CREDIT-RELATED DISCRIMINATION: Not All Guarantors Are Eligible to Assert ECOA Claims

KEY POINTS

- Trade creditors must be conscious of the Equal Credit Opportunity Act (ECOA) and its accompanying Regulation B, as they preclude various forms of discrimination in credit transactions and give applicants for credit standing to sue a potential creditor for any such discrimination.
- The recent decision of the U.S. Court of Appeals for the Tenth Circuit in *Miller v. First United Bank and Trust Co.* sheds light on whether and to what extent a guarantor may have standing to sue for violations of the ECOA.
- Specifically, the Tenth Circuit held that guarantors generally do not have such standing; only spousal guarantors may, with respect to certain claims. Clearly, this decision benefits potential creditors as it supports a limitation on the universe of potential parties that may allege ECOA-based claims against creditors.

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TRADE CREDITORS EXTENDING CREDIT TO CUSTOMERS SHOULD BE AWARE OF THE EQUAL CREDIT OPPORTUNITY ACT (ECOA) AND ITS COINCIDING REGULATION B. THIS FEDERAL REGULATORY SCHEME GENERALLY PROHIBITS VARIOUS FORMS OF DISCRIMINATION IN CONNECTION WITH APPLICATIONS FOR AND EXTENSIONS OF CREDIT. THE ECOA PROTECTS "APPLICANTS" FOR CREDIT AND THEREFORE GIVES APPLICANTS STANDING TO SUE A CREDITOR FOR ACTUAL AND PUNITIVE DAMAGES AND ATTORNEYS' FEES IF THE CREDITOR VIOLATES THE ECOA'S ANTI-DISCRIMINATION PROVISIONS.

A trade creditor that extends credit may seek a guaranty from the customer's principals, parent and/or affiliates to backstop the amounts owed by the customer. So, does a guarantor qualify as an applicant that can sue for alleged violations of the ECOA? In the recent decision of *Miller v. First United Bank and Trust Co.*, the United States Court of Appeals for the Tenth Circuit held that, except for spousal guarantors, the answer is "no." This decision limits the potential universe of parties that may allege ECOA-based discrimination claims against a creditor for denying credit. Nonetheless, creditors should remain cautious when considering requests for credit and corresponding guarantees so as not to potentially face litigation risk and the risk of significant damages resulting from alleged credit-related discrimination claims.

RELEVANT BACKGROUND REGARDING THE ECOA, REGULATION B AND THE SIGNATURE RULES

The ECOA makes it "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 (provided the applicant has the capacity to contract)." Regulation B (the implementing regulation of ECOA) includes guarantors in the definition of applicant with standing to sue under the ECOA, but only for purposes of § 1002.7(d) with respect to spousal guarantees. Regulation B defines an "applicant" as:

[A]ny 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 § 1002.7(d) [of Regulation B], the term includes guarantors, sureties, endorsers, and similar parties.

Specifically, Regulation B prohibits creditors from "requir[ing] the signature of an applicant's spouse . . . 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." This prohibition against requiring spousal guarantees is sometimes referred to as the "signature rules" or the "spouse-guarantor rules." The *Miller* court held that the guarantors were not applicants that can assert ECOA claims because they were not spousal guarantors subject to the signature rules.

RELEVANT BACKGROUND REGARDING THE MILLER DECISION

Four individual plaintiffs in the *Miller* case asserted credit discrimination claims arising from a lending institution's denial of a loan application to finance the purchase of an apartment complex. The applicant for the loan was CDMR, LLC, an entity owned by the individual plaintiffs; the individual plaintiffs were proposed guarantors of the loan. The plaintiffs asserted that the lender had denied their application for financing based on their race.[1]

The district court held that the individual plaintiffs lacked standing to assert ECOA claims because the ECOA's general definition of "applicant" does not include guarantors. While Regulation B defines an "applicant" to include a guarantor, it only does so for purposes of the signature rules (i.e. spousal guarantees). The individual plaintiffs had not alleged any violation of the signature rules; their alleged discrimination claims were based solely on race, not marital status.

The individual plaintiffs then appealed to the Tenth Circuit. On appeal, the individual plaintiffs relied heavily on a prior decision by the Sixth Circuit Court of Appeals, in *RL BB Acquisitions, LLC v. Bridgemill Commons Development Group*. Specifically, the individual plaintiffs pointed to that court's statements that (i) the statutory definition of "applicant" is "ambiguous because it could be read to include third parties who do not initiate an application for credit, and who do not seek credit for themselves—a category that includes guarantors", and (ii) there is "no reason to artificially limit the possible meanings of 'applicant'" because the "ECOA prohibits discrimination 'with respect to *any aspect* of a credit transaction[.]'" and the ECOA "has broad remedial goals[.]"

The individual plaintiffs also argued that Regulation B's definition of applicant necessarily includes guarantors, since it includes "any person who is or may become contractually liable regarding an extension of credit."

THE TENTH CIRCUIT'S RULING

The Tenth Circuit affirmed the district court's ruling, holding that the individual plaintiffs lacked standing to assert ECOA claims because they were not "applicants" for credit under the ECOA. The Tenth Circuit, like the district court, concluded that Regulation B's inclusion of guarantors within the definition of "applicant" applies solely to spousal guarantors under the signature rules. The individual plaintiffs were not spousal guarantors and had not alleged any violation of the signature rules.

The Tenth Circuit was unpersuaded by the plaintiffs' reliance on the Sixth Circuit's decision in *RL BB Acquisitions, LLC* because the relevant portions of that decision were also limited to spousal guarantors and violations of the signature rules. In fact, in that case, the Sixth Circuit specifically observed that treating guarantors as applicants for the limited purpose of the signature rules was "a result that the regulators reached with caution." The initial versions of Regulation B proposed that guarantors would be deemed applicants generally, but the final version limited the definition of applicant to only apply to the spousal-guarantors. As noted in the Sixth Circuit's decision, Regulation B was promulgated "… in response to the concerns of industry commenters who believed that the unlimited inclusion of guarantors and similar parties in the definition might subject creditors to a risk of liability for technical violations of various provisions of the regulation."[2]

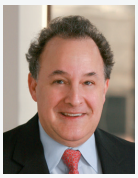
The Tenth Circuit also rejected the plaintiffs' argument that they should have standing because guarantors may become contractually liable for the applicable debt, and Regulation B's definition of applicant includes anyone who "may become contractually liable." While that language is included in Regulation B's definition of an "applicant", the Court noted that "[one] of the most basic interpretive canons [is] that a statute should be construed so that effect is given to all its provisions, so that no part will be inoperative or superfluous, void or insignificant." There would be no need to specify that only spousal guarantors are applicants for purposes of the signature rules under Regulation B if courts accepted the plaintiffs' proposed interpretation of the definition of "applicant."

The Tenth Circuit was similarly unpersuaded that guarantors must have standing simply because the ECOA has "broad remedial goals." As the Court stated, "[the Court] may not use [legislative intent] to employ a liberal construction of the statute or the regulation 'as a substitute for a conclusion grounded in ... text and structure.'" Here, the text and structure indicate that the ECOA and its implementing regulations define an applicant as including only spousal guarantors for purposes of the signature rules.[3] BC

1 The plaintiffs had also asserted claims under the Fair Housing Act and US Code § 1981. However, the FHA claim was dismissed by the district court and that decision was not appealed by the plaintiffs. As for § 1981 claim, the Tenth Circuit held that such a claim must be based on "injuries flowing from a racially motivated breach of [the plaintiffs'] own contractual relationship, not of someone else's." Here, the contractual relationship was not the individual plaintiffs', but rather CDMR, LLC's.

2 The United States Courts of Appeal have also reached conflicting holdings over whether spousal guarantors have standing to assert discrimination claims with respect to credit decisions under the ECOA. The Seventh, Eighth, and Eleventh Circuits have held that ECOA's definition of "applicant" is unambiguous and does not include guarantors. The Sixth Circuit has taken a contrary approach, having held that the ECOA's definition of applicant is ambiguous and ECOA's protections apply to spousal guarantors. The United States Supreme Court was unable to resolve this Circuit split. The Tenth Circuit did not weight in on the split.

3 The plaintiffs also asserted several state and common law (i.e., not ECOA-based) theories under which they, as guarantors, should be afforded the same rights as applicants since they are essentially co-borrowers. The Court rejected these arguments, holding that it only needs to resort to state and common law where the question at issue cannot be answered by statutory interpretation. Here, the ECOA and its implementing regulations adequately answered the question before the Court.



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