

## LEGAL ENVIRONMENT OF CREDIT – NACM LEARNING CENTER

Wanda Borges, Esq.  
Borges & Associates, LLC  
575 Underhill Blvd.  
Syosset, NY 11791  
516-677-8200 x 225  
[borgeslawfirm@aol.com](mailto:borgeslawfirm@aol.com)

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## ANTITRUST STATUTES

- The Sherman Antitrust Act of 1890
  - Prohibits contracts, combinations and conspiracies in restraint of trade in interstate commerce or with foreign nations.
  - Felony to conspire to *restrain trade*; or to *monopolize* (or attempt to monopolize).

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## ANTITRUST STATUTES (cont.)

- The Clayton Act of 1914
  - Passed to “correct” defects in Sherman Act.
  - Unlawful to enter into any of several specified types of prohibited transactions whose purpose or effect would be to restrain trade or injure a competitor.

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## ANTITRUST STATUTES (cont.)

- The Robinson-Patman Act of 1936
  - Partially an amendment to The Clayton Act.
  - Unlawful to “discriminate in price between different purchasers of commodities of like grade and quality”...
  - ...or knowingly to induce or receive a prohibited discrimination in price.
  - Liability could be *civil* or *criminal*.

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## ANTITRUST STATUTES (cont.)

- The Federal Trade Commission Act of 1914
  - Broadest of the antitrust statues; includes:
    - mergers & acquisitions
    - unfair trade practices
    - unfair arrangements btw suppliers & dealers
    - deceptive sales approaches
    - discrimination in price, services or facilities
    - false advertising, and
    - any other practice to deceive the public.

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## ANTITRUST STATUTES (cont.)

- The Antitrust Procedure & Penalties Act of 1976
  - Gives Fed, govt. new disclosure powers.
  - Permits a State attorney general to sue for damages on behalf of a state's citizens.
  - Requires companies of a certain size to file pre-merger notices.

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## ANTITRUST STATUTES (cont.)

- State Antitrust Statutes
- Almost every State has independent laws prohibiting monopolies, contracts, conspiracies and combinations in restraint of trade.

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## RESTRAINT OF TRADE (Unfair Competition, Price Fixing, Group Boycott)

- “Restraint of trade” = unreasonable
  - *per se* unreasonable (did the incident occur?); or
  - in violation of the “rule of reason” (judged by actual or potential effect on competitive marketplace).

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## RESTRAINT OF TRADE (CONT.)

- “Combination / Conspiracy”--4 elements:
  1. Knowledge
  2. Common purpose
  3. *Actual* restraint, not merely *facilitating*
  4. Intent to restrain trade
- “Conspiracy” = unity of purpose, common design, meeting of minds re: unlawful purpose

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## PRICE FIXING ISSUES FOR CREDIT GRANTORS

- Discussion *beyond* a “mere announcement”
- Agreement to *maintain prices*, with an enforcement mechanism (mfr./distrs.)
- Agreement to fix or set *payment terms*

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## CREDIT TERMS = PRICE

- **Catalano Inc. v Target Sales (Supreme Court 1980)**

“Extending interest-free credit for a period of time is equivalent to giving a discount equal to the value of the use of the purchase price for that period of time. Thus, credit terms must be characterized as an inseparable part of the price”

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## GROUP BOYCOTTING

- Concept of *sufficient market power*
- Hallmarks of illegal group boycott:
  1. Denial of access to a competitively useful commodity or service
  2. *Collective* refusal to deal
- Group boycotting can exist even through action of only one party

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## INVOLUNTARY PETITION IN BANKRUPTCY

- CAN BE DEEMED A GROUP BOYCOTT
- MUST NOT BE DISCUSSED BEFOREHAND

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## INVOLUNTARY PETITION IN BANKRUPTCY – PROPER STEPS

- MAKE INDEPENDENT DECISION
- GET COMPANY AUTHORIZATION
- RETAIN ATTORNEY
- SEEK OTHER CREDITOR(S)

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## PRICE DISCRIMINATION

- A single party can violate.
- Robinson-Patman -- *illegal to discriminate in prices between different purchasers of like goods, incl. credit and shipping terms*
- C.O.D. vs. Open credit can be deemed discriminatory

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## PRICE DISCRIMINATION

- Different price to different purchasers
- Differences in terms and conditions of sale
- Preferential credit terms

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## PREFERENTIAL CREDIT or CREDIT DENIAL PERMITTED in SPECIFIC INSTANCES

- Legitimate business reasons
- History of late payments
- Financial difficulty
- Superior credit records

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## MEETING COMPETITION

- Discriminatory price allowed when offered "in good faith" to meet an equally low price of a competitor
- Verify existence of competitor's offer
- Do not exceed competitors in size, duration or scope
- Refuse to meet the competitor's offer if illegal

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## GOOD FAITH STANDARD

- Reasonable belief the situation is of competitive necessity
- Belief that granting a lower price would meet the lower price of a competitor
- Substantial efforts must be made to verify actual price

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## DOCUMENTATION SUGGESTED

- Date of competitor's offer
- Name of competitor making offer
- Name of customer
- Terms and conditions of offer
- Source of the Information & why you believe it

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## LEGITIMATE BUSINESS REASON

- Cost Justification
- Market Conditions
- Superior Credit History or Records

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## PROMOTIONAL ALLOWANCES

- Proportionally equal terms
- Dollar volume or quantity purchased during specific period of time
- Equal rate per unit or amount purchased
- Specified part or percentage of local advertising

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## FAIR CREDIT REPORTING ACT

- FAIR CREDIT REPORTING ACT (FCRA) governs:
  - Obtaining and using a
  - Consumer Credit Report

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## FAIR CREDIT REPORTING ACT DEFINITIONS

- “Consumer” is “any individual”
- “Consumer Report” is “any written, oral, or other communication of any information by a consumer reporting agency bearing on a consumer’s credit worthiness...serving as a factor in establishing the consumer’s eligibility for –
  - (A) credit or insurance to be used primarily for personal, family, or household purposes;
  - (B) employment purposes; or
  - (C) any other purpose authorized under section 1681b of this title

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**FAIR CREDIT REPORTING ACT  
DEFINITIONS (cont'd)**

- “Investigative Consumer Report” is a consumer report or portion thereof in which information on a consumer’s character, general reputation, personal characteristics, or mode of living is obtained through personal interviews with neighbors, friends, or associates of the consumer reported on or with others with whom he is acquainted or whom may have knowledge concerning any such items of information.

**FAIR CREDIT REPORTING ACT  
PERMISSIVE USE OF CONSUMER  
REPORT**

- In response to the order of a court having jurisdiction to issue such an order, or a subpoena issued in connection with proceedings before a Federal grand jury
- In accordance with the *written* instructions or permission of the consumer to whom it relates
- In connection with a legitimate business need for the information

**FAIR CREDIT REPORTING ACT  
NON-PERMISSIBLE PURPOSE**

- The Federal Trade Commission has stated that the extension of trade credit was NOT a legitimate business need and insisted that written authorization be obtained prior to a trade credit grantor obtaining or utilizing a consumer credit report.

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**FAIR CREDIT REPORTING ACT  
PERMISSIBLE PURPOSE**

- A business transaction in which an individual has accepted personal liability for business debt, such as in the case of a sole proprietor, partner, or guarantor, DOES provide a permissible purpose under Section 604 of the FCRA to obtain and use a consumer credit report

**INDIVIDUAL CREDIT REPORT  
AUTHORIZATION**

- Permissible business purpose though it may be, It is recommended that you include authorization in your credit application

*The undersigned is either a sole proprietor, a partner in a partnership, an individual who may be executing a personal guarantee in connection with the extension of credit to Applicant, or one of the principal stockholders of a corporation. I give permission to \_\_\_\_\_ to obtain and utilize an individual credit report on me personally to determine my creditworthiness.*

**EQUAL CREDIT OPPORTUNITY ACT**

- The Equal Credit Opportunity Act (ECOA) is a federal law that makes it unlawful for any creditor to discriminate with respect to the extension of credit against an applicant on the basis of sex, race, color, creed, national origin, age or marital status.

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## EQUAL CREDIT OPPORTUNITY ACT DEFINITIONS

- Adverse Action means:
  - (i) refusal to grant credit in substantially the amount or on substantially the terms requested in an application
  - (ii) a termination of an account or an unfavorable change in the terms of an account that does not affect all or substantially all of a class of the creditor's accounts
  - (iii) a refusal to increase the amount of credit available to an applicant who has asked for increase

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## EQUAL CREDIT OPPORTUNITY ACT DEFINITIONS

- Adverse Action DOES NOT INCLUDE:
  - (i) a change in terms of an account expressly agreed to by an applicant
  - (ii) action or forbearance relating to an account taken in connection with inactivity, default, or *current* delinquency as to that account.
  - (iii) a refusal because creditor does not offer the type of credit or credit plan requested

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## EQUAL CREDIT OPPORTUNITY ACT DEFINITIONS

- Applicant means any person who requests or who has received an extension of credit from a creditor, and includes any person who is or may become contractually liable regarding an extension of credit.
  - The definition of Applicant includes guarantors, sureties, endorsers and similar parties

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**EQUAL CREDIT OPPORTUNITY ACT  
DEFINITIONS**

- **Business Credit** refers to extensions of credit primarily for business or commercial (including agricultural) purposes, but excludes extensions of credit in certain types of transactions, such as public utilities, securities and government credit.

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**EQUAL CREDIT OPPORTUNITY ACT  
DEFINITIONS**

- **Trade Credit** is NOT defined in the ECOA
  - Staff Commentary states that “the term ‘trade credit’ generally is limited to a financing arrangement that involves a buyer and a seller – such as a supplier who finances the sale of equipment, supplies, or inventory; it does not apply to an extension of credit by a bank or other financial institution for the financing of such terms.”

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**EQUAL CREDIT OPPORTUNITY ACT  
DEFINITIONS**

- **Creditor** means a person who, in the ordinary course of business, regularly participates in a credit decision, including setting the terms of credit.

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**EQUAL CREDIT OPPORTUNITY ACT**

**● SIGNATURE OF SPOUSE PROHIBITED**

- A creditor shall NOT require the signature of an applicant's spouse or other person, other than a joint applicant, on any credit instrument if the applicant qualifies under the creditors' standards of creditworthiness for the amount and terms of the credit requested.

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**EQUAL CREDIT OPPORTUNITY ACT**

- A creditor shall not deem the submission of a joint financial statement or other evidence of jointly held assets as an application for joint credit

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**EQUAL CREDIT OPPORTUNITY ACT**

**● PROPERTY JOINTLY OWNED BY APPLICANT AND NON-APPLICANT**

- If a creditor relies upon property that the applicant owns jointly with another person, then the creditor may require the signature of the other person on instruments necessary to reach that property in the event of death or default

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**EQUAL CREDIT OPPORTUNITY ACT**

● **COMMUNITY PROPERTY STATE**

- A creditor may require the signature of the spouse of any instrument necessary, or reasonably believed to be necessary under applicable state law to make the community property available to satisfy the debt in the event of default under certain circumstances

**EQUAL CREDIT OPPORTUNITY ACT**

● **COMMUNITY PROPERTY STATE (cont'd)**

- If applicable state law denies the applicant power to manage or control sufficient community property to qualify for the amount of credit requested; and
- The Applicant does not have sufficient separate property to qualify for the amount of credit requested without regard to community property

**EQUAL CREDIT OPPORTUNITY ACT  
REQUISITE NOTICE**

*The federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age; (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is Federal Trade Commission, Equal Credit Opportunity, Washington, D.C. 20580.*

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**EQUAL CREDIT OPPORTUNITY ACT  
NOTIFICATION REQUIREMENTS**

- Business Credit Applicants
  - \$1 million or less – gross revenues in preceding fiscal year
  - gross revenues in excess of \$1 million **OR AN EXTENSION OF TRADE CREDIT**

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**EQUAL CREDIT OPPORTUNITY ACT  
NOTIFICATION TIMING & MANNER**

- Business Credit Applicants
  - Within 30 days after
    - receiving a completed application
    - taking adverse action on existing account
    - receiving an incomplete application

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**EQUAL CREDIT OPPORTUNITY ACT  
NOTIFICATION TIMING & MANNER**

- If counteroffer has been made by a creditor and the applicant does not expressly accept or use the credit offered, then notification of the creditor's action must be within 90 days of notifying the applicant of a counteroffer

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**EQUAL CREDIT OPPORTUNITY ACT  
CONTENTS OF NOTIFICATION**

- A statement of the action taken orally or in writing
- Inform applicant of its right to a statement of reasons AND provide the requisite ECOA notice

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**EQUAL CREDIT OPPORTUNITY ACT  
NOTIFICATION TIMING & MANNER**

- Trade Credit Applicants
  - Notify applicant, within a reasonable time
    - orally or in writing; and
  - If and only if applicant makes a written request for reasons behind credit decision within 60 days of being notified of adverse action,
    - THEN creditor must provide a written statement of reasons
    - AND requisite ECOA notice

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**EQUAL CREDIT OPPORTUNITY ACT  
SPECIFICITY OF REASONS**

- Suggestions
  - Insufficient number of credit references provided
  - Unacceptable type of credit references provided
  - Unable to verify credit references
  - Poor credit performance with us
  - Delinquent past or present credit obligations with others
  - Garnishment, attachment, foreclosure, collection action, or judgment
  - Bankruptcy
  - Value or type of collateral not sufficient
  - Lack of established earnings record
  - Slow or past due in trade or loan payments
  - Other, specify \_\_\_\_\_

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## EQUAL CREDIT OPPORTUNITY ACT RETENTION OF RECORDS

- **Special Rule for Certain Business Credit Applications**

*With regard to a business that had gross revenues in excess of \$1 million in its preceding fiscal year, or an extension of trade credit, credit incident to a factoring agreement, or other similar types of business credit, the creditor shall retain records for at least 60 days after notifying the applicant of the action taken. If within that time period the applicant requests in writing the reasons for adverse action or that records be retained, the creditor shall retain records for 12 months.*

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## EQUAL CREDIT OPPORTUNITY ACT RECORDS TO MAINTAIN

- Any application together with written or recorded information obtained and used to evaluate application unless information is returned to applicant
- Copy of written notification of action taken and statement of specific reasons for adverse action
- Written statement submitted by applicant alleging a violation of ECOA or Regulation B

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## EQUAL CREDIT OPPORTUNITY ACT

- **Recommended Notification on Credit Application**

*If your application for business credit is denied, you have the right to a written statement of the specific reasons for the denial. To obtain the statement, please contact (name, address and telephone number of the person or office from which the statement of reasons can be obtained) within 60 days from the date you are notified of our decision. We will send you a written statement of reasons for the denial within 30 days of receiving your request for the statement.*

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## FAIR AND ACCURATE CREDIT TRANSACTIONS ACT OF 2003

- **Disposal Rule** - Requires proper disposal of information in consumer reports and records to protect against "unauthorized access to or use of the information"
- **Organizations Covered** – include credit grantors, debt collectors, attorneys, lenders, consumer reporting companies
- **Requirement** – BURN, PULVERIZE OR SHRED

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## ESCHEATMENT

- **Definition of "Escheat"**
  - **Seizure by the state of property which has no owner.**

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## ESCHEATMENT

- **Dormancy Period:**
  - applicable period of time which must lapse before property will escheat to the state
  - Each state's unclaimed property laws specifically define the dormancy period for each type of property
  - Generally between three and five years

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## ESCHEATMENT

- Unclaimed Property
  - Tangible
  - Intangible
  - Owed to a person or Entity
  - Held by another
  - Owner cannot be located

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## ESCHEATMENT

- Jurisdiction
  - State of the owner's last known address
  - Holder's state is no last known address is shown

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## ESCHEATMENT

- Statute of Limitations
  - Definition: a time period, within which a party must bring suit for its claims
  - Most states have no limit
  - Even where Statute of Limitations exists – generally longer than a tax statute
  - Failure to Report/Fraudulent Report eliminates any Statute of Limitations

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## ESCHEATMENT

- **Due Diligence Required**
  - One last Effort to reunite propert with the owner prior to reporting it to the state

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## ESCHEATMENT

- Compliance
  - Due Diligence
- Reporting

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## SARBANES-OXLEY ACT OF 2002

- FRAUD PREVENTION
- PROTECT INVESTORS
- ENSURE ACCURACY AND RELIABILITY IN CORPORATE DISCLOSURES

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## SARBANES-OXLEY ACT OF 2002

### ■ Public Company Accounting Oversight Board

- register public accounting firms that prepare audit reports
- establish auditing, quality control, ethics, independence and other standards relating to the preparation of audit reports
- conduct inspections, investigations and disciplinary proceedings of audit firms where necessary

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## SARBANES-OXLEY ACT OF 2002

### ■ PUBLIC ACCOUNTING FIRM MUST

- prepare and maintain all work papers, etc for not less than 7 years.
- provide a concurring or second partner review of each audit report
- describe in each audit report the scope of the auditor's testing of the internal control structure and procedures of the issuer, as required by section 404(b)

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## SARBANES-OXLEY ACT OF 2002

### ■ Quality Control Standards of Public Accounting Firms

- monitoring of professional ethics and independence from issues
- consultation within such firm on accounting and auditing questions
- supervision of audit work

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## SARBANES-OXLEY ACT OF 2002

- **Quality Control Standards of Public Accounting Firms**
  - hiring, professional development and advance of personnel
  - acceptance and continuation of engagements
  - internal inspection

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## SARBANES-OXLEY ACT OF 2002

- **Auditor Independence – some samples**
  - No bookkeeping or related services
  - No financial information systems design
  - No actuarial services
  - No management or human resources functions

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## SARBANES-OXLEY ACT OF 2002

- **Corporate Responsibility**
  - principal executive officer or officers and the principal financial officer or officers responsible for proper audit procedures and financial reporting

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## SARBANES-OXLEY ACT OF 2002

- **Corporate Responsibility**
  - **Certification by responsible officer**
    - Report has been reviewed
    - Report does not contain any untrue statement of a material fact
    - Report does not omit any material fact
      - Report is not misleading

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## SARBANES-OXLEY ACT OF 2002

- **Corporate Responsibility**
  - **Certification by responsible officer**
    - Report fairly presents financial conditions and results of operations
    - Officer is responsible for establishing and maintaining internal controls

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## SARBANES-OXLEY ACT OF 2002

- **Responsible Officer - Internal Controls**
  - ensure material information of issuer and its consolidated subsidiaries is made known to such officers by others within those entities
  - evaluated the effectiveness of the issuer's internal controls as of a date within 90 days prior to the report
  - presented conclusions about the effectiveness of internal controls evaluated as of that date

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## SAS 70 REPORTS

### ■ Purpose

- To gain an understanding of the internal controls in operation at a service organization that may be used by a client's auditors to plan and execute

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## SAS 70 REPORTS

### ■ SAS 70 Audit

- Must be performed by an independent certified public accountant or firm.

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## SAS 70 REPORTS

### ■ Benefits

- Satisfy customer Sarbanes Oxley 404 requirements
- Satisfy customer audit requirements
- Compliance with regulatory requirements
- Satisfy contract requirements
- Documentation and testing internal controls
- Streamline business processes and controls

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