The Fair Lending Laws and Their Enforcement

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Journalists, businessmen, politicians, and regulators are paying increasing attention to the subject of discrimination in lending, with particular emphasis on mortgage lending. It sometimes seems as though the main issues in antidiscrimination efforts have shifted from education and labor markets to the credit markets.

Two different federal laws deal with discrimination in lending: the Fair Housing Act (FHAct) and the Equal Credit Opportunity Act (ECOA). These fair lending laws prohibit lenders from discriminating in credit transactions on the basis of race, color, national origin, religion, sex, and other specified grounds.[1] But the laws provide little practical guidance for enforcement, particularly with regard to the role of the banking regulatory bodies. Congress left to these agencies and to the courts the job of working out the specifics of how to define and promote the laws' purpose—fair lending.

While discrimination has been discussed widely in the popular and professional press, an overview of the two fair lending laws and their enforcement is difficult to find. Section 1 describes these laws, their origins, and the interpretations that the courts and enforcement agencies have given some of

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[1] Two other laws often mentioned in discussions of fair lending are the Home Mortgage Disclosure Act of 1975 (HMDA) and the Community Reinvestment Act of 1977 (CRA). While both laws play a part in current fair lending enforcement, neither prohibits discriminatory lending, so neither is defined as a fair lending law. The HMDA requires depository institutions to report data that are frequently used in investigations and studies of lending discrimination. The CRA requires the banking agencies to consider a depository institution's efforts to meet the needs of its community when it applies to the banking agencies for permission to expand. As currently interpreted by the agencies, this has meant that a bank's fair lending performance is weighed when considering such an application. For discussions of the HMDA and the CRA, see Canner and Smith (1991) and Lacker (1995), respectively.

their provisions. Section 2 discusses the three major methods of enforcement of the laws: (1) complaints from aggrieved parties leading to investigations by enforcement agencies, (2) civil court actions, and (3) examination by the federal banking agencies.[2] When it comes to their part of enforcing the fair lending laws, the banking agencies follow procedures long used in carrying out their responsibilities for bank safety and soundness. Specifically, they employ periodic fair lending examinations of all banks.[3] Yet the examination of every institution, whether or not the agency suspects discrimination, is strikingly different from the practices of the federal agencies responsible for other areas of anti-discrimination law enforcement. Section 3 discusses the enforcement of other antidiscrimination laws. The absence of periodic exams in other areas of antidiscrimination law enforcement naturally leads one to ask whether routine use of exams for banks is the most efficient means of enforcing the fair lending laws. The concluding section raises briefly some issues that bear on this question.

1. THE FAIR LENDING LAWS

The Fair Housing Act (FHAct) was passed as part of the Civil Rights Act of 1968, which Congress enacted following urban unrest in many U.S. cities in 1965, 1966, 1967, and after Rev. Martin Luther King, Jr.'s assassination in early 1968. According to a Supreme Court opinion, Congress intended the FHAct to contribute to the elimination of ghettos by reducing discriminatory housing practices (*Trafficante v. Metropolitan Life Insurance Company,* 409 U.S. 205 [1972], cited in Board of Governors, *Consumer Compliance Handbook* [1995]).

The FHAct prohibits discrimination in many activities of the residential real estate industry besides lending. The act prohibits discrimination by race, color, religion, sex, handicap, familial status (if a household includes children), and national origin.[4,5] It prohibits the refusal to sell, rent, or negotiate for the sale or rental of housing for discriminatory reasons. Varying the terms of sale or rental in a discriminatory manner is prohibited, as is falsely claiming that housing is not available for inspection, sale, or rental. The act also prohibits real estate

[2] These agencies are the Federal Deposit Insurance Corporation, the Federal Reserve, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, and the National Credit Union Administration.

[3] I will use the term "banks" throughout to refer to commercial banks, thrifts, and credit unions.

[4] As passed, the FHAct prohibited discrimination on the basis of race, color, religion, and national origin. A 1974 amendment added sex as a basis. A 1988 amendment added handicap and familial status.

[5] Unless otherwise noted, I will use the word "discrimination" throughout to mean discriminating on the basis of categories such as race, gender, or familial status.

brokerage organizations, such as multiple-listing services, from discriminating in their terms of access to the organization.

Section 805, the fair lending portion of the FHAct, makes discrimination unlawful in several aspects of home finance. Specifically, it prohibits discrimination in the making or purchasing of loans, the proceeds of which are for purchasing, constructing, improving, repairing, or maintaining a dwelling. The prohibition applies to any person or entity whose business includes engaging in residential real estate-related credit transactions.

The FHAct is enforced by the Department of Housing and Urban Development (HUD), by individuals, and by the Justice Department. Under the act, HUD may take enforcement actions against lenders based on complaints from individuals or on its own initiative. Individuals, or organizations representing individuals, may pursue civil court actions under the act for discrimination against them. A civil action may be brought in a federal court by the Justice Department whenever it believes that a lender is engaged in a pattern of discrimination.

The federal bank regulatory agencies also enforce the act. These agencies are the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve (Fed), the Office of the Comptroller of the Currency (OCC), the Office of Thrift Supervision (OTS), and the National Credit Union Administration (NCUA). Since the act says little about their enforcement responsibilities, the banking agencies have been left to determine largely on their own how to enforce the FHAct.

The fair lending section of the FHAct does not specify actions or policies that are considered discrimination.[6] This means that the agencies responsible for the act's enforcement have little to guide them in the investigation of lending discrimination. At first blush, the identification of lending discrimination might seem a simple matter. The difficulty arises because discrimination, in the broad sense of the word, is a fundamental function of a successful lender. To remain profitable, a lender must avoid (discriminate against) borrowers who are unlikely to repay, and favor those who will repay. Enforcement agencies are left with the difficult job of separating appropriate discrimination from discrimination prohibited by the act. Court decisions have provided broad guidance, but detailed direction is lacking.

In 1972, a U.S. Supreme Court ruling established a procedure for determining whether an individual has been treated differently based on his minority status. Such discrimination goes by the phrase "disparate treatment." The case dealt with employment discrimination, but the courts later applied the precedent to lending discrimination. The Supreme Court set out four factors that a plaintiff

[6] This contrasts with the housing section of the FHAct, which provides an explicit list of actions which are discriminatory under the law.

must establish to make a prima facie case of employment discrimination. The plaintiff must show (1) that he belongs to a racial minority, (2) that he applied and was qualified for a job for which the employer was seeking applicants, (3) that, despite his qualifications, he was rejected, and (4) that, after his rejection, the position remained open and the employer continued to seek equivalently qualified applicants (*McDonnell-Douglas Corp. v. Green*, 411 U.S. 792 [1973], cited in Board of Governors, *Consumer Compliance Handbook* [1995]).

To translate these standards for use in lending cases, the courts simply substituted the idea of creditworthiness qualifications for job qualifications (*Hickson v. Home Federal of Atlanta*, 805 F. Supp. 1567 [N.D. Ga., 1992]; *aff'd*, 14 F.3d 59 [11th Cir. 1994], *Gross v. U.S. Small Business Admin*., 669 F. Supp. 50 [N.D. N.Y., 1987]). Therefore, to make a prima facie case, the plaintiff must show (1) that he is a member of a protected class, (2) that he attempted to get a loan and met all relevant qualifications for doing so, (3) that the bank refused to make the loan despite the plaintiff's qualifications, and (4) that, after his rejection, the bank continued to make loans to equivalently qualified applicants. Banking agency investigation procedures are based in part on determining whether these factors are met (see Board of Governors, *Consumer Compliance Handbook* [1995], p. 1.19). The courts and the agencies are left to make difficult decisions, however. No two loan applications are exactly alike, so it is impossible to match a rejected minority application perfectly to an accepted non-minority application, and by doing so show discrimination. The courts and agencies must decide whether similar applications are enough like the rejected minority application to persuasively show discrimination. At the very least, however, this ruling provided what the statute lacked—a doctrine to guide policy.

In addition, courts and banking agencies have recognized that the FHAct's prohibitions against discrimination extend to "redlining" (*Laufman v. Oakley Building and Loan Co*., 408 F. Supp. 489 [S.D. Ohio, 1976]; *Ring v. First Interstate Mortgage, Inc*., 984 F.2d 924 [8th Cir. 1993]; Cloud and Galster 1993, p. 109; Board of Governors, *Consumer Compliance Handbook* [1995], p. 1.59). Redlining is the practice of denying loans for housing in certain neighborhoods, even if the loan applicants are creditworthy. According to the courts and banking agencies, redlining is unlawful when the decision to avoid making loans in a particular neighborhood is based on the race, national origin, religion, or other similar categorization of residents of the neighborhood. Redlining is not unlawful when based entirely on economic considerations, such as the location of a neighborhood in a flood plain (Interagency Task Force on Fair Lending [1994], p. 5; Board of Governors, *Consumer Compliance Handbook* [1995], pp. 1.58–1.59).

The Equal Credit Opportunity Act also prohibits lending discrimination. This act was passed in 1974 as an amendment to the much broader Consumer

Credit Protection Act, passed in 1968.[7] Specifically, the ECOA prohibits discrimination in all personal and commercial credit transactions based on race, color, religion, national origin, sex, marital status, age, and other bases.[8] The prohibitions apply to anyone regularly extending credit or arranging for the extension of credit. The ECOA is broader than the FHAct since the ECOA covers virtually all lenders while the FHAct covers only real estate-related lending. Housing lenders are subject to both statutes.

As originally passed in 1974, the ECOA only prohibited discrimination based on sex and marital status. Congressional hearings preceding the passage of the ECOA had produced testimony of lending discrimination against women and particularly of women denied credit without the signature of a male (Senate Rep. No. 589, 94th Cong., 2d Sess. 2, reprinted in *U.S. Code: Congressional and Administrative News* 403, 404 [1976]; Board of Governors, *Consumer Compliance Handbook* [1995], p. 1.12). Additional bases were added by a 1976 amendment. In 1974 hearings, instances were reported of discrimination based on age and race. In addition, during 1974 the banking agencies conducted studies on loan acceptance and rejection rates for minority versus non-minority applicants. Holding creditworthiness factors constant, the studies found much higher rejection rates for minorities (Senate Rep. No. 589, 94th Cong., 2d Sess. 2, reprinted in *U.S. Code: Congressional and Administrative News* 403, 405 [1976]; U.S. Congress, Senate [1993], pp. 570–71).

Besides prohibiting lending discrimination, the ECOA includes some requirements not explicitly related to fair lending. Within thirty days of an application, a lender must notify the loan applicant whether the application has been accepted or rejected. In the case of a rejected application, a lender must state the reasons for the denial or tell the denied applicant that he may have a statement of the reasons on request. Lenders also must provide, either routinely or at the applicant's request, copies of any appraisal reports.

The ECOA requires the banking agencies to ensure that depository institutions comply with the act's requirements. The ECOA delegates to the Fed the authority to "prescribe regulations to carry out the purposes of the title." These regulations are the Fed's Regulation B. Each regulatory agency is responsible for ensuring that the depository institutions it normally supervises comply with the ECOA and Regulation B. Several other federal agencies are responsible for enforcing compliance by other types of firms that make loans.

[7] The Consumer Credit Protection Act encompasses the Truth in Lending Act, the Fair Credit Reporting Act, the Equal Credit Opportunity Act, the Fair Debt Collection Practices Act, and the Electronic Fund Transfer Act.

[8] Other bases on which lenders may not discriminate include an applicant's status as a recipient of public assistance and an applicant's claim of any right under the Consumer Credit Protection Act.

These agencies include the Federal Trade Commission, the Small Business Administration, the Farm Credit Administration, and others.

The ECOA has left the agencies and the courts with much to work out concerning its enforcement. For instance, like the FHAct, the ECOA leaves largely undefined the actions and policies that are considered discrimination. In addition, the act does not tell the enforcement agencies how to uncover discriminating creditors or discriminating actions. While the FHAct outlines HUD's complaint response procedures, the ECOA does not address such procedures.

Nevertheless, like the FHAct, the ECOA stipulates that any creditor is subject to one of three enforcement actions. First, a person alleging injury may sue the creditor in a federal district court. Second, the federal agency with jurisdiction may take action against the creditor. Third, the Justice Department may pursue a civil action against a suspected violator. Such action may occur if another enforcement agency refers the case to the Justice Department or if the Justice Department suspects a pattern of violations.

Court decisions have helped to define discrimination under the ECOA as they have under the FHAct. In the legislative history of the 1976 amendment to the ECOA, Congress showed that it meant for the act to encompass a new concept of lending discrimination. Discrimination is to include not only disparate treatment (discussed above) but a discrimination standard recently developed by the courts, "disparate impact" (Senate Rep. No. 589, 94th Cong., 2d Sess. 2, reprinted in *U.S. Code: Congressional and Administrative News* 403, 406 [1976]). Disparate treatment occurs when individuals receive different treatment because of their minority status. Disparate impact occurs when minority individuals and non-minority individuals receive equivalent treatment but a lending policy has a disparate effect on minorities. Making loans for amounts no smaller than a set minimum is the classic example of a policy with a disparate impact. Since, on average, minorities are over-represented in low income brackets, they will more frequently seek low value loans. Therefore, they will be rejected more frequently for loans than will non-minorities under a minimum-loan-amount policy.

The courts developed the disparate impact standard in employment discrimination cases, including a 1971 Supreme Court ruling, *Griggs v. Duke Power Co.* (401 U.S. 424 [1971]). In that case, several black employees of Duke Power Company challenged as discriminatory the company's policy of requiring a high school diploma and a passing score on an intelligence test as a prerequisite for hiring and promotion. The Court ruled that the Civil Rights Act of 1964 outlawed practices that had the effect of discriminating and that Duke's prerequisites had such an effect and were not significantly related to performance of the jobs in question (Board of Governors [1977b], p. 106; *Griggs v. Duke Power Co*. (401 U.S. 424 [1971]).

Following the 1976 amendment to the ECOA, courts extended this rule to lending discrimination. They ruled that a complainant can make a prima facie case of illegal lending discrimination if he can show that a lender's policy has a disproportionately adverse effect on a protected class. A policy is said to fail the so-called "effects test" if it has a disproportionately adverse effect (*Cherry v. Amoco Oil Co.*, 490 F. Supp. 1026 [N.D. Ga., 1980]).

Various courts have come to different conclusions over the burden of proof the lender must carry to rebut the complainant's prima facie disparate impact case. Some courts have ruled that a lender must show a "legitimate business reason" for a practice that produces the disparate impact. Other courts have ruled that the lender must show a "business necessity," a more stringent standard. In 1994 the federal agencies enforcing the fair lending laws came out in favor of requiring the more strict burden for the lender (Interagency Task Force on Fair Lending [1994], p. 7).[9]

2. ENFORCEMENT OF THE FAIR LENDING LAWS

There are three methods of enforcing the fair lending laws. First, the enforcement agencies may take action in response to complaints. Second, individuals or the Justice Department may bring civil court actions. Third, the banking agencies periodically examine every bank for evidence of discrimination. The agencies take remedial or punitive action if evidence of discrimination is found.

Complaints

An individual who believes he has suffered prohibited credit discrimination may complain to (1) the Justice Department, (2) HUD if the loan is for real estate, or (3) the federal agency with fair lending enforcement powers over the institution believed to have discriminated. The FHAct requires HUD to receive and respond to complaints of fair lending violations. The FDIC, the Fed, and the OCC are each required to maintain a consumer affairs division by the Magnuson-Moss Warranty—Federal Trade Commission Improvement Act of 1975 (U.S. Congress, Senate [1976], p. 1).[10] These divisions receive and take action upon consumer complaints, such as complaints of fair lending violations. The Justice Department also responds to lending discrimination complaints that it receives.

Each year these organizations together receive over a thousand complaints of alleged credit discrimination (see U.S. Congress, Senate [1993], pp. 668–69,

[9] For further discussion of the history and current status of the disparate impact standard in lending discrimination, see Vartanian, Ledig, and Babitz (1995), Dennis and Bachman (1995), and Board of Governors of the Federal Reserve System, *Official Staff Commentary on Regulation B, Equal Credit Opportunity* (1995), sect. 202.6(a)-2.

[10] The name of the act derives from its sponsors Senator Warren G. Magnuson and Representative John E. Moss.

680, 700, and 742; U.S. Department of Justice, annual reports of the Attorney General [1977–1987]; U.S. Congress, Senate [1990], p. 119). The agencies investigate each complaint of suspected lending discrimination. If the agencies uncover evidence of discrimination, they may attempt to resolve the complaint by obtaining agreement between the parties. Beyond this, the banking agencies and HUD may require remedial action or may penalize the violator, while the Justice Department can sue. Sometimes one agency refers the case to another agency.

Courts

Based on provisions in both the ECOA and the FHAct, an individual who believes he has suffered prohibited credit discrimination may also seek relief directly from the courts. According to the legislative history of the ECOA, Congress viewed the power of individual claimants to bring civil court cases as a primary mode of enforcement of the statute (Senate Rep. No. 589, 94th Cong., 2d Sess. 2, reprinted in *U.S. Code: Congressional and Administrative News* 403, 415 [1976]).

Private fair housing and civil rights agencies have become more active in facilitating fair lending actions taken by individuals. For instance, one of the first agencies, the Toledo Fair Housing Center, has produced a number of victories for borrowers either in court, in settlements outside court, or through complaints made to the federal enforcement agencies (Cloud and Galster 1993). Similar organizations also have become active recently, producing several large settlements for their clients, and initiating additional suits (Sweet 1995, p. 4; *Washington Post,* September 22, 1995; *American Banker,* January 10, 1995).

Beyond the ability of individuals to bring court cases, the Justice Department may bring civil court actions under both the FHAct and the ECOA. Before 1988, Justice Department enforcement powers were limited under the FHAct and the ECOA; the Justice Department was not granted the power to seek monetary awards. In 1988, an amendment to the FHAct granted the Justice Department the authority to seek monetary awards for damages and civil penalties. A 1991 amendment to the ECOA similarly expanded the types of relief the Justice Department could seek in fair lending cases brought under that statute.

Before these amendments provided the Justice Department with the authority to seek monetary awards, most fair lending actions by the Justice Department resulted in small out-of-court settlements that aroused little popular interest.[11] Since the early 1990s, however, every suit brought by the U.S. Department of Justice has been the focus of great interest, at least among lenders. Each year

[11] At least one lending discrimination case brought by the U.S. Justice Department went to trial (*U.S. v. American Future Systems, Inc*., 743 F.2d 169 [3d Cir. 1984]).

since 1992 the Justice Department has investigated several fair lending cases resulting in large out-of-court settlements against lenders. In these settlements, the lenders agreed to significant penalties, including compensation for victims, modification of lending procedures, and increased efforts to reach minority individuals or communities.

In civil court cases brought by individuals under the FHAct, the courts may award actual and punitive damages and other equitable relief. The act sets no maximum for these damage awards. In court cases brought by the Justice Department under the FHAct, penalties for violations are the same as in cases brought by individuals, except that civil penalties beyond actual damages are limited to $50,000 for the first violation and $100,000 for any subsequent violations. Under the ECOA, individuals and the Justice Department may seek actual damages and the imposition of injunctions. An injunction is a court order requiring a party to do or refrain from doing a specified act. But lenders may not be made to pay punitive damages to an aggrieved individual greater than $10,000. In class action suits, punitive damages are limited to the lesser of $500,000 or 1 percent of the lender's net worth.

Examination

Examination by the banking agencies provides the third method of enforcing the fair lending laws. The banking agencies probe the institutions they supervise for evidence of lending discrimination in periodic, on-site fair lending examinations. For banks examined by the Fed, a fair lending examination occurs at least every two years. The other agencies have differing schedules.

Fair lending examinations have their origin in, and are modeled after, bank safety and soundness examinations. In a safety and soundness examination, examiners from a federal banking agency investigate a bank's riskiness and financial health. The agencies examine every bank periodically. The examinations include an on-site analysis of the bank's management, its policies and procedures, and its key financial factors. Additionally, examiners verify that a bank is complying with banking laws and regulations. Because of this, examiners gained responsibility for verifying compliance with the fair lending laws when these laws were passed.

Besides the fair lending laws, a number of other banking consumer protection laws, such as the Truth in Lending Act, the Fair Credit Reporting Act, and the Fair Credit Billing Act, were passed by Congress during the 1960s and early 1970s. Examiners gained responsibility for banks' compliance with these laws too. Between 1976 and 1980 the FDIC, the Fed, the OCC, and the NCUA established "consumer compliance" examinations separate from safety and soundness examinations because performing both consumer law compliance and safety and soundness tasks within the same examination was too burdensome.[12] Examiners who specialize in consumer law compliance (compliance examiners) perform fair lending examinations. The consumer compliance examination covers the fair lending laws and the other consumer protection laws. While separate from the soundness examination, the consumer compliance examination follows the model of periodic, on-site examinations used in the soundness examination.[13]

In the fair lending portion of compliance examinations, the examiner checks for evidence of disparate treatment, redlining, and disparate impact. The examination for disparate treatment of minorities may proceed along several lines. Since the early 1990s, the banking agencies have been using statistical tests to aid them in their search for evidence of discrimination.[14] Compliance examiners may run statistical tests on the outcomes of a bank's loan approval process to decide if minority status is correlated with the frequency of denial, factors other than minority status held equal. When such a correlation is found, examiners manually review a sample of loan application files to determine whether factors omitted by the statistical testing methods explain the statistical results. The main focus of statistical testing is mortgage lending, since minority status data are available only for mortgage loans.

Relatively large numbers of mortgage applications from both minorities and non-minorities are necessary for valid testing. Without large numbers, the tests cannot produce meaningful results. Only one in ten banks receives enough mortgage loan applications to allow the use of these tests.[15] Since these banks tend to be the largest mortgage lenders, large portions of all outstanding mortgage loans are therefore made by banks subject to statistical testing.[16]

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[12] In January 1989, separate consumer compliance examinations for savings institutions were established by the Federal Home Loan Bank Board (U.S. Congress, Senate [1990], pp. 36–37; U.S. Congress, Senate [1993], p. 693). In late 1989, Congress created the OTS to replace the Federal Home Loan Bank Board as supervisor of savings institutions, following the thrift crisis of the 1980s. The OTS continued the practice of separate consumer compliance examinations.

[13] See Board of Governors (1977a) for a discussion of the history of consumer compliance examination.

[14] In the late 1970s and early 1980s, two of the banking agencies began using functionally similar but less sophisticated tests. The OCC and the FDIC collected data from banks they supervised regarding loans accepted and rejected, race, income, and measures of creditworthiness of the applicant. They then ran statistical analyses that tested for correlations between minority status and rejection, with creditworthiness held equal. The results of these tests guided examiner efforts in searching for evidence of discrimination. While the statistical testing procedures begun in the 1990s are more sophisticated and employ more creditworthiness variables, the methodology and goals are equivalent. The FDIC dropped its use of this technique in 1982 (U.S. Congress, Senate [1990], pp. 44, 155, and 170–71). For discussion of these early techniques, see U.S. General Accounting Office (1981), pp. 50 and 84, and Milroy (1980), pp. 17–33, and 128.

[15] Calem and Canner (1995), p. 121.

[16] For discussions of fair lending testing techniques, see Calem and Canner (1995), Bauer and Cromwell (1994), and Stengel and Glennon (1995).

Examiners use only informal techniques when examining most banks, since formal statistical tests can be used only on a small portion of banks. Fair lending examinations have included informal techniques since the late 1970s. The examiner typically chooses a sample of accepted and rejected applicants and gathers key creditworthiness information for the applicants from the bank's loan application files. The examiner secures a written copy of the bank's lending decision criteria or interviews bank officials to learn the criteria. For example, lending decision criteria might include the bank's minimum down payment percentage, its maximum loan-to-value ratio, and its maximum debt-payments-to-income ratio. The examiner determines whether treatment of accepted and rejected applicants accords with the bank's written or articulated loan criteria. If the bank rejects minorities when its loan criteria suggest acceptance, or accepts non-minorities when the loan criteria suggest rejection, the examiner has reason to suspect discrimination. The examiner will then expand his investigation. For example, assume a bank has a policy of normally rejecting applicants whose debt-payments-to-income ratio will exceed 36 percent if granted the loan. The examiner might become suspicious if this bank allows higher ratios more frequently for whites than for Hispanics. Characteristics of sampled rejected and accepted applicants are also compared directly to determine if the bank accepts non-minority applicants but rejects similarly qualified minority applicants. If this comparison leads the examiner to suspect disparate treatment, he conducts a more intensive investigation.

In searching for signs of disparate treatment by a bank, the examiner also compares the racial and ethnic makeup of the bank's application and loan pools to the racial and ethnic makeup of its market area. If the proportion of applications from minorities differs significantly from the proportion in the bank's market area, the examiner might suspect that the bank is discouraging minorities from applying for loans ("prescreening" minority applicants). Alternatively, a significant differential between the proportion of minority loan approvals and the proportion of minorities in the bank's market area could be a sign that the bank is rejecting minorities for discriminatory reasons. In either case, further investigation would be called for (Board of Governors, *Consumer Compliance Handbook* [1995], pp. 1.43–1.48).

Next, the examiner reviews the bank's loan policies for any that could amount to redlining or for any discriminatory impact. If the examiner finds policies he believes may have such effects, the bank is allowed to present an explanation.

The agencies' responses to violations uncovered during examinations can vary. They may simply require the bank to change its loan policy. They may go further and require it to pay a sizeable monetary penalty either as restitution to injured parties or to the U.S. Treasury. More serious or repeated violations can earn more severe penalties. Whenever an examination uncovers a pattern of fair lending violations, a provision of the ECOA requires the agencies to notify the

Justice Department.[17] While the requirement applies explicitly only to ECOA violations, it covers most FHAct violations as well. Most fair lending violations of the FHAct will be violations of the ECOA, since the former act includes only real estate lending, while the latter covers all types of lending. Some FHAct violations will not be ECOA violations because protected classes differ slightly under the two acts. Once notified, the Justice Department may then choose to investigate and bring a civil action. If the agencies find violations of the FHAct, they must report them either to HUD or to the Justice Department.

3. ENFORCEMENT OF OTHER ANTIDISCRIMINATION LAWS

The first two sections of this article have discussed the fair lending laws and their enforcement. But these fair lending laws are only part of antidiscrimination law. For instance, laws also prohibit discrimination in employment, housing, and voting opportunities. This section contains a brief description of the enforcement activities of several major federal agencies responsible for employment and housing antidiscrimination law. In contrast to the banking agencies' practice of examining all banks for evidence of credit discrimination, the federal employment and housing agencies do not employ routine examinations to enforce antidiscrimination statutes. Instead they investigate institutions only in response to a complaint or other signal of a possible violation. Alternatively, one employment-discrimination law-enforcement agency conducts audits (examinations) of a small subset of institutions. It also responds to complaints.

The major federal agency responsible for employment-discrimination law enforcement investigates employers only if there is prior suspicion of discriminatory activity. The Equal Employment Opportunity Commission (EEOC) is responsible for enforcing four laws prohibiting employment discrimination: the Civil Rights Act of 1964, the Equal Pay Act, the Age Discrimination in Employment Act, and the Americans with Disabilities Act. The EEOC's principal means of enforcing these statutes is through response to complaints of discrimination. These complaints may come from an employee, a rejected job applicant, or an individual or organization acting on an employee's behalf. The EEOC handles complaints by investigating and making a determination on the merits of the complaint. It may seek a settlement between the parties. If the EEOC cannot produce a settlement, it may litigate the case (Bureau of National Affairs 1995, pp. 0:3101–0:3812).

Though complaints are the primary source of EEOC action, the EEOC may itself initiate an investigation. Leads for these charges may come from tips gathered during investigations of other employers. They also may come

[17] This requirement was established by a 1991 amendment to the ECOA.

from the media, other government or private civil rights groups, union and trade associations, and employment agencies. Data from employers on numbers and classifications of minority and non-minority employees can provide a lead (Bureau of National Affairs 1995, p. 8:0002).

Another leading federal employment discrimination enforcement agency is the Office of Federal Contract Compliance Programs (OFCCP), a division of the Department of Labor. The OFCCP is responsible for the enforcement of three antidiscrimination and affirmative action statutes covering institutions receiving government contracts. It enforces the statutes with complaint investigations and compliance reviews ("audits"), which are similar to the banking agencies' examinations.

Although the techniques used in an OFCCP audit are similar to those used in a bank fair lending examination, OFCCP audits only a small subset of contractors.[18] For example, in 1994 it audited 4,100 contractors, selected from a population of 192,500, for compliance with the laws (Office of Federal Contract Compliance Programs [Undated]). Contractors are selected to be audited based in part on the percentage of women and minorities employed relative to comparable percentages employed by the aggregate of all such employers (Fox 1993). Even if no problems are found, an audit is costly for the audited contractor.[19] Therefore, the threat of an audit provides an incentive for contractors to maintain the percentage of women and minorities they employ at or above their peer group's average. This helps the OFCCP meet its affirmative action responsibilities. Other factors are considered when deciding which contractor to audit. These factors are the time elapsed since the last audit, employee or job applicant complaints, negative community group comments, and whether the contractor is adding employees (Fox 1993). Unlike bank fair lending examinations, to which all banks are subject periodically, contractors may go years without an OFCCP audit, if they are audited at all.

The primary federal enforcement agency responsible for housing discrimination is HUD. Like the EEOC, HUD investigations typically result from complaints of discrimination. Occasionally HUD initiates an investigation. For example, some sign of housing discrimination, such as a newspaper story, can generate this type of investigation.

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[18] During OFCCP audits, personnel files are examined to determine if comparable minority and non-minority individuals are treated similarly. Personnel policies are examined for any policies that may have a discriminatory effect. The treatment of minorities relative to policies are examined for signs of discrimination.

[19] According to Fox (1993), an audit costs a contractor an average of $25,000.

4. CONCLUDING COMMENT

Banking agencies enforce fair lending laws by examining all banks for evidence of discrimination. As we saw in Section 3, this contrasts sharply with enforcement in other areas of antidiscrimination law, where routine examinations are not employed. The banking agencies' general use of routine exams has evolved as the best means of guaranteeing the safety and soundness of the banking system. But are routine examinations the most efficient means of ensuring fair lending? This is a difficult question.

The examination of every bank, whether or not it is suspected of discrimination, is expensive for both banking agencies and banks themselves. Relying instead on other enforcement mechanisms, such as complaints and legal actions, has the great advantage of directing scarce resources to identifiable problems. Nevertheless, one can imagine several issues that ought to be considered in weighing the costs and benefits of the alternatives. Victims of discriminatory lending practices may not always be aware of the discrimination. If this is the case, then complaints and private lawsuits might not induce sufficient enforcement. On the other hand, enforcement agencies receive hundreds of complaints of discrimination each year. Moreover, the growing interest of housing groups, the press, and attorneys in credit discrimination will expand borrowers' knowledge of the laws that protect them and thus encourage complaints and lawsuits.

Matters are complicated further by the fact that fair lending legal actions seem likely to produce benefits to society beyond those received by the plaintiff alone. For example, policies of a defendant bank that are unknowingly discriminatory may be identified by a lawsuit, and eliminated as a result. Consequently, future customers will be less likely to be victims of discrimination. Since plaintiffs do not reap all the benefits of their own legal actions, the number of court cases brought may be too low from society's point of view. On this basis one might argue that routine examination of all banks, coupled with the threat of penalties, supplements the antidiscrimination benefits provided by lawsuits. But an alternative to employing routine exams to supplement legal actions would be to increase monetary awards to successful plaintiffs or to perform random examinations on a small percentage of banks as done by the OFCCP on government contractors.

From long practical experience, routine exams have been found necessary to ensure the safety and soundness of the banking system. Whether or not routine exams are also the most efficient means of ensuring fair lending is a matter deserving of further research.

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