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**CURRENT ISSUES IN FAIR LENDING**

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**MBA's Legal Issues and  
Regulatory Compliance Conference**

**April 29-30, 2008**

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# OVERVIEW

- **Legal Framework**
  - ECOA
  - FHA
  - HMDA
  
- **Government Investigations and Litigation**
  
- **Reducing The Risk**

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# LEGAL FRAMEWORK

## ■ **Equal Credit Opportunity Act (“ECOA”)**

- A creditor may not discriminate against any applicant with respect to any aspect of a credit decision on the basis of, among other things, race, color, religion, national origin, sex, marital status, and age.

## ■ **Fair Housing Act (“FHA”)**

- It is unlawful to discriminate on the basis of race, color, religion, sex, familial status, or national origin in the provision of services with respect to the sale of a dwelling.

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# LEGAL FRAMEWORK

- Disparate Treatment
  - Overt discrimination
  - Inconsistent application of facially-neutral policies that is not fully explained through legitimate nondiscriminatory factors
    - May be shown through comparative evidence
  
- Disparate Impact
  - A discriminatory effect on a protected class caused by the application of a facially-neutral policy or practice
  
- Agencies required to refer violations of either the ECOA or the FHA to DOJ for further investigation

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# LEGAL FRAMEWORK

- **Home Mortgage Disclosure Act (“HMDA”)**
- **HMDA Phase I: 1975-1989**
  - Required reporting of lending volume in particular MSAs
  - Focus on redlining
- **HMDA Phase II: 1989-2004**
  - Required reporting application decisions
  - Focus on denial-disparity ratios
- **HMDA Phase III: 2004-?**
  - Required reporting rate-spread on trigger loans
  - Primary focus on pricing disparities

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# GOVERNMENT INVESTIGATIONS AND LITIGATION

- Regulators under pressure
  - From Congress
  - From the Administration
  - From the media
  - From the public
  
- Effects of pressure
  - Regulators anxious to investigate potential fair lending violations to demonstrate that they are responding to concerns
  - Pursuing “leads” where they may not have done so in the past
    - Agencies are aggressively pursuing cases

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# GOVERNMENT INVESTIGATIONS AND LITIGATION

- Focus of inquiries:
  - Pricing discretion
  - Steering
  - Redlining
  - Denial Disparity
    - Credit crunch likely to lead to increased underwriting investigations
  
- Statistical analyses are driving investigations
  - Data “sliced and diced” dozens of different ways

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# GOVERNMENT INVESTIGATIONS AND LITIGATION

- Public interest group complaints
  - NAACP complaint
    - Class action against numerous lenders alleging discriminatory lending practices
  - Other public interest group complaints
  
- Complaints filed by municipalities
  - Cities seeking to force lenders to shoulder costs of foreclosures
  
- Wave of private civil litigation
  - Allegations that “Discretionary Pricing Policies” are inherently discriminatory

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# REDUCING THE RISK

## Before the knock at your door...

- Establish a strong and effective fair lending program
  - Impress upon employees the importance that the institution places on treating all applicants and borrowers equally
  - Emphasize equal treatment at every stage of the loan process
  - Program should be documented in writing
  - Policies should be readily available
  - Frequent training

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# REDUCING THE RISK

- Know your data
  - Conduct privileged statistical analyses of HMDA data and non-triggered loans
  - Focus on disparities
  - Analyze underwriting criteria and decisions
- Know your institution
  - Conduct interviews and reviews to determine the factors that affect pricing and underwriting decisions in the real world
- Identify potential causes of any disparities and take steps to address causes where appropriate

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# REDUCING THE RISK

- Policy and Practice Considerations
  - Minimize trigger loans
    - Some institutions have prohibited trigger loans
    - Apply and enforce maximum rates or spreads
    - Limit fees on small loans with short amortization period
  - Limit and document discretion
    - Apply and follow rate sheet or pricing matrix
    - Require deviations from rate sheet to be documented
    - Track and limit pricing exceptions

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# REDUCING THE RISK

- After the knock at the door . . .
  - You probably have only one chance to get it right
    - Know the answer before you start talking
  - Importance of accurate and complete response
    - If wrong answer given, provide a correction
  - Don't be afraid to make changes
    - Improving the process doesn't mean you admit it was broken

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# CONCLUSION

- Pricing issues to remain at forefront for foreseeable future
  - But credit crunch likely to lead to more denial disparity cases
  
- Civil litigation following government action
  - Recent increase in disparate impact civil litigation based on HMDA data
  
- Know your data
  - *Before* the government or class action lawyers do
  
- Goal: Consistent and documented decisions
  - Be able to explain why you did what you did

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## **For further information contact:**

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