

Appendices

Compliance Management Analysis Checklist

This checklist is for use in conjunction with Part II of these procedures as a device for evaluating the quality of preventive and corrective measures, identifying worthwhile innovations and offering suggestions for improvement. The checklist is not, however, intended to be an absolute test of a lender’s compliance management program. Lender programs containing all or most of the features described in the list may nonetheless be flawed for other reasons; conversely, a compliance program which encompasses only a portion of the factors listed below may nonetheless adequately support a strong program under appropriate circumstances. In short, the examiner must exercise his or her best judgment in utilizing this list and in assessing the overall quality of a lender’s efforts to ensure fair lending compliance.

If the transactions within the proposed scope are covered by a listed self-compliance measure, check the box in the left

column. Reduce the intensity (mainly the sample size) of the planned comparative file review to the degree that the self-compliance measures cover transactions within the proposed scope. Document your findings in sufficient detail to justify any resulting reduction in the intensity of the examination.

You are not required to learn whether self-compliance measures apply to specific products outside the proposed scope. However, if the information you have obtained shows that the self-compliance measure is a general practice of the lender, check the box in the second column in order to assist future examination planning.

Preventive Measures

Determine whether policies and procedures exists that tend to prevent illegal disparate treatment in the transactions you plan to examine. There is no legal or agency requirement for institutions to conduct these activities. The absence of any of these policies and practices is never, by itself, a violation.

1. Lending Practices and Standards		
	Within the proposed scope	Lender-wide
a. Principal policy issues:		
1. Are underwriting practices clear and similar to industry standards?		
2. Is pricing within reasonably confined ranges with guidance linking variations to risk and/or cost factors?		
3. Does management monitor the nature and frequency of exceptions to its standards?		
4. Are denial reasons accurately and promptly communicated to unsuccessful applicants? <i>Note:</i> The items above are not compliance measures, but they are fundamental features of lending that tend to work against disparate treatment.		
b. Do training, application-processing aids, and other guidance correctly and adequately describe:		
1. Prohibited bases under ECOA, Regulation B, and the Fair Housing Act?		
2. Other substantive credit access requirements of Regulation B (e.g. spousal signatures, improper inquiries, protected income)?		
c. Is it specifically communicated to employees that they must not, on a prohibited basis:		
1. Refuse to deal with individuals inquiring about credit?		
2. Discourage inquiries or applicants by delays, discourtesy, or other means?		

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	Within the proposed scope	Lender-wide
3. Provide different, incomplete, or misleading information about the availability of loans, application requirements, and processing and approval standards or procedures (including selectively informing applicants about certain loan products while failing to inform them of alternatives)?		
4. Encourage or more vigorously assist only certain inquirers or applicants?		
5. Refer credit seekers to other lenders?		
6. Waive or grant exceptions to application procedures or credit standards?		
7. State a willingness to negotiate?		
8. Use different procedures or standards to evaluate applications?		
9. Use different procedures to obtain and evaluate appraisals?		
10. Provide certain applicants opportunities to correct or explain adverse or inadequate information, or to provide additional information?		
11. Accept alternative proofs of creditworthiness?		
12. Require co-signers?		
13. Offer or authorize loan modifications?		
14. Suggest or permit loan assumptions?		
15. Impose late charges, reinstatement fees, etc.?		
16. Initiate collection or foreclosure?		
d. Has the institution taken specific initiatives to prevent forms of unintentional discrimination, including:		
1. Basing credit decisions on assumptions derived from racial, gender, and other stereotypes, rather than facts?		
2. Seeking customers from a particular racial, ethnic, or religious group, or of a particular gender, to the exclusion of other types of customers, on the basis of how “comfortable” the employee may feel in dealing with those different from him/her?		
3. Because of their discomfort or unease in dealing with customers from certain racial, ethnic, or religious groups, or of a certain gender, limiting the exchange of credit-related information or their effort to qualify the applicant?		
4. Is the institution’s CRA assessment area drawn without unreasonably excluding minority areas?		

	Within the proposed scope	Lender- wide
e. Does the institution have procedures to ensure that it does not:		
1. State racial or ethnic limitations in advertisements?		
2. Employ code words in advertisements that convey racial or ethnic limitations?		
3. Place advertisement that a reasonable person would regard as indicating minority customers are less desirable?		
4. Advertise only in media serving non-minority areas of the market?		
5. Conduct other forms of marketing only in non-minority areas of the market?		
6. Market only through brokers known to serve only one racial or ethnic group in the market?		
7. Use a prohibited basis in any pre-screened solicitation?		

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2. Compliance Audit Function: Does the Bank Attempt to Detect Prohibited Disparate Treatment by Self-Test or Self-Evaluation?

Note: A self-test is any program, practice or study that is designed and specifically used to assess the institution’s compliance with the ECOA and the Fair Housing Act statute or regulation and creates data or factual information that is not otherwise available and cannot be derived from loan, application or other records related to credit transactions (12 CFR 202.15(b)(1) and (24 CFR 100.141). The report, results, and many other records associated with a self-test are privileged unless an institution voluntarily discloses the report or results or otherwise forfeits the privilege. See 12 CFR 202.15(b)(2) and 24 CFR 100.142(a) for a complete listing of the types of information covered by the privilege. A self-evaluation, while generally having the same purpose as a self-test, does not create any new data or factual information, but uses data readily available in loan or application files and other records used in credit transactions and, therefore, does not meet the self-test definition. See Streamlining the Examination in this **Job Aids** for more information about self-tests and self-evaluations.

While you may request the results of self-evaluations, you should not request the results of self-tests or any of the information listed in 12 CFR 202.15(b)(2) and 24 CFR 100.142(a). If an institution discloses the self-test report or results to its regulator, it will lose the privilege. The following items are intended to obtain information about the bank’s approach to self-testing and self-evaluation, not the findings. Complete the checklist below for each self-evaluation and each self-test, where the institution voluntarily discloses the report or results. Evaluating the results of self-evaluations and voluntarily disclosed self-tests is described in **Streamlining the Examination** in the **Appendix**.

Mark the box if the answer is “yes” for the transactions within the scope.

	Within the proposed scope	Lender- wide
a. Are the transactions reviewed by an independent analyst who:		
1. Is directed to report objective results?		
2. Has an adequate level of expertise?		
3. Produces written conclusions?		
b. Does the bank’s approach for self-testing or self-evaluation call for:		
1. Attempting to explain major patterns shown in the HMDA or other loan data?		
2. Determining whether actual practices and standards differ from stated ones and basing the evaluation on the actual practices?		
3. Evaluating whether the reasons cited for denial are supported by facts relied on by the decision maker at the time of the decision?		
4. Comparing the treatment of prohibited basis group applicants to control group applicants?		
5. Obtaining explanations from decision makers for any unfavorable treatment of the prohibited basis group that departed from policy or customary practice?		
6. Covering significant decision points in the loan process where disparate treatment or discouragement might occur, including:		
The approve/deny decision?		
Pricing?		
Other terms and conditions?		

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	Within the proposed scope	Lender-wide
7. Covering at least as many transactions as examiners would independently, if using the Fair Lending Sample Size Tables for a product with the application volumes of the product to be evaluated?		
8. Maintaining information concerning personal characteristics collected as part of a self-test separately from application or loan files?		
9. Timely analysis of the data?		
10. Taking appropriate and timely corrective action?		
c. In the bank's plan for comparing the treatment of prohibited basis group applicants with that of control group applicants:		
1. Are control and prohibited basis groups based on a prohibited basis found in ECOA or the FHAAct and defined clearly to isolate that prohibited basis for analysis?		
2. Are appropriate data to be obtained to document treatment of applicants and the relative qualifications vis-à-vis the requirement in question?		
3. Are the data to be obtained the data on which decisions were based, not later or irrelevant information?		
4. Does the plan call for comparing the denied applicants' qualifications related to the stated reason for denial with the corresponding qualifications for approved applicants?		
5. Are comparisons designed to identify instances in which prohibited basis group applicants were treated less favorably than control group applicants who were no better qualified?		
6. Is the evaluation designed to determine whether control and prohibited basis group applicants were treated differently in the processes by which the bank helped applicants overcome obstacles and by which their qualifications were enhanced?		
7. Are responses and explanations to be obtained for any apparent disparate treatment on a prohibited basis or other apparent violations of credit rights?		
8. Are reasons cited by credit decision makers to justify or explain instances of apparent disparate treatment to be verified?		
d. For self-tests under ECOA that involved the collection of applicant personal characteristics, did the institution:		
1. Develop a written plan that describes or identifies the:		
specific purpose of the self-test?		
methodology to be used?		

	Within the proposed scope	Lender- wide
geographic area(s) to be covered?		
type(s) of credit transactions to be reviewed?		
entity that will conduct the test and analyze the data?		
timing of the test, including start and end dates or the duration of the self-test?		
other related self-test data that is not privileged?		
2. Disclose at the time applicant characteristic information is requested, that:		
the applicant will not be required to provide the information?		
the creditor is requesting the information to monitor its compliance with ECOA?		
federal law prohibits the creditor from discriminating on the basis of this information or on the basis of an applicant's decision not to furnish the information?		
if applicable, certain information will be collected based on visual observation or name if not provided by the applicant?		

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3. Correcting Discriminatory Conduct		
	Within the proposed scope	Lender- wide
a. Determine whether the lender has provisions to take appropriate corrective action and provide adequate relief to victims for any violations in the transactions you plan to review.		
1. Who is to receive the results of a self-evaluation or voluntarily disclosed self-test?		
2. What decision process is supposed to follow delivery of the information?		
3. Is feedback to be given to staff whose actions are reviewed?		
4.. What types of corrective action may occur?		
5. Are customers to be:		
Offered credit if they were improperly denied?		
Compensated for any damages, both out of pocket and compensatory?		
Notified of their legal rights?		
b. Other corrective action:		
1. Are institutional policies or procedures that may have contributed to the discrimination to be corrected?		
2. Are employees involved to be trained and/or disciplined?		
3. Is the need for community outreach programs and/or changes in marketing strategy or loan products to better serve minority segments of the lender's market to be considered?		
4. Are audit and oversight systems to be improved in order to ensure there is not recurrence of any identified discrimination?		

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Credit Scoring Analysis

These procedures are intended to assist an examiner in arriving at supportable conclusions with respect to an institution's record of non-discrimination when the Focal Point involves a product for which the institution uses automated underwriting or when credit scoring risk factors make such a product the Focal Point.

A. Structure and Organization of the Scoring System

Determine the utilization of credit scoring at the institution, including

1. For each customized credit scoring model or scorecard for any product, or for any credit scoring model used in connection with a product held in portfolio, identify:
 - a. the number and inter-relationship of each model or card applied to a particular product;
 - b. the purposes for which each card is employed (e.g., approval decision, set credit limits, set pricing, determine processing requirements, etc.);
 - c. the developer of each card used (e.g., in-house department, affiliate, independent vendor name) and describe the development population utilized;
 - d. the types of monitoring reports generated (including front-end, back-end, account management and any disparate impact analyses), the frequency of generation and recent copies of each;
 - e. all policies applicable to the use of credit scoring;
 - f. training materials and programs on credit scoring for employees, agents and brokers involved in any aspect of retail lending;
 - g. any action taken to revalidate or re-calibrate any model or scorecard used during the exam period and the reason(s) why;
 - h. the number of all high-side and low-side overrides for each type of override occurring during the exam period and any guidance given to employees on their ability to override;
 - i. all cutoffs used for each scorecard throughout the examination period and the reasons for any change made during the exam period;
 - j. all variables scored by each product's scorecard(s) and the values that each variable may take; and
 - k. the method used to select for disclosure those adverse action reasons arising from application of the model or scorecard.
2. For each judgmental underwriting system that includes as an underwriting criterion a standard credit bureau or secondary market credit score identify:

- a. the vendor of each credit score and any vendor recommendation or guidance on the usage of the score relied upon by the institution;
- b. the institution's basis for using the particular bureau or secondary market score and the cutoff standards for each product's underwriting system and the reasons for any changes to the same during the exam period;
- c. the number of exceptions or overrides made to the credit score component of the underwriting criteria and the basis for those exceptions or overrides, including any guidance given to employees on their ability to depart from credit score underwriting standards, and;
- d. types of monitoring reports generated on the judgmental system or its credit scoring component (including front-end, back-end, differential processing and disparate impact analysis), the frequency of generation and recent copies of each.

B. Adverse Action Disclosure Notices

Determine the methodology used to select the reasons why adverse action was taken on a credit application denied on the basis of the applicant's credit score. Compare the methodology used to the examples recited in the Commentary to Regulation B and decide acceptability against that standard. Identify any consumer requests for reconsideration of credit score denial reasons and review the action taken by management for consistency across applicant groups.

Where a credit score is used to differentiate application processing, and an applicant is denied for failure to attain a judgmental underwriting standard that would not be applied if the applicant had received a better credit score (thereby being considered in a different—presumably less stringent application processing group), ensure that the adverse action notice also discloses the bases on which the applicant failed to attain the credit score required for consideration in the less stringent processing group.

C. Disparate Treatment in the Application of Credit Scoring Programs

1. Determine what controls and policies management has implemented to ensure that the institution's credit scoring models or credit score criteria are not applied in a discriminatory manner; in particular:
 - a. Examine institution guidance on using the credit scoring system, on handling overrides and on processing applicants and how well that guidance is understood and observed by the targeted employees and monitored for compliance by management.
 - b. Examine institution policies that permit overrides or that provide for different processing or underwriting requirements based on **geographic identifiers** or

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borrower score ranges to assure that they do not treat protected group applicants differently than other similarly situated applicants.

2. Evaluate whether any of the bases for granting credit to control group applicants who are low-side overrides are applicable to any prohibited basis denials whose credit score was equal to or greater than the lowest score among the low-side overrides. If such cases are identified, obtain and evaluate management's reason for why such different treatment is not a fair lending violation.
3. Evaluate whether any of the bases for denying credit to any prohibited basis applicants who are high side overrides are applicable to any control group approvals whose credit score was equal to or less than the highest score among the prohibited basis high-side overrides. If such cases are identified, obtain and evaluate management's reason for why such different treatment is not a fair lending violation.
4. If credit scores are used to segment applicants into groups that receive different processing or are required to meet additional underwriting requirements (e.g., "tiered risk underwriting"), perform a comparative file review, or confirm the results and adequacy of management's comparative file review, that evaluates whether all applicants within each group are treated equally.

D. Credit Scoring Systems that Include Age

Regulation B does not require initial validation or periodic revalidation of a credit scoring system unless it considers age. There are two ways a credit scoring system can consider age: 1) the system can be split into different scorecards depending on the age of the applicant; and 2) age may be directly scored as a variable. Both features may be present in some systems. Regulation B requires that all credit scoring systems that consider age in either of these ways must be validated (in the language of the regulation, empirically derived, demonstrably and statistically sound (EDDSS)).

1. **Age-Split Scorecards:** If a system is split into only two cards and one card covers a wide age range that encompasses elderly applicants (applicants 62 or older), the system is treated as considering, but not scoring, age. Typically, the younger scorecard in an age-split system is used for applicants under a specific age between 25 and 30. It de-emphasizes factors such as the number of trade lines and the length of employment, and increases the negative weight of any derogatory information on the credit report. Systems such as these do not raise the issue of assigning a negative factor or value to the age of an elderly applicant. However, if age is directly scored as a variable (whether or not the system is age-split), or if elderly applicants are included in a card with a narrow age range in an age-split system, the system is treated as scoring age.
2. **Scorecards that Score Age:** If a scorecard scores age directly, in addition to meeting the EDDSS requirement, the creditor must ensure that the age of an elderly applicant is not assigned a negative factor or value. (*See* the staff commentary about 12 CFR 202.2(p) and 202.6(b)(2)). A negative factor or value means utilizing a factor, value, or weight that is less favorable than the creditor's experience warrants or is less favorable than the factor, value, or weight assigned to the most favored age group below the age of 62 (12 CFR 202.2(v)).

E. Examination for Empirical Derivation and Statistical Soundness

Regulation B requires credit scoring systems that use age must be EDDSS to be empirically derived, and demonstrably and statistically sound. This means that they must fulfill the requirements of 12 CFR 202.2(p)(1)(i) - (iv). Obtain documentation provided by the developer of the system and consult the agency's most recent guidance for making that determination.