



BACKGROUND | October 2017

Disparate Impact and Fair Housing

New Developments Legal Summary

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Table of Contents

Introduction	3
Disparate Impact Overview	3
Disparate Impact Generally.....	4
Origins of the Diverging Standards of Liability	4
2013 HUD Regulations: The Lower Standard.....	5
2015 Supreme Court Standard in <i>TDHCA</i> : The Higher Standard	5
HUD’s Promulgation of Rules and Guidance Post-TDHCA Expansively Interprets Disparate Impact Liability	6
HUD Actions Regarding Private Housing Providers	7
HUD Regulation on Affirmatively Furthering Fair Housing	8
Post-TDHCA, Federal Courts Have Aligned With the Higher Supreme Court Standard Over the HUD Regulations.....	8
Tax Credit Allocation.....	8
Project Decision Making.....	9
Mortgage Lending.....	9
Zoning and Ordinance Decisions.....	10
Preferences Policies.....	10
Insurance.....	10
Criminal Screening.....	11
Conclusion.....	12

Introduction

This Legal Summary analyzes the divergence between the standards used by the Department of Housing and Urban Development (“HUD”) and the United States Supreme Court in assessing disparate impact liability under the Fair Housing Act (“FHA”). While disparate impact liability in housing discrimination has long been recognized by courts as a valid remedy at law, it was not until recently that HUD and the Supreme Court issued their own respective standards.

In 2013, HUD issued regulations establishing a three-step burden-shifting standard for determining whether a housing provider is liable under disparate impact theory. This standard, generally viewed to be a lower threshold, contrasts with the standard advanced by the Supreme Court in 2015 in the case of *Texas Department of Housing and Community Affairs v. Inclusive Communities Project, Inc.*, which sets a higher burden for those who bring claims.

The cases collected and analyzed in this Legal Summary reflect that nearly all courts have aligned with the Supreme Court’s standard and largely omitted reference to HUD’s regulations in determining whether disparate impact liability exists. This judicial treatment comes in spite of HUD’s attempts from 2015 through the end of the Obama Administration to expand disparate impact liability through guidance and regulations.

The disparate impact cases following *TDHCA* can be categorized as cases involving: tax credit allocation, project decision making, mortgage lending, zoning, preference policies, insurance, and screening policies. Analyzed fully in Part IV, the case law demonstrates that courts are generally adhering to the Supreme Court’s instruction that disparate impact liability should be limited only to situations where there is a specific, facially neutral policy, causing an artificial barrier to fair housing, that has a discriminatory effect on a protected class where the adverse effect is specifically caused by being a member of that protected class.

Nearly all of the courts have dismissed the disparate impact claims, usually by finding that the person making the claim has not met the “robust causality requirement” directly linking the adverse effect to the protected class. Courts rarely mention the burden shifting framework advanced by HUD’s 2013 regulations. However, when courts do analyze disparate claims under the three-part test, the outcome is typically that the case moves forward in litigation instead of the claims being dismissed.

The divergence largely lies in the regulations lacking a strong causation requirement at the initial stage, allowing claimants simply to show a statistical disparity without having to show that the defendant is liable for creating and causing that disparity. But with the potential to reconcile the divergence, there is currently a case challenging whether HUD’s regulations unlawfully conflict with the Supreme Court’s holding in *TDHCA*.¹

Disparate Impact Overview

The FHA, among other things, prohibits discrimination in the sale, rental, and conditions of housing because of an individual’s membership in one of the protected classes of race, color, religion, sex, familial status, national origin, or disability.² HUD is the primary federal agency tasked with enforcing the FHA.

Disparate Impact Generally

Individuals who feel they have been victims of housing discrimination can bring a lawsuit under two different theories of liability: discriminatory intent (also called disparate treatment) or under discriminatory effects (usually called disparate impact). Disparate treatment liability arises when the housing provider has a policy or practice that, on its face and in practice, discriminates against a protected class. For example, if a housing provider had a policy against leasing to applicants with Afghani national origin or of Asian race, such a policy would violate the FHA under disparate treatment liability.

Because many policies and practices today do not openly discriminate against protected classes in that way, disparate impact liability is used to attack policies that might initially seem neutral but actually have the underlying effect of discriminating against a protected class. Thus, under disparate impact liability, even if the housing provider did not intend to discriminate against a protected class, it could still be liable if the effect of the policy or practice does in fact disproportionately and adversely affect a protected class. For example, a seemingly neutral policy of not leasing to applicants with a prior criminal conviction could lead to disparate impact liability because of how that policy could adversely and disproportionately affect members of a protected class that generally have more arrests and convictions.

Origins of the Diverging Standards of Liability

Before discussing the diverging standards used by HUD and the Supreme Court, some context is necessary to discuss what precipitated the need for an authoritative standard on disparate impact liability. Although disparate impact liability is not included in the text of the FHA, all of the Circuit Courts of Appeals to consider the issue since the 1980's recognized it as a valid theory of recovery under the FHA.³ Despite this agreement, different circuits utilized different standards of reviewing those claims.⁴

Most circuits initially agree that after a person making a claim establishes a *prima facie* case, the burden shifts to the defendant to show that the challenged policy or practice serves a "legitimate interest."⁵ After that stage, the circuits applied varying standards and burdens. For example, the Second and Third Circuits required the *defendant* to prove that there is no less discriminatory way to achieve that stated interest.⁶ In contrast, the Eighth and Tenth Circuits required the *plaintiff* to prove that there are less discriminatory alternatives.⁷

Making matters more complicated, the Seventh Circuit used a different four-factor test instead of the burden shifting approach.⁸ The Fourth and Sixth Circuits applied a balancing test to public defendants but a burden-shifting test to private defendants.⁹

The incongruent standards applied to disparate impact cases made the issue ripe for authoritative guidance. Seeking to resolve the inconsistencies, HUD in 2011 issued a Notice of Proposed Rulemaking, where it advanced what would become the three-part burden shifting framework finalized in its 2013 regulations.¹⁰ Around the same time, the *TDHCA* case was proceeding to the Supreme Court on appeal, paving the way for the two different standards to be announced within two years of each other—exacerbating the confusion on this issue.

This Legal Summary analyzes the standard for judging the viability of a disparate impact claim, which has diverged recently into two strains as a result of the attempts by HUD and the Supreme Court to resolve the prior inconsistent treatment among the circuit courts.

2013 HUD Regulations: The Lower Standard

The first strain, which is the minority approach under the case law, assesses a disparate impact claim using the standard articulated by HUD in its 2013 regulations. Under the HUD regulations, which comprise a three-part burden shifting framework, the complaining party must first demonstrate that the challenged practice caused or predictably will cause a discriminatory effect.¹¹ Then, the burden shifts to the housing provider to prove that the challenged practice is necessary to achieve one or more “substantial, legitimate, nondiscriminatory interests.”¹² If satisfied, the burden shifts back to the complaining party to prove that the “substantial, legitimate, nondiscriminatory interest” could be accomplished through a practice that has a less discriminatory effect.¹³ A housing provider will be able to prevail if it can show that the substantial, legitimate, nondiscriminatory interest cannot be achieved through a practice that has any less discriminatory effect.¹⁴

2015 Supreme Court Standard in TDHCA: The Higher Standard

In 2015, the Supreme Court affirmed disparate impact liability as a valid theory of recovery under the FHA and articulated a standard of its own.¹⁵ The Supreme Court’s standard diverged from that of HUD’s regulations by imposing a significantly higher burden on the party making a claim. The Supreme Court did not reject HUD’s three-part burden shifting test, rather, it imposed higher standards that limit liability. The Court held that a claim would fail if the claimant could not “produce statistical evidence demonstrating a causal connection” between the policy and discriminatory effect.¹⁶

The Court termed this a “robust causality requirement,” which would protect housing providers “from being held liable for racial disparities they did not create.”¹⁷ Using stricter language than the “legitimate, nondiscriminatory interests” defense in the HUD regulations, the Court stated that a housing provider’s policy would not cause disparate impact liability unless it constituted an “artificial, arbitrary, and unnecessary barrier” to fair housing.¹⁸

The Court did not want its acknowledgement of disparate impact liability to put housing providers in an impossible bind where they would be subject to liability no matter what action they chose; for example, whether they chose to rejuvenate an inner city or to promote low income housing in the suburbs. In support of this recognition, the Court reiterated that the FHA “does not decree a particular vision of urban development” and that “disparate impact liability ‘does not mandate that affordable housing be located in neighborhoods with any particular characteristic.’ ”¹⁹

The Court expressed disfavor for expansively interpreting disparate impact liability, as that could stifle low-income housing development by private developers and housing authorities, thus undermining the purpose of the FHA.²⁰ Further limiting an expansive view of liability, the Court emphasized that there must be a policy or practice causing the disparity, cautioning that “a one-time decision may not be a policy at all.”²¹

The limiting language and narrowing of liability that the Supreme Court emphasized in its opinion demonstrates that it did not intend for its recognition of disparate impact liability under the FHA to open the gates for plaintiffs to bring a flood of claims related to any minor negative impact on protected

classes, or for judges to second-guess every policy, practice, or project development decision. The Court viewed its safeguards in protecting developers and owners of housing as necessary for ensuring that disparate impact liability is used only for “removing artificial, arbitrary, and unnecessary barriers” to finding or having housing.²²

The HUD and Supreme Court standards diverge from each other, in that the Court’s opinion suggests a higher standard than that of HUD, which properly limits disparate impact claims to egregious, arbitrary and negative situations. Courts addressing disparate impact claims since *TDHCA* have nearly all aligned with the Supreme Court’s standard, as they should, in requiring the plaintiff to meet the robust causality requirement in advancing statistical support for the policy causing a discriminatory effort. Part VI analyzes these cases by category. Before that analysis, the ensuing section discusses HUD’s substantial efforts to expand disparate impact liability between the issuance of the *TDHCA* opinion and end of the Obama Administration.

HUD’s Promulgation of Rules and Guidance Post-TDHCA Expansively Interprets Disparate Impact Liability

After the Supreme Court’s decision in 2015, which most legal commentators agree narrowed disparate impact liability, and through the end of the Obama Administration’s term, HUD advanced its disparate impact rule and promulgated rules and guidance that expansively interpreted disparate impact liability.²³ HUD took this active position in a variety of subject areas, despite the body of judicial decisions dismissing most disparate impact claims. This activity took the form of issuing informal guidance or formal regulations, applying to private housing providers or public entities, or, in some cases, both.

Agencies issue guidance to explain their understanding of a statute, not to create substantive law. On the contrary, when an agency issues formal regulations as part of the notice and comment rulemaking process, the regulations do carry the force of law. Courts therefore do not have to accept conclusions reached in agency guidance, but are instead able to provide the guidance the proportionate amount of deference that the court feels it deserves, based on factors such as its legal persuasiveness, thoroughness, validity of its reasoning, and consistency with prior agency pronouncements.²⁴

Final regulations promulgated by HUD, because they carry the force of law, can only be overturned through the long and procedural notice-and-comment process. Agency guidance, however, which does not carry the force of law, can be immediately withdrawn by the new HUD secretary.

HUD Actions Regarding Private Housing Providers

HUD took four formal and informal actions in 2016 broadening disparate impact liability as applied to private housing providers, on the topics of criminal screening, hostile environment harassment, limited English proficiency, and insurer liability.

In April 2016, HUD issued informal guidance subjecting criminal screening policies to disparate impact liability by applying the standard from its 2013 regulations. HUD admits that convicted criminals are not

a protected class under the FHA, but explains that the disproportionate incarceration rate for African Americans and Hispanics provides support for the proposition that a screening policy based on criminal convictions can have a discriminatory racial effect.²⁵

Housing providers can still employ criminal screening policies so long as the policy's screening mechanisms are tailored to legitimate, nondiscriminatory justifications and do not categorically ban all applicants with a criminal conviction.²⁶ Despite issuing the Criminal Screening Guidance over one year after the *TDHCA* opinion, HUD does not reference any of the heightened standards that the Supreme Court seemed to impose on disparate impact determinations. Instead, HUD simply analyzed criminal screening policies exclusively using its own 2013 regulations.

In September 2016, HUD issued guidance employing disparate impact theory to expand FHA protections to persons with limited English proficiency ("LEP").²⁷ Although being a LEP individual is not a protected class under the FHA, HUD justified that LEP's close nexus with the protected class of national origin permits disparate impact recovery because nearly all LEP persons are themselves from, or have family from, non-English speaking countries.²⁸ The LEP Guidance, similar to the Criminal Screening Guidance, makes only a passing reference to the Supreme Court opinion and instead advances using the three step standard from the HUD regulations.

HUD issued formal regulations that same month in September 2016 prohibiting "hostile environment harassment," which demonstrate HUD's attempt to broaden discrimination remedies for persons with claims.²⁹ The regulations impose liability upon a housing provider when discrimination or hostile environment harassment occurs on its property, including when solely between two tenants, if the housing provider "knew or should have known of the discriminatory conduct and had the power to correct it."³⁰

In October 2016, HUD released Supplemental Public Comments on the applicability of the insurance industry to the 2013 disparate impact regulations.³¹ During the notice-and-comment stage of the 2013 regulations, the insurance industry requested a categorical exemption from disparate impact claims because insurers could be liable under it for using certain well-accepted risk factors in underwriting that might have an unintended yet discriminatory effect.³² After HUD denied the request and stated that the concerns could be resolved on a case-by-case basis, a federal judge mandated that HUD provide an explanation for its reasoning.³³

HUD responded that it could not precisely define the scope of any exemption without sacrificing the remedial nature of the FHA but reassured insurers that "practices that an insurer can prove are risk-based, and for which no less discriminatory alternative exists, will not give rise to discriminatory effects liability."³⁴ By refraining from granting a categorical exemption to the insurance industry on disparate impact liability, HUD again revealed its desire to broaden the impact of disparate impact liability where possible. Currently, however, and as discussed in depth in Part IV.F, the insurance industry continues to litigate this issue in a way that could result in a court ruling that HUD's regulations are unlawful under the FHA as exceeding the scope of disparate impact liability set forth by the Supreme Court in *TDHCA*.

HUD Regulation on Affirmatively Furthering Fair Housing

In July 2015, just a month after the Supreme Court's *TDHCA* decision, HUD began its flurry of activity that continued through the end of the Obama Administration by issuing a final rule on affirmatively furthering fair housing. The rule had the stated purpose of providing HUD program participants with an

effective strategy to further the FHA's goals of overcoming historic patterns of segregation, promoting fair housing choice, and fostering inclusive communities that are free from discrimination.³⁵

The purpose of this regulation was to reinvent the means by which HUD achieves the FHA-mandated goal of administering its programs in a way that affirmatively furthers fair housing.³⁶ Finding the existing decentralized system ineffective and over-reliant on individual jurisdictions to assess their impediments to fair housing, HUD, through its new regulations, imposed a centralized system that will provide program participants with more data with which to assess their strategic plans for discriminatory effects.³⁷ However, contrary to HUD's regulation, Congress, in 2017, proposed legislation in both the House of Representatives and the Senate that would specifically nullify the 2015 Affirmatively Further Fair Housing rule.³⁸

Post-TDHCA, Federal Courts Have Aligned with the Higher Supreme Court Standard Over the HUD Regulations

HUD and the Supreme Court have diverged on the standard on which to base disparate impact claims under the FHA. The Supreme Court, in its 2015 *TDHCA* opinion, expressed concerns about the effects and constitutionality of an overly broad view of disparate impact liability. For those and other reasons, it discussed the need for a "robust causality requirement" to ensure that housing providers are not being held liable for racial disparities that they did not create.³⁹

The case law below demonstrates that federal courts have aligned largely with the Supreme Court's standard, which imposes a higher standard that limits liability. Plaintiffs have brought disparate impact cases on topics including tax credit allocation, project placement decision making, mortgage lending, zoning and preferences, insurance, and screening policies. In nearly all of these cases, the housing provider has prevailed in getting the disparate impact claim dismissed because the plaintiff could not satisfy the heightened standard articulated by the Supreme Court. Interestingly, in one of the seldom victories for a plaintiff, the court applied the HUD regulations as opposed to the standard of *TDHCA*, which illuminates the heightened nature of the Court's standard compared to HUD's.⁴⁰

New cases and appeals continue to be filed under this theory, therefore this Legal Summary only analyzes significant disparate impact cases through the spring of 2017. Although nearly all courts seem to be following the Supreme Court standard, ultimately, and potentially through a pending insurance category case,⁴¹ a court will have to reconcile the divergence and formally resolve which standard should govern these types of claim.

Tax Credit Allocation

Low income tax credit allocation was the genesis in *TDHCA* for disparate impact liability rising to national prominence, but plaintiffs have not encountered success bringing these claims. The Supreme Court remanded the seminal *TDHCA* case back to the district court, which had originally found disparate

impact liability but now dismissed the claims, finding that the plaintiffs failed to identify a specific policy causing a discriminatory effect.⁴²

The reversal in outcomes shows how the Supreme Court changed the legal landscape. By complaining of the agency's exercise of discretion in making allocation decisions, as opposed to identifying a specific allocation policy, the district court was unable to evaluate any statistical effect of the policy to fashion an appropriate remedy.⁴³ The court indicated that the plaintiffs' failure to meet the Supreme Court's "robust causality requirement" demonstrated the difficulty in proving causality where multiple factors are involved in a decision.⁴⁴

Another case challenging the Department of the Treasury's program for allocation of low income tax credits came to the same result, with the court again finding that exercising discretion in the allocation of tax credits is not a specific policy that can give rise to disparate impact liability.⁴⁵ The court emphasized the Supreme Court's instructions that disparate impact liability should be used to remove "artificial, arbitrary, and unnecessary barriers" in pointing out that the plaintiffs were actually seeking for the court to impose upon the Treasury a policy of affirmatively preventing racial segregation, rather than seeking to remove a policy causing such effect.⁴⁶ The court also utilized the Supreme Court heightened standard in finding that the plaintiffs failed the causation requirement.⁴⁷

The tax credit allocation cases demonstrate the difficulties plaintiffs will encounter in attacking governmental decisions made not based on a specific policy but instead on the permitted exercise of discretion, as courts are now loathe to second-guess their reasonable judgment. These courts did not discuss the HUD burden-shifting framework and solely relied on the Supreme Court's standard in dismissing the disparate impact claims.

Project Decision Making

Tenants have attempted, largely unsuccessfully, to use disparate impact liability to attack decisions made by apartment building owners that change the nature or services of the building. For example, one court⁴⁸ dismissed a disparate impact action where African-Americans residents challenged the condemnation of their apartment complex by emphasizing the Supreme Court's language that a one-time decision is not necessarily a "policy or practice" and that compliance with safety codes is a legitimate governmental interest.⁴⁹

In another case,⁵⁰ the court dismissed a disparate impact action brought by residents after management discontinued acceptance of Section 8 vouchers (used by members of protected classes), because the plaintiffs failed to meet the rigorous pleading requirements of *TDHCA*, including the robust causality standard.⁵¹

Only in one case did plaintiffs successfully overcome a motion to dismiss, and interestingly, the court there mistakenly emphasized adherence to the HUD regulations over that of the Supreme Court standard, which may explain that success.⁵²

Despite the one outlier, these cases are also demonstrative of how courts regard the Supreme Court's heightened standard as authoritative. The cases also demonstrate that one-time project related decisions (like condemnation or discontinuation of vouchers) might not even fall under the purview of disparate impact theory because they do not constitute a practice or policy.

Mortgage Lending

There have been three mortgage lending cases involving allegations that a bank's lending practices caused a disparate impact on protected classes through varying types of predatory lending. All of these claims failed because, primarily, the plaintiffs were unable to identify a specific facially neutral policy employed by the lenders that was the cause of the adverse impact. Interestingly, two of the courts interpreted *TDHCA* to impose a four-pronged test to determine whether a plaintiff has met the high prima facie burden. It does not appear that other courts have employed this four-pronged test, but it accurately captures the key requirements of the Supreme Court.

One of the courts highlighted a theme from the tax credit allocation cases in that the plaintiffs were actually complaining that the bank *lacked* a policy of correcting disproportionate effects as opposed to complaining about a policy that caused disproportionate effects.⁵³ Another court attempted to clarify the conflation between disparate impact and discriminatory intent claims, by explaining that a policy of intentionally predatory lending to take advantage of minorities does not satisfy the disparate impact prerequisite of a policy that is "neutral on its face."⁵⁴ Instead, such a claim is actually one of discriminatory intent under the FHA. The third court to analyze this issue noted the same conflation, expressing concern about using disparate impact liability to hold a bank liable for disparities caused by other factors.⁵⁵

These cases show that plaintiffs will not likely be able to successfully use disparate impact liability to attack banks for making lending decisions that adversely affect minorities or other protected classes. First, this is because if the bank were truly engaging in predatory lending to target minorities, that would be an intentionally discriminatory policy, which is the opposite of a disparate impact claim. Second, the courts have noted the difficulty in proving higher default and foreclosure rates for minorities as being caused by the bank's lending practice without showing that this result was not caused by other factors.

Zoning and Ordinance Decisions

The zoning cases (and preferences cases, discussed next), more so than the other categories, serve as an example of the type of case the Supreme Court seemed to contemplate as within the bounds of the limitations it imposed on disparate impact liability. The Court specifically mentioned that liability would exist when zoning laws "function unfairly to exclude minorities from certain neighborhoods without any sufficient justification."⁵⁶ Municipalities must be diligent in crafting zoning policies that do not arbitrarily cause a disparate impact on protected classes.

Of the two zoning cases post-*TDHCA* involving disparate impact claims, the courts split on using the HUD regulations or the heightened Supreme Court standard. The Second Circuit analyzed the claim using the HUD regulations in finding that the city's zoning reclassification would perpetuate segregation by decreasing housing available to minorities.⁵⁷ The court remanded the case to the lower court to analyze the third prong (less discriminatory alternative) and surprisingly omitted reference to the *TDHCA* heightened standards. The other zoning case took the majority approach of analyzing the claim using the Supreme Court standard and easily determined that the city's construction ordinance was not causally connected to the complained of discriminatory effect.⁵⁸

Preference Policies

When a city awards open units in a new affordable housing project, it sometimes uses a preferences policy whereby a certain percentage of available units are allocated for residents from a designated area.

Although neutral on its face, a preferences policy that maintains the status quo in a district that is disproportionately segregated from surrounding areas is problematic and would likely survive a motion to dismiss. Even if the policy is well intentioned, like the San Francisco policy that sought to prevent low-income African Americans from being displaced by gentrification, it still must comply with FHA prohibitions against perpetuating segregation.⁵⁹ Like zoning ordinances, preferences policies are another example of what the Supreme Court likely contemplated in writing that the FHA's goal is to ensure that housing priorities "can be achieved without arbitrarily creating discriminatory effects or perpetuating segregation."⁶⁰

A prime example of the problems posed by preferences policies is a case where a city developed a lottery system to award affordable housing by giving preference to residents who already lived in the area surrounding the housing project.⁶¹ The plaintiffs, however, demonstrated with statistics that the area was already disproportionately segregated, meaning that the preferences policy maintained the status quo of segregation, causing an obvious discriminatory effect.⁶²

Insurance

The insurance industry is now leading the litigation efforts to render the HUD regulations unlawful under the FHA for imposing a higher liability standard than the Supreme Court pronounced in *TDHCA*.

Insurance industry expressed initial concern with HUD's 2013 regulations because HUD did not exempt them from disparate impact liability as they had requested. This exemption was important to the industry because of the bind it would impose on the risk-based methods that underlie insurance rates. In order to avoid disparate impact claims, insurers would have to collect racial and other protected characteristic data to revise underwriting models, so to account for any statistical disparities the data sets revealed. At the same time, changing rates because of the disparate statistical effect they could have on a protected class would be blatant differential treatment based on membership in the protected class, which would violate the FHA.

For these reasons, the insurance industry sought an exemption so that it could continue using rates based on traditional risk-factors. HUD denied the exemption in its final 2013 regulations, ultimately stating that it could handle these insurance issues by adjudicating them on a case-by-case basis because defining the scope of any categorical exemption would be "practically impossible."⁶³

Pending in federal court currently is an insurance case that would resolve the divergence on which this paper is based: whether the 2013 HUD regulations unlawfully impose liability in excess of the Supreme Court's limitations in *TDHCA*.⁶⁴ The insurance industry attacked the first and third prongs of the HUD regulations as being unlawful under the FHA.

They first argue that HUD's regulations are unlawful under the FHA because the regulations permit a *prima facie* showing so long as a plaintiff demonstrates that "a challenged practice caused or predictably will cause a discriminatory effect."⁶⁵ In contrast, the Supreme Court in *TDHCA* stated that, to make a *prima facie* case, a plaintiff must meet the "robust causality standard" so to ensure that a defendant is not "held liable for racial disparities they did not create."⁶⁶ Thus, the plaintiffs argue, the HUD regulations allow a plaintiff to make a *prima facie* case by just showing a statistical disparity in a situation without showing that the defendant's policy actually caused that effect as required by the Supreme Court.

Second, they contend that the third prong allows plaintiffs to displace the valid objectives and policies of a housing provider. The HUD regulations, at the third stage, allow the plaintiff to show that there is a

less discriminatory means of achieving the defendant's stated legitimate objective.⁶⁷ The Supreme Court, however, stated that disparate impact claims should not be used to "second-guess which of two reasonable approaches" a defendant should follow in achieving its objective.⁶⁸ The insurers argue that the HUD regulations do just that, by allowing them to propose alternative—and potentially less effective—means of the defendant achieving its stated objective. The parties currently both have cross motions for summary judgment pending before the court.

Criminal Screening

The recent decisions of courts accepting that criminal screening policies can cause a disparate impact should make housing providers give due consideration to HUD's April 2016 Criminal Screening Guidance when drafting their policies.⁶⁹ Both courts to analyze the issue have denied the defendant's motion to dismiss, finding that, given the disproportionate conviction rate for protected classes, a criminal screening policy that broadly rejects an applicant with a criminal conviction is a policy that will cause a disparate impact.

Housing providers, can, however, take some comfort in the fact that the means by which the defendants applied a criminal screening policy in each of these cases was contrary to the Criminal Screening Guidance's recommendations. This fact indicates that compliance with the Guidance, for example, by imposing time limitations and categorizing specific types of objectionable crimes, probably would have led the courts to rule differently.

For example, in one case, a new management company imposed a policy that all current tenants and future applicants had to submit to a criminal screening check that looked back on their records ninety-nine years.⁷⁰ Such a policy would clearly violate the HUD Guidance as being overly broad in duration. In the second case, a defendant violated its own screening policy by denying an applicant for a conviction that was older than the policy's three year look back period.⁷¹ This mistake shows how not following a policy can lead to disparate impact exposure.

Despite this recognition of the connection between criminal convictions and race, a court rejected the connection between legal status and race in a case where plaintiffs contended that a housing provider's screening policy requiring documentation of legal status caused a disparate impact on the race of Latinos.⁷² The court held the *TDHCA* robust causality standard was not satisfied because the disparate effects of a policy targeting illegal aliens was incidental to, and not because of, being Latino.⁷³

These cases demonstrate that when analyzing criminal screening policies under disparate impact theory, courts appear to accept HUD's conclusion that racially disproportionate conviction rates justify allowing liability for unnecessarily broad screening policies.

Conclusion

Disparate impact liability has undergone a dynamic change in the past few years. Five years ago, there was fractured case law about how to analyze liability, with some courts not even recognizing it. HUD then issued regulations to standardize the fractured case law, shortly followed by the Supreme Court's own pronouncement. The conflict between HUD and the Supreme Court's standard created a divergence between a lower and higher standard by which to judge disparate impact claims.

The courts since *TDHCA* have largely aligned with the Supreme Court's requirement that plaintiffs must demonstrate robust causality between the disparate impact and the challenged policy, staying true to the Court's cautionary advice to limit liability to only policies that are an "artificial, arbitrary, and unnecessary barrier" to fair housing. Although there are some outlier cases, the trend in the court decisions has been favorable to housing providers getting a disparate impact claim dismissed at the pleadings stage. The District of Columbia federal court overseeing the insurance case is of particular interest as a case that could potentially strike down the HUD rule entirely. If not that court, another future court or HUD itself will have to reconcile the divergence between the two standards and future Supreme Court decisions will probably then further shape the *TDHCA* principles.

References

¹ See Part IV.F., discussion of *Am. Ins. Ass'n v. United States Dep't of Hous. & Urban Dev.*, Docket No. 1:13-cv-00966-RJL, United States District Court for the District of Columbia.

² 42 U.S.C. § 3604.

³ *Texas Dep't of Hous. & Cmty. Affairs v. Inclusive Communities Project, Inc.*, 135 S. Ct. 2507, 2520 (2015) (collecting cases from the Second, Third, Fourth, Fifth, Sixth, Seventh, Eighth, Ninth and Eleventh Circuits).

⁴ *Inclusive Communities Project, Inc. v. Texas Dep't of Hous. & Cmty. Affairs*, 747 F.3d 275, 281 (5th Cir. 2014) (“Our sister circuits have applied multiple different legal standards to similar claims under the FHA.”).

⁵ *Mt. Holly Gardens Citizens in Action, Inc. v. Twp. of Mount Holly*, 658 F.3d 375, 382 (3d Cir. 2011); *Gallagher v. Magner*, 619 F.3d 823, 833–34 (8th Cir. 2010); *Graoch Assocs. # 33, L.P. v. Louisville/Jefferson Cty. Metro Human Relations Comm'n*, 508 F.3d 366, 374 (6th Cir. 2007); *Mountain Side Mobile Estates P'ship v. Sec'y of Hous. & Urban Dev.*, 56 F.3d 1243, 1254 (10th Cir. 1995); *Huntington Branch, N.A.A.C.P. v. Town of Huntington*, 844 F.2d 926, 936 (2d Cir. 1988).

⁶ *Huntington Branch*, 844 F.2d at 936; *Mt. Holly Gardens*, 658 F.3d at 382.

⁷ *Gallagher*, 619 F.3d at 834; *Mountain Side Mobile Estates*, 56 F.3d at 1254.

⁸ *Metro. Hous. Dev. Corp.*, 558 F.2d at 1290.

⁹ *Betsey v. Turtle Creek Assocs.*, 736 F.2d 983, 988 n. 5 (4th Cir. 1984); *Graoch Assocs.*, 508 F.3d at 371, 372–74.

¹⁰ Office of the Assistant Secretary for Fair Housing and Equal Opportunity, HUD, *Implementation of the Fair Housing Act's Discriminatory Effects Standard*, November 16, 2011, 76 Fed. Reg. 70,921, available at <https://www.federalregister.gov/documents/2011/11/16/2011-29515/implementation-of-the-fair-housing-acts-discriminatory-effects-standard>.

¹¹ 24 C.F.R. § 100.500(c)(1).

¹² *Id.* § 100.500(c)(2).

¹³ *Id.* § 100.500(c)(3).

¹⁴ *Id.* § 100.500(b).

¹⁵ *TDHCA*, 135 S. Ct. 2507.

¹⁶ *Id.* at 2523.

¹⁷ *Id.*

¹⁸ *Id.* at 2524.

¹⁹ *Id.* at 2523 (citing 78 Fed. Reg. 11476).

²⁰ *Id.* at 2524.

²¹ *Id.* at 2523.

²² *Id.* at 2524.

²³ For a complete discussion of HUD's recent activity on disparate impact theory, see White Paper dated April 2017: Recent HUD Actions on Disparate Impact Theory

²⁴ See *United States v. Mead Corp.*, 533 U.S. 218, 228 (2001) (quoting *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944)).

²⁵ Office of General Counsel Guidance on Application of Fair Housing Act Standards to the Use of Criminal Records by Providers of Housing and Real Estate-Related Transactions, April 4, 2016, available at https://portal.hud.gov/hudportal/documents/huddoc?id=hud_ogcguidappfhastandcr.pdf (hereinafter, “Criminal Screening Guidance”). For a complete discussion of Criminal Screening Policies and Disparate Impact Liability, see the NMHC/NAA White Paper titled Criminal Conviction Screening Policies Best Practices to Avoid Disparate Impact Liability dated May 2016.

²⁶ Criminal Screening Guidance, at 2–3.

²⁷ Office of General Counsel Guidance on Fair Housing Act Protections for Persons with Limited English Proficiency, September 15, 2016, at 1, available at <https://portal.hud.gov/hudportal/documents/huddoc?id=lepmemo091516.pdf> (hereinafter “LEP Guidance”).

²⁸ LEP Guidance, at 1.

²⁹ 24 C.F.R. § 100.600.

³⁰ *Id.* § 100.700(a)(1)(iii).

³¹ Applicability of the Fair Housing Act's Discriminatory Effects Standard to Insurance, 81 Fed. Reg. 69,012 (October 5, 2016), available at <https://www.gpo.gov/fdsys/pkg/FR-2016-10-05/pdf/2016-23858.pdf>.

³² *Id.* at 69,013.

³³ *Prop. Cas. Insurers Ass'n of Am. v. Donovan (PCIAA)*, 66 F. Supp. 3d 1018, 1049 (N.D. Ill. 2014).

³⁴ 81 Fed. Reg. at 69,015.

³⁵ 24 C.F.R. § 5.150.

³⁶ 42 U.S.C. § 3609(d).

³⁷ Affirmatively Furthering Fair Housing, 80 Fed. Reg. 42,272.

³⁸ *E.g.*, Local Zoning Decisions Protection Act of 2017, H.R. 482, 115th Cong. (2017).

³⁹ *TDHCA*, 135 S. Ct. at 2523.

⁴⁰ See Part IV.B., discussion of *Crossroads Residents Organized for Stable & Secure Residences (CROSSRDS) v. MSP Crossroads Apartments LLC*, No. CV 16-233 ADM/KMM, 2016 WL 3661146 (D. Minn. July 5, 2016).

⁴¹ *Am. Ins. Ass'n v. United States Dep't of Hous. & Urban Dev.*, Docket No. 1:13-cv-00966-RJL, United States District Court for the District of Columbia.

⁴² *Inclusive Communities Project, Inc. v. Texas Dep't of Hous. & Cmty. Affairs*, No. 3:08-CV-0546-D, 2016 WL 4494322 (N.D. Tex. Aug. 26, 2016). The Supreme Court remanded its seminal 2015 case back to the district court to assess the plaintiff's claims under its new disparate impact standard. There, the advocacy group Inclusive Communities Project ("ICP") alleged the Texas Department of Housing and Community Affairs allocated low income housing tax credits to developments in a way that had a disparate impact on certain races. *Id.* at 1.

Upon remand, the court recited the Supreme Court's "robust causality requirement" and indicated that demonstrating causation would be difficult in cases like this where multiple factors go into an allocation decision. *Id.* at 4 (citing *TDHCA*, 135 S. Ct. at 2523-24). The court took seriously the Supreme Court's guidance that it should not simply second-guess one of two reasonable approaches that the TDHCA reached in exercising its discretionary allocation authority. *Id.* at 5 (citing *TDHCA*, 135 S. Ct. at 2523).

The court dismissed the disparate impact claim and stressed two reasons for the importance of identifying a specific policy or practice that causes the disparate impact. *Id.* at 6. First, so that the court can evaluate whether that policy caused a statically significant disparity, and second, so that the court can fashion an appropriate remedy for the policy. *Id.* On the first point, the court dismissed the claim because ICP "failed to point to a specific, facially neutral policy that purportedly caused a racially disparate impact." *Id.* A generalized policy of discretion will not lead to disparate impact liability. *Id.* The court also noted that because ICP complained "of the results of TDHCA's exercise of discretion rather than of the existence of that discretion," the claim was actually for disparate treatment rather than disparate impact. *Id.* at 7. This case is a prime example of a court agreeing and accepting that the Supreme Court's standard is higher than that of the HUD regulations.

⁴³ *Id.* at 6.

⁴⁴ *Id.* at 4 (citing *TDHCA*, 135 S. Ct. at 2523-24).

⁴⁵ *Inclusive Communities Project, Inc. v. United States Dep't of Treasury*, No. 3:14-CV-3013-D, 2016 WL 6397643 (N.D. Tex. Oct. 28, 2016).

⁴⁶ *Id.* at 11.

⁴⁷ *Id.*

⁴⁸ *City of Joliet, Illinois v. New W., L.P.*, 825 F.3d 827 (7th Cir. 2016).

⁴⁹ *Id.* at 830 (citing *TDHCA*, 135 S. Ct. at 2523-24).

⁵⁰ *Burbank Apartments Tenant Ass'n v. Kargman*, 474 Mass. 107 (2016).

⁵¹ *Id.* at 110.

⁵² *Crossroads Residents Organized for Stable & Secure Residences (CROSSRDS) v. MSP Crossroads Apartments LLC*, No. CV 16-233 ADM/KMM, 2016 WL 3661146 (D. Minn. July 5, 2016).

Notably, the court here differed in its analysis of the applicable disparate impact standard in several ways from the other courts analyzed in this Legal Summary. First, the court recited the three prongs of the HUD framework, which other courts sparsely acknowledge or wholly omit. The court seemed to downplay the significance of the Supreme Court *TDHCA* case by merely stating that the Supreme Court incorporated "safeguards" into the HUD standard. The court also cited many pre-*TDHCA* cases in its analysis of why the plaintiffs' allegations satisfied their initial burden. These divergences from the other courts, coupled with the statistical data (albeit vague and bare) helps to explain why the defendants motion to dismiss was denied in this case.

⁵³ *City of Los Angeles v. Wells Fargo & Co.*, No. 2:13-CV-09007-ODWRZX, 2015 WL 4398858, (C.D. Cal. July 17, 2015).

⁵⁴ *City of Miami v. Bank of Am. Corp.*, 171 F. Supp. 3d 1314 (S.D. Fla. 2016). The court engaged in a unique analysis of *TDHCA*, interpreting it to impose a four pronged standard that a plaintiff must satisfy: “(1) show statistically-imbalanced lending patterns which adversely impact a minority group; (2) identify a facially-neutral policy used by Defendants; (3) allege that such policy was “artificial, arbitrary, and unnecessary;” and (4) provide factual allegations that meet the “robust causality requirement” linking the challenged neutral policy to a specific adverse racial or ethnic disparity.” *Id.* at 1320 (citing *TDHCA*, 135 S. Ct. at 2522-24). The court found the plaintiffs failed to allege facts satisfying the latter three requirements.

⁵⁵ *Cobb Cty. v. Bank of Am. Corp.*, 183 F. Supp. 3d 1332 (N.D. Ga. 2016). The court dismissed the disparate impact claim and employed the same four-prong standard used by the court *City of Miami v. Bank of America*. *Id.* at 1346.

⁵⁶ *TDHCA*, 135 S. Ct. at 2522.

⁵⁷ *Mhany Mgmt., Inc. v. Cty. of Nassau*, 819 F.3d 581 (2d Cir. 2016). Although the district court, on remand, has yet to issue a decision as to whether the plaintiffs’ disparate impact claim survives a motion to dismiss under the HUD framework, this case is a noteworthy outlier in not discussing the heightened and limited standards the Supreme Court advanced in its decision. Instead, the court exclusively relied on the HUD burden-shifting framework in analyzing the claim. It is most likely that, on remand, the district court will nevertheless align with the majority of courts and discuss the *TDHCA* limitations on disparate impact liability in its analysis.

⁵⁸ *Anthony v. City of Naples*, 2016 WL 7010949 (M.D. Fla. Dec. 1, 2016).

⁵⁹ The preferences policy that the federally subsidized Kennedy Apartments in San Francisco attempted to implement is an example of the dangers preference policies pose. In a well-intentioned move to help longtime residents combat rising rents, the city had originally proposed a preference policy for the complex allocating forty-percent of the subsidized units to residents living in the same district, or within a one-half mile of it. HUD objected to the city’s policy because it would perpetuate segregation in the already disproportionately African-American district.

The city appealed to HUD to reconsider the objection and the two sides came to a mutually agreeable resolution where the pool of eligible residents for preferences was expanded beyond the initial zone to include low income individuals in neighboring districts. By expanding the zone outside the initial majority African-American district, the new policy ensures equal access to the preferences regardless of race.

⁶⁰ *TDHCA*, 135 S. Ct. at 2522.

⁶¹ *Winfield v. City of N.Y.*, 2016 WL 6208564 (S.D.N.Y. Oct. 24, 2016). The court denied the city’s motion to dismiss the disparate impact claim, finding that the plaintiffs’ allegations made it plausible that, after discovery, they could prove the policy causes a disparate impact with complete statistical data. *Id.* at 6. The court cited to *TDHCA*’s pleading standard that a plaintiff only had to plead facts or produce statistical evidence at the pleading stage demonstrating a causal connection between the policy and discriminatory effect. *Id.* For these reasons, the plaintiffs’ allegations that the preferences policy perpetuates segregation by maintaining the status quo in neighborhoods that already suffer from segregation withstood the motion to dismiss. *Id.* The case is now in the discovery phase to further examine the effect of the preferences policy.

⁶² *Id.* at 6.

⁶³ *Prop. Cas. Insurers Ass’n of Am. v. Donovan (PCIAA)*, 66 F. Supp. 3d 1018 (N.D. Ill. 2014).

⁶⁴ After HUD issued its 2013 regulations that did not exempt the insurance industry from disparate impact liability, insurance associations sued HUD, contending that disparate impact claims are not cognizable under the FHA. *Am. Ins. Ass’n v. United States Dep’t of Hous. & Urban Dev.*, 74 F. Supp. 3d 30, 31–32 (D.D.C. 2014), *vacated and remanded* (Sept. 23, 2015). The district court agreed and held that the FHA does not allow disparate impact claims. *Id.* at 47. While on appeal, the Supreme Court issued its *TDHCA* opinion authorizing such a claim, causing the appellate court to remand the case back to the district court, where it remains today. Presently, each side has filed for summary judgment but agreed to stay the proceedings while the new HUD administration decides on how it wishes to pursue the case.

⁶⁵ 24 C.F.R. § 100.500(c)(1).

⁶⁶ *TDHCA*, 135 S. Ct. at 2523.

⁶⁷ 24 C.F.R. § 100.500(c)(3).

⁶⁸ *TDHCA*, 135 S. Ct. at 2522.

⁶⁹ A thorough discussion of compliance with HUD's Criminal Screening Guidance can be found in the NAA/NMHC White Paper dated May 2016.

⁷⁰ *Sams v. Ga W. Gate, LLC*, 2017 WL 436281 (S.D. Ga. Jan. 30, 2017).

⁷¹ *Alexander v. Edgewood Mgmt. Corp.*, 2016 WL 5957673 (D.D.C. July 25, 2016).

⁷² *De Reyes v. Waples Mobile Home Park Ltd. P'ship*, 205 F. Supp. 3d 782 (E.D. Va. 2016).

⁷³ *Id.* at 793.