DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Part 100

[Docket No. FR–4160–P–01]

RIN 2529–AA82

HUD's Regulation on Self-testing Regarding Residential Real Estate-Related Lending Transactions and Compliance With the Fair Housing Act

AGENCY: Office of the Assistant Secretary for Fair Housing and Equal Opportunity, HUD.

ACTION: Proposed rule.

SUMMARY: This rule proposes to implement section 2302 of the Economic Growth and Regulatory Paperwork Reduction Act (Pub. L. 104–208) (''Act''), which encourages voluntary compliance by lenders with the Fair Housing Act (FHAct) and the Equal Credit Opportunity Act (ECOA) through lender-initiated self-tests of lenders' residential real estate-related lending transactions and, where appropriate, corrective action designed to remedy any possible violations of the FHAct or ECOA revealed by such tests.

DATES: Comment due date: March 3, 1997.

ADDRESSES: Interested persons are invited to submit comments regarding this proposed rule to the Rules Docket Clerk, Office of General Counsel, Room 10278, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410. Communications should refer to the above docket number and title. A copy of each communication submitted will be available for public inspection and copying between 7:30 a.m. and 5:30 p.m. weekdays at the above address. FAXED comments will not be accepted.

FOR FURTHER INFORMATION CONTACT: Peter Kaplan, Director, Office of Policy and Regulatory Initiatives, Fair Housing and Equal Opportunity, (202) 708–2904. Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410. A telecommunications device for hearing- and speech-impaired persons (TTY) is available at (202) 708–9300 (these are not toll-free telephone numbers).

SUPPLEMENTARY INFORMATION:

I. General. Incentives for Self-testing and Self-correction

Background:

Section 2302 of the Omnibus Consolidated Appropriations Act for Fiscal Year 1997 (Pub. L. 104–208, approved September 30, 1996) (''Act''), found in Title II of the Act, entitled the ''Economic Growth and Regulatory Paperwork Reduction Act,'' creates a legal and administrative enforcement privilege for ''self-tests'' conducted by entities engaged in residential real estate-related lending to determine compliance under the Fair Housing Act (''FHAct'') and the Equal Credit Opportunity Act (''ECOA'').

Congress has declared that the results of ''self-testing'' should be protected by enabling lenders to assert a privilege against divulging the results of self-tests under precisely limited circumstances. The privilege arises only if the self-test leads to the adoption of remedies to correct any possible violations discovered.[1] Congress did not intend for violations to be known by lenders and not be remedied.

For purposes of the FHAct, under section 2302 of the Act (which adds a new section 814A to the FHAct), a report or result of a self-test is considered privileged if a lender conducts, or authorizes an independent third party to conduct, a self-test of a real estate-related lending transaction to determine the level or effectiveness of compliance with the FHAct, has identified any possible violations of the FHAct, and has taken, or is taking, appropriate corrective action to address the possible violations.

The Act requires HUD, with respect to the FHAct, and the Federal Reserve Board, with respect to the ECOA, to define self-testing in substantially similar regulations within six months of enactment of the Act. To address this requirement, this proposed regulation has been drafted in consultation with the Federal Reserve, following discussion with the Department of Justice, and appropriate federal financial regulators, including the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the National Credit Union Administration, and the Federal Trade Commission.

II. Proposed Regulatory Provisions

The proposed amendment to the FHAct would implement the Omnibus Consolidated Appropriations Act for Fiscal Year 1997 (Pub. L. 104–208, approved September 30, 1996) by defining what constitutes a privileged self-test. The Department proposes to define a ''self-test'' as any program, practice or study that a lender voluntarily conducts or authorizes a third party to conduct that creates data or factual information that is not available, and cannot be derived, from actual loan or application files or other records related to credit transactions, to determine the extent or effectiveness of the lender's compliance with the Fair Housing Act. This includes but is not limited to the practice of using fictitious loan applicants (''testers''), and may cover all or any part of a residential real estate lending transaction. The privilege would apply to the factual information generated by the self-test as well as any analysis or conclusions contained in reports prepared about the self-test. A self-test would not include any collection of data required by law or by any government authority, or a lender's review or evaluation of actual loan or application files.

The Act provides that once the rule is in effect, self-tests would become privileged even if they were conducted before the regulation's effective date. As an exception to this, self-tests previously conducted will not be privileged if, before that date, a complaint against a lender: (1) Was formally filed in any court of competent jurisdiction or (2) was the subject of an administrative law proceeding or had been formally filed with HUD or a substantially equivalent agency. In addition, a self-test previously conducted will not become privileged on the regulation's effective date if any part of the report or results has already been disclosed.

III. Section-by-Section Analysis of Proposed Rule

Section 100.140 Incentives for self-testing and self-correction

Section 100.140 would state the general rule that the report or results of a lender's self-test are privileged if the required conditions specified in this rule are satisfied. The privilege applies whether the lender conducts the self-test or employs the services of a third-party. However, a self-test must be conducted voluntarily; self-tests that are required by a government authority, including those conducted pursuant to a judicial order or directed by a Federal or state regulator, would not qualify for the privilege. Similarly, any collection of data required by law would not be considered voluntary under this rule. The privilege for self-testing is in addition to and independent of any other privilege that may exist, such as the attorney-client privilege or the privilege for attorney work product.

Section 100.141 Corrective action required

This section implements the requirement imposed by the Act that a

[1] Senate Report 104–185, page 15.

lender take appropriate corrective action to address any possible violations identified by the self-test in order for the privilege to apply. A lender must take whatever actions are reasonable given the nature and scope of the possible violations to fully remedy both their cause and effect(s). This may include both prospective and retroactive relief. Guidance on a lender's responsibility for taking appropriate corrective action is provided under § 100.144.

Although corrective actions are required when a possible violation is found, a self-test is also privileged when it does not identify any possible violations and no corrective action is necessary. The Department believes that the effectiveness of the privilege as an incentive to self-test would be significantly undermined if it only applied when violations were discovered. If that were the case, the mere assertion of the privilege would be tantamount to an admission that violations occurred. Under such circumstances, some lenders might be reluctant to engage in self-testing in light of the fact that the mere assertion of the privilege might prompt the filing of legal claims. In addition, a lender's findings made as a result of a self-test might be influenced by a perceived need to establish the self-test's eligibility for the privilege.

The Department also notes that a lender's determinations about the type of corrective action needed, or a finding that no corrective action is required, would not be conclusive in determining whether the requirements of this paragraph have been satisfied. If a claim of privilege is challenged, it would be necessary to assess the need for corrective action and the type of corrective action that is appropriate based on a review of the self-testing results. Such an assessment might be accomplished by an adjudication where the judge may conduct an in camera inspection of the privileged documents, or by the methods described in the section of this preamble pertaining to § 100.148. This section also recognizes that the privilege may be asserted by a lender even though the applicability of the privilege cannot be finally determined because the appropriate corrective actions have not yet been completed. To assert the privilege, a lender must be in the process of taking corrective actions which, at the minimum, requires establishing a plan for corrective action, a means for monitoring the lender's progress in implementing the plan, and activity to begin carrying out the plan. In such cases, a final decision on whether the privilege applies might be withheld pending the lender's having shown substantial progress in taking corrective action on a schedule imposed or agreed to by an agency or court, or by the other parties affected.

Section 100.142 Definitions

Lender, for purposes of this subpart only, means a person who engages in a residential real estate-related lending transaction.

Residential real estate-related lending transaction means the making of a loan:

(1) For purchasing, constructing, improving, repairing, or maintaining a dwelling; or

(2) Secured by residential real estate.

Self-test. This section would state what constitutes a ''self-test'' for purposes of this rule. The Act does not define ''self-test'' and authorizes the Department to define by regulation the practices to be covered by the privilege. The possible range of definitions includes a wide variety of practices, from matched pair testers to any form of self-assessment or self-evaluation.

In establishing the self-testing privilege, the Congress sought to encourage lenders to undertake voluntary efforts to assess their compliance with fair lending laws. In particular, the proposed definition is a needed incentive for lenders to use self-testing to monitor the pre-application stage of the loan process. See S. Rept. 104–185 at 15 (1995); GENERAL ACCOUNTING OFFICE, GAO/GGD–96–145, FAIR LENDING 10, 72 (1996). The pre-application process does not typically produce the type of documentation that lends itself to traditional file reviews. The privilege serves as an incentive, by assuring that evidence of discrimination voluntarily gathered through a self-test will not be used against a lender, provided the lender takes appropriate corrective actions for any possible discrimination found. Although the legislative history focuses on the traditional use of fictitious loan applicants in ''matched pair'' testing, it also recognizes the utility of other testing methods.

The Department is proposing to define a ''self-test'' as any program, practice or study that a lender voluntarily conducts or authorizes a third party to conduct that creates data or factual information that is not available, and cannot be derived, from actual loan or application files or other records related to credit transactions, to determine the extent or effectiveness of the lender's compliance with the Fair Housing Act. This definition includes but is not limited to the practice of using fictitious loan applicants (''testers''). For example, self-testing would also include a survey of mortgage customers conducted by the lender for fair lending purposes, or a specially designed test to evaluate loan officers' knowledge about fair lending laws.

Under the proposed rule, the principal attribute of self-testing is that it constitutes a voluntary undertaking by the lender to produce new factual information that otherwise would not be available or derived from actual loan or application files or other records related to credit transactions. The proposed rule does not define ''self-test'' so broadly as to include all types of self-evaluation or self-assessment performed by a lender. Self-evaluations based on lender reviews of actual loan or application files or other records related to credit transactions, and reviews of HMDA and similar types of records (such as broker or loan officer compensation records) that do not produce new factual information about a lender's compliance which cannot be derived from those files or records would not be covered by the privilege. Accordingly, a compilation of data or a regression analysis derived from the data in actual loan or application files would not be privileged.

A broader definition encompassing such audits or evaluations is within the Department's rulemaking authority under the statute. Principles of sound lending dictate that a lender have adequate policies and procedures in place to ensure compliance with applicable laws and regulations, and that lenders adopt appropriate audit and control systems. These may take the form of compliance reviews, file analyses, the use of second review committees, or other methods that examine lender records kept in the ordinary course of business. Notwithstanding any evaluation performed by the lender, the underlying loan records are themselves subject to examination by the supervisory and law enforcement agencies and must usually be disclosed to a private litigant alleging a violation. The Department believes that lenders already have adequate incentive to conduct such routine compliance reviews and file analyses as a good business practice to avoid or minimize potential liability for violations.

At this time, the Department does not believe it is appropriate to extend the privilege to audits of actual business records and make unavailable to private litigants and to supervisory agencies records lenders currently maintain as part of routine fair lending activities. This could have an unintended negative effect on the levels of cooperation between lenders and the supervisory

agencies and on actions by private litigants under the FHAct. The Department is soliciting public comment, however, on the scope of the proposed definition of ''self-test'' and how the definition could allow innovative, effective, non-routine lender monitoring and self-correction without unduly affecting the ability of aggrieved persons, complainants, departments, or agencies to obtain needed information for enforcement of the FHAct or to monitor compliance with that law. Comments should include specific regulatory language as well as criteria for, and examples of, types of activities that would be included and not included in the revised definition.

In order to qualify for the privilege, a self-test must be designed and conducted to assess the level or effectiveness of the lender's compliance with the rules prohibiting discrimination. Testing for compliance with the other requirements is not privileged. For instance, a self-test designed for other purposes, such as to observe employees' efficiency and thoroughness in meeting customer needs, is not covered by the privilege even if evidence of discrimination is uncovered incidentally.

Section 100.143 Types of information

This section would clarify that the types of information that would be covered by the privilege would include draft documents and work papers, as well as the final results or report of the self-test. The Act does not prohibit an aggrieved person, complainant, department or agency from requesting information about whether a lender has conducted a self-test. This section clarifies that the privilege does not prevent an aggrieved person, complainant, department or agency from obtaining information sufficient to determine whether to seek the final results or report. The fact that a lender has conducted a privileged self-test, as well as the time period, the methodology, and the geographic location of that self-test are not privileged. This ensures that the tests about which the privilege is asserted can be properly identified in any proceeding.

The Act provides that a challenge to a lender's claim of privilege may be filed in any court or administrative law proceeding with appropriate jurisdiction. The Department expects such challenges to be resolved according to the laws and procedures used for other types of privilege claims. This may include the use of in camera proceedings, the filing of documents and pleadings with the court under seal, or the production of documents to other parties under an appropriate protective order that limits the purpose for which they be used.

Section 100.144 Appropriate corrective action

Congress intended for the self-test privilege to apply only where self-correction follows self-testing. The language of sec. 2302 is identical to section 302 of an earlier bill on this issue, S. 650. The Committee Report on S. 650, Senate Report 104–185, in discussing sec. 302, reinforced the link between the discovery of potential violations and corrective remedial action.[2]

This section clarifies that a determination of whether a lender has taken appropriate corrective action must be made on a case-by-case basis. In April, 1994, the Interagency Task Force on Fair Lending, comprised of officials from the 10 federal agencies responsible for implementing and enforcing the fair lending laws, issued a policy statement on credit discrimination.[3] That policy statement advised lenders that discover discriminatory practices as a result of a self-test to ''make all reasonable efforts to determine the full extent of the discrimination and its cause'' and to ''determine whether the practices were grounded in defective policies, poor implementation or control of those policies, or isolated to a particular area of the lender's operations.'' The policy statement also provided a list of sample corrective actions that might be appropriate depending on the circumstances, while recognizing, however, that not all corrective measures listed would be appropriate in every case.

The proposed rule reflects the 1994 Interagency Policy Statement regarding corrective action. A lender must take corrective action that is reasonable in light of the potential violations to fully remedy both the cause and effect of any possible violation. It must be commensurate with the scope of the discrimination and specifically tailored to address the particular type of problem identified by the self-test.

To determine the appropriate corrective action, the lender must: (i) Identify the policies and practices that are the likely cause of the possible violation, such as inadequate or improper lending policies, failure to implement established policies, employee conduct, or other causes; and (ii) assess the extent and scope of any potential violation, by determining which areas of the operations are likely to be affected by those policies and practices. This would include identifying the stages of the loan application process, types of loans, or the particular branch where the possible discrimination has occurred.

For example, where a pre-application test reveals that potential borrowers in minority areas are not offered or made aware of the full range of available loan products and that borrowers in non-minority areas are offered or made aware of the full range of products, the lender should examine its marketing, sales, and outreach activities generally and the practices of individual branches and implement actions to address the results of the test.

The extent of this corrective action should be contrasted with the action appropriate where a test by a lender reveals disparate treatment with respect to a specific minority group at a single branch. In this situation, an examination of all branch loan officer activities would be appropriate, as would: A review to determine if there are other potential victims of disparate treatment at the branch; training; offers to extend credit and/or offers to provide compensation for damages to potential victims; notifications to potential victims regarding their legal rights; and appropriate monitoring procedures.

If a self-test reveals that loan officers discourage the submission of loan applications by minorities by quoting more onerous loan terms, such as larger down-payments or higher interest rates, retroactive relief may also be required. Appropriate corrective action also would include reviewing of actual loan files to determine if minority borrowers were actually granted loans on less favorable terms, and providing them with more favorable loans.

Section 100.145 Scope of privilege

This section explains the nature of the qualified privilege afforded by the Act. It states that privileged documents may not be obtained by an aggrieved person, complainant, department or agency for use in an examination or investigation relating to fair lending compliance or in any administrative or civil proceeding in which a violation of the FHAct is alleged. There may be other proceedings where the privilege would not apply, for example, in litigation unrelated to fair lending issues.

[2] ''The purpose of this provision is to encourage institutions to undertake candid and complete self-tests for possible fair lending violations and to act decisively to correct any discovered problems. The privilege ensures that such self-test efforts will not be used against an institution if that institution has undertaken remedial action.'' (emphasis added) Senate Report 104–185, page 15.

[3] 59 FR 18266, 18270–71 (April 15, 1994).

Section 100.146 Loss of privilege

This section explains the circumstances that would result in documents losing their privileged status. Generally, as provided in the Act, the results or report of a self-test, including any data generated by the self-test, will not be considered privileged under this section once the lender—or the lender's officers, employees, agents or contractors—has voluntarily disclosed all or any part of the contents to an aggrieved person, complainant, department or agency or to the general public. Also, if a lender elects to rely on the self-testing results as a defense to alleged violations of the FHAct, the privilege would not apply as the disclosure is voluntary.

Under the proposed rule, a lender's involuntary production of records in response to a judicial order, or a voluntary disclosure under circumstances where the privilege does not apply, does not necessarily evidence the lender's intent to give up the privilege. Accordingly, if such disclosures are made in a limited fashion that does not constitute a disclosure to the general public, e.g., under a protective order, it would not affect the privileged status of the documents.

The statute also provides that the report or results of a self-test are not privileged if they are disclosed by a person with lawful access to the report or results. Accordingly, disclosures made by such persons are treated as disclosures made by the lender, without regard to whether the person was authorized to make the particular disclosure.

The results or report of a self-test would not be privileged where a lender seeks to assert the privilege, but is unable to produce records or information pertaining to the self-test necessary to determine whether the requirements for the privilege have been met.

The Department solicits comments on whether it should establish by regulation a provision whereby lenders could voluntarily share privileged information with a federal or state bank supervisory or law enforcement agency without causing the information to lose its privileged status when it is subsequently sought by private litigants. However, such disclosures would cause the documents to lose their privileged status with respect to all supervisory and law enforcement agencies. Would an expanded privilege for information voluntarily shared with a federal or state bank supervisory or law enforcement agency carry out the intent of Congress to provide a privilege only insofar as it is necessary to supply an incentive to lenders, without lessening the responsibility of regulators to refer potential violations to the agency?[4] Would this approach provide further incentives to lenders while encouraging greater cooperation between lenders and the supervisory/enforcement agencies and assuring that appropriate self-correction has occurred through their oversight?

Section 100.147 Limited use of privileged information

This section provides for a limited use of privileged documents that will not be treated as a voluntary disclosure affecting the privileged status of the documents under § 100.145. The report or results of a privileged self-test may be obtained and used solely for the purpose of determining a penalty or remedy after a violation of the Act has been formally adjudicated or admitted. The production of privileged documents for this purpose does not necessarily evidence the lender's intent to give up the privilege. If such disclosures are made in a limited fashion that does not constitute a disclosure to the general public, the disclosure would not affect the privileged status of the documents.

A finding by a government agency, as part of a bank examination or investigation, that discrimination has occurred would not constitute an adjudication for this purpose. If such findings lead to formal adjudication or an admission by the lender, the limited use of privileged documents under this section would apply.

The Act provides that information disclosed for purposes of determining a penalty or remedy may be used only for the particular adjudication or proceeding in which the adjudication or admission is made. Accordingly, parties who obtain such information may be prohibited from any further dissemination.

Section 100.148 Adjudication

The Act provides that the privilege may be challenged in any court or administrative law proceeding with appropriate jurisdiction. The Department expects such challenges to be resolved according to the laws and procedures used for other types of privilege claims, such as attorney-client or attorney work product. This may include the use of *in camera* proceedings, the filing of documents and pleadings with the court under seal, or the production of documents to other parties under an appropriate protective order that limits the purpose for which they may be used. The determination shall include consideration of whether appropriate corrective action has been taken, using the criteria set forth in the explanation of ''appropriate corrective action'' in § 100.144.

It is further expected that these rulings will turn on the evidence involved in each case. It is not expected, nor intended, that to invoke the privilege the respondent must have taken each corrective measure listed for each possible instance of discrimination.

Section 100.149 Effective date

Lenders and others may invoke the self-testing privilege regarding self-tests undertaken prior to the effective date of the regulations, but not if either a formal complaint has been filed involving matters covered by the self-test, or if the privilege has been lost pursuant to § 100.146. A formal complaint includes one filed with HUD or a substantially equivalent agency, pursuant to subsection 810(f) of the FHAct, alleging a violation of the FHAct. A complaint filed in a court with jurisdiction over the FHAct also qualifies as a ''formal complaint.'' Any other interpretation would conflict with Congress' intent in the Fair Housing Amendments Act of 1988 to establish an administrative process that is an equally effective alternative to the filing of a complaint in a Federal court.

Findings and Certifications

Justification for Shortened Comment Period

It is the policy of the Department, consistent with 24 CFR part 10, that its notices of proposed rulemaking are to afford the public not less than sixty days for submission of comments. A shortened comment period is necessary for this proposed rule to ensure promulgation of a final rule within six months of enactment of the Act, as required by the authorizing statute. A substantially similar proposed rule by the Federal Reserve has been published in the Federal Register previously. To ensure broad and timely public review and comment, the Department is making available today the text of and preamble of this proposed rule on its World Wide Web site (http//www.HUD.gov).

Regulatory Planning and Review

This proposed rule has been reviewed in accordance with Executive Order

[4] ''This provision does not change the mandatory referral requirement for pattern and practice violations of ECOA or FHA.'' Senate Report 108–105, page 15. Similar referral requirements exist between the financial regulatory agencies and the Department.

12866, issued by the President on September 30, 1993 (58 FR 51735, October 4, 1993). Any changes to the proposed rule resulting from this review are available for public inspection between 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, local and tribal governments and the private sector. This proposed rule does not impose any Federal mandates on any State, local or tribal governments or the private sector within the meaning of the Unfunded Mandates Reform Act of 1995.

Environmental Impact

In accordance with 40 CFR 1508.4 of the regulations of the Council on Environmental Quality and 24 CFR 50.19(c)(1) of the HUD regulations, the policies and procedures contained in this proposed rule do not direct, provide for assistance or loan and mortgage insurance for, or otherwise govern or regulate property acquisition, disposition, lease, rehabilitation, alteration, demolition, or new construction, or set out or provide for standards for construction or construction materials, manufactured housing, or occupancy, and therefore, are categorically excluded from the requirements of the National Environmental Policy Act.

Impact on Small Entities

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)) has reviewed and approved this proposed rule, and in so doing certifies that this proposed rule will not have a significant economic impact on a substantial number of small entities, because the proposed rule only proposes to implement a statutory provision that allows an evidentiary privilege for the report and results of self-tests of Fair Housing Act compliance undertaken by lenders.

Federalism Impact

The General Counsel has determined, as the Designated Official for HUD under section 6(a) of Executive Order 12612, Federalism, that this proposed rule does not have federalism implications concerning the division of local, State, and federal responsibilities. The proposed rule only proposes to implement a statutory provision that allows an evidentiary privilege for the report and results of self-tests of Fair Housing Act compliance undertaken by lenders.

Impact on the Family

The General Counsel, as the designated official under Executive Order 12606, The Family, has determined that this proposed rule would not have significant impact on family formation, maintenance, and general well-being. The rule only proposes to implement a statutory provision that allows an evidentiary privilege for the report and results of self-tests of Fair Housing Act compliance undertaken by lenders.

List of Subjects in 24 CFR part 100

Aged, Fair housing, Individuals with disabilities, Mortgages, Reporting and recordkeeping requirements.

Accordingly, part 100 of title 24 of the Code of Federal Regulations is proposed to be amended as follows:

PART 100—DISCRIMINATORY CONDUCT UNDER THE FAIR HOUSING ACT

1. The authority citation for part 100 continues to read as follows:

Authority: 42 U.S.C. 3535(d), 3600–3620.

2. In subpart C, new §§ 100.140, 100.141, 100.142, 100.143, 100.144, 100.145, 100.146, 100.147, 100.148 and 100.149 are added to read as follows:

§ 100.140 Incentives for self-testing and self-correction.

General rule. If a lender voluntarily conducts or authorizes a third party to conduct a self-test, the report or results of the self-test are privileged as provided in this subpart. A self-test required by any government authority is not privileged.

§ 100.141 Corrective action required.

The report or results of a self-test are privileged only if the lender has taken or is taking appropriate corrective action to address any possible violation identified by the self-test. The lender must take whatever actions are reasonable in light of the scope of the possible violations to fully remedy both their cause and effect.

§ 100.142 Definitions.

As used in this subpart:

Lender means a person who engages in a residential real estate-related lending transaction.

Residential real estate-related lending transaction means the making of a loan:

(1) For purchasing, constructing, improving, repairing, or maintaining a dwelling; or

(2) Secured by residential real estate.

Self-test means any program, practice or study that a lender voluntarily conducts or authorizes a third party to conduct that creates data or factual information that is not available, and cannot be derived, from actual loan or application files or other records related to credit transactions, to determine the extent or effectiveness of the lender's compliance with the Fair Housing Act. Self-testing includes, but is not limited to, the practice of using fictitious applicants for credit (''testers''). Self-testing does not include the collection of data required by law or by any government authority, or a lender's review or evaluation of actual loan or application files or other records related to credit transactions.

§ 100.143 Types of information.

(a) The privilege applies to the report or the results of a self-test, including any data generated by the self-test and any analysis of such data and any workpapers and draft documents.

(b) The privilege does not cover information about whether a lender has conducted a self-test, or information concerning the scope of or the methodology used in conducting the self-test.

§ 100.144 Appropriate corrective action.

(a) Whether a lender has taken or is taking appropriate corrective action will be determined on a case-by-case basis. Corrective action may include both prospective and retroactive relief. To determine the appropriate corrective action, the lender must:

(1) Identify the policies or practices that are the likely cause of the possible violation, such as inadequate or improper lending policies, failure to implement established policies, employee conduct, or other causes; and

(2) Assess the extent and scope of any possible violation, by determining which areas of its operations are likely to be affected by those policies and practices. This would include identifying the stages of the loan application process, types of loans, or the particular branch where possible discrimination has occurred.

(b) Depending on the specific facts involved, appropriate corrective action may include, but is not limited to, one or more of the following:

(1) Identifying customers whose applications may have been inappropriately processed; offering to extend credit if they were improperly denied; compensating them for any damages, both out-of-pocket and compensatory; and notifying them of their legal rights;

(2) Correcting any institutional policies or procedures that may have contributed to the discrimination;

(3) Identifying, and then training and/or disciplining, the employees involved;

(4) Considering the need for community outreach programs and/or changes in marketing strategy or loan products to better serve minority segments of the lender's market; and

(5) Improving audit and oversight systems to ensure there is no recurrence of the discrimination.

(c) Not every corrective measure listed in paragraph (b) of this section, above, need be taken each time a possible violation is discovered. Rather, the determination of ''appropriate corrective action'' shall be based upon the facts of each situation.

§ 100.145 Scope of privilege.

The report or results of a privileged self-test may not be obtained or used by an aggrieved person, complainant, department or agency in any:

(a) Proceeding or civil action in which a violation of the Fair Housing Act or this regulation is alleged; or

(b) Examination or investigation relating to compliance with the Fair Housing Act or this part.

§ 100.146 Loss of privilege.

The report or results of a self-test are not privileged under § 100.145 if the lender or any person with lawful access to the self-test:

(a) Voluntarily discloses all or any part of the report or results of the self-test or any privileged information to any aggrieved person, complainant, department, agency, or to the public.

(b) Refers to or describes the report or results or any privileged information as a defense to charges that the lender has violated the Fair Housing Act or this part.

(c) In the case of the lender, fails or is unable to produce required records or information pertaining to the self-test that are necessary to determine whether the privilege applies.

§ 100.147 Limited use of privileged information.

Notwithstanding the privilege under § 100.145, the report or results of a privileged self-test may be obtained and used by an aggrieved person, applicant, department or agency solely for the purpose of determining a penalty or remedy after a violation of the Fair Housing Act or this part has been adjudicated or admitted. Disclosures made for this limited purpose may be used only for the particular proceeding in which the adjudication or admission has been made. Information disclosed under this section remains privileged.

§ 100.148 Adjudication.

An aggrieved person, complainant, department or agency that challenges a privilege asserted under § 100.145 may seek a determination of the existence and application of that privilege in:

(a) A court of competent jurisdiction; or

(b) An administrative law proceeding with appropriate jurisdiction.

§ 100.149 Effective date.

The privilege applies to self-tests conducted both before and after the effective date of this regulation, except that a lender's self-test that was conducted before that date is not privileged:

(a) If there was a court action or administrative proceeding, including a proceeding involving a complaint alleging a violation of the Fair Housing Act filed with HUD or a substantially equivalent agency; or

(b) If any part of the report or results were disclosed before that date to any aggrieved person, complainant, department or agency, or to the public.

Dated: January 10, 1997.

Susan M. Forward,

Deputy Assistant Secretary for Enforcement and Investigations, Fair Housing and Equal Opportunity.

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