CFPB Request for Information on Regulation B

(Link to FRN)

I. Introduction

The staff of the Federal Trade Commission ("FTC" or "Commission")[1] appreciates the opportunity to provide information to the Consumer Financial Protection Bureau ("CFPB") regarding Regulation B, 12 C.F.R. §§ 202, 1002, the implementing regulation of the Equal Credit Opportunity Act ("ECOA"), 15 U.S.C. § 1691. ECOA and Regulation B make it unlawful to discriminate against applicants for credit on the basis of race, national origin, sex, marital status, age, or other prohibited factors.

The Commission has wide-ranging responsibilities regarding consumer financial issues, and has enforced ECOA's and Regulation B's provisions against auto dealers, subprime lenders, and non-mortgage creditors.[2] Recently, the FTC brought an action against an auto dealership and its manager alleging that the defendants violated ECOA and Regulation B by discriminating against African-American and Hispanic consumers who financed vehicle purchases.[3] According to the complaint, defendants charged higher markups for financing on a prohibited basis, approximately $163 and $211 more for African-American and Hispanic applicants, respectively. The order requires defendants to pay $1.5 million to settle these charges.

Our agencies have formed a valuable partnership in rooting out unlawful practices and coordinating to protect consumers, including against ECOA violations. The agencies recently filed a joint amicus brief stating that the term "applicant" in the Equal Credit Opportunity Act and Regulation B includes both those who are currently seeking credit and those who sought and have now received credit.[4] Through this type of advocacy work, our agencies have reminded market participants that ECOA applies broadly in prohibiting discrimination with respect to any aspect of a credit transaction, and not just, for example, to initial extensions of credit.

Below, we respond the CFPB's questions concerning disparate impact and small business lending.

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[1] This comment expresses the views of staff of the FTC's Bureau of Consumer Protection. It does not necessarily represent the views of the Federal Trade Commission or of any individual Commissioner. The Commission has, however, voted to authorize the submission of this comment.

[2] Pursuant to ECOA, a violation of ECOA is deemed to be a violation of the FTC Act. 15 U.S.C. § 1691c(c).

[3] *Federal Trade Commission v. Liberty Chevrolet, Inc*., et al., No. 20-3945 (S.D.N.Y. 2020).

[4] *See* Br. of Amici Curiae, *Tewinkle v. Capital One, N.A.*, No. 20-2049 (9th Cir. Oct. 7, 2020), *available at* https://www.ftc.gov/system/files/documents/amicus_briefs/bradley-tewinkle-v-capital-one-na/tewinkle_amicus_brief.pdf.

II. Disparate Impact

The first question in the CFPB's request for information concludes as follows: Should the Bureau provide additional clarity regarding its approach to disparate impact analysis under ECOA and/or Regulation B? If so, in what way(s)?

By way of background, when enacted in 1974, the ECOA prohibited discrimination on the basis of marital status and sex.[5] Two years later, when the Act was amended to add other prohibited bases of discrimination, Congress noted that courts and enforcement agencies were to analyze creditors' policies and practices for disparate impact, also known as the "effects test."[6]

Based on this legislative history, since 1977, Regulation B has explicitly incorporated disparate impact,[7] and the Commentary accompanying Regulation B explains that, "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."[8]

Courts have considered this framework in cases involving disparate impact, examining whether there is an outwardly neutral practice or policy that has caused a significantly adverse or disproportionate impact on applicants of a particular type.[9] Courts also have explained that, to defeat a claim of disparate impact, defendants must show a legitimate business need for the

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5 The Supreme Court has held that the same language in the Civil Rights Act, prohibiting sex discrimination, includes discrimination on the basis of homosexuality or transgender status. *Compare Bostock v. Clayton Cty., Georgia*, 140 S. Ct. 1731, 207 L. Ed. 2d 218 (2020) (holding that language in Title VII of the Civil Rights Act of 1964 barring an employer from "discriminat[ing] against any individual … because of such individual's … sex" also bars similar discrimination "for being homosexual or transgender") *with* 15 U.S.C. § 1691(a) (ECOA prohibition of "discriminat[ion] against any applicant … on the basis of … sex").

6 S. REP. 94-589, 1976 U.S.C.C.A.N. 403, p. 406; House Report that accompanied H.R. 6516, No. 94-210, p. 5.

7 12 C.F.R § 1002.6 ("[t]he legislative history of the Act indicates that the Congress intended an "effects test" concept"); *see also* 42 Fed. Reg. 1242, 1246 (Jan. 6, 1977) (amending Regulation B to explicitly incorporate the effects test, and stating that the rule "is not limited to intentional acts of discrimination," but rather "may be interpreted as prohibiting actions that have the effect of discriminating against applicants on a prohibited basis").

8 12 C.F.R. pt. 1002, Supp. I, § 1002.6, ¶ 6(a)-2.

9 *See, e.g., Adhvaryu v. Bank of Am., N.A.*, No. 18-1836, 2019 WL 6499211, at *5 (C.D. Cal. Aug. 1, 2019); *Duarte v. Quality Loan Serv. Corp.*, No. 217CV08014ODWPLA, 2018 WL 2121800, at *4 (C.D. Cal. May 8, 2018); *see also Hernandez v. Sutter W. Capital*, No. C 09-03658 CRB, 2010 WL 3385046, at *4 (N.D. Cal. Aug. 26, 2010) (denying motion to dismiss where complaint alleged neutral policies with discriminatory effects); *Miller v. Countrywide Bank, N.A.*, 571 F. Supp. 2d 251, 255 (D. Mass. 2008) (same).

policy that cannot be met with a less discriminatory alternative.[10] Using this framework, the FTC and other federal law enforcement agencies have brought multiple cases alleging discrimination, in a variety of different circumstances.[11] Articulating a single approach to disparate impact analysis that covers diverse sets of present and future facts and circumstances of discrimination may be difficult and could risk being both over and under inclusive. Therefore, if the CFPB provides additional detail, we urge it to include a reminder that such information is intended to provide examples of how the agency might approach a fair lending matter, that approaches may vary according to the facts and circumstances of each situation, and that such information is not intended to bless any violations of ECOA and Regulation B.

III. Small Business Lending

The CFPB's request for information also asks the following: In light of the Bureau's authority under ECOA/Regulation B, in what way(s) might it support efforts to meet the credit needs of small businesses, particularly those that are minority-owned and women-owned?

As part of its law enforcement efforts, the FTC has brought a number of cases involving small businesses; many recent actions involve deceptively advertised financing products and unfair billing and collection practices. For example, in *FTC v. Yellowstone Capital*, the FTC's complaint includes allegations that the financing company made false claims regarding collateral, personal guarantees, and financing amounts, and continued charging small business consumers after they had already paid what they owed.[12] In *FTC v. RCG Advances*, the FTC has alleged that the defendants marketed deceptive financing products to small businesses and unfairly used confessions of judgments, collection threats, and unauthorized withdrawals.[13] In *FTC v. Fleetcor Technologies*, the FTC has charged a company marketing fuel payment cards to small businesses with misrepresenting savings and fees, and employing deceptive and unfair billing practices.[14] Most recently, the FTC settled another law enforcement action against a company for allegedly falsely claiming an affiliation with the U.S. Small Business Administration (SBA) and marketing itself to small businesses as an approved lender under

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10 *See e.g., Ramirez v. GreenPoint Mortgage Funding, Inc.*, No. C08-0369-TEH, 2008 U.S. Dist. LEXIS 62810, at *7-*11 (N.D. Cal. May 13, 2008).

11 *See e.g., Federal Trade Commission v. Liberty Chevrolet, Inc*., et al., No. 20-3945 (S.D.N.Y. 2020); *United States v. American Honda Finance Corp.*, No. 15-05264 (C.D. Cal. 2015); *United States v. Ally Financial, Inc.*, *et al.*, No. 13-15180 (E.D. Mich. 2013); *United States v. GFI Mortgage Bankers, Inc.*, No. 12-2502 (S.D.N.Y. 2012).

12 *Federal Trade Commission v. Yellowstone Capital, LLC, et al*., No. 20-06023 (S.D.N.Y. Aug. 4, 2020).

13 *Federal Trade Commission v. RCG Advances, LLC*, *et al*. No. 20-04432 (S.D.N.Y. June 10, 2020).

14 *Federal Trade Commission v. Fleetcor Technologies, Inc., et al*., No. 19-05727 (N.D. Ga. Dec. 20, 2019).

SBA's Paycheck Protection Program.[15] In addition to these law enforcement actions, the FTC along with the SBA sent eight warning letters to companies potentially misleading small businesses seeking SBA loans as a result of the coronavirus pandemic.[16]

While the FTC has been able to bring many actions protecting small businesses, detecting illegal conduct in this space can be challenging. Small business consumers do not always report illegal conduct to law enforcement agencies, perhaps due to uncertainty over their rights and recourse when something goes wrong. For example, after entering into a transaction with a financing company, the small business consumer may later learn that the company does not view its product as a credit product, and thus the consumer cannot be assured that protections under credit statutes are available.

This is a particular concern with Merchant Cash Advances ("MCAs"). In exchange for a lump sum cash infusion, small businesses typically agree to repay the MCA provider a larger (often 50% more), fixed sum via daily installment payments over a period of several months. MCA providers have taken the position that they are not offering credit because their contracts often state that daily repayment amounts will fluctuate according to the businesses' fluctuating daily revenues, and that there is no obligation to repay if the business fails.[17] If in practice, however, MCA companies are seeking repayment regardless of contract terms, small business consumers are entering into credit arrangements without the certainty that the protections offered under credit statutes would apply as they would if the consumer obtained credit elsewhere. Indeed, many MCA arrangements come with other hallmarks of traditional credit, including personal guarantees of payment, and the FTC has sued one MCA provider for allegedly engaging in collection measures such as confessions of judgment against small business consumers regardless of whether the business has failed, and regardless of the limitations the provider's contract claims to have placed on such measures.[18]

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15 *Federal Trade Commission v. Ponte Investments, LLC, et al*., No. 20-cv-00177 (D. RI Aug. 17, 2020).

16 *See* FTC Press Release, *FTC and SBA Warn Six Companies to Stop Potentially Misleading Marketing Aimed at Small Businesses Seeking Coronavirus Relief Loans* (June 24, 2020), https://www ftc.gov/news-events/press-releases/2020/06/ftc-sba-warn-six-companies-stop-potentially-misleading-marketing; FTC Press Release, *FTC and SBA Warn Operator of SBA.com and Lead Generator Lendio to Stop Potentially Misleading Coronavirus Relief Loan Marketing* (May 18, 2020), https://www ftc.gov/news-events/press-releases/2020/05/ftc-sba-warn-operator-sbacom-lead-generator-lendio-stop?utm_source=govdelivery.

17 "Strictly Business" Forum, Staff Perspective 6 (Feb. 2020), *available at* https://www.ftc.gov/system/files/documents/reports/staff-perspective-paper-ftcs-strictly-business-forum/strictly_business_forum_staff_perspective.pdf; Transcript at 40, Strictly Business: An FTC Forum on Small Business Financing (May 8, 2019), *available at* https://www ftc.gov/system/files/documents/videos/strictly-business-ftc-forum-small-business-financing/ftc_strictly_business_forum_on_small_business_ financing_transcript_5-8-19.pdf.

18 *Federal Trade Commission v. RCG Advances, LLC, et al.*, No. 20-4432 (S.D.N.Y. June 10, 2020).

Therefore, the FTC urges the CFPB to remind entities offering credit to small businesses that credit statutes such as ECOA and Regulation B apply, and that whether a particular statute applies depends on the actual facts and circumstances involved, and not solely on how one party characterizes the transaction or the benefits it claims to provide.[19] The CFPB's rulemaking under Dodd-Frank to require financial institutions to collect demographic data in connection with small-business lending also will aid in enforcement efforts.[20] Encouraging small businesses to complain about misconduct, and referring complaints to the FTC and states, also would aid in enforcement. Additionally, educating small business consumers about different products and terms, and potential law violations—as the FTC has done[21]—could assist small businesses in comparing products, lead them to look for and obtain less expensive financing, and encourage them to report misconduct to aid in law enforcement.

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We appreciate the opportunity to provide this information, and look forward to continued collaboration on fair lending issues.

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[19] For example, while some entities have claimed they are exempt from FTC jurisdiction by virtue of their nonprofit status, courts routinely have looked beyond the label and examined whether the company is in fact operating for the profit its members. *See, e.g., Community Blood Bank of the Kansas City Area, Inc. v. FTC*, 405 F.2d 1011, 1019 (8th Cir. 1969) ("mere form of incorporation does not put them outside the jurisdiction of the Commission"); *FTC v. Ameridebt, Inc*., 343 F. Supp. 2d 451, 460 (D. Md. 2004) ("Although Ameridebt is incorporated as a non-stock corporation with tax-exempt status, the Court finds this insufficient to insulate it from the regulatory coverage of the FTC Act."); *see also, e.g., In re Daniel Chapter One*, 2009 WL 5160000 at *12 (F.T.C. 2009) ("As recognized by the ALJ, however, 'courts and the Commission look to the substance, rather than the form, of incorporation in determining jurisdiction under the FTC Act.'"), *aff'd*, 405 Fed. Appx. 505 (D.C. Cir. 2010).

[20] *See* Small Business Advisory Review Panel for Consumer Financial Protection Bureau, Small Business Lending Data Collection Rulemaking, Outline of Proposals Under Consideration and Alternatives Considered (Sept. 15, 2020), https://files.consumerfinance.gov/f/documents/cfpb_1071-sbrefa_outline-of-proposals-under-consideration_2020-09.pdf.

[21] *See, e.g.*, Andrew Smith, Protecting Small Businesses Seeking Financing During the Pandemic (Aug. 3, 2020), https://www.ftc.gov/news-events/blogs/business-blog/2020/08/protecting-small-businesses-seeking-financing-during; Lesley Fair, Looking for Small Business Financing? Read This First (June 10, 2020), https://www.ftc.gov/news-events/blogs/business-blog/2020/06/looking-small-business-financing-read-first; Lesley Fair, Small Business Financing: Considerations for Borrowers and Lenders During the Coronavirus Crisis (Apr. 15, 2020), https://www ftc.gov/news-events/blogs/business-blog/2020/04/small-business-financing-considerations-borrowers-lenders; FTC Press Release, *FTC Staff Perspective Recaps Small Business Financing Forum* (Feb. 26, 2020), https://www ftc.gov/news-events/press-releases/2020/02/ftc-staff-perspective-recaps-small-business-financing-forum.