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GENERAL

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**Via Electronic Submission**

Anna Maria Farías  
Assistant Secretary for Fair Housing and Equal Opportunity  
Department of Housing and Urban Development  
451 7th Street, NW  
Washington, DC 20410

**Re: Docket No. FR-6111-P-02  
HUD's Implementation of the Fair Housing Act's Disparate Impact  
Standard**

Dear Assistant Secretary Farías:

The 22 undersigned Attorneys General submit comments to the Department of Housing and Urban Development's ("HUD") above-referenced notice of proposed rulemaking ("the Proposed Rule"). We strongly oppose the proposal, which attempts to render disparate impact liability a dead letter under the Fair Housing Act ("FHA"). The proposal is antithetical to ensuring all Americans have equal access to safe and decent housing and the ability to enjoy the American dream by living in the community of their choice.

The Proposed Rule, if adopted, would ignore the Supreme Court's binding interpretation of the FHA, would drastically exceed HUD's authority, would ignore HUD's statutory mandate, and would be arbitrary and capricious in light of its numerous substantive defects. For all of the reasons described below, we urge HUD to rethink these efforts and to not adopt the proposal.

A similar group of Attorneys General submitted a letter on August 20, 2018 responding to HUD's solicitation of comments on whether it should amend the FHA's current disparate impact regulation. The Attorneys General's 2018 letter is attached to, and is part of, this comment. In addition to the reasons discussed in this comment, HUD should not finalize the Proposed Rule because numerous aspects are inconsistent with the statutory and case law analysis discussed in the August 2018 letter.

## **I. Disparate Impact Liability Represents an Important Tool to Combat Housing Discrimination on which States Have Relied and Will Continue To Use.**

Our country has a sordid history of engaging in discrimination related to housing. Such discrimination included explicitly discriminatory restrictive covenants providing for white-only ownership of houses in certain neighborhoods, the refusal of governments to guarantee home loans in neighborhoods with significant non-white populations, and towns that declared that non-white individuals were banned from being within the city limits between dusk and dawn.<sup>1</sup> Congress finally took action in 1968 to address this explicit, *de jure* discrimination through passage of the FHA. However, this legacy could not be wiped away by eliminating only overtly discriminatory housing practices. Courts and government agencies soon began analyzing claims of housing discrimination using the disparate impact theory of liability first developed in the employment context as endorsed by the Supreme Court in *Griggs v. Duke Power Co.*, 401 U.S. 424 (1971).

The Supreme Court in *Texas Department of Housing & Community Affairs v. Inclusive Communities Project, Inc.*, 135 S. Ct. 2507 (2015), provided a strong endorsement of disparate impact liability in the housing context. *Inclusive Communities* squarely held that “[r]ecognition of disparate-impact claims is consistent with the FHA’s central purpose.” *Id.* at 2521. The Court noted disparate impact liability “allow[s] private developers to vindicate the FHA’s objectives and to protect their property rights” and that some practices made unlawful by disparate impact liability “function unfairly to exclude minorities from certain neighborhoods without any sufficient justification.” *Id.* at 2522. Additionally, the Court observed that “[r]ecognition of disparate-impact liability under the FHA also plays a role in uncovering discriminatory intent: It permits plaintiffs to counteract unconscious prejudices and disguised animus that escape easy classification as disparate treatment” and thereby “may prevent segregated housing patterns that might otherwise result from overt and illicit stereotyping.” *Id.* The Court concluded its opinion by emphasizing the continued importance of the FHA’s disparate impact theory of liability in advancing the nation’s efforts to advance justice and equality:

Much progress remains to be made in our Nation’s continuing struggle against racial isolation. In striving to achieve our historic commitment to creating an integrated society, we must remain wary of policies that reduce homeowners to nothing more than their race. But since the passage of the Fair Housing Act in 1968 and against the backdrop of disparate-impact liability in nearly every jurisdiction, many cities have become more diverse. The FHA must play an important part in avoiding the . . . grim prophecy that our 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 Nation toward a more integrated society.

*Id.* at 2525-26 (formatting changed).

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<sup>1</sup> See *Shelley v. Kraemer*, 334 U.S. 1 (1948); *Thompson v. U.S. HUD*, 348 F. Supp. 2d 398, 471-72 (D. Md. 2005); James W. Lowen, *Sundown Towns* (2005).

Enforcement actions under the FHA and similar state laws<sup>2</sup> based on disparate impact theories are a critical component of states' efforts to combat discrimination and ensure greater equality of opportunity in obtaining housing. States have used disparate impact claims to challenge many types of seemingly neutral housing policies that have a discriminatory effect, such as zoning ordinances, occupancy restrictions, no pet policies, and English-only policies.<sup>3</sup> For example, in just the past four years, the State of Washington has brought 16 enforcement actions and filed two amicus briefs involving disparate impact discrimination in violation of the FHA, including issues related to overbroad use of criminal background checks by landlords and the effect of crime-free rental housing ordinance on victims of domestic violence.<sup>4</sup> Additionally, the states' enforcement

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<sup>2</sup> See, e.g., Cal. Gov. Code § 12955.8 (prohibiting housing discrimination “if an act or failure to act . . . has the effect, regardless of intent, of unlawfully discriminating”); D.C. Code § 2-1402.68 (“Any practice which has the effect or consequence of violating any of the provisions of [the District’s fair housing law] shall be deemed to be an unlawful discriminatory practice.”); N.C. Gen. Stat. § 41A-5(a)(2) (prohibiting housing discrimination if a “person’s act or failure to act has the effect, regardless of intent, of discriminating”); Haw. Code R. § 12-46-305(8); *Saville v. Quaker Hill Place*, 531 A.2d 201, 206 (Del. 1987) (“[C]laims of disparate impact against the handicapped may lie in appropriate cases under [Delaware’s fair housing law.]”); *Burbank Apartments Tenant Ass’n v. Kargman*, 48 N.E.3d 394, 408 (Mass. 2016) (disparate impact claims cognizable under Massachusetts’ fair housing law).

<sup>3</sup> See, e.g., *R.I. Comm’n for Human Rights v. Graul*, 120 F. Supp. 3d 110 (D.R.I. 2015) (landlord’s policy of limiting occupancy had disparate impact based on familial status); *Support Ministries for Persons with AIDS, Inc. v. Vill. of Waterford*, 808 F. Supp. 120 (N.D.N.Y. 1992) (city’s interpretation and application of a local zoning ordinance had disparate impact on basis of disability); *Conn. Comm’n on Human Rights & Opportunities (“CHRO”) ex rel. Hurtado*, CHRO No. 8230394 (landlord’s English-only policy had disparate impact based on national origin and ancestry); *CHRO ex rel. Schifini*, CHRO No. 8520090 (landlord’s policy of limiting occupancy had disparate impact based on familial status); *In re-Accusation of the Dep’t of Fair Employment & Hous. v. Merribrook Apartments, James C. Beard, Owner*, FEHC Dec. No. 88-19, 1988 WL 242651, at \*12-13 (Cal. F.E.H.C. Nov. 9, 1988) (facially neutral occupancy limit had adverse disparate impact on prospective renters with children); *McGlawn v. Pa. Human Relations Comm’n*, 891 A.2d 757 (Pa. Commw. Ct. 2006) (lending practices of obtaining predatory and unfair sub-prime mortgage loans had a disparate impact based on race); *Girard Fin. Co. v. Pa. Human Relations Comm’n*, 52 A.3d 523 (Pa. Commw. Ct. 2012) (finance company’s predatory and unfair lending practices and loan terms had a disparate impact based on race); *Detter v. Sharp’s Village Mobile Home Park*, Doc. No. H-7404 (Pennsylvania Human Relations Commission’s order finding a mobile home park’s imposition of a fee on residents in excess of two per unit had a disparate impact based on family status).

<sup>4</sup> See *State v. DSB Invs., LLC*, No. 15-2-26732-9 (King Cty. Super. Ct., Wash. Nov. 2, 2015) (application of tenancy terms and conditions that discriminated on the basis of race); *State v. Pac. Crest, LLC*, No. 16-2-20773-1 (King Cty. Super. Ct., Wash. Aug. 29, 2016) (criminal history screening practices that discriminated on the bases of race or color); *State v. Premier Residential*, No. 16-2-19043-0 (King Cty. Super. Ct., Wash. Aug. 10, 2016) (same); *State v. Coho Real Estate*

efforts against the mortgage lending industry illustrates the critical importance of disparate impact theories to combat housing discrimination.<sup>5</sup> States have also joined city and local governments' efforts to combat lending discrimination through disparate impact liability. As an example, California recently joined the City of Oakland as amicus on appeal in a case against Wells Fargo, alleging the bank harmed the city through a pattern of illegal and discriminatory mortgage lending,

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*Grp.*, LLC, No. 16-2-26931-1 (King Cty. Super. Ct., Wash. Nov. 4, 2016) (same); *State v. Dobler Mgmt. Co.*, No. 16-2-12461-1 (Pierce Cty. Super. Ct., Wash. Nov. 7, 2016) (same); *State v. Weidner Prop. Mgmt.*, LLC, No. 17-2-00821-4 (King Cty. Super. Ct., Wash. Jan. 19, 2017) (same); *State v. KPS Realty, LLC*, No. 17-2-00564-3 (Spokane Cty. Super. Ct., Wash. Feb. 15, 2017) (blanket refusal to accept veterans' housing choice vouchers discriminated on the basis of disability); *State v. Realty Mart Prop. Mgmt, LLC*, No. 17-2-00677-1 (Spokane Cty. Super. Ct., Wash. Feb. 23, 2017) (policy of charging double damage deposit to tenants who pay rent with disability income discriminated on the basis of disability); *Yakima Neighborhood Health Servs. v. City of Yakima*, No. 1:16-cv-03030 (E.D. Wash. Aug. 10, 2017) (adoption of zoning and land use ordinances to limit housing for homeless individuals discriminated against people with disabilities); *State v. TJ Cline, LLC*, No. 17-2-00716-2 (Walla Walla Cty. Super. Ct., Wash. Aug. 30, 2017) (blanket refusal to accept veterans' housing choice vouchers discriminated on the basis of disability); *State v. Domus Urbis, LLC*, No. 17-2-03584-4 (Spokane Cty. Super. Ct., Wash. Sept. 14, 2017) (same); *State v. Rowley Props.*, No. 17-2-27276-1 (King Cty. Super. Ct., Wash. Oct. 19, 2017) (same); *State v. Welcome Home Props., LLC*, No. 17-2-00861-4 (Walla Walla Cty. Super. Ct., Wash. Oct. 25, 2017) (same); *State v. Yelm Creek Apartments, LLC*, No. 17-2-06117-34 (Thurston Cty. Super. Ct., Wash. Nov. 21, 2017) (disability and housing vouchers); *State v. Celski & Assocs., Inc.*, No. 17-2-03255-4 (Benton Cty. Super. Ct., Wash. Jan. 17, 2018) (same); *State v. Country Homes Realty, LLC*, No. 18-2-00336-3 (Spokane Cty. Super. Ct., Wash. Jan. 26, 2018) (same); *Fair Housing Center of Wash. v. Breier-Scheetz Props., LLC*, 743 F. App'x. 116 (9th Cir. 2018) (multi-family property's occupancy standards discriminated against families with children); *Washington v. City of Sunnyside*, No. 19-cv-03174-RMP (E.D. Wash. filed July 30, 2019) (municipal police department's enforcement of its crime-free rental housing ordinance discriminated on the basis of national origin, sex, and familial status).

<sup>5</sup> See *Commonwealth v. H&R Block, Inc.*, Civ. No. 08-2474-BLS1 (Mass. Suffolk Sup. Ct. 2011) (consent order in case where the Massachusetts Attorney General alleged that Option One's discretionary pricing policy caused African-American and Hispanic borrowers to pay, on average, hundreds of dollars more for their loans than similarly-situated white borrowers); *In re Countrywide Home Loans*, Assurance of Discontinuance Pursuant to N.Y. Exec. Law § 63(15) (N.Y. Nov. 22, 2006) (settlement of investigation where the New York Attorney General found statistically significant discriminatory disparities in "discretionary components of pricing, principally [p]ricing [e]xceptions in the retail sector and [b]roker [c]ompensation in the wholesale sector"); *United States v. Countrywide Fin. Corp.*, No. 2:11-cv-10540 (C.D. Cal. 2011) (settlement resolving discriminatory lending lawsuits filed by the Illinois Attorney General and the United States Department of Justice); *United States v. Wells Fargo Bank, NA*, No. 12-cv-1150 (D.D.C. 2012) (same).

heavily impacting minority community members in violation of the FHA and California Fair Employment and Housing Act.<sup>6</sup>

Disparate impact liability provides Attorneys General and state fair housing enforcement agencies a critical tool to combat this form of discrimination where direct proof of overt bias is hidden or impossible to ferret out. The Attorneys General thus share the Supreme Court's observation in *Inclusive Communities* that disparate impact liability "permits plaintiffs to counteract unconscious prejudices and disguised animus that escape easy classification as disparate treatment. In this way disparate-impact liability may prevent segregated housing patterns that might otherwise result from covert and illicit stereotyping." 135 S. Ct. at 2522.

Because of Attorneys General's experience combatting housing discrimination using disparate impact claims, the judiciary and interested entities have come to rely on our views concerning disparate impact liability under the FHA. Indeed, the Supreme Court in *Inclusive Communities* favorably cited an amicus brief submitted by a group of 17 Attorneys General in concluding that "residents and policymakers have come to rely on the availability of disparate-impact claims." *Id.* at 2525. Additionally, Congress directed state and local governments to share responsibility with the federal government to process and investigate administrative complaints made pursuant to the FHA.<sup>7</sup>

Given the Attorneys General's wide-ranging experience with and reliance on disparate impact liability under the FHA, HUD should closely consider our comments. In offering these comments addressing HUD's proposal to weaken protections under the FHA, the Attorneys General are addressing neither whether fair housing protections should be further strengthened nor how our state fair housing laws should be interpreted.

## **II. HUD Proposes a Rule that Radically Differs from the Current Disparate Impact Regulation.**

In order to understand the radical change represented by the Proposed Rule, it is first necessary to review the regulation it would be replacing ("the Current Rule") and the actions HUD has taken since that regulation went into effect.

### *A. The Current Rule and HUD's Consistent Defense of It.*

The Current Rule, issued in 2013, provides for a simple three-step framework for proving FHA disparate impact claims that clearly assigns burdens at each step. At the first step, commonly known as the "prima facie case," the plaintiff "has the burden of proving that a challenged practice caused or predictably will cause a discriminatory effect" on a protected class. 24 C.F.R. § 100.500(c)(1). At the second step, a defendant "has the burden of proving that the challenged practice is necessary to achieve one or more substantial, legitimate, nondiscriminatory interests."

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<sup>6</sup> *City of Oakland v. Wells Fargo Bank, N.A., et al.*, No. 19-15169 (9th Cir. 2019), Dkt. 41.

<sup>7</sup> See 42 U.S.C. § 3610(f); see also *id.* § 3616 (providing for cooperation between HUD and state and local governments); H.R. Rep. No. 100-711, at 35 (1988) (House Committee Report to the Fair Housing Amendments Act of 1988 noting "the valuable role state and local agencies play in the [FHA] enforcement process").

*Id.* § 100.500(c)(2). In the third step, a plaintiff prevails if it proves that interest could be served by a less discriminatory alternative to the challenged practice. *Id.* § 100.500(c)(3). Both the second and third steps “must be supported by evidence and may not be hypothetical or speculative.” *Id.* § 100.500(b)(2). This three-step framework is consistent with the standard that has prevailed for decades under Title VII, including as codified in the Civil Rights Act of 1991. 42 U.S.C. § 2000e-2(k). The Current Rule does not purport to dictate how the three-step framework should be considered by courts for purposes of judging whether a plaintiff has adequately pled a disparate impact claim.

Until it issued the Proposed Rule, HUD had consistently explained that the Current Rule matches the requirements for disparate impact liability under *Inclusive Communities*. HUD has strongly argued in two separate lawsuits from insurance trade associations that, contrary to plaintiffs’ allegations, the Current Rule is consistent with *Inclusive Communities*.

In one of these lawsuits, HUD filed briefs that could not have been clearer about its position: “*Inclusive Communities* is fully consistent with the standard that HUD promulgated.”<sup>8</sup> Specifically, HUD took the position that the Current Rule “is consistent with the causality requirement specified in *Inclusive Communities*” and “[c]onsistent with *Inclusive Communities*, allows [defendants] to maintain policies that are not artificial, arbitrary, and unnecessary barriers.” *AIA* Opening Br. at 35, 39 (capitalization altered). HUD also observed that the Current Rule, “consistent with *Inclusive Communities*, requires identification of a policy or policies causing a disparity.” *AIA* Reply Br. at 16 (capitalization altered). Finally, HUD contended that “[w]hile *Inclusive Communities* elucidated the broad principles governing discriminatory effects liability, it did not mandate any specific articulation of the burden-shifting framework different from that applied to Title VII disparate impact cases.” *Id.* at 24.

In the other lawsuit, HUD under the leadership of Secretary Carson filed a brief that unequivocally argued the Current Rule was consistent with *Inclusive Communities*:

[T]he 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. And the portions of the Court’s opinion cited by Plaintiff—which discuss limitations on the application of disparate impact liability that have long been part of the standard—do not give rise to new causes of action, nor do they conflict with the Rule. *Indeed, nothing in Inclusive Communities casts any doubt on the validity of the Rule.* To the contrary, the Court cited the Current Rule twice in support of its analysis.<sup>9</sup>

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<sup>8</sup> Defs.’ Mem. in Supp. of Mot. for Summ. J., *Am. Ins. Ass’n v. HUD*, No. 13-cv-966 (D.D.C. Aug. 30, 2016), Dkt. 65, at 33 (“*AIA* Opening Br.”); *see also* Defs.’ Reply Mem. in Supp. of Mot. for Summ. J., *Am. Ins. Ass’n v. HUD*, No. 13-cv-966 (D.D.C. Oct. 28, 2016), Dkt. 70, at 16 (“*AIA* Reply Br.”) (“[T]he Rule’s burden-shifting framework is consistent with *Inclusive Communities*.”).

<sup>9</sup> Defs.’ Opp’n to Pl.’s Mot. for Leave to Am. Compl., *Prop. Cas. Insurers Ass’n of Am. v. Carson*, No. 13-cv-8564 (N.D. Ill. Apr. 21, 2017), Dkt. 122, at 9 (“*PCIAA* Opp’n”) (citations omitted) (emphases added); *see also id.* at 10 (“[T]he Court’s opinion in *Inclusive Communities* did not

*B. The Proposed Rule.*

Despite its consistent position that the Current Rule is consistent with *Inclusive Communities*, HUD now proposes to radically alter the simple, three-step framework of the Current Rule and turn it into a complex, four-step framework. Although the Proposed Rule's complexity makes it difficult to summarize or compare to the framework of the Current Rule, it appears to make at least the following changes:

- It amends the first step, the prima facie case, from its prior simple formulation of “a challenged practice [that] caused or predictably will cause a discriminatory effect” to a five-element test with specific requirements on matters including causation and significance. Compare 24 C.F.R. § 100.500(a), with Proposed Rule § 100.500(b)(1)-(5).<sup>10</sup>
- It amends the first step into both a standard that must be alleged by “stat[ing] facts plausibly alleging each of the [five] elements,” and then “prove[n] by the preponderance of the evidence, through evidence that is not remote or speculative.” Proposed Rule § 100.500(b), (d)(1), (d)(2)(ii).<sup>11</sup>
- It adds a new step, after the first step, allowing a defendant at both the pleading and proof stage to “establish that a plaintiff’s allegations do not support a prima facie case” by showing either (1) “its discretion is materially limited” by federal, state, or local law or (2) one of three facts<sup>12</sup> when the plaintiff’s allegations involve “a model used by defendant.” Proposed Rule § 100.500(c)(1)-(2), (d)(2)(i); see also 84 Fed. Reg. at 42,859 (“[I]n a rule 12(b)(6) motion to dismiss, the defendant can make an argument under the paragraph (c).”).

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alter the limitations on the application of disparate impact liability and indeed affirmed the validity of the Rule’s approach.”).

<sup>10</sup> Specifically, the five factors require the plaintiff to allege and prove: (1) the “challenged policy or practice is arbitrary, artificial, and unnecessary to achieve a valid interest or legitimate objective such as practical business, profit, policy consideration, or requirement of law”; (2) “there is a robust causal link . . . that shows the specific practice is the direct cause of the discriminatory effect”; (3) the disparity “has an adverse effect on members of a protected class”; (4) the disparity “is significant”; and (5) “a direct link between the disparate impact and the [plaintiff’s] . . . injury.”

<sup>11</sup> One of the five factors that must be plead, the factor concerning the “arbitrary, artificial, and unnecessary” nature of the practice, does not have to be proven. See Proposed Rule § 100.500(d)(1)(i) (“A plaintiff must prove . . . each of the elements in paragraphs (b)(2) through (5) . . .”).

<sup>12</sup> Specifically, the three facts are: (1) the “material factors that make up the inputs” of the algorithm are not “substitutes or close proxies for protected classes” under the FHA, (2) the algorithmic model is “produced, maintained, or distributed by a recognized third party,” or (3) the algorithmic model has been “validated by an objective and unbiased neutral third party.”

- It amends the Current Rule’s second step (now the third step because of the addition noted above) from imposing on a defendant the “burden of proving that the challenged practice is necessary to achieve one or more substantial, legitimate, nondiscriminatory interests” with evidence that “may not be hypothetical or speculative” to requiring only that a defendant “produc[e] evidence showing that the challenged policy or practice advance a valid interest (or interests)” with no prohibition on the use of hypothetical or speculative evidence. Compare 24 C.F.R. § 100.500(b)(2), (c)(2), with Proposed Rule § 100.500(d)(1)(ii).
- It amends the Current Rule’s third step (now the fourth step) to add two further requirements on a plaintiff’s burden to prove a less discriminatory alternative policy or practice: the plaintiff must prove it would (1) serve the defendant’s identified interest in “an equally effective manner”; and (2) “without imposing materially greater costs on, or creating other material burdens for, the defendant.” Compare 24 C.F.R. § 100.500(b)(3), with Proposed Rule § 100.500(d)(1)(ii), (d)(2)(iii).

### III. The Proposed Rule Is Procedurally Defective.

#### A. *The Proposed Rule Fails to Match Its Stated Premise Because It Does Not Reflect Inclusive Communities.*

The Proposed Rule is built upon the stated foundational premise that it is “intended to bring HUD’s disparate impact rule into closer alignment with the analysis and guidance provided in *Inclusive Communities*.” 84 Fed. Reg. at 42,857. But the Proposed Rule in fact radically deviates from *Inclusive Communities*. If finalized, the Proposed Rule will be legally invalid because it relies on such a faulty premise.<sup>13</sup> See *FEC v. Akins*, 524 U.S. 11, 25 (1998) (“If a reviewing court agrees that the agency misinterpreted the law, it will set aside the agency’s action . . . .”); *SEC v.*

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<sup>13</sup> Even had HUD not made the choice to build upon the premise that it was intended to adhere to *Inclusive Communities*, the Proposed Rule will be legally invalid if finalized because HUD is powerless to alter the results of *Inclusive Communities*. As the Proposed Rule correctly recognizes, the Supreme Court “did not rely on [the Current Rule] for its holding” but “undertook its own analysis of the Fair Housing Act.” 84 Fed. Reg. at 42,855; see also *Inclusive Cmty.*, 135 S. Ct. at 2542 (Alito, J., dissenting) (“The principal respondent and the Solicitor General—but not the Court—have one final argument regarding the text of the FHA. They maintain that even if the FHA does not unequivocally authorize disparate-impact suits, it is at least ambiguous enough to permit HUD to adopt that interpretation.”) (emphasis added). Accordingly, courts will not defer to any interpretation by HUD that deviates from *Inclusive Communities*. See *United States v. Home Concrete & Supply, LLC*, 566 U.S. 478, 487 (2012) (“In our view, [a prior Supreme Court decision] has already interpreted the statute, and there is no longer any different construction that is consistent with [that decision] and available for adoption by the agency.”); see also *de Reyes v. Waples Mobile Home Park L.P.*, 903 F.3d 415, 424 n.4 (4th Cir. 2018) (“[T]he standard announced in *Inclusive Communities* rather than the HUD regulation controls our inquiry.”).

*Chenery Corp.*, 318 U.S. 80, 87 (1943) (“The grounds upon which an administrative [action] must be judged are those upon which the record discloses that its action was based.”).<sup>14</sup>

*I. Inclusive Communities Does Not Support Adding New Limitations on Disparate Impact Liability that Differ from the Current Rule.*

As described in Section I, *Inclusive Communities* provided a strong endorsement of disparate impact liability. The Proposed Rule’s disconnect from its stated central premise is demonstrated by its preface making only one passing reference to the core holding of *Inclusive Communities* recognizing disparate impact liability under the FHA, and never once mentioning the Supreme Court’s strong endorsement of the theory. See 84 Fed. Reg. at 42,855 (“In 2015, . . . the Supreme Court held that disparate impact claims are cognizable under the Fair Housing Act.”). Immediately after this one-sentence recognition, the preface includes four paragraphs cataloguing myriad “necessary limitations” that *Inclusive Communities* purportedly placed on disparate impact liability. *Id.* at 42,855-56.

But *Inclusive Communities* did not place any significant “limitations” that did not already exist in case law. In discussing the standards applicable to an FHA disparate impact claim that ensure that liability is not limitless, the Supreme Court explicitly drew on disparate impact employment discrimination claims under Title VII. See *Inclusive Cmty.*, 135 S. Ct. at 2522 (giving covered entities “leeway to state and explain the valid interest served by their policies . . . analogous to the business necessity standard under Title VII”). The Court heavily relied on *Griggs v. Duke Power Co.*, which is the foundation of Title VII disparate impact proof standards, to articulate the limits of FHA disparate impact. See *id.* (quoting *Griggs*, 401 U.S. at 431). Moreover, the Court observed that “disparate-impact liability *has always been* properly limited in key respects,” *id.* (emphasis added), further evidencing that it was not calling for a departure from its preexisting FHA and Title VII case law.<sup>15</sup> Despite *Inclusive Communities* clearly providing that Title VII was to remain a touchstone in how questions about disparate impact liability under the FHA were to be addressed, HUD does not refer to Title VII in the preface of the Proposed Rule.

Courts that have interpreted *Inclusive Communities* generally agree that *Inclusive Communities* dictates continuing reliance on preexisting FHA and Title VII law in resolving granular questions about disparate impact liability. For example, the Fourth Circuit has held both that “*Inclusive Communities* . . . expressly acknowledged that its FHA burden-shifting framework closely resembles the Title VII framework for disparate-impact claims” and that “pre-*Inclusive Communities* FHA disparate-impact cases are consistent with [*Inclusive Communities*]’ robust

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<sup>14</sup> The Proposed Rule’s stated purpose also includes one other narrow type of change: “to codify HUD’s position that its rule is not intended to infringe upon any State law *for the purpose of regulating the business of insurance.*” 84 Fed. Reg. 42,857 (emphasis added). This purposes is fully achieved by Proposed Rule § 100.500(e). It therefore does not justify any other provision.

<sup>15</sup> In response to Justice Alito’s dissent, the majority suggested that the Eighth Circuit had adopted too broad a theory of liability in one prior case. See *Inclusive Cmty.*, 135 S. Ct. at 2524 (citing *Gallagher v. Magner*, 619 F.3d 823 (8th Cir. 2010)). The Current Rule does not support the Eighth Circuit’s outcome in that case.

causality requirement.” *de Reyes*, 903 F.3d at 426 n.6, 428; *see also Wetzel v. Glen St. Andrew Living Cmty., LLC*, 901 F.3d 856, 863 (7th Cir. 2018) (citing *Inclusive Communities* to support that Title VII and the FHA are “functional equivalents to be given like construction and application”) (internal quotation marks omitted); *Nat’l Fair Hous. Alliance v. Travelers Indem. Co.*, 261 F. Supp. 3d 20, 30 (D.D.C. 2017) (holding preexisting FHA cases remain “sound” pursuant to *Inclusive Communities*’ “robust causality requirement.”).<sup>16</sup>

Most courts squarely addressing the issue have also held that the Current Rule is fully consistent with *Inclusive Communities*. *MHANY Mgmt., Inc. v. Cty. of Nassau*, 819 F.3d 581, 618 (2d Cir. 2016) (“Supreme Court implicitly adopted HUD’s approach”); *Ave. 6E Invs., LLC v. City of Yuma*, 818 F.3d 493, 512-13 (9th Cir. 2016) (describing what the Supreme Court “made clear” in *Inclusive Communities* followed by a “see also” cite to the Rule); *Kargman*, 48 N.E.3d at 411 (“framework laid out by HUD and adopted by the Supreme Court”).<sup>17</sup> In one of the lawsuits against HUD challenging the Current Rule—in which HUD argued there is no inconsistency or conflict between the Current Rule and *Inclusive Communities*—then-District (now-Circuit) Judge Amy St. Eve ruled that “the Supreme Court in *Inclusive Communities* . . . did not identify any aspect of HUD’s burden-shifting approach that required correction.” *Prop. Cas. Insurers Ass’n of Am. v. Carson*, No. 13-cv-8564, 2017 U.S. Dist. LEXIS 94502, at \*29 (N.D. Ill. June 20, 2017). HUD’s explanation of the Proposed Rule does not address any of these cases, even though many of them were cited in the comments of the Attorneys General submitted to HUD in 2018. Given HUD’s prior position that *Inclusive Communities* is consistent with the Current Rule, as well as courts’ similar conclusions, HUD relies on an unfounded premise in seeking to modify the Current Rule’s well-reasoned framework. *See Akins*, 524 U.S. at 25; *Chenery*, 318 U.S. at 87.

In truth, the Proposed Rule is an attempt to avoid post-*Inclusive Communities* precedent in several circuits and contains numerous provisions that are contrary to, among others, the recent decisions cited above by the Second (*MHANY Management*), Fourth (*de Reyes*), and Ninth (*Avenue 6E*) Circuits. HUD has only limited authority to deviate from circuit precedent when ambiguous statutory provisions are at issue. The Proposed Rule goes far beyond that authority and would raise constitutional concerns if followed. *Cf. De Niz Robles v. Lynch*, 803 F.3d 1165, 1171-72 (10th Cir. 2015) (Gorsuch, J.) (cataloguing constitutional problems with deference to agencies overriding the function of courts). HUD should not finalize the Proposed Rule.

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<sup>16</sup> Courts in Title VII cases treat the burden-shifting standards applied to employment discrimination claims to be consistent with the limitations explained in *Inclusive Communities*, which further supports treating the disparate impact standards under the FHA and Title VII as the same after *Inclusive Communities*. *Davis v. Dist. of Columbia*, 925 F.3d 1240, 1251 (D.C. Cir. 2019); *Abril-Rivera v. Johnson*, 806 F.3d 599, 606-07 (1st Cir. 2015).

<sup>17</sup> A divided panel of the Fifth Circuit has disagreed, although seven members of that court dissented from the failure to rehear that case en banc. *Inclusive Cmty. Project v. Lincoln Prop. Co.*, 920 F.3d 890, 903, *reh’g en banc denied*, 930 F.3d 660 (5th Cir. 2019).

2. *Inclusive Communities Does Not Support Adding the Unprecedented Defenses Found in the Proposed Rule.*

Moreover, *Inclusive Communities* cannot be stretched to support many of the radical changes found in the Proposed Rule.<sup>18</sup> Particularly egregious is the unprecedented four-step framework that purports to allow a defendant as part of the pleading stage to “establish that a plaintiff’s allegations do not support a prima facie case” by either showing “that its discretion is materially limited” by federal, state, or local law or one of three facts when the plaintiff’s allegations involve “a model used by defendant.” Proposed Rule § 100.500(c). The preface cites nothing from *Inclusive Communities*—or any other case law or statute—that provides for this new framework. Nor could it. Indeed, “[i]n *Inclusive Communities*, the Supreme Court explained that an FHA disparate-impact claim should be analyzed under a three-step, burden-shifting framework.” *de Reyes*, 903 F.3d at 424.

The proposed “algorithmic defense” has no basis in the text of the FHA and is inconsistent with longstanding judicial application of the disparate impact standard. A prime example of how the new framework is unsupported by any precedent is the new standard of proof for claims of housing discrimination “[w]here a plaintiff alleges that the cause of a discriminatory effect is a model used by the defendant, such as a risk assessment algorithm.”<sup>19</sup> Proposed Rule § 100.500(c)(2). First, the text of the FHA does not indicate that there should be any higher standard of proof for claims of housing discrimination when lenders or housing providers use algorithms or other models to make lending or housing decisions. *See Nationwide Mut. Ins. Co. v Cisneros*, 52 F.3d 1351, 1359 (6th Cir. 1995) (“The purpose of the [FHA] as a whole is to eliminate the discriminatory business practices which might prevent a person economically able to do so from purchasing a house regardless of his race”) (internal citations and quotations omitted). Instead, the lending-specific provision of the FHA assigns liability for parties “engag[ed] in...[t]he making or purchasing of loans or providing other financial assistance.” 42 U.S.C. § 3605. This language was not meant to cover the developer of an algorithm who has taken no part in the use of the algorithm.

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<sup>18</sup> Given the absence of any directive from the Supreme Court to modify the burden-shifting test, several lower courts have interpreted *Inclusive Communities* as, at most, emphasizing the need to robustly evaluate plaintiffs’ existing prima facie burden. As an example, a federal district court has disapprovingly characterized defendants as “strain[ing] to turn the Court’s decision to their advantage, insisting that although it affirmed that such claims are cognizable, [the Supreme Court] established ‘rigorous, pleading-stage requirements’ . . . .” *Cty. of Cook v. Bank of Am. Corp.*, No. 14 C 2280, 2018 U.S. Dist. LEXIS 55138, at \*25 (N.D. Ill. Mar. 30, 2018). The court concluded that the complaint stated a FHA claim under a disparate impact theory because the allegations “articulate both a statistical race-based disparity and a specific, multifaceted policy with a robust causal connection to that disparity” and, importantly here, that “[d]efendants have not shown that *Inclusive Communities* requires more.” *Id.* at \*29.

<sup>19</sup> An “algorithm” should be defined as “any well-defined computational procedure that takes some value, or set of values, as input and produces some value, or set of values as output.” Cormen et al., *Introduction to Algorithms* 5 (3d ed., MIT Press 2009).

Second, the proposed defense deviates from the FHA’s text by incorrectly attempting to tie the standard of proof to the development of the algorithm rather than the use by a lender or housing provider. See *Miller v. Countrywide Bank, N.A.*, 571 F. Supp. 2d 251, 260 (D. Mass. 2008) (where plaintiffs asserted disparate impact claims under the FHA based on bank’s discretionary pricing policy, the court found that the “[bank’s] liability, if any, flows directly from its own participation in the transactions as the ‘creditor’ which set the markup policy at issue”). The text of the FHA, on the other hand, makes clear that liability should be with the party who has primarily “engag[ed] in” the unfair use of the algorithm.

The Proposed Rule’s algorithmic defense further upends the burden-shifting framework employed by the Current Rule, acknowledged by *Inclusive Communities*, and evident throughout the canon of FHA and Title VII case law, by incorrectly allowing lenders, landlords and others plainly covered by the FHA, to shield themselves from liability simply by outsourcing decisions to a “model.” In particular, Proposed Rule § 100.500(c)(2)(ii)-(iii) allows a housing entity to be exempt from liability if the algorithm is produced by a “recognized third party,” or is validated by “an objective and unbiased neutral third party.” As discussed later in Section IV.C.1, there are no “industry standards” or “recognized third parties” for the creation or implementation of algorithms.

Further, the defense puts more emphasis on the input (factors the algorithm computes) rather than the output (result of the algorithm). Proposed Rule § 100.500(c)(2)(i) allows a defendant to evade liability if the algorithmic model does not “rely in any material part on factors that are substitutes or close proxies for protected classes under the [FHA];” however, this prong fails to consider that a proxy can be an interaction of two factors and components. Simply put, having neutral factors does not ensure that the output from the algorithm will be non-discriminatory.<sup>20</sup> See Robert Brauneis & Ellen P. Goodman, *Algorithmic Transparency for the Smart City*, 20 Yale J.L. & Tech. 103, 125 (2018). And while the inputs are important to understanding the tool, in the context of disparate impact claims the output of the algorithm, and the weight that output is given in a user’s decision-making is where liability should be primarily focused. See *Watson v. Fort Worth Bank & Tr.*, 487 U.S. 977, 987 (1988) (“[t]he evidence in these “disparate impact” cases usually focuses on statistical disparities, rather than specific incidents,

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<sup>20</sup> In the employment discrimination context, the Supreme Court long ago made clear that “good intent or absence of discriminatory intent does not redeem employment procedures or testing mechanisms that operate as ‘built-in headwinds’ for minority groups and are unrelated to measuring job capability.” *Griggs*, 401 U.S. at 432; see also *id.* at 436 (“Nothing in [Title VII] precludes the use of testing or measuring procedures; obviously they are useful. What Congress has forbidden is giving these devices and mechanisms controlling force unless they are demonstrably a reasonable measure of job performance.”); *Guardians Ass’n of N.Y.C. Police Dept., Inc. v. Civ. Serv. Comm’n of City of N.Y.*, 630 F.2d 79, 103 (2d Cir. 1980) (“If test scores produce disparate racial results, an employer who wants to use rank-ordering of the scores for hiring decisions faces a substantial task in demonstrating that rank-ordering is sufficiently justified to be used”). Nothing in *Inclusive Communities* authorizes HUD to depart from this longstanding precedent in the housing context.

and on competing explanations for those disparities”). Therefore, in line with FHA practice, liability should be on the entity using the tool in a manner that has a disparate impact, not solely on the developer that has no role in the tool’s use.

HUD should not finalize the Proposed Rule, which purports to reflect Supreme Court precedent, because its unprecedented defenses are entirely inconsistent with case law. Any effort to do so will represent grave legal error.

*B. The Proposed Rule Exceeds HUD’s Authority by Attempting to Alter Judicial Procedures.*

Through the Proposed Rule, HUD inappropriately intrudes on questions of judicial process. The Proposed Rule, unlike the Current Rule, purports to specify how the burden-shifting framework would apply at the pleading stage of a case. It would also allow defendants to have a case dismissed at the pleading stage by making certain affirmative showings even when the complaint alleges all the necessary elements of the claim. HUD lacks authority to make these changes. The latter amendment treads even further into the authority of the judiciary by purporting to create a procedure contrary to the Federal Rules of Civil Procedure and state rules of civil procedure in the many states that provide for motion to dismiss practice modeled on Federal Rule of Civil Procedure 12. These provisions will be ignored by courts even if HUD unlawfully plows forward in finalizing the Proposed Rule.

The Supreme Court has clearly explained that the question of what is required to plead a discrimination claim is distinct from the “evidentiary standard” necessary to prove the claim. *Swierkiewicz v. Sorema N.A.*, 534 U.S. 506, 510-12 (2002) (Title VII). Additionally, it has explained that the prima facie case is an evidentiary standard that does not need to be pled. *Id.*; see also *Ring v. First Interstate Mortg., Inc.*, 984 F.2d 924, 927 (8th Cir. 1993) (FHA), cited with approval in *Swierkiewicz*, 534 U.S. at 512. The Supreme Court has also clearly explained that the question of what is required to plead a discrimination claim is controlled by Federal Rule of Civil Procedure 8(a)(2). *Swierkiewicz*, 534 U.S. at 512-13. Although the Supreme Court can certainly opine on what Rule 8(a)(2) requires either as a general matter or in specific contexts, HUD has no authority to tell courts how to proceed on such questions even in the guise of interpreting *Inclusive Communities*. This is no different than HUD’s lack of authority to issue a regulation attempting to override *Ashcroft v. Iqbal*, 556 U.S. 662 (2009), and *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), for purposes of FHA disparate impact claims—and no court would defer to HUD if it did issue such a regulation. See *Colesanti v. Dickinson*, No. 18-491, 2019 U.S. Dist. LEXIS 145578, at \*14 n.6 (D.R.I. July 19, 2019) (rejecting argument that *Iqbal* and *Twombly* did not apply to a claim based on administrative interpretation). HUD must leave questions of pleading standards to the courts. If it does not, courts will not defer to HUD’s position since it involves a body of law (the Rules of Civil Procedure) for which the agency has no authority to administer. See *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837, 842-44 (1984) (limiting administrative deference to an “agency’s construction of the statute which it administers”).

Even more egregious is HUD’s attempt to create a pleading-stage defense in which a defendant can have the case dismissed if it makes one of several possible evidentiary “show[ings].” Proposed Rule § 100.500(c)(1)-(2); see also 84 Fed. Reg. at 42,859 (“[I]n a rule 12(b)(6) motion

to dismiss, the defendant can make an argument under the paragraph (c).”<sup>21</sup> This squarely contravenes the Federal Rule of Civil Procedure that specifies if a motion to dismiss is sought based on “matters outside the pleadings . . . the motion must be treated as one for summary judgment under Rule 56.” Fed. R. Civ. P. 12(d). It is also inconsistent with the requirements in Rule 12(d) that “[a]ll parties must be given a reasonable opportunity to present all the material that is pertinent to the motion.” HUD has no authority to repeal Rule 12(d) regardless if the case deals with a claim under the FHA.<sup>22</sup> See *Chevron*, 467 U.S. at 842-43 (limiting administrative deference to when a statute is ambiguous).

Similarly, the Proposed Rule advises defendants (including defendants in disparate treatment suits) that “[t]he absence of” certain data “shall not result in any adverse inference against a party.” Proposed Rule § 100.5(d). But interpretation of where and when inferences can be drawn in court are typically matters for the Federal Rules of Evidence, *e.g.*, Fed. R. Evid. 407, 412, 512; or the Federal Rules of Civil Procedure, *e.g.*, Fed. R. Civ. P. 37(e). HUD lacks authority to amend either.

Finally, HUD’s attempt to dictate court procedures raises issues of federalism because the Proposed Rule does not limit its purported reach to questions of pleading or inferences in federal court. FHA disparate impact claims are regularly litigated in state court, *see, e.g., Kargman*, 48 N.E.3d at 398, so the Proposed Rule is apparently attempting to dictate the pleading standards and motion to dismiss procedures of state courts hearing those cases. This is problematic because

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<sup>21</sup> It appears that Proposed Rule § 100.500(c)(3) does nothing more than purport to authorize a defendant to file a standard motion to dismiss under Federal Rule of Civil Procedure 12(b)(6) arguing that the plaintiff has failed to allege necessary facts. Of course, courts do not need HUD’s permission to allow defendants to file 12(b)(6) motions in FHA disparate impact cases; courts regularly dismiss disparate impact claims on such motions today even without HUD providing for it in the Current Rule. *See, e.g., Frederick v. Wells Fargo Home Mortg.*, No. 15-1457, 649 F. App’x 29 (2d Cir. May 18, 2016) (unpublished).

<sup>22</sup> HUD attempts to alter the Rules of Civil Procedure to a degree that appears unprecedented in case law in creating this pleading-stage defense. But even less extreme efforts for federal agency to affect the application of Rules of Civil Procedures have been regularly rejected. *See, e.g., In re Bankers Trust Co.*, 61 F.3d 465, 470 (6th Cir. 1995) (holding a regulation of the Federal Reserve requiring banks to withhold certain documents from discovery “is plainly inconsistent with [Federal] Rule [of Civil Procedure] 34 and cannot be enforced” and further holding that “[t]o allow a federal regulation issued by an agency to effectively override the application of the Federal Rules of Civil Procedure and, in essence, divest a court of jurisdiction over discovery, the enabling statute must be more specific than a general grant of authority”). HUD’s attempt to dictate a procedure contrary to the Rules of Civil Procedure is not supported by decisions that have permitted agency regulations to limit the scope of discoverable materials because government agencies have a legitimate interest in providing regulated entities with “sufficient assurances about the treatment of their proprietary information so they will cooperate in federal programs and supply the government with information vital to its work.” *Food Mktg. Inst. v. Argus Leader Media*, 139 S. Ct. 2356, 2366 (2019). No such interests are relevant in HUD purporting to alter Rule 12.

federal administrative action creates “concern [that] is heightened where the administrative interpretation alters the federal-state framework by permitting federal encroachment upon a traditional state power.” *Solid Waste Agency v. U.S. Army Corp of Eng’rs*, 531 U.S. 159, 173 (2001). The Proposed Rule creates such concern, which HUD apparently overlooks given its statement that “[t]his rule does not have federalism implications.” 84 Fed. Reg. at 42,861.

For all of these reasons, HUD would act unlawfully by finalizing the Proposed Rule.

*C. HUD’s Regulatory Flexibility Act Analysis Fails to Consider the Impact that the Proposed Rule’s Algorithmic Defense Will Have on Small Businesses.*

The Regulatory Flexibility Act (“RFA”) requires that whenever an agency publishes a notice of proposed rulemaking for any proposed rule “the agency shall prepare and make available for public comment an initial regulatory flexibility analysis . . . [which] shall describe the impact of the proposed rule on small entities.” 5 U.S.C. § 603(a). Here, the Agency included an RFA analysis but failed to include the impact the “recognized third party” and “neutral third party” provisions will have on small businesses. 84 Fed. Reg. at 42,861.

First, there are no identifiable “recognized third party,” “neutral third party,” nor “industry standards” in this context. Second, the analysis fails to recognize the likely barrier to entry on small businesses. Because many of the algorithms that could be used in housing and lending are extremely complex, it is likely that small entities source relevant algorithms from big technology companies. Larger technology companies would naturally become the “recognized third part[ies],” due to their ability to invest in the complex development of algorithms. This would lead to a much higher barrier to entry for small businesses to develop their own algorithms, as they would need to become “recognized.” Proposed Rule § 100.500(c)(2)(ii). Further, Proposed Rule § 100.500(c)(2)(iii) would likely require that small businesses incur the cost of validating their algorithms by a “neutral third party.” HUD failed to address the impact of these two third parties on small businesses and the fact that there are currently no applicable “industry standards,” in its RFA Analysis, in violation of the RFA. 5 U.S.C. § 603(a).

**IV. HUD’s Proposed Rule Is Substantively Flawed.**

The Proposed Rule creates a needlessly complicated four-step framework. This complexity, in and of itself, is a significant substantive flaw because it will create substantial difficulty for regulated parties, government investigators, parties to litigation, or factfinders to follow. HUD should not finalize the Proposed Rule on that basis alone. But each of the individual components are substantively flawed in their own right, providing even more reason why HUD would err to finalize the Proposed Rule.

*A. The Proposed Rule Creates Uncertainty and Costs by Jettisoning a Workable, Established Framework for an Unprecedented Alternative.*

The Current Rule draws from decades of established FHA and Title VII disparate impact case law and provides courts, housing providers, lenders, individuals, and other interested stakeholders a predictable, but flexible, burden-shifting test to assess whether housing policies or practices are discriminatory. Cases decided after *Inclusive Communities* illustrate how the Current Rule’s burden-shifting test provides a balanced and familiar framework for courts to identify discriminatory barriers to housing while protecting defendants from unmeritorious challenges that

threaten their legitimate business or governmental interests. The Proposed Rule would upend this status quo and result in costly uncertainty, including for state housing-related agencies that are regulated by the FHA.

Courts applying and following *Inclusive Communities* have used the Current Rule’s burden-shifting test to dismiss unmeritorious claims quickly and to permit meritorious claims to proceed, while giving both sides meaningful opportunities to present their positions. This burden-shifting test allows courts to sift through disparate impact claims to make sure that only those practices that result in artificial, arbitrary, and unnecessary barriers warrant liability. The Current Rule strikes a careful balance between varying interests: It imposes a threshold burden on the plaintiff to demonstrate a disparate impact caused by the defendant’s challenged practice or policy, provides the defendant a meaningful opportunity to demonstrate a legitimate business interest that the challenged policy or practice advances, and then in turn permits the plaintiff to identify another, less discriminatory means for the defendant to advance that interest.

Several post-*Inclusive Communities* cases illustrate how the Current Rule’s balanced approach protects against discriminatory housing practices while also providing safeguards against unmeritorious challenges to legitimate practices.

*Inclusive Communities* itself is one such example. On remand from the Supreme Court, the district court found no disparate impact. Relying on the Supreme Court’s holding in *Inclusive Communities*, as well as prior cases, the district court concluded that the plaintiff “failed to point to a specific, facially neutral policy that purportedly caused a racially disparate impact.” *Inclusive Cmty. Project, Inc. v. Tex. Dep’t of Hous. & Cmty. Affairs*, No. 08-cv-546, 2016 U.S. Dist. LEXIS 114562, at \*20 (N.D. Tex. Aug. 26, 2016). The district court found that “[b]y relying simply on [defendant’s] exercise of discretion in awarding tax credits, [plaintiff] has not isolated and identified the specific practice that caused the disparity in the location of low-income housing. *Id.*

In *Boykin v. Fenty*, plaintiffs challenged the closure of two homeless shelters, alleging a disparate impact based on disability. 650 F. App’x. 42, 43 (D.C. Cir. 2016) (unpublished). The D.C. Circuit affirmed the district court’s dismissal of plaintiffs’ disparate impact claim, finding that the complaint “failed to allege facts suggesting that the closure affected a greater proportion of disabled individuals than non-disabled, as it did not, for instance, include an allegation that disabled homeless individuals are more likely to rely on low-barrier shelters than non-disabled homeless individuals.” *Id.* at 44. *Inclusive Communities* and *Boykin* reflect how the Current Rule’s burden-shifting test permits courts to quickly dismiss unmeritorious claims.

Other courts, employing the same flexible burden-shifting test, have concluded that plaintiffs demonstrated a disparate impact caused by the challenged policy or practice. In *MHANY Management*, the Second Circuit affirmed the district court’s holding that the plaintiffs showed a disparate impact by demonstrating that a zoning decision to limit multiple-family housing “perpetuates segregation generally because it decreases the availability of housing to minorities . . . .” 819 F.3d at 620 (internal quotation marks omitted). The Second Circuit also affirmed the district court’s holding that the defendant proffered legitimate governmental interests, including the need not to increase traffic or put strain on public schools. The Second Circuit then remanded the case to the district court to consider—in line with the Current Rule—whether the plaintiffs had provided a less discriminatory alternative that achieves the same legitimate government interests.

On remand, the district court concluded that the plaintiffs provided sufficient evidence demonstrating that an alternate zoning plan would neither increase traffic nor put a strain on schools. *MHANY Mgmt., Inc. v. Cty. of Nassau*, No. 05-cv-2301, 2017 U.S. Dist. LEXIS 153214, at \*26-37 (E.D.N.Y. Sept. 19, 2017). Accordingly, *MHANY Management* demonstrates that the burden-shifting test provides both sides with a meaningful opportunity to present evidence for their competing positions.

Similarly, in *Avenue 6E*, the district court on remand from the Ninth Circuit considered whether plaintiff housing developers met their prima facie burden of showing that the denial of their rezoning application to create high-density housing had a disparate impact against Latinxs. Plaintiffs' expert submitted evidence that "compare[d] the percentages of Hispanics and whites who were qualified home buyers in the identified price ranges in the Yuma market." 217 F. Supp. 3d 1040, 1049 (D. Ariz. 2017). The district court concluded "that Plaintiffs' evidence is sufficient to show a prima facie case of disparate impact." *Id.* at 1050. The court explained that plaintiffs "provided statistical evidence—based on a pool of qualified home purchasers within the relevant market area and during the relevant time frame—regarding the racial makeup of those priced out of the market as a result of the price increase associated with the City of Yuma's denial of Plaintiffs' rezoning application." *Id.* The court then examined the city's proffered bases for its denial of plaintiffs' rezoning application and concluded that both were "legally sufficient." *Id.* at 1056. However, the court then evaluated evidence demonstrating that those proffered governmental interests were pretextual, in part because approving the zoning application would not interfere with those interests. *Id.* at 1056-57.

In short, these post-*Inclusive Communities* cases demonstrate that the Current Rule's burden-shifting test provides courts with both guidance and flexibility to quickly dismiss uncertain disparate impact cases while allowing meritorious cases to proceed. By abandoning the Current Rule, HUD will unnecessarily introduce uncertainty into decades of established legal precedent and undermine the purpose of the FHA to root out and eliminate discrimination in housing. The Proposed Rule will increase costs in several ways to plaintiffs, defendants, private and public entities alike. These added costs on both sides are troubling to the Attorneys General, as we have a unique perspective of representing both prospective plaintiffs and prospective defendants in FHA actions.

First, the stricter pleading requirements will increase costs to litigants. The requirements for a disparate impact claim under the Current Rule and *Inclusive Communities* already make it difficult for plaintiffs to allege disparate impact claims, let alone prove them on the merits.<sup>23</sup> The

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<sup>23</sup> Stacy E. Seicshnaydre, *Is Disparate Impact Having Any Impact? An Appellate Analysis of Forty Years of Disparate Impact Claims Under the Fair Housing Act*, 63 Am. U. L. Rev. 357 (2013); Lorren Patterson, *The Impact of Disparate Impact: The Benefits Outweigh the Costs of Recognizing Disparate Impact Claims Under the Fair Housing Act*, 8 Geo. J. L. & Mod. Critical Race Persp. 211 (2016). Importantly, plaintiffs already face an uphill battle to plead and prove disparate impact claims, even prior to the 2013 final rule and *Inclusive Communities*. According to one analysis of 40 years of disparate impact litigation, as of December 2013, (1) plaintiffs secured favorable decisions in only 20% of the disparate impact claims considered on appeal; (2) defendants had 83.8% of their favorable trial court disparate impact rulings affirmed on appeal

new pleading burden that the Proposed Rule purports to impose would raise this bar even higher. That in turn will result in an increased dismissal of meritorious claims at the pleading stage, long before discovery can commence. Plaintiffs will therefore bear the costs of having to perform extensive pre-litigation investigation without the benefit of formal discovery. Assuming that this pre-litigation discovery is even attainable, it may create additional workloads for other entities, including state governments. For example, when a private sector lender, bank, or insurer is the prospective defendant, a plaintiff may need to look to state regulatory agencies to secure pre-litigation information from the private sector entity through administrative procedures, thereby increasing costs to the public.

Additionally, the Proposed Rule adds undefined, ambiguous phrases to the regulation<sup>24</sup> that will likely create needless litigation on defining their meaning. The ambiguity of these phrases may also make such actions more difficult to resolve by settlement, where the litigants may have a fundamental, irreconcilable legal dispute over the meaning of these terms. This will likely increase costs and burdens to all potential litigants and decrease potential litigants' and liability insurers' ability to analyze the risks and costs of litigating. These ambiguities will likely result in inconsistent results in different courts, contravening HUD's sensible goal in drafting the Current Rule to "provide nationwide consistency in the application of [disparate impact] liability." 78 Fed. Reg. at 11,460.

*B. The Proposed Rule Seeks to Impose Overly Onerous Burdens on Victims of Housing Discrimination, Including for Claims the Supreme Court Specifically Endorsed.*

*Inclusive Communities* highlighted certain categories of disparate impact claims as particularly meritorious: those targeting "zoning laws and other housing restrictions that function unfairly to exclude minorities from certain neighborhoods without any sufficient justification"; those "allow[ing] private developers . . . [to] stop[] municipalities from enforcing arbitrary and, in practice, discriminatory ordinances barring the construction of certain types of housing units"; and those "permit[ting] plaintiffs to counteract unconscious prejudices and disguised animus that escape easy classification as disparate treatment." 135 S. Ct. at 2522. But Proposed Rule § 100.500(b) seeks to establish prima facie burdens so high that it would make it practically impossible for meritorious claims endorsed by the Supreme Court to proceed. Such a result is contrary to the text and purpose of the FHA as well as HUD's statutory duty to affirmatively further fair housing. 42 U.S.C. § 3608(e)(5).

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while plaintiffs received affirmance on appeal of only 33.3% of their favorable trial court rulings; and (3) plaintiffs successfully reversed on appeal only four adverse summary judgment rulings in the 40-year period studied. Seicshnaydre, *supra*, at 362, 391-403. Adding more stringent requirements for pleading and proving a disparate impact claim, and affording defendants new complete defenses to such claims, will only heighten this imbalance.

<sup>24</sup> For example, the Proposed Rule does not define "significant" or "direct link." Proposed Rule § 100.500(b)(4)-(5). Similarly, while the Proposed Rule appears to borrow the phrase "robust causal link" from *Inclusive Communities*, it does not define that term. *Id.* § 100.500(b)(2)

*1. Proposed Rule § 100.500(b)(1) Wrongly Imposes a “Magic Words” Requirement on Plaintiffs and Wrongly Creates a List of Regulated Entities’ Valid Interests.*

The Proposed Rule specifies that a challenged policy or practice must be “arbitrary, artificial, and unnecessary to achieve a valid interest or legitimate objective” of a regulated entity to satisfy the prima facie case. Proposed Rule § 100.500(b)(1). It purports to “require a plaintiff to *plead* that the challenged policy or practice is arbitrary, artificial and unnecessary to achieve” the interest or objective. 84 Fed. Reg. at 42,858 (emphases altered). The Proposed Rule also specifies that such an interest or objective includes a “practical business, profit, policy consideration, or requirement of law.” Proposed Rule § 100.500(b)(1).

Putting aside the fact already discussed that HUD has no power to dictate court pleading requirements,<sup>25</sup> the Proposed Rule can be read to require plaintiffs to formalistically include the words “arbitrary,” “artificial,” and “unnecessary,” in their complaints or face dismissal. HUD provides no reason such formalistic pleading should be required. Although *Inclusive Communities* used that phrase in describing the attributes of a valid disparate impact claim, it did not suggest that that phrase must appear in a plaintiff’s complaint. To the contrary, that language in *Inclusive Communities* was quoted directly from *Griggs*. See 135 S. Ct. at 2522 (“Disparate-impact liability mandates the ‘removal of artificial, arbitrary, and unnecessary barriers,’ not the displacement of valid governmental policies.”) (quoting *Griggs*, 401 U.S. at 431); see also *id.* at 2524 (cautioning against proof standards that “displace valid governmental and private priorities, rather than solely ‘remov[ing] . . . artificial, arbitrary, and unnecessary barriers’”) (alterations in original). The only logical conclusion that can be drawn from that quotation is that the Supreme Court expected the burden-shifting and pleading regime that has been developed for Title VII disparate impact claims after *Griggs* would also be used for FHA disparate impact claims. HUD should not finalize a rule that includes any magic word pleading requirements that deviate from the Title VII framework.

Additionally, HUD errs by creating a list of regulated entities’ valid interests in Proposed Rule § 100.500(b)(1). As HUD correctly observed in finalizing the Current Rule, the FHA “covers many different types of entities and practices, and a determination of what qualifies as a substantial, legitimate, nondiscriminatory interest for a given entity is fact-specific and must be determined on a case-by-case basis.” 78 Fed. Reg. at 11,471. As a result, HUD made the decision in 2013 to “not provide examples of interests that would always qualify as substantial, legitimate, nondiscriminatory interests for every respondent or defendant in any context.” *Id.* This was a sensible, well-reasoned decision at that time, and it is still true today. HUD should not finalize a rule that recognizes interests of regulated entities that are automatically deemed valid or legitimate.

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<sup>25</sup> HUD’s attempt to usurp the role of courts in setting pleading standards is highlighted by HUD’s lengthy three-sentence discourse about what would constitute “a plausible allegation” in various contexts. 84 Fed. Reg. at 42,858. HUD has no statutory authority to interpret the meaning of the plausibility standard that the Supreme Court has laid out in *Iqbal* and *Twombly*.

2. *Proposed Rule § 100.500(b)(2)-(4) Wrongly Creates Confusing and Fundamentally Flawed Requirements for the Use of Statistical Evidence.*

Three different subsections of the Proposed Rule address the required causal link between a challenged practice or policy and the disparity at issue. Among other things, these subsections require a plaintiff to demonstrate that the challenged practice or policy is “the direct cause of the discriminatory effect” and that a “disparity caused by the policy or practice is significant.” Proposed Rule § 100.500(b)(2), (4). Although not explicitly stated in the text of the subsections, they are largely focused on statistical evidence. 84 Fed. Reg. at 42,858-59.

These three subsections are extremely problematic because of their confusing overlap and lack of precision. As an example of the confusing overlap, Proposed Rule § 100.500(b)(2) requires a “disparate impact on members of a protected class” while Proposed Rule § 100.500(b)(3) requires “an adverse effect on members of a protected class.” Those appear to be substantively identical requirements, yet the existence of two separate requirements suggests that they are intended to do independent work. As an example of the confusing lack of precision, it is unclear from the text of Proposed Rule § 100.500(b)(2) whether a plaintiff must demonstrate both a “robust causal link” and “direct cause,” or whether a showing of “direct cause” conclusively establishes the “robust causal link.”<sup>26</sup> Similarly confusing: although the text of Proposed Rule § 100.500(b)(4) requires a disparity to be “significant,” the explanation of that subsection states that the disparity needs to be “material.” 84 Fed. Reg. at 42,858-59. Regulated parties, government investigators, parties to litigation, and factfinders will find the requirements of these three subsections impossible to follow without greater clarity.

These subsections also pose problems by purporting to require pleading about statistical significance before a plaintiff has access to data through discovery. Even if HUD had the authority to impose a pleading standard, the standard proposed here would be inappropriate prior to discovery. As the Eleventh Circuit held after *Inclusive Communities* in evaluating a complaint filed under the FHA, “[i]n a discrimination case, before discovery has unearthed relevant facts and evidence, it may be difficult to define the precise formulation of the required prima facie case in a particular case.” *Hunt v. Aimco Props., L.P.*, 814 F.3d 1213, 1221 (11th Cir. 2016) (alteration and internal quotation marks omitted); see also *Swierkiewicz*, 534 U.S. at 512 (“Before discovery has unearthed relevant facts and evidence, it may be difficult to define the precise formulation of the required prima facie case in a particular case.”); *Woods v. City of Greensboro*, 855 F.3d 639, 652 (4th Cir. 2017) (“[C]ivil rights cases are more likely to suffer from information-asymmetry, pre-discovery.”) Although the Home Mortgage Disclosure Act (“HMDA”), 12 U.S.C. § 2803(b)(4), sometimes provides sufficient data to plead discrimination in mortgage lending cases, some of the requirements purportedly imposed by Proposed Rule § 100.500(b)(2)-(4) may not be possible to meet even with HMDA data.<sup>27</sup> At the very least, HUD needs to consider this issue and should

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<sup>26</sup> HUD’s explanation of this subsection furthers the confusion because it never mentions “direct cause” even though that term is part of the proposed text. 84 Fed. Reg. at 42,858.

<sup>27</sup> For example, it is difficult to tell whether the HMDA-based statistical disparities that case law holds are sufficient at the pleading stage would satisfy the requirements of Proposed Rule

adjust the requirements of these subsections to reflect what is actually possible to know at the pleading stage if it continues to purport to impose a pleading requirement.

But even if the drafting errors could be fixed and HUD eliminated the provisions purporting to dictate pleading requirements, Proposed Rule § 100.500(b)(2)-(4) is fundamentally flawed because it ignores the substantial body of case law that has been developed on the statistics necessary to prove a prima facie case in a FHA disparate impact case, including after *Inclusive Communities*. The recent decision of the Fourth Circuit in *de Reyes v. Waples Mobile Home Park L.P.* does a comprehensive job canvassing case law on the issue and explaining what constitutes a statistical disparity satisfying the prima facie case after *Inclusive Communities*. See 903 F.3d at 426-28. By failing to engage with the preexisting case law in explaining these subsections, HUD has made it impossible to understand the practical import of these subsections or to allow others to apply them. For example, HUD explains that under Proposed Rule § 100.500(b)(2), “[c]laims relying on statistical disparities must . . . provid[e] an appropriate comparison that shows that the policy is the actual cause of the disparity” but provides no further detail. 84 Fed. Reg. at 42,858. It is unclear from that statement whether HUD is simply seeking to reflect established case law on proving discriminatory disparities,<sup>28</sup> or seeking to establish unprecedented requirements of an indefinite nature.

In finalizing the Current Rule, HUD explicitly declined to include a statistical significance standard or otherwise opine on necessary statistical showings to prove a prima facie case because “[g]iven the numerous and varied practices and wide variety of private and governmental entities covered by the [FHA], it would be impossible to specify in the rule the showing that would be required to demonstrate a discriminatory effect in each of these contexts.” 78 Fed. Reg. at 11,468. This conclusion was correct then, and nothing in *Inclusive Communities* alters it,<sup>29</sup> so HUD should

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§ 100.500(b)(2)-(4). See, e.g., *City of Memphis v. Wells Fargo Bank, N.A.*, No. 09-2857, 2011 U.S. Dist. LEXIS 48522, at \*49-51 (W.D. Tenn. May 4, 2011).

<sup>28</sup> See, e.g., *Tsombanidis v. W. Haven Fire Dep’t*, 352 F.3d 565, 575 (2d Cir. 2003) (“The basis for a successful disparate impact claim involves a comparison between two groups—those affected and those unaffected by the facially neutral policy. This comparison must reveal that although neutral, the policy in question imposes a ‘significantly adverse or disproportionate impact’ on a protected group of individuals.”), *superseded on other grounds as recognized by MHANY Mgmt.*, 819 F.3d at 619. Among the principles that would apply based on case law is that “[t]here is no requirement . . . that a statistical showing of disproportionate impact must always be based on analysis of the characteristics of actual applicants.” *Dothard v. Rawlinson*, 433 U.S. 321, 330 (1977) (Title VII).

<sup>29</sup> *Inclusive Communities* stated that FHA disparate impact claims must satisfy a “robust causality requirement,” which means “a disparate-impact claim that relies on a statistical disparity must fail if the plaintiff cannot point to a defendant’s policy or policies causing that disparity.” 135 S. Ct. at 2523. The Current Rule is consistent with that requirement by specifying a plaintiff must prove that “a challenged practice caused or predictably will cause a discriminatory effect.” 24 C.F.R. § 100.500(c)(1). Moreover, the Current Rule recognizes that the plaintiff “on a case-by-case basis”

not include Proposed Rule § 100.500(b)(2)-(5) in any final rule. But, even if HUD determines that it is now necessary to address the question, it should do so in a way that explicitly adheres to the longstanding case law.

3. *Proposed Rule § 100.500(b)(5) Wrongly Imports Proximate Causation into the Prima Facie Case and Imposes an Inappropriate Standard.*

Notwithstanding the supposed basis of seeking to reflect *Inclusive Communities* and to articulate what is required to satisfy the prima facie burden for disparate impact discrimination, HUD turns to a wholly separate legal issue in Proposed Rule § 100.500(b)(5) by purporting to impose a proximate cause requirement as part of the disparate impact prima facie burden. HUD explains this is an attempt “to codify the proximate cause requirement under the Fair Housing Act that there be ‘some direct relationship between the injury asserted and the injurious conduct alleged’” as articulated by the Supreme Court in *Bank of America Corp. v. City of Miami*. 84 Fed. Reg. at 42,859 (quoting 137 S. Ct. 1296, 1306 (2017)).

Proximate causation is a wholly separate legal concept from the prima facie case in a disparate impact case. Although the Supreme Court held that proximate causation is a required element of a FHA claim in the context of a case alleging disparate impact discrimination, the case did not address the prima facie case or any issues related to pleading or proving disparate impact claims. Indeed, subsequent to *City of Miami*, the Eleventh Circuit has confirmed the separate nature of these concepts by treating the failure to prove “proximate cause” and to prove “a prima facie case of disparate impact” as “independent reasons” to dismiss a disparate impact case under the FHA. *Oviedo Town Ctr. II, LLLP v. City of Oviedo*, 759 F. App’x 828, 833 (11th Cir. 2018) (unpublished). By importing the proximate cause requirement into the disparate impact prima facie case, the Proposed Rule would unnecessarily add confusion.

Additionally, even if it were appropriate to import proximate causation into the prima facie case, the Proposed Rule incorrectly codifies it. Notwithstanding the statement in the preface of merely “seek[ing] to codify” *City of Miami*, the actual text of Proposed Rule § 100.500(b)(5) uses the phrase “direct link” that appears nowhere in the Supreme Court’s opinion.<sup>30</sup> As previously discussed, HUD has no authority to finalize a rule that deviates from the Supreme Court’s holding.

4. *Proposed Rule § 100.500(b) Wrongly Limits the Type of Policies and Practices Subject to Disparate Impact Liability.*

In addition to the errors and concerns described above related to the Proposed Rule’s five steps to plead and prove a prima facie case, the Proposed Rule also seeks to add other erroneous requirements to the prima facie case. HUD states that “a single event—such as a local government’s zoning decision” will “likely not meet the standard” laid out in the Proposed Rule

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will need to “identify[] the specific practice that caused the alleged discriminatory effect.” 78 Fed. Reg. at 11,469.

<sup>30</sup> Similarly, HUD explains that Proposed Rule § 100.500(b)(5) requires a plaintiff to show that the policy at issue “directly caused” the injury, but that phrase appears nowhere in *City of Miami*. 84 Fed. Reg. at 42,859.

§ 100.500(b) that a challenge must be linked to a “specific, identifiable policy or practice.” 84 Fed. Reg. at 42,858. But the Second Circuit has squarely held that this is an inaccurate understanding of the law after *Inclusive Communities*. Instead, that court was “confident” that the case before it, in which the plaintiff “complain[ed] about a [rezoning] decision affecting one piece of property,” “falls well within a classification of a ‘general policy’” susceptible to a disparate impact challenge. *MHANY Mgmt.*, 819 F.3d at 619. Indeed, HUD’s newfound hostility toward disparate impact challenges of zoning decisions violates the Supreme Court’s declaration that challenges to “zoning laws . . . reside at the heartland of disparate-impact liability.” *Inclusive Cmty.*, 135 S. Ct. at 2521-22. Moreover, as the Second Circuit has explained, “the distinction between a single isolated decision and a practice [is] analytically unmanageable—almost any repeated course of conduct can be traced back to a single decision.” *MHANY Mgmt.*, 819 F.3d at 619 (internal quotation marks omitted). HUD should not finalize any regulation that purports to try to draw such distinctions in a rule-based manner.<sup>31</sup>

HUD also appears to intend that the “specific, identifiable” requirement means that “[i]t is insufficient to identify a program as a whole,” rather, a plaintiff must identify “a particular element of the program” that creates a disparate impact. 84 Fed. Reg. at 42,858.<sup>32</sup> However, this is inconsistent with HUD’s prior position, relying on a Title VII statutory provision and on case law related to reverse mortgage redlining claims under the FHA, that there are situations in which it “may be appropriate to challenge the decision-making process as a whole” because “the elements of a decision-making process [are] not . . . capable of separation for analysis.” 78 Fed. Reg. at 11,469 (citing 42 U.S.C. § 2000e-2(k)(1)(B)(i); *Hargraves v. Capital City Mortg. Corp.*, 140 F. Supp. 2d 7, 20-22 (D.D.C. 2000)). It is particularly inappropriate to require such specificity as part of a purported pleading requirement, as plaintiffs are unlikely to have access to the granular elements of challenged practices and policies prior to discovery. *Cf. id.* at 11,474 (noting in finalizing the Current Rule that it is fair to require plaintiffs to prove a less discriminatory alternative

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<sup>31</sup> HUD implicitly recognizes the difficulties in drawing such distinctions by qualifying its statement about challenges to “a single event.” HUD specifies that a single event can be the basis of a disparate impact challenge if “the plaintiff can show that the single decision is the equivalent of a policy or practice.” 84 Fed. Reg. at 42,858. But HUD then qualifies that qualification by stating such a showing will occur only “[i]n unusual cases.” *Id.* Such difficulties exemplify why HUD should refrain from attempting to regulate this issue in any final rule.

<sup>32</sup> The sentence articulating this requirement is confusing, and read in isolation suggests that HUD believes that *only* challenges to “programs as a whole” should succeed and *not* challenges to particular elements of a program. *See* 84 Fed. Reg. at 42,858 (“It is insufficient to identify a program as a whole without explaining how the program itself causes the disparate impact as opposed to a particular element of the program.”) But such a reading does not appear to reflect HUD’s intent because it is at odds with the preceding and following sentence. *See id.* (“HUD notes that since *Inclusive Communities* many parties have failed to identify a ‘specific, identifiable practice.’ . . . Plaintiffs must identify the particular policy or practice that causes the disparate impact.”).

because of their ability to use discovery to obtain relevant facts). HUD should eliminate the need to identify specific elements of a policy or practice from any final regulation.

*C. The Proposed Rule Seeks to Provide Unwarranted Defenses that Short Circuit Meritorious Discrimination Claims and Impose Excessive Costs.*

The Proposed Rule creates three separate defenses that purport to shift the burden of proof at the pleading, almost completely, onto the plaintiff. All of these defenses unfairly skew the plausibility of a disparate impact claim in defendants' favor, greatly increasing the difficulty of proving even meritorious claims. HUD would violate its statutory duty to affirmatively further fair housing by finalizing a rule with such defenses. 42 U.S.C. § 3608(e)(5).

*1. The Proposed Rule Creates an Unprecedented Defense for Algorithmic Models that Fails to Reflect the "Complicated Nature" of the Relevant Issues.*

All three components of the algorithmic defense under the Proposed Rule are vague, misunderstand the development and operation of algorithms,<sup>33</sup> reference entities and standards that do not yet exist, and skew so heavily in defendants' favor that it would prevent disparate impact claims from being fairly litigated. Within this defense lies at least three ways in which a defendant can defeat a claim of disparate impact: (1) if the defendant is able to prove that the "material factors that make up the inputs" of the algorithm are not "substitutes or close proxies for protected classes" under the FHA,<sup>34</sup> (2) if the defendant can show that the algorithmic model is "produced, maintained, or distributed by a recognized third party"; or (3) if the defendant can show that the algorithmic model has been "validated by an objective and unbiased neutral third party." Proposed Rule § 100.500(c)(2)(i)-(iii).

With regard to the first requirement, having neutral input factors does not mean an algorithm is nondiscriminatory. This concern is especially valid here where the term "proxy" is not defined, and where these requirements could authorize algorithms that rely on the interaction between two factors or components that appear neutral on their face but are an indicator of race when taken

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<sup>33</sup> The definition of an "algorithmic model" must include how data mining "automates the process of discovering useful patterns, revealing regularities upon which subsequent decision making can rely. The accumulated set of discovered relationships is commonly called a 'model.'" Solon Barocas & Andrew D. Selbst, *Big Data's Disparate Impact*, 104 Calif. L. Rev. 671, 677 (2016).

<sup>34</sup> The interaction between factors in an algorithm must be included by HUD when defining "material part." Further, HUD should consider that there are instances when excluding race and race proxies can actually hurt protected classes. See Sandra G. Mayson, *Bias In, Bias Out*, 128 Yale L.J. 2218, 2263 (2019) (explaining that if an algorithm treated arrest rates equally as a predictor of risk for black and white men, it would fail to account for real, prejudice-based differences in the likelihood of arrests between the two groups, "perpetuat[ing] the historical inequality by overestimating the black man's relative riskiness and underestimating the relative riskiness of the white man"). Moreover, simply eliminating the variable would have a cost in accuracy which can fall disproportionately on protected classes. *Id* at 2265.

together.<sup>35</sup> For example, two separate factors, such as an individual’s favorite restaurant alongside another factor such as an individual’s favorite workout class, when taken together could be more of an indicator of race than the sole factor of zip code or than the two factors on their own. Further, the term “predictive of credit risk or other similar valid objective,” can be read to indicate that if an entity can use the algorithm to measure profitability, that is enough to evade liability at the pleading stage. Proposed Rule § 100.500(c)(2)(i).

The second and third prongs of the proposed defense, reference standards and industries that simply do not yet exist. First, there is currently no “recognized third party,” nor are there any “industry standards” in this context. Proposed Rule § 100.500(c)(2)(ii). Only a tiny number of public entities appear to do work in this area;<sup>36</sup> however, it is not clear that such work is accurate, let alone applicable in this context.

Further, the requirement that the model be “validated by an objective and unbiased neutral third party” that finds the model “statistically sound,” also references an entity that does not yet exist. Proposed Rule § 100.500(c)(2)(iii). And merely because a model is “statistically sound” does not ensure that it is not discriminatory. Even when an algorithm is statistically sound, it can still be discriminatory. *See Barocas & Selbst, supra*, 104 Cal. L. Rev. at 680 (an algorithm which is itself statistically sound may nonetheless cause a discriminatory impact if, for example, the data on which it is trained is biased). It is also unclear when the validation of the algorithm would occur, particularly whether it would be before or after initial use by the user of the algorithm. The timing is critical because the validation may not catch changes in input, if validated before use.

Also, there are currently no “industry standards” to implement in this context and to develop such standards will require more academic scholarship. Many in academia fear that neither faculty nor their students can conduct relevant research due to the Access Provision of the Computer Fraud and Abuse Act (“CFAA”), 18 U.S.C. § 1030(a)(2)(C). *See Sandvig v. Sessions*, 315 F. Supp. 3d 1, 14 (D.D.C. 2018) (researchers planning to engage in audit testing of internet real estate, hiring, or other websites through the use of bots and fictitious user profiles, and then to make their findings public had standing to bring action alleging that prosecuting them for violating the Access

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<sup>35</sup> The term “proxy” is itself ambiguous; while some define it as a perfect replacement for another variable in a model such that it has no independent predictive value, others define it more modestly as a variable that is correlated with another. Mayson, *supra*, 128 Yale L.J. at 2232. This distinction is a critical one in determining what counts as a “proxy” variable—under the first definition, very few variables would serve as a “proxy” for race, whereas under the second, many more would qualify. This distinction as well as a definition of a “proxy,” in this context, must be included by HUD in any definition of “material part.”

<sup>36</sup> *E.g.* National Institutes of Standards and Technology, Face Recognition Vendor Test (FRVT) Ongoing, <https://www.nist.gov/programs-projects/face-recognition-vendor-test-frvt-ongoing>; *see* National Institutes of Standards and Technology, Cryptographic Algorithm Validation Program, <https://csrc.nist.gov/projects/cryptographic-algorithm-validation-program/validation>; *see also* Governor Lael Brainard, What are we Learning about Artificial Intelligence in Financial Services? (Nov. 13, 2018), at <https://www.federalreserve.gov/newsevents/speech/brainard20181017a.htm>.

Provision of the CFAA would violate their First and Fifth Amendment rights); *see also Sandvig v. Barr*, 2019 WL 2526495 (D.D.C. 2019) (pending cross-motions for summary judgment).

The problems with the defenses in Proposed Rule § 100.500(c)(2) become all the greater if HUD actually were able to make them applicable to the pleading stage of the case as it purports to do. Although it is legally unable to do this for the reasons explained in Section III.B, in cases where an algorithm is at issue, it is unlikely that a plaintiff will have access to any aspects of defendant’s algorithm, unless a defendant disclosed that information beforehand. *See DeHoyos v. Allstate Corp.*, 240 F.R.D. 269, 305 (W.D. Tex. 2007) (settlement where plaintiffs claimed insurance company’s predictive credit algorithm was discriminatory, court stated that “Allstate had never voluntarily disclosed its credit scoring algorithms prior to this settlement. Thus, there was presumably no avenue for independent observers to verify” Allstate’s actions regarding the algorithm); *see also Houston Fed’n. of Teachers, Loc. 2415 v. Houston Indep. Sch. Dist.*, 251 F. Supp. 3d 1168, 1178 (S.D. Tex. 2017) (court granted summary judgement on procedural due process claim in favor of teacher’s union where school district used employee-performance based algorithm, and stated “Of greater concern is the house-of-cards fragility of the [algorithm], where the wrong score of a single teacher could alter the scores of every other teacher in the district. This interconnectivity means that the accuracy of one score hinges upon the accuracy of all . . . without access to data supporting all teacher scores, any teacher facing discharge for a low value-added score will necessarily be unable to verify that her own score is error-free”). Under this framework, a plaintiff’s ability to refute any claims about defendant’s algorithm is close to nil. Therefore, the Proposed Rule’s algorithmic defense would be simply unfair if actually applicable at the pleading stage.

Additionally, the defenses that the Proposed Rule would create based on defendants’ use of algorithmic models will introduce new costs and burdens. Purely from a litigation perspective, the introduction of these new defenses adds “additional layers to the burden-shifting analysis” in disparate impact cases.<sup>37</sup> HUD acknowledged the “complicated nature” of algorithmic model defenses. 84 Fed. Reg. at 42,860. Litigating whether a defendant qualifies for the new defenses would increase the costs of litigation to all parties as well as decrease the ability of potential litigants and liability insurers to analyze the downside risk and likely costs of litigating. That is particularly true given that Proposed Rule § 100.500(c)(2) does not define such terms as “industry standards,” “recognized third party,” or “statistical sound[ness].” *See, e.g., Kriston Capps, How HUD Could Dismantle a Pillar of Civil Rights Law*, Citylab (Aug. 16, 2019), <https://www.citylab.com/equity/2019/08/fair-housing-act-hud-disparate-impact-discrimination-lenders/595972/>.

The algorithmic models defenses will have broader costs as well. The Proposed Rule affords a complete defense to disparate impact claims where a defendant uses a model that a third party

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<sup>37</sup> Austin Holland, Heather Howell Wright, Christopher K. Friedman, *HUD Proposed Rule Demands More Disparate and More Impact to Establish Disparate Impact Liability*, Financial Services Perspectives (Aug. 12, 2019), <https://www.financialservicesperspectives.com/2019/08/hud-proposed-rule-demands-more-disparate-and-more-impact-to-establish-disparate-impact-liability/>.

produces or maintains. Proposed Rule § 100.500(c)(2)(ii). Allowing defendants a path to avoid liability based merely on the use of third-party algorithmic models will therefore incentivize housing providers to outsource the development and maintenance of such models. Such companies will in turn have an incentive to pass the costs of doing so on to consumers.

Shielding companies from liability merely because of their reliance on third-party algorithmic models will also disincentivize those companies from developing in-house algorithmic expertise, scrutinizing the potential discriminatory impact algorithmic models supplied by third-party vendors, and seeking improvements to these models when defective. Capps, *supra*. At the same time, third-party vendors' interest in securing repeat business from such companies will give them little incentive either to ensure their models are free from discriminatory impact or to give candid advice to their customers about such impacts when they occur. *Id.* The end result may well be that a wide array of discriminatory practices facilitated by faulty algorithmic models will escape liability.

Moreover, housing providers and their third-party vendors would be incentivized to use trade secret arguments to shield outsourced algorithmic models from scrutiny. *Id.* Development of broader knowledge about how such models impact those most vulnerable to housing discrimination would suffer if information about the structure of, and potential flaws in, these models were so shielded. Previously unforeseeable discriminatory impacts made possible by continually evolving algorithmic models may go unaddressed if the mere use of such models, by itself, creates a shield against liability. Extensive literature has explained that algorithmic models can have their own discriminatory results based on biases within the information on which they are built.<sup>38</sup>

All of these effects would result in a loss of transparency and consumer confidence in the lending, banking, and insurance industries. HUD's own announcement seems to recognize uncertainty and concern about affording defendants a defense based on the use of algorithmic models. Even while proposing to establish these defenses, HUD has solicited comments on "the nature, propriety, and use of algorithmic models as related to [these] defenses" in the first place. 84 Fed. Reg. at 42,860. Common sense would dictate that HUD resolve such serious questions before proposing to add algorithmic model-based defenses into law.

## 2. *The Proposed Rule Disregards the Supremacy of Federal Civil Rights Laws.*

The defense created by Proposed Rule § 100.500(c)(1) for "discretion [that] is materially limited by a third party" erroneously denies the express supremacy of federal civil rights laws. The defense as written would apply whenever a housing provider's discretion is limited by state or local law. Proposed Rule § 100.500(c)(1)(i). Accordingly, the defense purports to excuse a defendant's discriminatory conduct that is in violation of federal law—the FHA—simply because

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<sup>38</sup> See, e.g., Barocas & Selbst, *supra*; Andrew D. Selbst, *A New HUD Rule Would Effectively Encourage Discrimination by Algorithm*, Slate (Aug. 9, 2019), <https://slate.com/technology/2019/08/hud-disparate-impact-discrimination-algorithm.html>; Daniel Greene et al., *Better, Nicer, Clearer, Fairer: A Critical Assessment of the Movement for Ethical Artificial Intelligence and Machine Learning*, Proceedings of the 52nd Hawaii International Conference on System Sciences (2019), <https://hdl.handle.net/10125/59651>.

a state or local law tends to permits it. Such an attempt effectively to create reverse preemption, whereby state and local law supersede federal law, is directly contrary to the FHA's strong preemption provision that "any law of a State, a political subdivision, or other such jurisdiction that purports to require or permit any action that would be a discriminatory housing practice under this title shall to that extent be invalid." 42 U.S.C. § 3615.

Proposed Rule § 100.500(c)(1) applies to a broad range of defendants so it cannot be justified by the McCarran-Ferguson Act that only applies to the "business of insurance." 15 U.S.C. § 1012(b). Indeed, HUD has previously taken the position that it would not recognize a defense to disparate impact based on conflicts with state law, except when required by the McCarran-Ferguson Act, because that "would seem to stand the Supremacy Clause on its head." 81 Fed. Reg. 69,018. HUD cannot promulgate a final regulation with such a defense.<sup>39</sup>

3. *The Proposed Rule Incorrectly Imports Standards that Congress Rejected for the Final Two Stages of the Burden Shifting Framework.*

Most of the changes that the Proposed Rule makes to the final two stages of the burden shifting framework reflect HUD's decision to import the Supreme Court's abrogated holdings from *Wards Cove Packing Co. v. Antonio*, 490 U.S. 642 (1989), in Proposed Rule § 100.500(d). See 84 Fed. Reg. at 42,860 n.55. Both the requirement in the Proposed Rule that a defendant merely has a burden of production concerning a valid interest and the specification that a plaintiff must prove a less discriminatory alternative that would satisfy that interest in an "equally effective" manner come directly from *Wards Cove*. 490 U.S. at 659, 661. But the burden-shifting standards established by *Wards Cove* were quickly rejected by Congress in the Civil Rights Act of 1991. See 42 U.S.C. § 2000e-2(k).

In finalizing the Current Rule, HUD thoroughly explained why it rejected including various provisions from *Wards Cove*. See 78 Fed. Reg. at 11,472-74. HUD specifically rejected placing on the defendant only a burden of production, but not persuasion, about a valid interest because it is consistent with the allocation of the burden of proof in settled FHA case law and with the standard under Title VII and the Equal Credit Opportunity Act. *Id.* at 11,474. HUD also rejected the "equally effective" requirement and stated it was especially inappropriate "in the housing context [versus] in the employment area in light of the wider range and variety of practices covered by the [FHA] that are not readily quantifiable." *Id.* at 11,473; see also *MHANY Mgmt.*, 2017 U.S. Dist. LEXIS 153214, at \*23 ("HUD's interpretation could not be clearer that a plaintiff's burden under 24 C.F.R. § 100.500(c)(3) is not to show that the less discriminatory practice would be equally effective, but merely that it must serve a defendant's legitimate interests."). HUD was sued specifically about its decision to reject incorporating *Wards Cove* into the Current Rule, and

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<sup>39</sup> HUD purports to qualify this defense by declaring it inapplicable when "a State actor or municipality is the defendant." 84 Fed. Reg. at 42,859. Assuming that HUD can create defenses that apply to only certain types of defendants, this limitation would not bring the defense into compliance with 42 U.S.C. § 3615. A state or local law that authorizes a violation of the FHA is preempted, and cannot be the basis for defending housing discrimination, regardless of who is the defendant or whether litigation against some other defendant might provide for redress.

Judge St. Eve found it to have been a lawful decision. *Prop. Cas. Insurers Ass'n of Am. v. Donovan*, 66 F. Supp. 3d 1018, 1051-53 (N.D. Ill. 2014).<sup>40</sup>

Nothing in *Inclusive Communities* now renders it more appropriate to import the *Wards Cove* abrogated holdings into the FHA. Although *Inclusive Communities* includes one favorable citation to *Wards Cove*, it is to a portion of *Wards Cove* that was not abrogated by the Civil Rights Act of 1991. *See* 135 S. Ct. at 2523 (citing 490 U.S. at 653). Indeed, a federal district court has squarely rejected an argument that *Inclusive Communities* imposed stricter standards for the final step of the burden-shifting test. In that case, the defendant argued that plaintiffs must affirmatively demonstrate that the less discriminatory alternative they proffer is “equally effective” as the existing challenged practice or policy. *MHANY Mgmt.*, 2017 U.S. Dist. LEXIS 153214, at \*20. But, the court noted, *Inclusive Communities* used language consistent with the Current Rule’s rejection of such a heightened standard. *Id.* at \*25 (citing 135 S. Ct. at 2518). Consistent with that interpretation, Judge St. Eve determined that *Inclusive Communities* did not allow relitigation of her prior rejection of the challenge to HUD’s refusal to incorporate *Wards Cove*. *Prop. Cas. Insurers Ass'n v. Carson*, 2017 U.S. Dist. LEXIS 94502, at \*26-27. Given HUD’s unequivocal and well-reasoned position and the absence of any directive in *Inclusive Communities*, HUD’s proposal to lessen the burden for defendants when the burden shifts to them and to require plaintiffs prove an equally effective alternative is unreasonable and should be abandoned.

*D. The Proposed Rule Adds Several Unnecessary and Unwise Provisions Applying Beyond Disparate Impact.*

*1. The Proposed Rule Wrongly Discourages Data Collection.*

Proposed Rule § 100.5(d) provides that “[n]othing in” HUD’s Fair Housing regulations “requires or encourages the collection of data” relevant to characteristics protected by the FHA and that “[t]he absence of any such collection efforts shall not result in any adverse inference against a party.” This provision would apply to any FHA claim, not just limited to disparate impact claims. This effective discouragement of data collection will have a grave effect on disparate impact litigation, as requests by a plaintiff for data from defendant could be rendered defunct if a defendant has not tracked critical data. Particularly in the housing context, data can be germane to the determination of disparate impact. *See Inclusive Cmty.*, 135 S Ct. at 2525 (“it is also true that race may be considered in certain circumstances and in a proper fashion”); *see also Mt. Holly Gardens Citizens in Action, Inc. v. Twp. of Mount Holly*, 658 F.3d 375, 382 (3d Cir. 2011) (“Typically, ‘a disparate impact is demonstrated by statistics’”) (internal quotation marks omitted).

*2. The Proposed Rule Unnecessarily Confuses Questions of Vicarious Liability.*

Additionally, the Proposed Rule would amend the regulatory provision addressing vicarious liability for all types of FHA cases. In 2016, HUD added a provision specifying that a “person is vicariously liable for a discriminatory housing practice by the person’s agent or

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<sup>40</sup> As noted earlier, this comment does not address whether the Current Rule should be stronger. California has recognized a need to strengthen disparate impact protections by requiring defendants to bear the burden of showing that less discriminatory alternatives are not available. Cal. Code. Regs. tit. 2, § 12062 (effective Jan. 1, 2020).

employee, regardless of whether the person knew or should have known of the conduct that resulted in a discriminatory housing practice, consistent with agency law.” 24 C.F.R. § 100.7(b). HUD explained that reference to “agency law” was consistent with the Supreme Court’s ruling in *Meyer v. Holley*, 537 U.S. 280 (2003) which held that the common law’s “traditional vicarious liability rules” govern such liability under the FHA. *Id.* at 282; *see* 81 Fed. Reg. at 63,072. The preface went on to observe that “[u]nder agency principles, a principal is vicariously liable for the actions of his or her agents taken within the scope of their relationship or employment, or for actions taken outside the scope of their relationship or employment when the agent is aided in the commission of such acts by the existence of the agency relationship.” 81 Fed. Reg. at 63,072; *see also id.* n.41 (citing cases).

Proposed Rule § 100.7(b) acknowledges that principals “may be held vicariously liable” when their agents or employees engage in discrimination without any language in the text of the amended regulation itself purporting to limit vicarious liability to such situations. HUD explains that the revised language is intended to ensure the regulation is “consistent with” *Meyer*. 84 Fed. Reg. at 42,857. However, HUD also states that under the Proposed Rule, “there *must* be a principal-agent relationship under common law for there to be vicarious liability on the part of a person for a discriminatory housing policy or practice by that person’s agent or employee.” *Id.* (emphasis added). To the extent that this mandatory language is purporting to prevent plaintiffs from relying on any other applicable common law vicarious liability rules, it is contrary to *Meyer* because the Supreme Court did not impose such a limitation. HUD should not amend the vicarious liability provision as *Meyer* will apply regardless of HUD’s regulations and any amendment will create unnecessary confusion on whether its 2016 explanation of vicarious liability principles still applies.

*E. The Proposed Rule Wrongly Attempts to Immunize the Lending and Insurance Industries from Liability.*

Discrimination in the home lending and homeowners’ insurance industries during the course of the last three decades is well documented. During the boom of the subprime market in the early-to-mid 2000s, discretionary pricing systems allowed both the intentional and unconscious bias of individual loan officers and brokers to operate unchecked.<sup>41</sup> As a result, African-American and other minority borrowers were more likely to receive subprime loans, pay higher rates, and incur more charges than white borrowers—even after controlling for income and neighborhood characteristics.<sup>42</sup> Even today, borrowers of color are substantially more likely than white

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<sup>41</sup> *See, e.g.,* Robert G. Schwemm & Jeffrey L. Taren, *Discretionary Pricing, Mortgage Discrimination, and the Fair Housing Act*, 45 Harv. C.R.-C.L. L. Rev 375, 385-402 (2010).

<sup>42</sup> *See, e.g.,* Justin P. Steil, *Innovative Responses to Foreclosures: Paths to Neighborhood Stability and Housing Opportunity*, 1 Colum. J. Race & L. 63, 80-83 (2011); Debbie Gruenstein Bocian et al., *Lost Ground, 2011: Disparities in Mortgage Lending and Foreclosure* 8, 11 (Nov. 2011), <https://www.responsiblelending.org/mortgage-lending/research-analysis/Lost-Ground-2011.pdf>.

borrowers to be denied conventional loans.<sup>43</sup> HUD has noted a substantial history of discrimination in the insurance industry that “beg[an] with insurers overtly relying on race to deny insurance to minorities and evolve[ed] into more covert forms of discrimination.” 81 Fed. Reg. at 69,014.

Addressing this pervasive discrimination in mortgage lending and homeowners’ insurance is a challenge, given that lending is a complex multistep process involving numerous decision-makers making discretionary judgments. *See, e.g., Schwemm & Taren, supra*, at 395-98. Discretion at various steps obscures the factors that defendants use to make decisions. And because the final lending decision is the cumulative result of multiple actors’ judgments at multiple steps, it is difficult, if not impossible, to isolate where the taint of discriminatory motive infects the decisional chain. Moreover, the victims of lending discrimination typically are unaware of the discrimination because they are generally unable to compare themselves to similarly situated counterparts.<sup>44</sup> Accordingly, the nature of the lending process makes disparate impact liability an essential tool to address and prevent discrimination.

The lending and insurance industries have been longtime opponents of disparate impact liability under the FHA. HUD has previously observed that the homeowners’ insurance “industry’s concern that [disparate impact] liability makes it ‘near impossible for an insurer to successfully defend himself’” goes back for decades. 81 Fed. Reg. at 69,015 (quoting *Fair Housing Act: Hearings before the Subcom. on Civil and Constitutional Rights of the H. Comm. on the Judiciary*, 95th Cong. 20, 616 (1978) (statement of the Am. Ins. Ass’n)). The Supreme Court in *Inclusive Communities* received amicus briefs from dozens of lending and insurance trade organizations arguing that the FHA did not allow for disparate impact lawsuits.<sup>45</sup> During the rulemaking process that led to the Current Rule, HUD received comments from the “insurance and lending industries” that “requested ‘safe harbors’ or exemptions” from liability. 78 Fed. Reg. at 11,477. Obviously, those efforts failed.

Both the lending and insurance industries trotted out their previously unsuccessful arguments yet again in response to HUD’s 2018 solicitation of comments on whether amendments are appropriate to the Current Rule. *See* 84 Fed. Reg. at 42,856 (acknowledging receiving requests from the two industries, among others, seeking exemptions). They have also employed lobbyists to approach HUD on the issue. *See, e.g.,* Lobbying Report of Williams and Jensen, PLLC., <http://disclosures.house.gov/ld/ldxmlrelease/2019/Q1/301035525.xml> (reporting on lobbying of

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<sup>43</sup> *See* Aaron Glantz & Emmanuel Martinez, *For People of Color, Banks Are Shutting the Door to Homeownership*, Reveal (Feb. 15, 2018), <https://www.revealnews.org/article/for-people-of-color-banks-are-shutting-the-door-to-homeownership/>.

<sup>44</sup> And because federal law prohibits false statements on mortgage applications, “testers” cannot submit hypothetical applications to probe for discriminatory intent in the mortgage context as they can in the rental context. *Schwemm & Taren, supra*, at 386.

<sup>45</sup> *See* Br. of *Amici Curiae* the Am. Bankers Ass’n et al. in Support of Petitioners; Br. for the Am. Fin. Servs. Ass’n et al. as *Amici Curiae* in Support of Petitioners; Br. for the Am. Ins. Ass’n et al. as *Amici Curiae* Supporting Petitioners.

HUD during the first quarter of 2019 related to “HUD Disparate Impact” on behalf of the Property Casualty Insurers Association of America). This time their efforts have succeeded because several provisions of the Proposed Rule seem specially designed to immunize those industries from disparate impact liability.

The provision that provides the most obvious benefit to the lending and insurance industry is the model defense contained in Proposed Rule § 100.500(c)(2). Indeed, although nowhere acknowledged by HUD, several aspects of this defense seem drafted with specific current industry practices in mind. For example, the reference in Proposed Rule § 100.500(c)(2)(ii) to a “model [that] is produced, maintained, or distributed by a recognized third party that determines industry standards,” is tailor made to fit well known systems used in lending underwriting like Fannie Mae’s Desktop Underwriting, Freddie Mac’s Loan Prospector, and the credit scoring products developed by FICO. Creating loopholes designed for specific products is troubling. But more problematic, HUD, without any further analysis, suggests that when Proposed Rule § 100.500(c)(2)(ii) applies, “the proper party responsible for the challenged conduct is not the defendant, but the party who establishes the industry standard” because “suing the party that is actually responsible for the creation and design of the model would remove the disparate impact from the industry as a whole.” 84 Fed. Reg. at 42,859. But in the context of the FHA’s lending-specific provision that covers only parties “engag[ed] in . . . [t]he making or purchasing of loans or providing other financial assistance,” coverage might not extend to at least some such “actually responsible” parties. 42 U.S.C. § 3605. For example, it seems uncertain that a company responsible for designing credit score models but not directly engaged in making or purchasing loans would face any potential liability under that provision. Such an example raises the question whether HUD (or lending industry representatives that advised HUD) wrote this provision knowing that in practice it would mean that nobody can be held liable even when the plaintiff can prove there is a less discriminatory underwriting risk model that satisfies a lender’s legitimate interests.

More generally, Proposed Rule § 100.500(c)(2) appears to provide a loophole for the lending and insurance industries because many processes related to lending and insurance, especially related to underwriting and pricing, could be potentially understood as the products of models.<sup>46</sup> As explained above, the Proposed Rule tries to create a nearly impossible burden for plaintiffs trying to rebut the algorithmic model defense. Accordingly, Proposed Rule § 100.500(c)(2) effectively seeks to create categorical exemptions for categories of practices in the lending and insurance industry notwithstanding HUD’s cogent prior explanations in 2013 and 2016 why categorical exemptions from disparate impact liability are undesirable. Indeed, the Attorneys General agree with HUD’s 2016 assessment that such “categorical exemptions would undermine the Act’s broad remedial purpose and contravene HUD’s own statutory obligation to affirmatively further fair housing.” 81 Fed. Reg. at 69,014; *see* 42 U.S.C. § 3608(e)(5). We also agree with HUD’s consistent assessment from at least 1994 up until now that “discriminatory

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<sup>46</sup> The undefined nature of many terms in the defense created by Proposed Rule § 100.500(c)(2) makes it difficult to know how large a portion of lending and insurance industry practices would come within its scope. However, there are some lending and insurance practices that clearly would *not* be protected by this defense, such as marketing in both industries, servicing and foreclosure-related activities by lenders, or claims adjusting by insurers.

effects liability has proven workable in other contexts involving risk-based decisions, such as mortgage lending, without the need for exemptions or safe harbors.” 81 Fed. Reg. at 69,014-15 & n.40.

Further, Proposed Rule § 100.120(b)(1), which amends the list of generally applicable examples of prohibited lending discrimination that is not limited to disparate impact liability, would purport to allow lenders to engage in certain types of intentional discrimination. By adding a “material” qualifier to the current prohibition on “providing information which is inaccurate or different from that provided others, because of” a protected characteristic, a lender could admit to intentionally giving a borrower inaccurate information because she was African-American or Jewish or a woman yet face no liability unless the victim could prove the information was “material.” Additionally, by creating an absolute safe harbor for when a lender “provid[es] accurate responses to requests for information,” the amendment would allow a lender to intentionally discourage a borrower on the basis of a protected characteristic by, for example, choosing to respond to questions by only Hispanic or disabled or childless borrowers with information about nominally applicable, but frequently waived, minimum requirements or fees. Although HUD claims this amendment reflects *Inclusive Communities*, 84 Fed. Reg. at 42,857, nothing in it excused or even touched on instances of intentional discrimination. HUD should not amend the FHA regulation to start permitting intentional discrimination, even if it deems such discrimination *de minimis*. Such an amendment would be contrary to the text of the FHA that prohibits statements “indicat[ing] any preference, limitation, or discrimination” based on a protected class. 42 U.S.C. § 3604(c) (emphasis added); *see also Nealey v. Univ. Health Servs.*, 114 F. Supp. 2d 1358, 1372 (S.D. Ga. 2000) (rejecting “the notion of a ‘safe harbor’ for *de minimis* international discrimination” under Title VII).

Although the immunity that the Proposed Rule tries to provide to the lending industry is troubling in its own right, it becomes even more dangerous when considered in the context of the Trump Administration’s overall antipathy toward ensuring equal access to housing credit. Just this week, the period for comments closed on the Consumer Financial Protection Bureau’s (“CFPB”) proposals to water down the efficacy of HMDA, a statute that provides lending data so that the public and state enforcement agencies can ensure fair lending in their communities. 84 Fed. Reg. 37,804 (Aug. 2, 2019); 84 Fed. Reg. 20,972 (May 13, 2019). CFPB proposed to substantially cut the number of covered institutions as well as the data they must report, which would render HMDA far less effective.<sup>47</sup> Moreover, the CFPB last year floated the idea of eliminating the Equal Credit Opportunity Act’s prohibition on disparate impact discrimination.<sup>48</sup>

Also, and as observed by a coalition of civil rights groups, the Administration’s recently announced proposal for “reform” of the federal government’s role in housing finance “will

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<sup>47</sup> Letter from Attorney General James et al. to CFPB Director Kraninger (Oct. 15, 2019), [https://ag.ny.gov/sites/default/files/hmda\\_data\\_point\\_comments\\_-\\_nyag\\_and\\_others\\_-\\_final\\_-\\_10.15.2019.pdf](https://ag.ny.gov/sites/default/files/hmda_data_point_comments_-_nyag_and_others_-_final_-_10.15.2019.pdf)

<sup>48</sup> Letter from Attorney General Stein et al. to CFPB Acting Director Mulvaney (Sept. 5, 2018), [https://ncdoj.gov/wp-admin/admin-ajax.php?juwpfisadmin=false&action=wpfd&task=file.download&wpfd\\_category\\_id=16&wpfd\\_file\\_id=12419](https://ncdoj.gov/wp-admin/admin-ajax.php?juwpfisadmin=false&action=wpfd&task=file.download&wpfd_category_id=16&wpfd_file_id=12419).

increase the cost of mortgages for all borrowers, especially families of color, low- to moderate-income families, and rural families.”<sup>49</sup> Additionally, CFPB has recently raised the prospect that it will amend the “Qualified Mortgage” provision of the Dodd-Frank Act. 84 Fed. Reg. 37,155 (July 31, 2019). While it is critical for CFPB to enforce Dodd-Frank reforms that prevent lenders from making risky and unaffordable mortgage loans, research also suggests that any restrictions on the availability of affordable credit will fall disproportionately on families of color.

Collectively, these moves ignore the history of redlining and reverse redlining that has hindered homeownership in communities of color for decades, and that has contributed to the persistent racial wealth gap in America.<sup>50</sup> HUD’s explanation of the Proposed Rule provides no consideration of these actions across the federal government that will limit access to credit for borrowers of color, and will further deregulate private credit markets that have historically failed to serve borrowers of color equally. Such moves make the importance of the FHA’s protection against disparate impact discrimination in lending, and the use of disparate impact analysis to root out and remedy unconscious biases and structural barriers to equality, all the more important. The Proposed Rule cannot be justified in light of these efforts, and any final rule that HUD issues must take these efforts into account.

## **V. Conclusion.**

As described above, the Proposed Rule would create uncertainty, increase costs, and make it more likely that meritorious claims will be needlessly dismissed. Given these concerning implications of the Proposed Rule, HUD should leave the Current Rule undisturbed.

The existing burden-shifting test in the Current Rule provides both clarity and flexibility so that courts can apply it on a case-by-case basis and in a wide variety of housing contexts. *See Ave. 6E*, 217 F. Supp. 3d at 1050 (“Indeed, there is no rigid mathematical formula to show disparate impact and the inquiry is necessarily fact-specific.”). HUD itself recognized that the Current Rule needs to be nimble enough to allow for a case-by-case, fact-specific inquiry. *See* 78 Fed. Reg. at 11,471 (the FHA “covers many different types of entities and practices, and a determination of what qualifies as a substantial, legitimate, nondiscriminatory interest for a given entity is fact-specific and must be determined on a case-by-case basis”); *see id.* at 11,468 (“Whether a particular practice results in a discriminatory effect is a fact-specific inquiry. Given the numerous and varied practices and wide variety of private and governmental entities covered by the [FHA], it would be impossible to specify in the rule the showing that would be required to demonstrate a discriminatory effect in each of these contexts.”). A decision not to amend the Current Rule as proposed is also consistent with Congress’s intent in passing the FHA “to advance equal opportunity in housing and achieve racial integration for the benefit of all people in the United States.” *Id.* at 11,461.

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<sup>49</sup> National Urban League et al., *Don’t Disrupt Lending or Increase the Cost of Housing: Civil Rights Coalition Warns Against White House Plan for Housing Finance Reform* (Sept. 5, 2019), <https://www.responsiblelending.org/media/dont-disrupt-lending-or-increase-cost-housing-civil-rights-coalition-warns-against-wh-plan>.

<sup>50</sup> *See, e.g.*, Calvin Schermerhorn, Op.-Ed., *Why the Racial Wealth Gap Persists, More than 150 Years After Emancipation*, Wash. Post, June 19, 2019.

For all the reasons described in this letter, HUD should not amend the Current Rule and certainly should not finalize the Proposed Rule.

Sincerely,



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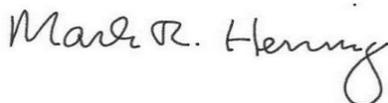
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**Attachment – Attorneys General August 20, 2018 letter to  
HUD**

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

August 20, 2018

**Re: Comment from the Attorneys General of North Carolina, California, District of Columbia, Illinois, Iowa, Maine, Maryland, Massachusetts, Minnesota, New Jersey, New York, Oregon, Pennsylvania, Rhode Island, Vermont, Virginia, and Washington Regarding the Reconsideration of HUD's Implementation of the Fair Housing Act's Disparate Impact Standard (Docket No. FR-6111-A-01)**

The undersigned state attorneys general appreciate HUD's solicitation of comments on whether amendments are appropriate to HUD's 2013 final rule ("the Rule") implementing the Fair Housing Act's ("FHA") disparate impact standard<sup>1</sup> or the 2016 supplement concerning comments made by the insurance industry.<sup>2</sup> Based on our experience enforcing fair housing laws and addressing discrimination in housing and lending, we firmly advise that no amendments are warranted. The Rule strikes the proper balance between promoting an integrated society and protecting housing providers from unmeritorious discrimination claims. Indeed, the Rule is entirely consistent with the United States Supreme Court's 2015 ruling in *Texas Department of Housing & Community Affairs v. Inclusive Communities Project, Inc.*,<sup>3</sup> which HUD has no power to alter, and other developments since 2013 only reinforce the need for it to remain unchanged.

After explaining why state attorneys general possess expertise that HUD should consider in deciding whether to propose amendments, we then explain why neither *Inclusive Communities* nor other developments warrant any amendments. Where to find our answers to each of the six specific questions posed by HUD is noted by the subsection headers.

**I. The Expertise of State Attorneys General on Disparate Impact**

Enforcement actions under the FHA and similar state laws<sup>4</sup> based on disparate impact theories are a critical component of states' efforts to combat discrimination and ensure greater equality of opportunity. The mortgage lending industry provides many of the most recent examples of state enforcement efforts based on disparate impact theories.

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<sup>1</sup> 78 Fed. Reg. 11,460 (Feb. 15, 2013) (codified at 24 C.F.R. § 100.500).

<sup>2</sup> 81 Fed. Reg. 69,012 (Oct. 5, 2016).

<sup>3</sup> 135 S. Ct. 2507 (2015).

<sup>4</sup> See, e.g., N.C. Gen. Stat. § 41A-5(a)(2) (prohibiting housing discrimination if a "person's act or failure to act has the effect, regardless of intent, of discriminating").

The history of discrimination in the lending industry is well documented.<sup>5</sup> During the boom of the subprime market in the last decade, discretionary pricing systems allowed both the intentional and unconscious bias of individual loan officers and brokers to operate unchecked. As a result, African-American and other minority borrowers were more likely to receive subprime loans, pay higher rates, and incur more charges than white borrowers—even after controlling for income and neighborhood characteristics.<sup>6</sup> Even today, borrowers of color are substantially more likely than white borrowers to be denied conventional loans.<sup>7</sup>

The nature of the lending process make the meaningful potential for disparate impact liability essential to preventing discrimination. Mortgage lending is a complicated multistep process involving numerous decision-makers making discretionary judgments.<sup>8</sup> The discretionary decision-making scheme obscures the factors that defendants use to make decisions. And because the ultimate result is the cumulative product of multiple actors, it is difficult, if not impossible, to isolate where the taint of discriminatory motive infects the decisional chain. Further compounding the challenge of enforcement, the victims of lending discrimination typically do not have any means of comparing themselves to similarly situated counterparts. And because federal law prohibits false statements on mortgage applications, “testers” cannot submit hypothetical applications to probe for discriminatory intent in the mortgage context as they can in the rental context.<sup>9</sup>

In 2011, Massachusetts resolved by consent judgment an enforcement action against Option One Mortgage Corp., a subsidiary of H&R Block, Inc.<sup>10</sup> The Massachusetts Attorney General alleged that Option One’s discretionary pricing policy—the manner by which its independent mortgage brokers were compensated—caused African-American and Hispanic borrowers to pay, on average, hundreds of dollars more for their loans than similarly-situated white borrowers. New York also resolved an investigation involving similar allegations against Countrywide Home Loans through an Assurance of Discontinuance.<sup>11</sup> Underlying that matter was the New York Attorney General’s finding of statistically significant disparities in “discretionary components of pricing, principally [p]ricing [e]xceptions in the retail sector and [b]roker [c]ompensation in the wholesale sector.” In addition, Illinois filed discriminatory lending lawsuits against Countrywide and Wells Fargo Bank alleging that African-American and Hispanic borrowers were disproportionately placed in high-cost loans and paid more for their loans. Those lawsuits were resolved in connection with a \$335 million settlement entered into

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<sup>5</sup> See, e.g., Robert G. Schwemm & Jeffrey L. Taren, *Discretionary Pricing, Mortgage Discrimination, and the Fair Housing Act*, 45 Harv. C.R.-C.L. L. Rev 375, 385-402 (2010).

<sup>6</sup> See, e.g., Justin P. Steil, *Innovative Responses to Foreclosures: Paths to Neighborhood Stability and Housing Opportunity*, 1 Colum. J. Race & L. 63, 80-83 (2011).

<sup>7</sup> See Aaron Glantz & Emmanuel Martinez, *For People of Color, Banks Are Shutting the Door to Homeownership*, *Reveal* (Feb. 15, 2018), <https://www.revealnews.org/article/for-people-of-color-banks-are-shutting-the-door-to-homeownership/>.

<sup>8</sup> See, e.g., Schwemm & Taren, *supra* note 5, at 395-98.

<sup>9</sup> *Id.* at 386.

<sup>10</sup> See *Commonwealth v. H&R Block, Inc.*, Civ. No. 08-2474-BLS1 (Suffolk Sup. Ct. 2011).

<sup>11</sup> See *In re Countrywide Home Loans*, Assurance of Discontinuance Pursuant to N.Y. Exec. § 63(15) (Nov. 22, 2006).

by the United States Department of Justice with Countrywide in 2011 and a \$175 million settlement between the United States Department of Justice and Wells Fargo in 2012.<sup>12</sup>

Though the allegations in each of these cases differ slightly, they all concern discretionary decision-making aggregated over large groups of borrowers. While direct proof of overt bias was unavailable, there were substantial and statistically significant disparities that state attorneys general did not believe could be justified by legitimate, nondiscriminatory business needs. Accordingly, the state attorneys general have first-hand experience confirming the Supreme Court’s conclusion in *Inclusive Communities* that disparate impact liability “permits plaintiffs to counteract unconscious prejudices and disguised animus that escape easy classification as disparate treatment. In this way disparate-impact liability may prevent segregated housing patterns that might otherwise result from covert and illicit stereotyping.”<sup>13</sup>

States’ use of disparate impact claims in the housing context is not limited to cases involving either lending or racial discrimination. States have also used disparate impact claims to challenge zoning ordinances, occupancy restrictions, and English-only policies.<sup>14</sup>

States also rely on the United States Department of Justice and a variety of private organizations to assist and supplement our efforts to combat discrimination and its resulting social and economic costs. Like the states, these groups have used disparate impact theories increasingly in recent years to address contemporary manifestations of discrimination, particularly in the mortgage lending context. Between 2010 and 2016, the United States Department of Justice obtained over \$1.6 billion in monetary relief for individual borrowers and impacted communities through its fair lending enforcement, the bulk of which came through settlement of cases that included FHA disparate impact claims.<sup>15</sup> Several of these cases were substantially similar to the cases brought by Massachusetts, New York, and Illinois, in that they challenged the discriminatory effects of discretionary decision-making across large groups of actors.

The United States Department of Justice and private organizations also bring cases, like those brought by states challenging zoning and occupancy restrictions, involving policies outside

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<sup>12</sup> See *United States v. Countrywide Fin. Corp.*, No. 2:11-cv-10540 (C.D. Cal. 2011); *United States v. Wells Fargo Bank, NA*, No. 12-cv-1150 (D.D.C. 2012).

<sup>13</sup> 135 S. Ct. at 2522.

<sup>14</sup> See, e.g., *R.I. Comm’n for Human Rights v. Graul*, 120 F. Supp. 3d 110 (D.R.I. 2015) (landlord’s policy of limiting occupancy had disparate impact based on familial status); *Support Ministries for Persons with AIDS, Inc. v. Vill. of Waterford*, 808 F. Supp. 120 (N.D.N.Y. 1992) (city’s interpretation and application of a local zoning ordinance had disparate impact on basis of disability); *Conn. Comm’n on Human Rights & Opportunities (“CHRO”) ex rel. Hurtado*, CHRO No. 8230394 (landlord’s English-only policy had disparate impact based on national origin and ancestry); *CHRO ex rel. Schifini*, CHRO No. 8520090 (landlord’s policy of limiting occupancy had disparate impact based on familial status); *In re-Accusation of the Dep’t of Fair Employment & Hous. v. Merrbrook Apartments, James C. Beard, Owner*, FEHC Dec. No. 88-19, 1988 WL 242651, at \*12-13 (Cal. F.E.H.C. Nov. 9, 1988) (facially neutral occupancy limit had adverse disparate impact on prospective renters with children).

<sup>15</sup> See Justice Department Reaches Settlement with Ohio-Based Banks to Resolve Allegations of Lending Discrimination (Dec. 28, 2016), <https://www.justice.gov/opa/pr/justice-department-reaches-settlement-ohio-based-banks-resolve-allegations-lending>.

of the lending context that were not expressly discriminatory, but nonetheless had a direct impact on residential housing patterns in ways that perpetuated segregation and, in many instances, indicated discriminatory intent. The Supreme Court favorably described these cases as “the heartland of disparate-impact liability.”<sup>16</sup> Had disparate impact claims not been realistically available, the victims of the discriminatory policies and practices likely would have been left without a meaningful remedy.

Based on this experience of state attorneys general regularly relying on disparate impact liability to combat housing and lending discrimination, HUD and the judiciary have regularly relied on our views concerning disparate impact liability under the FHA. As HUD acknowledged in issuing the Rule, it considered the comments submitted by a group of six state attorneys general supporting the proposed version of the Rule.<sup>17</sup> The Supreme Court in *Inclusive Communities* favorably cited an amicus brief submitted by a group of 17 state attorneys general in concluding that “residents and policymakers have come to rely on the availability of disparate-impact claims.”<sup>18</sup> Additionally, Congress established a system of enforcing the FHA in which the federal government shares responsibility with state and local governments.<sup>19</sup> Accordingly, HUD should closely consider the comments that we offer below.

## **II. The Rule Is Fully Consistent with *Inclusive Communities* and HUD May Not Alter the Supreme Court’s Ruling**

*Inclusive Communities* endorsed the continued importance of the FHA, and its disparate impact theory of liability, in advancing the nation’s efforts to advance justice and equality:

Much progress remains to be made in our Nation’s continuing struggle against racial isolation. In striving to achieve our “historic commitment to creating an integrated society,” we must remain wary of policies that reduce homeowners to nothing more than their race. But since the passage of the Fair Housing Act in 1968 and against the backdrop of disparate-impact liability in nearly every jurisdiction, many cities have become more diverse. The FHA must play an important part in avoiding the . . . 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 Nation toward a more integrated society.<sup>20</sup>

Consistent with this conclusion by the Supreme Court, the Rule adopted a framework for proving disparate impact claims reflecting the FHA’s “broad remedial intent.”<sup>21</sup>

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<sup>16</sup> 135 S. Ct. at 2522.

<sup>17</sup> 78 Fed. Reg. at 11,465.

<sup>18</sup> 135 S. Ct. at 2525.

<sup>19</sup> See 42 U.S.C. § 3610(f); see also *id.* § 3616 (providing for cooperation between HUD and state and local governments); H.R. Rep. No. 100-711, at 35 (1988) (House Committee Report to the Fair Housing Amendments Act of 1988 noting “the valuable role state and local agencies play in the [FHA] enforcement process”).

<sup>20</sup> *Inclusive Cmty.*, 135 S. Ct. at 2525-26 (citations omitted) (brackets in original).

<sup>21</sup> 78 Fed. Reg. at 11,461, 11,466.

A. *The Rule Adopted a Clear and Appropriate Burden-Shifting Framework Consistent with Inclusive Communities (Question #1)*

In promulgating the Rule, HUD relied on existing law under the FHA and Title VII to specify the framework for proving a disparate impact claim.<sup>22</sup> In so doing, the Rule provides for a three-step framework that clearly and appropriately assigned burdens at each step.<sup>23</sup>

The standard that HUD promulgated relying on these preexisting sources of law is fully consistent with *Inclusive Communities*. The Supreme Court explicitly drew on Title VII in discussing the standards applicable to an FHA disparate impact claim.<sup>24</sup> The Court heavily relied on *Griggs v. Duke Power Co.*, which is the foundation of Title VII disparate impact proof standards, to articulate the limits of FHA disparate impact.<sup>25</sup> Moreover, the Court’s observation that “disparate-impact liability *has always been* properly limited in key respects,”<sup>26</sup> further evidences that it was not calling for a significant departure from preexisting FHA and Title VII law. Indeed, in the portion of the *Inclusive Communities* opinion discussing the standards of proving a disparate impact claim, the Supreme Court cited the Rule twice in support of its analysis.<sup>27</sup>

Accordingly, two federal courts of appeals and a state supreme court have held after *Inclusive Communities* that the Rule is “adopted” by, or consistent with, the Supreme Court’s decision.<sup>28</sup> District courts have ruled similarly. Most directly on point, then-District (now-Circuit) Judge Amy St. Eve ruled last year that “the Supreme Court in *Inclusive Communities* . . . did not identify any aspect of HUD’s burden-shifting approach that required correction.”<sup>29</sup> We are aware of no court that has held that the Rule is inconsistent with *Inclusive Communities* in the three years since the Supreme Court’s decision. Accordingly, the Rule clearly and appropriately assigns burdens of production and persuasion.

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<sup>22</sup> See *id.* at 11,462 (“[T]his final rule embodies law that has been in place for almost four decades . . . .”); 76 Fed. Reg. 70,921, 70,924 (Nov. 16, 2011) (explaining the framework set out in the proposed rule is consistent with Title VII’s framework).

<sup>23</sup> 24 C.F.R. § 100.500(c)(1)-(3).

<sup>24</sup> See *Inclusive Cmty.*, 135 S. Ct. at 2522 (giving covered entities “leeway to state and explain the valid interest served by their policies . . . analogous to the business necessity standard under Title VII”).

<sup>25</sup> See *id.* (quoting *Griggs v. Duke Power Co.*, 401 U.S. 424, 431 (1971)).

<sup>26</sup> *Id.* (emphasis added).

<sup>27</sup> See *id.* at 2522-23.

<sup>28</sup> *MHANY Mgmt., Inc. v. Cty. of Nassau*, 819 F.3d 581, 618 (2d Cir. 2016) (“Supreme Court implicitly adopted HUD’s approach”); *Ave. 6E Invs., LLC v. City of Yuma*, 818 F.3d 493, 512-13 (9th Cir. 2016) (describing what the Supreme Court “made clear” in *Inclusive Communities* followed by a “see also” cite to the Rule); *Burbank Apartment Tenant Ass’n v. Kargman*, 48 N.E.3d 394, 411 (Mass. 2016) (“framework laid out by HUD and adopted by the Supreme Court”).

<sup>29</sup> *Prop. Cas. Insurers Ass’n of Am. v. Carson*, No. 13-cv-8564, 2017 U.S. Dist. LEXIS 94502, at \*29 (N.D. Ill. June 20, 2017).

B. *The Rule Already Limits Liability to “Artificial, Arbitrary, and Unnecessary Barriers” (Question #2)*

The Supreme Court observed in *Inclusive Communities* that “[d]isparate-impact liability mandates the ‘removal of artificial, arbitrary, and unnecessary barriers,’ not the displacement of valid governmental policies.”<sup>30</sup> The Supreme Court specified that this means disparate impact liability will not be found when a claim is “simply . . . an attempt to second-guess which of two reasonable approaches” a covered entity should follow.<sup>31</sup>

This limitation is found in the Rule. A burden-shifting standard has been developed and refined as part of Title VII over the past half century to effectuate the limitation articulated by *Griggs*, which *Inclusive Communities* repeated.<sup>32</sup> As noted above, the Rule relied on the Title VII burden-shifting standard.

In promulgating the Rule, HUD sought to fairly allocate, consistent with Title VII, the burdens of proof among the parties and the showing the parties must make at each stage.<sup>33</sup> Specifically, the second and third steps of the Rule’s burden-shifting standard protect a covered entity from liability based on “second-guess[ing]” of a policy choice between “reasonable approaches.”<sup>34</sup> At the second step, a defendant has the opportunity to prove that the policy or policies at issue “is necessary to achieve one or more substantial, legitimate nondiscriminatory interest.”<sup>35</sup> In the third step, a plaintiff prevails if it proves that interest could be served by a less discriminatory alternative to the challenged practice.<sup>36</sup> In proving the less discriminatory alternative, the plaintiff must show it “serve[s] the . . . defendant’s substantial, legitimate nondiscriminatory interest.”<sup>37</sup> The alternative “must be supported by evidence, and may not be

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<sup>30</sup> 135 S. Ct. at 2522 (quoting *Griggs*, 401 U.S. at 431); *see also id.* at 2524 (cautioning against proof standards that “displace valid governmental and private priorities, rather than solely ‘remov[ing] . . . artificial, arbitrary, and unnecessary barriers’”) (alterations in original).

<sup>31</sup> *Id.* at 2522.

<sup>32</sup> *See Abril-Rivera v. Johnson*, 806 F.3d 599, 606-07 (1st Cir. 2015) (treating the burden-shifting standards applied to a Title VII claim to be consistent with the limitations explained in *Inclusive Communities*).

<sup>33</sup> 78 Fed. Reg. at 11,472 (noting the definition of “legally sufficient justification” “fairly balances the interests of all parties”); *id.* at 11,473-74 (“HUD believes that the burden of proof allocation in § 100.500(c) is the fairest and most reasonable approach to resolving the claims. . . . [T]his framework makes the most sense because it does not require either party to prove a negative.”).

<sup>34</sup> *Inclusive Cmty.*, 135 S. Ct. at 2522; *see Johnson v. City of Memphis*, 770 F.3d 464, 472 (6th Cir. 2014) (noting under the Title VII burden-shifting standard analogous to the Rule that “the purpose of step three is not to second guess the employer’s business decisions”) (brackets omitted).

<sup>35</sup> 24 C.F.R. § 100.500(c)(2).

<sup>36</sup> *Id.* § 100.500(c)(3). HUD’s decision not to include the term “equally effective” in Section 100.500(c)(3), 78 Fed. Reg. at 11,473, is consistent with *Inclusive Communities*’ failure to use that phrase. *See Ave. 6E Inv.*, 818 F.3d at 512-13 (recognizing the Rule’s burden-shifting standard provides the limits to liability specified in *Inclusive Communities* and that Section 100.500(c)(3) means that “an adjustment or accommodation can still be made that will allow both interests to be satisfied”).

<sup>37</sup> 78 Fed. Reg. at 11,473.

hypothetical or speculative.”<sup>38</sup> Based these elements, the second and third steps of the Rule’s burden-shifting framework already limit liability to artificial, arbitrary, and unnecessary barriers.

*C. The Rule Already Requires “Robust Causality” (Question #4)*

Again drawing on Title VII, the Supreme Court stated that FHA disparate impact claims must satisfy a “robust causality requirement” that means “a disparate-impact claim that relies on a statistical disparity must fail if the plaintiff cannot point to a defendant’s policy or policies causing that disparity.”<sup>39</sup> This “robust causality requirement” reiterates the causal connection required by FHA disparate impact case law from which the Rule drew, which mandated disparate impact claims to be linked to a “specific policy [that] caused [the] significant disparate effect.”<sup>40</sup> Notably, these preexisting FHA cases remain “sound” pursuant to *Inclusive Communities*’ “robust causality requirement.”<sup>41</sup>

Consistent with this “robust causality requirement,” the Rule specifies that a plaintiff must prove that “a challenged practice caused or predictably will cause a discriminatory effect.”<sup>42</sup> Moreover, the Rule recognizes that the plaintiff “on a case-by-case basis” will need to “identify[] the specific practice that caused the alleged discriminatory effect.”<sup>43</sup> Also in accord with the Supreme Court drawing of the causality standard from Title VII law, HUD specified that the Rule’s standard of liability “is consistent with the discriminatory effects standard confirmed by Congress in the 1991 amendments to Title VII.”<sup>44</sup> Adopting that standard was equally sound before and after *Inclusive Communities*, and there is no reason to amend the Rule to clarify the causality standard based on *Inclusive Communities* or any other Supreme Court ruling.

*D. Inclusive Communities Does Not Suggest the Need for Additional Defenses or Safe Harbors (Question #5)*

Nothing in *Inclusive Communities* suggests that HUD should create additional defenses or non-statutory safe harbors to liability, such as treating compliance with another law as a per se defense to disparate impact liability. Massachusetts’ highest court rejected just such an argument after *Inclusive Communities* because “concluding that an action need be otherwise violative of the law before facing a disparate impact claim [would] ignore the legislative policies behind the fair housing regime.”<sup>45</sup> Moreover categorical defenses and safe harbors would provide no additional benefit over the mechanisms in the Rule that limit liability to “artificial, arbitrary, and unnecessary barriers,” as discussed earlier, because parties would dispute application of any

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<sup>38</sup> *Id.*; see also 24 C.F.R. § 100.500(b)(2).

<sup>39</sup> *Inclusive Cmty.*, 135 S. Ct. at 2523 (citing *Wards Cove Packing Co. v. Atonio*, 490 U.S. 642, 653 (1989)).

<sup>40</sup> *E.g.*, *Mountain Side Mobile Estates v. HUD*, 56 F.3d 1243, 1251 (10th Cir. 1995).

<sup>41</sup> *Nat’l Fair Hous. Alliance v. Travelers Indem. Co.*, 261 F. Supp. 3d 20, 30 (D.D.C. 2017).

<sup>42</sup> 24 C.F.R. § 100.500(c)(1).

<sup>43</sup> 78 Fed. Reg. at 11,469.

<sup>44</sup> 76 Fed. Reg. at 70,924 (citing 42 U.S.C. § 2000e-2(k)). Among the “standard confirmed by Congress” through codification into Title VII in 1991 is a causation requirement. See 42 U.S.C. § 2000e-2(k)(1)(B).

<sup>45</sup> See *Kargman*, 48 N.E.3d at 408-11 & n.27.

defense or safe harbor on a case-by-case basis just as they dispute the application of the generally applicable burden-shifting framework. Indeed, parties would face increased uncertainty as they would have no precedent to guide their disputes over new defenses and safe harbors unlike their disputes over the burden-shifting framework guided by nearly a half century of established Title VII and FHA case law. HUD should not amend the Rule to provide additional defenses or safe harbors to claims of disparate impact liability.

*E. HUD Cannot Reinterpret the Contours of Disparate Impact Liability Established by the Supreme Court*

HUD is constrained in considering whether to amend the Rule by the Supreme Court's ruling in *Inclusive Communities*. The Solicitor General of the United States argued before the Supreme Court in *Inclusive Communities* that the Court should hold that the FHA provided for disparate impact liability based on deference to the Rule. Notwithstanding that argument, the Supreme Court neither found the FHA to be ambiguous nor deferred to HUD's interpretation.<sup>46</sup> This forecloses any ability of HUD to reinterpret the contours of disparate impact liability established by the Supreme Court.<sup>47</sup>

As noted above, the Supreme Court clearly established that FHA disparate impact claims are to be evaluated based on the type of burden-shifting framework used to evaluate Title VII disparate impact claims. HUD, therefore, cannot amend the Rule to introduce concepts that are foreign to the Title VII framework. Troublingly, many of the items on HUD's list of questions for comment suggest defenses or limitations to disparate impact liability that have no parallel in Title VII. Adopting any such defense or limitation would be unlawful usurpation of judicial power by the Executive Branch.

### **III. No Other Developments Would Justify a Change in the Rule**

Even if *Inclusive Communities* left any room for revision to the Rule, no revision would be warranted. In the five years since the Rule was finalized, the issues of segregation and discrimination in housing and lending have not abated. Among other reasons, many urban centers have seen increasing displacement of communities of color amidst a decreasing supply of affordable housing,<sup>48</sup> lending standards have remained abnormally restrictive and left persons of

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<sup>46</sup> *Inclusive Cmty.*, 135 S. Ct. at 2542 (Alito, J., dissenting) (“The principal respondent and the Solicitor General—but not the Court—have one final argument regarding the text of the FHA. They maintain that even if the FHA does not unequivocally authorize disparate-impact suits, it is at least ambiguous enough to permit HUD to adopt that interpretation.”) (emphasis added).

<sup>47</sup> See *United States v. Home Concrete & Supply, LLC*, 566 U.S. 478, 487 (2012) (“In our view, [a prior Supreme Court decision] has already interpreted the statute, and there is no longer any different construction that is consistent with [that decision] and available for adoption by the agency.”).

<sup>48</sup> See Anne Bellows & Michael Allen, *The Fair Housing Imperative to Address the Displacement Crisis*, Civil Rights Insider 5, 5 (Winter 2018), available at <http://www.fedbar.org/Image-Library/Sections-and-Divisions/Civil-Rights/Civil-Rights-Winter-2018.aspx>. A recent report noted that Charlotte and Durham, North Carolina were two of four metropolitan areas with the lowest percentage of homes for sale at the affordable end of the market. Joint Ctr. for Housing Studies of Harvard Univ., *The State of the Nation's Housing: 2018*, at 4, available at [http://www.jchs.harvard.edu/sites/default/files/Harvard\\_JCHS\\_State\\_of\\_the\\_Nations\\_Housing\\_2018.pdf](http://www.jchs.harvard.edu/sites/default/files/Harvard_JCHS_State_of_the_Nations_Housing_2018.pdf).

color to be underserved by the conventional (no government guarantee) mortgage market,<sup>49</sup> and the de-segregative potential of the Low Income Housing Tax Credit (“LIHTC”) has been reduced as a result of the Tax Cuts and Jobs Act of 2017.<sup>50</sup> Moreover, the growing role of data analytics and online platforms in the housing sale and rental markets means that risks are greater that segments of society will be steered away from or denied housing in a way that is immune to examination of intent yet results in even more segregated housing patterns.<sup>51</sup> That these developments may be resulting in greater housing discrimination is borne out by data in a recent Harvard University report that found the gap between whites and African Americans in homeownership rate has risen in recent years and now stands at an appalling 29.2 percentage points, with the gap for Hispanics and Asians at nearly as troubling levels—26.1 and 16.5 percentage points.<sup>52</sup> These gaps are similar, or worse, than were observed in 1983.<sup>53</sup>

A. *The Rule Still Strikes the Proper Balance Between Encouraging the Pursuit of Legitimate Claims While Avoiding Unmeritorious Ones (Question #3)*

In promulgating the Rule, HUD explained that it was trying to “fairly balance the interests of all parties.”<sup>54</sup> We are not aware of any credible evidence that the Rule or *Inclusive Communities* have caused a disruptive upswing in unwarranted FHA litigation or unwarranted compliance costs that might suggest HUD struck the wrong balance. To the contrary, courts since 2013 have timely disposed of unmeritorious disparate impact claims<sup>55</sup> consistent with the Supreme Court’s call for “prompt resolutions of [such] cases.”<sup>56</sup> Accordingly there is no need to amend the balance that HUD previously struck between encouraging the pursuit of legitimate disparate impact claims while avoiding unmeritorious ones.

In its request for comments, HUD cites to an October 2017 report issued by the United States Department of Treasury as one potential reason for considering revisions to the Rule.

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<sup>49</sup> See Peter Smith & Melissa Stegman, Ctr. Responsible Lending, *Repairing a Two-Tiered System: The Crucial but Complex Role of FHA 6-11* (May 2018), available at <https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-repairing-two-tiered-system-fha-may2018.pdf>. According to this report, the conventional mortgage market has “shut out over 6 million creditworthy borrowers” between 2009 and 2015. *Id.* at 6.

<sup>50</sup> The tax changes caused an estimated loss of 232,000 units of affordable housing that otherwise would be built through LIHTC over the next 10 years. Joint Ctr. for Housing Studies, *supra* note 48, at 34. Increased LIHTC funding in the 2018 federal omnibus spending bill offset 28,000 units of this loss. *Id.*

<sup>51</sup> See *Sandvig v. Sessions*, No. 16-cv-1368, 2018 U.S. Dist. LEXIS 54339, at \*4-6 (D.D.C. Mar. 30, 2018) (describing work of researchers looking into the effect of these trends on housing (and employment) discrimination based on the “concern[] that, ‘when algorithms automate decisions, there is a very real risk that those decisions will unintentionally have a prohibited discriminatory effect’”).

<sup>52</sup> Joint Ctr. for Housing Studies, *supra* note 48, at 3.

<sup>53</sup> *Id.* at 3 & fig. 3.

<sup>54</sup> 78 Fed. Reg. at 11,472.

<sup>55</sup> See, e.g., *Ellis v. City of Minneapolis*, 860 F.3d 1106, 1112 (8th Cir. 2017) (affirming judgment on the pleadings on a disparate impact claim against a city-defendant for enforcing its housing code that required landlords to maintain apartments in a habitable condition); *Kargman*, 48 N.E.3d at 412-14 (applying the Rule and affirming a trial court’s motion to dismiss disparate impact claim based on an apartment complex’s decision not to renew participation in a voluntary HUD subsidy program).

<sup>56</sup> *Inclusive Cmty.*, 135 S. Ct. at 2523.

Based entirely on two conclusory sentences of discussion, citing two court decisions in lawsuits that insurance trade associations filed against HUD, the report recommends that “HUD reconsider its use of the disparate impact rule” with respect to insurance based on a handful of legal and practical concerns.<sup>57</sup> But HUD has already conducted just such a reconsideration, resulting in HUD’s 2016 supplement published in the Federal Register, based on one of these decisions that found procedural—but no substantive—fault with HUD’s original consideration of the insurance industry’s concerns.<sup>58</sup> Moreover, for the reasons that the State of Illinois explained in an amicus brief filed as part of that litigation, the concerns raised by the insurance industry (and repeated by the Treasury Department) concerning state law do not warrant a change in HUD’s determination that the Rule should apply to insurers.<sup>59</sup>

*B. Revising the Rule Would Reduce Clarity and Increase Uncertainty (Question #6)*

We have identified no developments since 2013 rendering the Rule unclear, uncertain, or burdensome. The Supreme Court’s long-awaited definitive decision that the FHA provides for disparate impact liability and the Rule’s clarification of the proof framework have made the application of disparate impact under the FHA much more clear and certain. With the exception of the above-noted lawsuit filed by insurance trade groups, none of the wide array of entities regulated by the Rule challenged its legality. This lack of reaction suggests that the vast majority of regulated entities understand the obligations created by the Rule and find compliance is not unduly burdensome.

Accordingly, there are no revisions to the Rule that would add clarity, reduce uncertainty, decrease unwarranted regulatory burdens, or otherwise assist in determining lawful conduct. To the contrary, revisions to the Rule would reduce clarity and add uncertainty, especially because any revision would likely fail to rely on the half century of disparate impact case law.

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<sup>57</sup> U.S. Dep’t of Treasury, *A Financial System that Creates Economic Opportunities: Asset Management and Insurance* 110 (2017).

<sup>58</sup> *See Prop. Cas. Insurers Ass’n of Am. v. Donovan*, 66 F. Supp. 3d 1018 (N.D. Ill. 2014). The other decision cited by the Treasury Department had been vacated by the United States Court of Appeals for the District of Columbia Circuit two years before the report was issued. *Am. Ins. Ass’n v. HUD*, No. 14-5321, 2015 U.S. App. LEXIS 16894 (D.C. Cir. Sept. 23, 2015), *vacating*, 74 F. Supp. 3d 30 (D.D.C. 2014).

<sup>59</sup> Brief of the State of Illinois as Amicus Curaie, *Prop. Cas. Insurers Ass’n of Am. v. Donovan*, No. 13-cv-8564, Doc. 80 (N.D. Ill. July 7, 2014); *see also Nat’l Fair Hous. Alliance*, 261 F. Supp. 3d at 29 (“There is a large body of case law holding that insurers—including insurers who sell products to landlords—can be held liable under the FHA, and *Inclusive Communities* does not call those cases into question. . . . Numerous courts have applied disparate-impact liability to insurers that provide (or don’t provide) insurance to homeowners or renters.”).

#### **IV. Conclusion**

For all the reasons stated above, the undersigned state attorneys general respectfully advise HUD that no changes are appropriate to the Rule and that any changes would be susceptible to meritorious legal challenge.

Sincerely,

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