountered and consider examining those products determined to have sufficient risk of discriminatory conduct.

Step Seven: Identify Commercial Lending Discrimination Risk Factors

Where an institution does a substantial amount of lending in the commercial lending market, most notably small business lending and the product has not recently been examined or the underwriting standards have changed since the last examination of the product, the examiner should consider conducting a risk factor review similar to that performed for residential lending products, as feasible, given the limited information available. Such an analysis should generally be limited to determining risk potential based on risk factors U4-U8; P1-P3; R5-R7; and M1-M3.

If the institution makes commercial loans insured by the Small Business Administration (SBA), determine from agency supervisory staff whether SBA loan data (which codes race and other factors) are available for the institution and evaluate those data pursuant to instructions accompanying them.

For large institutions reporting small business loans for CRA purposes and where the institution also voluntarily geocodes loan denials, look for material discrepancies in ratios of approval-to-denial rates for applications in areas with high concentrations of minority residents compared to areas with concentrations of non-minority residents.

Articulate the possible discriminatory patterns identified and consider further examining those products determined to have sufficient risk of discriminatory conduct in accordance with the procedures for commercial lending described in Part III, F.

Step Eight: Complete the Scoping Process

To complete the scoping process, the examiner should review the results of the preceding steps

and select those focal points that warrant examination, based on the relative risk levels identified above. In order to remain within the agency's resource allowances, the examiner may need to choose a smaller number of focal points from among all those selected on the basis of risk. In such instances, set the scope by first, prioritizing focal points on the basis of (i) high number and/or relative severity of risk factors; (ii) high data quality and other factors affecting the likelihood of obtaining reliable examination results; (iii) high loan volume and the likelihood of widespread risk to applicants and borrowers; and (iv) low quality of any compliance program and, second, selecting for examination review as many focal points as resources permit.

Where the judgment process among competing focal points is a close call, information learned in the phase of conducting the compliance management review can be used to further refine the examiner's choices.

PART II

COMPLIANCE MANAGEMENT REVIEW

The Compliance Management Review enables the examination team to determine:

- The intensity of the current examination based on an evaluation of the compliance management measures employed by an institution
- The reliability of the institution's practices and procedures for ensuring continued fair lending compliance.

Generally, the review should focus on

- Determining whether the policies and procedures of the institution enable management to prevent, or to identify and self-correct, illegal disparate treatment in the transactions that relate to the products and issues identified for further analysis under Part I of these procedures
- Obtaining a thorough understanding of the manner by which management addresses its fair lending responsibilities with respect to (a) the institution's lending practices and standards, (b) training and other application-processing aids, (c) guidance to employees or agents in dealing with customers, and (d) its marketing or other promotion of products and services.

To conduct this review, examiners should consider institutional records and interviews with appropriate management personnel in the lending, compliance, audit, and legal functions. The examiner should also refer to the *Compliance Management Analysis Checklist* contained in the Appendix to evaluate the strength of the compliance programs in terms of their capacity to prevent, or to identify and self-correct, fair lending violations in connection with the products or issues selected for analysis. Based on this evaluation

- Set the intensity of the transaction analysis by minimizing sample sizes within the guidelines established in Part III and the *Fair Lending Sample Size Tables* in the Appendix, to the extent warranted by the strength and thoroughness of the compliance programs applicable to those focal points selected for examination
- Identify any compliance program or system deficiencies that merit correction or improvement and present these to management in accordance with Part IV of these procedures.

Where an institution performs a self-evaluation or has voluntarily disclosed the report or results of a self-test of any product or issue that is within the scope of the examination and has been selected for analysis pursuant to Part I of these procedures, examiners may streamline the examination, consistent with agency guidance, provided the self-test or self-evaluation meets the

requirements set forth in *Using Self-Tests and Self-Evaluations to Streamline the Examination* located in the Appendix.

PART III EXAMINATION PROCEDURES

Once the scope and intensity of the examination have been determined, assess the institution's fair lending performance by applying the appropriate procedures that follow to each of the examination focal points already selected.

A. Verify Accuracy of Data

Prior to any analysis and preferably before the scoping process, examiners should assess the accuracy of the data being reviewed. Data verifications should follow specific protocols (sampling, size, etc.) intended to ensure the validity of the review. For example, where an institution's LAR data is relied upon, examiners should generally validate the accuracy of the institution's submitted data by selecting a sample of LAR entries and verifying that the information noted on the LAR was reported according to instructions by comparing information contained in the loan file for each sampled loan. If the LAR data are inconsistent with the information contained in the loan files, depending on the nature of the errors, examiners may not be able to proceed with a fair lending analysis until the LAR data have been corrected by the institution. In cases where inaccuracies impede the examination, examiners should direct the institution to take action to ensure data integrity (data scrubbing, monitoring, training, etc.).

Note: While the procedures refer to the use of HMDA data, other data sources should be considered, especially in the case of non-HMDA reporters or institutions that originate loans but are not required to report them on a LAR.

B. Documenting Overt Evidence of Disparate Treatment

Where the scoping process or any other source identifies overt evidence of disparate treatment, the examiner should assess the nature of the policy or statement and the extent of its impact on affected applicants by conducting the following analysis

Step 1: Where the indicator(s) of overt discrimination are found in or based on a written policy (for example, a credit scorecard) or communication, determine and document:

- a. The precise language of the apparently discriminatory policy or communication and the nature of the fair lending concerns that it raises
- b. The institution's stated purpose in adopting the policy or communication and the identity of the person on whose authority it was issued or adopted
- c. How and when the policy or communication was put into effect
- d. How widely the policy or communication was applied
- e. Whether and to what extent applicants were adversely affected by the policy or

communication.

Step 2: Where any indicator of overt discrimination was an oral statement or unwritten practice, determine and document:

- a. The precise nature of both the statement or practice and of the fair lending concerns that they raise
- b. The identity of the persons making the statement or applying the practice and their descriptions of the reasons for it and the persons authorizing or directing the use of the statement or practice
- c. How and when the statement or practice was disseminated or put into effect
- d. How widely the statement or practice was disseminated or applied
- e. Whether and to what extent applicants were adversely affected by the statement or practice.

Assemble findings and supporting documentation for presentation to management in connection with Part IV of these procedures.

C. Transactional Underwriting Analysis - Residential and Consumer Loans.

Step 1: Set Sample Size

- a. For each focal point selected for this analysis, two samples will be utilized: (i) prohibited basis group denials and (ii) control group approvals, both identified either directly from monitoring information in the case of residential loan applications or through the use of application data or surrogates in the case of consumer applications.
- b. Refer to *Fair Lending Sample Size Tables, Table A* in the Appendix and determine the size of the initial sample for each focal point, based on the number of prohibited basis group denials and the number of control group approvals by the institution during the twelve month (or calendar year) period of lending activity preceding the examination. In the event that the number of denials and/or approvals acted on during the preceding 12 month period substantially exceeds the maximum sample size shown in Table A, reduce the time period from which that sample is selected to a shorter period. (In doing so, make every effort to select a period in which the institution's underwriting standards are most representative of those in effect during the full 12 month period preceding the examination.)
- c. If the number of prohibited basis group denials or control group approvals for a given focal point that were acted upon during the 12 month period referenced in 1.b., above, do not meet the minimum standards set forth in the Sample Size Table, examiners need not attempt a transactional analysis for that focal point. Where other risk factors favor analyzing such a focal point, consult with agency supervisory staff on possible alternative

methods of judgmental comparative analysis.

d. If agency policy calls for a different approach to sampling (e.g., a form of statistical analysis, a mathematical formula, or an automated tool) for a limited class of institutions, examiners should follow that approach.

Step 2: Determine Sample Composition.

a. To the extent the institution maintains records of loan outcomes resulting from exceptions to its credit underwriting standards or other policies (e.g., overrides to credit score cutoffs), request such records for both approvals and denials, sorted by loan product and branch or decision center, if the institution can do so. Include in the initial sample for each focal point all exceptions or overrides applicable to that focal point.

b. Using HMDA/LAR data or, for consumer loans, comparable loan register data to the extent available, choose approved and denied applications based on selection criteria that will maximize the likelihood of finding marginal approved and denied applicants, as discussed below.

c. To the extent that the above factors are inapplicable or other selection criteria are unavailable or do not facilitate selection of the entire sample size of files, complete the initial sample selection by making random file selections from the appropriate sample categories in the Sample Size Table.

Step 3: Compare Approved and Denied Applications

Overview: Although a creditor's written policies and procedures may appear to be nondiscriminatory, lending personnel may interpret or apply policies in a discriminatory manner. In order to detect any disparate treatment among applicants, the examiner should first eliminate all but "marginal transactions" (see 3.b. below) from each selected focal point sample. Then, a detailed profile of each marginal applicant's qualifications, the level of assistance received during the application process, the reasons for denial, the loan terms, and other information should be recorded on an Applicant Profile Spreadsheet. Once profiled, the examiner can compare the target and control groups for evidence that similarly qualified applicants have been treated differently as to either the institution's credit decision or the quality of assistance provided.

a. Create Applicant Profile Spreadsheet

Based upon the institution's written and/or articulated credit standards and loan policies, identify categories of data that should be recorded for each applicant and provide a field for each of these categories on a worksheet or computerized spreadsheet. Certain data (income, loan amount, debt, etc.) should always be included in the spreadsheet, while the other data selected will be tailored for each loan product and institution based on

applicable underwriting criteria and such issues as branch location and underwriter. Where credit bureau scores and/or application scores are an element of the institution's underwriting criteria (or where such information is regularly recorded in loan files, whether expressly used or not), include a data field for this information in the spread sheet.

In order to facilitate comparisons of the quality of assistance provided to target and control group applicants, respectively, every work sheet should provide a "comments" block appropriately labeled as the site for recording observations from the file or interviews regarding how an applicant was, or was not, assisted in overcoming credit deficiencies or otherwise qualifying for approval.

b. Complete Applicant Profiles

From the application files sample for each focal point, complete applicant profiles for selected denied and approved applications as follows:

- A principal goal is to identify cases where similarly qualified prohibited basis and control group applicants had different credit outcomes, because the agencies have found that discrimination, including differences in granting assistance during the approval process, is more likely to occur with respect to applicants who are *not* either clearly qualified or unqualified, i.e., “marginal” applicants. The examiner-in-charge should, during the following steps, judgmentally select from the initial sample only those denied and approved applications which constitute marginal transactions. (See Appendix on *Identifying Marginal Transactions* for guidance)
- If few marginal control group applicants are identified from the initial sample, review additional files of approved control group applicants. This will either increase the number of marginal approvals or confirm that marginal approvals are so infrequent that the marginal denials are unlikely to involve disparate treatment.
- The judgmental selection of both marginal-denied and marginal-approved applicant loan files should be done together, in a “back and forth” manner, to facilitate close matches and a more consistent definition of “marginal” between these two types of loan files.
- Once the marginal files have been identified, the data elements called for on the profile spreadsheet are extracted or noted and entered.
- While conducting the preceding step, the examiner should simultaneously look for and document on the spreadsheet any evidence found in marginal files regarding the following:
 - the extent of any assistance, including both affirmative aid and waivers or partial waivers of credit policy provisions or requirements, that appears to have been provided to marginal-approved control group applicants which

- enabled them to overcome one or more credit deficiencies, such as excessive debt-to-income ratios
- the extent to which marginal-denied target group applicants with similar deficiencies were, or were not, provided similar affirmative aid, waivers or other forms of assistance.

c. Review and Compare Profiles

- For each focal point, review all marginal profiles to determine if the underwriter followed institution lending policies in denying applications and whether the reason(s) for denial were supported by facts documented in the loan file and properly disclosed to the applicant pursuant to Regulation B. If any (a) unexplained deviations from credit standards, (b) inaccurate reasons for denial or (c) incorrect disclosures are noted, (whether in a judgmental underwriting system, a scored system or a mixed system) the examiner should obtain an explanation from the underwriter and document the response on an appropriate workpaper.

NOTE: In constructing the applicant profiles to be compared, examiners must adjust the facts compared so that assistance, waivers, or acts of discretion are treated consistently between applicants. For example, if a control group applicant's DTI ratio was lowered to 42% because the institution decided to include short-term overtime income, and a prohibited basis group applicant who was denied due to "insufficient income" would have had his ratio drop from 46% to 41% if his short-term overtime income had been considered, then the examiners should consider 41%, not 46%, in determining the benchmark.

- For each reason for denial identified within the target group, rank the denied prohibited basis applicants, beginning with the applicant whose qualification(s) related to that reason for denial were least deficient. (The top-ranked denied applicant in each such ranking will be referred to below as the "benchmark" applicant.)
- Compare each marginal control group approval to the benchmark applicant in each reason-for-denial ranking developed in step (b), above. If there are no approvals who are equally or less qualified, then there are no instances of disparate treatment for the institution to account for. For all such approvals that appear no better qualified than the denied benchmark applicant
 - identify the approved loan on the worksheet or spreadsheet as an "overlap approval", and
 - compare that overlap approval with other marginal prohibited basis denials in the ranking to determine whether additional overlaps exist. If so, identify all overlapping approvals and denials as above.
- Where the focal point involves use of a credit scoring system, the analysis for

disparate treatment is similar to the procedures set forth in (c) above, and should focus primarily on overrides of the scoring system itself. For guidance on this type of analysis, refer to *Considering Automated Underwriting and Credit Scoring, Part C* in the Appendix.

Step 4: If there is some evidence of violations in the underwriting process but not enough to clearly establish the existence of a pattern or practice, the examiner should expand the sample as necessary to determine whether a pattern or practice does or does not exist.

Step 5: Discuss all findings resulting from the above comparisons with management and document both the findings and all conversations on an appropriate worksheet.

D. Analyzing Potential Disparities in Pricing and Other Terms and Conditions

Depending on the intensity of the examination and the size of the borrower population to be reviewed, the analysis of decisions on pricing and other terms and conditions may involve a comparative file review, statistical analysis, a combination of the two, or other specialized technique used by an agency. Each examination process assesses an institution's credit-decision standards and whether decisions on pricing and other terms and conditions are applied to borrowers without regard to a prohibited basis.

The procedures below encompass the examination steps for a comparative file review. Examiners should consult their own agency's procedures for detailed guidance where appropriate. For example, when file reviews are undertaken in conjunction with statistical analysis, the guidance on specific sample sizes referenced below may not apply.

Step 1: Determine Sample Selection

Examiners may review data in its entirety or restrict their analysis to a sample depending on the examination approach used and the quality of the institution's compliance management system. The *Fair Lending Sample Size Tables* in the Appendix provide general guidance about appropriate sample sizes. Generally, the sample size should be based on the number of prohibited basis group and control group originations for each focal point selected during the 12 months preceding the examination and the outcome of the compliance management system analysis conducted in Part II. When possible, examiners should request specific loan files in advance and request that the institution have them available for review at the start of the examination.

Step 2: Determine Sample Composition and Create Applicant Profiles

Examiners should tailor their sample and subsequent analysis to the specific factors that the institution considers when determining its pricing, terms, and conditions. For example, while decisions on pricing, and other terms and conditions are part of an institution's underwriting

process, general underwriting criteria should not be used in the analysis if they are not relevant to the term or condition to be reviewed. Additionally, consideration should be limited to factors which examiners determine to be legitimate.

- a. While the period for review should be 12-months, prohibited basis group and control group borrowers should be grouped and reviewed around a range of dates during which the institution's practices for the term or condition being reviewed were the same. Generally, examiners should use the loan origination date or the loan application date.
- b. Identify data to be analyzed for each focal point to be reviewed and record this information for each borrower on a spreadsheet to ensure a valid comparison regarding terms and conditions. For example, in certain cases, an institution may offer slightly differentiated products with significant pricing implications to borrowers. In these cases, it may be appropriate to group these procedures together for the purposes of evaluation.

Step 3: Review Terms and Conditions; Compare with Borrower Outcomes

- a. Review all loan terms and conditions (rates, points, fees, maturity variations, LTVs, collateral requirements, etc.) with special attention to those which are left, in whole or in part, to the discretion of loan officers or underwriters. For each such term or condition, identify (a) any prohibited basis group borrowers in the sample who appear to have been treated unfavorably with respect to that term or condition and (b) any control group borrowers who appear to have been treated favorably with respect to that term or condition. The examiner's analysis should be thoroughly documented in the workpapers.
- b. Identify from the sample universe any control group borrowers who appear to have been treated more favorably than one or more of the above-identified prohibited basis group borrowers and who have pricing or creditworthiness factors (under the institution's standards) that are equal to or less favorable than the prohibited basis group borrowers.
- c. Obtain explanations from the appropriate loan officer or other employee for any differences that exist and reanalyze the sample for evidence of discrimination.
- d. If there is some evidence of violations in the imposition of terms and conditions but not enough to clearly establish the existence of a pattern or practice, the examiner should expand the sample as necessary to determine whether a pattern or practice does or does not exist.
- e. Discuss differences in comparable loans with the institution's management and document all conversations on an appropriate worksheet. For additional guidance on evaluating management's responses, refer to *Part A, 1 - 5, Evaluating Responses to Evidence of Disparate Treatment* in the Appendix.

E. Steering Analysis

An institution that offers a variety of lending products or product features, either through one channel or through multiple channels, may benefit consumers by offering greater choices and meeting the diverse needs of applicants. Greater product offerings and multiple channels, however, may also create a fair lending risk that applicants will be illegally steered to certain choices based on prohibited characteristics.

Several examples illustrate potential fair lending risk:

- An institution that offers different lending products based on credit risk levels may present opportunities for loan officers or brokers to illegally steer applicants to the higher-risk products
- An institution that offers nontraditional loan products or loan products with potentially onerous terms (such as prepayment penalties) may present opportunities for loan officers or brokers to illegally steer applicants to certain products or features
- An institution that offers prime or sub-prime products through different channels may present opportunities for applicants to be illegally steered to the sub-prime channel

The distinction between guiding consumers toward a specific product or feature and illegal steering centers on whether the institution did so on a prohibited basis, rather than based on an applicant's needs or other legitimate factors. It is not necessary to demonstrate financial harm to a group that has been "steered." It is enough to demonstrate that action was taken on a prohibited basis regardless of the ultimate financial outcome. If the scoping analysis reveals the presence of one or more risk factors S1 through S8 for any selected focal point, consult with agency supervisory staff about conducting a steering analysis as described below.

Step 1: Clarify what options are available to applicants.

Through interviews with appropriate personnel of the institution and review of policy manuals, procedure guidelines and other directives, obtain and verify the following information for each product-alternative product pairing or grouping identified above:

- a. All underwriting criteria for the product or feature and their alternatives that are offered by the institution or by a subsidiary or affiliate. Examples of products may include stated income, negative amortization and options ARMs. Examples of terms and features include prepayment penalties and escrow requirements. The distinction between a product, term, and feature may vary institution to institution. For example, some institutions may consider "stated income" a feature, while others may consider that a distinct product.
- b. Pricing or other costs applicable to the product and the alternative product(s), including interest rates, points, and all fees.

Step 2: Document the policies, conditions or criteria that have been adopted by the institution for determining how referrals are to be made and choices presented to applicants.

- a. Obtain not only information regarding the product or feature offered by the institution and alternatives offered by subsidiaries/affiliates, but also information on alternatives offered solely by the institution itself.
- b. Obtain any information regarding a subsidiary of the institution directly from that entity, but seek information regarding an affiliate or holding company subsidiary only from the institution itself.
- c. Obtain all appropriate documentation and provide a written summary of all discussions with loan personnel and managers.
- d. Obtain documentation and/or employee estimates as to the volume of referrals made from or to the institution, for each product, during a relevant time period.
- e. Resolve to the extent possible any discrepancies between information found in the institution's documents and information obtained in discussions with loan personnel and managers by conducting appropriate follow-up interviews.
- f. Identify any policies and procedures established by the institution and/or the subsidiary or affiliate for (i) referring a person who applies to the institution, but does not meet its criteria, to another internal lending channel, subsidiary or affiliate; (ii) offering one or more alternatives to a person who applies to the institution for a specific product or feature, but does not meet its criteria; or (iii) referring a person who applies to a subsidiary or affiliate for its product, but who appears qualified for a loan from the institution, to the institution; or referring a person who applies through one internal lending channel for a product, but who appears to be qualified for a loan through another lending channel to that particular lending channel.
- g. Determine whether loan personnel are encouraged, through financial incentives or otherwise, to make referrals, either from the institution to a subsidiary/affiliate or vice versa. Similarly, determine whether the institution provides financial incentives related to products and features.

Step 3: Determine how referral decisions are made and documented within the institution.

Determine how a referral is made to another internal lending channel, subsidiary, or affiliate. Determine the reason for referral and how it is documented.

Step 4: Determine to what extent individual loan personnel are able to exercise personal discretion in deciding what loan products or other credit alternatives will be made available to a given applicant.

Step 5: Determine whether the institution's stated policies, conditions or criteria in fact are adhered to by individual decision makers. If not, does it appear that different policies or practices are actually in effect?

Enter data from the prohibited basis group sample on the spread sheets and determine whether the institution is, in fact, applying its criteria as stated. For example, if one announced criterion for receiving a "more favorable" prime mortgage loan was a back end debt ratio of no more than 38%, review the spread sheets to determine whether that criteria was adhered to. If the institution's actual treatment of prohibited basis group applicants appears to differ from its stated criteria, document such differences for subsequent discussion with management.

Step 6: To the extent that individual loan personnel have any discretion in deciding what products and features to offer applicants, conduct a comparative analysis to determine whether that discretion has been exercised in a nondiscriminatory manner.

Compare the institution's or subsidiary/affiliate's treatment of control group and prohibited basis group applicants by adapting the "benchmark" and "overlap" technique discussed in Part III, Section C. of these procedures. For purposes of this Steering Analysis, that technique should be conducted as follows:

- a. For each focal point to be analyzed, select a sample of prohibited basis group applicants who received "less favorable" treatment (e.g., referral to a finance company or a subprime mortgage subsidiary or counteroffers of less favorable product alternatives).

NOTE: In selecting the sample, follow the guidance of *Fair Lending Sample Size Tables, Table B* in the Appendix and select "marginal applicants" as instructed in Part III, Section C, above.

- b. Prepare a spread sheet for the sample which contains data entry categories for those underwriting and/or referral criteria that the institution identified in Step 1.b as used in reaching underwriting and referral decisions between the pairs of products.
- c. Review the "less favorably" treated prohibited basis group sample and rank this sample from least qualified to most qualified.
- d. From the sample, identify the best qualified prohibited basis group applicant, based on the criteria identified for the control group, above. This applicant will be the "benchmark" applicant. Rank order the remaining applicants from best to least qualified.
- e. Select a sample of control group applicants. Identify those who were treated "more favorably" with respect to the same product-alternative product pair as the prohibited basis group. (Again refer to the Sample Size Table B and marginal applicant processes noted above in selecting the sample.)
- f. Compare the qualifications of the benchmark applicant with those of the control group applicants, beginning with the least qualified member of that sample. Any control group

applicant who appears less qualified than the benchmark applicant should be identified on the spreadsheet as a "control group overlap".

g. Compare all control group overlaps with other, less qualified prohibited basis group applicants to determine whether additional overlaps exist

h. Document all overlaps as possible disparities in treatment. Discuss all overlaps and related findings (e.g., any differences between stated and actual underwriting and/or referral criteria) with management, documenting all such conversations.

Step 7: Examiners should consult with their agency's supervisory staff if they see a need to contact control group or prohibited basis group applicants to substantiate the steering analysis.

F. Transactional Underwriting Analysis - Commercial Loans.

Overview: Unlike consumer credit, where loan products and prices are generally homogenous and underwriting involves the evaluation of a limited number of credit variables, commercial loans are generally unique and underwriting methods and loan pricing may vary depending on a large number of credit variables. The additional credit analysis that is involved in underwriting commercial credit products will entail additional complexity in the sampling and discrimination analysis process. Although ECOA prohibits discrimination in all commercial credit activities of a covered institution, the agencies recognize that small businesses (sole proprietorships, partnerships, and small, closely-held corporations) may have less experience in borrowing. Small businesses may have fewer borrowing options, which may make them more vulnerable to discrimination. Therefore, in implementing these procedures, examinations should generally be focused on small business credit (commercial applicants that had gross revenues of \$1,000,000 or less in the preceding fiscal year), absent some evidence that a focus on other commercial products would be more appropriate.

Step 1: Understand Commercial Loan Policies

For the commercial product line selected for analysis, the examiner should first review credit policy guidelines and interview appropriate commercial loan managers and officers to obtain written and articulated standards used by the institution in evaluating commercial loan applications.

NOTE: Examiners should consult their own agencies for guidance on when a comparative analysis or statistical analysis is appropriate, and follow their agencies procedures for conducting such a review/analysis.

Step 2: Conduct Comparative File Review

- a. Select all (or a maximum of ten) denied applications that were acted on during the three month period prior to the examination. To the extent feasible, include denied applications from businesses that are (i) located in minority and/or integrated geographies or (ii) appear to be owned by women or minority group members, based on the names of the principals shown on applications or related documents. (In the case of institutions that do a significant volume of commercial lending, consider reviewing more than ten applications.)
- b. For each of the denied commercial applications selected, record specific information from loan files and through interviews with the appropriate loan officer(s), about the principal owners, the purpose of the loan, and the specific, pertinent financial information about the commercial enterprise (including type of business - retail, manufacturing, service, etc.), that was used by the institution to evaluate the credit request. Maintenance or use of data that identifies prohibited basis characteristics of those involved with the business (either in approved or denied loan applications) should be evaluated as a potential violation of Regulation B.
- c. Select ten approved loans that appear to be similar with regard to business type, purpose of loan, loan amount, loan terms, and type of collateral, as the denied loans sampled. For example, if the denied loan sample includes applications for lines of credit to cover inventory purchases for retail businesses, the examiner should select approved applications for lines of credit from retail businesses.
- d. For each approved commercial loan application selected, obtain and record information parallel to that obtained for denied applications.
- e. The examiner should first compare the credit criteria considered in the credit process for each of the approved and denied applications to established underwriting standards, rather than comparing files directly.
- f. The examiner should identify any deviations from credit standards for both approved and denied credit requests, and differences in loan terms granted for approved credit requests.
- g. The examiner should discuss each instance where deviations from credit standards and terms were noted, but were not explained in the file, with the commercial credit underwriter. Each discussion should be documented.

Step 3: Conduct Targeted Sampling

- a. If deviations from credit standards or pricing are not sufficiently explained by other

factors either documented in the credit file or the commercial underwriter was not able to provide a reasonable explanation, the examiner should determine if deviations were detrimental to any protected classes of applicants.

- b. The examiner should consider employing the same techniques for determining race and gender characteristics of commercial applicants as those outlined in the consumer loan sampling procedures.
- c. If it is determined that there are members of one or more prohibited basis groups among commercial credit requests that were not underwritten according to established standards or received less favorable terms, the examiner should select additional commercial loans, where applicants are members of the same prohibited basis group and select similarly situated control group credit requests in order to determine whether there is a pattern or practice of discrimination. These additional files should be selected based on the specific applicant circumstance(s) that appeared to have been viewed differently by lending personnel on a prohibited basis.
- d. If there are not enough similarly situated applicants for comparison in the original sample period to draw a reasonable conclusion, the examiner should expand the sample period. The expanded sample period should generally not go beyond the date of the prior examination.

Sampling Guidelines

- a. Generally, the task of selecting an appropriate expanded sample of prohibited basis and control group applications for commercial loans will require examiner judgment. The examiner should select a sample that is large enough to be able to draw a reasonable conclusion.
- b. The examiner should first select from the applications that were acted on during the initial sample period, but were not included in the initial sample, and select applications from prior time periods as necessary.
- c. The expanded sample should include both approved and denied, prohibited basis and control group applications, where similar credit was requested by similar enterprises for similar purposes.

G. Analysis of Potential Discriminatory “Redlining”.

Overview: For purposes of this analysis, traditional “redlining” is a form of illegal disparate treatment in which an institution provides unequal access to credit, or unequal terms of credit, because of the race, color, national origin, or other prohibited characteristic(s) of the residents of the area in which the credit seeker resides or will reside or in which the residential property to be

mortgaged is located. Redlining may also include “reverse redlining,” the practice of targeting certain borrowers or areas with less advantageous products or services based on prohibited characteristics.

The redlining analysis may be applied to determine whether, on a prohibited basis:

- an institution fails or refuses to extend credit in certain areas;
- an institution targets certain borrowers or certain areas with less advantageous products
- an institution makes loans in such an area but at a restricted level or upon less-favorable terms or conditions as compared to contrasting areas; or
- an institution omits or excludes such an area from efforts to market residential loans or solicit customers for residential credit.

This guidance focuses on possible discrimination based on race or national origin. The same analysis could be adapted to evaluate relative access to credit for areas of geographical concentration on other prohibited bases -- for example, age.

NOTE: It is true that neither the Equal Credit Opportunity Act (ECOA) nor the Fair Housing Act (FHAct) specifically uses the term “redlining.” However, federal courts as well as agencies that have enforcement responsibilities for the FHAct, have interpreted it as prohibiting institutions from having different marketing or lending practices for certain geographic areas, compared to others, where the purpose or effect of such differences would be to discriminate on a prohibited basis. Similarly, the ECOA would prohibit treating applicants for credit differently on the basis of differences in the racial or ethnic composition of their respective neighborhoods.

Like other forms of disparate treatment, redlining can be proven by overt or comparative evidence. If any written or oral policy or statement of the institution (see risk factors R6-10 in Part I, above) suggests that the institution links the racial or national origin character of an area with any aspect of access to or terms of credit, the examiners should refer to the guidance in Section B of this Part III, on documenting and evaluating overt evidence of discrimination.

Overt evidence includes not only explicit statements, but also any geographical terms used by the institution that would, to a reasonable person familiar with the community in question, connote a specific racial or national origin character. For example, if the principal information conveyed by the phrase “north of 110th Street” is that the indicated area is principally occupied by Hispanics, then a policy of not making credit available “north of 110th Street” is overt evidence of potential redlining on the basis of national origin.

Overt evidence is relatively uncommon. Consequently, the redlining analysis usually will focus

on comparative evidence (similar to analyses of possible disparate treatment of individual customers) in which the institution's treatment of areas with contrasting racial or national origin characters is compared.

When the scoping process (including consultation within an agency as called for by agency procedures) indicates that a redlining analysis should be initiated, examiners should complete the following steps of comparative analysis:

1. Identify and delineate any areas within the institution's CRA assessment area and reasonably expected market area for residential products that have a racial or national origin character;
2. Determine whether any minority area identified in Step 1 appears to be excluded, under-served, selectively excluded from marketing efforts, or otherwise less-favorably treated in any way by the institution;
3. Identify and delineate any areas within the institution's CRA assessment area and reasonably expected market area for residential products that are non-minority in character and that the institution appears to treat more favorably;
4. Identify the location of any minority areas located just outside the institution's CRA assessment area and market area for residential products, such that the institution may be purposely avoiding such areas.
5. Obtain the institution's explanation for the apparent difference in treatment between the areas and evaluate whether it is credible and reasonable; and
6. Obtain and evaluate other information that may support or contradict interpreting identified disparities to be the result of intentional illegal discrimination.

These steps are discussed in detail below.

Using information obtained during scoping

Although the six tasks listed are presented below as examination steps in the order given above, examiners should recognize that a different order may be preferable in any given examination. For example, the institution's explanation (Step 5) for one of the policies or patterns in question may already be documented in the CRA materials reviewed (Step 1) and the CRA examiners may already have verified it, which may be sufficient for purposes of the redlining analysis.

As another example, as part of the scoping process, the examiners may have reviewed an analysis of the geographic distribution of the institution's loan originations with respect to the racial and national origin composition of census tracts within its CRA assessment or residential

market area. Such analysis might have documented the existence of significant discrepancies between areas, by degree of minority concentration, in loans originated (risk factor R1), approval/denial rates (risk factor R2) and/or rates of denials because of insufficient collateral (risk factor R3). In such a situation in which the scoping process has produced a reliable factual record, the examiners could begin with Step 5 (obtaining an explanation) of the redlining analysis below.

In contrast, when the scoping process only yields partial or questionable information, or when the risk factors on which the redlining analysis is based on complaints or allegations against the institution, Steps 1-4 must be addressed.

Comparative analysis for redlining

Step 1: Identify and delineate any areas within the institution's CRA assessment area and reasonably expected market area for residential products that are of a racial or national origin minority character.

NOTE: The CRA assessment area can be a convenient unit for redlining analysis because information about it typically already is in hand. However, the CRA assessment area may be too limited. The redlining analysis focuses on the institution's decisions about how much access to credit to provide to different geographical areas. The areas for which those decisions can best be compared are areas where the institution actually marketed and provided credit and where it could reasonably be expected to have marketed and provided credit. Some of those areas might be beyond or otherwise different from the CRA assessment area.

If there are no areas identifiable for their racial or national origin minority character within the institution's CRA assessment area or reasonably expected market area for residential products, a redlining analysis is not appropriate. (If there is a substantial but dispersed minority population, potential disparate treatment can be evaluated by a routine comparative file review of applicants.)

This step may have been substantially completed during scoping, but unresolved matters may remain. (For example, several community spokespersons may allege that the institution is redlining, but disagree in defining the area). The examiners should:

- a. Describe as precisely as possible why a specific area is recognized in the community (perceptions of residents, etc.) and/or is objectively identifiable (based on census or other data) as having a particular racial or national origin minority character.
 - The most obvious identifier is the predominant race or national origin of the residents of the area. Examiners should document the percentages of racial or national origin minorities residing within the census tracts that make up the area.

Analyzing racial and national origin concentrations in quartiles (such as 0 to <=25%, >25% to <= 50%, >50% to <= 75%, and >75%) or based on majority concentration (0 to <=50%, and >50%) may be helpful. However, examiners should bear in mind that it is illegal for the institution to consider a prohibited factor in any way. For example, an area or neighborhood may only have a minority population of 20%, but if the area's concentration appears related to lending practices, it would be appropriate to use that area's level of concentration in the analysis. Contacts with community groups can be helpful to learn whether there are such subtle features of racial or ethnic character within a particular neighborhood.

- Geographical groupings that are convenient for CRA may obscure racial patterns. For example, an underserved, low-income, predominantly minority neighborhood that lies within a larger low-income area that primarily consisted of non-minority neighborhoods, may seem adequately served when the entire low-income area is analyzed as a unit. However, a racial pattern of underservice to minority areas might be revealed if the low-income minority neighborhood shared a border with an underserved, middle-income, minority area and those two minority areas were grouped together for purposes of analysis.

b. Describe how the racial or national origin character changes across the suspected redlining area's various boundaries.

c. Document or estimate the demand for credit, within the minority area. This may include the applicable demographics of the area, including the percentage of homeowners, the median house value, median family income, or the number of small businesses, etc. Review the institution's non-originated loan applications from the suspected redlined areas. If available, review aggregate institution data for loans originated and applications received from the suspected redlined areas. Community contacts may also be helpful in determining the demand for such credit. If the minority area does not have a significant amount of demand for such credit, the area is not appropriate for a redlining analysis.

Step 2: Determine whether any minority area identified in Step 1 is excluded, underserved, selectively excluded from marketing efforts, or otherwise less-favorably treated in any way by the institution.

The examiners should begin with the risk factors identified during the scoping process. The unfavorable treatment may have been substantially documented during scoping and needs only to be finished in this step. If not, this step will verify and measure the extent to which HMDA data show the minority areas identified in Step 1 to be underserved and/or how the institution's explicit policies treat them less favorably.

- a. Review prior CRA lending test analyses to learn whether they have identified any excluded or otherwise under-served areas or other significant geographical disparities in the institution's lending. Determine whether any of those are the minority areas identified in Step 1.
- b. Learn from the institution itself whether, as a matter of policy, it treats any separate or distinct geographical areas within its marketing or service area differently from other areas. This may have been done completely or partially during scoping analysis related to risk factors R5-R9. The differences in treatment can be in marketing, products offered, branch operations (including the services provided and the hours of operation), appraisal practices, application processing, approval requirements, pricing, loan conditions, evaluation of collateral, or any other policy or practice materially related to access to credit. Determine whether any of those less-favored areas are the minority areas identified in Step 1.
- c. Obtain from the institution: (i) its reasons for such differences in policy, (ii) how the differences are implemented, and (iii) any specific conditions that must exist in an area for it to receive the particular treatment (more favorable or less favorable) that the institution has indicated.

Step 3: Identify and delineate any areas within the institution's CRA assessment area and reasonably expected market area for residential products that are non-minority in character and that the institution appears to treat more favorably.

To the extent not already completed during scoping:

- a. Document the percentages of control group and of racial or national origin minorities residing within the census tract(s) that comprise(s) the non-minority area
- b. Document the nature of the housing stock in the area
- c. Describe, to the extent known, how the institution's practices, policies, or its rate of lending change from less- to more-favorable as one leaves the minority area at its various boundaries (Examiners should be particularly attentive to instances in which the boundaries between favored and disfavored areas deviate from boundaries the institution would reasonably be expected to follow, such as political boundaries or transportation barriers)
- d. Examiners should particularly consider whether, within a large area that is composed predominantly of racial or national origin minority households, there are enclaves that are predominantly non-minority or whether, along the area's borders, there are irregularities where the non-minority group is predominant. As part of the overall comparison, examiners should determine whether credit access within those small non-minority areas

differs from credit access in the larger minority area.

Step 4: Identify the location of any minority areas located just outside the institution's CRA assessment area and market area for residential products, such that the institution may be purposely avoiding such areas.

Review the analysis from prior CRA examinations of whether the assessment area appears to have been influenced by prohibited factors. If there are minority areas that the institution excluded from the assessment area improperly, consider whether they ought to be included in the redlining analysis. Analyze the institution's reasonably expected market area in the same manner.

Step 5: Obtain the institution's explanation for the apparent difference in treatment between the areas and evaluate whether it is credible and reasonable.

This step completes the comparative analysis by soliciting from the institution any additional information not yet considered by the examiners that might show that there is a nondiscriminatory explanation for the apparent disparate treatment based on race or ethnicity.

For each matter that requires explanation, provide the institution full information about what differences appear to exist in how it treats minority and non-minority areas, and how the examiners reached their preliminary conclusions at this stage of the analysis.

- a. Evaluate whether the conditions identified by the institution in Step 2 as justifying more favorable treatment pursuant to institutional policy existed in minority neighborhoods that did not receive the favorable treatment called for by institutional policy. If there are minority areas for which those conditions existed, ask the institution to explain why the areas were treated differently despite the similar conditions.
- b. Evaluate whether the conditions identified by the institution in Step 2 as justifying less favorable treatment pursuant to institutional policy existed in non-minority neighborhoods that received favorable treatment nevertheless. If there are non-minority areas for which those conditions existed, ask the institution to explain why those areas were treated differently, despite the similar conditions.
- c. Obtain explanations from the institution for any apparent differences in treatment observed by the examiners but not called for by the institution's policies
 - If the institution's explanation cites any specific conditions in the non-minority area(s) to justify more favorable treatment, determine whether the minority area(s) identified in Step 1 satisfied those conditions. If there are minority areas for which those conditions existed, ask the institution to explain why the areas were treated differently despite the similar conditions
 - If the institution's explanation cites any specific conditions in the minority area(s)

to justify less favorable treatment, determine whether the non-minority area(s) had those conditions. If there are non-minority areas for which those conditions existed, ask the institution to explain why those areas were treated differently, despite the similar conditions.

d. Evaluate the institution's responses by applying appropriate principles selected from the Appendix on *Evaluating Responses to Evidence of Disparate Treatment*.

Step 6: Obtain and evaluate specific types of other information that may support or contradict a finding of redlining.

As a legal matter, discriminatory intent can be inferred simply from the lack of a legitimate explanation for clearly less-favorable treatment of racial or national origin minorities. Nevertheless, if the institution's explanations do not adequately account for a documented difference in treatment, the examiners should consider additional information that might support or contradict the interpretation that the difference in treatment constituted redlining.

- a. Comparative file review. If there was a comparative file review conducted in conjunction with the redlining examination, review the results; or, if it is necessary and feasible to do so to clarify what appears to be discriminatory redlining, compare denied applications from within the suspected redlining area to approved applications from the contrasting area.
- Learn whether there were any denials of fully qualified applicants from the suspected redlining area. If so, that may support the view that the institution was avoiding doing business in the area.
 - Learn whether the file review identified instances of illegal disparate treatment against applicants of the same race or national origin as the suspected redlining area. If so, that may support the view that the institution was avoiding doing business with applicants of that group, such as the residents of the suspected redlining area. Learn whether any such identified victims applied for transactions in the suspected redlining area.
 - If there are instances of either of the above, identify denied non-minority residents, if any, of the suspected redlining area and review their application files to learn whether they appear to have been treated in an irregular or less favorable way. If so, that may support the view that the character of the area rather than of the applicants themselves appears to have influenced the credit decisions.
 - Review withdrawn and incomplete applications for the suspected redlining area, if those can readily be identified from the HMDA-LAR, and learn whether there are reliable indications that the institution discouraged those applicants from applying. If so, that may support the view that the institution was avoiding conducting business in the area and may constitute evidence of a violation of Section 202.4(b) of Regulation B.

Conversely, if the comparisons of individual transactions show that the institution treated minority and non-minority applicants within and outside the suspected redlining area similarly, that tends to contradict the conclusion that the institution avoided the areas because it had minority residents.

b. Interviews of third parties. The perspectives of third parties will have been taken into account to some degree through the review of available materials during scoping. Later in the examination, in appropriate circumstances, information from third parties may help determine whether the institution's apparent differences in treatment of minority and non-minority areas constitute redlining.

- Identify persons (such as housing or credit counselors, home improvement contractors, or real estate and mortgage brokers) who may have extensive experience dealing with credit applicants from the suspected redlined area.
- After obtaining appropriate authorization and guidance from your agency, interview those persons to learn of their first-hand experiences related to:
 - oral statements or written indications by an institution's representatives that loan applications from a suspected redlined area were discouraged;
 - whether the institution treated applicants from the suspected redlining area as called for in its own procedures (as the examiners understand them) and/or whether it treated them similarly to applicants from non-minority areas (as the examiners are familiar with those transactions);
 - any unusual delays or irregularities in loan processing for transactions in the suspected redlining area;
 - differences in the institution's pricing, loan conditions, property valuation practices, etc., in the suspected redlining area compared to contrasting areas.

Also, learn from the third parties the names of any consumers they described as having experienced the questionable behavior recounted by the third party, and consider contacting those consumers.

If third parties witnessed specific conduct by the institution that indicates the institution wanted to avoid business from the area or prohibited basis group in question, this would tend to support interpreting the difference in treatment as intended. Conversely, if third parties report proper treatment or positive actions toward such area or prohibited basis group, this would tend to contradict the view that the institution intended to discriminate.

c. Marketing. A clear exclusion of the suspected redlining area from the institution's marketing of residential loan products supports the view that the institution did not want to do business in the area. Marketing decisions are affirmative acts to include or exclude areas. Disparities in marketing between two areas may reveal that the institution prefers one to the other. If sufficiently stark and supported by other evidence, a difference in marketing to racially different areas could itself be treated as a redlining violation of the

Fair Housing Act. Even below that level of difference, marketing patterns can support or contradict the view that disparities in lending practices were intentional.

- Review materials that show how the institution has marketed in the suspected redlined area and in non-minority areas. Begin with available CRA materials and discuss the issues with CRA examiners, then review other materials as appropriate. The materials may include, for example, the institution's guidance for the geographical distribution of pre-approved solicitations for credit cards or home equity lines of credit, advertisements in local media or business or telephone directories, business development calls to real estate brokers, and calls by telemarketers.

d. Peer performance. Market share analysis and other comparisons to competitors are insufficient by themselves to prove that an institution engaged in illegal redlining. By the same token, an institution cannot justify its own failure to market or lend in an area by citing other institutions' failures to lend or market there.

However, an institution's inactivity in an underserved area where its acknowledged competitors are active would tend to support the interpretation that it intends to avoid doing business in the area. Conversely, if it is as active as other institutions that would suggest that it intends to compete for, rather than avoid, business in the area.

- Develop a list of the institution's competitors.
- Learn the level of lending in the suspected redlining area by competitors. Check any public evaluations of similarly situated competitors obtained by the CRA examiners as part of evaluating the performance context or obtain such evaluations independently.

e. Institution's record. Request from the institution information about its overall record of serving or attempting to serve the racial or national origin minority group with which the suspected redlining area is identified. The record may reveal an intent to serve that group that tends to contradict the view that the institution intends to discriminate against the group.

NOTE: For any information that supports interpreting the situation as illegal discrimination, obtain and evaluate an explanation from the institution as called for in Part IV. If the institution's explanation is that the disparate results are the consequence of a specific, neutral policy or practice that the institution applies broadly, such as not making loans on homes below a certain value, review the guidance in the *Special Analyses* section of the Appendix under *Disproportionate Adverse Impact Violations* and consult agency managers.

H. Analysis of Potential Discriminatory Marketing Practices.

When scoping identifies significant risk factors (M1-M7) related to marketing, examiners should consult their agency's supervisory staff and experts about a possible marketing discrimination

analysis. If the supervisory staff agrees to proceed, the examiners should collect information as follows:

Step 1: Identify the institution's marketing initiatives.

a. Pre-approved solicitations

- Determine whether the institution sends out pre-approved solicitations:
 - for home purchase loans
 - for home improvement loans
 - for refinance loans
- Determine how the institution selects recipients for such solicitations
 - learn from the institution its criteria for such selections
 - review any guidance or other information the institution provided credit reporting companies or other companies that supply such lists

b. Media Usage

- Determine in which newspapers and broadcast media the institution advertises.
 - identify any racial or national origin identity associated with those media
 - determine whether those media focus on geographical communities of a particular racial or national origin character
- Learn the institution's strategies for geographic and demographic distribution of advertisements.
- Obtain and review copies of the institution's printed advertising and promotional materials.
- Determine what criteria the institution communicates to media about what is an attractive customer or an attractive area to cultivate business.
- Determine whether advertising and marketing are the same to racial and national origin minority areas as compared to non-minority areas.

c. Self-produced promotional materials

- Learn how the institution distributes its own promotional materials, both methods and geographical distribution
- Learn what the institution regards as the target audience(s) for those materials

d. Realtors, brokers, contractors, and other intermediaries

- Determine whether the institution solicits business from specific realtors, brokers, home improvement contractors, and other conduits.
 - learn how the institution decides which intermediaries it will solicit
 - identify the parties contacted and determine the distribution between minority and non-minority areas
 - obtain and review the types of information the institution distributes to intermediaries
 - determine how often the institution contacts intermediaries

- Determine what criteria the institution communicates to intermediaries about the type of customers it seeks or the nature of the geographic areas in which it wishes to do business.
- e. Telemarketers or predictive dialer programs
 - Learn how the institution identifies which consumers to contact, and whether the institution sets any parameters on how the list of consumers is compiled.

Step 2: Determine whether the institution's activities show a significantly lower level of marketing effort toward minority areas or toward media or intermediaries that tend to reach minority areas.

Step 3: If there is any such disparity, document the institution's explanation for it.

For additional guidance, refer to *Part C* of the *Special Analyses* section in the Appendix.

I. Credit Scoring.

If the scoping process results in the selection of a focal point that includes a credit or mortgage scored loan product, refer to the *Considering Automated Underwriting and Credit Scoring* section of the Appendix.

If the institution utilizes a credit scoring program which scores *age* for any loan product selected for review in the scoping stage, either as the sole underwriting determinant or only as a guide to making loan decisions, refer to *Part E* of the *Considering Automated Underwriting and Credit Scoring* section of the Appendix.

J. Disparate Impact Issues.

These procedures have thus far focused primarily on examining comparative evidence for possible unlawful disparate treatment. Disparate impact has been described briefly in the Introduction. Whenever an examiner believes that a particular policy or practice of an institution appears to have a disparate impact on a prohibited basis, the examiner should refer to Part A of the *Special Analyses* section of the Appendix or consult with agency supervisory staff for further guidance.

**PART IV
OBTAINING AND EVALUATING RESPONSES FROM THE INSTITUTION
AND CONCLUDING THE EXAMINATION**

Step 1: Present to the institution’s management for explanation:

- a. Any overt evidence of disparate treatment on a prohibited basis.
- b. All instances of apparent disparate treatment (e.g., overlaps) in either the underwriting of loans or in loan prices, terms, or conditions.
- c. All instances of apparent disparate treatment in the form of discriminatory steering, redlining, or marketing policies or practices.
- d. All instances where a denied prohibited basis applicant was not afforded the same level of assistance or the same benefit of discretion as an approved control group applicant who was no better qualified with regard to the reason for denial.
- e. All instances where a prohibited basis applicant received conspicuously less favorable treatment by the institution than was customary from the institution or was required by the institution's policy.
- f. Any statistically significant average difference in either the frequency or amount of pricing disparities between control group and prohibited basis group applicants.
- g. Any evidence of neutral policies, procedures or practices that appear to have a disparate impact or effect on a prohibited basis.

Explain that unless there are legitimate, nondiscriminatory explanations (or in the case of disparate impact, a compelling business justification) for each of the preliminary findings of discrimination identified in this Part, the agency could conclude that the institution is in violation of the applicable fair lending laws.

Step 2: Document all responses that have been provided by the institution, not just its “best” or “final” response. Document each discussion with dates, names, titles, questions, responses, any information that supports or undercuts the institution's credibility, and any other information that bears on the issues raised in the discussion(s).

Step 3: Evaluate whether the responses are consistent with previous statements, information obtained from file review, documents, reasonable banking practices, and other sources, and satisfy common-sense standards of logic and credibility.

- a. Do not speculate or assume that the institution's decision-maker had specific intentions or considerations in mind when he or she took the actions being evaluated. Do not, for example, conclude that because you have noticed a legitimate, nondiscriminatory reason for a denial (such as an applicant's credit weakness), that no discrimination occurred unless it is clear that, at the time of the denial, the institution actually based the denial on that reason.
- b. Perform follow-up file reviews and comparative analyses, as necessary, to determine the accuracy and credibility of the institution's explanations.
- c. Refer to *Evaluating Responses to Evidence of Disparate Treatment* in the Appendix for guidance as to common types of responses.
- d. Refer to the *Disproportionate Adverse Impact Violations* portion of the *Special Analyses* section of the Appendix for guidance on evaluating the institution's responses to apparent disparate impact.

Step 4: If, after completing Steps 1 - 3 above, you conclude that the institution has failed to adequately demonstrate that one or more apparent violations had a legitimate nondiscriminatory basis or were otherwise lawful, prepare a documented list or discussion of violations, or a draft examination report, as prescribed by agency directives.

Step 5: Consult with agency supervisory staff regarding whether (a) any violations should be referred to the Departments of Justice or Housing and Urban Development and (b) enforcement action should be undertaken by your agency.

DECEMBER 2012

Fair Lending Report of the Consumer Financial Protection Bureau



Consumer Financial
Protection Bureau

Message from Richard Cordray

Director of the CFPB



On July 21, 2011, the Consumer Financial Protection Bureau was launched as the first government agency solely dedicated to consumer financial protection. This report on Fair Lending describes the Bureau's efforts to build and implement our fair lending program.

As the past few years have shown, financial products have the potential to wreak havoc on consumers and the wider economy. Far too often, unequal access to responsible credit can be at the root of these trends and problems. When a potential homeowner cannot get a home mortgage or a small business owner cannot obtain a loan for capital improvements, because of the neighborhood where the home or business is located, both the consumer and the community they belong to suffer.

The belief that each of us can better our lot in life – that our children's future will be brighter than our own – is deeply ingrained in the fabric of this country. Essential to that belief is the premise that each of us can access equality of opportunity, and that it is not limited only to a certain privileged set of Americans who are especially blessed by fortune or background. Too often, that equality of opportunity is harder to find than any of us would like or want to believe.

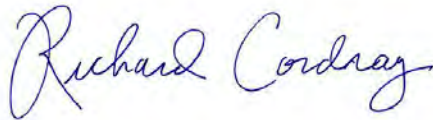
The CFPB is committed to making fair, equitable, and nondiscriminatory access to credit for both individuals and communities a reality. Through the leadership of the Office of Fair Lending and Equal Opportunity and the collaboration of various divisions and offices across the Bureau, we strive to make the financial markets work for consumers, honest businesses, and the economy as a whole. We will work to educate consumers about their fair lending rights, and we will warn them

about the costs and risks associated with financial products and services while working to improve the practices of financial institutions.

Dr. Martin Luther King, Jr. once said, “Our lives begin to end the day we become silent about things that matter.” The Consumer Financial Protection Bureau is still in its infancy, but we are here today to say plainly that we will not be silent about discriminatory lending practices. Illegal discrimination in all of its forms is wrong, and it violates the fundamental American precept that each individual should have access to equality of opportunity. Our twin goals are to protect consumers and empower them to be able to protect themselves.

We are intent on making the financial markets work better for the people we serve. Consumers deserve to have someone who stands on their side and sees to it that they are treated fairly and equally in the financial marketplace.

Sincerely,

A handwritten signature in blue ink that reads "Richard Cordray". The signature is written in a cursive, flowing style.

Richard Cordray

Message from Patrice Alexander Ficklin



Assistant Director for Fair Lending and Equal Opportunity

In mid-May 2011, I took my oath to serve as Assistant Director and lead the Office of Fair Lending and Equal Opportunity at the Consumer Financial Protection Bureau. Since that day, the Office of Fair Lending and Equal Opportunity has been hard at work to ensure that all consumers, regardless of protected status, have fair and equal access to credit. I am honored to serve as Assistant Director for Fair Lending and Equal Opportunity and to share with you a progress report on the Bureau's efforts in this important area, which is at the intersection of consumer financial protection and civil rights.

Having served as counsel to financial services providers and to civil rights and advocacy groups, my role as Assistant Director for Fair Lending at the Bureau is deeply informed by these varied perspectives. Because of my experience, I came to the Bureau well aware of the deep commitment to fair lending that is shared by a broad constituency of consumer advocates, civil rights groups, and many in industry as well. These experiences have also led me to embrace this opportunity as one that will allow a fresh look at ways that a federal agency with fair lending supervisory, enforcement, and rulemaking responsibilities can ensure compliance with the federal fair lending laws, while also promoting access to responsible credit for underserved markets and consumers.

I have the honor of leading a team with diverse expertise and perspectives. These experiences translate into innovative thinking and approaches to questions related to equal access to credit and fair lending that thousands of consumers face every day. In addition to our supervisory,

enforcement, and rulemaking activities, our outreach efforts have deployed CFPB team members across the country, to work with industry and advocacy groups on the promotion of fair lending compliance and education. Our work is informed by these collaborative partnerships and ongoing dialogue, and we remain committed to these efforts as a means to consistently review and reassess our perspectives on the consumer financial marketplace and access to credit.

The Bureau's fair lending mission is not pursued in a vacuum. We will continue to collaborate with federal and state partners to achieve efficient and effective outcomes for the benefit of consumers. The Bureau is also an active participant in several interagency fair lending efforts, and works closely with the various federal agencies charged with fair lending supervisory and enforcement responsibilities. As you will see in this Report, the Bureau now has responsibility for preparing the comprehensive fair lending reports to Congress that are prescribed by the Equal Credit Opportunity Act and the Home Mortgage Disclosure Act. These reports are the result of coordination and collaboration with other federal partners.

As a 21st century agency, the Bureau communicates with consumers in varied ways – through traditional means, including “Outside the Beltway” field hearings that are open to the public, and also through the latest technologies. I have been enriched by the opportunity to interact with consumers, and I look forward to continued dialogue. We want to hear from consumers about their personal consumer finance stories, and we also want to ensure that they have the latest and best information available to make informed decisions about the financial products that are best suited for their family's needs.

I encourage you to visit our website, consumerfinance.gov, where consumers can learn about the next field hearing; understand their fair lending rights; ask the CFPB a question; tell their consumer finance story through the “Tell Your Story” function; or read a blog entry about a current trend in the consumer finance marketplace. Consumers can also follow the Bureau via our Twitter feed and tweet their voice on consumer financial issues to us.

I am proud to present the Bureau's first Report on Fair Lending.

Sincerely,

A handwritten signature in blue ink that reads "Patrice Alexander Ficklin". The signature is written in a cursive, flowing style.

Patrice Alexander Ficklin

Table of Contents

| | |
|---|-----------|
| Message from Richard Cordray | 2 |
| Message from Patrice Alexander Ficklin | 4 |
| Executive Summary | 8 |
| Fair Lending Mandate..... | 8 |
| First Year Accomplishments | 10 |
| Next Steps | 11 |
| 1. Building and Implementing the CFPB’s Fair Lending Program | 12 |
| 1.1 Building the Office of Fair Lending and Equal Opportunity..... | 13 |
| 2. First Year Accomplishments..... | 14 |
| 2.1 Using Fair Lending Supervisory Oversight and Enforcement to Identify and Eliminate Consumer Harm | 14 |
| 2.2 Fair Lending Enforcement Activity | 16 |
| 2.3 Fair Lending Consumer Education and Engagement..... | 17 |
| 2.4 A Data-Driven Approach to Fair Lending – Collaboration with Research, Markets, and Regulations | 19 |
| 2.5 Dodd-Frank Act Report to Congress on Private Student Loans | 20 |
| 2.6 Amending Fair Lending Regulations | 25 |

| | |
|---|-----------|
| 3. Reporting on the Equal Credit Opportunity Act and the Home Mortgage Disclosure Act | 27 |
| 3.1 Reporting on the Equal Credit Opportunity Act | 27 |
| 3.2 Reporting on the Home Mortgage Disclosure Act | 32 |
| 4. CFPB Outreach: Working with Private Industry, Fair Lending, Civil Rights, Consumer and Community Advocates..... | 34 |
| 4.1 Private Industry Outreach | 34 |
| 4.2 Outreach to Fair Lending, Civil Rights, Consumer and Community Advocates..... | 35 |
| 5. Fair Lending Look Ahead | 38 |

Executive Summary

Endowed by Congress with a unique consumer financial protection mission, the Consumer Financial Protection Bureau (CFPB) brings a new focus to questions of fair lending and equal access to credit in the consumer finance marketplace.

In this inaugural Report on Fair Lending, the CFPB provides a comprehensive overview of our fair lending program and describes our work in this area from July 21, 2011 through July 20, 2012. Additionally, this Report fulfills congressional reporting requirements under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) (§ 1013(c)(2)(D) of Public Law 111-203), the Equal Credit Opportunity Act (ECOA) (15 U.S.C. § 1691f),¹ and the Home Mortgage Disclosure Act (HMDA) (12 U.S.C. § 2807).

Fair Lending Mandate

The Dodd-Frank Act vests the CFPB with specified supervisory, enforcement, and rulemaking authority with respect to a number of federal consumer financial laws, including ECOA and HMDA. ECOA has broad coverage, prohibiting discrimination in mortgage lending and a wide array of other types of lending, including auto finance, credit cards, business loans, and unsecured loans. HMDA requires that specified mortgage lenders annually collect and report mortgage lending data in order to determine whether institutions are serving the housing needs of their communities, to aid in targeting public investment, and to identify possible discriminatory lending patterns and enforce fair lending laws.

¹ The ECOA Report covers the period from July 21, 2011 through December 31, 2011.

In addition to responsibilities for ECOA and HMDA, Congress also charged the CFPB with addressing a number of fair lending-related areas of interest, set forth in the Dodd-Frank Act. These include:

- *Establishment of the Office of Fair Lending and Equal Opportunity.* Congress required the creation of the Office of Fair Lending and Equal Opportunity within the CFPB, and charged the office with ensuring that the CFPB provides “oversight and enforcement of Federal laws intended to ensure the fair, equitable, and nondiscriminatory access to credit for both individuals and communities that are enforced by the CFPB, including the Equal Credit Opportunity Act and the Home Mortgage Disclosure Act.” (Dodd-Frank Act § 1013(c)).
- *Rulemaking.* Congress mandated new rules under:
 - ECOA – to “facilitate enforcement of fair lending laws and enable communities, governmental entities, and creditors to identify business and community development needs and opportunities of women-owned, minority-owned, and small businesses” (Dodd-Frank Act § 1071);
 - HMDA – to require mortgage lenders to collect and report additional data fields (Dodd-Frank Act § 1094); and
 - The Truth in Lending Act (TILA) (15 U.S.C. § 1602) – to “prohibit . . . abusive or unfair lending practices that promote disparities among consumers of equal credit worthiness but of different race, ethnicity, gender, or age” (Dodd-Frank Act § 1403).
- *Reports to Congress.* Congress mandated CFPB reports on topics that raise fair lending-related issues, including remittances, credit scoring, and reverse mortgages. In addition, Congress directed the CFPB to “examine, at a minimum . . . the underwriting criteria used by private education lenders, including the use of cohort default rate” and to examine whether federal regulators and the public have access to sufficient information to “determine lender compliance with fair lending laws” (Dodd-Frank Act § 1077). Finally, the Dodd-Frank Act transferred to the CFPB annual reporting responsibilities set forth in ECOA and HMDA.

First Year Accomplishments

The Office of Fair Lending and Equal Opportunity, in conjunction with other CFPB offices, has spent considerable time during the CFPB's first year addressing the priorities established in our mandate, and expects that some will remain priorities in the months and years to come. In addition to our Congressional directives, we have identified a number of other important areas to be addressed as the CFPB executes its fair lending mission. This includes ensuring the appropriate breadth of the CFPB's fair lending supervision and enforcement activities, and specifically addressing compliance by a range of financial services providers – including both banks and nonbanks – that offer a variety of loan products such as home mortgages, auto loans, student loans, credit cards, and small-business loans.

Our first-year accomplishments include:

- Establishment of the Office of Fair Lending and Equal Opportunity, and the recruitment of a diverse and highly-qualified fair lending team;
- Commencement of the CFPB's fair lending supervision program, and completion of various levels of fair lending reviews at dozens of bank and nonbank institutions offering a variety of lending products;
- Commencement of the CFPB's fair lending enforcement program, and initiation of fair lending investigations;
- Ongoing work on amendments to the regulation that implements HMDA, and planning for the amendments to regulations that implement ECOA and TILA;
- Completion of an empirical study and report to Congress on the use of cohort default rates in private education lending;
- Ongoing collaboration and coordination with federal and state partners; and
- Outreach to private industry as well as fair lending, civil rights, and consumer and community advocates through dozens of meetings and events in Washington, DC and across the country.

Next Steps

The CFPB is committed to ensuring that all consumers and communities have fair and equal access to credit. We are still in the process of building our fair lending program and expect the CFPB's contribution to the work of ensuring compliance with fair lending laws and promoting access to credit will grow as our program progresses. We are also developing risk-based approaches to our fair lending supervision and enforcement work to efficiently allocate the CFPB's resources in a manner that provides the greatest benefit to consumers. As the CFPB and the Office of Fair Lending and Equal Opportunity mature, we pledge to continue to promote fair, equal, and nondiscriminatory access to credit and fair lending for all consumers and communities.

1. Building and Implementing the CFPB's Fair Lending Program

The Office of Fair Lending and Equal Opportunity plays a leading role in the CFPB's efforts to ensure fair, equitable, and nondiscriminatory access to credit for both individuals and communities. Our vision is a consumer finance marketplace where individuals and communities have fair and equal access to financial products and services, product pricing reflects risk and value, and terms and conditions are clear and nondiscriminatory. Because our mission intersects with that of many other offices within the CFPB, we are involved with initiatives in many areas of the CFPB's work.

Congress created the Office of Fair Lending and Equal Opportunity² in the Dodd-Frank Act.³ The Office of Fair Lending is located within the Division of Supervision, Enforcement, and Fair Lending, which is headed by Associate Director Steven Antonakes. Within the Division, the Office of Fair Lending works closely with our supervision and enforcement counterparts to ensure that financial institutions supervised by the CFPB comply with federal fair lending laws and regulations over which the CFPB has jurisdiction. We provide guidance and support to large bank and nonbank examination teams to ensure that financial institutions' fair lending policies and practices are thoroughly examined and that concerns or violations are identified and addressed. We are also active in the CFPB's enforcement process and, together with our enforcement colleagues, lead the CFPB's fair lending enforcement program and priorities.

² Hereinafter referred to as the Office of Fair Lending.

³ Pub. L. No. 111-203, tit. X, § 1013(c)(1), 124 Stat. 1376, 1970 (2010) (codified at 12 U.S.C. § 5493(c)(1)).

1.1 Building the Office of Fair Lending and Equal Opportunity

To implement the CFPB's vision for the consumer financial marketplace, Assistant Director Patrice Alexander Ficklin has assembled a diverse and highly-qualified fair lending team consisting of attorneys, law clerks, risk analysts, operations analysts, and administrative specialists. The team brings to the CFPB a vast array of expertise and experience, from the federal prudential regulators, the United States Department of Justice (DOJ), the United States Department of Housing and Urban Development (HUD), the Federal Trade Commission (FTC), state attorneys general offices, a local human relations commission, civil rights organizations, and financial services providers. This diverse group is unified by one common goal – a commitment to promoting fair lending and equal access to credit.

Access to credit is the ticket to a middle-class lifestyle, which typically requires loans to go to college, make everyday consumer purchases, buy a car, own a home, or to cope with temporary financial difficulties. Those who work to promote equal access to credit – whether in government, private practice, or within regulated institutions themselves – are truly advancing the current civil rights cause.

Counsel, Office of Fair Lending and Equal Opportunity

2. First Year Accomplishments

The CFPB has many tools across several divisions – including the Division of Supervision, Enforcement, and Fair Lending; the Division of Research, Markets, and Regulations; and the Division of Consumer Education and Engagement – to fulfill its fair lending mission. Through close collaboration with CFPB partners, the Office of Fair Lending uses all the tools at its disposal, including supervision, enforcement, consumer education and engagement, the study of consumer financial markets, empirical research and analysis, and rulemaking to ensure that the CFPB’s mission of promoting fair and equal access to credit is a reality for consumers and communities alike.

2.1 Using Fair Lending Supervisory Oversight and Enforcement to Identify and Eliminate Consumer Harm

On October 13, 2011, the CFPB released its Supervision and Examination Manual, which was the culmination of months of work by many offices within the CFPB, including the Office of Fair Lending. The Manual is a guide to how the CFPB will supervise and examine consumer financial services institutions under its jurisdiction for compliance with the Federal consumer financial laws. The Manual contains supervisory guidance on ECOA and HMDA. On April 18, 2012, the CFPB

issued a Compliance Bulletin on Fair Lending that addressed lending discrimination.⁴ The Bulletin stated that “[c]onsistent with other federal supervisory and law enforcement agencies, the CFPB reaffirms that the legal doctrine of disparate impact remains applicable as the Bureau exercises its supervision and enforcement authority to enforce compliance with the ECOA and Regulation B.”⁵

The CFPB’s supervision program assesses large bank and nonbank compliance with Federal consumer financial laws and regulations. CFPB-supervised entities include banks, thrifts, and credit unions with assets over \$10 billion, and their affiliates and service providers, as well as nonbank financial services providers such as mortgage lenders and brokers, payday lenders, private education lenders, and their service providers. In the CFPB’s supervision of large banks and nonbank financial entities, we are committed to conducting examinations that focus on risk to consumers and place the highest importance on identifying any violations of Federal consumer financial laws and eliminating any resulting harm to consumers. We also expect that regulated entities under the CFPB’s jurisdiction will have effective compliance management systems, including effective *fair lending* compliance management systems, which are adapted to the institution’s business strategy and operation.

Thus far in fiscal year 2012, the Office of Fair Lending has supported CFPB examiners in activities at dozens of institutions – both bank and nonbank. These activities ranged from assessments of the institutions’ fair lending compliance management systems to in-depth reviews of products or activities that may pose heightened fair lending risks to consumers.

The Office of Fair Lending has led efforts to train CFPB examiners on the federal fair lending laws, and developed procedures to assist these examiners in the identification of potential fair lending violations. As part of the CFPB’s new employee orientation program, every examiner joining the CFPB receives fair lending training, which was developed and is conducted by the Office of Fair Lending. In addition, attorneys from the Office of Fair Lending periodically brief regional examination teams on fair lending topics and provide updates on fair lending trends and issues observed through examinations. In June 2012, the CFPB launched its Fair Lending Examination

⁴ CFPB Bulletin 2012-04 (Fair Lending) (Apr. 18, 2012), *available at* http://files.consumerfinance.gov/f/201404_cfpb_bulletin_lending_discrimination.pdf.

⁵ CFPB Bulletin, *supra* note 4, at 1.

Techniques training program, a two-week course that was developed through close collaboration among the Offices of Fair Lending, Large Bank and Nonbank Supervision, and others. The course is designed to provide additional in-depth training to CFPB examiners and is a prerequisite to the CFPB's examiner commissioning process.



Assistant Director Patrice Alexander Ficklin, CFPB Deputy Director Raj Date, and Nonbank Supervision Assistant Director Peggy Twohig participate in a field hearing on payday lending in Birmingham, AL.

2.2 Fair Lending Enforcement Activity

The CFPB has many tools available to promote fair and nondiscriminatory treatment of consumers, including the authority to bring enforcement actions. The CFPB has the ability to conduct investigations, file administrative complaints, and hold hearings and adjudicate claims through the CFPB's administrative enforcement process. The CFPB has independent litigating authority and can therefore file cases in federal court alleging violations of fair lending laws under the CFPB's jurisdiction. The CFPB will also refer findings of certain ECOA violations to the DOJ. The CFPB coordinates closely not only with the DOJ, but also with other federal enforcement agencies and state regulators, including the FTC, HUD, and state attorneys general, to ensure that fair lending enforcement efforts are consistent, efficient, and effective.

The Offices of Fair Lending and Enforcement work closely and collaboratively on investigations that may involve fair lending issues, in order to leverage the expertise of the respective offices toward the goal of effective enforcement of fair lending laws. The CFPB's Fair Lending and Enforcement offices have a number of pending fair lending investigations, including matters arising from the CFPB's supervisory activity and joint investigations with other federal agencies. While the details of ongoing investigations are confidential, the CFPB's conclusions will typically be made public if an enforcement action is filed at the conclusion of an investigation.

The Office of Fair Lending has developed and conducted training courses for enforcement attorneys on fair lending issues as well.

2.3 Fair Lending Consumer Education and Engagement

Central to the CFPB's work is consumer education and engagement. The Dodd-Frank Act established the Office of Financial Education, which is vested with the responsibility of developing and implementing initiatives intended to educate and empower consumers to make better financial decisions.⁶ The Offices of Fair Lending and Financial Education work together to educate consumers and promote awareness of federal fair lending laws, such as ECOA, with the goal of helping consumers recognize prohibited practices and protect themselves from discriminatory acts. For example, in a brochure released in May 2012, entitled "Credit Discrimination is Illegal," consumers are advised about ECOA's protections, warning signs of discrimination, and how to protect themselves by being active, engaged consumers. More information is available at consumerfinance.gov/fair-lending/.

⁶ Dodd-Frank Act, § 1013(d)(1).

As a 21st century agency, the CFPB uses both traditional resources, such as its “Credit Discrimination is Illegal” brochure; and social media connections, including a post by Assistant Director Ficklin titled “Fair Notice on Fair Lending”⁷ and other blog entries, to reach and engage consumers. Because educated consumers are the first line of defense against discriminatory practices, consumer education in fair lending and access to credit matters is and will remain essential to achieving the CFPB’s fair lending mission.

About the Consumer Financial Protection Bureau

The Consumer Bureau is focused on making the consumer financial markets work for families by helping consumers to take more control over their financial lives. We are working to foster a marketplace:

- Where consumers can see prices and risks up front and can easily compare products
- Where financial service providers can't build a business model around unfair, deceptive, or abusive practices
- That works for all consumers, responsible lenders, and the economy as a whole

Submit a complaint

If you believe you have been discriminated against, you can file a complaint with the Consumer Bureau by visiting:

- consumerfinance.gov
- complaint line (855) 411-CFPB (2372)
- TTY/TDD (855) 729-CFPB (2372)

Tell us your story

Whether or not you file a complaint, you can help us protect consumers and create a fairer marketplace by telling us about your experience. Visit our website and look for **Tell Your Story** under the Participate tab.

Join our social networks

- facebook.com/cfpb
- twitter.com/cfpb

consumerfinance.gov

Know Your Rights: Credit Discrimination is Illegal

cfpb Consumer Financial Protection Bureau

cfpb Consumer Financial Protection Bureau

cfpb Consumer Financial Protection Bureau
Dedicated to making markets work for American consumers

⁷ Patrice Ficklin, Fair Notice on Fair Lending, Consumer Financial Protection Bureau (Apr. 18, 2012), available at <http://www.consumerfinance.gov/blog/fair-notice-on-fair-lending/>.

2.4 A Data-Driven Approach to Fair Lending – Collaboration with Research, Markets, and Regulations

The Division of Research, Markets, and Regulations brings together Ph.D. economists, financial industry experts, and experienced attorneys to lead the CFPB's efforts to articulate informed perspectives about current issues in consumer financial markets. Each of these offices plays an integral role in the CFPB's mission of ensuring equal access to credit.

The Office of Research includes dedicated fair lending research staff who conduct empirical fair lending analyses in connection with the CFPB's supervisory and enforcement activities, as well as special projects and initiatives. Together we have developed and continue to develop tools that allow the CFPB to identify areas of heightened fair lending risk and promote efficiency in our supervisory and enforcement efforts.



CFPB Director Richard Cordray and CFPB Deputy Director Raj Date take questions from the audience at the field hearing on payday lending in Birmingham, AL.

The various Markets offices are organized by product area and are charged with providing guidance on, and analysis of, specific consumer financial services markets. The offices also participate in the

development and analysis of consumer protection policy options in a variety of areas that are relevant to fair lending and access to credit matters. These areas are Mortgage and Home Equity Markets; Card and Payment Markets; Installment and Liquidity Lending Markets; and Deposits, Collections, and Credit Information Markets. Information on market trends relating to fair lending is then fed into other aspects of the CFPB's work in fair lending. For example, the Office of Fair Lending worked closely with the Office of Installment and Liquidity Lending Markets and the Office of Research this year to respond to Congress's request that the CFPB examine and report on a series of questions related to private education loans and private educational lenders. A detailed description of this study and our conclusion follows.

2.5 Dodd-Frank Act Report to Congress on Private Student Loans

On July 20, 2012, the CFPB and the Department of Education (DOE) submitted a report to Congress on Private Student Loans (PSL),⁸ responding to the Dodd-Frank Act's mandate that the agencies discuss:

- [T]he underwriting criteria used by private educational lenders, including the use of cohort default rate (as such term is defined in section 435(m) of the Higher Education Act of 1965);
- [W]hether Federal regulators and the public have access to information sufficient to provide them with assurances that private education loans are provided in accord with the Nation's fair lending laws and that allows public officials to determine lender compliance with fair lending laws; and
- [A]ny statutory or legislative recommendations necessary to improve consumer protections for private education loan borrowers and to better enable Federal

⁸ Consumer Financial Protection Bureau and the Department of Education, *Private Student Loans (2012)*, available at http://files.consumerfinance.gov/f/201207_cfpb_Reports_Private-Student-Loans.pdf.

regulators and the public to ascertain private educational lender compliance with fair lending laws.⁹

In addition to an in-depth discussion of the private student lending market, products, and consumers, the report also considered fair lending compliance in the PSL market. In particular, the report examined the eligibility, underwriting, and pricing criteria used by private educational lenders, with a specific focus on the use of cohort default rate.

2.5.1 COHORT DEFAULT RATE

Cohort default rate (CDR) is a measure of the federal student loan repayment history of a particular group or “cohort” of borrowers. The CDR is the percentage of each post-secondary school’s borrowers entering repayment on federal student loans in a particular two-year period who default prior to the end of that period.

CDR is one tool used for determining a school’s eligibility for federal student loan programs. The DOE removes a school’s eligibility for these programs when the institution’s three most recent CDRs are above 25%, or where the most recent CDR is greater than 40%. The DOE uses CDR as an eligibility cutoff at these relatively high levels because CDR is intended to be used as a broad measure to evaluate the risk to taxpayers of guaranteeing loans at a particular school. CDR was not specifically intended to assist private lenders in eligibility, underwriting, and pricing decisions,¹⁰ particularly at much lower levels of default (e.g., under 8%). However, CDR has been used by private student lenders as a proxy for a student’s likelihood of repaying debt.

2.5.2 USE OF CDR BY PRIVATE STUDENT LENDERS

The CFPB received information from nine of the largest private student lenders about how they use CDR and other institution-based criteria to determine a student’s eligibility¹¹ for their loan

⁹ See Dodd-Frank Act, § 1077.

¹⁰ See *Ass’n of Accredited Cosmetology v. Alexander*, 979 F.2d 859, 861 (D.C. Cir. 1992); see also S. Rep. No. 102–58 (1991).

¹¹ The term “eligibility” refers to whether a lender accepts applications from a particular postsecondary school’s students. In other words, if a lender set its eligibility cutoff at a CDR of 8%, then students from those schools with a

programs, as well as underwriting and pricing. We found that the primary use of CDR by the sample lenders is to set school eligibility cutoffs; in fact, a majority reported relying almost exclusively on CDR to set their school eligibility cutoffs,¹² with eligibility cutoffs between 6% and 12%.¹³ A few lenders also reported using CDR as part of, if not the primary consideration in, underwriting and pricing decisions; however, most reported using traditional, individually-applied criteria, such as minimum credit score, debt-to-income ratio, etc.

2.5.3 FAIR LENDING IMPLICATIONS OF CDR

The use of CDR at very low default levels is a fair lending concern because racial and ethnic minority students are disproportionately concentrated in schools with higher CDRs.¹⁴ For instance, we found that African American students attending public four-year institutions were almost four times more likely than students generally to attend schools with a CDR above 8%.

Hispanic students attending private four-year institutions were over seven times more likely than students generally to attend schools with a CDR above 8%.^{15,16} Accordingly, use of CDR to

rate at or below 8% would be eligible to be considered for a loan, whereas students from schools with a rate above 8% could not receive a loan, regardless of any particular student's creditworthiness (or that of his or her co-applicant).

¹² Most lenders who provided data also reported reliance on other nominal criteria such as requiring that a school be Title IV eligible, be located in the United States or Canada, and have had no sanctions imposed by the DOE related to financial, administrative, or loan performance reasons. Some lenders reported that they except Historically Black Colleges and Universities. Additionally, a few lenders reported setting eligibility cutoffs using CDR in conjunction with other factors such as internal portfolio performance, while others have phased out this particular use of CDR and replaced it with a school's graduation rate (which we note may raise similar fair lending concerns).

¹³ We note that some lenders had substantially more generous cutoffs.

¹⁴ To analyze the relationship between CDR and schools' racial and ethnic demographics we studied 2007, 2008, and 2009 Integrated Post-Secondary Educational System data on school characteristics and enrollment, including statistics on race and ethnicity, with the DOE's official CDRs from 2007, 2008, and 2009. Due to the two-year nature of the statistic, 2007, 2008, and 2009 are the three most recent CDR datasets available as of the writing of the CFPB's July report.

¹⁵ We carried out a regression analysis with CDR as the dependent variable and various racial and ethnic demographic categories as the explanatory variables. This analysis confirmed the results discussed above as it found that CDR was positively correlated with the percentage of minority students enrolled at postsecondary schools.

determine loan eligibility, underwriting, and pricing may have a disparate impact on minority students by reducing their access to credit and requiring those minority students who do meet the lenders' eligibility thresholds to pay higher rates than are otherwise available to similarly creditworthy non-Hispanic White students at schools with lower CDRs.

¹⁶ We tested the 8% cutoff because it is the most common CDR cutoff used by the lenders who provided data, not because it has any obvious intrinsic predictive value.

TABLE 1: AVERAGE RACIAL AND ETHNIC DEMOGRAPHICS ABOVE AND BELOW 8%, BY SCHOOL TYPE, 2008-2009 ACADEMIC YEAR

| | Demographic Distribution Below 8% | | | | | | |
|--|--|---------------|--------------|-----------------|--------------|------------------------|--------------|
| | Male | Female | White | Hispanic | Black | American Indian | Asian |
| | % | % | % | % | % | % | % |
| All | 44.0% | 56.0% | 60.5% | 9.3% | 10.0% | 0.8% | 6.6% |
| Public 4-Year | 45.5% | 54.5% | 63.9% | 8.7% | 8.3% | 0.8% | 7.2% |
| Private Not-for-Profit-4-Year | 42.6% | 57.4% | 60.6% | 6.5% | 8.8% | 0.6% | 6.0% |
| Private for-Profit-4-Year | 39.0% | 61.0% | 46.5% | 7.9% | 20.8% | 0.7% | 3.9% |
| Public 2-Year | 43.0% | 57.0% | 51.3% | 15.4% | 16.9% | 1.3% | 6.6% |
| Private Not-for-Profit-2-Year | 28.3% | 71.7% | 63.8% | 16.2% | 10.9% | 0.3% | 3.3% |
| Private for-Profit-2-Year | 37.6% | 62.4% | 47.3% | 23.9% | 15.0% | 0.9% | 4.1% |
| Public Less-than-2-Year | 44.8% | 55.2% | 44.0% | 33.3% | 11.7% | 4.3% | 4.3% |
| Private Not-for-Profit, Less-than-2-Year | 32.5% | 67.5% | 46.3% | 22.5% | 20.3% | 0.5% | 4.0% |
| Private for-Profit, Less-than-2-Year | 20.1% | 79.9% | 40.8% | 26.4% | 19.2% | 0.5% | 3.4% |

| | Demographic Distribution Above 8% | | | | | | |
|--|--|---------------|--------------|-----------------|--------------|------------------------|--------------|
| | Male | Female | White | Hispanic | Black | American Indian | Asian |
| | % | % | % | % | % | % | % |
| All | 41.2% | 58.8% | 49.4% | 17.0% | 16.7% | 1.0% | 4.7% |
| Public 4-Year | 40.8% | 59.2% | 46.6% | 17.7% | 25.1% | 1.4% | 2.7% |
| Private Not-for-Profit-4-Year | 39.9% | 60.1% | 33.9% | 33.2% | 23.9% | 0.7% | 1.2% |
| Private for-Profit-4-Year | 35.2% | 64.8% | 33.4% | 10.5% | 23.3% | 0.8% | 2.4% |
| Public 2-Year | 43.1% | 56.9% | 55.0% | 15.6% | 12.4% | 1.0% | 5.9% |
| Private Not-for-Profit-2-Year | 37.6% | 62.4% | 41.5% | 17.9% | 22.3% | 0.5% | 4.8% |
| Private for-Profit-2-Year | 36.1% | 63.9% | 37.7% | 20.8% | 24.2% | 0.8% | 3.2% |
| Public Less-than-2-Year | 35.7% | 64.3% | 70.8% | 5.1% | 19.8% | 1.0% | 1.0% |
| Private Not-for-Profit, Less-than-2-Year | 54.8% | 45.2% | 12.8% | 58.9% | 20.7% | 0.3% | 6.9% |
| Private for-Profit, Less-than-2-Year | 28.0% | 72.0% | 30.2% | 31.3% | 26.4% | 0.6% | 2.6% |

Source: IPEDS 2009 and PEPS. Data are reported for the 50 States, D.C., Puerto Rico, and the territories.

While we were mindful that our analysis used aggregate data – and we were therefore prevented from drawing conclusions about any specific lender’s practice – we were able to generally conclude that lenders’ consideration of CDR in either school eligibility or underwriting and pricing criteria may reduce credit access and increase costs disproportionately for minority borrowers. Accordingly, use of CDR may require further analysis by lenders to ensure compliance with fair lending laws.

Federal student loans are generally a better choice for consumers than PSL. However, the availability of such loans is statutorily limited and they do not cover the full cost of attendance at many schools. Accordingly, PSL can be an important consumer financial product and lenders that offer the product must do so in accordance with the nation’s fair lending laws.

The CFPB will continue to work with federal partners, industry, and consumer advocates to explore means through which fair lending risk in private student lending can be mitigated, given the unique underwriting challenges presented.

2.6 Amending Fair Lending Regulations

The Dodd-Frank Act transferred rulemaking authority under ECOA and HMDA to the CFPB.¹⁷ The CFPB published its restatements of ECOA’s implementing regulation, Regulation B, and HMDA’s implementing regulation, Regulation C, in interim final rules in December 2011.¹⁸

Section 1071 of the Dodd-Frank Act amended ECOA to require financial institutions to collect and report to the CFPB data on lending to small, minority-, and women-owned businesses in order to “facilitate the enforcement of fair lending laws and enable communities, governmental entities, and creditors to identify business and community development needs and opportunities of women-owned, minority-owned, and small businesses.”¹⁹ The Dodd-Frank Act also directed the CFPB to prescribe rules and guidance as necessary to carry out, enforce, and compile data pursuant to that

¹⁷ See Dodd-Frank Act, §§ 1002(12), (14), and 1022.

¹⁸ Equal Credit Opportunity (Regulation B), 76 Fed. Reg. 79,442 (Dec. 21, 2011) (codified at 12 C.F.R. pt. 1002); Home Mortgage Disclosure Act (Regulation C), 76 Fed. Reg. 78,465 (Dec. 19, 2012) (codified at 12 C.F.R. pt. 1003).

¹⁹ Dodd-Frank Act, § 1071(a).

section. In April 2011, the CFPB issued guidance stating that the data collection and submission obligations arising under these ECOA amendments do not arise until the CFPB issues implementing regulations.²⁰

The CFPB has begun the planning process to promulgate rules concerning small, minority-, and women-owned business loan data collection and reporting. We are currently gathering information from stakeholders to better understand the relevant business lending markets, and to determine what data are available and how best to collect those data. The CFPB has also been in dialogue with a number of interested governmental stakeholders about this issue, including the DOJ, the Department of Commerce, the Department of Treasury, the Small Business Administration, and the Board of Governors of the Federal Reserve System (FRB).

Section 1094 of the Dodd-Frank Act amends HMDA to require the collection and submission of additional data fields related to mortgage loans, including certain applicant, loan, and property characteristics, as well as “such other information as the Bureau may require.”²¹ The CFPB is examining what changes it may propose to Regulation C. As required under the Dodd-Frank Act, the CFPB will ensure the protection of mortgage applicants’ and mortgagors’ privacy interests in the disclosure of any additional data fields to the public under HMDA.²² A discussion of the prescribed amendments to Regulation C follows, in the HMDA Report section of this Report to Congress.

Finally, section 1403 of the Dodd-Frank Act requires that the CFPB prescribe regulations under TILA to prohibit “abusive or unfair lending practices that promote disparities among consumers of equal credit worthiness but of different race, ethnicity, gender or age.”²³ The CFPB has begun preliminary planning with regard to this rule.

²⁰ Letter from Leonard Kennedy, CFPB General Counsel, to Chief Executive Officers of Financial Institutions under Section 1071 of the Dodd-Frank Act (Apr. 11, 2011), *available at* <http://files.consumerfinance.gov/f/2011/04/GC-letter-re-1071.pdf>.

²¹ Dodd-Frank Act, § 1094(3).

²² *See* Dodd-Frank Act, § 1022(C)(8).

²³ Dodd-Frank Act, § 1403.

3. Reporting on the Equal Credit Opportunity Act and the Home Mortgage Disclosure Act

3.1 Reporting on the Equal Credit Opportunity Act

Prior to the passage of the Dodd-Frank Act, the FRB was required under ECOA to file an annual report to Congress describing the administration of its functions under ECOA, an assessment of the extent to which compliance with ECOA has been achieved, and a summary of enforcement actions taken by other agencies with responsibilities under ECOA. On the CFPB's designated transfer date of July 21, 2011, the FRB's responsibility for this report was transferred to the CFPB.²⁴ This part of the CFPB's Fair Lending Report will provide the information required by ECOA: first, it will describe the CFPB's and other agencies' enforcement efforts and assessment of the extent of compliance with ECOA; then, it will summarize the outreach efforts of the various agencies charged with responsibility under ECOA. This ECOA report will cover the period between July 21, 2011, and December 31, 2011; future reports will encompass an entire calendar year.

²⁴ See 15 U.S.C. § 1691f.

3.1.1 ECOA ENFORCEMENT

Several federal government agencies, including the CFPB, have administrative enforcement authority under ECOA. ECOA makes it illegal for a creditor to discriminate in any aspect of a credit transaction against any applicant on the basis of race, color, national origin, religion, sex, marital status, age (so long as the applicant is old enough to enter into a binding contract), receipt of income from any public assistance program, or exercising in good faith a right under the Consumer Credit Protection Act.

As discussed in Part II, the CFPB is committed to ensuring that the institutions under its jurisdiction comply with ECOA. The CFPB's efforts related to ECOA, as prescribed by the Dodd-Frank Act, and the enforcement efforts and compliance assessments made by all the agencies assigned enforcement authority under section 704 of ECOA²⁵ are discussed in this section.

3.1.2 PUBLIC ENFORCEMENT ACTIONS

In addition to the CFPB, the agencies charged with enforcement of ECOA under section 704 include: the FRB, the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the National Credit Union Administration (NCUA) (collectively the Federal Financial Institutions Examination Council agencies or FFIEC agencies);²⁶ the FTC, the Farm Credit Administration (FCA), the Department of Transportation (DOT), the Securities and Exchange Commission (SEC), the Small Business Administration (SBA), and the Grain Inspection, Packers and Stockyards Administration of the Department of Agriculture (GIPSA).²⁷ During the reporting period, from July 21, 2011 through December 31, 2011, the FDIC filed one public ECOA

²⁵ 15 U.S.C. § 1691c.

²⁶ The FFIEC is a "formal interagency body empowered to prescribe uniform principles, standards, and report forms for the federal examination of financial institutions" by the member agencies listed above and the State Liaison Committee "and to make recommendations to promote uniformity in the supervision of financial institutions." See <http://www.ffiec.gov/>.

²⁷ 15 U.S.C. § 1691c.

enforcement action.²⁸

3.1.3 VIOLATIONS CITED DURING ECOA EXAMINATIONS

Of the institutions examined, the FFIEC agencies reported that the most frequently cited Regulation B violations were:

TABLE 2: MOST FREQUENTLY CITED REGULATION B VIOLATIONS BY FFIEC AGENCIES

| FFIEC Agencies Reporting | Regulation B Violations |
|----------------------------|--|
| CFPB, FRB, FDIC, OCC, NCUA | <p>12 C.F.R. § 1002.4 – Discrimination on a prohibited basis in a credit transaction.</p> <p>12 C.F.R. § 1002.5(b) – Improperly requesting information about race, color, religion, national origin, or sex.</p> <p>12 C.F.R. § 1002.13(a) and (b) – Failure to collect information about applicants seeking credit primarily for the purchase or refinancing of a principal residence, including applicant race, ethnicity, sex, marital status, and age, for monitoring purposes.</p> <p>12 C.F.R. § 1002.9 (a)(2) and (b)(2) – Failure to provide sufficient information, including specific reasons for adverse action, in adverse action notification.</p> <p>12 C.F.R. § 1002.7(d)(1) – Improperly requiring a borrower to obtain the signature of a spouse or other person in order to be considered for credit approval.</p> |

²⁸ Because the authorities under the Dodd-Frank Act transferred to the CFPB on July 21, 2011, this report’s reporting period is July 21, 2011, through December 31, 2011. The FTC reported for the entire calendar year 2011 and reported a public enforcement action in April 2011. This action is not reported here because it is outside of the time period of this report. Similarly, the FRB reported that a referral made to the DOJ prior to the time period covered by this report, led to a public enforcement action by the DOJ in December 2011. For more information about that action, please see <http://www.justice.gov/opa/pr/2011/December/11-ag-1694.html>.

Of the remaining agencies, only the FCA conducted examinations and reported results. The Regulation B violations most frequently cited by the FCA were:

TABLE 3: MOST FREQUENTLY CITED REGULATION B VIOLATIONS BY OTHER ECOA AGENCIES

| Other ECOA Agencies | Regulation B Violations |
|---------------------|--|
| FCA | <p>12 C.F.R. § 1002.9 – Failure to provide timely adverse action notices, incomplete documentation to support the adverse action taken, or failing to give specific reasons for adverse actions taken.</p> <p>12 C.F.R. § 1002.13(b) – Failure to complete voluntary monitoring forms when borrower chose not to provide requested information regarding ethnicity, race, and sex.</p> |

The DOT, GIPSA, the SBA, and the SEC reported that they received no complaints based on ECOA or Regulation B. The FTC is an enforcement agency and does not conduct compliance examinations.

3.1.4 REFERRALS TO THE DEPARTMENT OF JUSTICE

Three FFIEC agencies referred a total of 12 matters to the DOJ during the reporting period. These matters alleged discriminatory treatment of persons in credit transactions due to race, national origin, age, or marital status.

3.1.5 INTERAGENCY OUTREACH RELATED TO ECOA

The FFIEC agencies all report substantial outreach and interagency activity aimed at ensuring creditors’ compliance with ECOA and Regulation B, and that fair lending laws are enforced in a consistent and fair manner.

The CFPB, along with the DOJ, HUD, the FRB, and the National Association of Attorneys General serves as co-chair of the Federal Financial Fraud Enforcement Task Force’s Non-Discrimination Working Group, with Assistant Director Ficklin representing the CFPB. The Financial Fraud Enforcement Task Force was established in November 2009 by an Executive Order to strengthen the efforts of the DOJ in conjunction with federal, state, and local agencies “to investigate and

prosecute significant crimes and other violations relating to the . . . financial crisis and economic recovery efforts, recover the proceeds of such financial crimes and violations, and ensure just and effective punishment of those who perpetuate financial crimes and violations.”²⁹ The Task Force brings together representatives from law enforcement agencies, regulatory authorities, inspectors general, and state attorneys general in order to combat financial fraud. This interaction fosters high level discussions among relevant stakeholders about policies, procedures, rulemakings, and other major initiatives. The Task Force’s Non-Discrimination Working Group in particular is dedicated to improving efforts to detect and eliminate discrimination in the lending and financial markets.

The FRB took a lead role in the Working Group’s effort to analyze data on the Department of Treasury’s Home Affordable Modification Program for evidence of potential discrimination by participating servicers. The Working Group sponsored a field hearing in San Francisco in the fall of 2011, providing outreach to local housing organizations, community groups, and financial institutions. In addition, on November 2, 2011, the FRB hosted an interagency webinar, *Fair Lending Issues and Hot Topics*, along with the CFPB, the OCC, the DOJ, HUD, the NCUA, and the FDIC. Over 6,000 registrants participated in the webinar, which included presentations on redlining, fair lending exams, maternity leave discrimination, broker compensation, and unsecured consumer loans.

The CFPB, HUD, the DOJ, the OCC, the FRB, the FDIC, the Federal Housing Finance Agency, the NCUA, and the FTC participate in the Federal Interagency Task Force on Fair Lending to discuss and coordinate fair lending activities. The Task Force meets bimonthly to share information and views on emerging fair lending issues.

The CFPB also belongs to a working group of federal agencies – with the DOJ, HUD, and the FTC – that regularly meets to discuss fair lending enforcement. These regular discussions are designed to ensure that enforcement efforts are well-coordinated. Additionally, the CFPB is part of the FFIEC Subcommittee on HMDA and the Community Reinvestment Act (CRA). The purpose of this subcommittee is to encourage the discussion of issues pertaining to the collection and processing of HMDA and CRA data, which financial institutions are legally obligated to report.

²⁹ Exec. Order No. 13519, 74 Fed. Reg. 60,123 (Nov. 17, 2009).

In addition, several FFIEC agencies participated in meetings, conferences, and trainings throughout the country. Outreach efforts included meetings with consumer advocates, civil rights groups, supervised institutions, and industry representatives. The CFPB's fair lending outreach is described in detail later in this Report.

3.2 Reporting on the Home Mortgage Disclosure Act

The CFPB's HMDA reporting requirement³⁰ calls for the CFPB, in consultation with HUD, to report annually on the utility of itemizing certain mortgage loan data.³¹ Like the reporting requirement under ECOA, the HMDA reporting requirement was transferred from the FRB to the CFPB pursuant to the Dodd-Frank Act. The CFPB's reporting on HMDA, made in consultation with HUD, is presented here.

Congress enacted HMDA in 1975 in response to Congressional findings indicating that some depository institutions had at times contributed to the decline of certain geographic areas by failing to provide adequate housing financing on reasonable terms and conditions. HMDA and its implementing regulation, Regulation C, require the collection and reporting of loan-level mortgage data by certain financial institutions, including banks, savings associations, credit unions, and other mortgage lending institutions. The data include, for example, the total number and dollar volume of mortgage applications and resulting mortgage loans and, for each application, the action taken by the creditor; the location of the property to be mortgaged; the race, ethnicity, and gender of each applicant; and the income relied on in the application.

Regulation C states three purposes of HMDA served by the collection and reporting of these data. First, these data help in determining whether financial institutions are serving the housing finance needs of their communities.³² These data are also relevant to reviewing certain institutions'

³⁰ See 12 U.S.C. § 2807.

³¹ 12 U.S.C. § 2803(b)(4).

³² 12 C.F.R. § 1003.1(b)(1)(i).

obligations under the CRA. Second, the data can be used to assist public officials in the distribution of public-sector investment, so as to attract private investment to areas that need it most.³³ Third, the mortgage loan data submitted under HMDA are used to assist in identifying possible discriminatory lending patterns and enforcing antidiscrimination statutes,³⁴ including ECOA and the Fair Housing Act.³⁵

The Dodd-Frank Act transferred HMDA rulemaking authority from the FRB to the CFPB³⁶ and expanded the scope of the data that must be collected and submitted under HMDA. Section 1094 of the Dodd-Frank Act amended HMDA to require HMDA-reporting entities to collect and report a number of new data elements, including elements related to additional loan, applicant, and property characteristics, as well as to allow the CFPB to require the collection and reporting of “such other information as the Bureau may require.”³⁷ At present, the CFPB’s efforts to implement these changes are in the pre-rule stage.

³³ 12 C.F.R. § 1003.1(b)(1)(ii).

³⁴ 12 C.F.R. § 1003.1(b)(1)(iii).

³⁵ 42 U.S.C. § 3601 *et seq.*

³⁶ See Dodd-Frank Act, §§ 1061 and 1094.

³⁷ Dodd-Frank Act, § 1094(3).

4. CFPB Outreach: Working with Private Industry, Fair Lending, Civil Rights, Consumer and Community Advocates

4.1 Private Industry Outreach

As one of its core functions, the Office of Fair Lending is responsible for “working with private industry . . . on the promotion of fair lending compliance and education.”³⁸ Consequently, the CFPB regularly engages with representatives from private industry – including financial services providers, fair lending compliance specialists, and regulatory attorneys – at conferences, meetings, colloquia, and roundtables throughout the country. The CFPB seeks to engage stakeholders with an interest in fair lending, with the understanding that there is much insight to be gained from varied perspectives that represent many distinct points of view. In this spirit, the CFPB frequently meets with private industry. These interactions have allowed the CFPB to learn about emerging fair lending and regulatory issues, convey the CFPB’s regulatory compliance expectations, and promote fair lending compliance and education pursuant to Congress’s direction.

³⁸ Dodd-Frank Act., § 1013(c)(2)(C).

Since July 2011, the CFPB has participated in numerous formal events with a fair lending focus; additional engagements with private industry are being planned. The CFPB has addressed trade associations, several leading industry law firms, executives from leading consulting compliance firms, and state banking associations as well as senior officials at banks and nonbanks subject to the CFPB's jurisdiction. In addition, Assistant Director Ficklin and senior fair lending staff regularly answer questions from industry counsel, bank representatives, and fair lending specialists about CFPB examinations, enforcement actions, and interagency coordination; similarly, staff attorneys in the Office of Regulations regularly answer questions from the same stakeholders about the correct interpretation of fair lending regulations and application to their business practices.

4.2 Outreach to Fair Lending, Civil Rights, Consumer and Community Advocates

As a civil rights-oriented office within the CFPB, the Office of Fair Lending works with “fair lending, civil rights, [and] consumer and community advocates” to promote fair lending compliance and education.³⁹ These engagements take place throughout the country in government offices, places of worship, community meeting spaces, at CFPB headquarters, and via teleconference or videoconference. Consumer advocates communicate directly with the CFPB, and the CFPB learns about emerging fair lending issues from these groups that have regular interactions with the consumers they serve.

³⁹ Dodd-Frank Act § 1013(c)(2)(C).



Office of Fair Lending and Equal Opportunity Assistant Director Patrice Alexander Ficklin, along with other members of the CFPB's leadership, speak at the National Community Reinvestment Coalition's annual conference.

During the past year, CFPB staff traveled throughout the country to meet with groups focused on fair lending issues; since July 2011, Fair Lending staff members participated in several dozen such events. The Office of Fair Lending regularly meets with civil rights organizations as well as consumer and community advocates.

In April 2012, which the CFPB recognized as Fair Housing and Fair Lending Month, Director Cordray delivered a keynote address announcing the CFPB's release of a Compliance Bulletin regarding fair lending, discussed in Part II. In support of this focus, the CFPB released an informative brochure and blog post that empower consumers to protect themselves from credit discrimination. This event exemplifies how the CFPB can raise awareness about fair lending education and compliance simultaneously. The Compliance Bulletin provides guidance to regulated entities and their affiliates in industry; the credit discrimination brochure and blog arm consumers with knowledge to navigate the consumer marketplace in a more secure manner.

In addition, senior CFPB leadership participated in periodic "Outside the Beltway" events at cities and communities across the country. These field hearings allow CFPB leadership to meet and

participate in roundtables and larger discussions with consumers, consumer advocates, community groups, civil rights groups, and industry representatives. As part of this outreach, Assistant Director Ficklin co-led a hearing panel at the payday lending field hearing held in January 2012 in Birmingham, Alabama.

All of these events provide the CFPB and the Office of Fair Lending with the opportunity to reach out in order to promote fair lending compliance and education, identify emerging issues and new risks, and champion fair and equal access to credit.

5. Fair Lending Look Ahead

In this inaugural Fair Lending Report, we have introduced some of the CFPB's collaborative work in fair lending, both within the CFPB's various divisions and offices and across federal and state agencies. We have also introduced the Office of Fair Lending and Equal Opportunity – its mission, staff, and work. The CFPB's work in the area of fair lending is a priority and has only just begun.

The CFPB will provide its Fair Lending Report annually. In future reports, we look forward to updating Congress about the CFPB's accomplishments in the areas of fair lending and equal access to credit. We will provide an update on the CFPB's work to supervise bank and nonbank financial services institutions and the CFPB's public fair lending enforcement actions, as well as activities and accomplishments across various offices to further the CFPB's fair lending mission. We will report on ECOA compliance as assessed by the agencies charged with enforcing that statute as well as fulfill the HMDA reporting requirement. Finally, we will describe our efforts to reach consumers and industry to promote fair lending compliance and education. In doing so, we will strive to fulfill Congress's mandate that the CFPB work to "ensure the fair, equitable, and nondiscriminatory access to credit for individuals and communities" across America.



CFPB Bulletin 2012-04 (Fair Lending)

Date: April 18, 2012

Subject: Lending Discrimination

In response to recent inquiries, the Consumer Financial Protection Bureau (“CFPB” or “Bureau”) issues this bulletin to provide guidance about compliance with the fair lending requirements of the Equal Credit Opportunity Act (“ECOA”),¹ and its implementing regulation, Regulation B.² The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act” or “Act”) granted CFPB authority to supervise and enforce compliance with the ECOA for entities within CFPB’s jurisdiction and to issue regulations and guidance to interpret the ECOA.³

The ECOA makes it illegal for a creditor to discriminate in any credit transaction against any applicant because of race, color, religion, national origin, sex, marital status, age (if the applicant is old enough to enter into a contract), receipt of income from any public assistance program; or the exercise in good faith of a right under the Consumer Credit Protection Act.⁴ As the legislative history of the ECOA emphasizes, “[t]he availability of credit often determines an individual’s effective range of social choice and influences such basic life matters as selection of occupation and housing.”⁵ Without nondiscriminatory access to credit, consumers face obstacles in obtaining equal access to housing.

In response to recent inquiries, the CFPB states that it will continue to adhere to the fair lending principles outlined in Regulation B. Consistent with other federal supervisory and law enforcement agencies, the CFPB reaffirms that the legal doctrine of disparate impact remains applicable as the Bureau exercises its supervision and enforcement authority to enforce compliance with the ECOA and Regulation B.

¹ 15 U.S.C. § 1691 *et seq.*

² 12 C.F.R. pt. 1002 *et seq.*

³ Sections 1022, 1024 -1026, 1053, 1054, 1061, and 1085 of the Dodd-Frank Act.

⁴ 15 U.S.C. § 1691(a)(1).

⁵ House Report that accompanied H.R. 6516, No. 94-210, p. 3.

In 1994, the Interagency Task Force on Fair Lending – which was composed of ten federal agencies, including the Department of Justice, each of the federal prudential agencies with regulatory authority over financial institutions, and the Federal Trade Commission – released the Policy Statement on Discrimination in Lending (“Policy Statement”).⁶ The Policy Statement notes that the courts have recognized the following methods of proving lending discrimination under the ECOA:

- Overt evidence of discrimination;
- Evidence of disparate treatment; and
- Evidence of disparate impact.

The CFPB, which did not yet exist at that time, concurs with the Policy Statement. In addition, the Bureau’s ECOA Examination Procedures, Mortgage Origination Examination Procedures, and Mortgage Servicing Examination Procedures also adopt and reference the Interagency Fair Lending Examination Procedures, including those designed to identify evidence of disparate impact.⁷

The applicability of disparate impact doctrine, also known as the “effects test,” to credit transactions is reflected in the legislative history of the ECOA. Regulation B, which the Federal Reserve Board adopted to implement the ECOA, provides that:

The legislative history of the Act indicates that the Congress intended an “effects test” concept, as outlined in the employment field by the Supreme Court in the cases of *Griggs v. Duke Power Co.*, 401 U.S. 424 (1971), and *Albemarle Paper Co. v. Moody*, 422 U.S. 405 (1975), to be applicable to a creditor’s determination of creditworthiness.⁸

⁶ Interagency Task Force on Fair Lending, *Policy Statement on Discrimination in Lending*, 59 Fed. Reg. 18,266 (Apr. 15, 1994) (online at www.occ.treas.gov/news-issuances/federal-register/94fr9214.pdf).

⁷ CFPB, *Supervision and Examination Manual* (Oct. 2011) (online at www.consumerfinance.gov/wp-content/themes/cfpb_theme/images/supervision_examination_manual_11211.pdf).

⁸ 12 C.F.R. § 1002.6.

The Commentary explicating Regulation B further elaborates:

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.⁹

In accordance with the foregoing authorities, as the CFPB exercises its supervisory and enforcement authority, it will consider evidence of the disparate impact doctrine as one method of proving lending discrimination under the ECOA and Regulation B.

⁹ 12 C.F.R. pt. 1002, Supp. I, § 1002.6, ¶ 6(a)-2.