NEW FRONTIERS IN FAIR LENDING: CONFRONTING LENDING DISCRIMINATION AGAINST EX-OFFENDERS

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The dramatic increase in the number of people leaving the nation's prisons and jails has contributed to a renewed interest in safe community reentry strategies. While issues surrounding housing, employment, and recidivism have dominated the scholarly landscape in this area, far less attention has been paid to those collateral consequences which affect ex-offender access to credit and financial services. For example, government financial assistance agencies and the private lenders that participate in government-sponsored lending programs routinely inquire into borrowers' criminal histories, and one federal court has held that criminal exposure bears a direct relationship to creditworthiness. In this Note, the author weaves fair lending principles (as expressed in the Equal Credit Opportunity Act) with the goals of effective reentry policies and argues that despite the possible existence of a correlation between criminal exposure and likelihood of default, the use of criminal history in any determination of creditworthiness should be prohibited or at least curtailed. Given the practice's serious implications for both the ability of individual ex-offenders to reenter society effectively, as well as for the ability of receiving communities to effectuate crime prevention and community development initiatives, the author argues that the federal government ought to take the lead in developing statutory and administrative solutions that effectively fill the "advocacy gap" in credit and financial services where recourse to the courts is not available.

This year alone, over 600,000 individuals will leave prison and return home.[1] It is estimated that, by the year 2010, nearly 1.2 million inmates will be released annually from the nation's prisons and jails.[2]

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[1] *See* TIMOTHY HUGHES & DORIS JAMES WILSON, U.S. DEP'T OF JUSTICE, REENTRY TRENDS IN THE UNITED STATES, http://www.ojp.usdoj.gov/bjs/reentry/reentry.htm (last revised Aug. 20, 2003) (noting that, in 2001, approximately 592,000 prisoners were released). At the end of 2003, a record 6.9 million people in the U.S. (or 1 in 32 adults) were either incarcerated or on probation or parole. *See* LAUREN E. GLAZE & SERI PALLA, PROBATION AND PAROLE IN THE UNITED STATES, 2003, at 1 (2004), http://www.ojp.usdoj.gov/bjs/pub/pdf/ppus03.pdf.

[2] *See* Vincent D. Basile, *A Model for Developing a Reentry Program*, FED. PROBATION, Dec. 2002, at 55. The skyrocketing incarceration rate in America is partly

This projected increase in the number of individuals incarcerated in (and released from) state and federal correctional institutions has contributed to a surge in interest among policy circles relating to the successful and safe reentry of former prisoners and probationers into the communities from which they came. Since at least ninety-five percent of all criminal offenders eventually will return home, reentry has assumed an importance second only to incarceration in its implications for criminal justice policy.

The enduring impact of "criminal exposure"[3] on the post-release experiences of arrested, convicted, and incarcerated individuals has been the subject of intense examination by legal scholars.[4] This current scholarly interest in the "collateral consequences" of criminal exposure primarily focuses on three areas: political participation,[5] employment,[6] and public benefits.[7] This targeted focus on recidivism, disenfranchisement, and unemployment, however, obscures other

attributable to the stiffening of penalties tied to drug-related offenses, including possession and use. Although a critical assessment of these penalties is outside the scope of this Note, the author's opinions about the propriety of certain collateral consequences are informed by the fact that a significant proportion of the people currently held in this nation's jails and prisons are nonviolent drug offenders.

[3] As used in this Note, the term "criminal exposure" refers to any experience of arrest, detention, conviction (resulting in probation or suspended sentences), or incarceration.

[4] *See, e.g.*, JAMIE FELLNER & MARC MAUER, HUMAN RIGHTS WATCH & THE SENTENCING PROJECT, LOSING THE VOTE: THE IMPACT OF FELONY DISENFRANCHISEMENT LAWS IN THE UNITED STATES 2 (1998) (describing disenfranchisement as among "collateral 'civil' consequences" accompanying felony conviction), http://www.naacpldf.org/content/pdf/felon/sentancingproject.pdf; INVISIBLE PUNISHMENT: THE COLLATERAL CONSEQUENCES OF MASS IMPRISONMENT (Marc Mauer & Meda Chesney-Lind eds., 2002) [hereinafter INVISIBLE PUNISHMENT] (compiling perspectives of various authors on effects of mass incarceration on families and communities); PAUL SAMUELS & DEBBIE MUKAMAL, AFTER PRISON: ROADBLOCKS TO REENTRY (2004) (providing comprehensive listing of civil collateral consequences by state), http://www.lac.org/lac/upload/lacreport/LAC_PrintReport.pdf; Gabriel J. Chin, *Race, the War on Drugs, and the Collateral Consequences of Criminal Conviction*, 6 J. GENDER RACE & JUST. 253, 253 (2002) (describing collateral consequences as "the most significant penalties resulting from a criminal conviction"); John Hagan & Ronit Dinovitzer, *Collateral Consequences of Imprisonment for Children, Communities, and Prisoners*, 26 CRIME & JUST. 121 (1999) (analyzing aggregate effects of mass incarceration).

[5] *See* FELLNER & MAUER, *supra* note 4, at 1.

[6] *See* Nora V. Demleitner, *Preventing Internal Exile: The Need for Restrictions on Collateral Sentencing Consequences*, 11 STAN. L. & POL'Y REV. 153, 156 (1999) (describing limitations on ex-offenders' access to employment due to licensing and other regulatory restrictions).

[7] *See* Sandra Guerra, *The Myth of Dual Sovereignty: Multijurisdictional Drug Law Enforcement and Double Jeopardy*, 73 N.C. L. Rev. 1159, 1168 n.34 (1995) (citing OFFICE OF NAT'L DRUG CONTROL POLICY, EXECUTIVE OFFICE OF THE PRESIDENT, NATIONAL DRUG CONTROL STRATEGY 24 (1991), which found that ex-offenders could lose over 462 deniable benefits from fifty-three federal agencies); *see also* Demleitner, *supra* note 6, at 156. The Personal Responsibility and Work Opportunity Reconciliation Act of 1996, for example, imposes a long-term ban on public benefits for first-time drug offenders and a

consequences of criminal exposure, such as those surrounding ex-offender access to credit and financial services.[8]

Given that over 47 million Americans (or 1 in 4 adults) have a criminal record of either an arrest or a conviction,[9] it is imperative that policy advocates and scholars also investigate the effects that such a record has on those aspects of an ex-offender's life that have failed to garner such focused attention. Under federal law, for example, a lender may consider a small business loan applicant's history of criminal arrests or convictions in a determination of that applicant's creditworthiness.[10] Holding that an applicant's criminal record bears a "manifest relationship" to the ability to repay a loan, one federal court has legitimized a form of lending discrimination that has serious implications for the ability of any ex-offender to reenter society effectively, and for the ability of receiving communities to effectuate crime prevention and community development initiatives.[11]

The desirability of state-imposed collateral consequences remains a hotly debated topic among criminal justice commentators[12]—some restrictions serve important goals, while others are merely punitive and do not even serve to deter future offending. This Note criticizes barriers to certain forms of credit as an uncharted collateral consequence of criminal exposure, and offers remediation strategies for offender reentry advocates. The use of an applicant's criminal exposure history in determining creditworthiness is problematic on several fronts, and should be a matter of concern for both criminal justice advocates and proponents of fair lending.

Part I sketches the contours of civil collateral consequences generally and then examines the consequences affecting access to credit and financial services specifically. Part II describes the stigmatizing effects of restrictions on credit on the individual offender, as well as

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lifetime ban on public benefits for certain repeat offenders. *See* 21 U.S.C. § 862(a)(1) (2000).

[8] An important exception to this trend is the scholarship that examines the effects of the 1998 Drug Free Student Loans Act, 20 U.S.C. § 1091(r) (2000), which excludes individuals who have been convicted of drug-related crimes from federal educational assistance. *See, e.g.*, Eric Blumenson & Eva S. Nilsen, *How to Construct an Underclass, or How the War on Drugs Became a War on Education*, 6 J. GENDER RACE & JUST. 61, 68–71 (2002) (describing legislative priorities behind passage of Act).

[9] *See* DEBBIE MUKAMAL, U.S. DEP'T OF LABOR, FROM HARD TIME TO FULL TIME: STRATEGIES TO MOVE EX-OFFENDERS FROM WELFARE TO WORK 6 (2001) ("Over 47 million Americans . . . have a criminal history on file with state or federal governments."), http://www.hirenetwork.org/pdfs/From_Hard_Time_to_Full_Time.pdf.

[10] *See* A.B. & S. Auto Serv. v. South Shore Bank, 962 F. Supp. 1056 (N.D. Ill. 1997) (discussed *infra* notes 91–95 and accompanying text). This Note addresses credit generally, but focuses on barriers to small business and other collateralized loans.

[11] *See id.* at 1064.

[12] *See supra* notes 4–6.

the broader effects on the community of reentry, most notably with regard to community development efforts. Part III argues that challenges to this form of lending discrimination should find some recourse in the federal courts under existing fair lending laws, especially the Equal Credit Opportunity Act (ECOA),[13] but information gaps frustrate the viability of these claims. Part IV contends that, even in the absence of effective recourse to the courts, state and local initiatives to curtail civil collateral consequences ought to be encouraged and strengthened. This Part highlights the mixed success of efforts by some local governments to implement restrictions on various forms of discrimination against ex-offenders.

I

COLLATERAL CONSEQUENCES AND OFFENDER REENTRY IN CONTEXT

The civil, political, and economic disabilities that result from criminal convictions have been termed "invisible punishments" due to their obscurity from the purview of crime policymakers and the public.[14] These consequences are articulated in state and federal law,[15] and encompass restrictions and prohibitions on a number of rights and privileges, including infringement or abrogation of the right to vote,[16] potential public registration as a sex offender,[17] prohibitions

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[13] 15 U.S.C. § 1691 (2000).

[14] *See* Anthony C. Thompson, *Navigating the Hidden Obstacles to Ex-Offender Reentry*, 45 B.C. L. REV. 255, 273 (2004) ("Not only offenders, but many participants in the criminal justice system remain wholly unaware of these consequences."). Collateral consequences also raise important questions regarding the democratic process, since these sanctions usually are not imposed through meaningful legislative deliberation and are not subject to debate or public input. *See* Sabra Micah Barnett, *Collateral Sanctions and Civil Disabilities: The Secret Barrier to True Sentencing Reform for Legislatures and Sentencing Commissions*, 55 ALA. L. REV. 375, 387 (2004) (advocating legislative debate on collateral consequences).

[15] For an overview of consequences resulting from federal convictions, see OFFICE OF THE PARDON ATTORNEY, U.S. DEP'T OF JUSTICE, FEDERAL STATUTES IMPOSING COLLATERAL CONSEQUENCES UPON CONVICTION [hereinafter FEDERAL STATUTES IMPOSING COLLATERAL CONSEQUENCES], http://www.usdoj.gov/pardon/collateral_consequences.pdf (last visited June 10, 2005).

[16] *See, e.g.*, N.Y. ELEC. LAW § 5-106(2)–(5) (McKinney 1998) (revoking right to vote for any person convicted of felony under New York state law, federal law, or any other state's laws, until pardoned or maximum sentence of imprisonment expires).

[17] Sex offender registration laws, popularly known as "Megan's Laws," exist in some form in all fifty states. *See* SCOTT MATSON & ROXANNE LIEB, WASH. STATE INST. FOR PUB. POLICY, COMMUNITY NOTIFICATION IN WASHINGTON STATE: 1996 SURVEY OF LAW ENFORCEMENT 1 (1996) ("All states now require released sex offenders to register with law enforcement or state agencies.").

on the right to possess firearms,[18] enhanced penalties for future convictions,[19] exclusion from certain professions,[20] and restrictions on access to public housing.[21] This Part outlines the goals of traditional reentry initiatives and suggests that increasingly restrictive collateral punishments frustrate, rather than further, those goals.

By exploring the relationship between the stigma associated with criminal exposure and social belonging, this Part seeks to establish a framework for advocating reentry strategies that seek to reintegrate the whole person into the receiving community.[22] This Part draws connections between social engagement and recidivism, and argues that individual fulfillment, which ultimately contributes to public safety, ought to be the primary concern of reentry policymakers.

A. Collateral Consequences and Reentry Initiatives

Successful ex-offender reintegration accomplishes two separate public policy goals: promotion of public safety and self-realization of the individual as a productive citizen.[23] The difficulties surrounding effective reentry strategies raise community concerns regarding recidivism,[24] joblessness,[25] mental illness,[26] and substance abuse;[27] the current reentry scholarship focuses almost exclusively on these public

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[18] *See* 18 U.S.C. §§ 921–930 (2000) (forbidding person convicted of felony from shipping, transporting, possessing, or receiving firearm or ammunition "in interstate or foreign commerce").

[19] The Federal Sentencing Guidelines, for example, include a graduated "criminal history category" which substantially increases the recommended sentence as the criminal history category increases. U.S. SENTENCING GUIDELINES MANUAL § 4A1.1 (2004).

[20] *See* FEDERAL STATUTES IMPOSING COLLATERAL CONSEQUENCES, *supra* note 15, at 6–9 (detailing federally imposed restrictions on licensing and employment as example of collateral consequences).

[21] *See* Anti-Drug Abuse Act of 1988, 42 U.S.C. § 1437d(l)(4), (6) (2000) (permitting eviction from public housing for "criminal activity" by tenants or their guests).

[22] Many organizations presently are approaching reentry from this perspective. *See* Nora V. Demleitner, *Stopping a Vicious Cycle: Release, Restrictions, Re-Offending*, 12 FED. SENTENCING REP. 243, 243 (2000) ("Various organizations are studying the obstacles ex-offenders face . . . and developing legislative and judicial strategies to limit the negative consequences of restrictions on ex-offenders while providing incentives for them not to re-offend.").

[23] *See* JEREMY TRAVIS ET AL., FROM PRISON TO HOME: THE DIMENSIONS AND CONSEQUENCES OF PRISONER REENTRY 6 (2001) ("The release of prisoners back into their communities poses two fundamentally interrelated challenges: First, how to protect the safety of the public, and second, how to foster an individual's transition from life in prison to life as a productive citizen."), http://www.urban.org/UploadedPDF/from_prison_to_home.pdf.

[24] For example, nearly sixty-eight percent of the prisoners released in 1994 were rearrested within three years. *See* PATRICK A. LANGAN & DAVID J. LEVIN, RECIDIVISM OF PRISONERS RELEASED IN 1994, at 1 (2002) ("Among nearly 300,000 prisoners released in 15 states in 1994, 67.5% were rearrested within 3 years."), http://www.ojp.usdoj.gov/bjs/pub/pdf/rpr94.pdf; *see also* TRAVIS ET AL., *supra* note 23, at 1 ("Public safety gains are typically measured in terms of reduced recidivism.").

safety issues. As a result, little attention has been paid to strategies designed to foster the self-realization component of successful reintegration strategies.[28]

Since collateral punishments function in part to shame the offender, these policies may have a counterproductive effect on crime rates, as the resulting stigma undermines effective reentry and may even precipitate recidivist behavior. Such stigma constantly reminds the ex-offender, and the observing public, of her criminal background; in addition, this stigma may diminish the self-respect and perceived self-worth of the individual.[29] The result is that the stigmatized person "may suppress aspirations that look unattainable when seen with the restricted vision imposed by a withered self-concept."[30] Although stigma acts in varied ways to obscure the individual offender and her personal characteristics, arguably the most visible effects of stigmatization are the rates of re-offense, or recidivism, among ex-offenders.

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[25] *See generally* SVENJA HEINRICH, GREAT CITIES INST., REDUCING RECIDIVISM THROUGH WORK: BARRIERS AND OPPORTUNITIES FOR EMPLOYMENT OF EX-OFFENDERS 4–7 (2000) (examining factors that contribute to high joblessness among ex-offenders), http://www.uic.edu/cuppa/gci/publications/Workforce%20partnership%20series/pdf/Ex-offender%20Paper.pdf.

[26] *Id.* at 6–7 (outlining effects of mental illness on employment opportunities for ex-offenders); Mark J. Heyrman, *Mental Illness in Prisons and Jails*, 7 U. CHI. L. SCH. ROUNDTABLE 113, 113–19 (2000).

[27] *See generally* NAT'L CTR. ON ADDICTION AND SUBSTANCE ABUSE AT COLUMBIA UNIV., BEHIND BARS: SUBSTANCE ABUSE AND AMERICA'S PRISON POPULATION 2 (1998), *available at* http://www.casacolumbia.org/pdshopprov/files/5745.pdf (reporting that "81 percent of state inmates, 80 percent of federal inmates and 77 percent of local jail inmates" have some form of drug or alcohol problem).

[28] I use "reintegration" here to refer to reentry programs that intend to holistically integrate the individual into the daily functions of the community. *See, e.g.*, TRAVIS ET AL., *supra* note 23, at 1 ("Reintegration outcomes would include increased participation in social institutions such as the labor force, families, communities, schools, and religious institutions.").

[29] *See* KENNETH L. KARST, BELONGING TO AMERICA: EQUAL CITIZENSHIP AND THE CONSTITUTION 26 (1989) ("Any inequality, when it is taken as an index of personal worth, directly wounds self-respect."). *See generally* ERVING GOFFMAN, STIGMA (1963) (articulating social scientific theory of stigma and difference). Stigma does not merely circumscribe the potential of the stigmatized but also taints those close to the stigmatized. *See id.* at 47–48 (discussing effects of stigma on those "with"). For communities experiencing the return of increasingly concentrated numbers of ex-offenders, each individual in the community suffers from the stigma attached to the ex-offender. This effect is magnified in communities that house large concentrations of ex-offenders. *See infra* notes 67–71 and accompanying text. In families of ex-offenders, particularly, the social capital of the family is compromised by the return and continued presence of the ex-offender—just as the ex-offender herself experiences "moral disapproval, denigration, and avoidance," so, too, does her family. Stephen C. Ainlay et al., *Stigma Reconsidered*, *in* THE DILEMMA OF DIFFERENCE: A MULTIDISCIPLINARY VIEW OF STIGMA 1, 3 (Stephen C. Ainlay et al. eds., 1986).

[30] *See* KARST, *supra* note 29, at 26.

Recidivism is justifiably a major concern in crime policy.[31] High recidivism rates, however, do not justify further restrictions on the capacity of ex-offenders to reintegrate. In fact, according to reentry scholars, recidivism may be linked causally to the expansive net of collateral consequences that circumscribe post-release opportunities.[32] The difficulty that ex-offenders face when attempting to reintegrate, especially as a result of consequences that limit economic opportunities, frustrates the efforts of offenders to live crime-free. Without sufficient employment opportunities[33] and because of exclusion from state and federal welfare programs,[34] many offenders face pressure to engage in illegitimate money-earning enterprises.[35] These pressures may be so significant as to outweigh other considerations, including the risk of being caught and returned to prison.

B. Barriers to Credit as an Uncharted Consequence

Any banking practice that limits access to credit and services for some individuals has significant repercussions for those individuals and the communities of which they are a part. A practice in which banks consider criminal exposure when making determinations of creditworthiness is no different. In small business lending, for example, banks applying for Small Business Association (SBA) assistance routinely require that applicants divulge their criminal exposure. Banks' reliance on such a practice—the extent of which is difficult to ascertain since banks are not required to disclose whether they consider criminal exposure in making loans—erects yet another barrier to efforts at successful reentry for ex-offenders.

Even in the absence of statistical information suggesting a correlation between criminal exposure and creditworthiness,[36] many

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31 *See supra* note 24 and accompanying text.

32 *See* Barnett, *supra* note 14, at 392 (suggesting that "barriers to rehabilitation" lead to recidivism); Darryl K. Brown, *Cost-Benefit Analysis in Criminal Law*, 92 CAL. L. REV. 323, 346 (2004) (arguing that diminished job prospects and circumscribed opportunities to reintegrate fully "may increase the odds of recidivism"). President Bush recognized as much in his January 2004 State of the Union address: "We know from long experience that if [ex-offenders] can't find work, or a home, or help, they are much more likely to commit crime . . . ." President George W. Bush, State of the Union Address (Jan. 20, 2004) (transcript available at http://www.whitehouse.gov/news/releases/2004/01/20040120-7.html).

33 *See supra* note 25 and accompanying text.

34 *See supra* note 7 and accompanying text.

35 *See* Thompson, *supra* note 14, at 258 ("Without structural support or intervention, these individuals face a wide range of obstacles making it virtually impossible for them to pursue legitimate means of survival.").

36 In 1996, loan officers at the defendant bank in *A.B. & S. Auto Service*, discussed *infra* Part III.B, admitted having no knowledge of any data or published study supporting such a relationship. *See* Def.'s Resp. to Pl.'s First Set of Interrogs. at 5, A.B. & S. Auto Serv. v. South Shore Bank, 962 F. Supp. 1056 (N.D. Ill. 1997) (No. 95-C-5826).

lenders require that applicants disclose information regarding such exposure, and use that information in determining applicant creditworthiness.[37] The federal government has a role in the proliferation of mandated disclosures of criminal history: As lenders increasingly rely upon federally-insured credit instruments, federal agencies' inquiries into criminal histories for informational and underwriting procedures effectively disclose the information to prospective lenders, and implicate the procedures and criteria by which private lenders conduct assessments of creditworthiness. This phenomenon is particularly prevalent (and troubling) in the context of federally-insured home mortgage and small business loans.

Some federal agencies require that individuals seeking assistance under federal financial programs disclose their criminal background. The SBA, for example, requires that all applicants for SBA financial assistance complete and submit a "statement of personal history," commonly known as a Form 912.[38] This requirement extends not only to individuals who seek direct SBA assistance, but also to individuals who seek private loans that the lender anticipates may be eligible for SBA assistance or insurance.[39]

Form 912 requests information regarding the applicant's current and previous addresses, names used, citizenship status,[40] and the applicant's criminal history: whether the applicant is currently or has ever been "under indictment, on parole or probation;" and whether the applicant has ever been arrested for a charge other than a moving violation and, if so, an inquiry into the nature of the crime for which the applicant was arrested.[41] This information is required not only of the owner-applicant herself, but also of each partner (if a partnership) and each officer, director, or individual who holds at least twenty percent of an applicant company's equity.[42] The SBA reasons that the

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[37] *See infra* notes 38–43 and accompanying text.

[38] Small Bus. Admin., Form 912: Statement of Personal History [hereinafter Form 912], http://www.sba.gov/sbaforms/sba912.pdf (last visited June 13, 2005).

[39] The Small Business Administration (SBA) and the Federal Housing Authority (FHA) insure loans for applicants with less-than-ideal credit histories. Both agencies also extend insurance protection for loans made in underdeveloped communities.

[40] Form 912, *supra* note 38.

[41] *Id.* The form also states: "An arrest or conviction record will not necessarily disqualify you." *Id.*

[42] *Id.* This information is required of every applicant for SBA financial assistance as a supplement to the applications required for the particular program of interest. Form 912 is required of applicants for the following SBA programs: business loan, small business loan (short form), surety bond guarantee assistance, and the 8(a) business development program. While Form 912 is not specifically required of applicants for the SBALowDoc loan, Section D5 of the SBALowDoc loan application requests information about the applicant's criminal history that is identical to the language found in Form 912. *See* Small Bus. Admin., Form 4L: Application for LowDoc Loan, http://www.sba.gov/sbaforms/sba4-L.pdf

criminal history provisions of Form 912 indicate both the applicant's "willingness and ability to pay their debts and whether they abided by the laws of their community."[43] There are, however, no guidelines or other indications of how such information will be used in determinations of eligibility; it is unclear whether the SBA uses such information in its initial screening process, whether such information only comes into play for borderline applicants, or whether such information might preclude further consideration.

Even in the absence of explicit guidelines, lenders offering loans through SBA programs routinely request information regarding applicants' criminal histories.[44] The practice has serious implications for the ability of many communities to implement effective offender reentry and community development initiatives. Before this Note turns to an exploration of this practice from the one source which offers publicly available information regarding its use—a federal court case challenging the practice on the basis that it disparately harms protected minorities in violation of the Equal Credit Opportunity Act—it is important first to outline some of the difficulties faced by receiving communities in accessing mainstream forms of credit.

(last visited June 13, 2005). The Disaster Business Loan application asks whether applicant "has . . . been convicted of a criminal offense committed during and in connection with a riot or civil disorder." Small Bus. Admin., Form 5: Disaster Business Loan Application, http://www.sba.gov/sbaforms/SBA5.pdf (last visited June 13, 2005). The 8(a) Business Development application also requires that applicants whose Form 912 indicates an arrest must submit fingerprints to the SBA before their application will be considered. Small Bus. Admin., Form 1010: Application for 8(a) Business Development (8(a) BD) and Small Disadvantaged Business (SDB) Certification, http://www.sba.gov/sbaforms/sba1010.pdf (last visited June 13, 2005).

[43] Small Bus. Admin., Basic 7(a) Loan Program: Character Considerations, http://www.sba.gov/financing/sbaloan/7a.html (last visited June 13, 2005). The SBA is not alone in requiring that applicants for federal assistance disclose their criminal backgrounds. The Department of Agriculture (USDA), for example, requires that applicants for loans or guarantees for multifamily housing projects under the auspices of the Rural Development group disclose any and all litigation—both civil and criminal—initiated against the applicant, guarantors, partners, principals, or directors. *See* U.S. Dep't of Agric., Form RD 3565-1: Application for Loan and Guarantee (Multifamily Housing), http://forms.sc.egov.usda.gov/efcommon/eFileServices/Forms/RD3565-0001.pdf (last visited June 13, 2005). In addition to information regarding criminal exposure, the Department of Housing and Urban Development (HUD) also requires that applicants for HUD-insured loans disclose whether either the borrower or co-borrower is "a party to a lawsuit." *See* Fannie Mae, Form 1003, at 3, http://www.bankturndown.com/loan_app/65.pdf (last visited Apr. 6, 2005).

[44] *See, e.g.*, Diamond Fin. Servs., Loan Application, http://www.easysba.com/app_form1.htm (last visited Apr. 6, 2005) (inquiring as to whether applicant has "ever been arrested or convicted for a criminal offense"); MBS Fin. Servs., USDA Rural Development Loan Application, http://www.mbsfinancial.com/Loan_Questions.htm (inquiring into applicant's arrest and conviction history) (last visited Apr. 6, 2005).

II
EFFECTS OF CREDIT RESTRICTIONS ON INDIVIDUALS AND COMMUNITIES

The effects of restricting access to credit based on criminal exposure are acutely felt in communities of color, which sustain high concentrations of ex-offenders, and among individuals in those communities who suffer the stigma of such exposure. This focus on individuals, as well as communities, is keeping in line with a vision of offender reentry that seeks to promote both public safety and individual fulfillment. This Part outlines the extent of these effects at the macro and micro level, and argues that the harms of such a practice far outweigh any potential benefits presumed to be derived from it.

A. Credit and Social Belonging

The availability of and personal access to financial services is fundamental to modern notions of human engagement.[45] The marker of association that identifies one as a consumer is a hallmark of modern social belonging.[46] An individual's access to various financial resources, including credit, may determine the extent to which she is able to provide herself with basic human needs, such as food, shelter, education, healthcare, and clothing.[47] Credit also expands the spectrum of choices available to its holder: Through its use, a borrower can reimagine her material—and to a certain extent, her psychological—reality.[48] In this context, credit figures prominently as one of the symbols of community membership: In effect, the terms of credit relationships implicate the conditions of citizenship.[49] A lender's single decision to extend or deny credit to an individual thereby

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[45] *See, e.g.*, RALPH C. CLONTZ, JR., EQUAL CREDIT OPPORTUNITY MANUAL ¶ 1.02[1] (3d ed. 1979) (arguing that "[t]he ability to obtain credit has become . . . the threshold to participation as a full-fledged member of society").

[46] *See* LLOYD KLEIN, IT'S IN THE CARDS: CONSUMER CREDIT AND THE AMERICAN EXPERIENCE 1 (1999) (observing that "[a] person is almost a nonentity until he or she establishes an ongoing credit history. Receipt of an initial credit account is essentially a form of formal economic status recognition.").

[47] *Cf.* BRADLEY R. SCHILLER, THE ECONOMICS OF POVERTY AND DISCRIMINATION 26 (8th ed. 2001) (noting relationship between credit and purchasing power).

[48] *See* KLEIN, *supra* note 46, at 43 (observing that "[c]onsumer credit as an economic resource facilitates the immediate acquisition of knowledge, parasocial experience, or a temporary escape from the realities of everyday life"); *see also* Stuart Hall, *Brave New World*, SOCIALIST REV., Jan.–Mar. 1991, at 57, 63 (claiming that "[t]here has been an enormous expansion of 'civil society,' caused by the diversification of the different social worlds in which men and women can operate").

[49] *See* EDWARD J. BLAKELY, PLANNING LOCAL ECONOMIC DEVELOPMENT 2 (1994) ("The promise of a job and economic security are the hallmarks of citizenship."); *see also* KLEIN, *supra* note 46, at 8 (arguing that "[c]onsumer credit functions as a credentialing device that legitimates status attainment").

affects the terms on which that person engages with herself and the world around her.[50]

This debtor-citizen dialectic is particularly salient in terms of small business ownership. Small business owners—those who operate "mom and pop" shops, small groceries, snack shops, car repair shops, and the like—are catalysts of job creation and economic growth.[51] Entrepreneurs are also arguably more likely to be involved in civic and political activities, the benchmark of effective citizen participation in a republic. If participation and belonging are central to effective citizenship (and therefore, to successful social integration), then our criminal justice policies should recognize the importance of consumerism to engagement and collective experience. The unregulated exclusion of individuals with criminal convictions from this community of credit may foster resentment and precipitate further antisocial behavior.

Success in this area depends upon reentry strategies of full inclusion and engagement—ones that recognize the value of, and support the ex-offender's full participation in, all facets of community life, including the enjoyment of the same financial opportunities and protections that are accorded to the rest of the community. At a fundamental level, access to and use of credit directly implicates personal responsibility, the hallmark of rehabilitation. Legitimate entrepreneurs are also arguably less likely to be involved in anti-social or criminal activity. Moreover, the inclusion of such individuals in the nation's economic matrix serves to bolster community efforts at local economic development, as well as to benefit the individual herself. A successful loan applicant necessarily establishes a credit history that can then be deployed for securing future loans. In communities of color, which contain disproportionate concentrations of ex-offenders,[52] and in which racial animus long has prevented equal access to credit and financial services,[53] integration of offenders into the credit fabric of the community takes on critical significance.

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[50] *See* KLEIN, *supra* note 46, at 1 (arguing that "'[l]eaving home without it' is almost surely an invitation for risking nonperson status among members of the economic community"). *See also id.* at 18 ("Consumer credit, along with its interlinks designating honorific status, is a signification of socio-economic acceptance or rejection."). As MacDonald and Gastmann put it, "there is a direct relationship between credit and power." SCOTT B. MACDONALD & ALBERT L. GASTMANN, A HISTORY OF CREDIT AND POWER IN THE WESTERN WORLD 288 (2001).

[51] *See, e.g.*, Merrill F. Hoopengardner, Note, *Nontraditional Venture Capital: An Economic Development Strategy for Alaska*, 20 ALASKA L. REV. 357, 357 (2003) ("Small businesses add jobs, strengthen the tax base, and improve overall quality of life for many members of the surrounding community.").

[52] *See infra* notes 67–71 and accompanying text.

[53] *See infra* notes 55–60 and accompanying text.

B. Credit and Communities of Color

Limitations on ex-offender access to credit only exacerbate the economic gaps in this nation's poorer communities. Persistent barriers to equal access to financial services continue to plague communities of color,[54] affecting opportunities for class and social mobility by circumscribing residents' access to credit and higher education. People of color continue to face considerable discrimination when applying for various forms of credit:[55] African-American borrowers, for example, still lag considerably behind other groups in their access to loans. A 1992 study by the Federal Reserve Bank of Boston suggested that Black mortgage applicants are twice as likely to be rejected as similarly situated white applicants.[56] A more recent study suggests similar rates of denial for Black business loan applicants vis-

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[54] This Note commonly refers to men and women of Black, Latino, Asian, and American Indian descent as "communities of color." Of course, low-income communities also suffer harshly from any form of lending discrimination; however, because poverty is not one of fair lending's explicitly protected categories, such claims are not cognizable under the statute.

[55] *See, e.g.*, MARGERY AUSTIN TURNER ET AL., U.S. DEP'T OF HOUS. & URBAN DEV., ALL OTHER THINGS BEING EQUAL: A PAIRED TESTING STUDY OF MORTGAGE LENDING INSTITUTIONS 24–26 (2002) (finding that Black and Latino borrowers in Los Angeles face unequal treatment even when only inquiring about loans and financial services), http://www.huduser.org/Publications/PDF/aotbe.pdf; *see also* U.S. DEP'T OF HOUS. & URBAN DEV., WHAT WE KNOW ABOUT MORTGAGE LENDING DISCRIMINATION IN AMERICA, EXECUTIVE SUMMARY (1999) (concluding that "minorities are less likely than whites to obtain mortgage financing and, if successful in obtaining a mortgage, tend to receive less generous loan amounts and terms"), *at* http://www.hud.gov/library/bookshelf18/pressrel/newsconf/execsumm.html; Peter P. Swire, *The Persistent Problem of Lending Discrimination: A Law and Economics Analysis*, 73 TEX. L. REV. 787, 825–28 (1995) (suggesting that persistent discrimination encourages less investment in creditworthiness, thereby perpetuating discriminatory lending practices).

[56] ALICIA H. MUNNELL ET AL., MORTGAGE LENDING IN BOSTON: INTERPRETING HMDA DATA (Fed. Reserve Bank of Boston, Working Paper No. 92-7, 1992). The Boston Fed study sparked a flurry of scholarly debate on the racism of the mortgage lending industry. *See, e.g.*, Paulette Thomas, *Federal Data Detail Pervasive Racial Gap in Mortgage Lending*, WALL ST. J., Mar. 31, 1992, at A1 (noting that data disclosed by Federal Reserve Board show "[i]f you're black, it's twice as likely your mortgage application will be rejected as it is if you're white; and if you live in a low-income neighborhood, chances are that many lenders have little interest in mortgage-lending in your community anyway"). Since its publication, scholars have wavered on whether the statistical model proposed by the Boston Fed is the best way to isolate variables other than race (such as debt-to-income ratio). *See, e.g.*, Stephen L. Ross, *Mortgage Lending Discrimination and Racial Differences in Loan Default: A Simulation Approach*, 8 J. OF HOUSING RES. 277, 292–93 (1997) (suggesting that using rate of default as metric for assessing existence of discrimination may be undercounting actual rate of discrimination), *available at* http://www.fanniemaefoundation.org/programs/jhr.shtml. Despite its problems, the Boston Fed study succeeded in spotlighting the issue of racial discrimination in mortgage lending. *See, e.g.*, RAPHAEL W. BOSTIC, THE ROLE OF RACE IN MORTGAGE LENDING: REVISITING THE BOSTON FED STUDY 19–21 (Bd. of Governors of the Fed. Reserve Sys. Fin. and Econ. Disc. Series No. 97-2, 1997).

à-vis similarly situated white applicants.[57] African-American loan applicants may even experience similar discrimination from both white and Black-owned financial institutions.[58] Lenders, moreover, have long prescribed differing loan rates for urban versus suburban areas, along with requirements of higher down payments for urban borrowers than for their suburban counterparts.[59] For minority borrowers—who live in disproportionately large numbers in urban areas—these barriers often preclude significant economic development.[60]

As discussed above, collateral sanctions targeting ex-offenders frustrate the efforts of communities to engage actively in development and renewal. For example, incarceration has a measurable impact on the employment potential of ex-offenders, both in terms of wages and

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[57] *See* David G. Blanchflower et al., *Discrimination in the Small Business Credit Market*, 85 REV. ECON. & STAT. 930, 942 (2003) (finding that, while non-white borrowers were more likely overall to be denied credit than white borrowers, "loan denial rates are significantly higher for Black-owned firms than for white-owned firms even after taking into account differences in an extensive array of measures of creditworthiness and other characteristics").

[58] *See* Harold A. Black, et al., *Do Black-Owned Banks Discriminate Against Black Borrowers?*, 11 J. OF FIN. SERVICES RES. 185, 198 (1997) (suggesting that Black-owned banks also consider race in their lending decisions); *cf.* Michael F. Ferguson & Stephen R. Peters, *Cultural Affinity and Lending Discrimination: The Impact of Underwriting Errors and Credit Risk Distribution on Applicant Denial Rates*, 11 J. OF FIN. SERVICES RES. 153, 157–58 (1997) (arguing that cultural affinity may explain higher rates of loan approvals for white borrowers by white lenders).

[59] *See* HARRY EDWARD BERNDT, NEW RULERS IN THE GHETTO: THE COMMUNITY DEVELOPMENT CORPORATION AND URBAN POVERTY 92–93 (1977) (detailing study finding different loan policies in city than outside city).

[60] *See* DALTON CONLEY, BEING BLACK, LIVING IN THE RED: RACE, WEALTH, AND SOCIAL POLICY IN AMERICA 25–37 (1999) (arguing that historic economic inequality results in differential wealth accumulation among Blacks and whites); Blanchflower et al., *supra* note 57, at 942 ("[B]lack-owned firms, in particular, face obstacles in obtaining credit that are unrelated to their creditworthiness."). These trends of limited access are, of course, not recent developments. The history of discrimination in lending, especially mortgage lending, spans the twentieth century. *See generally* STEPHEN GRANT MEYER, AS LONG AS THEY DON'T MOVE NEXT DOOR: SEGREGATION AND RACIAL CONFLICT IN AMERICAN NEIGHBORHOODS (2000) (chronicling history of housing and mortgage discrimination in twentieth-century America); STEPHEN L. ROSS & JOHN YINGER, THE COLOR OF CREDIT: MORTGAGE DISCRIMINATION, RESEARCH METHODOLOGY, AND FAIR-LENDING ENFORCEMENT (2002) (arguing that mortgage discrimination persists and current methods of remediation fail to address its existence properly). Title VIII of the Civil Rights Act of 1968 (the Fair Housing Act) was enacted, in part, to address this persistent problem. *See* 42 U.S.C. § 3601 (2000) (articulating purpose as "to provide . . . for fair housing throughout the United States"). Once Congress acknowledged that mortgage lending and home sales were not the only areas in which borrowers of color faced such obstacles, the Equal Credit Opportunity Act (1976) was passed to protect access to consumer and personal loans. *See infra* notes 78–81 and accompanying text.

lifetime earnings.[61] As ex-offenders are likely to experience a decrease in their earned wages following release,[62] and unemployment remains a persistent problem for the majority of ex-offenders,[63] many of our most vulnerable communities are being stripped of opportunities to develop their human and financial capital and to engage in community development efforts. Even for those who are able to find work, the diminished skill set of this population—occasioned by drastic cuts in prison services,[64] coupled with reduced opportunities for higher education upon release[65]—necessarily circumscribes their potential employment and earning opportunities.

In sum, the implications of using criminal history to prevent ex-offenders from taking out loans pose a grave problem for urban economic development initiatives. Given the large numbers of people of color either currently incarcerated or on parole or probation,[66] restric-

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61 *See* BRUCE WESTERN ET AL., THE LABOR MARKET CONSEQUENCES OF INCARCERATION 21 (Indus. Relations Section, Princeton Univ., Working Paper No. 450, Jan. 2001) (estimating "wage penalty" of incarceration to be ten to thirty percent and finding that ex-offenders experience little to no increase in wages through their prime wage increase years), http://www.irs.princeton.edu/pubs/pdfs/450.pdf. Some jurisdictions, such as New York City, have established provisions whereby an individual convicted of a felony immediately becomes divested of any and all pension programs maintained by a city agency employer. *See, e.g.*, N.Y.C. ADMIN. CODE § 13-161(e)(6)(b)–(c) (2001) (permitting immediate divestment from retirement pension program for any New York City Transit Authority employee convicted of felony).

62 *See* WESTERN ET AL., *supra* note 61, at 11–15 (detailing wage penalty accompanying incarceration).

63 According to one study, within one year of release, over sixty percent of ex-offenders have not secured stable work. *See* JOAN PETERSILIA, U.S. DEP'T OF JUSTICE, WHEN PRISONERS RETURN TO THE COMMUNITY: POLITICAL, ECONOMIC, AND SOCIAL CONSEQUENCES 3 (2000), http://www.ncjrs.org/pdffiles1/nij/184253.pdf.

64 The services that have experienced the greatest cuts are educational and trade programs. Prior to 1994, the Pell Grant Program was a major source of funding for educational programs for prison inmates; in 1994, Congress imposed a ban on such funding. *See* Thompson, *supra* note 14, at 269–70.

65 In 2000, nearly 9000 students were found ineligible for federal financial aid due to a drug-related offense. *See* Jeremy Travis, *Invisible Punishment: An Instrument of Social Exclusion*, *in* INVISIBLE PUNISHMENT, *supra* note 4, at 24; *see also* 20 U.S.C. § 1091(r) (2000) (restricting eligibility for federal student aid for individuals with drug-related convictions). These effects extend beyond mortgage, business, and consumer finance and affect opportunities for educational finance. Students who come from low-income households increasingly rely upon loans in order to attend four-year colleges and universities. *See* DEREK V. PRICE, BORROWING INEQUALITY: RACE, CLASS, AND STUDENT LOANS 41 (2004) ("[L]ow-income students in particular must borrow to gain access to higher education."). For adult students—a population even more likely to have had some criminal exposure—"there is virtually no loan-free access to higher education." *Id.*

66 Out of a total estimated correctional population of 6.9 million people at the end of 2003, Blacks and Latinos together accounted for more than 40% of all probationers and nearly 60% of all parolees. *See* LAUREN E. GLAZE & SERI PALLA, PROBATION AND PAROLE IN THE UNITED STATES, 2003, at 4, 6 (2004), http://www.ojp.usdoj.gov/bjs/pub/pdf/ppus03.pdf. At the end of 2003, African-Americans accounted for one-third of all proba-

tions on lending to individuals with criminal exposure may result in a virtual freezing out of the credit market for large swaths of low-income and of-color communities.[67] In Brooklyn, for example, some neighborhoods admit 12.5% of their adult males to jail or prison every year.[68] The Brooklyn police precincts with the highest numbers of parolees comprise only one-quarter of the borough's population; these same precincts, however, hold over half of all the parolees in the borough.[69] Cleveland[70] and Baltimore[71] exhibit similar demographic patterns.

The high concentration of ex-offenders in these communities—with their limited access to opportunities for educational or employment advancement—effectively circumscribes the potential for small business incubators and ambitious homeownership programs that have been the hallmark of traditional community economic development initiatives.[72] Community residents who are denied access to

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tioners in the United States. *Id.* at 4. At the end of 2002, people of color accounted for over 60% of all jail inmates. *See* DORIS J. JAMES, U.S. DEP'T OF JUSTICE, PROFILE OF JAIL INMATES, 2002, at 1 (2004) (noting that "[m]ore than 6 in 10 persons in local jails in 2002 were racial or ethnic minorities"), http://www.ojp.usdoj.gov/bjs/pub/pdf/pji02.pdf. The Bureau of Justice Statistics estimates that at midyear 2003, nearly 12% of Black men and 3.7% of Latino men in their twenties were in jail or prison. *See* PAIGE M. HARRISON & JENNIFER C. KARBERG, U.S. DEP'T OF JUSTICE, PRISON AND JAIL INMATES AT MIDYEAR 2003, at 1 (2004), http://www.ojp.usdoj.gov/bjs/pub/pdf/pjim03.pdf; *see also* TRAVIS ET AL., *supra* note 23, at 12 ("Young, poor, black males are incarcerated at higher rates than any other group . . . .").

[67] *See* TRAVIS ET AL., *supra* note 23, at 1 ("[Incarceration and ex-offender reintegration] is increasingly concentrated in a relatively small number of communities that already encounter enormous social and economic disadvantages."); Demleitner, *supra* note 22, at 246 ("[A] very small number of communities across the United States accept the bulk of returning convicts."); *see also* Jeffrey Fagan et al., *Reciprocal Effects of Crime and Incarceration in New York City Neighborhoods*, 30 FORDHAM URB. L.J. 1551, 1568 (2003) ("In New York City, arrests and incarcerations . . . have long been spatially concentrated in the poorest neighborhoods."). These neighborhoods include the Lower East Side, the South Bronx, Harlem, Brownsville, Bedford-Stuyvesant, East New York, and South Jamaica. *See id.* at 1568 n.87.

[68] TRAVIS ET AL., *supra* note 23, at 41 (quoting Eric Cadora & Charles Swartz, Community Justice Project at the Center for Alternative Sentencing and Employment Services (CASES), Analysis of Parolees Per Block Group in Brooklyn, N.Y. (1999)).

[69] *Id.*

[70] In Cuyahoga County, of which Cleveland is a part, "two-thirds of the county's prisoners and most of the block groups with high rates of incarceration come from Cleveland. Concentrations are such that well under 1 percent of the block groups in the county account for approximately 20 percent of the county's prisoners." TRAVIS ET AL., *supra* note 23, at 42.

[71] In Baltimore, fifteen percent of the communities account for over fifty percent of prison releases. *See id.*

[72] *See, e.g.*, WILLIAM H. SIMON, THE COMMUNITY ECONOMIC DEVELOPMENT MOVEMENT: LAW, BUSINESS, AND THE NEW SOCIAL POLICY 7–26 (2001) (outlining history of community economic development strategies since 1970s).

credit because of an arrest or conviction history are unable to participate effectively in development projects.[73] Others who have been denied credit in the past may not seek further credit opportunities due to fear of further rejection.[74] These communities also become more susceptible to gentrification and its attendant displacement when community members are unable to hold a financial stake in the development of the area. Finally, because of the difficulty of qualifying for a traditional loan, individuals in these communities also are more likely to seek assistance from subprime lenders, as opposed to traditional lending institutions.

The penetration of subprime lenders in urban markets has not gone without notice, and has become the subject of research by federal agencies.[75] Subprime lenders do not require burdensome application processes, and, in fact, members of this sector—for example, pawnshops—require little if any personal information from the borrower. The denial of credit based on criminal backgrounds may induce potential borrowers to participate in these subprime capital markets—at a higher cost and with greater risks than in mainstream markets. Although subprime and predatory lending institutions are providing for credit needs in poor and working communities, the vacuum of services in the mainstream lending market in these communities fosters unnecessarily high financial risk and economic instability.[76]

As a result, in areas which are home to large numbers of ex-offenders, banks effectively (though inadvertently) may "redline" large swaths of a community through reliance on evidence of criminal exposure.[77] Absent the use of that evidence, banks would be unable

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[73] *See* BERNDT, *supra* note 59, at 69 (observing that "inner-city communities do not contain the resources necessary for community development"). Local economic development strategists long have recognized the primacy of capital to the success of the initiative. *See* PETER K. EISINGER, THE RISE OF THE ENTREPRENEURIAL STATE 29 (1988) (noting "the key to job creation . . . is to encourage and subsidize the investment of private capital").

[74] Blanchflower et al., *supra* note 57, at 933–34.

[75] *See generally* U.S. DEP'T. OF HOUS. AND URBAN DEV., UNEQUAL BURDEN: INCOME AND RACIAL DISPARITIES IN SUBPRIME LENDING IN AMERICA (2000), http://www.hud.gov/library/bookshelf18/pressrel/subprime.html.

[76] In Washington Heights, a largely Latino and Black community in New York City, it has been estimated that "loansharks account for a third of all business financing deals . . . amounting to about $10 million a year." CTR. FOR AN URBAN FUTURE, ENGINE FAILURE 28 (2003), http://www.citylimits.org/images_pdfs/pdfs/Engine_Failure.pdf.

[77] The term "redlining" historically refers to mortgage-lending practices that discriminate based on geographic area. Most states have enacted legislation prohibiting redlining. *See, e.g.*, N.Y. BANKING LAW § 9-f (McKinney 2001) (prohibiting geographic discrimination in making mortgage loans). In spite of such efforts to eliminate redlining practices, the practice remains pervasive. *See, e.g.*, Matt O'Connor, *First American Settles Bias Suit*,

to exclude those same applicants based on the presumed demographic characteristics of their zip code. The legality of lending discrimination based on criminal history effectively allows lending institutions to make an end run around federal anti-discrimination legislation and promotes a form of redlining without the blatant racial or ethnic discrimination that generally is associated with the term. The remaining Parts of this Note address the promise (and limitations) of litigation strategies to challenge the practice, as well as the potential for other remedial efforts which seek to address the worst effects of restricting credit on this basis.

III
FRONTIERS IN FAIR LENDING

The federal fair lending landscape should provide an avenue for challenging the use of criminal history in deciding whether or not to extend a loan to an applicant. For one thing, the availability of information detailing the disproportionate conviction and incarceration rates of men and women of African and Latino descent raises the possibility that minority plaintiffs might be able to make out viable disparate impact claims under the Equal Credit Opportunity Act (ECOA). This Part turns to a consideration of potential litigation strategies under the ECOA, and concludes that adversarial processes alone cannot adequately address concerns surrounding offender reentry and access to mainstream financial markets.

A. *Litigating Creditworthiness: The Equal Credit Opportunity Act*

The ECOA[78] prohibits creditors from discriminating against credit applicants "on the basis of race, color, religion, national origin, sex or marital status, or age."[79] When Congress enacted the ECOA in 1974, legislators championed the role of credit in American society,

CHI. TRIB., July 14, 2004, § 3, at 1 (describing $5.7 million settlement reached between federal prosecutors and bank accused of redlining).

[78] The Equal Credit Opportunity Act provides that:

> [i]t shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction—
> (1) on the basis of race, color, religion, national origin, sex or marital status, or age (provided the applicant has the capacity to contract);
> (2) because all or part of the applicant's income derives from any public assistance program; or
> (3) because the applicant has in good faith exercised any right under this chapter.

15 U.S.C. § 1691(a) (2000).

[79] *Id.* Although the statute's original version prohibited discrimination based only on sex or marital status—as a protective measure for married and divorced women—it was amended in 1976 to include race as a protected category.

arguing that credit was the linchpin of American economic systems. Supporters of the legislation lauded the statute's ability to eradicate discrimination in lending: Senator Bill Brock of Tennessee, who introduced the amendment that would later become the ECOA, remarked that "[e]very consumer deserves an equal opportunity for access to the credit market, and that credit should never be withheld because of . . . any other factor not related to ability and willingness to repay the loan."[80]

Plaintiffs in ECOA cases, as in Title VII employment discrimination cases, can prove discrimination using any of three approaches:[81] direct evidence,[82] disparate treatment,[83] or disparate impact. Direct evidence and disparate treatment claims require that the plaintiff meet a substantially higher burden of proof than the defendant—a burden so high that few plaintiffs are able to meet it.[84] Advocates, therefore, are left with the disparate impact test to establish unfair

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[80] 120 CONG. REC. 19,213 (1974) (statement of Sen. Brock proposing amendment to H.R. 11221, 93d Cong. (1974)).

[81] Historically, ECOA jurisprudence has turned to employment discrimination cases, including *Griggs v. Duke Power Co.*, 401 U.S. 424 (1971), and *Albemarle Paper Co. v. Moody*, 422 U.S. 405 (1975), to serve as models in the application of the disparate impact, direct evidence, and disparate treatment standards. *See* S. REP. NO. 94-589, at 4–5, *reprinted in* 1976 U.S.C.C.A.N. 403, 406; *see also* Policy Statement on Discrimination in Lending, 59 Fed. Reg. 18,266, 18,268–69 (Apr. 15, 1994).

[82] Direct evidence claims are the most difficult to make, as success requires a plaintiff to prove that an adverse credit action was a direct result of impermissible discrimination against one of the statute's protected groups. These claims rely on what generally is referred to as the "smoking gun," or indisputable evidence that the defendant lender has taken an adverse credit action on the basis of one of the prohibited categories. This standard stems from *Price Waterhouse v. Hopkins*, 490 U.S. 228 (1989). The direct evidence standard establishes proof of discrimination on its face without inference or presumption on the part of the fact-finder.

[83] Disparate treatment claims arise when a lender "treats a credit applicant differently based on one of the prohibited bases." Policy Statement on Discrimination in Lending, 59 Fed. Reg. at 18,268. Under the *McDonnell Douglas* burden of production scheme that governs disparate-treatment discrimination claims, the plaintiff must establish through inference a prima facie case of discrimination. McDonnell Douglas Corp. v. Green, 411 U.S. 792, 802, 804 (1973) (outlining prima facie, rebuttal, and pretext standards). Defendant lender's rebuttal that the subjective factor underlying the bank's adverse decision had a "manifest relationship to the creditworthiness of the applicant" will prevail unless met with further evidence from the plaintiff suggesting that the lender's proffered justification was purely a pretext for the prohibited discrimination. A.B. & S. Auto Serv. v. South Shore Bank, 962 F. Supp. 1056, 1061 (N.D. Ill. 1997). Given the discretion generally accorded to lending institutions by courts, nearly any factor—exclusive of race, religion, marital status, and gender—may be used to justify an adverse credit action. It is, therefore, undoubtedly difficult for plaintiffs in disparate treatment cases to establish that the lender's justification is pure pretext.

[84] Blatant evidence of bias is rare in racial discrimination cases. As the Fifth Circuit noted, racial discrimination is so insidious that there often "will be no 'smoking gun.'" Lodge v. Buxton, 639 F.2d 1358, 1363 n.8 (5th Cir. 1981), *aff'd sub nom.* Rogers v. Lodge, 458 U.S. 613 (1982); *see also supra* notes 82–83.

restrictions on lending against individuals with criminal histories. Under the traditional disparate impact analysis, the plaintiff must present statistical evidence indicating that the challenged action disproportionately harms one group of statutorily protected individuals. According to Regulation B, a policy document promulgated by the Federal Reserve Board to oversee lender compliance with the ECOA, defendant lenders may overcome the plaintiff's proof of disproportionate harm in one of two ways: by establishing either that (1) there is a measurable relationship between the information being used to determine creditworthiness and creditworthiness itself;[85] or (2) by establishing that the business need served by the creditor practice cannot be served by a less disparate procedure or policy.[86] However, neither the Act itself nor Regulation B offers guidance to lenders on how prospectively to determine creditworthiness in a manner that does not disparately impact members of the protected categories.[87]

The absence of a bright-line rule for determinations of creditworthiness leaves open the question of what forms of discriminatory behavior will be remediable by the ECOA,[88] and has left creditors with expansive discretion in this area.[89] Using a "gut sense"

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[85] Under ECOA, lenders generally are prohibited from the use of "information which is discriminatory in effect unless there is a statistically valid relationship between the criteria and creditworthiness." S. REP. NO. 102-167, at 86 (1991).

[86] The Regulation B guidelines require that the creditor practice in question meet a legitimate business need that "cannot reasonably be achieved as well by means that are less disparate in their impact." Equal Credit Opportunity Act (Regulation B), 12 C.F.R. pt. 202, supp. I (2004).

[87] Creditworthiness is defined by the *Equal Credit Opportunity Manual* as "a function of both the applicant's willingness and ability to pay the debt, and the creditor's rights and remedies with respect to property available for debt payment." CLONTZ, *supra* note 45, ¶ 1.05, at 1–19. Another author defines creditworthiness in these terms: "[T]o be 'creditworthy' is to be considered a suitable credit risk, qualified for an extension of credit by a particular creditor." GERRY AZZATA, EQUAL CREDIT OPPORTUNITY ACT ¶ 5.11, at 47–48 (2d ed. 1988).

[88] While the Fair Housing Act (FHA) and the ECOA both prohibit certain discriminatory lending practices in the mortgage lending market, only the ECOA offers a viable statutory basis for claims against lenders who engage in such practices in the small business loan market. Moreover, whereas HUD is the sole agency charged with enforcing the FHA, the ECOA may be enforced by various federal agencies, including the Federal Trade Commission. S. REP. NO. 102-167, at 85 (1991).

[89] To be sure, ECOA compliance also comes at a significant cost burden to the banking industry. *See, e.g.*, James F. Smith, *The Equal Credit Opportunity Act of 1974: A Cost/Benefit Analysis*, J. FIN. 609, 612–13 (1977). Costs of compliance under the ECOA include:

> [f]ees from legal counsel to interpret the regulation, approve new forms, and review various aspects of the regulation with the creditor[;] [t]raining costs to inform employees about the regulation and its implications for operating procedures[;] [c]osts for destroying old forms that can no longer be used[; and r]eprogramming to change computer systems to comply with the new regulations.

judgmental system of evaluation[90]—as opposed to a more empirically-derived formula—allows lenders to employ subjective criteria based on lenders' previous experience with, or stereotypes of, members of certain groups.

B. A.B. & S. Auto Service v. South Shore Bank

The disparate impact theory of discrimination, also known as the "effects test," has been litigated only once under the ECOA on behalf of an individual with a criminal history. In *A.B. & S. Auto Service v. South Shore Bank*,[91] the plaintiff, Jerry L. Bonner, an African-American and sole proprietor of an auto service shop, challenged under 42 U.S.C. § 1981 and ECOA the Bank's practice of taking into account an applicant's history of criminal convictions when considering applications for small business lines of credit. The facts of the case were undisputed by the parties.[92] Prior to submitting the loan guarantee request for Bonner's loan application, the SBA required the Bank to make an independent judgment concerning the applicant's criminal record "in evaluating the applicant's character and other relevant factors."[93] As the Bank's loan committee began consideration of Bonner's application, two members of the committee agreed that the loan should not be approved.[94] At that time, the committee members expressed concern over Bonner's criminal history as disclosed on the Form 912; specifically, the members "found the criminal record to reflect poorly on Bonner's judgment and character."[95]

Id. at 612–13. Smith estimates that the legal fees for commercial banks were some $2.4 million. *Id.* at 613. *See also* S. REP. NO. 95-915, at 26 (1978) (citing Smith, *supra*), *reprinted in* 1978 U.S.C.C.A.N. 9403, 9427 ("This was broken down into $127.5 million or $1.76 dollars per household in recurring costs every year under the Equal Credit Opportunity Act and $165.8 million or $2.28 per household in one time costs.").

90 The relevant factors in a judgmental system of evaluation are derived from any number of criteria, with the sole exception of those protected categories which are articulated in the ECOA, and may include address, nature of previous work, number of dependents, and history of criminal arrests and convictions.

91 962 F. Supp. 1056 (N.D. Ill. 1997).

92 In 1995, Bonner sought a business loan for A.B. & S. in the amount of $230,000 from defendant South Shore Bank. The Bank's inquiry into Bonner's eligibility for the business loan included the SBA Form 912. *Id.* at 1057–58. For a discussion of Form 912, see *supra* notes 38–43 and accompanying text.

93 *A.B. & S. Auto Serv.*, 962 F. Supp. at 1057–58.

94 Bonner disclosed on the Form 912 that he had been arrested and charged (but not convicted) for a series of criminal offenses, including domestic abuse, possession of controlled substances, disorderly conduct, and possession of a stolen car. He also disclosed on the form that he had once been convicted of aggravated battery for a stabbing in which Bonner claimed he acted in self-defense. *Id.* at 1058.

95 *Id.* At trial, the Bank argued that its general practice was to consider the criminal offenses of applicants on a "case-by-case basis and to utilize that information in evaluating the applicant's character and judgment which, in turn, is used in assessing the ability and

This "character"-based defense raises important questions about the use of "character" or other moral descriptives as a factor in determining creditworthiness.[96] The ability of lenders to invoke applicant "character" as a justification for adverse credit actions[97] stands to limit credit access subjectively, not based on one's ability to pay or credit history, but rather on the conclusions to be drawn from one's engagement with the criminal justice system.[98] In *A.B. & S.*, the applicant was a longtime resident of the community who had owned and operated his auto service center for several years. Based on the financial information submitted with his application, his *ability* to pay the debt was not in serious doubt. Concerns about his *willingness* to pay the loan—a subjective inquiry that looks to the intent of the borrower—were more difficult to allay, as is nearly every determination of a borrower's willingness to pay.

Although the plaintiff in *A.B. & S.* ultimately failed to satisfy the evidentiary burden required to overcome the Bank's motion to dismiss,[99] the disparate impact test may well provide an appropriate avenue for challenging the practices of lenders who request and consider an applicant's criminal record in a determination of creditworthiness. Under a totality of the circumstances analysis, as described below, proof of disproportionate policing, arrests, and convictions suffered by people of color may help to satisfy the mandate of the ECOA disparate impact standard.

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willingness of the applicant to repay the loan." *Id.* The trial court noted that the Bank also had a non-SBA loan program that required neither the filing of the Form 912 nor the disclosure of applicant criminal offense history. *Id.* at 1058 n.4.

96 The increasing use of "good character" as a prerequisite for obtaining certain occupational licenses has been cited as one of the factors contributing to the exclusion of ex-offenders from licensed trades. *See* Bruce E. May, *The Character Component of Occupational Licensing Laws: A Continuing Barrier to the Ex-Felon's Employment Opportunities*, 71 N.D. L. REV. 187, 188 (1995) (examining impact of state occupational licensing laws on felon employment).

97 An "adverse" credit action includes any denial or cancellation, or reduction, or unfavorable change in terms of a consumer or commercial credit line.

98 Credit and loan applications easily could solicit responses from any number of inquiries specifically designed to illuminate an applicant's character in relation to financial obligations, including: whether an applicant has ever been, or is currently, in arrears on any court-ordered family support obligation; whether an applicant has a history of "bouncing" checks; or whether an applicant has incurred a significant amount of unpaid parking tickets or moving violations.

99 The expert who testified on behalf of the plaintiff in *A.B. & S.* admitted that he knew of no studies indicating that African-Americans suffered disproportionately due to bank reliance on criminal history in making adverse credit actions. *See id.* at 1058–59. This Note proposes federally-mandated recordkeeping in this area, so as to facilitate the making of future claims and defenses on behalf of borrowers and banks. *See infra* Part IV.B.1.

C. *Towards a "Totality of the Circumstances" Disparate Impact Analysis*

Given the courts' longstanding recognition of the disproportionate policing and incarceration endured by communities of color,[100] the ECOA should be interpreted to include such disproportionality in a "totality of the circumstances" analysis that considers an assessment of the "disparateness" of adverse credit actions that are tied to criminal history. The Ninth Circuit has determined that, in examining disparate impact claims under the Voting Rights Act "totality of the circumstances" analysis, courts may consider the invidious history of racial discrimination in the criminal justice system.[101] This Note proposes a similar analysis under the ECOA—one that considers the effects of disproportionate policing and discrimination on criminal exposure.[102] This "effects" argument may be cognizable under the ECOA, as the test "prohibit[s] a creditor practice that is discriminatory in effect because it has a disproportionately negative impact on a prohibited basis, even though the creditor has no intent to discriminate and the practice appears neutral on its face."[103]

Offender reentry and fair lending advocates should be making these disparate impact arguments to federal courts in order to mitigate the harm that relying on criminal histories in credit applications poses to individuals and communities.[104] The disproportionate investigation, arrest, and conviction rates of people of color in this country are well-documented.[105] Even the courts have acknowledged that people of color—especially African-Americans—are disproportion-

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100 *See infra* notes 105–06 and accompanying text.

101 *See* Farrakhan v. Washington, 338 F.3d 1009, 1020 (9th Cir. 2003).

102 Such an analysis would require the trial court to consider evidence indicating that members of a certain racial group or women were disproportionately more likely to be members of a credit-disfavored group (e.g., ex-offenders or renters or bankruptcy filers).

103 Equal Credit Opportunity Act (Regulation B), 12 C.F.R. pt. 202, supp. I (2004).

104 This is, of course, not the first time that disparate impact has been lauded as the most appropriate method of remediating persistent discriminatory practices in lending. In their collaboration, Stephen Ross and John Yinger outlined the weaknesses in current fair-lending enforcement, concluding that the current regime fails to take seriously disparate impact claims, thereby insulating some lenders from scrutiny. *See* ROSS & YINGER, *supra* note 60, at 361.

105 *See* HOWARD N. SNYDER, U.S. DEP'T OF JUSTICE, JUVENILE JUSTICE BULLETIN: JUVENILE ARRESTS 2001, at 9 (2003) ("In contrast to their representation in the population, black youth were overrepresented in juvenile arrests for violent crimes, and, to a lesser extent, property crimes."), http://www.ncjrs.org/pdffiles1/ojjdp/201370.pdf. *See generally* Clarence M. Dunnaville, Jr., *Unequal Justice Under the Law—Racial Inequities in the Justice System*, VA. LAW., Dec. 2000, at 20 (detailing government findings of racial inequity in criminal sentencing and policy).

ately arrested and convicted.[106] In New Jersey, for example, eight out of ten prisoners are people of color.[107] Sixty-three percent of the state prisoners in New Jersey are Black, even though African-Americans comprise only fourteen percent of the state's population;[108] eighteen percent are Latinos. In the nation's capital, an estimated three-quarters of African-American men will be incarcerated in their lifetimes.[109]

The persistence of racial discrimination in these aspects of the criminal justice system—with the resulting disproportionality of individuals of color with criminal exposure—further militates against permitting lenders to limit access to credit on the basis of criminal history. This is especially true if and when an applicant's *arrest* record, as opposed to his or her conviction record, is viewed as indicative of character, and thereby an appropriate factor in a determination of creditworthiness. Arrests are, in fact, indicative of little except policing techniques and, as such, are at best a reflection of disproportionate policing in communities of color.[110] In New York City, for example, police enforcement is skewed from neighborhood to neighborhood—leaving poor and of-color communities to be more highly policed than others.[111] These disparities indicate that creditworthiness determinations which rely upon criminal exposure necessarily disproportionately impact minority applicants.

As outlined above, evidence of the disparate impact of adverse credit actions or practices on protected communities can be overcome in one of two ways: by proof of a measurable relationship between

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106 *See, e.g.*, Gregory v. Litton Sys., 316 F. Supp. 401, 403 (C.D. Cal. 1970) ("Negroes are arrested substantially more frequently than whites in proportion to their numbers."). The *Gregory* court went on to note "any policy that disqualifies prospective employees because of having been arrested . . . discriminates in fact against negro applicants." *Id.*; *see also* United States v. Clary, 846 F. Supp. 768, 782 (E.D. Mo. 1994) ("The . . . distorting effects of racial discrimination and poverty continue to be painfully visible in decisions to mete out criminal punishment.") (internal quotation marks and citations omitted) (ellipsis in original).

107 VINCENT SHIRALDI & JASON ZIEDENBERG, COSTS AND BENEFITS?: THE IMPACT OF DRUG INCARCERATION IN NEW JERSEY 10 (2003) (noting that Blacks and Latinos comprise roughly twenty-seven percent of state's population, but eighty percent of state's prison population), http://www.justicepolicy.org/downloads/nj-low.pdf.

108 *See* Kathy Barrett Carter, *N.J. Leads States in Disparity of Blacks in Prison*, STAR LEDGER (Newark), Jan. 7, 2004, at 1.

109 *See* Donald Braman, *Families and Incarceration*, *in* INVISIBLE PUNISHMENT, *supra* note 4, at 117.

110 *See* JANET B.L. CHAN, CHANGING POLICE CULTURE: POLICING IN A MULTICULTURAL SOCIETY 21 (1997) (describing how people of color are more likely than their white counterparts to be stopped or questioned by police).

111 Fagan et al., *supra* note 67, at 1568 (arguing that "racially-skewed street-level police enforcement" leads to disproportionate rates of incarceration in of-color neighborhoods).

the contested practice and risk, or by proof of a legitimate business practice that is served by the practice or policy.[112] Notably, neither the SBA nor the private banking industry has attempted to measure the relationship between criminal exposure and creditworthiness. Given the unavailability of empirical data measuring the relationship between criminal exposure and creditworthiness, it would appear that defendant lenders have few defenses to claims that any criteria prioritizing such exposure within the eligibility determination is prohibited by ECOA. Even assuming arguendo that there is a correlation between certain levels of criminal exposure (e.g., felony convictions and incarceration) and creditworthiness, the policy of restricting credit based on criminal exposure imposes far too many costs on members of our most vulnerable communities. The business need arguably served by the practice—mitigating risk for potential borrowers—certainly can be served better by alternative means, including utilization of a standard debt-to-income ratio. The debt-to-income ratio is a particularly appropriate proxy for risk, because it assesses those factors most salient to an applicant's likelihood of default, thereby allowing banks to make a larger number of profitable loans.[113] There is little reason to then penalize such potential borrowers twice—once as a result of their depressed wages, and again because of their criminal history.

Notwithstanding the vulnerability of such defenses, however, litigation challenges under ECOA are not likely to be successful. The dearth of available information about this particular aspect of underwriting frustrates efforts to seek remedies at law. Given this diminished likelihood of success, the next Part turns to a consideration of administrative and statutory remedies which may prove fruitful for progressive reentry strategists in this area.

IV
Other Remedial Measures

While the previous Part proposes a potential litigation strategy designed to combat the effects of restricting lending based on a history of criminal exposure, the adversarial process may not be the most effective way to address the concerns outlined above. It is in the interest of society as a whole that recidivism is not fostered by increasingly restrictive and unreasonably punitive collateral consequences. Given the limitations of litigation strategies to address this concern

112 *See supra* notes 85–86 and accompanying text.

113 Debt-to-income ratio utilization is, of course, no panacea for this population, as its use will still adversely affect ex-offenders given that such applicants likely will experience a lifetime wage reduction as a result of their criminal exposure. *See supra* notes 61–62 and accompanying text.

effectively, advocates should also push for statutory and administrative solutions to some of these issues. This Part considers the feasibility of potential regulatory solutions that could mitigate the effects of the financial industry's reliance on criminal history. While some local jurisdictions have taken steps to facilitate reentry through anti-discrimination regulation, these efforts have not always been successful. Given the difficulties facing local municipalities in effectuating their reentry policies through anti-discrimination legislation, the federal government should do more to help.

A. Local Law Protections for Ex-Offenders

Some municipalities have taken steps to remedy discriminatory practices through local anti-discrimination schemes. Some jurisdictions, for example, have attempted to remedy perceived gaps in fair lending laws with local legislation prohibiting discrimination in lending based on factors outside the purview of the federal fair lending acts, including the geographic location of the borrower or the property.[114] Similarly, some states have enacted anti-employment discrimination legislation with a focus on ex-offenders: Several currently prohibit employers from inquiring into the arrest records of potential employees, while others limit the information that an employer may use in an employment rejection.[115] The state of New York, for example, prohibits blanket employment discrimination against ex-offenders (with the exception of law enforcement employers), and the New York City Human Rights Code further limits the information that all employers (including law enforcement employers) may request or use in an evaluation of a given candidate.[116]

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[114] *See, e.g.*, N.Y. BANKING LAW § 9-f (McKinney 2001) (prohibiting refusal to make prudent loan upon security of real property because of geographic location of such property).

[115] Wisconsin, for example, categorically prohibits discrimination against individuals with criminal histories in the area of employment. *See* WIS. ADMIN. CODE § ER 43.01 (2003); *see also* CONN. GEN. STAT. ANN. § 31-51i(b) (West 2003) (prohibiting employer inquiries of erased criminal records); CONN. GEN. STAT. ANN. § 46a-80(d) (West 2004) (prohibiting arrest records from barring future employment by state or its agencies); HAW. REV. STAT. § 378-2(1)(A)–(B) (1993) (prohibiting discrimination in hiring or firing based on arrest or court record); R.I. GEN. LAWS § 28-5-7(7) (2003) (barring employer from inquiring into applicant's arrest record).

[116] New York is one of the more protective jurisdictions of ex-offender employment opportunities. New York state law prohibits employers and occupational licensors from denying an individual a job based on an arrest alone. With the exception of law enforcement, employers are prohibited from inquiring about arrests. In addition, New York law prohibits discrimination in employment based on convictions, and forces employers to consider applicants for jobs on a case-by-case basis, unless the nature of the offense is related to the job (e.g., child sex offender applying for day-care worker position). *See* N.Y. CORRECT. LAW § 752 (McKinney 2003). New York City also protects ex-offenders from licen-

These efforts have not, however, always been welcomed by statewide and national lenders, which claim that statewide laws regulating the banking industry preempt local laws that attempt to restrict the use of certain proxies for creditworthiness.[117] In a Wisconsin case considering the validity of a Madison ordinance banning certain discriminatory lending practices, and which included people with criminal convictions as members of a protected class, the state's highest court held that the state banking scheme preempted any local efforts to promulgate anti-discrimination legislation.[118]

In its holding, the court determined that the state statutory scheme for the regulation of banks—which included provisions prohibiting discrimination in lending on the basis of race, sex, marital status, or developmental disability[119]—preempted the field of lending discrimination to the exclusion of local municipalities.[120]

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sure or employment decisions that rely on "moral character" for determinations of eligibility. *See* N.Y.C. ADMIN. CODE § 8-107(10) (2003).

117 *See, e.g.*, Anchor Sav. & Loan Ass'n v. Equal Opportunities Comm'n, 355 N.W.2d 234, 238 (Wis. 1984) (outlining test for determining whether state law preempts power of municipality).

118 *Id.* at 240. In *Anchor Savings*, the Wisconsin Supreme Court considered whether a Madison ordinance banning discriminatory lending practices—and which included people with criminal convictions as members of a protected class—was preempted by the state's comprehensive banking code. *See id.* at 235–36. The defendant Commission found that a bank's consideration of an applicant's marital status constituted unlawful lending discrimination, thereby violating Section 3.23(3) of the Madison General Ordinances. *Id.* Madison General Ordinances Section 3.23(3) provided:

> It shall be an unfair discrimination practice and unlawful and hereby prohibited for any creditor to discriminate against any person in any credit transaction because of sex, race, religion, color, national origin or ancestry, age, handicap, marital status, source of income, arrest record or conviction record, less than honorable discharge, physical appearance, sexual orientation, political beliefs, or the fact that such person is a student as defined herein.

Id. at 236 n.1.

119 *See* WIS. STAT. § 138.20 (2004) (prohibiting lending discrimination on basis of developmental disability).

120 *See Anchor Sav. & Loan Ass'n*, 355 N.W.2d at 238. In crafting its analysis, the court considered whether the powers conferred upon the city by the local law provision of the state constitution limited the authority of the city to purely "local affairs." *Id.* at 237 (internal citations omitted). The court's analysis rested on a theory of preemption whereby the city's authority to regulate was contingent upon the state's determination that the regulation fell within the "constitutional initiative." *Id.* at 238 (internal citations omitted). In other words, the city's authority to regulate issues of statewide concern turned on whether the ordinance "infringe[d] the spirit of a state law or [was] repugnant to the general policy of the state." *Id.* (citing *Fox v. Racine*, 275 N.W. 513, 514 (Wis. 1937)); *see also* WIS. STAT. § 138.20 (2004). In its analysis, the court relied on the comprehensiveness of the state's "Fairness in Lending" legislation, which prohibits discrimination on the basis of race, sex, marital status, color, creed, religion, ancestry, or disability. *See* WIS. ADMIN. CODE § DFI-SB 8.03 (1997).

In state-local law conflicts, the preemption doctrine is implicated in one or more of three instances: first, under the "direct conflict" theory, state law prevails against local law if "there is a direct conflict between state law and a local law;"[121] second, state law trumps local law if the state's comprehensive regulatory scheme forecloses municipal legislation ("preempts the field");[122] and some states have retained the power, known as "denial authority," to restrict the power of local governments, even without enacting a state regulatory scheme of their own. Since legislation protecting ex-offenders from lending discrimination based solely on their status as ex-offenders does not implicate these fundamental concerns about state sovereignty, such legislative efforts should be allowed. As an initial matter, municipalities' interests in regulating offender reentry are profound. To the extent that *any* local law is crafted to facilitate this transition, the preemption doctrine should be construed narrowly so as not to trump the locality's interest in safe and productive reentry. Preemption should especially not be a barrier to protective enactments for individuals with criminal histories, if, as in *Anchor Savings & Loan Ass'n v. Equal Opportunities Comission*, that class finds no similar protection under applicable state law, or if the local legislation and state laws may coexist.[123]

State anti-discrimination laws can coexist unproblematically with local anti-discrimination laws. The city of New York, for example, includes people with criminal records as a protected class under the jurisdiction of the city's Human Rights Commission, even though the state of New York (which has a Home Rule provision in its constitution similar to that in Wisconsin's constitution) does not recognize a similar principle.[124] This is merely a difference; it is not a conflict. Similarly, while New York state law prohibits discrimination in lending based only on race, sex, religion, or marital status, the City's Administrative Code categorically prohibits discrimination in lending based on arrests and detentions, stating that criminal accusations that have not resulted in trial may not be used to act adversely upon appli-

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121 GERALD E. FRUG, ET AL., LOCAL GOVERNMENT LAW 254 (3d ed. 2001). Those states which permit municipal ordinances so long as there is no conflict are known as "home rule" states. *Id.* at 158–60. The preemption doctrine, as applied between states and the federal government, has been the subject of considerable scholarship. *See generally* Caleb Nelson, *Preemption*, 86 VA. L. REV. 225 (2000).

122 Those states which retain for themselves the exclusive power to regulate an entire field are known as "non home rule" states. *See* Larry T. Garvin, *Constitutional Limits on the Regulation of Laboratory Animal Research*, 98 YALE L.J. 369, 384–85 (1988).

123 *Cf.* WIS. ADMIN. CODE § DFI-Bkg 80.85 (2004) (prohibiting discriminatory lending practices on basis of sex or marital status).

124 *See* N.Y.C. ADMIN. CODE § 8-101 (2003).

cations for credit.[125] Any claim that state law has preempted the field of banking and lending regulation is undermined by the existence of municipal laws regulating the industry.[126]

Even if local efforts to regulate various forms of lending discrimination arguably might be preempted by state law, such efforts should nonetheless be insulated from preemption challenges. Given that the effects of such discrimination are experienced more acutely at the local level,[127] municipalities ought to be able to protect themselves effectively from lenders whose practices frustrate the efforts of communities to successfully reintegrate ex-offenders. Local governments are more attuned than the faraway state or federal government to the particular problems facing individuals in their communities. In addition, local legislation is more likely to reflect the commitments of local residents: Whereas state legislators are likely to trade the interests of residents of one locale for those of another, city politicians arguably face less diversity among constituents' interests. Any interest in statewide uniformity in underwriting simply does not outweigh the interests of municipalities that bear the burden of effectively reintegrating ex-offenders into their home communities. Given that anti-discrimination legislation need not always involve an overhaul of underwriting or loan risk assessment procedures for lenders, the restrictions imposed by a local law protecting ex-offenders from unfair discrimination would not interfere with the sound and uniform management of lending institutions throughout the state.

Local, state, and federal efforts to mitigate the difficulties of reentry should work in tandem and should not be hampered by the application of preemption doctrine. Just as municipalities are permitted to impose additional burdens on those convicted of crimes,[128] so too should those same municipalities be permitted to reduce the impact of collateral consequences. Since local regulation of lending

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125 *See* N.Y.C. ADMIN. CODE § 8-107(11) (2003).

126 Several municipalities specifically prohibit predatory lending practices and impose severe sanctions, including the potential loss of city contracts, on institutions that engage in such practices. *See, e.g.*, CHI. MUN. CODE § 2-32-455 (1999); N.Y.C. ADMIN. CODE § 6-128 (2003). In similar fashion, New York City imposes detailed disclosure requirements on tax-preparation services that offer refund anticipation loans. Local preparers offering such loans are required to disclose applicable interest rates, as well as the identity of the lending institution making the loan. *See* N.Y.C. ADMIN. CODE § 20-741.1 (2003).

127 *See supra* notes 67–71 and accompanying text.

128 *See, e.g.*, N.Y.C. ADMIN. CODE § 10-202(a) (2003) (holding those convicted of drug crimes liable to city "for a civil penalty in the amount of not less than ten thousand dollars nor more than one hundred thousand dollars for each count of an indictment"); N.Y.C. ADMIN. CODE § 13-161(e)(6)(b)–(c) (2003) (mandating immediate divestment from retirement pension program for any New York City Transit Authority employee convicted of felony).

discrimination neither directly conflicts with state banking law schemes, and lending discrimination does not fall within a category of laws that "preempt the field" to the exclusion of local experimentation, preemption should not foreclose future efforts to find local solutions to the problems identified here.

Moreover, even if concerns over potential conflicts in the area arise, since restrictions on local law experimentation with regard to easing the burdens on ex-offenders impede reintegration and impose further long-term costs on society, such experimentation ought to withstand the supremacy analysis which is at the heart of the preemption doctrine.

B. Federal Intervention

Criminal exposure is a particularly problematic proxy for ability and willingness to repay loans given the impact of overt and unconscious racism in the disproportionate policing and prosecution of African-Americans and Latinos, and therefore should not be used as such. One factor that may have contributed to lenders' consideration of criminal history in lending decisions may be the lack of readily-available information with which to assess the creditworthiness of certain applicants.[129] Information asymmetries that hinder appropriate determinations of creditworthiness may only be mitigated through federal intervention in the form of mandatory reporting.[130]

Because criminal exposure is arguably not more indicative of an applicant's willingness or ability to pay than an adverse credit action, such as a history of bankruptcy or charge-offs, this Section advocates strategies designed to remediate the effects of the consequences outlined above: improved federal record-keeping in this area, restrictions on the use of such information in determinations of creditworthiness, stronger enforcement of the protections of the Fair Credit Reporting Act (FCRA), and federal subsidization of business and other loans for individuals with criminal backgrounds (in the form of microlending initiatives).

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[129] Whereas the Home Mortgage Disclosure Act (HMDA) requires lenders to submit reports of the race and gender of mortgage applicants, along with acceptance rates, there is no similar statutory mandate for consumer credit or small business loans. *See* H.R. REP. NO. 100-955, at 16 (1988) (lamenting fact that "empirical documentation relating to access to business credit is lacking, due, in part, to the lack of record keeping in lending institutions").

[130] On asymmetries of financial information, see SIMON, *supra* note 72, at 27–28.

1. *Closing Relevant Information Gaps*

Improved federal record-keeping in this specific area of banking practice may illuminate the extent and effects of the practice. Statistics detailing the prevalence of discriminatory lending practices toward applicants with criminal histories are largely unavailable. Currently, banks are not required by statute or regulation to report or to track accurately the rates at which an applicant's criminal history is dispositive in a denial of credit. While the amount of publicly available information regarding racial and gender discrimination in lending is dictated by statute, there are no similar legislative mandates for aggregating the economic and social costs of limiting access to credit based on criminal exposure. Without this empirical information, it is nearly impossible to answer some lingering questions: How many applicants for business, home, or personal loans indicate some criminal exposure in their applications? How many of these applicants otherwise are qualified for such credit—in terms of their employment history, credit history, and debt-to-income ratio? What is the rate of acceptance for the "otherwise qualified" applicant pool? How many of these applicants are people of color?[131] The availability of such information also would facilitate the articulation of ECOA claims in efforts to challenge the practice.

The other relevant information gap is the unavailability of studies that directly correlate criminal exposure to risk of default. Although apparently neither lenders nor the federal government have studied this phenomenon, the Form 912 remains in use at every lending institution that offers federally-backed small business loans. The availability of such information would give content and legitimacy to lending decisions that currently may turn almost exclusively on the intuition of a lending officer that criminal history is indicative of a higher risk of default.[132] Moreover, given the potential disparate impact claims that the practice may give rise to, the availability of such information also would provide lenders with the data necessary to mount successful defenses to such claims.

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[131] In *A.B. & S.*, the court ultimately agreed with the defendants that, unless the plaintiff could cite empirical data indicating the rate of rejection of Black, ex-offender applicants in the bank's lending history, the claim must be rejected. A.B. & S. Auto Serv. v. South Shore Bank, 962 F. Supp. 1056, 1061 (N.D. Ill. 1997).

[132] Such decisions may also turn on actuarial information attesting to higher risk among this population; however, without available additional information, it is difficult to characterize these actions confidently based on actuarial data.

2. *Statute of Limitations on Materiality*

A statutorily mandated "limited-use provision" relating to disclosures of criminal exposure also may mitigate the undesirable effects of utilizing such information in determinations of creditworthiness. Congress has set similar "statutes of limitation" on the use of adverse credit actions in determinations of creditworthiness. The Fair Credit Reporting Act (FCRA), for example, requires that credit-reporting agencies cease to report an applicant's Chapter 11 or bankruptcy action after ten years, and any charge-offs may not be reported after seven years.[133] FCRA also forbids the reporting of arrest records that are older than seven years.[134] The FCRA apparently has not been seriously enforced, however; the SBA continues to require disclosure of all arrests, not just recent ones, on the Form 912.[135]

A provision denying banks the discretion to refuse loans to people on the basis of old criminal records, if inserted into the FCRA, would function in much the same way as a similar limited-use provision in the trial context. Federal Rule of Evidence 609(b), which governs the information admissible to impeach a witness, provides for the exclusion of evidence of a criminal conviction that is more than ten years old.[136] Although Rule 609 has exceptions, it can be understood to balance the factfinder's interest in the witness' capacity for truthfulness with an understanding that a conviction alone is not dispositive of character. A limitation of years on the use of such information in determinations of creditworthiness may function similarly.

3. *Further Use Restrictions*

Finally, the SBA (along with other federal agencies providing financial services and support) should consider altering those "personal information" forms which are required parts of the application,

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[133] *See* 15 U.S.C. § 1681c (2000). The Fair Credit Reporting Act restricts the inclusion of certain information in consumer credit reports as follows:

> [N]o consumer reporting agency may make any consumer report containing any of the following items of information: [C]ases under title 11 [of the United States Code] or under the Bankruptcy Act that, from the date of entry of the order for relief or the date of adjudication, as the case may be, antedate the report by more than 10 years. Civil suits, civil judgments, and records of arrest that, from the date of entry, antedate the report by more than seven years or until the governing statute of limitations has expired, whichever is the longer period. . . . Accounts placed for collection or charged to profit and loss which antedate the report by more than seven years.

Id. § 1681c(a)(1)-(4).

[134] *Id.* § 1681c(a)(2).

[135] Any inquiry into the viability of claims under the Fair Credit Reporting Act (FCRA) is beyond the scope of this Note.

[136] *See* FED. R. EVID. 609(b).

so as not to disclose an applicant's criminal exposure to potential lenders. Especially for those lenders who do not seek this information on their own applications, the government should not be in the position of erecting additional barriers to the availability of credit. This is especially true given the precision, care, and personal responsibility which is required to complete the application processes properly for small business and mortgage loans. Moreover, the inclusion of this inquiry on the SBA form may act as a signal to private lenders that criminal exposure somehow is indicative of creditworthiness, even though such a relationship has not been established.

To the extent that lenders are unable to access an applicant's criminal record from a consumer credit report,[137] lenders similarly should be unable to require that applicants themselves divulge that information.[138] The FCRA currently prohibits use of some publicly available crime file data in credit eligibility determinations.[139] While the text of the FCRA explicitly excludes "records of convictions of crimes" from its protections,[140] the Act does not exclude records of arrest from its protections.[141] Although the primary concern of the FCRA is to protect borrowers against banks' use of inaccurate information, and requiring an applicant to report her own criminal exposure undeniably mitigates some potential inaccuracies, forcing applicants to divulge information about previous criminal exposure may work as a disincentive for embarrassed but otherwise-qualified applicants, thereby encouraging cash-only local economies and potentially perpetuating the crippling cycle of recidivism.[142]

4. *Federal Subsidization*

Federal subsidization of loans to applicants with criminal histories may help promote financial responsibility and independence for ex-

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[137] The three leading consumer credit reporting agencies are Equifax, TransUnion, and Experian.

[138] One federal court, in examining the legality of an employer practice that required the disclosure of past arrests, stated that restrictions on such information should be enforced in order to effectuate the policies of federal civil rights legislation. According to the court, employers should not be allowed to request information that remained outside of the public domain, i.e., arrests. *See* Gregory v. Litton Sys., 316 F. Supp. 401, 403 (C.D. Ca. 1970) (noting that "Negroes are arrested substantially more frequently than whites in proportion to their numbers. . . . Thus, any policy that disqualifies prospective employees because of having been arrested . . . discriminates in fact against negro applicants.").

[139] 15 U.S.C. § 1681c(a)(5) (2000).

[140] *See* 15 U.S.C. § 1681c(a)(5) (2000) (extending protection to "[a]ny other adverse item of information, other than records of convictions of crimes which antedates the report by more than seven years").

[141] *See id.* § 1681c(a)(2).

[142] *See supra* Part I.

offenders. Such intervention on the part of the federal government is not rare.[143] Rather than focus on the correlation between criminal exposure and probability of default, federal subsidies could be used to make credit and business ownership affordable for this population, especially given the difficulties that ex-offenders face in securing stable, at-will employment. Initiatives such as this, which are designed to promote self-sufficiency and economic development, mirror microlending initiatives, which have been hailed widely as one of the best available tools in the fight against poverty and joblessness.[144]

CONCLUSION

> *America is the land of second chance, and when the gates of the prison open, the path ahead should lead to a better life.*
>
> *-President George W. Bush*[145]

Prohibitions on the use of criminal history as a proxy for creditworthiness would impose some costs. Even if lenders are unable to use this information to screen applicants initially, it is likely that such information would be used when setting higher-than-average interest rates. Given the consequences to individuals and communities, these attendant incremental costs simply do not justify the burdens borne by offenders and their home communities if credit is limited to those with little or no interaction with the criminal justice system.[146] Banking policies that focus exclusively on likelihood of default are simply shortsighted: It is possible to imagine a system

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[143] *See Microlending Is Latest Trend in Business Assistance*, RURAL CONDITIONS & TRENDS, Sept. 1999, at 18 ("In those cases where businesses are startups or where information gaps preclude lenders from properly assessing loan potential, Federal programs provide more direct sources of debt and venture capital."), *available at* http://www.ers.usda.gov/publications/rcat/rcat101/rcat101d.pdf.

[144] *See* Louise A. Howells, *The Dimensions of Microenterprise: A Critical Look at Microenterprise as a Tool to Alleviate Poverty*, 9 J. AFFORDABLE HOUSING & COMMUNITY DEV. L. 161, 161 (2000) (discussing microenterprise programs' success in filling significant credit gaps). The federal government has recognized its duty to help effectuate smooth transitions for ex-offenders. The Federal Bonding Program, for example, offers bonding to cover potential tort liability (under theories of negligent hiring) to some employers who hire ex-offenders. The Federal Bonding Program is sponsored by the Department of Labor and provides bonding insurance to employers willing to hire certain high-risk job applicants who may otherwise be denied coverage from commercial bond carriers. The bonds protect employers against theft, forgery, larceny, and embezzlement. *See* Fidelity Bonding website, *at* http://www.bonds4jobs.com/bondingprogram.html (last visited Apr. 25, 2005).

[145] Bush, *supra* note 32.

[146] Claims that prohibiting the use of certain borrower characteristics as a proxy for risk impose unfair costs on the rest of society have been raised to justify various forms of exclusionary lending practices, including redlining, and Congress and the courts generally have rejected these arguments as illegitimate.

where, as a society, we aim to put people in a position of financial security where they do *not* have to default. In balancing a commitment to rehabilitation against the societal desire to punish, this Note proposes several strategies to mitigate the effects of disproportionate policing and convictions on the ability of some of our more vulnerable communities to access badly-needed financial resources.

These possibilities need not force lenders to make bad loans as they can continue to use set formulas for ascertaining risk probabilities.[147] The federal government itself recognizes that nondiscriminatory lending policies need not abrogate good business policies.[148] Whether or not it makes business sense for banks, the costs of their reliance on criminal exposure as a predictor of creditworthiness is simply too great. Banks' unwillingness to lend contributes to individual stigma, community harms, and helps create a cycle in which future unlawful activity is the only alternative open to many. This has a disproportionate impact on minorities and the poor, and itself contributes to the very recidivism that makes felons such poor credit risks. Even if that credit ultimately costs more, credit is far too important to modern economic engagement to be limited solely on the basis of criminal exposure.

This Note has attempted to draw useful connections between advocates' concerns over the expansion of collateral consequences for criminal convictions and the future of fair lending in an age of easy access to personal information. In the context of lending practices that discriminate against individuals with criminal arrests and convictions, an "effects" analysis may go a long way toward establishing that the practice of limiting credit opportunities based solely on criminal convictions indirectly discriminates based on race. These effects should not be underestimated: One such effect is the hindrance of community development initiatives that rely upon the credit capacity of community residents. Perhaps more importantly, another effect is the frustration of efforts to reintegrate individuals into their home communities. If denying credit because of past criminal convictions

147 There are five traditional measures of risk pertaining to credit evaluations: character, capital, capacity, collateral, and cycle conditions. *See* ANTHONY SAUNDERS, CREDIT RISK MEASUREMENT: NEW APPROACHES TO VALUE AT RISK AND OTHER PARADIGMS 8 (1999). The most commonly used formulas in assessing creditworthiness are debt-to-income ratio and history of prior defaults. For prospective borrowers with recent criminal histories—especially incarcerations—the debt-to-income ratio necessarily will be affected by the gap in work history. Under the model proposed in this Note, those gaps in work history—not the incarceration which produced them—would factor into a determination of creditworthiness.

148 *See* Policy Statement on Discrimination in Lending, 59 Fed. Reg. 18,266, 18,267 (1994) ("[F]air lending is not inconsistent with safe and sound operations.").

circumvents the letter and the spirit of our laws and policies promoting the smooth reentry of individuals with criminal records into the community, then our criminal justice policies (even if effectuated through our fair lending jurisprudence) should attempt to mitigate those negative effects.