

The Law of Lending Discrimination



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Introduction

Home ownership has long been touted as the culmination of the American Dream. It has become an engine of economic expansion, a point of political pride, and a social signal. Yet for many, unscrupulous lending companies make the dream of homeownership impossible. For others, homeownership becomes a nightmare once jumps in interest rates and balloon payments associated with their predatory loans come to fruition.

In any lending transaction, it is illegal for certain personal characteristics of the applicant or borrower to be used as a factor in the lending institution's decision-making process. Lending discrimination can take the form of loan or application denials on the basis of a person's protected class, and different rates or other terms to an individual or a group of people based upon one or more of these protected characteristics (including race, gender, ethnicity, and religion, among others).

A slightly different form of lending discrimination exists in cases of predatory lending. In these situations a lender seeks out members of a protected class for the purpose of establishing an expensive, sometimes unnecessary loan or mortgage. This is the type of practice that is partially responsible for the recent housing crisis.

The purpose of this article is two-fold. First, it provides an overview of the types of lending discrimination, discusses what laws apply to lending discrimination, and explains how to establish a prima facie case and pretext. This discussion will borrow concepts and case law from the areas of employment discrimination and the related issue of rental discrimination. Each of these areas share similar required elements as well as

the need to establish pre-text. Second, this article provides an overview of predatory lending practices, applicable law, and potential remedies.

I. Types of Lending Discrimination

The majority of housing discrimination cases involves claims of disparate treatment.¹ A typical case arises when a mortgage application is denied and the applicant alleges that the denial was based upon consideration of the applicant's race or other protected characteristic. Often, there is no direct evidence of intentional discrimination and the lender will defend against the allegations on the basis that the application was denied for legitimate, nondiscriminatory reasons.

Disparate impact claims focus on a lender's policy that allegedly results in discrimination against a protected class. Here, the plaintiff alleges the discriminatory effect that a lender's facially neutral policy has on a protected class. It is not uncommon for plaintiffs to allege claims of both disparate treatment and disparate impact.

Another type of discrimination is called redlining. This occurs when a lender does not approve a mortgage because the home is located in a particular neighborhood. These neighborhoods usually consist predominately of minority homeowners, and lenders often consider them high-risk. This has the effect of reducing the availability of credit in certain areas and may play a part in the alternative problem of reverse redlining and predatory lending.

¹ ROBERT G. SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION § 10:2 (1990 & Supp. 2001).

II. Laws that prohibit housing discrimination: What law applies and when?

Lending discrimination is regulated at the federal level under the Equal Credit Opportunity Act (ECOA)² and the Fair Housing Act (FHA).³ The ECOA was enacted in 1974 in an effort to eradicate discrimination in credit transactions against women. Subsequent amendments include other protected classes.⁴ The statute is applicable to any entity that extends credit to consumers, including banks, credit card companies, and other lenders,⁵ prohibiting discrimination in the financing, sale, or rental of residential real estate.⁶

The FHA (Title VIII of the Civil Rights Act of 1968) was meant as a vehicle to prohibit discrimination in the sale, lease, or rental of housing based upon specific, protected characteristics.⁷ As defined in 42 U.S.C. § 3602(b), the FHA applies to all structures that will be or are occupied as a residence as well as land to be sold for the construction of a residence. This includes homes, apartment buildings, trailer parks, condominiums, or any of the numerous other structures that are used as residences. FHA prohibits discrimination in all aspects of "residential real-estate related transactions," including but not limited to:

- Making loans to buy, build, repair or improve a dwelling
- Purchasing real estate loans
- Selling, brokering, or appraising residential real estate
- Selling or renting a dwelling

² 15 U.S.C.A. § 1691 (2010).

³ 42 U.S.C.A. § 3601 (2010).

⁴ In 1976, amendments added race, color, religion, national origin, and age as protected classes, Pub. L. No. 94-239.

⁵ 15 U.S.C.A. § 1691(a).

⁶ *Id.*

⁷ 42 U.S.C.A. §§ 3604-3605 (2010).

It is important to note that these statutes differ in the protected classes that they cover. The ECOA does not prohibit discrimination based on familial status (children) or handicap, which is protected by the FHA.⁸ In contrast, it does cover public assistance based upon income, age, marital status and retaliation for claims under the Consumer Protection Act, areas not covered by the FHA.⁹

Another major difference between the ECOA and the FHA is that the ECOA¹⁰ does not apply to activities prior to application, while the FHA does; the FHA not only applies to post-application lending activities or transactions, but also pre-application lending activities such as marketing and solicitation.¹¹ Under the ECOA, it is unlawful for a lender to discriminate on a prohibited basis in any aspect of a credit transaction, and under both the ECOA and the FHA, it is unlawful for a lender to discriminate on a prohibited basis in a residential real estate related transaction. Under one or both of these

⁸ ECOA prohibits discrimination based on any of these “classes” or protected personal characteristics: Race or color, Religion, National origin, Gender, Martial status, age, income derived from any public assistance program, and the applicant’s exercise, in good faith, of any right under the Consumer Credit Protection Act.

⁹ FHA prohibits discrimination based on any of these classes or characteristics: Race or color, National origin, Religion, Gender, Familial Status (defined as children under the age of 18 living with a parent or legal custodian, pregnant women, and people securing custody of children under 18), and Handicap.

¹⁰ *Ordille v. U.S.*, 216 Fed. Appx. 160, 164 (3d Cir. 2007) (citing 12 C.F.R. § 202.2(m), which states that “Credit transactions” are defined by the regulations governing the ECOA to include every aspect of an applicant’s dealings with a creditor regarding an application for credit or an existing extension of credit (including, but not limited to, information requirements; investigation procedures; standards of creditworthiness; terms of credit; furnishing of credit information; revocation, alteration, or termination of credit; and collection procedures”).

¹¹ *Raso v. Lago*, 958 F. Supp. 686, 698 (D. Mass. 1997) (stating that “FHA subsidized and unsubsidized housing programs shall pursue affirmative fair housing marketing policies in soliciting buyers and tenants, in determining their eligibility, and in concluding sales and rental transactions”).

laws, a lender may not, because of a protected personal characteristic, do any of the following:

- Fail to provide information or services or provide different information or services regarding any aspect of the lending process, including credit availability, application procedures, or lending standards
- Discourage or selectively encourage applicants with respect to inquiries about or applications for credit
- Refuse to extend credit or use different standards in determining whether to extend credit
- Vary the terms of credit offered, including the amount, interest rate, duration, or type of loan
- Use different standards to evaluate collateral
- Treat a borrower differently in servicing a loan or invoking default remedies
- Use different standards for pooling or packaging a loan in the secondary market.

In Iowa, the statute that prohibits discrimination in lending is the Iowa Civil Rights Act of 1965 (ICRA).¹² Section 216.10 of the ICRA makes discrimination in credit transactions unlawful and sections 216.8 and 216.8A discuss housing discrimination. The Iowa Supreme Court, in *State v. Keding*¹³, succinctly confirmed the similarity of the ICRA and the FHA by stating, “[F]ederal court decisions interpreting the FHA are persuasive when we consider the provisions of the Iowa Act.” It is important to recognize that the Iowa statute prohibits discrimination for additional classes, specifically sexual orientation and gender identity.¹⁴

Additional claims under Iowa law, besides those codified in the ICRA, may also exist. Section 537.3311 prohibits discrimination in credit transactions, but its applicability to lending discrimination—specifically mortgages—is limited because it

¹²The “Iowa Civil Rights Act of 1965” is codified in Iowa Code Chapter 216 (2009).

¹³ 553 N.W.2d 305, 307 (Iowa 1996).

¹⁴ IOWA CODE ANN. § 216.8 (West 2010).

does not apply to amounts financed greater than \$25,000. Sections 535A.1 to 535A.9 forbid redlining in lending decisions.

III. Bringing a Claim

The FHA provides a victim of lending discrimination different methods for bringing a claim.¹⁵ An individual can file a complaint with the Department of Housing and Urban Development (HUD), which will initiate an administrative hearing or a court suit. She may also file a direct court action either simultaneously or sequentially to the administrative hearing. In addition, the Attorney General can file suit on behalf of aggrieved parties. The procedures for bringing the complaint vary depending on the mechanism used.

Victims of ECOA violations can file a complaint with HUD or file their own private civil action. HUD complaints must be filed within one year of the incident. Given the number of procedural requirements of the ECOA, there exist many ECOA violations on non-discriminatory grounds.¹⁶

Other ECOA considerations include where and if a complaint can be filed.¹⁷ Of special concern to both ECOA and FHA claims is the applicability of an arbitration agreement. The existence of an arbitration agreement may bar the plaintiff from filing a civil action, leaving them with a less than desirable option of arbitration. Arbitration

¹⁵ SCHWEMM, *supra* note 1, at § 12A:1 (1990 & Supp. 2003).

¹⁶ ALYS COHEN ET. AL., NATIONAL CONSUMER LAW CENTER, CREDIT DISCRIMINATION 231-32 (5th ed. 2009).

¹⁷ Chicago Lawyer's Committee for Civil Rights Under Law, Inc., *The Law of Mortgage Lending and Insurance Discrimination: A Substantive and Procedural Manual for Attorneys*, <http://www.clccrul.org/publications.html> (accessed June 1, 2010) (providing a listing of the advantages and disadvantages of administrative hearings and private civil actions).

agreements often require each party to pay their own attorney's fees. These costs have been found to be unenforceable given the prohibitive nature such requirements have in the context of discriminatory lending.¹⁸

ECOA and FHA claims have a two-year statute of limitations for private civil actions. Under the ECOA this generally begins to run on the date of the violation, not the date when credit was applied for.¹⁹ A FHA complaint must be filed within one year of the violation and, if the plaintiff chooses to file a private suit, the two-year limitations period is tolled while the complaint is proceeding.²⁰ The Iowa Code requires that an administrative complaint be filed within 300 days from the date of the violation.²¹ A civil action must be filed within two years from the date of occurrence with the stipulation that the claim is tolled during the administrative hearing process.²²

IV. Disparate Treatment

When making a case for disparate treatment, if the plaintiff is able to supply sufficient direct evidence indicating that prohibited factors were used in the denial of a loan application, then there is no need to complete the more difficult circumstantial evidentiary process.²³ However, as is often the case, direct evidence is difficult to obtain and thus the courts frequently require the following *McDonnell Douglas* analysis.

First, it is necessary to distinguish the difference between the requirements of the ECOA and the FHA and other claims that may be brought under sections 1981 and 1982

¹⁸ *Id.* at 229. (citing *Kristian v. Comcast Corp.*, 446 F.3d 25, 52-53 (1st Cir. 2006)).

¹⁹ *Id.* at 250-251.

²⁰ *Id.*

²¹ § 216.15.

²² § 216.16.

²³ COHEN, *supra* note 18, at 70 (2009).

of the Civil Rights Act of 1964.²⁴ These sections not only give citizens the right to enforce contracts and buy or sell property,²⁵ but also maintain a higher standard in discrimination cases by requiring a plaintiff to show intentional discrimination. In contrast, under the ECOA and the FHA the plaintiff must merely show that race, or some other protected factor was a component in the denial of the loan application.

With the exception of the Seventh Circuit, in order to establish a prima facie showing of discrimination under the FHA and the ECOA, a plaintiff must show (1) membership in a protected class; (2) he or she applied for and was qualified for a loan with a lending institution; (3) the loan was rejected despite his or her qualifications; and (4) the lending institution continued to approve loans for applicants with similar qualifications.²⁶

The fourth element, especially in the context of lending, can be difficult to prove. The decision in *Latimore v. Citibank Federal Savings Bank* proves that showing the lending institution approved loans for similarly qualified applicants in a credit transaction is challenging given the non-competitive nature of those transactions.²⁷ In addition, it can be extremely difficult to show that the plaintiff's application was exactly the same as the loans that were approved. In this regard, courts have been lenient in not requiring strict similarity in loan applications.²⁸ The fourth element could also be proved if "the

²⁴ 42 U.S.C.A. §§ 1981-1982.

²⁵ *Id.*

²⁶ *Rowe v. Union Planters Bank*, 289 F.3d 533, 535 (8th Cir. 2003).

²⁷ *Latimore v. Citibank Fed. Savings Bank*, 151 F.3d 712, 714-16 (7th Cir. 1998).

²⁸ COHEN, *supra* note 18, at 73 (2009).

plaintiff presents direct evidence that the lender intentionally targeted” them in a lending transaction.²⁹

After establishing a prima facie case, the plaintiff creates a presumption of discrimination, which must then be rebutted by the defendant. The defendant has the burden of production and must provide admissible evidence that would allow the trier of fact to reasonably determine that the denial was not based on impermissible, discriminatory considerations.³⁰ In essence, it is up to the defendant to “articulate some legitimate, nondiscriminatory reason...” for the denial.³¹ Should the defendant fail to produce such evidence, the plaintiff prevails.

If the defendant is able to rebut the presumption of discrimination, then the plaintiff “is given a final opportunity to show that the legitimate reasons offered by the defendant were merely a ‘pretext’ for discrimination.”³² The plaintiff maintains the burden of persuasion and must convince the trier of fact beyond a preponderance of the evidence that the defendant illegally discriminated against them. Rebutting the presumption of discrimination and establishing a pre-text for discrimination becomes the most challenging aspect of housing discrimination litigation.

Many of the principles of housing discrimination cases have been imported from employment discrimination litigation. With regard to employment discrimination, the introduction of evidence related to the defendant’s treatment of similarly qualified applicants is very persuasive.³³ However, in lending discrimination this can be difficult

²⁹ *House v. Cal State Mortg. Co.*, 2009 U.S. Dist. LEXIS 58529 (E.D. Cal. 2010).

³⁰ *Texas Dept. of Community Affairs v. Burdine*, 450 U.S. 248, 257 (1981).

³¹ *McDonnell Douglas Corp. v. Green*, 411 U.S. 792, 802 (1973).

³² SCHWEMM, *supra* note 1, at § 10:2 (1990 & Supp. 2001).

³³ *McDonnell Douglas Corp.*, 411 U.S. at 804.

to ascertain because of its less adversarial nature. Unlike in employment cases, here there are often not a lot of similarly qualified applicants for a mortgage or a rental property.

Therefore, testers, or comparators, are utilized.

A tester is a similarly qualified applicant, not a member of the plaintiff's protected class that is used to evaluate whether a defendant's motives for denying the plaintiff were legitimate.³⁴ If the tester is approved for financing where the plaintiff was not, this may indicate that the defendant was illegally discriminating when declining the plaintiff's application. Testing evidence can be crucial and dispositive in establishing lending discrimination.³⁵

The effectiveness of testers is best seen through judicial decisions. A plain and effective use of testers is illustrated in *Pollitt v. Bramel*,³⁶ where testers were employed after the conduct of the defendant in the rental of a mobile home indicated a possibility of discrimination, and the plaintiff initiated a complaint.³⁷ Here, a pair of white testers was shown mobile homes that the defendant indicated were available for immediate occupancy.³⁸ However, a black tester inquiring the next day was told there were no homes available.³⁹ Evidence at trial indicated that as of the date the black testers were denied, there were four trailers vacant.⁴⁰ The court found that the defendant had discriminated against plaintiffs on the basis of race and awarded compensatory and

³⁴ *Havens Realty Corp. v. Coleman*, 455 U.S. 363, 373 (1982).

³⁵ *Hamilton v. Miller*, 477 F.2d 908, 910 (10th Cir. 1973).

³⁶ *Pollitt v. Bramel*, 69 F. Supp. 172 (S.D. Ohio 1987).

³⁷ *Id.*

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ *Id.*

punitive damages.⁴¹ The court noted that the testing evidence, combined with the other actions of the defendant, indicated that the reasons provided by defendant for denying the rental of a mobile home were merely a pretext for discrimination.⁴² This decision, and others like it, shows that testing evidence can provide a nearly insurmountable hurdle for defendants to jump.

Of course, presenting testing evidence provides its own difficulties. The plaintiff “is required to show that [he or she] is similarly situated in all relevant aspects to the non-minority comparator.”⁴³ Testers must be “nearly identical to prevent courts from second-guessing” reasonable decisions and “confusing apples with oranges.”⁴⁴ While extremely useful in the context of rental discrimination, the use of testers is more difficult in determining the existence of lending discrimination. Because loan applications are extremely detailed and often costly, the use of tests is often more difficult.⁴⁵ In addition, practical problems exist in supplying the amount of personal detail required from a loan application and correlating that information to match that of the protected class applicant.⁴⁶

Offering direct evidence of discriminatory statements made by the defendant, or his agent can strengthen a plaintiff’s case.⁴⁷ Such discriminatory remarks can be made directly to the plaintiff, a third party, another employee or resident, or tester.⁴⁸ These

⁴¹ *Id.* at 177.

⁴² *Id.* at 176.

⁴³ *Boykin v. Bank of America Corp.* 162 Fed. Appx. 837, 839 (11th Cir. 2005) (citing *Silvera v. Orange County Sch. Bd.*, 244 F.3d 1253, 1259 (11th Cir. 2001)).

⁴⁴ *Id.*

⁴⁵ COHEN, *supra* note 18, at 86 (2009).

⁴⁶ *Id.*

⁴⁷ *Thronson v. Meisels*, 800 F.2d 136, 142 (7th Cir. 1986).

⁴⁸ SCHWEMM, *supra* note 1, at § 32:3 (1990 & Supp. 2001).

statements may provide strong evidence of discrimination and the courts have found them to be very persuasive.⁴⁹

V. Disparate Impact

In the context of disparate impact claims, in order to establish the prima facie case the plaintiff needs to show that a defendant's facially neutral policy has a significant and adverse impact on a protected group.⁵⁰ There must also be a causal link between the policy and the disparate impact.⁵¹ These principles, like those of disparate treatment, are imported from employment litigation.

The introduction of statistical evidence to illustrate the policy's effect on the protected group is essential. Producing statistical evidence indicating discrimination, however, is not dispositive. While no bright line rule exists, the courts have established that the plaintiff must prove that the defendant's policy has a "significantly adverse or disproportionate impact on persons of a particular [type] produced by the [defendant's] facially neutral acts or practices."⁵² Notice that this also requires the plaintiff to show that the policy does not adversely impact other, non-protected groups or, if it does, that the policy still primarily harms members of the protected class.

The persuasiveness of statistical evidence was acknowledged in *McDonnell*, within the context of an employment discrimination suit, when the court stated, "statistics as to petitioner's employment policy and practice may be helpful to determine whether

⁴⁹ *Phillips v. Hunter Trails Community Ass'n*, 685 F.2d 184, 188 (7th Cir. 1982) (Court found reference of defendant's attorney calling plaintiffs "niggers" to be indicative of defendant's discrimination).

⁵⁰ *Ramirez v. GreenPoint Mortg. Funding, Inc.*, 633 F. Supp. 2d 922 (N.D. Cal. 2008).

⁵¹ COHEN, *supra* note 18, at 76 (2009).

⁵² *Pfaff v. HUD*, 88 F.3d 739, 745 (9th Cir. 1996) (quoting *Palmer v. United States*, 794 F.2d 534, 538 (9th Cir. 1986)).

petitioner's refusal to rehire respondent in this case conformed to a general pattern of discrimination against blacks.”⁵³ Local statistics are generally more effective, but national statistics can still be utilized. Statistical evidence was provided in *Ramirez* when it was shown that “the Home Mortgage Disclosure Act data from the federal government showed that minorities who borrowed from 2004 and 2006 were almost 50 percent more likely than white borrowers to have received a high-APR loan to purchase or refinance their home.”⁵⁴

Statistical evidence of a company’s lending habits is readily available. Since the Home Mortgage Disclosure Act of 1975, the majority of lending companies have been required to annually disclose information regarding their lending activities. This information is used to evaluate whether lenders are adequately serving minority communities. Information about specific lenders can be obtained by visiting one of eight central depositories throughout the state of Iowa.⁵⁵

After establishing the prima facie case of a disparate impact claim, the defendant has the opportunity to provide a business justification for the discrimination. Here, the defendant has both the burden of production⁵⁶ and persuasion.⁵⁷ While there is some disagreement between the circuits,⁵⁸ generally a defendant can provide evidence of a “business necessity” or show that such a practice serves the legitimate goals of the lender.

⁵³ *McDonnell Douglas Corp.*, 411 U.S. at 805.

⁵⁴ *Id.* at 928-29.

⁵⁵ Federal Financial Institutions Examination Council, *Central Depository Database*, <http://www.ffiec.gov/CentralDepository/default.aspx>; *select IA – IOWA* (2010).

⁵⁶ *Cota v. Tucson Police Dept.*, 783 F. Supp. 458, 472 (D. Ariz. 1992).

⁵⁷ SCHWEMM, *supra* note 1, at § 10:5 (1990 & Supp. 2001) (Stating it is unclear whether the 1991 Civil Rights Act, which shifted the burden of persuasion in Title VII cases of employment discrimination to defendants, is also applicable to cases under Title VIII).

⁵⁸ *Compare Huntington Branch, NAACP v. Town of Huntington*, 844 F.2d 926, 939 (2d Cir. 1988). And *Pfaff v. HUD*, 88 F.3d 739, 747 (9th Cir. 1996).

The Eighth Circuit has defined a business necessity as a policy that has a “manifest relationship.”⁵⁹ In *Smith v. Des Moines*, the majority found that the defendant established a manifest relationship for requiring captains in the fire department to pass a fitness test that was necessary to wear a self-contained breathing apparatus because those devices are used when suppressing fires, which is a duty often performed by captains.⁶⁰

Even upon a showing of business necessity, the plaintiff may still prevail if they can demonstrate that there are other effective policies that result in a lesser discriminatory impact.⁶¹ “If the creditor demonstrates a significant business justification, the plaintiff can still prove discrimination if another practice meeting the creditor’s legitimate concerns would have less of a discriminatory impact.”⁶² The plaintiff has to illustrate that the less discriminatory policy will equally meet the defendant’s business concerns and objectives.⁶³

Some courts have implemented criteria for the evaluation of a disparate impact claim under the FHA:

(1) the strength of the plaintiff's statistical showing; (2) the legitimacy of the defendant's interest in taking the action complained of; (3) some indication-which might be suggestive rather than conclusive-of discriminatory intent; and (4) the extent to which relief could be obtained by limiting interference by, rather than requiring positive remedial measures of, the defendant.⁶⁴

The first criterion requires the court to assess the strength of the plaintiff’s statistical evidence and its effect on not just the protected class, but also the population in general.

This has sometimes led to an evaluation of the demographic background of the affected

⁵⁹ *Smith v. Des Moines*, 99 F.3d 1466, 1471 (8th Cir. 1996).

⁶⁰ *Id.*

⁶¹ *Cota*, 783 F. Supp. at 472.

⁶² COHEN, *supra* note 18, at 83 (2009).

⁶³ COHEN, *supra* note 18, at 84 (2009).

⁶⁴ *Phillips*, 685 F.2d at 184.

area as a means to determine if the policy may have some discriminatory undertones.⁶⁵

The second factor determines the legitimacy of the defendant's use of a potentially discriminatory policy. Deference is given to an authorized action by a governmental body; but, unauthorized governmental action—or the policy of a defendant that perpetuates segregation—is strictly scrutinized.⁶⁶

In finding the third criterion the least important of all, the court in *Metropolitan v. Arlington Heights* stated, “The equitable argument for relief is stronger when there is some direct evidence that the defendant purposefully discriminated against members of minority groups because that evidence supports the inference that the defendant is a wrongdoer.”⁶⁷ If the plaintiff is unable to provide direct evidence of purposeful discrimination, then the court may require a greater showing of adverse impact before supplying a remedy.

Finally, the fourth factor illustrates the court's wish to avoid intruding too deeply upon private rights in establishing a remedy. “The courts ought to be more reluctant to grant relief when the plaintiff seeks to compel the defendant to construct integrated housing...then when the plaintiff is attempting to build integrated housing on his own land and merely seeks to enjoin the defendant from interfering with that construction.”⁶⁸ Courts are more willing to grant relief when the remedy merely requires the defendant to cease an activity that intrudes upon the plaintiff's private rights.

⁶⁵ *Metro. Hous. Dev. Corp. v. Arlington Heights*, 558 F.2d 1283, 1291 (7th Cir. 1977) (stating “construction of low-cost housing was effectively precluded throughout the municipality or section of the municipality which was rigidly segregated. Thus, the effect of the municipal action in both cases was to foreclose the possibility of ending racial segregation in housing within those municipalities”).

⁶⁶ *Id.* at 1293.

⁶⁷ *Id.* at 1292.

⁶⁸ *Id.* at 1293.

VI. Redlining

As described previously, redlining is the practice of using certain neighborhood characteristics as a basis for declining to lend to a borrower who wishes to purchase a home in that area. An ancillary practice called insurance redlining involves the policy of declining to provide homeowner's insurance or charging higher rates for insurance in the same areas. Both practices can severely limit the ability to purchase a home in certain neighborhoods because the approval of a mortgage application is often contingent upon the ability to obtain insurance on the property. Therefore, the ECOA and the FHA prohibit both practices.

In most redlining cases, the same prima facie requirements of a disparate treatment case are used.⁶⁹ Generally there exists no facially neutral policy when it comes to redlining. The lender is intentionally discriminating by refusing to grant a mortgage to the applicant because of the area in which the residence is located. However, there have been cases where the disparate impact analysis has been allowed.⁷⁰ Its use depends on the factual scenario involved and, in the case of insurance redlining, whether or not state law pre-empts the FHA in this area via the McCarran-Ferguson Act.⁷¹

In *Old West End Association v. Buckeye Federal Savings & Loan*, the Northern District of Ohio found that the plaintiff had established the prima facie requirements for redlining by showing (1) that the house was in a minority neighborhood, (2) an application was submitted and the appraisal indicated a fair sale price, (3) the mortgage

⁶⁹ *Latimore*, 979 F. Supp. at 666-67.

⁷⁰ See *Dehoyos v. Allstate Corp.*, 345 F.3d 290 (5th Cir. 2003); *Owens v. Nationwide Mut. Ins. Co.*, 2005 WL 1837959 (N.D. Tex. 2005).

⁷¹ *Id.*

application was denied, and (4) the plaintiff was qualified for the mortgage.⁷² These requirements, while not widely adopted, are certainly elements worth considering in determining the validity and likely success of a redlining claim.

Redlining cases can be challenging to prove given the difficulty in distinguishing between discrimination with regard to a particular neighborhood and legitimate factors of that neighborhood which may result in the decline of a loan application.⁷³ As stated in *Cartwright v. American Savings & Loan Association*, “The Fair Housing Act’s prohibition against denying a loan based upon the location of the dwelling does not require that a lender disregard its legitimate business interests or make an investment that is not economically sound.”⁷⁴ In this way, the courts give deference to a lender for denying loans to particular areas.

In response to this deference, the plaintiff should offer statistical evidence of the defendant’s lending pattern in the redlined area.⁷⁵ In *Buycks-Roberson v. Citibank Federal Savings Bank*, the plaintiff offered evidence showing that defendant approved fewer loan applications in predominately African-American neighborhoods.⁷⁶ In this class action suit, the court noted that in addition to providing such statistical evidence, the plaintiffs would need to offer individual financial information indicating that they should have been approved for the loan.⁷⁷ “Without such evidence neither the Court nor the jury

⁷² *Old West End Ass'n v. Buckeye Federal S & L*, 675 F. Supp. 1100, 1103 (N.D. Ohio 1987)

⁷³ ALYS COHEN ET. AL., NATIONAL CONSUMER LAW CENTER, CREDIT DISCRIMINATION 156 (5th ed. 2009).

⁷⁴ 880 F.2d 912, 923 (7th Cir. 1989).

⁷⁵ *Id.* at 922.

⁷⁶ 162 F.R.D. 322, 327 (N.D. Ill. 1995).

⁷⁷ *Id.* at 336.

could infer – on the basis of statistics alone – that Citibank engaged in discriminatory redlining.”⁷⁸

VII. Predatory Lending and Reverse Redlining

As described thus far, under the FHA and the ECOA a lender cannot use an applicant’s race, gender, or other protected status characteristic as a reason for denying the application. The courts have also found that the consideration of an applicant’s protected status cannot be used as a reason for approving an application. The practice of approving loan applications for minority homebuyers in a predatory manner is a cause of action under the ECOA.⁷⁹

Predatory lending has been attributed as a major cause of the housing industry collapse. Home loans were targeted toward and approved for subprime borrowers and then sold in complex financial instruments in the securities market. When a large number of these borrowers defaulted on their mortgages, the lending industry seized and that reverberated through the world economy. In Iowa alone, it is estimated that foreclosures resulted in a \$1.2 billion decline in home equity.⁸⁰ As a result, predatory lending has come under increased scrutiny.

Like housing discrimination, predatory lending can also take a variety of forms. The practice of asset-based lending essentially results in the approval of a mortgage, not because of the borrower’s ability to pay, but because of the underlying value of the

⁷⁸ *Id.*

⁷⁹ *Wilson v. Toussie*, 260 F. Supp. 2d 530 (E.D. N.Y. 2003).

⁸⁰ Center for Responsible Lending, *The Cost of Bad Lending in Iowa*, <http://www.responsiblelending.org/mortgage-lending/tools-resources/factsheets/iowa.html> (last updated April 2010).

home.⁸¹ As such, the borrower may eventually default on the home and be forced into foreclosure wherein the mortgage holder takes possession.⁸²

Another type of predatory lending practice is referred to as rent seeking. This occurs when the lender charges the borrower fees and interest rates in excess of the borrower's risk level.⁸³ This in itself would not be so terrible if only the lenders were not acting in a nearly monopolistic fashion, eliminating the ability of borrower's to obtain mortgages elsewhere.⁸⁴

Predatory lending can involve fraud and misrepresentation.⁸⁵ They might also contain binding arbitration agreements, which wholly deprive the borrower of the ability to utilize the federal court system.⁸⁶ Oftentimes a mortgage contract will contain some or all of these predatory loan practices.⁸⁷

These practices, while egregious on their own, are often targeted at society's most vulnerable populations, usually the elderly and minority groups. Predatory lenders seek out those whom lack the information and resources to comparison shop.⁸⁸ They then utilize aggressive marketing tactics and pressure to get borrowers to close on the mortgage.⁸⁹

The mortgage contract itself is usually complex and difficult to understand and is much less straightforward than prime mortgages. "In contrast to prime-mortgage lenders,

⁸¹ Kathleen C. Engel & Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending*, TEX. L. REV. 1255, 1261-65 (2002).

⁸² *Id.*

⁸³ *Id.* at 1265-67.

⁸⁴ *Id.*

⁸⁵ *Id.* at 1267-68.

⁸⁶ *Id.* at 1270.

⁸⁷ *Id.* at 1261.

⁸⁸ *Id.* at 1281-83.

⁸⁹ *Id.* at 1283.

predatory lenders rarely make plain-vanilla, fixed-rate loans with easily understood payment terms. Most predatory loans contain terms that require borrowers to make difficult probabilistic computations about the likelihood and magnitude of future market events that are entirely outside their control.”⁹⁰ Predatory loans are more likely to contain adjustable-rate mortgages that also have prepayment penalties.⁹¹

Current remedies for predatory lending consist of an array of statutory law and common law. The Truth in Lending Act (TILA) is often used in suits against predatory lenders. TILA ensures disclosure of credit terms to consumers and was meant to create an atmosphere in which borrowers are able to make knowledgeable decisions.⁹² While TILA does not attack the substantive and policy related issues of predatory lending, it can allow a plaintiff to recover if the lender violates one of the disclosure provisions.⁹³ However, a disclosure violation is not likely to provide an adequate remedy for a plaintiff and therefore a TILA claim should be brought together with additional claims.⁹⁴

Like TILA, the ECOA can also be used in the predatory lending context because of its disclosure requirements, being applicable in situations where the borrower is approved for a loan in excess of the original amount requested.⁹⁵ The lender would then violate the notification requirements of the ECOA by not sending a denial for the original application.⁹⁶

⁹⁰ *Id.* at 1284.

⁹¹ *Id.* at 1284-85.

⁹² 15 U.S.C.A. § 1601 (West 2010).

⁹³ *Id.*

⁹⁴ ELIZABETH RENUART & ALYS I. COHEN, STOP PREDATORY LENDING: A GUIDE FOR LEGAL ADVOCATES 99 (The National Consumer Law Center ed., 2007).

⁹⁵ RENUART, *supra* note 80, at 69.

⁹⁶ *Id.*

There may also exist remedies under state unfair-and-deceptive-acts and practices (UDAP) statutes. UDAP statutes “usually allow for private damages actions as well as state enforcement.”⁹⁷ Even so, state UDAP statutes are often limited in their scope and are not applicable to credit transactions, exempting predatory lenders from court action.⁹⁸

While formerly one of the weakest in the nation, Iowa’s UDAP law⁹⁹ was recently amended to allow a private right of action against companies that engage in consumer fraud or deceptive practices.¹⁰⁰ Its use in credit transactions related to housing is not entirely clear, but it appears mortgage brokers are subject to the law.¹⁰¹ Also, given the lack of judicial decisions and litigation, its usefulness in the prevention of predatory lending is unknown at this time.

Common law remedies can be used as the basis of claims against predatory lenders. Borrowers may rely upon contract law and assert failures of formation or assent.¹⁰² A civil action for fraud to rescind a contract may pose some practical problems¹⁰³ and may be more difficult to prove than a UDAP violation.¹⁰⁴

The doctrine of unconscionability, as derived from section 2-302 of the Uniform Commercial Code (UCC), is one possible tool, but has been limited by the court and can

⁹⁷ *Id.* at 1303.

⁹⁸ *Id.*

⁹⁹ Iowa Code §714.16 (2010).

¹⁰⁰ Iowa Code § 714H.5 (2010).

¹⁰¹ *Id.* at § 714H.3.

¹⁰² *Id.* at 1299.

¹⁰³ *Id.* at 1302-1303. (stating that Under the “American Rule,” in which each party bears its own attorneys’ fees and costs, suits for injunctive relief such as rescission or loan forgiveness generally do not generate sufficient funds to compensate plaintiffs’ counsel”).

¹⁰⁴ RENUART, *supra* note 80, at 76 (stating that “the consumer often need not prove reliance or intent to deceive under UDAP acts” but reliance would need to be proven in fraud case).

be expensive to litigate.¹⁰⁵ Courts are wary about second-guessing the terms of a contract, especially any terms relating to price, and thus successful lawsuits have “prevailed only with regard to non-price terms in loan contracts.”¹⁰⁶

Predatory lending is intrinsically related to another practice called reverse redlining. Reverse redlining occurs when a lending company intentionally targets protected classes for predatory home loans or refinancing.¹⁰⁷ These cases involve a similar burden shifting approach, but require the plaintiff to show that (1) he is a member of protected class, (2) he applied for and was approved for a loan, (3) the loan’s provisions were “grossly unfavorable”, and (4) the lending institution provided more favorable terms to other similarly qualified applicants.¹⁰⁸ The fourth element can be met as long as the plaintiff can provide evidence that the defendant was specifically targeting minorities, even without a showing of disparate treatment or impact.¹⁰⁹

Conclusion

This paper is intended to provide an overview of the practices and causes of action for lending discrimination to novices of the subject. In order to keep the topic manageable, its complexity is not fully described. Multiple issues arise when determining which avenue to bring a claim, whether through administrative proceeding or judicial action. A private civil action provides a plaintiff with numerous causes of action based upon federal and state law.

¹⁰⁵ *Id.* at 1300-1301.

¹⁰⁶ *Id.* at 1300.

¹⁰⁷ COHEN, *supra* note 18, at 169 (2009).

¹⁰⁸ COHEN, *supra* note 18, at 74 (2009).

¹⁰⁹ *Id.*

Lending discrimination necessarily borrows from the more robust area of law concerning employment discrimination. Thus, practitioners in this area must keep abreast of developments not only in the arena of lending discrimination, but also employment discrimination. As described throughout this analysis, however, litigating lending discrimination cases can prove more difficult because of the difficulty in evaluating and making a showing of discrimination in a less adversarial type of transaction. Because of this inherent difference, the courts are sometimes wary of a dogmatic utilization of the *McDonnell Douglas* burden-shifting analysis.

The law in this area continues to develop as legislators recognize that additional regulation of the lending industry is necessary in the wake of the sub-prime housing collapse. As mentioned, Iowa's UDAP statute was recently amended to allow for a private right of action against mortgage brokers. In addition, Congress is currently discussing financial industry regulation, which could have an enormous impact on the lending industry. Most notably the legislation seeks to consolidate consumer protection initiatives within one oversight agency.

Lending discrimination is a challenging area of law to master. The variety of potential remedies to lending discrimination violations is extensive and evolving. The kinds of lending discrimination vary from practices that extend far too little credit to home buyers who need it to those that provide far too much for people that cannot afford it. The burden-shifting analysis used by the courts is derived from an area of law that is fundamentally distinguishable and its application to lending discrimination is difficult and sometimes unworkable. While the Home Mortgage Disclosure Act provides a plethora of information regarding lending activity, a plaintiff's case is complicated by the

difficulty in supplying testing evidence. Practitioners are faced with a court system that favors the terms of a contract, even if those terms are fundamentally unfair, and defers to the lender's business expertise when one of its policies results in a discriminatory effect. Yet, as daunting as these challenges may seem, they are but pittance to the troubles faced by those who are denied mortgages because of their race or, in the alternative, are faced with the prospect of losing their home as a result of unscrupulous mortgage lenders.

Where to report discrimination

For retail and department stores; mortgage, small loan and consumer finance companies; oil companies; public utilities; state credit unions; government lending programs; or travel and expense credit card companies are involved, contact:

Federal Trade Commission
Consumer Response Center
Washington, DC 20580
1-877-FTC-HELP (1-877-382-4357); TDD: 1-866-653-4261
www.ftc.gov

The FTC generally does not intervene in individual disputes, but the information you provide may indicate a pattern of violations that the Commission would investigate.

For nationally-chartered banks (National or N.A. will be part of the name):

Comptroller of the Currency
Consumer Assistance Group
1301 McKinney Street
Houston, TX 77010-9050
1-800-613-6743
www.helpwithmybank.gov

For state-chartered banks insured by the Federal Deposit Insurance Corporation, but not members of the Federal Reserve System:

Federal Deposit Insurance Corporation
Consumer Response Center
2345 Grand Boulevard
Suite 100
Kansas City, MO 64108
1-877-ASK-FDIC (1-877-275-3342)
www.fdic.gov

For federally-chartered or federally-insured savings and loans:

Office of Thrift Supervision
Consumer Affairs
1700 G Street NW
Washington, DC 20552
1-800-842-6929; TTY: 800-877-8339
www.ots.treas.gov

For federally-chartered credit unions:

National Credit Union Administration
1775 Duke Street
Suite 4206
Alexandria, VA 22314-3437
1-800-755-1030
www.ncua.gov

For state member banks of the Federal Reserve System:

Federal Reserve Consumer Help Center
P.O. Box 1200
Minneapolis, MN 55480
1-888-851-1920; TDD: 877-766-8533
www.federalreserveconsumerhelp.gov

For discrimination complaints against all kinds of creditors:

Department of Justice
Civil Rights Division
Washington, DC 20530
www.usdoj.gov/crt

Still Not Sure Who to Contact?

If you can't figure out which federal agency has responsibility for the financial institution you dealt with, visit www.federalreserveconsumerhelp.gov or call 1-888-851-1920.

For FHA violations:

Office of Fair Housing and Equal Opportunity
US Department of Housing and Urban
Development (HUD), Room 5204
Washington, DC 20410-2000
1-800-424-8590; TDD: 1-800-543-8294
www.hud.gov/fairhousing

Iowa Civil Rights Commission
400 East 14th Street
Des Moines, Iowa 50319
<http://www.state.ia.us/government/crc/index.html>