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BANKING AND FINANCIAL SERVICES AND CONSUMER CLASS ACTIONS UPDATE

No Disparate Impact Liability Under The Fair Housing Act

On November 3, 2014, a federal court ruled that disparate impact claims are not cognizable under the Fair Housing Act ("FHA"). *American Insurance Association v. HUD*, Civ. No. 13-00966 (RJL) (D.D.C. Nov. 3, 2014) ("*AIA*"). Disparate impact claims impose liability for using a facially neutral policy that nevertheless disproportionately affects – or has a "disparate impact" on – a protected class. This ruling is the latest decision in a long brewing debate over the use of disparate impact claims in discrimination cases brought under the FHA and the Equal Credit Opportunity Act ("ECOA"). Disparate impact claims have been the basis of enforcement action by the Consumer Financial Protection Bureau ("CFPB"), the Department of Housing and Urban Development ("HUD"), and other regulators. The *AIA* decision is notable because eleven federal courts of appeals have reached the opposite conclusion and have held that disparate impact claims are cognizable under the FHA.

The Supreme Court has never ruled on this issue, but that is set to change this term as the Court granted certiorari on this question last month. *See Texas Department of Housing and Community Affairs v. The Inclusive Communities Project, Inc.*, No. 13-1371, 2014 WL 4916193 (U.S. Oct. 2, 2014) ("*TDHCA*"). Twice before this issue reached the Court and had been fully briefed, but the cases settled before a decision was issued. *See Magner v. Gallagher*, *132* S. Ct. 548 (2011); *Township of Mount Holly, N.J. v. Mt. Holly Gardens Citizens in Action Inc.*, 133 S. Ct. 2824 (2013).

Background. The *AIA* case involves a HUD rule that permits disparate impact challenges to housing and mortgage lending practices under the FHA. *See* IMPLEMENTATION OF THE FAIR HOUSING ACT'S DISCRIMINATORY EFFECTS STANDARD, 78 Fed. Reg 11,460 (Feb. 15, 2013) (the "Rule"). HUD's position is that the Rule simply formalized, and provided a consistent interpretation of, its longstanding position that facially neutral policies with discriminatory effects violate the FHA.

The *AIA* case was brought by two insurance industry trade groups who raised concerns about the Rule and its potential reach into the insurance space during the rulemaking process. In particular, the Rule identifies "the provision and pricing of homeowner's insurance" as a potential basis for disparate impact liability. After the final Rule was promulgated, those trade groups filed suit challenging HUD's authority to promulgate the Rule and extend disparate impact liability to homeowners insurance.

The Holding. The *AIA* court concluded that HUD exceeded its statutory authority when it promulgated the Rule, concluding that the plain language of the FHA did not allow disparate impact claims. The court recognized that its decision contradicted the eleven Courts of Appeals that have decided this issue, and expressly relied on *Smith v. City of Jackson*, 544 U.S. 228 (2005), which was decided after those circuit-level decisions. *Smith*

clarified that the presence of "effects-based" language in a statute is key in determining the availability of disparate impact liability. The *AIA* court applied the *Smith* analysis and determined that:

- The FHA contains intentional conduct language but no effects-based language that would signal an intent to allow disparate impact claims.
- The statutory language in the FHA is materially identical to language included in the disparate treatment prohibitions contained in Title VII (which prohibits discrimination in employment based on race) and the Age Discrimination in Employment Act ("ADEA"), but the FHA's language is very different from the disparate impact prongs of Title VII and ADEA.
- Congress amended the FHA in 1988 but did not change the relevant language. This is notable because shortly thereafter, in 1990 and 1991, Congress explicitly provided for disparate impact claims in the Americans with Disabilities Act and Title VII by using effects-based language.
- Application of the Rule to insurers, like AIA, would "run afoul" of the McCarran-Ferguson Act, which ensures the primacy of state law with respect to the insurance space. *See* 15 U.S.C. § 1012(b).

Conclusion. The reasoning presented by the *AIA* court offers a preview of the debate the Supreme Court will face when it addresses the outcome of disparate impact claims under the FHA in the *TDHCA* case. The *AIA* case, by applying the *Smith* analysis, represents the first real shift from a long line of precedent that has recognized the availability of disparate impact claims in discrimination cases.

The final resolution of this question may have wide-ranging effects, under the FHA and the ECOA. Federal agencies like the CFPB have heavily relied on the disparate impact theory to assert discrimination claims, most notably in the mortgage and auto lending space, and a decision by the Supreme Court could require a substantial change in agencies' enforcement posture as well as private litigation.

If you have any questions regarding this update, please contact the Sidley lawyer with whom you usually work.

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