Center for Responsible Lending
Self-Help Credit Union
Self-Help Federal Credit Union

Comment to the Department of Housing and Urban Development

Notice of Proposed Rulemaking

24 CFR 100

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I. Introduction

The Center for Responsible Lending, Self-Help Credit Union, and Self-Help Federal Credit Union[1] appreciate the opportunity to comment on the Department of Housing and Urban Development's proposed rule to recodify its previously promulgated rule titled, "Implementation of the Fair Housing Act's Discriminatory Effects Standard" (2013 Rule).

The 2013 Rule remains in effect due to a preliminary injunction in *Massachusetts Fair Housing Center* v. *HUD*, which stayed HUD's implementation and enforcement of HUD's 2020 rule titled "HUD's Implementation of the Fair Housing Act's Disparate Impact Standard." HUD reconsidered the 2020 Rule and concluded that the 2013 Rule better states Fair Housing Act jurisprudence and is more consistent with the Act's remedial purposes. CRL, Self-Help Credit Union, and Self-Help Federal Credit Union unequivocally agree with this assessment and strongly support HUD's proposed rule to reinstate the 2013 Rule. The 2013 Rule properly codified the disparate impact standard that has prevailed in the courts and has been used by regulators, including HUD, for decades.[2]

The 2020 Rule was opposite to HUD's mission, decades of legal precedent, and the Supreme Court's decision in *Texas Department of Housing and Community Affairs v. Inclusive Communities Project* (2015).[3] In particular, the 2020 Rule was inconsistent with the existing burden-shifting framework – a framework supported by over 40 years of case law – and placed all the burdens on the victims of housing discrimination. The 2020 Rule would have placed insurmountable barriers for a potential complainant to make it past the pleading stage when bringing a claim under disparate impact theory. HUD's 2020 Rule also introduced confusing and harmful defenses, such as the "outcome prediction" defense that would obfuscate discrimination in lender models and algorithmic systems.

The proposed rule appropriately returns the definition of "discriminatory effect" that was eliminated by the 2020 Rule, including by acknowledging "perpetuation of segregation" as a recognized type of discriminatory effect. The proposed rule also recodifies that actions that could predictably result in a disparate impact on a group of persons are prohibited by the Fair Housing Act.

It is critical that HUD proceed with reinstituting a meaningful disparate impact standard and vigorously enforce our nation's fair housing laws.

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[1] The Center for Responsible Lending (CRL) is a nonprofit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help Credit Union (SHCU) and Self-Help Federal Credit Union (SHFCU). SHCU is a North Carolina-chartered, federally-insured credit union with 90,000 members served out of 35 branches in North Carolina, South Carolina and Florida with $1.6 billion in assets. SHFCU is a federally-chartered and insured credit union with 90,000 members served out of 32 branches in California, Illinois, Washington, and Wisconsin with $1.7 billion in assets.

[2] Implementation of the Fair Housing Act's Discriminatory Effects Standard, 78 Fed. Reg. 11460 (Feb. 15, 2013) (codified at 24 C.F.R. § 100.500).

[3] *Texas Dept. of Housing and Community Affairs v. Inclusive Communities Project Inc.*, 135 S. Ct. 2507 (2015).

II. Background

Discrimination in our nation's lending and housing markets has a long history, driven by the federal government, state and local governments, private industry, and individual actors.[4] Today's racial wealth gap and lending disparities are in large part the result of decades of government policies and practices that enabled the redlining of communities of color for most of the 20th century. In the post-Depression era, federal policies that created housing opportunities for returning veterans and their families explicitly excluded people of color from the benefits of government-supported housing programs. Among these programs were public housing, the Home Owners Loan Corporation, and mortgage insurance through the Federal Housing Administration.[5] Not only did this redlining segregate residential neighborhoods across the United States, but it granted whites the ability to build wealth through homeownership while denying equal opportunities for families of color to build similar home equity over the same period. As a result, whites accrued an economic advantage in the form of home equity that has been passed on to future generations through intergenerational wealth transfers.

Homeownership is a critical component of family wealth, particularly for low-income families and people of color, and has been shown to explain much of the observed racial wealth gap. There continues to be a stark disparity in the homeownership rate between whites and people of color, with the white homeownership rate at 72% while the rate is 42% and 48% for Black and Hispanic borrowers respectively.[6] In large part because families of color were excluded from the opportunity to build wealth through federally supported investment in homeownership and were later devastated by the financial crisis, Black and Hispanic families have considerably less wealth than white families. In fact, Black families' median wealth is less than 15% that of white families, at $24,100 and $142,500, respectively.[7]

While discrimination and its ill effects continue to the present day, much of it has become covert and harder to pinpoint. Disparate impact theory is intended to root out discriminatory policies and practices that are difficult (and sometimes impossible) to prove via a finding of intentional discrimination. As the Supreme Court stated in *Inclusive Communities*, the theory "permits plaintiffs to counteract unconscious prejudices and disguised animus that escape easy classification as disparate treatment."[8] Disparate impact theory also allows companies to identify and prevent facially neutral, but unjustified, policies that disproportionately harm particular communities. Moreover, strong disparate impact standards incentivize housing providers, lenders, and other participants in the housing market to have systems in place to identify and implement the least discriminatory policies consistent with their business needs. This is a win-win for everyone. It encourages entities to innovate and improve decision-making, and it makes the housing market more inclusive.

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[4] Richard Rothstein, *The Color of Law: A Forgotten History of How Our Government Segregated America.* New York: Liveright Publishing Corporation (2017).

[5] *See, e.g.*, National Community Reinvestment Coalition, *HOLC "Redlining" Maps: The Persistent Structure of Segregation and Economic Inequality* (2018), https://ncrc.org/holc/.

[6] Alanna McCargo and Jung Hyun Choi, *Closing the Gaps: Building Black Wealth Through Homeownership*, Figure 3, Urban Institute (November 2020), https://www.urban.org/sites/default/files/publication/103267/closing-thegaps-building-black-wealth-through-homeownership_0.pdf.

[7] Neil Bhutta, Andrew C. Lang, Lisa J. Dettling, and Joanne W. Hsu, *Disparities in Wealth by Race and Ethnicity in the 2019 Survey of Consumer Finances*, Federal Reserve Board, FEDS Notes, Sept. 28, 2020, https://www.federalreserve.gov/econres/notes/feds-notes/disparities-in-wealth-by-race-and-ethnicity-in-the-2019-survey-of-consumer-finances-20200928.htm.

[8] 135 S. Ct. at 2522.

III. Disparate Impact Theory and HUD's 2013 Disparate Impact Rule Have Driven the Lending Industry to Root Out Discriminatory Practices While Identifying More Accurate Means of Assessing Creditworthiness

The Fair Housing Act's disparate impact doctrine has played a critical role in helping make fair housing available to all, while at the same time making the lending industry better at evaluating creditworthiness. A ban on unjustified disparate impact has encouraged the lending industry to systematically scrutinize its procedures and requirements to ensure that lenders more precisely measure creditworthiness and lending practices do not have unnecessary discriminatory impact.

As the Supreme Court noted, in upholding disparate impact "residents and policymakers have come to rely on the availability of disparate-impact claims."[9] Disparate impact, far from imposing excessive burdens and encouraging abusive litigation, has introduced needed innovation in mortgage and insurance markets, eliminating barriers to homeownership and encouraging more rigorous and accurate assessment of risk. Indeed, an analysis of "less discriminatory alternatives" encourages innovation. It does not require lenders to ignore relevant and material underwriting criteria, but rather to avoid factors that disadvantage protected classes unnecessarily.

Under the existing disparate impact rule and before it under decades of case law, industry has had strong incentive to root out discriminatory practices while identifying more fair and accurate means of assessing creditworthiness, pricing mortgage products, and underwriting homeowners' insurance. Industry for decades has been adopting more reliable and accurate credit underwriting standards because the Fair Housing Act requires industry not turn a blind eye to the discriminatory impact of criteria. For example, following explosive reports based on HMDA data that showed discriminatory underwriting and disparities that could not be explained by economic factors,[10] the GSEs introduced automated underwriting systems that permitted any lender to evaluate prospective loans using objective criteria such as loan-to-value and debt-to-income ratios that were, at least in theory, based on sound statistical principles. Their use quickly proved to make lending decisions both more accurate and fair.[11]

Since that time, industry has further developed lending standards that more accurately and reliably assess creditworthiness. Contrary to the claims that disparate impact "litigation risks" might reduce the availability of credit, the result of these developments is that these credit markets, while far from completely fair, are now more open than ever before to those traditionally shut out of access to credit.

Today, lending institutions often seek to identify the least discriminatory underwriting criteria that also are reliable indicators of risk. As more information is available on prospective borrowers, lenders assess the utility of new variables, and can then identify the handful of factors that, collectively, are sufficiently predictive of risk. The lender then tests that collection of variables for discriminatory impact. Because different factors often correlate, a lender can substitute a different criterion for one that through testing

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[9] 135 S. Ct. at 2525.

[10] *See* Margery Austin Turner & Felicity Skidmore, *Introduction, Summary, and Recommendations in Mortgage Lending Discrimination: A View Of Existing Evidence, Urban Institute*, at 1, 10 (1999) (describing "explosive effect" of Boston Fed study on industry and the "extensive soul searching" that followed), http://webarchive.urban.org/publications/309090.html.

[11] *See, e.g.*, Susan Wharton Gates, et al., *Automated Underwriting in Mortgage Lending: Good News For The Underserved?*, 13 Hous. Policy Debate 369, 383-85 (2002).

reveals a discriminatory impact and repeat the testing process. Through this process, lenders can isolate and eliminate those variables that cause unnecessary discriminatory impact, without compromising identification of credit risk.

The 2020 Rule would have short circuited this process, first by requiring that plaintiffs allege not only that a given policy results in disparate impact, but that it is "arbitrary, artificial, and unnecessary."[12] This requires a plaintiff to understand and allege the motives and reasoning of a defendant at the time of filing a complaint. Such a requirement goes far beyond avoiding risks that prevent industry "from achieving legitimate objectives"[13] to creating a virtually impossible pleading requirement that the plaintiff identify an illegitimate objective based on speculation. Moreover, this requirement ignores the well-established burden-shifting under disparate impact doctrine that allows for the defendant, who presumably is best positioned to do so, to allege a legitimate purpose for the policy.

This disparate impact process – developed as a direct result of the challenge the disparate impact doctrine posed to the lending industry – is now standard practice among major lenders and balances the very real problem of proving discrimination for private/individual borrowers with the compliance capacity of lenders. It has resulted in a fairer loan process for all borrowers and a more profitable one for banks. Some of those who historically have been denied loans at a disproportionate rate now have greater access. And not only have lenders fully retained their ability to identify and respond to risk, they have also expanded their customer base. This offers enormous potential to increase profit. The industry is better off for the rationalization of its processes required by disparate impact doctrine.

In fact, during the summer of 2020, several large banks and trade organizations sent letters to HUD, endorsing the use of disparate impact theory under the Fair Housing Act, and urging HUD to delay finalizing the 2020 Rule.[14]

IV. HUD's 2013 Rule Was Consistent with Well-Established Legal Precedent, Including the Supreme Court's Decision in *Inclusive Communities*, and Did Not Require Revision

The Supreme Court's holding in *Inclusive Communities* is entirely consistent with HUD's 2013 disparate impact rule and rewriting the rule in 2020 was wholly unnecessary. The Supreme Court *affirmed* the 5th Circuit's decision, which expressly adopted the 2013 Rule's standard ordering remand to the District

[12] HUD's Implementation of the Fair Housing Act's Disparate Impact Standard, 84 Fed. Reg. 42854, 42862 (August 19, 2019).

[13] 135 S. Ct. at 2523-24.

[14] *See, e.g.*, Letter to HUD from Bank of America (June 29, 2020), https://nationalfairhousing.org/wp-content/uploads/2020/07/Letter-from-BofA.pdf ("Given the recent protests and events, and the recognition of where we are as a country, we would respectfully offer that the time is not right to issue a new rule on disparate impact. We have all heard the legitimate concerns that have been raised that the proposed rule could make it more difficult to ensure that the Fair Housing Act's protections and avenues of redress against unlawful discrimination are available to all Americans. The proposed rule could have significant impact and come in the context of what we as a country are currently experiencing. We believe more deliberation is required."); Letter to HUD from Wells Fargo (July 14, 2020), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/disparate-impact-letter-hud-14jul2020.pdf ("Wells Fargo commits itself to working with HUD, other lenders, and the civil rights community to participate in this discussion and ensure that the disparate impact framework remains a vital tool towards fighting unjust discrimination.")

Court to apply it.[15] HUD's 2013 rule simply reaffirmed HUD's longstanding interpretation that the Fair Housing Act authorizes disparate impact claims. The rule did not change decades-old substantive law but rather "formalizes a clear, consistent, nationwide standard for litigating discriminatory effects cases under the Fair Housing Act."[16] In short, the rule did not go beyond the contours of existing disparate impact law. As HUD itself stated in a 2017 motion in *Property Casualty Insurers Association of America v. Carson*, "the Supreme Court's holding in *Inclusive Communities* is entirely consistent with the Rule's reaffirmation of HUD's longstanding interpretation that the FHA authorizes disparate impact claims."[17] HUD further stated: "[N]othing in *Inclusive Communities* casts any doubt on the validity of the Rule."[18] Additionally, HUD's disparate impact rule was implicitly adopted in the *Inclusive Communities* decision; the Supreme Court cited HUD's rule multiple times to support its analysis.[19]

Moreover, the *Inclusive Communities* decision did not change existing disparate impact law. In fact, the Supreme Court granted certiorari *solely* to address whether disparate impact claims are cognizable under the Fair Housing Act.[20] The Court explicitly declined to grant certiorari on the question of what standards and burdens of proof should apply, even though petitioner sought review of those questions.[21] Thus, while HUD's 2020 Rule destroyed the longstanding burden shifting framework used to analyze disparate impact cases, the *Inclusive Communities* decision did not require any change to the burden-shifting test. The case simply reaffirmed that disparate impact claims are cognizable under the Fair Housing Act. The Court further acknowledged that disparate impact theory already properly limits liability: "[D]isparate-impact liability has always been properly limited in key respects."[22] For example, a statistical disparity has never been enough to establish disparate impact liability. Likewise, HUD's 2013 Rule does not provide for the finding of disparate impact liability based solely on statistical evidence.

For additional background on why the 2020 Rule was problematic and inconsistent with the Fair Housing Act, please see our October 2019 comment.[23]

V. Reinstating the 2013 Rule is Consistent with President Biden's Memorandum to HUD

The federal government must address its role in fostering racial discrimination in the mortgage market and the resulting racial wealth gap. A straightforward and legally required method is to vigorously enforce existing fair lending laws and work to eradicate inequitable and unjustified policies. As the Court in *Inclusive Communities* stated: "The FHA must play an important part in avoiding the Kerner Commission's grim prophecy that '[o]ur Nation is moving toward two societies, one black, one white – separate and unequal.' The Court acknowledges the Fair Housing Act's continuing role in moving the

[15] *Inclusive Communities Project, Inc. v. Texas Dep't of Hous. & Cmty. Affairs*, 747 F.3d 275, 282 (5th Cir. 2014), aff'd and remanded, 576 U.S. 519 (2015) ("These standards are in accordance with disparate impact principles and precedent.")
[16] Implementation of the Fair Housing Act's Discriminatory Effects Standard, 78 Fed. Reg. 11,460 (Feb. 15, 2013).
[17] HUD's Opposition to Plaintiff's Motion for Leave to Amend Complaint, No. 1:13-cv-08564 (N.D. Ill. 2017).
[18] *Id*.
[19] 135 S. Ct. at 2514, 2515 and 2522.
[20] *Id*. at 2515.
[21] *Id*. at 2525.
[22] *Id*. at 2512.
[23] CRL and Self-Help Comment to HUD, Implementation of the Fair Housing Act's Disparate Impact Standard (Oct. 18, 2019), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-sh-commentdisparateimpact-oct2019.pdf.

Nation toward a more integrated society."[24] However, by weakening the disparate impact standard under the Fair Housing Act, HUD's 2020 Rule ignored our nation's history and would thwart us from reaching a more integrated and equitable future.

HUD's current proposed action is consistent with President Biden's memorandum to the Secretary of HUD, instructing the department to redress the nation's history of discriminatory housing practices and affirming the administration's commitment to ending housing discrimination.[25] The memorandum ordered the Secretary of HUD to take the necessary steps to prevent practices that have a disparate impact. HUD is working toward fulfilling its obligation by reinstating the 2013 Rule.

But more must be done. With a strong disparate impact standard reinstituted, HUD will be better situated to challenge systemic discrimination in the housing and lending market, including discrimination arising from emerging technology and algorithmic systems. Once the 2013 Rule is back in effect, HUD should bring more Secretary-Initiated complaints as well as work with the Department of Justice to challenge systemically harmful practices that have an unjustified and discriminatory effect on protected classes.

Conclusion

For more than 45 years, disparate impact theory has been a crucial legal tool to fight discrimination and ensure equal housing opportunity. CRL, Self-Help Credit Union, and Self-Help Federal Credit Union strongly support HUD's proposed rule to rescind the 2020 Rule and reinstate the 2013 Rule. Thank you for considering our comments.

[24] 135 S. Ct. 2525-26. Kerner Commission Report (1968), http://www.eisenhowerfoundation.org/docs/kerner.pdf.
[25] The White House, Memorandum on Redressing Our Nation's and the Federal Government's History of Discriminatory Housing Practices and Policies (January 26, 2021), https://www.whitehouse.gov/briefingroom/presidential-actions/2021/01/26/memorandum-on-redressing-our-nations-and-the-federal-governmentshistory-of-discriminatory-housing-practices-and-policies/.