The Forthcoming Amendments to Regulation C – a Litigation Perspective

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This article discusses three specific ways in which amendments to Regulation C, the regulation that implements the Home Mortgage Disclosure Act, are important from a litigation perspective.

The Consumer Financial Protection Bureau ("CFPB") currently is finalizing significant amendments to Regulation C, the regulation that implements the Home Mortgage Disclosure Act ("HMDA").[1] HMDA and Regulation C require financial institutions to report, in connection with certain residential mortgage applications, demographic data such as a borrower's race and ethnicity, and other information such as the action taken on the application, the rate spread, and the property location. The government makes much of this data available to the public, such that anyone can review the activities of a financial institution and draw comparisons to the performance of peer institutions.

Although HMDA does not provide for a private right of action, HMDA data often plays a role in disparate impact litigation under the Fair Housing Act ("FHA").[2] In a disparate impact case under the FHA, a plaintiff typically will seek to use HMDA data and other statistical evidence to show that, even if a defendant did not intentionally discriminate, the defendant's lending policies nonetheless caused disproportionate harm to members of a protected class who applied for or received a residential mortgage loan. The Supreme Court recently held that disparate impact claims are legally cognizable under the FHA,[3] and HMDA data thus will continue to play a role in such cases.

The amendments to Regulation C will represent the first imprint made by the CFPB to the HMDA reporting rules. In 2010, the Dodd-Frank Act created the CFPB, made several direct changes to HMDA's statutory language, and placed Regulation C under the purview of the CFPB. The CFPB subsequently concluded that, for purposes of disparate impact analysis, the data currently reported by financial institutions pursuant to Regulation C is insufficient, and "cannot demonstrate whether borrowers and applicants have received nondiscriminatory treatment by financial institutions."[4]

The CFPB's proposed amendments will approximately double the number of data points that financial institutions must report

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under HMDA. For example, under the proposed amendments, the reporting requirements now will encompass a borrower's credit score and income, the debt-to-income ("DTI") ratio and loan-to-value ("LTV") ratios associated with the transaction, the action (approval or denial) recommended by the lender's automated underwriting system (if any), the reason for denial of the loan application (if the application was denied), and whether the application was received through a broker or retail channel.

These amendments to Regulation C may reshape disparate impact litigation under the FHA in a number of respects. This article discusses three specific ways in which these amendments are important from a litigation perspective.

First, the amendments can strengthen the rationale for a strict application of the FHA's two-year statute of limitation.

Second, the amendments will increase the volume of data available to the parties and the court at the pleading stage of a case, when a defendant makes an initial motion to dismiss. Third, the amendments should help to minimize disputes between the parties as to the reliability of different sources of data concerning the impact of a defendant's lending policies.

The Statute of Limitations Issue

Statute of limitation defenses can be crucial in FHA disparate impact cases, as such cases often concern policies dating back many years. When an FHA claim is brought by a private person, a two-year statute of limitation applies,[5] while an 18-month statute of limitation applies to FHA claims brought by the Attorney General.[6] These deadlines generally spring from the occurrence of the alleged discriminatory act.

In some cases not involving the FHA, federal courts have held that a statute of limitation may be tolled if the plaintiff did not discover, and could not have discovered, key facts underlying a claim. The Supreme Court has held that this "discovery rule" should not be imputed into every federal statute of limitation, and that, instead, the applicability of this rule turns on the relevant statutory language and intent.[7] In addition, except where explicit language to this effect is found in the governing statute, the Supreme Court has never permitted federal regulatory agencies to invoke the discovery rule.[8] Based on these principles, the discovery rule likely would be deemed inapplicable to FHA disparate impact claims – however, the Court has not yet considered this specific question.

Assuming *arguendo* that the discovery rule does apply to FHA disparate impact claims, at least when such claims are brought by private citizens, the question is when a plaintiff should be deemed to have discovered, or had the ability to discover, the factual underpinnings of such a claim. Notably, the explicit purpose of HMDA is to "provide the citizens and public officials of the United States with *sufficient information* to enable them to determine whether depository institutions are fulfilling their obligations. . . ."[9] Once a defendant's HMDA data has been published, and "sufficient information" is available, a court arguably should not find that a plaintiff was reasonably ignorant of the facts.[10]

The intent behind Regulation C is that, as the field of disparate impact analysis continues to evolve, HMDA should adapt in accordance with the statutory purpose of providing "sufficient information." The proposed amendments are not explicitly indended to support statute of limitation defenses, but

that may be the effect of the amendments. Because the government is updating Regulation C in view of current techniques of disparate impact analysis, it is difficult for a plaintiff to prove that an alleged disparate impact remained unknown, and undiscoverable, even after a defendant's HMDA data was published. Thus, when an FHA disparate impact case is commenced more than two years after the occurrence of the alleged discriminatory act, the amendments should tend to support the statute of limitations defense to the claim.

Motions to Dismiss

In its recent opinion holding that disparate impact claims are cognizable under the FHA, the Supreme Court stressed the importance of guarding against meritless disparate impact claims. As the Court noted, it is crucial to "examine with care whether a plaintiff has made out a *prima facie* showing," and "prompt resolution of these cases is important."[11] Specifically, "[a] plaintiff who fails to allege facts at the pleading stage or produce statistical evidence demonstrating a causal connection [between the defendant's policies and the alleged impact] cannot make out a *prima facie* case of disparate impact."[12]

In connection with this guidance, the forthcoming amendments to Regulation C will be significant in two main respects. First, the amendments will make more data available to plaintiffs at the threshold stage of a case. Data that previously was obtainable only by means of a discovery request now will be publicly available pursuant to HMDA. A plaintiff thus may be able to incorporate more data into a complaint in an attempt to create the appearance of a potentially valid disparate impact claim.

Second, the amendments will increase the scope of data that a defendant, in a motion to dismiss, can cite to demonstrate that a disparate impact case is statistically flawed. In the context of a motion to dismiss, a court typically will not consider documents or information outside the scope of the complaint. This limitation may not apply, however, to facts that are subject to judicial notice.[13] In a disparate impact case, the court may accord the defendant latitude to cite HMDA data in support of a motion to dismiss, as such data is publicly available and may have been relied upon in the complaint. However, the court may decline to consider proprietary, non-HMDA data that has not previously been produced to the plaintiff and is not in the public domain. By expanding the scope of HMDA data, the amendments to Regulation C will make it possible for a defendant to offer a more detailed presentation to the court in support of a motion to dismiss prior to commencement of discovery.

In sum, the amendments will level the statistical playing field at the outset of an action by creating a more complete data set from which both parties can draw in support of or in opposition to a motion to dismiss. This phenomenon will allow courts to analyze certain aspects of a disparate impact case at the pleading stage to an extent that previously was not feasible until summary judgment. On balance, this change will benefit defendants. All else being equal, it is in a defendant's interest to expose fatal defects in a plaintiff's case before the defendant has undergone the expense and inconvenience of discovery.

Sources of Data

When certain categories of data are not reported to the government pursuant to HMDA, parties to a disparate impact case

may look to various other sources for such information. However, disputes can ensue as to the reliability and relevance of such alternative data sources. Such disputes can muddy the waters of a disparate impact case and make it more difficult to define the parties' deeper disagreements in the areas of law and policy. By expanding the scope of HMDA data, the forthcoming amendments to Regulation C may help to obviate such disputes, allowing courts to concentrate instead on the parties' respective legal arguments, their competing techniques for interpreting relevant impact data, and the defendant's proffered justification for any alleged impact on a protected class.

Not only will the use of one, centralized data set clarify the deeper legal and philosophical differences between the parties, but it also will highlight key disagreements between the plaintiff and other, non-party constituencies. Indeed, when a private citizen or non-governmental organization brings a disparate impact claim, the plaintiff's position may not be shared by the government or other interest groups. For example, in a disparate impact case, the City of Los Angeles asserted that Wells Fargo's policy of offering loans backed by the Fair Housing Administration was creating a disparate impact on minority borrowers because these loans, in some instances, were more expensive than conventional loans.[14] The Fair Housing Administration did not believe that these loans were discriminatory, and indeed had endorsed them. The court dismissed the case.

As the Wells Fargo case illustrates, a disparate impact claim may be, at its base, a tug of war on a defendant's resources and policies. This problem is legally relevant for two reasons. First, as the Supreme Court has noted, a disparate impact claim should not "put housing authorities and private developers in a double bind of liability."[15]

Second, as noted, a plaintiff must identify a "causal connection" between, on the one hand, voluntary policy choices by the defendant, and, on the other hand, the alleged disparate impact.[16] If the policy at issue is a product of the regulatory environment, the plaintiff cannot satisfy that burden. As the court held in the Wells Fargo case, "[i]f any disparate impact results from USFHA loans, it is a result of federal policy and not Wells Fargo policy."[17]

To the extent that relevant parties and non-parties have based their respective positions on the same set of impact data, such fundamental issues of law and policy can more easily come into focus. The forthcoming amendments to Regulation C thus can help to distill the key issues in a disparate impact case and, in particular, show that the plaintiff's arguments may not be universally accepted by other interested parties.

Conclusion

The proposed amendments to Regulation C are, in some respects, less than ideal for financial institutions. After all, these amendments will require reporting entities to divulge more data that could be misconstrued in the context of disparate impact cases. In another sense, however, the real effect of these amendments is a matter of the timing of the production of such data. Previously, certain data points were obtainable only through discovery. Now, such data may be in the public domain before a case is filed. As discussed, this change should accelerate the merits-based assessment of impact cases, eliminate certain excuses for the untimely filing of such cases, and help to crystallize

certain substantive arguments on the basis of which lenders potentially can seek the early dismissal of such cases.

NOTES:

[1]*See* 12 U.S.C. § 2810 et seq. *See also Home Mortgage Disclosure Act (Regulation C): Proposed Rule with Request for Public Comment*, 79 Fed. Reg. 51,731 (Consumer Fin. Prot. Bureau Aug. 29, 2014) (the "Proposed Amendments").

[2]*See* 42 U.S.C. § 3601 et seq.

[3]*See Texas Dept. of Housing and Community Affairs v. Inclusive Communities Project, Inc.*, 135 S. Ct. 2507, 192 L. Ed. 2d 514 (2015).

[4]*See* Proposed Amendments § VI(B).

[5]*See* 42 U.S.C. § 3613.

[6]*See* 42 U.S.C. § 3614.

[7]*See TRW Inc. v. Andrews*, 534 U.S. 19, 122 S. Ct. 441, 151 L. Ed. 2d 339 (2001).

[8]*See Gabelli v. S.E.C.*, 133 S. Ct. 1216, 185 L. Ed. 2d 297, Fed. Sec. L. Rep. (CCH) P 97299 (2013).

[9]*See* 12 U.S.C. § 2801 (emphasis added).

[10]*See also* Remarks of Rep. St. Germain, Dec. 18, 1975, 121 Cong. Rec. 41,709 ("[W]e will enable citizens and public officials – by arming them with the facts – to combat what has been known as 'redlining': that is, when certain institutions refuse to lend mortgage money in our Nation's older urban and ethnic neighborhoods."); Remarks of Sen. Proxmire, July 26, 1975, 121 Cong. Rec. 25,160 ("With this information, depositor[s] can find out whether the bank or the savings and loan is giving reasonable service to the community."); House Report No. 94-561 (Oct. 10, 1975) ("The purpose of this title [HMDA] is, by providing facts, to bring to an end more than a decade of 'redlining' charges and countercharges. . . . Your committee believes that disclosure will identify the beginning stages of redlining. . . .").

[11]*Texas Dept. of Housing and Community Affairs v. Inclusive Communities Project, Inc.*, 135 S. Ct. 2507, 192 L. Ed. 2d 514 (2015).

[12]*Texas Dept. of Housing and Community Affairs v. Inclusive Communities Project, Inc.*, 135 S. Ct. 2507, 192 L. Ed. 2d 514 (2015).

[13]*Global Network Communications, Inc. v. City of New York*, 458 F.3d 150, 65 Fed. R. Serv. 3d 1081 (2d Cir. 2006).

[14]*City of Los Angeles v. Wells Fargo & Co.*, 2015 WL 4398858 (C.D. Cal. 2015).

[15]*Texas Dept. of Housing and Community Affairs v. Inclusive Communities Project, Inc.*, 135 S. Ct. 2507, 192 L. Ed. 2d 514 (2015).

[16]*Texas Dept. of Housing and Community Affairs v. Inclusive Communities Project, Inc.*, 135 S. Ct. 2507, 192 L. Ed. 2d 514 (2015).

[17]*City of Los Angeles v. Wells Fargo & Co.*, 2015 WL 4398858 (C.D. Cal. 2015).