



# Compliance Corner

FEDERAL RESERVE BANK OF PHILADELPHIA

Prepared for institutions supervised by the Consumer Compliance & CRA Unit

## It's A Commercial Loan: Reg B Doesn't Apply, Does It?

by Carletta M. Longo, Examiner

You bet it does! Regulation B, the *Equal Credit Opportunity Act* (ECOA), applies to every aspect of a credit transaction. There is no Regulation B exception for commercial loans, even though there are exceptions for commercial loans in other regulations, including Regulation Z, the *Truth in Lending Act*.

Regulation B prohibits discrimination in any aspect of a credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, or age (provided the applicant has the ability to enter into a contract); receipt of public assistance; or the fact that the applicant has exercised any right under the *Consumer Credit Protection Act*. The regulation applies to all individuals and institutions that regularly participate in decisions to grant credit.

In the First Quarter 2001 issue of *SRC Insights*, the article "Sign Here, Please!" reviewed the Regulation B signature requirements that are important to commercial lending. The purpose of this article to provide an understanding of how other aspects

of the regulation apply to commercial credit transactions.

What is "an aspect of a credit transaction"? An aspect of a credit transaction refers to the action or behavior of the creditor before, during, and after the credit evaluation process. Let's look at each period...

### Discouraging Applicants

Regulation B's reach begins even before the creditor takes an application. Lending personnel should be careful not to discourage anyone from applying for a loan. The prohibition against discouraging an applicant extends to written, oral, or telephone inquiries and applications. A creditor may not advertise in a manner that encourages certain persons and discourages others. Additionally, the selective use of newspapers, magazines, or radio or TV stations with a well-defined audience that would tend not to include, as a class, members of one or more of the protected categories of potential customers is also prohibited.

### Evaluation of Credit Applicants

Following the receipt of a credit application, the creditor must evaluate

## IN THIS ISSUE:

**It's A Commercial Loan:  
Reg B Doesn't Apply,  
Does It? .....CC1**

**Are You Ready  
for Privacy? .....CC3**

## CIRCULATE TO:

- Compliance Officer
- Compliance Manager
- Compliance Staff
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the applicant's creditworthiness. The regulation neither requires nor endorses any particular method of credit analysis. A creditor may use traditional methods that rely on a subjective evaluation of an applicant's creditworthiness, or may rely on an objective method such as credit scoring. Regardless of the method of credit analysis selected, it should be nondiscriminatory and should be applied uniformly and consistently without regard to any prohibited basis.

### Approval and Denial Process

Regulation B requires a creditor to notify the applicant of its decision within 30 days from receipt of a complete application. The regulation defines a complete application as one that contains all of the information necessary for the creditor to make a credit decision. If the application is **approved**, the creditor may notify the applicant by letter, telephone call, or by issuing the loan proceeds.

The notification requirements in §202.9(a)(3) provide some flexibility for commercial loan customers based on their annual gross revenues. For business loan requests that are **denied**, the creditor has the option to use the notification rules for consumer credit or to use the following rules specifically designed for business credit:

**Businesses with annual gross revenues of more than \$1 million.** The notice may be formal or informal, oral or written, and must be provided to the applicant within a reasonable period. Thirty days generally is considered reasonable. A written statement of the reasons for the denial is required only if the applicant makes a written request for such a statement within 60 days of receiving the denial notice.

**Businesses with annual gross revenues of less than \$1 million.** The creditor is required to follow the same procedure it uses to comply with consumer credit adverse action notifications, with the following exceptions:

- The creditor may make the notification orally or in writing. However, if the creditor chooses to provide the reasons for denial orally, then it must also disclose that the applicant has the right to have the reasons confirmed in writing.
- At the time the written business loan application is taken (rather than on a notice of adverse action), the creditor may advise the applicant in writing and in a form that the applicant may keep of their right to request a statement of reasons for denial. This notice must contain the following information:
  - The time periods within which the applicant must act;
  - The name, address, and telephone number of the lending personnel from whom the reasons for denial may be obtained; and
  - If the creditor provides the reasons orally, the applicant has the right to have the reasons confirmed in writing.
- For applications taken by telephone, a creditor satisfies the requirements by providing an oral statement of the reasons for adverse action and of the applicant's right to a statement of the reasons for adverse action.

### Signature Requirements

Regulation B prohibits a creditor from

requiring a signature other than the applicant's or joint applicant's if the applicant is qualified (i.e., creditworthy) based on the creditor's underwriting standards for the loan requested. A creditor may not routinely require the spouse of the applicant to sign any document that establishes a contractual obligation to repay the loan. If an applicant does not qualify for a loan based on a creditor's underwriting standards, the creditor may require a creditworthy co-signer, but the creditor may not require that person to be the applicant's spouse. A creditor may require signatures on documents that are used as security for a loan or that support the customer's creditworthiness, but Regulation B limits the creditor's ability to obtain signatures other than the applicant's to establish a contractual obligation to repay the debt.

For a more detailed discussion on the signature requirements of Regulation B, refer to "Sign Here, Please!" in the First Quarter 2001 issue of *SRC Insights*.

### Providing Appraisals

The regulation requires a creditor to provide the applicant with a copy of the appraisal report used in connection with an application for credit that is to be secured by a lien on a one-to-four family unit residential structure. The regulation provides two options to the creditor in delivering the appraisal to the applicant. The creditor may routinely provide a copy of the appraisal regardless of whether the credit was approved. Alternatively, the creditor may choose to provide a copy of the appraisal report only upon the applicant's written request. The creditor is required to notify an ap-

*continued on page CC4*

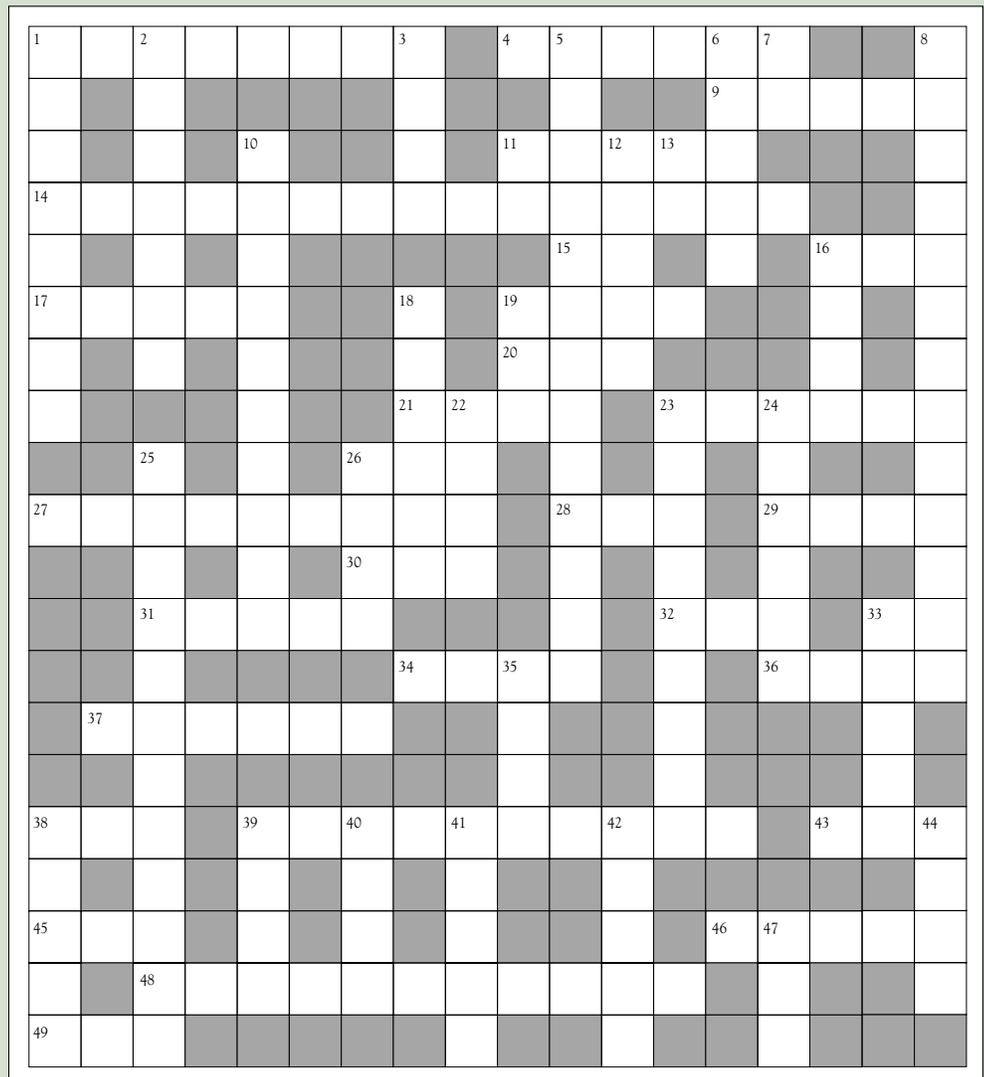
# Are You Ready for Privacy?

## ACROSS

- 1 A consumer who has a continuing relationship with a financial institution
- 4 Banks must provide this choice to all customers and consumers under the privacy rules (2 words)
- 9 Out of the office (2 words)
- 11 Jumped in headfirst
- 14 Third party covered by privacy rules
- 15 Preposition indicating location or presence
- 16 Souvenir from 18 Down
- 17 In an excited state
- 19 Identity theft might be a form of this
- 20 Organ for seeing
- 21 Saran \_\_\_\_\_
- 23 A married woman
- 26 Whom to call when the car breaks down
- 27 Information not generally available
- 28 Loan Application Register (abbr.)
- 29 Place where coins are made
- 30 Easy as \_\_\_\_\_
- 31 Ultimate consumers of a finished product
- 32 A guy's companion
- 33 Liquid measure (metric)
- 34 Out of the office
- 36 Ivy League school
- 37 The third name in privacy legislation
- 38 To and \_\_\_\_\_
- 39 Related parties
- 43 Adjustable Rate Mortgage (abbr.)
- 45 French friend
- 46 The first name in privacy legislation
- 48 With 33 Down, what a privacy notice must be
- 49 To color

## DOWN

- 1 An individual who obtains a financial product or service for personal or household use
- 2 Making information available
- 3 Short name for the privacy regulation (2 words)



- 5 Guidance governing a financial institution's treatment of nonpublic consumer and customer information
- 6 Opposite of over
- 7 Opposite of from
- 8 The first privacy disclosure provided to a consumer
- 10 Statement revealing something
- 11 To act
- 12 A brief biographical sketch
- 13 Name shared by Governors Kelley and Gramlich
- 16 Shakespeare's King \_\_\_\_\_
- 18 The 50th US State
- 19 A large body of salt water
- 22 Kind of competition
- 23 Holder of a mortgage
- 24 Promptly
- 25 Privacy disclosure sent yearly
- 26 Mountains in central Europe
- 33 With 48 Across, what a privacy notice must be
- 35 Against
- 38 Identity theft is a form of this
- 39 Abbr. for an unknown author
- 40 Action with a pancake
- 41 The second name in privacy legislation
- 42 Fresh water fish
- 44 A short note in the office
- 47 To hold up a bank

answers on page CC4

applicant in writing of the right to receive a copy of the appraisal report. The notice may be given to the applicant at any time during the credit evaluation process, but no later than the denial of the application.

### Record Retention Periods

The regulation requires the creditor to maintain evidence of compliance for business credit for a period of 12 months after the date of the notice of action taken.

### Collection and Recovery Process

A creditor may not use more onerous or more stringent collection or recovery practices or tactics on a prohibited basis. For example, a creditor could not impose more stringent collection techniques for members of one race or age group than for any other group of individuals.

### Conclusion

Violations of ECOA that result in discrimination are subject to referral to the Department of Justice. Certain violations of ECOA may also be violations of the *Fair Housing Act* and are subject to referral to the Department of Housing and Urban Development.

Violations of the *Equal Credit Opportunity Act* carry civil liability. ECOA allows an injured applicant to sue for punitive damages in addition to actual damages and attorney's fees. It also provides for class actions, with a limit on liability of the lesser of \$500,000 or 1 percent of the bank's net worth, plus attorney's fees.

To ensure compliance with Regulation B and avoid violations, management should initiate the following measures:

- Maintain an awareness of changes in consumer legislation and periodically review policies and procedures relative to Regulation B;
- Ensure that loan policies, procedures, forms, supporting documen-

tation, and underwriting practices are in compliance with the regulation;

- Periodically provide training to loan processors, lending staff, and other key personnel to ensure compliance with the regulation; and
- Ensure that loan documentation is maintained in accordance with the record retention requirements of the regulation.

If you have any questions about the applicability of Regulation B to commercial loans, contact Carletta M. Longo, Examiner, (carletta.longo@phil.frb.org) at (215) 574-3458; John D. Fields, Supervising Examiner, (john.d.fields@phil.frb.org) at (215) 574-6044; or Connie Wallgren, Manager, Consumer Compliance/CRA Examinations Unit, (connie.wallgren@phil.frb.org) at (215) 574-6217. ■



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