ICBA
Independent Community Bankers *of* America®

Via Electronic Submission

December 1, 2020

Comment Intake
Bureau of Consumer Financial Protection
1700 G Street, NW
Washington, DC 20552

Re: Request for Information on the Equal Credit Opportunity Act and Regulation B [Docket No. CFPB-2020-0026]

Dear Director Kraninger,

The Independent Community Bankers of America ("ICBA")[1] appreciates this opportunity to provide feedback to the Consumer Financial Protection Bureau's ("CFPB") Request for Information ("RFI") on the Equal Credit Opportunity Act ("ECOA") and Regulation B.[2] ECOA was passed by Congress in 1974 in order to prohibit discrimination with respect to any aspect of a credit transaction. Community banks are committed to eliminating illegal discrimination in lending and to ensuring that the credit needs of their communities are met on fair terms, regardless of an applicant's race, color, religion, national origin, sex, marital status, or age.

The RFI, promulgated pursuant to the CFPB's authority to "engage in . . . requests for information, [which] includes matters relating to fair lending,"[3] "seeks comments on the actions it can take or should consider taking to prevent credit discrimination, encourage responsible innovation, promote fair, equitable, and nondiscriminatory access to credit, address potential regulatory uncertainty, and develop viable solutions to regulatory compliance challenges under ECOA and Regulation B."[4]

ICBA commends the willingness of the CFPB to engage in a constructive dialogue with stakeholders to ensure that Reg B is appropriately tailored to the modern lending market. The fundamental purpose of ECOA and Reg B is to ensure that all loan applicants, regardless of their

[1]The Independent Community Bankers of America® creates and promotes an environment where community banks flourish. With more than 50,000 locations nationwide, community banks constitute 99 percent of all banks, employ nearly 750,000 Americans and are the only physical banking presence in one in three U.S. counties. Holding more than $5 trillion in assets, nearly $4 trillion in deposits, and more than $3.4 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America.
[2] 85 Fed. Reg. 46600, (available at: https://www.federalregister.gov/documents/2020/08/03/2020-16722/request-for-information-on-the-equal-credit-opportunity-act-and-regulation-b).
[3] 12 U.S.C. 5562(a)(2).
[4] 85 Fed. Reg. 46601.

membership in any protected class, have fair and equitable access to credit. In this comment letter, ICBA will respond to the questions posed in the RFI with feedback designed to help the Bureau ensure that ECOA remains an effective tool that loan applicants who have been illegally discriminated against can use to enforce their civil rights, while not unfairly burdening lenders or inadvertently reducing access to credit in disadvantaged communities.

Disparate Impact

ICBA and community bankers across the nation abhor illegal discrimination and support all efforts to combat illegal discrimination. Community banks strive to ensure that all banking needs, including lending, are met for the customers they serve. ICBA strongly supports the prohibition against illegal discrimination under the ECOA. However, the Bureau's current application of disparate impact liability under ECOA has particularly deleterious effects on community bank consumer lending because of the inconsistent frameworks between Reg B and the U.S. Supreme Court's ruling in *Texas Department of Housing & Community Affairs v. The Inclusive Communities Project, Inc* ("*Inclusive Communities*").[5]

Since the enactment of the Dodd Frank Wall Street Reform and Consumer Protection Act, the CFPB has been responsible for implementing ECOA through Regulation B ("Reg B").[6] The statute makes it unlawful for "any creditor to discriminate against any applicant with respect to any aspect of a credit transaction (1) on the basis of race, color, religion, national origin, sex or marital status, or age (provided the applicant has the capacity to contract); (2) because all or part of the applicant's income derives from any public assistance program; or (3) because the applicant has in good faith exercised any right under the Consumer Credit Protection Act."[7]

Under ECOA, there have traditionally been two primary theories of liability: disparate treatment and disparate impact. According to a summary published by the CFPB, "[d]isparate treatment occurs when a creditor treats an applicant differently based on a prohibited basis such as race or national origin. Disparate impact occurs when a creditor employs facially neutral policies or practices that have an adverse effect or impact on a member of a protected class unless it meets a legitimate business need that cannot reasonably be achieved by means that are less disparate in their impact."[8]

In practice, the disparate impact framework functions as a burden-shifting regime in litigation. If the charging party establishes a prima facie case (for example, by providing statistical evidence of a disparate impact on a protected class), the burden of proof shifts to the defendant, or lender, to prove that the challenged practice is necessary to achieve on a legitimate business need. If the defendant satisfies this burden, the charging party may still establish liability by proving that the business need could reasonably be met by a practice that has a less discriminatory effect.

---

[5] 135 S. Ct. 2507 (2015).
[6] *See* 12 C.F.R. Part 1002.
[7] 15 U.S.C. 1691.
[8] CFPB, "Consumer Laws and Regulations: ECOA" (June 2013) at 1, available at: https://files.consumerfinance.gov/f/201306_cfpb_laws-and-regulations_ecoa-combined-june-2013.pdf.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

In light of the United States Supreme Court's recent decision in *Inclusive Communities* – which established a standard for proving disparate impact claims in the context of the Fair Housing Act ("FHA") – the CFPB should revise its own disparate impact rule under Reg B to make it consistent with current Supreme Court jurisprudence and the Department of Housing and Urban Development's ("HUD") regulations implementing the FHA.[9]

The Disparate Impact Standard

Disparate impact liability, defined in Reg B as "an 'effects test' concept, as outlined in the employment field by the U.S. 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)"[10] does not require a facially discriminatory policy or a discriminatory intent. The doctrine, which originally emerged in the context of employment discrimination, focuses on identifying discriminatory effects of facially neutral policies or practices.

Since its creation in the 1970s, the application of disparate impact liability has moved far beyond its original, limited scope. As Reg B indicates, the CFPB, HUD, and other federal agencies have applied disparate impact liability to prevent discrimination in lending. In 2015, the U.S. Supreme Court upheld the application of disparate impact under the FHA in its ruling in *Inclusive Communities*; however, the Court significantly narrowed its scope to cases where direct causality can be conclusively shown.

In *Inclusive Communities*, the Court imposed a robust causality requirement and held that a "disparate-impact claim relying on a statistical disparity must fail if the plaintiff cannot point to a defendant's policy or policies causing that disparity."[11] The Court also established a burden-shifting framework for courts and the government adjudicating disparate impact claims. Specifically, the Supreme Court required that a charging party or plaintiff bringing a disparate impact claim must first demonstrate a causal connection between the challenged practice or policy and the statistical disparity affecting a protected class.

This robust causality requirement was designed to prevent defendants from being held liable for racial disparities that their policies and practices did not create. Likewise, the Court reiterated that a plaintiff who fails to allege facts at the pleading stage or produce statistical evidence demonstrating a causal connection cannot make out a prima facie case of disparate impact.

The Court was clear that "[w]ithout adequate safeguards at the prima facie stage, disparate impact liability might cause race to be used and considered in a pervasive way and 'would almost inexorably lead' governmental or private entities to use 'numerical quotas,' and serious constitutional questions then could arise."[12] The Court also cautioned that "limitations on disparate-impact liability … are also necessary to protect potential defendants against abusive disparate-impact claims. If the specter of disparate-impact litigation causes private developers to

[9] 24 C.F.R. Part 100; 85 Fed. Reg. 60288.
[10] 12 C.F.R. Pt. 1002.6(a).
[11] *Texas Dept. of Housing & Community Affairs v. The Inclusive Communities Project, Inc*, 135 S.Ct. 2507 at 2524, (2015).
[12] *Id.* at 2523.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

no longer construct or renovate housing units for low-income individuals, then the FHA would have undermined its own purpose as well as the free-market system."[13]

While *Inclusive Communities* was a Fair Housing Act case, and did not specifically address liability under ECOA, there are important commonalities between the two laws. Therefore, ICBA urges the CFPB to update its disparate impact standard in Reg B in order to ensure that it is consistent the *Inclusive Communities* decision and FHA's implementing regulations.

The CFPB Lacks the Statutory Authority to Infer Disparate Impact Liability from the Text of ECOA

In *Inclusive Communities*, the Court looked to the text of the FHA and determined that disparate impact claims were cognizable. It held, "Title VII's and the ["Age Discrimination in Employment Act"] ADEA's 'otherwise adversely affect' language is equivalent in function and purpose to the FHA's 'otherwise make unavailable' language. In these three statutes the operative text looks to results. The relevant statutory phrases, moreover, play an identical role in the structure common to all three statutes: Located at the end of lengthy sentences that begin with prohibitions on disparate treatment, they serve as catchall phrases looking to consequences, not intent. All three statutes use the word 'otherwise' to introduce the results-oriented phrase."[14]

ECOA, by contrast, does not include an equivalent catch-all phrase and is not a "results oriented" statute. The prohibition in ECOA reads, "It shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction … on the basis of race, color, religion, national origin, sex or marital status, or age…"[15] This language clearly prohibits overt discriminatory conduct (i.e. disparate treatment), but, in stark contrast to Title VII or the ADEA, it does not include an "otherwise adversely affect" clause that would trigger a disparate impact analysis.

Therefore, while ICBA and community banks abhor illegal discrimination, it is important to ensure that laws are not interpreted beyond the scope intended by Congress. Reading disparate impact liability into a statute that was not designed to include it may have a chilling effect on the ability of lenders to serve underserved populations, frustrating the intent of Congress. Disparate impact liability is not expressly contemplated by Congress in the text of ECOA and the statute lacks the key triggering phrase that allows for results analysis in the context of Title VII, ADEA, and FHA claims. For this reason, we believe it is beyond the scope of the CFPB's statutory authority to extend disparate impact liability to ECOA.

[13] *Id.* at 2524.
[14] 135 S. Ct. 2507, 2519.
[15] 12 U.S.C. 1619(a)

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

<u>If the CFPB Determines that Disparate Impact Liability is Permissible Under ECOA, the Bureau Should Conduct a Cost-Benefit Analysis Before Making a Determination</u>

Disparate impact liability, in the first instance, was not created by Congress. Instead, it was a tool developed by the Equal Employment Opportunity Commission in the 1970s to combat institutionalized discrimination. Most civil rights legislation prohibited overt acts of discrimination flowing from an evil state of mind, but there was still discrimination that stemmed from unconscious biases and the structure of institutions.

Before the CFPB interprets ECOA to create disparate impact liability, it is appropriate to conduct a formal assessment of the prevalence of institutionalized discrimination in lending in order to determine if the benefits of imposing disparate impact liability exceed the costs. It may be the case that unconscious racial biases present at the institutional level could be corrected with a less costly tool than disparate impact liability.

<u>If the CFPB Interprets ECOA to Include Disparate Impact Liability, the Bureau's Standard Must Be In-Line with the Supreme Court's Decision in Inclusive Communities</u>

To ensure that its disparate impact standard is in-line with the requirements created by the Supreme Court, the Bureau must include a robust causality requirement. Because abusive and frivolous disparate impact claims may have a chilling effect on lenders' willingness to extend credit, an overly permissive disparate impact rule frustrates the purpose of ECOA by reducing access to credit.

A robust causality standard would require plaintiffs to prove a direct connection between a challenged policy or practice and the discriminatory effect at the prima facie stage of litigation. This would allow plaintiffs to obtain a remedy in well-plead, meritorious cases without unfairly placing the burden on lenders to prove that their neutral policies lead to the smallest possible disparate impact.

To heed the Supreme Court's decision that there must be "adequate safeguards at the prima facie stage," the CFPB should create a comprehensive prima facie case that must be plead to prove an ECOA claim. If the CFPB interprets ECOA to include a disparate impact standard, the pleading standard should be consistent with existing disparate impact standard and require plaintiffs to prove causality and materiality, in accordance with the Supreme Court's decision and the FHA's implementing regulation. This will prevent meritless and frivolous lawsuits from advancing past the pleading stage and consuming valuable resources that could be used to increase access to credit. Any standard adopted by the CFPB should reflect that bare statistical evidence is insufficient to prove a disparate impact claim without proving a direct causal link between that discriminatory effect and a challenged policy or practice.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

Punitive Damages in Disparate Impact Cases

Punitive damages are designed to punish defendants for outrageous conduct and to deter future bad acts. As such, they are reserved for cases where the defendant's actions are truly reprehensible and demonstrate a disregard for the rights of others. By definition, disparate impact claims do not rise to this level because they deal with facially neutral policies or practices and do not require intent. A neutral policy does not demonstrate disregard for the rights of others, even if it creates a discriminatory effect. In general, the purpose of a meritorious disparate impact claim should be to correct the policy to remove the discriminatory effect and to provide compensatory damages, not to punish defendants for unintentional violations.

While ECOA does permit punitive damages as a remedy, ICBA urges the CFPB to adopt a rule that limits this remedy to the most egregious cases, whether based on disparate treatment or disparate impact.[16] For example, Title VII of the Civil Rights Act of 1964 limits the application of punitive damages to cases where "the complaining party demonstrates that the respondent engaged in a discriminatory practice or discriminatory practices with malice or with reckless indifference to the federally protected rights of aggrieved individual."[17]

A similar "malice or reckless indifference" standard for punitive damages in ECOA cases would be appropriate. Such a standard would limit punitive damages to their proper role of deterring and punishing willful or egregious conduct. Punitive damages should not be applicable in cases of inadvertent and unintended discrimination

Small Business Lending

Small businesses are a key driver of economic growth, job creation, and, especially in traditionally underserved and disadvantaged communities, an engine of wealth creation and financial independence. Community banks play a central role in small business lending, accounting for over 60% of small business loans nationwide. Furthermore, according to the Federal Reserve, small businesses that borrow from small banks report a 79% satisfaction rate with the process, compared to a 67% satisfaction rate with large banks and just a 49% satisfaction rate with online lenders.[18]

Community banks are founded on the principal of relationship banking. Because community banks are based in the communities where they operate, they know their customers and their financial circumstances on an individual basis. For small businesses, this relationship-based approach is essential, because community banks can serve not just as lenders, but as informal financial advisers, helping the business structure their loans in a way that makes financial sense. Furthermore, small banks are not constrained by the rigid processes of larger banks and can make lending decisions based on qualitative factors like the viability of the borrower's business plan, rather than basing decisions on impersonal, quantitative factors like credit score.

---

[16] *See 15 U.S.C. 1691e.*

[17] 42 U.S.C. 1981a(b)(1).

[18] Federal Reserve Banks, "Small Business Credit Survey," 2019 Report on Employer Firms, p. 21 (2019), available at: https://www.fedsmallbusiness.org/medialibrary/fedsmallbusiness/files/2019/sbcs-employer-firms-report.pdf.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

A perfect illustration of the commitment of community banks to small businesses is their outsized contribution to the success of the Paycheck Protection Program ("PPP"). Despite the rapid rollout and complexity of the program, community banks were able to make over 2.8 million PPP loans – which amounts to 57.5% of all loans originated under that program. As impressively, community banks originated 72.6% of PPP loans made to non-white small business owners, and 71.5% of PPP loans made to female small business owners.[19]

While all community banks work with minorities and the underserved in their communities, this commitment is core to the mission of Community Development Financial Institutions (CDFIs) and Minority Depository Institutions (MDIs), the majority of which are also community banks. Minority bank shareholders, directors, officers and staff know and understand the culture and language of the communities they serve, allowing them to customize culturally sensitive products and services. Women-owned and minority-owned small businesses often turn to CDFIs and MDIs for funding and the CFPB should not create regulations that impair these important relationships.

Section 1071 of the Dodd Frank Act amended ECOA to require the CFPB to conduct small business loan data collection.[20] The purpose of this section was "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."[21] To meet this end, Section 1071 requires the CFPB to require financial institutions to gather and record whether the recipients of business loans are minority-owned, women-owned, or small business.

From October 19 through 22, 2020 the CFPB held a legally required Small Business Regulatory Enforcement Fairness Act (SBREFA) Panel regarding its Section 1071 rulemaking, in which community banks participated as Small Entity Representatives. ICBA wishes to thank the Bureau for conducting the process in an extremely well-organized way and for allowing meaningful stakeholder participation. ICBA will provide more detailed comments on Section 1071 in a subsequent letter related to the SBREFA Panel, but we urge the Bureau to take seriously the burden that Section 1071 may impose on small institutions. We look forward to continuing to provide feedback to the Bureau and to ensure that the final regulation does not create undue costs that inhibit lending to small businesses.

---

[19] *See* Noah Yosif, "When the Going Gets Tough, the Tough Get Lending," ICBA Mainstreet Matters Blog (Jul 22, 2020), available at: https://www.icba.org/news/blog-details/main-street-matters---advocacy/2020/07/22/when-the-going-gets-tough-the-tough-get-lending?utm_campaign=MainStreetMattersBlog&utm_content=135338650&utm_medium=social&utm_source=twitter&hss_channel=tw-155954102

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

Artificial Intelligence and Machine Learning:

The CFPB is seeking comment on how lenders using complex artificial intelligence ("AI") or machine learning ("ML") models satisfy ECOA's adverse action notice requirements. ECOA requires creditors to provide consumers with the principal reason(s) for a denial of credit or other adverse action.

Community banks are becoming increasingly interested in using AI and ML to augment their more traditional underwriting models. These technologies hold tremendous promise because, by examining non-intuitive relationships between data points, they are able to identify creditworthy borrowers that traditional underwriting might overlook. This is a true win-win situation because it enables lenders to expand access to credit for borrowers who previously might not have qualified for a bank loan.

Despite this potential, the non-intuitive nature of AI also presents significant compliance challenges. Specifically, Reg B requires a notification to be sent when an adverse action on a credit application is taken. The notification includes "[a] disclosure of the applicant's right to a statement of specific reasons [that the adverse action was taken.]"[22] When using conventional underwriting methods, it is possible to determine which aspects of a customer's application led to their application being rejected. However, AI may examine relationships between data in ways that are more difficult to explain.

The CFPB is seeking comment on whether it should modify requirements or guidance concerning notifications of action taken, including adverse action notices, under ECOA and/or Regulation B to better empower consumers to make more informed financial decisions and/or to provide additional clarity when credit underwriting decisions are based in part on models that use AI/ML.

ICBA believes the Bureau's existing guidance provides an adequate solution. CFPB states:

> The existing regulatory framework has built-in flexibility that can be compatible with AI algorithms. For example, although a creditor must provide the specific reasons for an adverse action, the Official Interpretation to ECOA's implementing regulation, Regulation B, provides that a creditor need not describe how or why a disclosed factor adversely affected an application, or, for credit scoring systems, how the factor relates to creditworthiness. Thus, the Official Interpretation provides an example that a creditor may disclose a reason for a denial, even if the relationship of that disclosed factor to predicting creditworthiness may be unclear to the applicant. This flexibility may be useful to creditors when issuing adverse action notices based on AI models where the variables and key reasons are known, but which may rely upon non-intuitive relationships.[23]

[22] 12 CFR 1002.9(a)(2).

[23] Consumer Financial Protection Bureau, "Fair Lending Report of the Bureau of Consumer Financial Protection" (April, 2020), available at: https://files.consumerfinance.gov/f/documents/cfpb_2019-fair-lending_report.pdf.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

Of greater concern is the potential for fair lending violations under the disparate impact theory. Disparate impact does not require a finding of intent to discriminate, only the finding that a bank's policies or practices created a discriminatory effect. Therefore, even a totally race-blind AI that is not given any data about applicants' race, sex, or national origin may result in a potential fair lending violation if the effects of loan approvals create a disparate impact.

It is our view that the best way to realize the potential of AI in lending is to provide a safe harbor from disparate impact claims for algorithms that do not consider race as a variable and are created for the purpose of minimizing predictive error. An artificial intelligence set to minimize predictive error will result in the greatest improvement to access to credit, because it will find the greatest number of truly creditworthy applicants that previous underwriting models would have missed. The difficulty such AI models may encounter under the current standard is that, if the loans they make are evaluated on a percentage basis, they may still appear to create a disparate impact. However, if evaluated on an absolute basis, they would actually make a greater number of loans to creditworthy borrowers that are members of a protected class than traditional underwriting. These gains are possible because AI will drive down underwriting costs and evaluate data in novel ways.

More analysis of the use of AI in lending is necessary, but if it can be shown that algorithms decrease loan prices and increase access to credit for members of protected classes, it is appropriate to grant the use of these algorithms some legal protection from discrimination claims. If no such safe harbor is granted, banks will continue to shy away from the use of AI. This may force customers to borrow from less scrutinized, less regulated institutions, where they are more likely to be the victim of discriminatory lending practices.

Conclusion

Once again, ICBA appreciates this opportunity to provide feedback to the CFPB regarding the actions it can take or should consider taking to prevent credit discrimination, encourage responsible innovation, promote fair, equitable, and nondiscriminatory access to credit, address potential regulatory uncertainty, and develop viable solutions to regulatory compliance challenges under ECOA and Regulation B.

In particular, we would like to emphasize the point that complying with regulations is not costless, so as the Bureau moves forward with new regulations, the Bureau should use its existing authority to issue tailored regulations to highly regulated and responsible, financial institutions, including community banks. Please feel free to contact me at Michael.Marshall@icba.org if you have any questions about the positions stated in this letter.

Sincerely,

M. Marshall

Mickey Marshall
Director, Regulatory Legal Affairs