No. 14-520

In the Supreme Court of the United States

VALERIE J. HAWKINS AND JANICE A. PATTERSON,
Petitioners,

v.

COMMUNITY BANK OF RAYMORE,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

BRIEF FOR THE AMERICAN BANKERS ASSOCIATION, INDEPENDENT COMMUNITY BANKERS OF AMERICA, MISSOURI BANKERS ASSOCIATION AND MISSOURI INDEPENDENT BANKERS ASSOCIATION AS *AMICI CURIAE* IN SUPPORT OF RESPONDENT

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QUESTION PRESENTED

Does the ECOA's express definition of "applicant," when given its ordinary meaning and read in the context of the statute as a whole, include a guarantor, who merely signs a contract in support of the borrower's application for credit, or did the Federal Reserve Board attempt to redefine impermissibly the ECOA's "applicant" provision when the FRB amended its implementing regulation (Regulation B) to expressly include guarantors?

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

STATUTES AND REGULATIONS

OTHER AUTHORITIES

BRIEF OF THE BANK INDUSTRY *AMICI* IN SUPPORT OF THE RESPONDENTS

INTEREST OF THE *AMICI*[1]

This brief is filed by the American Bankers Association, Independent Community Bankers of America, Missouri Bankers Association, and Missouri Independent Bankers Association (collectively the "*Amici*") in support of Respondent's position requesting affirmance of the Eighth Circuit's ruling.

The American Bankers Association ("ABA") is the principal national trade association of the financial services industry in the United States. Founded in 1875, the ABA is the voice for the nation's $13 trillion banking industry and its over 1 million employees. ABA members provide banking services in each of the fifty States and the District of Columbia. ABA membership includes all sizes and types of financial institutions, including very large and very small banking operations.

The Independent Community Bankers of America ("ICBA") represents more than 6,000 community banks of various sizes and charter types and dedicates itself to giving voice to the interest of the community banking industry through effective advocacy, best-in-

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[1] No counsel for a party authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of this brief. No one other an amici or their counsel made a monetary contribution to the preparation or submission of this brief. Letters from the parties consenting to the filing of this brief have been filed with the Clerk of the Court.

class educational seminars, and high-quality products and services. ICBA members operate 52,000 locations nationwide, provide jobs for 700,000 employees and hold $3.6 trillion in assets, $2.9 trillion in deposits and $2.4 trillion in loans to customers, small businesses and the agricultural community.

The Missouri Bankers Association ("MBA") is a statewide association advocating for and representing more than 300 state and federally chartered banks located in Missouri. The MBA maintains an interest in promoting laws and policies that preserve a vibrant, free-market economy, and promote the availability of both sound and affordable credit for the benefit of the public and MBA member banks.

Missouri Independent Bankers Association ("MIBA") is a statewide trade association exclusively representing independent community banks serving over 400 communities across Missouri. The MIBA is dedicated to the preservation of banking law and structure which will assure the continued survival and prosperity of Missouri's independent, community banks for Missouri and its citizens.

Virtually all of the member financial institutions of the *Amici* provide business and commercial loans to corporations that involve personal guaranties of the commercial borrower's obligations. While the commercial venture holds the primary obligation to repay the loan, the guaranties provide secondary sources of potential payment in the event the corporate borrower defaults.

During the steep decline in the United States economy beginning in the fall of 2008, members of the

Amici frequently looked to guarantors to shore up the financial health of the commercial borrower, to provide necessary cash flow infusions, to find solutions and effective business strategies for the commercial borrower to rehabilitate problem loans, and, in the worst case of a default, to be responsible to pay the commercial borrower's obligations. Increasingly since 2009, member banks face claims from non-owner spousal guarantors contending that spousal guaranties constitute *per se* discrimination in violation of the ECOA and seeking a range of remedies including voiding the guaranties, voiding the entire loan obligation, and recovering money damages, including punitive damages.

The *Amici* therefore have a strong interest in the question whether the federal regulatory agencies exceeded their authority by re-writing definitions otherwise contained in the ECOA, without taking into account the necessity and real world requirements of assuring safe and sound lending practices which protect lenders and their customers. Neither lenders nor their customers benefit from over-reaching policies that weaken loan underwriting standards, that increase borrowing costs, or that restrict business credit.

SUMMARY OF ARGUMENT

Amici support the Respondent's position and ask the Court to enforce Congress' express definition of "applicant" in the ECOA and find that the federal agencies exceeded their rulemaking authority by impermissibly expanding the scope of the ECOA. The *Amici* do *not* seek to discriminate based on marital status against individuals or entities applying for commercial loans. In fact, the impermissible extension of the ECOA definition of "applicant" to non-owner spousal guarantors, places married business owners at a significant disadvantage compared to unmarried persons. By reaffirming the specific scope of "applicant" as plainly defined by Congress, the Court will assure that Regulation B implements the ECOA consistent with safe and sound lending practices involving business and commercial loans, and the Court will avoid permitting an agency "re-write" of the ECOA that disadvantages married persons.

In support of their position, the *Amici* advance three arguments. First, guarantors should not be considered "applicants" even setting aside the clear Congressional definition of that term in the ECOA, because the creditworthiness analysis of a guarantor differs from the creditworthiness of a prospective borrower and these differences make Regulation B's language extending anti-discrimination protections to guarantors unworkable. Second, permitting non-owner spousal guarantors to bring discrimination claims exposes lenders to liability and the risk of costly litigation based on an otherwise common-sense underwriting practice of obtaining guaranties to support commercial loans. Third, affirming the scope of "applicant" as

Congress originally intended will not permit lenders to engage in illegal discrimination because the parties that Congress chose to protect – applicants for credit – will still be empowered to bring discrimination claims.

ARGUMENT

I. GUARANTORS ARE NOT "APPLICANTS" FOR BUSINESS AND COMMERCIAL CREDIT; THE STANDARD CREDITWORTHINESS ANALYSIS OF THE BUSINESS ENTITY REQUESTING THE LOAN DIFFERS FROM THE SEPARATE CREDIT ANALYSIS OF A PERSONAL GUARANTOR AS A SECONDARY REPAYMENT SOURCE.

Separate and apart from the problem of re-defining Congress' definition of "applicant" the provisions of Regulation B which purport to grant ECOA claims and remedies to spousal guarantors cannot be reconciled with widely accepted practices lenders utilize to review and to underwrite commercial loans. In the commercial loan setting, the entity applies for a loan and becomes the subject of the lender's underwriting and creditworthiness analysis. Lenders will request guaranties of commercial loans not necessarily because the entity lacks creditworthiness, but to provide additional support to the commercial loan. The analysis to determine the type of support a guarantor can provide differs markedly from the creditworthiness analysis of the prospective borrower. In circumstances where a guarantor is married, the analysis, by necessity, must consider whether the guarantor's assets consist of individually owned or jointly owned property. Under common lending practices, a spouse's guaranty becomes necessary, not because of discrimination, but because of the need to support a

commercial loan with an effective guaranty from a married owner.

A. Under Congress' precise wording, only borrowers "directly" apply for credit or "indirectly" apply for credit under an existing credit plan for an amount exceeding previously approved credit limits - guarantors do not.

The clear wording Congress employed to define an "applicant" under ECOA excludes guarantors. Congress expressly defined the term "applicant" to encompass only those who apply "directly for an extension, renewal, or continuation of credit" or apply "indirectly by use of an existing credit plan for an amount exceeding a previously established credit limit". 15 U.S.C. § 1691a(b). Guarantors do not apply for credit under these circumstances. *Moran Foods, Inc. v. Mid-Atlantic Market Dev. Co., LLC*, 476 F.3d 436, 441 (7th Cir. 2007). The guarantor neither receives credit nor is the guarantor denied credit. *Id*.; *See also*, *Champion Bank v. Reg. Dev. LLC*, Case No. 08CV1807, 2009 WL 1351122 at *2 (E.D. Mo., May 13, 2009) (noting that "a guarantor cannot be denied credit for which he or she did not apply, and thus it is difficult to conceive how a guarantor can claim to have been discriminated against.")

This very deliberate definition crafted by Congress serves the dual purpose of (1) clearly delineating those persons for whom Congress sought to provide protection from discrimination as well as (2) requiring that lenders perform their credit analysis on the *borrower* actually seeking the loan. When considering a commercial loan, such as the loans involved in this

case, the lender evaluates the creditworthiness of the entity applying for the loan to determine the willingness and capacity of the borrower to repay the loan under the terms proposed. A lender typically identifies the primary repayment source and one or more secondary repayment sources from the applicant borrower.

The primary repayment sources for commercial loans typically are the borrower's current and anticipated business revenues. The borrower's business assets and their potential liquidation value might also serve as a primary repayment source, such as in the case of a real estate development loan. Underwriting standards for most lenders include evaluating the prospective borrower's debt-service coverage ratios, loan to value ratios, global financial condition including amount and liquidity of assets, cash flow, direct and contingent liabilities, and equity. *See e.g.* Office of the Comptroller of the Currency, *Comptroller's Handbook on Safety and Soundness for Commercial Real Estate Lending*, August 2013 at pp. 8-9.[2]

In this regard "[t]he primary focus of an examiner's review of a commercial loan and binding commitments is the borrower's ability to repay the loan." *Id*. at p. 72. In commercial lending, including most small business loans (such as the loans here) the "primary source of repayment is often the cash flow of the business, either through the conversion of current assets or ongoing business operations." Office of the Comptroller of the Currency, *Interagency Statement on Meeting the Credit*

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[2] http://www.occ.gov/publications/publications-by-type/comptrollers-handbook/cre.pdf.

Needs of Creditworthy Small Business Borrowers, OCC 2010-6, Feb. 2010.[3]

While the business revenues and assets provide primary repayment sources, a guaranty always functions as a secondary repayment source. A critical aspect of an "owner" guaranty in commercial and business loans is that it increases the business borrower's willingness to perform and to avoid a default on a commercial loan in order to protect the owner's personal assets and credit. The lender evaluates the guarantor to determine the guarantor's capacity and *willingness* to provide credit support, possibly through making payments, but also through continued involvement (expertise, management and time) in the borrower's business operations and in executing the business plan presented to the lender as part of the original loan request. Significantly for purposes of the ECOA, the role of the guarantor is to support the entity seeking the loan, not to apply for the loan individually based on her individual creditworthiness.

The Government argues that guarantors are properly considered "applicants" because guarantors are frequently involved in the application process. U.S. Br. at 20. While not yet determined, even if guarantors are involved in the application process Congress did not make "involvement" the touchstone for whether an individual or entity was an "applicant" under the ECOA. Instead, the definition focuses on whether the individual or entity *directly applied* for credit. 15

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[3] http://www.occ.gov/news-issuances/bulletins/2010/bulletin-2010-6a.pdf.

U.S.C. § 1691a. In this context, substituting "guarantor" for "applicant" in the provisions of Regulation B makes little sense and does not further the purposes of the ECOA.

At 12 C.F.R. § 202.7(d), Regulation B prohibits requesting a signature from a spouse or other person on any credit instrument if the applicant otherwise qualifies under the standards of creditworthiness for the amount and terms of the credit requested.[4] In this case, the borrower was seeking (and received) loans totaling over $2 million dollars. Pet. Br. 2. Nothing in the record establishes that either of the borrower's two owners (the guarantors) would have qualified for that magnitude of loans under Respondent's standards of creditworthiness. As a result, it makes little sense to provide guarantors with a discrimination claim based upon a creditworthiness analysis that never applied to the guarantors.

Substituting "guarantor" for "applicant" would require the lender to consider the individual creditworthiness of each guarantor for any commercial loan being requested. Affording guarantors the status of "applicant" under the ECOA does not comport with typical loan underwriting analysis nor with the secondary role that personal guaranties serve. Instead, Petitioners' position renders provisions of Regulation B incoherent in this respect. Extending the right to bring claims under the ECOA to guarantors cannot be

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[4] While the CFPB re-promulgated the provisions of Reg. B at 12 C.F.R. Pt. 1002 & Sup. I, the *Amici*, consistent with the practices of the United States and Petitioners, will refer to the provisions of Regulation B previously contained in 12 C.F.R. Pt. 202.

reconciled with the narrow Congressional definition of "applicant" or the separate credit analysis lenders must undertake to determine the willingness and capacity of a guarantor to perform his or her contracted obligations.

B. Lenders often obtain guaranties for commercial loans as part of safe, sound, lending practices.

Obtaining a guaranty for a commercial loan results from sound credit-making decisions and not from illegal discrimination.[5] In fact, bank regulators encourage lenders to obtain guaranties to provide valuable credit support. For example, when issuing its policy statement on commercial real estate workouts, the Office of the Comptroller of the Currency ("OCC") observed that guaranties from "financially responsible guarantor[s] may improve the prospects for repayment of the debt obligation[.]" Office of the Comptroller of the Currency *Policy Statement on Prudent Commercial Real Estate Loan Workouts*, OCC 2009-32, Oct. 30, 2009.[6]

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[5] The June 28, 1973 Senate Report for the bill creating the ECOA, S. 2101, recognized that credit decisions, by necessity, involved "discriminating" against applicants to determine which are creditworthy and which are not. The crux of an impermissible discriminatory lending decision, according to the Report, was that the lender denied credit to an applicant, not based on credit criteria, but based on membership in a class. S. Rep. No. 93-278, at 19 (1973).

[6] http://www.occ.gov/news-issuances/bulletins/2009/bulletin-2009-32.html.

Guarantors can support a loan application and the likelihood of repayment because guarantors may continue business operations in the face of economic stress, provide management and expertise, and provide financial support to the enterprise to meet expenses during periods of negative cash flow. At the extreme end of the spectrum, guarantors may serve as an additional, but always secondary, source of recovery for the lender if the commercial enterprise fails and defaults on payment of the commercial loan.

For most small business loans, and in most, if not all project-based loans (where, as here, the loan finances a real estate development) the business acumen/expertise of the owner is a key factor in the success of the business or project. As the recent economic downturn illustrated, competent and committed ownership may be the difference between an enterprise that closes its doors and an enterprise that weathers the downturn and survives. In circumstances where an owner might be tempted to abandon a project, handing the keys to the bank, and walking away, the personal guaranty obligations incentivize the owner not to throw in the towel but, instead, to double-down and work to make the business successful and viable.

Given that the value of the guarantor's support depends on the ability to provide financial support to the borrower, prudent lenders evaluate the potential guarantor's global financial condition to determine whether the guarantor possesses sufficient assets to assist the borrower and help fund a shortfall. An analysis, by necessity, considers whether the guarantor's global financial condition includes jointly held assets, including marital assets and earnings

which, in the case of a married guarantor, without a joint-spousal guaranty would be unavailable to provide support for the owner's guaranty.

The strength of a married person's guaranty, in most cases, will be much weaker without their spouse joining in the guaranty since all assets and earnings acquired during a marriage are marital assets regardless of how assets may be titled. The individual guaranty of one spouse does little to demonstrate or procure the capacity and willingness of the guarantor to perform his or her obligations. The individual guaranty of a married business owner often has little practical value because the assets demonstrating the quality and strength of the guaranty are part of a marital estate and cannot be placed in peril by one spouse acting alone. Thus, the requirement of a non-owner spousal guaranty has little to do with outdated stereotypes based on gender or marital status and everything to do with sound underwriting analysis and obtaining maximum credit support for a commercial loan. In fact, the June 28, 1973 Senate Report acknowledged as much when it observed that "[i]f an applicant does not have and control his or her *own* income or assets which can clearly be used as a source of repayment, denial of credit would be based on proper credit criteria and the concept of discrimination would be inapplicable." S. Rep. 93-278 at 19 (1973) (emphasis in original).[7]

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[7] Of note, the legislative history of the ECOA focused entirely on protecting applicants as individuals applying for credit, not protecting guarantors.

C. *Signatures from spouses for commercial loans are frequently obtained not because of any discriminatory "marital status" animus toward the borrower or guarantor / owner but because marital assets may provide the sole basis for ascribing "value" to their guaranties.*

Lenders can obtain guaranties from the individual owners of a corporate borrower without even potentially running afoul of the ECOA. But where the business owner is married, the lender faces significant risks in either proceeding to make the loan without a spousal guaranty (in which case the owner-spouse's guaranty is probably worthless) or in obtaining the non-owner spouse's guaranty (which may result in Regulation B litigation if the lender is forced to pursue the guaranty). Permitting the spouses of the corporate owners to challenge the validity of their guaranties under the ECOA contradicts the very common sense reasons why lenders can (and should) obtain these spousal guaranties.

Recognizing the important role individual owners play in the operation of an entity, the Regulations expressly permit a lender to obtain guaranties from corporate owners and officers without fear of violating the ECOA. Official Staff Interpretations at Paragraph 202.7(d)(1), Comment 3, as amended by 68 Fed. Reg. 13,144, 13,191 (2003). The FDIC echoes this interpretation in its guidance letters to the banking industry. FDIC FIL-6-2004 – Guidance on Regulation B Spousal Signature Requirements.[8] Similarly, where the applicant requests credit but relies on the income

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[8] https://www.fdic.gov/news/news/financial/2004/fil0604a.html.

of another person (including a spouse) the signature of the other person on a credit instrument may be required to make the income available to pay the debt. 12 C.F.R. Part 202, ECOA (Reg. B), Supplement I to Part 202 – Official Staff Interpretations, § 202.7 ¶7(d)(2). Under these interpretations, where a spouse is also an owner of the corporate borrower, there is no Regulation B violation at all if the lender obtains a guaranty from the co-owner spouse.

As discussed above, in the case of a closely-held business, the owner's individual guaranty reinforces the owner's commitment to support the entity receiving financing. The reinforcement occurs, typically, through two methods (1) a source of capital and liquidity to the corporate borrower; and (2) an incentive for the owners to provide continued management and expertise. Because a central purpose of incorporating an entity to transact business is to protect personal, individual assets, the importance of guaranties from corporate owners is that they provide assurances to the lender that the owners will be personally responsible if the entity fails and the business's assets do not provide sufficient value to repay the loan. The guaranty makes those personal assets available to the lender as a source of repayment. That otherwise sensible trade-off becomes undeniably inequitable if the corporate owner's jointly-owned, marital assets can be put "off limits" because the lender cannot obtain a guaranty from the spouse because doing so would allegedly violate Regulation B. If a lender cannot obtain a guaranty of business debt from a non-owner spouse, then the lender runs the risk that the borrower entity will dissolve and the lender will have little or no effective recourse against a guarantor whose joint

assets are exempt from an individual judgment. *See* Leslie A. Kulik, *Guaranteeing Credit for Others; the Federal Reserve Board's "Regulation B" Requires Amendment*, 67 J. Mo. Bar. 224, 227 (2011) (noting that under Regulation B, "requiring the spousal guaranty is prohibited, even if the spouse partakes of the enjoyment of the profits of the business and even if there are joint assets that appear in the owner-spouse's financial statements.")

In most circumstances, corporate owners who are married attempt to establish the "value" of their personal guaranty by submitting joint financial statements showing most (if not all) assets to be jointly owned. A guaranty signed by only one spouse cannot be evaluated and underwritten on this basis. A paradox in the official interpretations shows that a lender *is* permitted to consider the marital status of an applicant when evaluating "rights and remedies" applicable to the particular extension of credit – giving the example of a secured transaction involving real property and the necessity of considering whether the applicant's spouse would have an interest in the property (and, if so, the necessity of a spousal signature to secure the transaction). Supp. I, Official Staff Interpretation, ¶ 6(b)(8). Similarly, when evaluating the strength of a guaranty, the lender must consider how the guarantor's marital status affects the guaranty's value. To prohibit such analysis – as Regulation B purports to do – defies logic.

If Regulation B prohibits the lender from obtaining a guaranty from the non-owner spouse, then married guarantors will in most instances never be able to provide evidence of sufficient, individually-owned

property to satisfy the lender's requirement of the necessary value to support the guaranty. The FDIC recognizes this very practical consideration and, in its interpretative letters, states as follows:

> Some states' property laws treat married applicants differently from unmarried applicants in a way that affects their creditworthiness. For example, several states provide that real property and/or personal property acquired by married persons jointly is owned as tenants by the entirety[.] In such states, if state law so provides, a creditor could require the signature of the non-applicant spouse . . . where the creditor relies upon real property and/or personal property owned by the applicant and the applicant's spouse as tenants by the entirety in order to qualify the applicant for the loan.

FIL-6-2004. This instruction emphasizes two things: (1) the legitimate, non-discriminatory reasons for obtaining a spousal guaranty; and (2) the unworkable analysis if the word "guarantor" is substituted for "applicant".

By acknowledging a broad category of circumstances where a spousal signature legitimately may be required, the FDIC recognizes multiple scenarios where the requirement of a spousal signature to a note, guaranty or security agreement has appropriate and non-discriminatory purposes. The same is true where an owner/guarantor purports to show the value of a guaranty by relying on jointly-owned assets. Particularly, in tenancy by the entirety states, such as Missouri (whose law governs in the general the loans at issue in this case) the spouse's guaranty becomes

necessary not because of antiquated stereotypes involving gender or marital status, but because of state property laws and the inability to look to jointly-owned property to underwrite a guaranty without the spouse's guaranty. *See e.g. Blakewell v. Breitenstein*, 396 S.W.3d 406, 412 (Mo. Ct. App. 2013).

In addition to highlighting that there is no discriminatory intent necessarily attendant with many instances of obtaining spousal guaranties, the FDIC's instruction further underscores the difficulty associated with extending "applicant" status to guarantors. The guideline speaks of different ways in which state laws treat the property of married applicants versus unmarried applicants, noting the difference because such discrepancies impact the applicant's "creditworthiness". FIL-6-2004. In the context of guarantors, Regulation B provides no clarity regarding the underwriting of married guarantors to assure that the guaranty is creditworthy. As discussed above, lenders do not evaluate the prospects of a commercial loan based on the guarantor's creditworthiness. Instead, the loan will be underwritten based on the *borrower's* creditworthiness, not the guarantor's.

A guaranty is a secondary repayment source and the strength of a guaranty is separately evaluated from the credit analysis of the applicant. Additionally, the FDIC guidelines refer to the circumstance where the jointly-owned property forms the basis for the "applicant" qualifying for the loan. But in the guarantor context, the guarantor is not the individual applying for a loan. The guarantor's financial strength factors into whether the guarantor will provide a

secondary source of repayment in the event of the borrower's default and also to incentivize the borrower's and the owner/guarantor's willingness to repay and to stay engaged in the business enterprise.

Prudent credit standards typically require the personal guaranty of the business owner for a commercial loan. In this regard the incongruity of Regulation B is revealed in 12 C.F.R. § 202.7(d)(5) because it prohibits a lender from "requiring" the spouse of a married guarantor to be an "additional party" to a personal guaranty. As noted previously, a married owner's guaranty is of dubious value unless it is joined with the spouse's guaranty since all property and assets acquired in a marriage are presumed to be marital assets. If only one spouse signs, the guaranty is not effective to serve its intended purposes.

Because lenders seek guaranties to support commercial loans, and because Regulation B permits lenders to obtain individual guaranties from corporate owners without fear of violating the ECOA it makes little sense to deny lenders the ability to obtain a guaranty from the spouse of the corporate owner. This is true because, as demonstrated above, married guarantors rarely have readily identifiable, individually-owned assets sufficient to provide adequate credit support. Married owner/guarantors commonly rely on jointly-owned assets to demonstrate the financial strength of their guaranty. Obtaining a guaranty from a non-owner spouse in such circumstances is not "discrimination" on the basis of marital status stereotypes, but rather a sound lending practice for obtaining an effective and creditworthy guaranty. If guarantors are permitted to raise

discrimination claims under these facts, lenders will face unacceptable litigation risks and will be forced to increase the cost of credit and in some cases deny commercial loans where an owner is married but has inadequate assets to support a guaranty as a secondary repayment source.

II. PERMITTING GUARANTORS TO BRING ECOA CLAIMS WILL EXPOSE LENDERS TO UNWARRANTED, INCREASED RISKS OF LITIGATION COSTS THE RESULTS OF WHICH WILL BE TO EITHER INCREASE THE COST OF CREDIT OR INCENTIVIZE LENDERS TO INCREASE BUSINESS AND COMMERCIAL UNDERWRITING STANDARDS FOR MARRIED BUSINESS OWNERS OR BOTH.

A. Litigation risk and costs associated with lending discrimination claims by a massive class of guarantors represents a significant concern for lenders.

By including guarantors as "applicants" for purposes of 12 C.F.R. § 202.7(d), the Government (previously the Board of Governors and now the CFPB) exposes banks and other creditors to unnecessary litigation risk and costs associated with loans that involve non-owner spousal guarantors. The risks of litigation arising from discrimination claims brought by guarantors raise significant concerns among lenders, including litigation exposure and costs, reputational harm, and the possibility of a guarantor invalidating not only the alleged offending guaranty, but also the underlying loan transaction itself. Additionally, the lender runs the risk that the guarantor will seek money damages (including punitive damages) as part

of the guarantor's lawsuit. *See* 15 U.S.C. § 1691e. Regardless of whether a lender is found to have, in fact, discriminated against a guarantor, the lender will be forced to incur the cost of defending against any and all guarantors' discrimination claims. Defending against an ECOA claim can wipe out a bank's earnings not just of the loan at issue but also the earnings for an entire commercial portfolio.

Of further concern to lenders, court rulings appear to restrict the lenders' ability to document the non-discriminatory nature of the guaranties. Thus, if Regulation B permissibly extends the scope of "applicant" to include spouses of owners who have signed guaranties for commercial loans, a lender may be unable to insulate itself from liability no matter the language used in the guaranties. For example in *Frontenac Bank v. T.R. Hughes, Inc.*, the Missouri Court of Appeals concluded that language in the spouse's guaranties making clear that the spouse had *volunteered* to sign the guaranty (i.e., the lender did not "require" it) was not dispositive of the issue of marital status discrimination. 404 S.W.3d 272, 287-88 (Mo. Ct. App. 2012).

Just as in this case, the guaranties in *Frontenac* Bank stated that "this guaranty is executed at borrower's request and not at the request of the lender[.]" *Id*. at 287. According to the testimony from the non-owner spouse, she only signed what her husband, the owner of the corporate borrower, asked her to sign. *Id*. at 288. The owner spouse testified that, to the contrary, he did not offer the guaranties, but instead they were required by the bank. *Id*. The testimony contradicting the allegedly "involuntary"

nature of the guaranties came *8 years* after the parties signed the guaranties, and was given only in the context of the commercial loans having gone into default, the bank selling the collateral, and then seeking to recover from the guarantors for the deficiencies on the loans. *Id*. at 276-77.

By finding that the trial court could conclude, based on the "evidence," that the guaranties were not voluntarily provided, the Missouri Court of Appeals effectively nullified lenders' ability to document the non-discriminatory basis for a spousal guaranty, and thus to guard against discrimination claims from individuals who signed guaranties so that their spouses' companies could obtain credit. Upholding Regulation B's re-write of the ECOA to include guarantors therefore exposes lenders to litigation risks against which lenders have few, if any, defenses.

B. In the face of increased litigation risk and minimal protections, lenders likely will avoid loans where an owner of a corporate borrower is married, but the spouse is not also a documented owner of the entity.

Perversely, Regulation B's re-write of ECOA results in a married business owner facing different and higher credit thresholds than a single person – a result contrary to the objectives of Congress in enacting the ECOA. A lender evaluating a commercial loan request involving a married owner with jointly owned assets faces, essentially, three options: (1) deny the loan; (2) extend the loan without the non-owner spouse's guaranty; or (3) make the loan, accept the non-owner spouse's guaranty, but face the risk that the non-owner spouse may, at some point in the future, claim the

lender discriminated in accepting the guaranty. Given the litigation and liability risks, making the loan and obtaining a guaranty from the non-owner spouse would be most imprudent. In order to mitigate the risks of proceeding without a spousal guaranty, the lender might increase the fees and costs for the loan (e.g. increase the interest rate), shorten the loan term to provide for the borrower pay off the lender at an accelerated rate to reduce the length and amount of the exposure, or, seek express pledges of collateral, some of which could be marital property which would require the spouse's signature in any event. These alternate options are often unattractive to a borrower, may cause the borrower to reject the loan, and perversely could result in less favorable treatment of a married business owner as compared to an unmarried business owner.

In a lending climate where federal and state regulators press lenders to do everything possible to secure loans, lenders would become understandably fearful and wary of extending loans which would otherwise require a spousal guaranty. As a result, married small business owners face daunting obstacles to obtaining credit. A married business owner could make the non-owner spouse a co-owner of the business. However, this might not be a viable option if there are other investors in the ownership structure of the borrower. Perhaps another option for a married business owner would be to find a third-party willing to invest in the company or provide a guaranty, but even if such a person could be found, it would not solve the problem of the married owner whose financial statement shows only jointly-owned, marital assets that are otherwise unavailable if the lender needs to

enforce the guaranty.[9] Finally, a married owner might volunteer the non-owner, spouse's guaranty (as is often the case), but this presents a significant risk for the lender in the event the loan goes into default (as it did in this case) because the spousal guarantor, contrary to written representations made to induce the extension of credit, may contend the guaranty was the product of "marital status" discrimination (as the spousal guarantors did in this case) or was not given voluntarily (as the spousal guarantors argued in this case).

To the contrary, if non-owner guarantors cannot bring discrimination claims under the ECOA because they are not "applicants," and instead the ECOA is limited to what Congress intended (only those directly applying for credit) then the lender can evaluate the creditworthiness of the borrower, and if guarantor support is warranted then the lender can underwrite the guaranty as secondary loan support without concern that a guaranty agreement provides an unwarranted claim for discrimination several years after the lender makes the loan. Under this framework, if the prospective borrower (as applicant) believes a lender's decision to decline the loan or to extend the loan only on less favorable terms resulted from

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[9] Additionally, it is likely that the married business owner who is required to obtain a third party guaranty because of the lack of non-marital property would claim that such a requirement discriminates based on marital status. Thus the Catch-22 for lenders: either accept a spousal guaranty and face claims of marital status discrimination, or request a third party guaranty (not from the spouse) and face claims that the request for an additional guaranty resulted from marital status discrimination.

discriminatory animus, the borrower/applicant can bring a claim under the ECOA. But it is the borrower's claim to bring, and this posture permits the lender to explain its underwriting analysis and show why the guaranty requirements did not result from discriminatory "marital status" animus but, rather, resulted from legitimate considerations such as state property laws with respect to marital property rights. *See* 12 C.F.R. § 202.6(c). In that scenario, the discrimination analysis becomes similar to the familiar *McDonnell Douglas* burden-shifting framework for employment discrimination.[10] *See McDonnell Douglas Corp. v. Green*, 411 U.S. 792 (1973).

C. By extending the ECOA to non-applicant guarantors, Regulation B exposes lenders to strict liability, effectively imposing on lenders the burden to prove the lack of discrimination.

In addition to providing non-owner guarantors the ability to challenge loan transactions many years after the loan has been approved and extended to the corporate borrower, Regulation B imposes near strict, or *per se,* liability for discrimination in any context where the lender obtains a non-applicant spouse's guaranty, unless the lender can satisfy the heavy and costly burden of proving non-discrimination. In *RL BB Acquisition, LLC v. Bridgemill Commons Development*

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[10] The ECOA plaintiff would have to first establish a *prima facie* case of discrimination e.g. (1) that the applicant is a member of a protected class; (2) the applicant qualified for the loan under the lender's standards of creditworthiness; and (3) the lender denied the loan or extended the loan but on more onerous or less favorable terms that applicants from a non-protected class.

Group, LLC, the Sixth Circuit illustrated this approach, declaring that Regulation B prohibits "'requir[ing]' the guaranty of a spouse as a general matter, *regardless of whether the creditor's motivation is benign or invidious*." 754 F.3d 380, 389 (6th Cir. 2014) (emphasis added). Therefore, according to the Sixth Circuit, the plaintiff guarantors "do not need to prove discrimination". *Id*. Instead, the guarantor only needs prove that the "spouse applied for credit and either the creditor 'require[d] the signature of [the] applicant's spouse' if the applicant was individually creditworthy . . . or the creditor 'require[d] that the spouse be the additional party' when it determined that the applicant was not independently creditworthy and would need the support of an additional party." *Id*. Again, the error is in not recognizing that underwriting a guaranty is separate from and not the same as underwriting the commercial loan applicant.

These putative elements highlight the reasons why extending "applicant" status to guarantors becomes problematic as discussed above. The first element articulated in *RL BB Acquisition* refers to when a spouse "applied for credit" but in the guarantor context, the guarantor *never* applies for credit. The element proceeds to focus on situations where the applicant was "individually creditworthy" even though the lender evaluating a corporate loan is not evaluating the creditworthiness of the *guarantor*. Thus, the Sixth Circuit's erroneous decision further demonstrates why including guarantors as "applicants" for the purpose of spousal signature provisions strains the ECOA beyond all reason.

Furthermore, the Sixth Circuit's and the Government's approach shifts the full burden of proving the *absence* of discrimination to the lender. Under the provisions of Regulation B, if a lender obtains a guaranty of a corporate loan from the spouse of an owner, the guaranty by the non-owner spouse is *presumed* to be discriminatory. *See* 12 C.F.R. § 202.7(d)(1). And in accepting the guaranty from the non-owner spouse, the lender likewise accepts the risks that if the borrower becomes unable to repay the debt, then the non-owner guarantors may claim the guaranties were discriminatory and seek to undo not only the guaranty, but also the full underlying loan transaction *and* seek money damages including punitive damages.[11]

This case clearly demonstrates the risk facing lenders who choose to make loans which include obtaining non-owner spousal guaranties. Here, a company owned by Petitioners' husbands obtained several loans from Respondent over the course of a multi-year relationship. Several times, CBR obtained guaranties from the owner-husbands as well as from the Petitioners, and each time Petitioners promised to

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[11] The Government argues that potential remedies for ECOA violations should not factor into the analysis of whether the federal agencies permissibly expanded the definition of "applicant" to include guarantors, but only for purposes of § 202.7(d). U.S. Br. at 34. Far from being irrelevant, the potential remedial implications of obtaining a non-owner spousal guaranty illustrate the risks lenders face when considering whether to obtain all the documentation necessary to make a safe and secure loan in light of the risk that doing so may ultimately require the lender to prove, through costly litigation, the absence of discrimination against the non-owner spouse.

repay the corporate borrower's indebtedness in the event of default.[12] Seven years later, after the borrower had defaulted on the loan and was unable to repay the indebtedness, the Petitioners asserted for the first time that they were the victims of marital status discrimination each and every time they signed a personal guaranty.

Strikingly, Petitioners made no allegation that the owner spouses were individually creditworthy for the loan being requested by the corporate borrower. Granting Petitioners a cause of action under the ECOA based on these facts would demonstrate why Regulation B impermissibly expands the definition of "applicant" to a category of persons for whom Congress did not intend to provide protection under the ECOA.

III. LENDERS WILL NOT BE AUTHORIZED TO DISCRIMINATE AGAINST BORROWERS ON A PROHIBITED BASIS IF THE ECOA DEFINITION OF "APPLICANT" DOES NOT INCLUDE GUARANTORS.

Contrary to the arguments of Petitioners and the Government, excluding guarantors from the definition of "applicant" will not lead to widespread, illegal discrimination by lenders against borrowers. When Congress first enacted the ECOA, no part of the

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[12] Petitioners repeatedly and mistakenly assert that guaranty agreements placed the Petitioners in the same position as if they had co-signed the promissory notes. *See e.g.* Pet. Br. at 34. This inaccurately describes guaranty agreements. Instead, as the Government correctly sets forth, a guaranty agreement is one in which a party assumes secondary liability for a debt obligation in the event the primary obligor defaults. Gov. Br. at 4.

legislative history focused on any need to protect non-owner spouses who were asked to guarantee loans obtained by entities in which the other spouse was either an owner or co-owner. Interpreting the ECOA's definition of "applicant" consistent with the statute's plain language will not permit wanton and illegal discrimination by lenders. In fact, the position taken by both Petitioners and the Government places married business owners at a disadvantage compared to non-married owners.

As both Petitioners and the Government acknowledge, Congress' purpose in enacting the ECOA was to make credit available to all creditworthy applicants without regard to the applicant's gender or marital status. Pet. Br. at 21-22; Gov. Br. at 2. However, Petitioners and the Government gloss over Congress' very specific definition of "applicant" and proceed to try and justify Regulation B without even addressing the fact that the language of the ECOA expressly defines "applicant" as one who *directly* applies for credit or indirectly applies under an existing credit plan for an amount in excess of previously established credit limits. 15 U.S.C. § 1691a(b). The Government only references this definitional constraint in passing and simply asserts, in conclusory fashion, that "[g]uarantors . . . apply for credit 'directly'". U.S. Brief at 19 n.7. Notably, the Government never explains *how* guarantors apply "directly" for credit.

The Government also suggests that the language of the ECOA should be read to provide non-owner spouses who guarantee the business debts of their spouse's company a cause of action for discrimination, but none of the Government's arguments satisfactorily establish

how such causes of action are consistent with the central purpose of the ECOA. In passing the ECOA, Congress focused on eradicating credit discrimination against women, particularly married women, who traditionally experienced challenges in obtaining individual credit. *Anderson v. United Fin. Co.*, 666 F.2d 1274, 1277 (9th Cir. 1982). The discrimination women suffered from lenders took the form of the inability to receive individual credit on the same or similar terms that men, including married men, received. *Rowe v. Union Planters Bank of S.E. Mo.*, 289 F.3d 533, 535 (8th Cir. 2002). Thus, a woman could prove a claim of lending discrimination under the ECOA by showing that she was qualified for the loan but that the lender refused to extend the loan despite her qualifications or that the lender required additional terms (such as co-signature by husband) that the lender did not require if the borrower was a man. *Rowe*, 289 F.3d at 535.

The language in the ECOA was deliberately chosen and appropriately reflects Congress' intent to protect women who "applied" "directly" for credit, without extending the ECOA to all persons involved, in any way, in a credit transaction. Giving effect to the plain language of the ECOA's definition of "applicant" will not permit lenders to discriminate against an applicant who applies for a loan based on that person's gender or marital status. If a woman applies for a personal, or commercial loan from a bank and she meets the lender's requirements for creditworthiness, she will receive that loan on the same basis as if her spouse had been the applicant and met the same requirements. Her right to receive credit without discrimination can be protected by giving her a cause of action against the lender under the ECOA. Her rights are not protected,

however, by providing her husband with a cause of action to contend his joint-guaranty, if obtained, is discriminatory.

In the case where a women-owned business attempts to receive a loan, but the lender refuses to provide the loan based on the fact that women own the borrower, the ECOA would provide the business itself with a cause of action for discriminatory lending.[13] It is conceivable that an entity received discriminatory treatment because its women owners were required to obtain their husbands' guaranty of the debt whereas businesses owned by men did not have to satisfy such a requirement under similar circumstances. In both those circumstances, however, the cause of action under the language of the ECOA belongs to the borrower – the "applicant". Permitting the husband-guarantors to bring a claim under the ECOA, based on this hypothetical, would do nothing to further the anti-discrimination purposes of the statute. *See Champion Bank*, 2009 WL 1351122 at *3 (noting that stretching the ECOA's protections to a non-owner, guarantor spouse "expands the ECOA beyond its intended purpose"). Expanding the class of "applicants" would, however, have significant consequences for both lenders and borrowers as explained previously.

Petitioners' and the Government's overreaching becomes more apparent if one considers a hypothetical

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[13] The Government acknowledges that such a business entity would be able to bring an ECOA claim, even though it is a corporate entity. U.S. Br. at 28 n. 14. Petitioners' argument that such a claim would not be recognized is flatly, incorrect. Pet. Br. at 29-30.

situation where a non-owner spouse *declines* to sign a guaranty and the lender refuses, therefore, to make a loan to the corporate borrower. Would any purpose of the ECOA be furthered by permitting the non-owner spouse to bring a cause of action for discrimination under the ECOA where the non-owner spouse did not apply for a loan, did not sign a guaranty, and was not denied a loan? Against whom was the discrimination? And what are the damages?

Yet under the language of the spousal signature provisions in Regulation B the infraction occurs when the lender required the additional party's signature, and Regulation B does not differentiate between whether the additional party actually signed the document or not. If it makes little sense to provide the non-owner spouse with a cause of action if she *declines* to sign the guaranty, it also makes little sense to provide the non-owner spouse with an ECOA cause of action if she *does* sign the guaranty.[14] This is true because the person who would have a claim in both circumstances would be the borrower/applicant who was either denied the loan because the spouse refused to guaranty the debt, or who received the loan but only because the spouse agreed to guaranty the debt where such guaranty would not otherwise have been required.

Petitioners incorrectly suggest that no remedy exists for discrimination if the ECOA does not provide

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[14] Indeed the Eighth Circuit noted the internal inconsistency in reading the ECOA (designed to protect women from being excluded from credit) to recognize a claim by non-owner spouse who alleges discrimination precisely because she was *included* in a loan transaction. *Hawkins v. Cmty. Bank of Raymore*, 761 F.3d 937, 942 (8th Cir. 2014).

a cause of action to non-owner spousal guarantors. That is simply not true. Based on the facts of this case, an ECOA claim could have been brought by the borrower, PHC Development, LLC. Pet. Br. at 2. If, in fact, PHC received less-favorable loan terms because of the alleged requirement of guaranties from non-owner spouses, then the ECOA afforded PHC a cause of action. At the very least, PHC's owners could have pursued such a claim arguing that the lender discriminated against their company by denying a loan without the additional party guaranties. These would be the parties that ostensibly suffered from putative discrimination.

Identifying proper plaintiffs under the ECOA as only those persons or entities that applied for credit (and excluding guarantors) would not alter or reduce the ability of PHC to assert discrimination claims. Rather, the only claim that would be excluded would be a claim of discrimination by a non-owner spouse who, as is alleged in this case, had no ownership interest or role in the corporate borrower (even though non-owner spouses made contrary representations in their guaranties). Pet. Br. at 2. Nothing in the legislative history of the ECOA suggests that Congress sought to provide such non-owner spousal guarantors with a cause of action alleging lending discrimination. And as demonstrated previously, extending the ECOA to non-owner guarantors may have the ironic result of disadvantaging married business owners who seek credit – a perversion of the ECOA that Congress did not intend.

CONCLUSION

For the reasons set forth above, the *Amici* support Respondent Community Bank of Raymore in its request that this Court to affirm the Eighth Circuit.

Respectfully submitted,

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