framework. Although privatizing Fannie and Freddie would afford Fannie and Freddie added flexibility to engage in other activities (and to stop sending profits to the Treasury Department), privatization would eliminate significant benefits currently enjoyed by Fannie and Freddie, such as local and state tax exemptions and lower federal borrowing costs. More important, without government backing, Fannie and Freddie may be less likely to purchase longer-term mortgage loans from banks and lenders, which means financial institutions may be less likely to extend 30-year fixed rate mortgages to borrowers and, instead, opt for shorter mortgage terms or adjustable rate mortgage that protect lenders but generally are viewed as less predictable and, therefore, riskier for borrowers.

If Biden is elected president, his administration could attempt to replace Calabria (pending the outcome of a Supreme Court case to determine whether a President can remove the FHFA director without cause) and prolong the conservatorship. In addition, if Democrats win majority control of the Senate, a Biden administration could push forward legislative efforts to reform Fannie and Freddie as a public utility, which would place limits on their profitability and pricing.

What does this mean for Banks and their Customers?

Consistency and predictability, particularly in the legislative and regulatory space, are highly valued by banks. Regardless of the outcome of the 2020 presidential election, banks likely will face some degree of regulatory whiplash and the associated costs. And clarity likely will not come until months after the presidential election.

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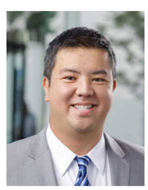

HUD Issues Final Rule Redefining the Standard for Fair Housing Disparate Impact Discrimination Claims

by Christopher Friedman and Austin Holland

On Sept. 3, the U.S. Department of Housing and Urban Development (HUD) issued its final rule on the implementation of the Fair Housing Act's disparate impact standard. The Fair Housing Act (FHA) prohibits discrimination in many housing-related activities on the basis of race, color, religion, sex, disability, familial status, and national origin. For at least the past four decades, HUD and federal courts have read the FHA to prohibit "disparate impact" discrimination, which is conduct that, while not motivated by discriminatory intent, has a discriminatory effect. The final rule became effective 30 days from the date of publication in the Federal Register.

The path to the most recent disparate impact final rule has been long and circuitous. In February 2013, HUD codified its long-held view that the FHA bans disparate impact discrimination by issuing a rule entitled Implementation of the Fair Housing Act's Discriminatory Effects Standard. That rule established a three-part, burden-shifting test to determine whether a housing practice that results in discrimination violates the FHA.

However, in 2015, the U.S. Supreme Court decided Texas Department of Housing and Community Affairs v. Inclusive Communities, in which a non-profit organization claimed that policies of the Texas Department of Housing and Community Affairs regarding the distribution of low-income housing development tax credits resulted in discrimination against African Americans in violation of both 42 U.S.C. § 1983 and the FHA. In Inclusive Communities, the Supreme Court did not rely upon HUD's 2013 disparate impact, burden-shifting test. Rather, the court undertook its own analysis, resulting in standards that differed from HUD's rule. While holding that the FHA prohibited disparate impact discrimination, the decision also established several guard rails designed to "protect potential defendants against abusive disparate impact claims." For instance, the court held that a disparate impact claim cannot be sustained solely by evidence of a statistical disparity. Instead, the court enacted a "robust causality" rule requiring that a plaintiff show that a policy or procedure actually caused the disparity.

Several years after Inclusive Communities, in June 2018, HUD issued an advanced notice of proposed rulemaking purporting to realign its disparate impact regulation to better match the Supreme Court's holding. In August 2019, HUD issued the proposed rule, very similar to this recently released final rule, that sought to align HUD's disparate impact analysis with the standards applied by the Supreme Court in Inclusive Communities. After more than two years, HUD finally issued the final rule.

Through its final rule, HUD aims to adopt the disparate impact analysis applied in Inclusive Communities. The final rule creates a new burden-shifting framework for disparate impact claims. Under the rule, a plaintiff must, as a threshold matter, sufficiently plead facts to support that a specific, identifiable policy or practice has a discriminatory effect, and that the challenged policy or practice was "arbitrary, artificial, and unnecessary to achieve a valid interest or legitimate objective." The plaintiff must further plead that the challenged policy or practice has a disproportionately adverse effect on members of a protected class, that the specific policy or practice is the direct cause of the discriminatory effect (i.e., robust causality), that the alleged disparity caused by the policy or practice is significant, and that there is a direct relation between the injury asserted and the injurious conduct alleged.

If a court finds that a plaintiff sufficiently pleads facts to support each of the requirements above, HUD's rule then provides the new burden-shifting test, which is summarized as follows:

- The plaintiff must first show by a preponderance of the evidence that the challenged policy or practice has a disproportionately adverse effect on members of a protected class, that the specific policy or practice is the direct cause of the discriminatory effect, that the alleged disparity caused by the policy or practice is significant, and that there is a direct relation between the injury asserted and the injurious conduct alleged.
- A defendant may then rebut the plaintiff's allegation that the challenged policy or practice is arbitrary, artificial, and unnecessary by producing evidence showing that the challenged policy or practice advances a valid interest and is therefore not arbitrary, artificial, and unnecessary.
- If a defendant rebuts a plaintiff's assertion under (1) above, the plaintiff must prove by a preponderance of the evidence either that the interest(s) advanced by the defendant are not valid or that a less discriminatory policy or practice exists that would serve the defendant's identified interest(s) in an equally effective manner without imposing materially greater costs or burdens on the defendant.

In addition, the rule lists a number of defenses that may be used during and after the pleading stage, including that the plaintiff failed to sufficiently plead facts to support the allegations and that the defendant's policy or practice is reasonably necessary to comply with certain third-party requirements. In administrative cases, HUD will only pursue civil money penalties in a disparate impact case where the defendant has previously been adjudged within the last five years to have violated the FHA.

The language of the final disparate impact rule will not prove too surprising to anyone who has followed the rulemaking process. However, the theory of disparate impact liability has always been, and remains, complicated. Although the final rule appears to reduce the burden on defendants, it also provides additional layers of complexity through the new burden-shifting analysis. Thus, while the proposed rule is likely welcome relief to businesses that are vulnerable to disparate impact claims, it will likely not decrease the number of Fair Housing Act claims and may very well increase the costs to defend the claims.

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