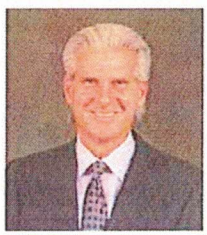
ECOA's Reg. B: Does the Term 'Applicant' Include Guarantors?

By Anthony Lamm, Esq., The Lamm Group

Reg. B aims to promote the availability of credit to all creditworthy applicants and prohibits creditor practices that discriminate on the basis of any irrelevant factors.

From whence do the Equal Credit Opportunity Act and Regulation B come one might wonder? Chapter 12 C.F.R. 202. 7(d) of the ECOA (Regulation B) provides in pertinent part that "a creditor shall not require the signature of an applicant's spouse or other person other than a joint applicant on any credit instrument if the applicant qualifies under the creditor's standards of creditworthiness for the amount and terms of the credit requested." Regulation B is the result of Congress' directive. Like the ECOA, Regulation B aims to promote the availability of credit to all creditworthy applicants without regard to sex or marital status and other factors and prohibits creditor practices that discriminate on the basis of any of these factors. [1] The part of Regulation B referred to above involving the signature of an applicant's spouse or other person is referred to as the "spouse guarantors rule." This prohibits a creditor from requiring an applicant's spouse to guarantee a credit instrument, even if the creditor requires someone to execute a guaranty. [2] Put differently, the applicant's spouse may serve as an additional party supporting an application, but the creditor should not require that the spouse be the additional party. The Equal Credit Opportunity Act laid down the law against discriminatory practices against an applicant's spouse where it provides that it is "unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction…on the basis of marital status." [3]

The potential for abuse is obvious. Without ECOA and Regulation B, any creditor could subjectively deny credit to an applicant because the applicant's spouse would not sign a guarantee regardless of said applicant's creditworthiness on its own. Before ECOA, a creditor could flat out insist that applicants' wives become guarantors to reach assets for collateral jointly held even if a creditworthiness analysis would showed that the additional signature was not required by the creditor's own standards. Therefore, the discrimination and favor against an applicant with a spouse over a single applicant (regardless that he or she is creditworthy), had to be stopped. Whence comes ECOA and Regulation B.



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Creditors have always wanted applicant's spouses to sign guarantees because frequently applicants hold assets in joint names and to reach these assets for attachment or execution, the applicant's spouse had to "consensually" agree to add their name to a title document so that the creditor could reach those assets. In order to attach the asset of an applicant and its spouse that was held jointly, making the spouse sign a guaranty was not "consensual" at all because the guarantee itself operated to make an applicant's spouse a joint applicant (who would have to sign a note and become jointly and severally liable). 12 C.F.R. 202.7(3) was promulgated for the protection of applicant's spouses so that they did not have to become jointly liable for the debt along with the applicant itself. 12 C.F.R. 202.7(3) provides that "if an applicant

requests secured credit, a creditor may require the signature of the applicant's spouse or other person on any instrument necessary or reasonably believed by the creditor to be necessary under applicable state law to make the property being offered as security available to satisfy the debt in the event of default, for example, an instrument to create a valid lien, pass clear title, waive inchoate rights or assign earnings."

Accordingly, Regulation B puts a meaningful limitation on the applicant's spouse's liability in secured and unsecured credit transactions. It naturally follows then that the question of who an applicant is will be determinative of the applicant spouse's rights. The question of whether signing a guaranty is an application for credit or that the guarantor is an applicant is pivotal to whether a creditor violates Regulation B by requiring the applicant's spouse to sign a guarantee and also whether that act by the creditor can be used as an affirmative defense available to a guarantor who has been brought to charge concerning the guarantor's liability on the debt. Two very recent cases have taken up the issue of whether the definition of the word "applicant" as used in ECOA and Regulation B is meant to include guarantors, RL BB Acquisitions, LLC v. Bridgemill Commons Dev. Group, LLC, 754 F.3d 380; 2014 U.S. App. Lexis 10907; 2014 FED App. 0123P (6th CIR): 2014 WL 2609616 and Hawkins v. Cmty. Bank of Raymore 761 F. 3d 937; 2014 U.S. App. Lexis 15006 (8th Cir.); 2014 WL 3826820.

In Hawkins, the court concluded that the text of the ECOA clearly provided that a person did not qualify as an applicant under the statute solely by virtue of executing a guaranty to secure the debt of another and therefore in this case, the creditor did not violate the ECOA by requiring the guarantors to execute the guarantees. Consistent with that holding, there is no protection offered the guarantors under the Spouse Guarantor rule and said rule would not qualify as an affirmative defense. The Court in Hawkins analyzed that "A guaranty is collateral and secondary to the underlying loan transaction between the lender and the borrower. While a guarantor no doubt desires for a lender to extend credit to a borrower, it does not follow from the execution of guaranty that a guarantor has requested credit or otherwise been involved in applying for credit. Thus a guarantor does not request credit and therefore cannot qualify as an applicant under the unambiguous text of the ECOA." [4] To qualify as an applicant under the ECOA, a person must "apply to a creditor directly for … credit, or … indirectly by use of an existing credit plan for an amount exceeding a previously established credit limit." [5] As ruled in Hawkins, "Thus, the plain language of the ECOA unmistakably provides that a person is an applicant only if she requests credit". RL BB comes to the opposite position and finds that Regulation B's definition of applicant included guarantors as applicants and the spouse-guarantor could raise a violation of ECOA and deploy Regulation B as an affirmative defense of recoupment.

Creditors who violate the ECOA or Regulation B may be sued for actual damages, punitive damages, and attorney's fees. [6] But only applicants have the ability to sue for ECOA violations. While ECOA's definition of applicant does not overtly include guarantors, Regulation B's definition of applicant does for the purposes of enforcing the spouse-guarantor rule. [7] The RL BB Acquisition Court reasoned that "A guarantor does not traditionally approach a creditor herself asking for credit. Rather, as was the case here, a guarantor is a third party to the larger application process. But a guarantor does formally approach a creditor in the sense that the guarantor offers up her own personal liability to the creditor if the borrower defaults. Certainly, a guarantor does not ordinarily make the initial approach to a creditor, and one permissible reading of this term is that only the initial applicant can be deemed to "apply" for credit. But the text could just as easily encompass all those who offer promises in support of an application – including guarantors, who make formal requests for aid in the form of credit for a third party."

Since there is a split in the two Appellate courts as to whether the word "applicant" includes guarantors for the purpose of whether a guarantor can invoke the ECOA spouse-guarantor rule and sue a creditor for a violation of ECOA if they try to require the spouse's signature on a guaranty and also provide the basis for an affirmative defense to the payment of the borrower's debt, the issue of whether the term "applicant" is held to include guarantors is going to have to be resolved by the Supreme Court.

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1. 12 C.F.R. 201.1 (b). 2. 12 C.F.R. 202.7 (d)(5), 1002.7 (d)(5). 3. 15 U.S.C. 1691(a)(1). 4. Hawkins. 5. 15 U.S.C. 1691 a(b). 6. 15 U.S.C.S. 1691c. 7. 12 C.F.R. 202.2(e), 1002.2(e).