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Via electronic submission

August 20, 2018

Department of Housing and Urban Development
Office of General Counsel,
Rules Docket Clerk
451 7th Street SW
Room 10276
Washington, DC 20410-0001

Re: Reconsideration of HUD's Implementation of the Fair Housing Act's Disparate Impact Standard; Docket No. FR-6111-A-01

Dear Sir or Madam:

The Independent Community Bankers of America¹ (ICBA) appreciates the opportunity to provide comments to the Department of Housing and Urban Development ("HUD") on its advance notice of proposed rulemaking on reconsideration of its implementation of the Fair Housing Act's (FHA) disparate impact standard.

ICBA Position

As currently written, the application of HUD's disparate impact rule has particularly deleterious effects on community bank mortgage lending. The rule's burden-shifting framework is inconsistent with the Supreme Court's ruling in *Texas Department of Housing & Community Affairs v. The Inclusive Communities Project, Inc. (Inclusive Communities)*.² This inconsistency creates uncertainty for community banks and continues to subject lenders to legal challenges without appropriate safeguards in place.

¹ The Independent Community Banks of America®, the nation's voice for more than 5,800 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services.

With 52,000 locations nationwide, community banks employ 760,000 Americans, hold \$4.7 trillion in assets, \$3.7 trillion in deposits, and \$3.2 trillion in loans to consumers, small businesses, and the agricultural community. For more information, visit ICBA's website at www.icba.org.

² 135 S. Ct. 2507 (2015).

Under the existing HUD rules, private or governmental plaintiffs can challenge lending practices that result in, or would predictably result in, a discriminatory effect on the basis of a protected characteristic. However, the Supreme Court decision requires a charging party or plaintiff to demonstrate a causal connection between the practice and the alleged discriminatory impact before successfully making a prima facie case. Furthermore, the use of statistical evidence showing disparity could give rise to a disparate impact challenge under HUD's disparate impact rule but would not establish a prima facie case under the Court's ruling.

The differences in the framework and, specifically, the three prongs of the burden-shifting standards, create uncertainty and increase burdens for community banks, which must determine how to reconcile these different standards so that they are able to meet their fair lending responsibilities.

Background

On February 18, 2013, HUD issued a final rule which established liability under the Fair Housing Act for conduct that is otherwise lawful, but which has a disparate adverse impact on certain protected classes. Additionally, a three-part burden-shifting test was established for determining when a practice with a discriminatory effect violates the Fair Housing Act. Under this test, the charging party or plaintiff first bears the burden of proving its prima facie case that a practice results in, or would predictably result in, a discriminatory effect on the basis of a protected characteristic. If the charging party proves a prima facie case, the burden of proof shifts to the defendant to prove that the challenged practice is necessary to achieve one or more of its substantial, legitimate, nondiscriminatory interests. If the defendant satisfies this burden, then the charging party may still establish liability by proving that the substantial, legitimate, nondiscriminatory interest could be served by a practice that has a less discriminatory effect.

In 2015, the Supreme Court upheld the application of disparate impact under the Fair Housing Act in its ruling in *Inclusive Communities*; however, the Court significantly narrowed its scope. In its opinion, the Court imposed a robust causality requirement and held that a "disparate-impact claim relying on a statistical disparity must fail if the plaintiff cannot point to a defendant's policy or policies causing that disparity."³ The Court also established a burden-shifting framework for courts and the government adjudicating disparate-impact claims.

Specifically, the Court ruled that a charging party or plaintiff bringing a disparate impact claim must first demonstrate a causal connection between the challenged practice or policy and the statistical disparity affecting a protected class. This protects defendants from being held liable for racial disparities they did not create. The Court reiterated that a plaintiff who fails to allege facts at the pleading stage or produce statistical evidence

³ 135 S. Ct. at 2524.

demonstrating a causal connection cannot make out a prima facie case of disparate impact.

If the charging party or plaintiff proves a prima facie case, the defendant can then show a business rationale for the challenged practice to rebut the disparate impact claim. Finally, the burden shifts back to the charging party or plaintiff to show that an available alternative exists that has less disparate impact and serves the entity's legitimate needs.

Prima Facie Case

There are significant differences between HUD's regulation and the Supreme Court ruling in the first prong of the burden-shifting framework. HUD regulation defines "discriminatory effect" as a policy or practice that "actually or predictably results in a disparate impact on a group of persons or creates, increases, reinforces, or perpetuates segregated housing patterns because of race, color, religion, sex, handicap, familial status, or national origin."⁴ The rule states that, "[t]he charging party...has the burden of proving that a challenged practice caused or predictably will cause a discriminatory effect."⁵ This is inconsistent with the Supreme Court's ruling. The Supreme Court applied adequate safeguards at the prima facie stage to prevent abuse of disparate impact theory and to deter lawsuits initiated merely to second guess practical business decisions. At this prong, under *Inclusive Communities*, the charging party must satisfy a "robust causality requirement" that shows a specific policy that is artificial, arbitrary and unnecessary that caused a statistical disparity."⁶

Unlike the existing HUD rule, *Inclusive Communities* requires that a plaintiff show the *existence* of a disparity as well as a *specific* policy related to the disparity rather than merely showing that a challenged practice may *predictably* cause a discriminatory effect. There are several differences between the HUD rule and the *Inclusive Communities* decision that must be reconciled. To begin, when a plaintiff brings forth a claim under the HUD rule, a statistical analysis may be sufficient to make a prima facie case. However, the Court held that a mere showing of a statistical disparity is insufficient and noted that "a disparate impact claim that relies on statistical disparity must fail if the plaintiff cannot point to a defendant's policy or policies causing that disparity."⁷ Not only must a plaintiff point to a defendant's policy or policies that caused the disparity, *Inclusive Communities* explains that a single act or decision does not give rise to disparate impact liability since "a one-time act may not be policy at all."⁸

Furthermore, the Court requires a plaintiff to demonstrate a causal connection between challenged practice and the statistical disparity affecting a protected class. The Court

⁴ 24 CFR 100.500(a).

⁵ 24 CFR 100 (c)(1).

⁶ 135 S. Ct. at 2523, 2524.

⁷ *Id.* at 2523.

⁸ 135 S. Ct. at 2523.

stated that "racial imbalance does not, without more, establish a prima facie case of disparate impact."⁹

In addition to the uncertainty that these differing standards cause, maintaining the existing frameworks unnecessarily harms community banks that are the subject of banking agency enforcement actions or fair lending complaints. Currently, under HUD's standard and contrary to the Supreme Court's standard, the use of statistical disparities alone could trigger banking agency citations or referrals to the Department of Justice for alleged fair lending violations or at least the initial stages of a legal claim. Not only are community banks particularly vulnerable to reputational damage, they simply cannot afford to withstand protracted litigation.

Burden-Shifting Standard

If the plaintiff satisfies the first prong of the framework, the burden shifts to the defendant. Once again, the HUD rule does not use the same language as the Court in *Inclusive Communities*, representing the next significant difference between the two. Pursuant to the HUD rule, a defendant has the burden of proving that the challenged practice is necessary to achieve one or more substantial, legitimate, nondiscriminatory interests of the respondent or defendant. However, *Inclusive Communities* held that defendants need only offer a legitimate business justification for the specific policy underlying the disparate impact claim.¹⁰

Under the HUD rule, a defendant must prove that a challenged practice is necessary to establish a business justification. In providing a defense against disparate impact liability, *Inclusive Communities* gives leeway to defendants to explain the "valid interest served" by the policies being challenged. The Court also indicated that disparate impact should not interfere with valid policies, explaining that "[d]isparate-impact liability mandates the "removal of artificial, arbitrary, and unnecessary barriers," not the displacement of valid governmental policies."¹¹ The Court further articulated that disparate impact liability should not limit entities from "making the practical business choices and profit-related decisions that sustain a vibrant and dynamic free-enterprise system."¹²

Under the third prong of the burden-shifting framework in HUD's rule, a plaintiff may still prevail upon proving that the substantial, legitimate, nondiscriminatory interests supporting the challenged practice could be served by another practice that has a less discriminatory effect.¹³ Note that the plaintiff does not need to demonstrate that the defendant considered and rejected such a practice. The Supreme Court determined the burden rests with the plaintiff to prove that there is an available alternative practice that has less disparate impact that serves the defendant's legitimate needs. The less

⁹ 135 S. Ct. at 2523.

¹⁰ 135 S. Ct. at 2521.

¹¹ 135 S. Ct. at 2521, *citing* 401 U.S. 431 (1971).

¹² 135 S. Ct. at 2518.

¹³ 24 CFR 100.500(c)(3).

discriminatory alternative must be “equally effective” as the challenged practice.¹⁴ HUD’s rule is inconsistent with the appropriate burden of persuasion expressed by the Court.

These limitations underscore the fact that various legitimate factors go into making a lending policy decision, including market factors, credit history and other underwriting criteria, and banking relationships. Community banks should be able to make practical business choices that sustain a vibrant and dynamic free-enterprise system, and that allow them to continue providing loans, especially for those who need them most, without being subject to artificial barriers that can result from the application of inappropriate disparate impact standards.

Conclusion

We urge HUD to amend its disparate impact rule to align with the limitations set forth in *Inclusive Communities* to prevent the unnecessary and onerous costs placed on community banks to defend against frivolous claims inappropriately based on statistical disparities. Defending against these types of claims raises significant challenges to community bank mortgage lenders. A community bank may successfully argue that a claim failed to make a prima facie claim, or that a certain practice is necessary to reduce credit risk and maintain a certain level of loan quality and performance, which is a legitimate business interest. However, even if lenders prevail at this stage, community banks would have to expend substantial amounts of money and suffer the reputational consequences of a discrimination charge.

Thank you for the opportunity to respond to this notice. Given the significant amount of uncertainty created by the inconsistency of HUD’s current disparate impact rule and the Supreme Court decision, ICBA strongly urges HUD to amend and align its rule with the standards outlined by the Supreme Court in *Inclusive Communities* to halt the expansion of abusive, frivolous or illegitimate disparate impact claims and reduce confusion for community banks.

Please contact me at Lilly.Thomas@icba.org or (202) 659-8111 with any questions regarding our comments.

Sincerely,

/s/

Lilly Thomas
Senior Vice President & Senior Regulatory Counsel

¹⁴ 490 U.S. 642, 661 (1989).