American Bankers Association

Building Success. Together.

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By electronic delivery to:

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Re: Application of the Disparate Impact following Supreme Court Decision in *Texas Department of Housing and Community Affairs v. Inclusive Communities Project, Inc.*

Ladies and Gentlemen:

The American Bankers Association (ABA)[1] and our members are strong advocates for fair lending and proper enforcement of the Fair Housing Act. The banking industry supports equal housing opportunity and strives to make housing credit available to all qualified borrowers and to treat all similarly-situated applicants alike.

[1] The American Bankers Association is the voice of the nation's $15 trillion banking industry, which is composed of small, regional, and large banks that together employ more than 2 million people, safeguard $11 trillion in deposits, and extend more than $8 trillion in loans.

On June 25, 2015, the United States Supreme Court (the Court) held in *Texas Department of Housing and Community Affairs v. Inclusive Communities Project, Inc.* (*Inclusive Communities*) that disparate impact claims are recognized under the Fair Housing Act (FHA).[2] In upholding the use of disparate impact theory, the Court provided an important framework for the application of the doctrine in order to avoid potential inappropriate or abusive application. ABA requests that this framework be acknowledged expressly and adopted by the agencies charged with enforcing the FHA, including the banking agencies, the Department of Justice, and the Department of Housing and Urban Development (collectively, the Agencies). In particular, we ask the Agencies to confirm in interagency guidance, updated exam procedures, and where appropriate amended regulations that the burden-shifting framework outlined by the Supreme Court will govern the Agencies' consideration of disparate impact claims in both the supervisory and enforcement context.

Inclusive Communities addresses a supervisory standard that has its roots in the April 1994 Interagency Policy Statement on Discrimination in Lending, in which the Agencies expressed their view that discrimination in lending under the Equal Credit Opportunity Act (ECOA) and the Fair Housing Act can be identified using disparate impact analysis.[3] As the Agencies are aware, however, the statutory foundation for disparate impact liability *and* the appropriate standard for assessing a disparate impact claim under the FHA have been much debated.

To the extent that *Inclusive Communities* settled this debate—and more important, established a rigorous analytical framework that should apply— it is a positive development. The opinion of the Court in *Inclusive Communities* discusses at length the qualifications for recognition of disparate impact liability, emphasizing that a disparate impact challenge should apply only to "artificial, arbitrary, and unnecessary barriers." The Court established the following standards for analysis of a disparate impact claim:

1. A statistical imbalance is not enough to establish a *prima facie* case;[4]
2. A plaintiff must satisfy a "robust causality requirement" between a specific policy or practice and the statistical disparity to "protect defendants from being held liable for racial disparities they did not create;"[5]
3. A valid business or policy purpose rebuts a *prima facie* case; and
4. Before rejecting a business justification for a challenged practice, the court must find that the plaintiff has demonstrated that there is an "available alternative . . . practice that has less disparate impact and serves the [entity's] legitimate needs."[6]

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[2] *Texas Dep't of Housing & Community Affairs v. Inclusive Communities Project, Inc.*, 576 U.S. ___ (2015), *available at* http://www.supremecourt.gov/opinions/14pdf/13-1371_m64o.pdf.
[3] 59 Fed. Reg. 73 (April 15, 1994).
[4] The Court also admonished judges to "examine with care whether a plaintiff has made out a *prima facie* case of disparate impact and prompt resolution of these cases is important." (Slip Op. at 20).
[5] *Id.*

Fundamental to the Court's express framework for the application of disparate impact are limitations that the Court deemed "necessary to protect potential defendants against abusive disparate impact claims."[7] The banking industry agrees that this is critical to the legal rationale.

In future judicial challenges, the Court's decision will ensure that establishing a disparate impact claim must meet an appropriately high standard. As expected, in one of the first cases to apply *Inclusive Communities,* the U.S. District Court for the Central District of California rejected a disparate impact claim because the plaintiff failed to point to a specific defendant policy that caused the disparate impact and failed to show "robust causality" between any of defendant's policies and the alleged statistical disparity.[8] We can anticipate that other cases, initiated without sufficient proof of disparate impact or otherwise not complying with the Court's framework, also will be dismissed.

The Supreme Court is clear that the limitations in its decision are critical to preventing abusive claims. Prevailing on a summary judgment motion, however, can be a pyrrhic victory. Much expense and disruption to the provision of financial services can occur in the process of reaching a summary judgment. By that time, a defendant may have undergone significant business disruption, perhaps suspended operations and services, been compelled to retain counsel, and suffered immediate reputational damage, which is slowly - if ever - reversed by the subsequent dismissal of the case. Indeed, the Supreme Court recognized that the threat of an unfounded disparate impact challenge will prompt risk-adverse lenders to "displace valid governmental and private priorities rather than solely removing artificial, arbitrary, and unnecessary barriers" as the *Inclusive Communities* majority fears.[9] The specter of supervisory assertion of disparate impact claims without appropriate controls can exalt leverage over law and "tend to perpetuate race-based considerations rather than remove them,"[10]—undermining the statutory goal of expanding credit opportunity and availability.

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[6] The Court explained that the cases interpreting Title VII and the ADEA – *Griggs v. Duke Power Co.* and *Ricci v. DeStefano* – "provide essential background and instruction," including—

> These cases also teach that disparate-impact liability must be limited so employers and other regulated entities are able to make the practical business choices and profit-related decisions that sustain a vibrant and dynamic free-enterprise system. And before rejecting a business justification—or, in the case of a governmental entity, an analogous public interest—a court must determine that a plaintiff has shown that there is "an available alternative . . . practice that has less disparate impact and serves the [entity's] legitimate needs." (Slip op. at 10).

[7] Slip Op. at 21.

[8] *City of Los Angeles v. Wells Fargo & Co.*, No. 2:13-cv-09007-ODW (RZx) (C.D. Cal. July 17, 2015) *available at* http://www.aba.com/Compliance/Documents/City_of_LA_(Wells_Fargo)--Order_Granting_SJ_(2).pdf.

[9] *See Inclusive Communities,* Slip Op. at 22. *See also, Watson v. Fort Worth Bank & Trust,* 487 U.S. 977, 992-93 (1988); *Ricci v. DeStefano*, 129 S.Ct. 2658, 2675 (2009).

[10] *See Inclusive Communities,* Slip Op. at 21.

ABA and its members appreciate the Court's strong endorsement of the role of private discretion in lending decisions, witnessed by statements such as, "[e]ntrepreneurs must be given latitude to consider market factors,"[11] and "[c]ourts should avoid interpreting disparate impact liability to be so expansive as to inject racial considerations into every housing decision."[12] However, in order to have a prompt effect on promoting market activity consistent with the Supreme Court's decision, these statements need to be reinforced by agency supervisory positions and the exercise of prosecutorial discretion by HUD or DOJ. The Agencies can do this by pledging adherence to the "cautionary standards" expressed by the Court.

Accordingly, ABA formally requests that the Agencies confirm in interagency guidance, updated exam procedures, and where appropriate amended regulations that the Agencies' consideration of disparate impact claims in both the supervisory and enforcement context will be governed by standards consistent with the Court's framework:

1. The Agencies will give initial focus to enforcing fair lending requirements under a *disparate treatment* paradigm.

2. After exhausting a disparate treatment inquiry, the Agencies will pursue disparate impact or effects discrimination claims only where there is demonstrable evidence that the lender is applying an artificial, arbitrary, and unnecessary barrier in its credit granting process, applying the burden-shifting framework and associated cautionary standards established by *Inclusive Communities.*

In addition, ABA urges the Department of Housing and Urban Development to review and re-propose its rule so that it reflects and incorporates the framework set forth by the Court in *Inclusive Communities.*

In this way, the Agencies will place proper emphasis on the true objective of the fair lending laws: ensuring that lenders extend credit to prospective borrowers based on their qualifications, and similarly qualified individuals are treated alike. This obligation can be managed by compliance programs and can be embraced by all, because it assures equal opportunity and the extension of credit to all those who qualify regardless of their race, national origin, gender, age, or other prohibited characteristic. *Inclusive Communities* establishes that a *prima facie* case exists only when a creditor's policies result in artificial, arbitrary, and unnecessary barriers to otherwise qualified borrowers. Absent that showing, the Agencies should not expend enforcement resources that "may 'push cost-conscious defendants to settle even anemic cases'"[13] and put them in what the Court describes as a "double bind of liability" when they are following prudent lending criteria neutrally applied to all applicants.

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[11] *Id.* at 19.
[12] *Id.* at 21.
[13] *Inclusive Communities,* Alito Dissent at Slip Op. p. 32.

In a related vein, ABA urges the Agencies to address on an interagency basis standards for agency referrals to DOJ consistent with the Court's framework. We believe that there should be consensus and transparency regarding what constitutes a "pattern or practice" of discrimination based on a theory of disparate impact liability, consistent with the decision of the Court, that warrants a referral from one of the banking agencies or HUD to DOJ. Moreover, the standards should require facts establishing a *prima facie* case as a predicate to referral.

Finally, to recognize the Supreme Court's articulation of the need for care when using disparate impact theory, ABA strongly recommends that the Agencies incorporate in examination procedures the Court's admonishment that when courts do find liability under a disparate impact theory, their remedial orders must be consistent with the Constitution. "Remedial orders in disparate-impact cases should concentrate on the offending practice that arbitrarily operates invidiously to discriminate on the basis of race." The Court also noted, "Remedial orders that impose racial targets or quotas might raise more difficult constitutional questions." [14] Therefore, interagency exam procedures should clearly direct supervisory and enforcement staff to tailor carefully any remediation to correct only the offending practice through race-neutral means.

The Supreme Court's decision in *Inclusive Communities* clearly rests upon the premise that disparate impact cases will focus on the "heartland of disparate impact liability," that is they will target "artificial, arbitrary, and unnecessary barriers." ABA requests that the Agencies promptly promote this goal by developing and adhering to supervisory and enforcement standards that are consistent with the framework articulated by the Court.

The sooner that the Agencies do so through specific steps involving guidance, exam procedures, and appropriate regulation, the more positive the impact will be on the promotion of the availability of finance to credit-worthy borrowers.

Sincerely,

Frank Keating
President & CEO

[14] Slip op. at 22 (internal citations omitted).