Office of the Comptroller of the Currency
Federal Reserve Board
Federal Deposit Insurance Corporation
Office of Thrift Supervision

May 31, 2001

Joel Winston
Acting Associate Director
Division of Financial Practices
Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, DC 20580

Dear Mr. Winston:

This letter is to follow-up on the April 26th meeting among you, others at the Federal Trade Commission ("FTC"), and staff of the undersigned agencies. At that meeting, our agencies expressed our concerns regarding the July 26, 2000, informal interpretive letter issued by the staff of the FTC ("Tatelbaum Letter") on the application of the Fair Credit Reporting Act ("FCRA") to the extension of business credit. We greatly appreciate your and your staff's willingness to meet with our representatives and to listen to our additional thoughts, as outlined below, regarding the legal and policy concerns raised by the Tatelbaum Letter.

The Tatelbaum Letter addressed whether a lender may lawfully obtain a credit report about an individual who is a principal, owner, or officer of a business loan applicant (such as a sole proprietorship, partnership, or corporation). The Tatelbaum Letter also addressed whether a lender may lawfully obtain a credit report about an individual who signs a personal guarantee in connection with a commercial credit application by a third party.

The Tatelbaum Letter concluded that, in both circumstances, the credit report generally would constitute a "consumer report" subject to the FCRA. The letter also concluded that the lender would not have a permissible purpose under the FCRA to obtain the report, absent the "written instructions" of the consumer.

We agree with the conclusion that credit (or other) reports obtained in both of these situations generally are consumer reports within the meaning of the FCRA. However, after careful review, and for the reasons discussed below, we believe that section 604(a)(3)(A) of the FCRA authorizes lenders to obtain a consumer report in circumstances where the individual is personally liable on business credit, such as in the case of an individual proprietor, co-signer,

or guarantor.[1] Furthermore, we believe that a contrary view, as implied in the Tatelbaum Letter, raises concerns regarding safe and sound lending practices, operational efficiencies, and credit availability. Our interpretation of the FCRA, by contrast, would resolve those concerns in a manner that is fully consistent with the terms and purposes of the FCRA and that promotes prudent lending practices.

LEGAL ANALYSIS

Section 604(a)(3)(A) of the FCRA provides that a consumer reporting agency may furnish a consumer report to a person that it has reason to believe "intends to use the information in connection with a credit transaction involving the consumer on whom the information is to be furnished and involving the extension of credit to, or review or collection of an account of, the consumer." Thus, a lender has a permissible purpose for obtaining a consumer report if it intends to use the report in connection with a credit transaction (1) involving the consumer discussed in the report, and (2) involving the extension of credit to, or the review or collection of an account of, that consumer.

If a consumer is a signatory and party to the transaction, either as legal obligor (in the case of an individual proprietorship) or joint obligor (in the case in which the individual co-signs the loan), then such a credit transaction involves an extension of credit to the consumer who is the subject of the report because that consumer is legally liable for repayment of the credit. The "extension of credit" referenced in section 604(a)(3)(A) is not confined to credit extended for "personal, family, or household" purposes; that limitation is present only in the definition of "consumer report" in section 603(d), and serves to restrict the types of credit reports subject to the FCRA's provisions. In addition, the consumer in these circumstances is a principal of the business that will use the loan proceeds, may be actively involved in the operation of the business, and may have played an important role in initiating and negotiating the credit transaction. Permitting a lender to obtain a consumer report about an individual who is obligated to repay the loan—at the outset of the transaction—is consistent with the purposes of section 604(a)(3)(A), particularly because that section provides that the lender also could obtain such a report subsequently, in connection with the "review" of the account and, ultimately, the "collection of" the debt.

In the case of guarantors, there is also a sound legal basis for concluding that the transaction involves an "extension of credit to . . . the consumer," particularly in view of the fact that this conclusion is fully consistent with the purposes of Section 604 of the FCRA. A guarantor of the credit is obligated on the extension of credit. The statutory purpose of section 604 is to promote the confidentiality of consumer report information by restricting access to those with a legitimate business purpose for obtaining the information. As in the case of

[1] We generally agree that a lender would not have a permissible purpose under section 604(a)(3)(A) of the FCRA to obtain a consumer report on an individual who will not be personally liable for repayment of the credit, such as when the individual is a shareholder, director, or officer of a corporation, but does not guarantee or co-sign the loan, and is not an individual proprietor liable for the loan. We express no views here about the interpretation of section 604(a)(3)(F)(i) of the FCRA stated in the Tatelbaum Letter.

banking laws and regulations relating to insider lending and general lending limits,[2] treating the guarantor as one to whom credit is being extended is fully consistent with this statutory purpose. The guarantor is obligated to repay the loan, and the lender is relying on the creditworthiness of the guarantor, which is precisely why the guarantee was sought. For that reason, the lender has a clearly legitimate reason to obtain the information. Moreover, the guarantor has knowingly become a party to the transaction. These considerations indicate that there is no particularly strong privacy interest at stake that warrants greater protection than that presented in a typical consumer credit transaction.[3]

With respect to existing loans under review or collection, a similar analysis of section 604(a)(3)(A) shows that a lender would have a permissible purpose to obtain a credit report about an individual who has guaranteed, or is otherwise personally obligated to repay, a business loan. As noted above, this section of the FCRA permits a lender to obtain a consumer report if it intends to use the report (1) in connection with a credit transaction involving the consumer described in the report, and (2) involving the "review" of the account and, ultimately, the "collection of" a loan on which the consumer is obligated. By referring to a "credit transaction involving the consumer … and involving … the review or collection of an account of … the consumer," section 604(a)(3)(A) provides a broad conception of the whole "credit transaction" and is not limited strictly to the formation of the loan agreement and disbursement of funds. Rather, that provision encompasses the entire, ongoing relationship between the creditor and obligor. If the consumer is personally obligated to repay the loan, then the lender would be seeking the report in connection with a credit transaction involving the consumer described in the report. With respect to the second requirement, we believe that the plain meaning of the statute permits a lender to obtain a consumer report about a consumer who has guaranteed or otherwise become personally liable on any loan (or loan account) for the purpose of "review or collection of an account of … the consumer."

Finally, we believe that the interpretations delineated above—under which a consumer report may be obtained or used for business credit purposes in certain limited circumstances—is fully consistent with the general provisions and structure of the FCRA. It is notable, for example, that in section 604(a)(3)(A), Congress did not include limiting language parallel to that used in section 603(d): there is *no* requirement in the statutory text that the lender intend to use the credit information in connection with a "personal, family, or household" credit transaction involving the consumer, or an extension of "personal, family, or household" credit to the consumer.

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[2] See 12 U.S.C. § 375b(9)(D)(I); 12 C.F.R. 215.3(a)(7); and 12 C.F.R. 32.2(a). Under each of these provisions, an extension of credit is generally deemed to be made to a guarantor of the credit (as well as to the nominal borrower). This is consistent with the purposes underlying these provisions, which is to limit a bank's credit exposure to particular obligors.

[3] The "bright line" rule that a permissible purpose exists whenever the consumer will be personally liable on the loan also reduces legal uncertainty and, thereby, both operational and compliance burdens. In addition, this rule can be applied relatively easily in the context of consumer credit transactions.

IMPLICATIONS FOR SAFETY AND SOUNDNESS POLICIES AND PRACTICES

Based on the supervisory experiences of our agencies, we believe that financial institutions have developed common practices for extending credit to individual proprietorships, closely-held corporations, and other similar businesses that typically require the individual owners, primary stockholders, or other business principals to become directly liable on, or personally guarantee, the extension of credit. Those practices are important to maintaining prudent lending standards, especially where the businesses themselves may have few resources to support the loans requested.

As discussed below, the interpretation set forth in the Tatelbaum Letter—if it were to be followed in situations where the individual in question is obligated to repay the loan—would raise serious operational difficulties for insured depository institutions supervised by our respective agencies, as well as other lenders for which the FTC has enforcement authority under the FCRA. More important, we believe that the interpretation would raise concerns regarding safe and sound lending practices and credit availability.

Impact on the Credit Underwriting Process. Under the Tatelbaum Letter, a lender would need the written instructions of each of the individuals who becomes obligated on a business loan in order to obtain their credit reports in connection with the extension of credit.[4] As a practical matter, the additional paperwork and operational procedures entailed by such a requirement could significantly impede the ability of banks, thrifts, and other lenders to respond quickly and efficiently to business credit applicants that rely on the creditworthiness of their principals and guarantors. Moreover, we believe that requiring the written instructions of each of the individuals in question would increase the costs of making such loans.

Under ordinary circumstances, a lender receives credit applications from existing and potential small and other business loan customers that require rapid responses, often on the same day. In many cases, not all of the individuals who would become liable on the requested loan (or already be liable on any loan that may be made to the business) will be available on such short notice to provide the authorization that would be necessary for the lender to obtain a credit report. In such circumstances, a lender would confront two unsatisfactory options: either fail to satisfy in a timely manner the legitimate credit needs of its business customers (particularly emerging companies without their own independent credit history), or undertake other, presumably less efficient measures to review fully each individual's creditworthiness in accordance with safe and sound lending practices.

Impact on Evaluating Existing Loan Portfolios. The interpretation stated in the Tatelbaum Letter also would appear to require a lender to receive the written instructions of individual proprietors, guarantors, and co-signers in order to obtain their credit reports in connection with the review or collection of a business loan. Such a requirement would substantially raise the costs of complying with safe and sound lending principles, and would

[4] Similarly, the Tatelbaum Letter would appear to require similar procedures in connection with routine transactions such as credit renewals and refinancings.

have an immediate and significantly adverse impact on loan collection activities and on evaluating existing loan portfolios.

As a general matter, safe and sound lending practices require a creditor to review regularly the quality of its loan portfolio. These reviews necessarily include an assessment of the financial strength of all persons who may be liable on the creditor's loans, including individual proprietors, co-signers, and guarantors. Timely access to credit reports on an individual who may be personally liable on such a loan is essential to this process.[5] The Tatelbaum Letter would create significant impediments to these safe and sound lending practices for existing loan portfolios because lenders may be blocked from obtaining or may encounter severe obstacles in trying to obtain the consent of each of the individuals who may be obligated to pay on numerous loans. Moreover, requiring written authorization to obtain a credit report would interfere with and raise the costs of establishing appropriate loan loss reserves and capital allocations for small and other business loans because lenders would be required to allocate more resources to take the necessary steps to monitor and assess the quality of their loan portfolios.

The obstacles posed by the Tatelbaum Letter for maintaining safe and sound lending practices are aggravated in situations involving loan delinquencies and other events of default. In these cases, it is imperative for the lender to assemble all relevant information in order to assess its options and act promptly to minimize losses. Ascertaining the financial strength and other potential liabilities of all parties who may be liable on a loan, including individual proprietors, co-signers, and guarantors, is integral to this process. Because it is imperative to obtain accurate information quickly, a credit report may serve as the most effective and reliable resource. In the difficult circumstances surrounding an event of default, the problem of obtaining consents that would be required from individual guarantors may be magnified substantially. Moreover, if a lender is unable to obtain a credit report about a guarantor, then its ability to invoke its rights under the guarantee may be limited, and thereby compound the risk of losses on the loan.

CONCLUSION

For the reasons outlined above, we believe that the FCRA would permit a lender to obtain a consumer report in connection with a business credit transaction where the consumer in question is or will be personally liable on the loan, such as in the case of an individual proprietor, co-signer, or guarantor. Under these circumstances, the lender has a permissible purpose to obtain a consumer report about that individual under section 604(a)(3)(A). Our agencies' enforcement policies under the FCRA with respect to the institutions under our jurisdiction will be consistent with this interpretation of the law.

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[5] The lender's ability to obtain credit reports in these circumstances may assist borrowers and guarantors themselves. For example, if a current credit report indicates that a guarantor's financial position remains strong and stable, then a lender may waive or reduce normal requirements for an updated personal financial statement. Similarly, a lender may agree to additional advances under a credit line on the basis of a sound credit report pending the preparation of an updated financial statement (which may require more time and the assistance of an accountant).

We recognize that the legal arguments and policy concerns outlined above may not have been presented to the FTC staff when it issued the Tatelbaum Letter. We appreciate your willingness to consider the important issues raised on the basis of this supplementary information. We further appreciate your willingness to take such actions as may be appropriate to clarify the scope and meaning of the Tatelbaum Letter. Among other things, such actions would help to ensure the application of consistent principles and Federal government enforcement policies to all lenders, and to the credit bureaus on which they rely.

Thank you very much for your attention to these matters.

Very truly yours,

Julie L. Williams
First Senior Deputy Comptroller
and Chief Counsel
Office of the Comptroller of the Currency

J. Virgil Mattingly
General Counsel
Board of Governors of the
Federal Reserve System

William F. Kroener, III
General Counsel
Federal Deposit Insurance Corporation

Carolyn Buck
Chief Counsel
Office of Thrift Supervision