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A Dream Foreclosed?

Using the Equal Credit Opportunity Act to Challenge and Prevent Foreclosures

By Jennifer D. Newton and Tamara St. Hilaire

Jennifer D. Newton
Staff Attorney/Florida Bar Foundation Leadership Institute Fellow 2010

Tamara St. Hilaire
Florida Bar Foundation Summer Fellow 2011

Florida Legal Services
2425 Torreya Drive
Tallahassee, FL 32303

850.385.7900 ext. 1806
jennifer@floridalegal.org

850.322.5616
davenport_t@hotmail.com

While much has been reported on the foreclosure crisis, one of its most disturbing aspects has been its devastating impact on communities of color. According to a 2008 report by United for a Fair Economy, the foreclosure crisis has resulted in the greatest loss of wealth for people of color in U.S. history.[1] Much of this loss of wealth resulted from subprime lenders' targeting minorities for high-cost subprime loans.[2] Minorities were more than three times as likely to be sold subprime loan products, even after controlling for income.[3] Because subprime loans represent the vast majority of recent foreclosures, minorities have been disproportionately affected by the foreclosure crisis.[4]

This disproportionate effect reveals that race is still a significant factor in determining who receives conventional financing. The Equal Credit Opportunity Act forbids creditors from considering race and other prohibited factors when extending offers of credit. Not only does the Act prohibit blatant forms of lending discrimination, but also it prohibits subtle forms of discrimination that harm people of color.

Here we first examine the factors that led to the growth of the subprime lending market, encouraging predatory lending practices that targeted communities of color. Next we discuss how these discriminatory lending practices violate the letter and spirit of

[1] Amaad Rivera et al., United for a Fair Economy, Foreclosed: State of the Dream 2008 at 1 (Jan. 15, 2008), http://bit.ly/iNg3wc.

[2] *Id.* at v.

[3] *Id.* at 14–15.

[4] Debbie Gruenstein Bocian et al., Center for Responsible Lending, Foreclosures by Race and Ethnicity: The Demographics of a Crisis 7 (June 18, 2010), http://bit.ly/iOM6Bx.

the Act. After reviewing the history of government and private enforcement of the Act, we show how advocates can use noncompliance with the Act to challenge and prevent foreclosure.

I. Credit Discrimination in Residential Mortgage Lending

Not since the Great Depression has the country seen foreclosure rates rise to those of the last five years. In a recent study, the Center for Responsible Lending reported that as many as 2.5 million homes completed foreclosure between 2007 and 2009.[5] According to the study, subprime loans accounted for approximately 64 percent of these foreclosures, despite subprime mortgages constituting only 22 percent of the originations during these years.[6]

A. The Emergence and Growth of the Subprime Lending Market

Subprime lending generally refers to the practice of lending to borrowers who are believed to pose a higher credit risk.[7] These borrowers typically have a blemished credit record or lack payment and credit history. Subprime loans have such characteristics as prepayment penalties, higher interest rates, or balloon payments. The origins of subprime lending can be traced to the late twentieth century after the invention of credit scoring and automated underwriting and after the Tax Reform Act of 1986 eliminated the tax benefits of nonhousing consumer debt.[8] The 1980 Depository Institutions Deregulation and Monetary Control Act aided in the influx of subprime lending by allowing interest rates on home mortgages and equity lines to go as high as necessary to compensate lenders for the high risk of lending to subprime borrowers.[9]

Unregulated conditions and private securitization—the practice of repackaging, pooling, and reselling loans to private investors as securities—further drove the subprime market.[10] Many subprime loans were quickly packaged and sold to investors after their origination. To increase the volume of originations, lenders compensated mortgage brokers through yield-spread premiums or volume-based compensation.[11] This effectively encouraged mortgage brokers to steer borrowers into high-priced loans whether the borrower could afford to pay the loan or not—a practice most commonly referred to as predatory lending.[12]

B. Predatory Lending in Low-Income, Minority Communities

Mortgage brokers and subprime lenders targeted vulnerable populations for high-cost subprime loans, particularly focusing on those who resided in predominantly minority or low-income neighborhoods and lacked access to mainstream sources of credit.[13] Research and cases have documented the targeting of these vulner-

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[5]*Id.*

[6]*Id.*

[7]For an overview of the subprime mortgage market, see Elizabeth Renuart et al., Stop Predatory Lending: A Guide for Legal Advocates 21 (2d ed. 2007).

[8]Kristopher S. Gerardi & Paul S. Willen, Subprime Mortgages, Foreclosures, and Urban Neighborhoods 3 (Dec. 22, 2008), http://hvrd.me/pXacEg.

[9]Elizabeth Laderman, *Subprime Mortgage Lending and the Capital Markets*, [Federal Reserve Bank of San Francisco] Economic Letter, Dec. 28, 2001, http://bit.ly/qmkLVk.

[10]*Id.*

[11]For a description of yield-spread premiums or volume-based compensation, see Renuart et al., *supra* note 7, at 31.

[12]See generally *id.* at 21–22.

[13]U.S. Department of Housing and Urban Development & U.S. Department of the Treasury, HUD-Treasury Report Recommendations to Curb Predatory Home Mortgage Lending 4–5 (2000), http://archives.hud.gov/reports/; Allen Fishbein & Harold Bunce, *Subprime Market Growth and Predatory Lending*, in Housing Policy in the New Millennium Conference Proceedings 273, 279 (Susan M. Wachter & R. Leo Penne eds., 2001), http://bit.ly/pICwxZ; Juliana Barbassa, *Report: Minorities Hit by Foreclosures*, USA Today, March 6, 2008, http://usat.ly/rnfNwG; Michelle Singletary, *Subprime Loan Epidemic Preys on Poor, Minority Homeowners*, Sun Sentinel, July 3, 2000, http://bit.ly/puncrB. See also U.S. Government Accountability Office, GAO-04-280, Consumer Protection: Federal and State Agencies Face Challenges in Combating Predatory Lending 4 (2004), http://1.usa.gov/o8j5fh.

able groups for unnecessarily expensive loans.[14] Not only were borrowers of color more likely to receive subprime loans than white borrowers, but also these borrowers were placed in subprime loans in disproportionate numbers even when they qualified for prime loans.[15] In particular, African American and Latino borrowers were, on average, 30 percent more likely to receive high-cost subprime loans than similarly situated white borrowers with the same credit profile.[16] Even more troubling, within the subprime market, borrowers of color were more likely to receive the most expensive loans and the subprime terms associated with increased default risk.[17] While the subprime lending market is often credited with being the access to credit when borrowers may have lacked the income, assets, or credit history to obtain traditional financing, the market encouraged lending practices that disadvantaged minorities, low-income families, and the elderly.[18]

II. Enforcement of the Equal Credit Opportunity Act

When predatory lenders target communities of color, they deliberately violate the Equal Credit Opportunity Act by extending unfavorable credit terms on the basis of race or color. The Act prohibits discrimination, in any aspect of credit, on the basis of race, color, religion, national origin, sex, marital status, age, public assistance status, and the exercise of rights under the Consumer Credit Protection Act.[19] The law was enacted in 1974 to protect consumers from discrimination by financial institutions.[20] The Equal Credit Opportunity Act contains strict notification requirements that creditors must follow.[21]

The Equal Credit Opportunity Act applies to virtually all aspects of a credit transaction, including practices that occur before a credit application, during application, in the decision of whether to extend credit, and after the granting of credit.[22] Failure to comply with the Act subjects a creditor to civil liability for actual and punitive damages in either an individual or class action lawsuit.[23] The Act also expressly provides for equitable relief, declaratory relief, and the recovery of punitive damages, which are capped at $10,000 in individual lawsuits and at the lesser of $500,000 or 1 percent of the creditor's net worth in class action lawsuits.[24] Prevailing plaintiffs may recover reasonable attor-

[14]See *City of Memphis v. Wells Fargo Bank National Association*, No. 09-2857-STA, 2011 U.S. Dist. LEXIS 48522 (W.D. Tenn. May 4, 2011); *Mayor of Baltimore v. Wells Fargo Bank National Association*, No. JFM-08-62, 2011 U.S. Dist. LEXIS 44013, at *13 n.4 (D. Md. April 22, 2011) (alleging discriminatory lending practices targeting predominantly African American neighborhoods); *Woodworth v. Bank of America National Association*, No. 09-2857-STA, 2011 U.S. Dist. LEXIS 43255 at *32 (D. Or. March 23, 2011) (alleging loans made on terms and conditions less favorable than those offered to other applicants because income was derived exclusively from public assistance program); *NAACP v. Ameriquest Mortgage Company*, 635 F. Supp. 2d 1096 (C.D. Cal. 2009); *Ware v. Indymac Bank Federal Savings* Bank, 534 F. Supp. 2d 835, 840 (N.D. Ill. 2008); Debbie Gruenstein Bocian et al., Center for Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 3 (May 31, 2006), http://bit.ly/oVn4sV ("African-American and Latino borrowers are at greater risk of receiving higher rate loans than white borrowers, even after controlling for legitimate risk factors."); U.S. Government Accountability Office, *supra* note 13, at 3 (stating that predatory loans are "often targeted at the elderly, minorities, and low-income homeowners").

[15]Renuart et al., *supra* note 7, at 21.

[16]Bocian et al., Foreclosures, *supra* note 4, at 6.

[17]*Id*.

[18]See Gerardi & Willen, *supra* note 8 (attributing substantial increase in homeownership by minorities to subprime lending). But see generally Bocian et al., Foreclosures, *supra* note 4; Renuart et al., *supra* note 7.

[19]Equal Credit Opportunity Act, 15 U.S.C. § 1691(a) (2006).

[20]*Midlantic National Bank v. Hansen*, 48 F.3d 693, 699 (3d Cir. 1995); *Brown v. Interbay Funding Limited Liability Company*, 417 F. Supp. 2d 573, 578 (D. Del. 2006).

[21]See 15 U.S.C. § 1691(d).

[22]15 U.S.C. § 1691 (making it unlawful for any creditor to discriminate against any applicant with respect to any aspect of a credit transaction). See also Deanne Loonin & Chi Chi Wu, Credit Discrimination 85 (4th ed. 2005), for a discussion of the various stages in a credit application and the Equal Credit Opportunity Act's applicability.

[23]15 U.S.C. § 1691e.

[24]*Id.*

ney fees and costs from the defendant.[25] Before July 2010, the Act had a two-year statute-of-limitations period for filing a claim.[26] The Dodd-Frank Act of 2010 extended this period to five years.[27]

Congress conferred enforcement authority of the Equal Credit Opportunity Act on several federal banking regulatory agencies, the Federal Trade Commission, and the U.S. Department of Justice.[28] Private parties may bring civil suits to enforce the Act.[29] Despite this regulatory authority, enforcement of the Act has been nonexistent over the years. From 2005 to 2009, enforcement agencies settled only eight fair lending cases.[30] Private enforcement of the Act has similarly lagged. In the last twenty-four years, there have been only 952 reported cases under the Act, compared to 1,515 cases reported under the Truth in Lending Act in 2010 alone.[31]

Nevertheless, the disproportionate effect of the foreclosure crisis on minorities and other vulnerable groups has called national attention to the need for revisiting fair lending laws. In 2010 the Justice Department's Civil Rights Division announced a new Fair Lending Unit in its Housing and Civil Enforcement Section.[32] Congress established the Consumer Financial Protection Bureau—a new federal agency that is also empowered to enforce the Act and other fair lending laws.[33] The number of private enforcement cases reported has significantly increased in recent years. Of the 952 cases reported since 1986 under the Act, 13 percent were reported in 2010 alone.[34]

III. Raising Noncompliance with the Equal Credit Opportunity Act to Prevent Foreclosure

Foreclosing varies among states. In some states, foreclosing is judicial. In other states, foreclosing involves no court action so that a lender may foreclose on a property without a court order. Regardless of the method, both the antidiscriminatory provisions and the notification requirements of the Equal Credit Opportunity Act may be used either affirmatively or as a defense to a foreclosure action. The Act affords borrowers with a way to hold liable multiple parties who participate in a discriminatory residential lending transaction.

A. Judicial Foreclosure Proceedings: Affirmative Defense or Counterclaim

In judicial foreclosure proceedings a homeowner raises defenses to a foreclosure prior to a foreclosure judgment—usually through the use of affirmative defenses or counterclaims. However, courts are split on whether a violation of the Equal Credit Opportunity Act may be used as an affirmative defense or may

[25] *Id.*

[26] *Id.* § 1691e(f).

[27] See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1085, 124 Stat. 1376, 2085 (2010) (to be codified at 15 U.S.C. § 1691e(f)). Nothing in Dodd-Frank evidences a legislative intent to apply the limitations period retroactively. The new five-year limitations period may not apply to transactions before the effective date of Dodd-Frank.

[28] 15 U.S.C. §§ 1691c and 1691e.

[29] *Id.* § 1691e(a).

[30] U.S. Government Accountability Office, GAO-09-704, Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts 53 (2009), http://1.usa.gov/riYOMT.

[31] A search on LEXIS in "US District Court Cases, Combined" for "ECOA OR 'Equal Credit Opportunity Act'" from "1/1/1986" to "12/31/2010" yielded 952 results, compared to a LEXIS search in "US District Court Cases, Combined" for "TILA OR 'Truth in Lending Act'" from "1/1/2010" to "12/31/2010" yielding 1,515 results.

[32] Thomas E. Perez, U.S. Department of Justice, The Attorney General's 2010 Annual Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments of 1976, at 1 (2011), http://1.usa.gov/plHhAu.

[33] Dodd-Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C.A. § 5491 (West 2011).

[34] A search on LEXIS in "US District Court Cases, Combined" for "ECOA OR 'Equal Credit Opportunity Act'" from "1/1/1986" to "12/31/2010" yielded 952 results. Using the same search terms, but only for the year 2010, yielded 130 results, or 13 percent of the 952 total reported cases.

be asserted only as a counterclaim.[35] A number of courts have held that a violation of the Act cannot be used as an affirmative defense to invalidate a debtor's underlying loan obligation.[36] Such cases generally hold that a debtor may assert a violation of the Act only as a counterclaim for damages in a collection action, which must be filed within the statutory time frame. However, if the statute of limitations has run, some courts have left open the option for borrowers to assert under the doctrine of recoupment a violation of the Act as an affirmative defense.[37] The doctrine of recoupment allows a defendant to defend against a collection suit by asserting damages up to the amount of the creditor's claim.[38]

Another line of cases approves the use of the Act as an affirmative defense even after the two-year statute of limitations for filing a claim has passed. These cases hold that a borrower may assert a claim under the Act as an affirmative defense to the debt, based on the principle that a contract that was procured in violation of a statute is void and unenforceable. In these cases, courts have refused to enforce the underlying obligation.[39]

B. Nonjudicial Foreclosure Proceedings: Statute-of-Limitations Bar

In nonjudicial foreclosure states, a lender can foreclose on a homeowner's property without the court's supervision. An aggrieved homeowner typically needs to file an affirmative action under the Equal Credit Opportunity Act for an injunction to stop the foreclosure.[40] Advocates in nonjudicial foreclosure states should therefore give special consideration to the Act's limitation period. This lawsuit must generally be filed within two years of a violation.[41] Courts are split as to when the period begins to run. A majority of courts have found that the statute begins to run when the credit applicant becomes aware of the violation of the Act.[42] In other cases, courts have held

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[35]William R. Naeher, *Recent Developments Under the Equal Credit Opportunity Act*, 10 Probate and Property 44, 45–46 (1996).

[36]See, e.g., *Federal Deposit Insurance Corporation v. 32 Edwardsville Incorporated*, 873 F. Supp. 1474, 1480 (D. Kan. 1995) ("ECOA does not provide for the invalidation of a guaranty as a remedy for an ECOA violation, and defensive use of the ECOA in this case is therefore impermissible."); *Silverman v. Eastrich Multiple Investor Fund Limited Partnership*, 857 F. Supp. 447, 453 (E.D. Pa. 1994) (violation of Equal Credit Opportunity Act cannot be asserted as affirmative defense); *Riggs National Bank of Washington, D.C. v. Linch*, 829 F. Supp. 163, 169 (E.D. Va. 1993) (same).

[37]*Citgo Petroleum Corporation v. Bulk Petroleum Corporation*, No. 08-CV-654-TCK-PJC, 2010 U.S. Dist. LEXIS 82277, at *12–13 (N.D. Okla. Aug. 12, 2010); *Boyd v. U.S. Bank National Association*, No. 06-2115-KGS, 2007 U.S. Dist. LEXIS 72455 (D. Kan. Sept. 26, 2007); *Western Capital Partners Limited Liability Company v. Brookhollow Limited Liability Company*, No. 2:06cv590, 2007 U.S. Dist. LEXIS 29703, at *16–17 (E.D. Va. April 19, 2007); *Chittenden Trust Company v. Cabot*, No. 04-144-P-H, 2004 U.S. Dist. LEXIS 20461 (D. Me. Oct. 12, 2004); *Sovereign Bank v. Catterton*, No. 03-5021, 2004 U.S. Dist. LEXIS 11278, at *7–9 (E.D. Pa. April 15, 2004).

[38]*Bolduc v. Beal Bank State Savings Bank*, 167 F.3d 667, 672 (1st Cir. 1999) (citing 6 Charles Alan Wright et al., Federal Practice and Procedure § 1401 (2d ed. 1990)).

[39]See, e.g., *Integra Bank/Pittsburgh v. Freeman*, 839 F. Supp. 326, 329–31 (E.D. Pa. 1993); *Chen v. Whitney National Bank*, 36 Fla. L. Weekly D1587 (Fla. Dist. Ct. App. July 22, 2011); *Bank of the West v. Kline*, 782 N.W.2d 453, 458–63 (Iowa 2010); *Boone National Savings and Loan Association v. Crouch*, 47 S.W.3d 371, 374–76 (Mo. 2001) (citing broad equitable principles when permitting defendant to assert affirmative defense under Equal Credit Opportunity Act after statutory period had run); *Eure v. Jefferson National Bank*, 448 S.E.2d 417, 421 (Va. 1994) (defendant was entitled to assert violation of Equal Credit Opportunity Act as affirmative defense to avoid her liability because to do otherwise would be to enforce conduct that Act forbids).

[40]For a discussion of judicial and nonjudicial foreclosure proceedings, see John Rao et al., Foreclosures: Defenses, Workouts, and Mortgage Servicing (3d ed. 2010).

[41]The Equal Credit Opportunity Act's limitation period was recently extended from two to five years (see *supra* text accompanying note 27).

[42]See, e.g., *Estate of Henderson v. Meritage Mortgage Corporation*, 293 F. Supp. 2d 830, 834–35 (N.D. Ill. 2003) (allowing plaintiff to use federal discovery rule to toll statute of limitations to date plaintiff was aware of injury); *Wise v. Union Acceptance Corporation*, No. 02-0104-C-M/S, 2002 U.S. Dist. LEXIS 23335, at *17–18 (S.D. Ind. Nov. 19, 2002).

that the statute begins to run at the time of the violation.[43]

However, some courts have allowed plaintiffs to invoke the "continuing violation" exception to extend the limitation period.[44] Under the continuing violation doctrine, the limitation period may be extended if plaintiffs can show that the challenged violation is a continuing one.[45] In *Taylor v. Accredited Home Lenders* the court held that the monthly collection of payments from a loan procured in violation of the Act constituted a continuing violation and therefore tolled the limitation period.[46]

C. Who Can Be Held Liable

An aggrieved credit applicant can bring an action against any "creditor" who violates the Equal Credit Opportunity Act.[47] The Act broadly defines "creditor" to include "any person who regularly extends, renews, or continues credit; any person who regularly arranges for the extension, renewal, or continuation of credit; or any assignee of an original creditor who participates in the decision to extend, renew, or continue credit."[48] Regulation B, the Act's implementing regulation, interprets the Act's definition of "creditor" to mean simply "a person who, in the ordinary course of business, regularly participates in a credit decision including setting the terms of the credit."[49]

The Act's broad definition of "creditor" is particularly useful in today's securitization market where multiple players can be involved in a discriminatory lending transaction. The definition is extensive enough to include mortgage brokers, loan originators, and assignees to the extent that these parties had knowledge of or participated in the discriminatory lending transaction.[50] Courts have acknowledged that there is a continuum of participation in a credit decision, which can range from no involvement, to referring applications to the decision maker, to final decision making.[51]

Loan Servicers. When a mortgage is assigned in the secondary market, the mortgage is generally serviced by a bank or servicing company known as the "servicer."[52] Mortgage loan servicers can also be liable under the Equal Credit Opportunity Act for discrimination that occurs in the origination if the loan servicer participated in or had knowledge of the alleged violation.[53] Participation is likely to be found where the loan servicer is the same entity that originated the loan. Loan servicers may be liable under the Act for their own discriminatory conduct during the servicing of the loan as well as for acts that occurred in the origination.[54] Loan

[43]See, e.g., *Moore v. Wells Fargo Bank National Association*, No. 3:10-CV-94, 2011 U.S. Dist. LEXIS 14680, at *9–11 (E.D. Tenn. Feb. 14, 2011); *Claybrooks v. Primus Automotive Financial Services*, 363 F. Supp. 2d 969, 975 (M.D. Tenn. 2005); *Mills v. Equicredit Corporation*, 294 F. Supp. 2d 903, 909 (E.D. Mich. 2003).

[44]*Taylor v. Accredited Home Lenders Incorporated*, 580 F. Supp. 2d 1062 (S.D. Cal. 2008); *Ramirez v. Greenpoint Mortgage Funding Incorporated*, 633 F. Supp. 2d 922 (N.D. Cal. 2008) (claims under Equal Credit Opportunity Act and Fair Housing Act were timely under continuing violation doctrine); *Davis v. General Motors Acceptance Corporation*, 406 F. Supp. 2d 698, 705–7 (N.D. Miss. 2005) (applying continuing violation doctrine to claims under Equal Credit Opportunity Act alleging racially discriminatory markups on auto loans).

[45]*Ramirez*, 633 F. Supp. 2d at 929 ("A continuing violation … 'should be treated differently from one discrete act of discrimination.'") (quoting *Havens Realty Corporation v. Coleman*, 455 U.S. 363, 380 (1982)).

[46]*Taylor*, 580 F. Supp. 2d 1062. See also *Akhavein v. Argent Mortgage Company*, No. 5:09-cv-00634, 2009 U.S. Dist. LEXIS 61796, at *19–20 (N.D. Cal. July 18, 2009).

[47]15 U.S.C. § 1691a(e).

[48]*Id.*

[49]Equal Credit Opportunity Act (Regulation B), 12 C.F.R. § 202.2(l) (2011).

[50]15 U.S.C. § 1691a(e). See also 12 C.F.R. § 202.2(l) ("creditor" includes a creditor's assignee, transferee, or subrogee who participates in decision to extend credit).

[51]See *Treadway v. Gateway Chevrolet Oldsmobile Incorporated*, 362 F.3d 971, 980 (7th Cir. 2004).

[52]See Renuart et al., *supra* note 7, at 36.

[53]15 U.S.C. § 1691a(e).

[54]*Id.* ("creditor" includes any person who regularly *continues* credit).

servicers have already come under fire for loss mitigation and foreclosure practices alleged to be discriminatory.[55]

Identifying the Real Party in Interest. Whether noncompliance with the Equal Credit Opportunity Act is raised defensively or in an affirmative action, advocates must hold the actual owner of the loan liable when challenging or seeking to prevent a foreclosure. Only the actual legal owner of the loan has the right to foreclose on the mortgage or deed of trust.[56] Residential foreclosure actions are typically filed in the name of the homeowner's loan servicer. In today's securitization market, the legal owner may or may not be the homeowner's mortgage servicer; therefore, when seeking to extinguish a lender's foreclosure rights, advocates should be mindful to identify and include the owner of the loan.[57] The legal owner may not be the same entity that originated the loan, but under the Act a mortgage owner can be held liable not only for its own discriminatory conduct but also for the conduct of various third parties if the owner participated in or had knowledge of the discriminatory transaction.[58] Furthermore, owners can be held liable for the actions of a loan servicer under agency principles.[59]

D. Identifying Discrimination

Despite the broad reach of the Equal Credit Opportunity Act, the most challenging part of an advocate's claim is identifying and proving the discrimination. In residential lending, discrimination can take on many forms. It can consist in denying an applicant a home loan because of the applicant's race, age, or other prohibitive factor; encouraging or steering a protected group away from one type of loan product to another; using discriminatory application procedures; using a credit evaluation system that discriminates on the basis of any prohibited factor; pricing and setting credit terms based on race or other prohibited factors; or using discriminatory servicing and collection practices.[60] While this list is not meant to be exhaustive, it does emphasize that discrimination can occur at almost any point in the life cycle of the loan. Therefore advocates defending against or seeking to prevent a foreclosure should engage in a thorough fair lending analysis of the client's loan, including all the facts and circumstances that led to the loan origination, the origination itself, and the loan servicing and collection practices of the lender.

Advocates should note, however, that the Equal Credit Opportunity Act does not prohibit all forms of discrimination. A vital component of a claim is discrimination on the basis of a protected class.[61] However, courts have allowed other applicants not covered under the Act to assert claims if they have been directly harmed by a creditor's unlawful discrimination of others.[62] This is an important point not to be missed—a claim under the Act may be brought by *any applicant* who can establish standing.[63] In *Cherry v. Amoco Oil* the court held that a Caucasian woman who alleged that she was denied a credit card on the basis of the geographic area in which she

[55]See, e.g., *Adams v. U.S. Bank*, No. 10-10567, 2010 WL 2670702 (E.D. Mich. July 1, 2010) (alleging that bank failed to provide loan modification due to race and pretended that offer under Home Affordable Modification Program did not exist); *Mbaba v. Indymac Federal Bank Federal Savings Bank*, No. 1:09-CV-01452-OWW-GSA, 2010 WL 424363 (E.D. Cal. Jan. 27, 2010) (alleging that bank set higher interest rates for modifications to minorities and otherwise offered less favorable terms).

[56]See Rao et al., *supra* note 40, at 371.

[57]*Id.*

[58]12 C.F.R. § 202.2(l) ("creditor" includes any person who regularly participates in decision to extend credit).

[59]See *Boyd v. U.S. Bank National Association*, No. 10 C 3367, 2011 WL 1374986, at *9 (N.D. Ill. April 12, 2011) (refusing to dismiss mortgage owner from suit brought under Equal Credit Opportunity Act because complaint alleged that servicer, in taking unlawful actions against plaintiff, was acting as mortgage owner's agent).

[60]See generally Loonin & Wu, *supra* note 22, at 85–165.

[61]15 U.S.C. § 1691(a)(1).

[62]See *Cherry v. Amoco Oil Company*, 481 F. Supp. 727 (N.D. Ga. 1979).

[63]*Id.*

lived—the area was largely inhabited by African Americans—had standing to claim that the denial of her credit application was on the grounds of racial discrimination.[64] In the same way, applicants who have been targeted for predatory loans because they reside in areas that are largely populated by protected class members may be able to state a claim under the Act even if they are not members of the protected class themselves.

E. The Proof

Even after identifying a discriminatory act or practice, advocates may face a difficult task in proving the discrimination. In analyzing discrimination claims brought under the Equal Credit Opportunity Act, courts apply the analytical framework of Title VII of the Civil Rights Act of 1964, meaning that the plaintiff bears the burden of proving intentional discrimination.[65]

Disparate Treatment. In the absence of direct evidence of discrimination, a plaintiff may prove discrimination by circumstantial evidence of disparate treatment or disparate impact.[66] In disparate treatment cases, courts apply a four-prong test requiring plaintiffs to demonstrate that (1) they are members of a protected class; (2) they applied for an extension of credit; (3) they were rejected despite their qualifications; and (4) others of similar credit status were extended credit or given more favorable treatment.[67] If the plaintiff can establish a prima facie case of disparate treatment, the burden shifts to the defendant to produce a legitimate, nondiscriminatory reason for its actions.[68] If the defendant meets this burden, then the plaintiff must present substantial evidence that the defendant's justification is pretextual—either by showing that a discriminatory reason more likely motivated the creditor or by showing that the explanation offered by the creditor is frivolous.[69]

Disparate Impact. Despite the banking industry's recent contention that disparate impact claims are not cognizable under the Equal Credit Opportunity Act, an overwhelming majority of courts have allowed plaintiffs to assert claims using disparate impact theory.[70] In disparate impact cases, plaintiffs must show the disparate effect of a creditor's specific practice by demonstrating a significant discrepancy between the number of protected class members in the creditor's entire applicant pool and the number of protected class members to whom the creditor has actually extended credit.[71] While disparate claims can be a powerful weapon against subtle discrimination, these claims have typically required

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[64]*Id.*

[65]See *Cooley v. Sterling Bank*, 280 F. Supp. 2d 1331, 1338 (M.D. Ala. 2003) (concluding that Title VII's analytical approach applies to discrimination claims under Equal Credit Opportunity Act); *Gross v. U.S. Small Business Administration*, 669 F. Supp. 50, 52 (N.D.N.Y. 1987) ("[C]ourts have generally required proof in ECOA cases to conform to the traditional Title VII tests.").

[66]*Floyd-Keith v. Homecomings Financial Limited Liability Company*, No. 2:09cv769-WKW, 2010 WL 3927596, at *3 (M.D. Ala. Sept. 17, 2010).

[67]*Id.* (citing *McDonnell Douglas Corporation v. Green*, 411 U.S. 792, 802–4 (1973)). See also *Hilliard v. Vilsack*, No. 5:10-CV-202-BO, 2011 WL 474588 (E.D.N.C. Feb. 4, 2011).

[68]*Floyd-Keith*, 2010 WL 3927596, at *3 (citing *McDonnell Douglas Corporation v. Green*, 411 U.S. 792, 802–4 (1973)).

[69]*Id.*

[70]For a discussion on the banking industry's attack on disparate impact race discrimination claims under the Equal Credit Opportunity Act as well as the Fair Housing Act, see Michael Aleo & Pablo Svirsky, *Foreclosure Fallout: The Banking Industry's Attack on Disparate Impact Race Discrimination Claims Under the Fair Housing Act and the Equal Credit Opportunity Act*, 18 Boston University Public Interest Law Journal 1 (2008). For examples of courts rejecting the banking industry's contention, see *Budnick v. Town of Carefree*, 518 F.3d 1109 (9th Cir. 2008) (stating necessary elements of a prima facie case of disparate impact under Fair Housing Act); *National Community Reinvestment Coalition v. Accredited Home Lenders Holding Company*, 573 F. Supp. 2d 70 (D.D.C. 2008) (finding *Smith v. City of Jackson*, 544 U.S. 228 (2008), does not preclude disparate impact claims under Fair Housing Act); *Ramirez*, 633 F. Supp. 2d 922 (disparate impact claims cognizable under both Equal Credit Opportunity Act and Fair Housing Act).

[71]*Taylor*, 580 F. Supp. 2d 1062.

plaintiffs to show strong statistical evidence to demonstrate a discrepancy between protected class members and the applicant pool.[72] However, in a few recent decisions, courts have been less stringent in their scrutiny of the kinds of statistical evidence needed to establish a prima facie case.[73] In *Taylor v. Accredited Home Lenders Incorporated* the court held that the plaintiff could rely on national reports that documented the predatory practices of subprime lenders to establish the statistical evidence needed to state a disparate impact claim.[74]

Reverse Redlining Cases. Predatory lending that targets communities of color is often referred to as "reverse redlining."[75] Typically not involving a rejection of credit, reverse redlining instead involves the granting of credit, but on very unfavorable terms. Courts have traditionally followed the approach taken in *Matthews v. New Century Mortgage Corporation* to assess reverse redlining discrimination claims, under which plaintiffs must show that (1) they are members of a protected class; (2) they applied for and were qualified for a loan; (3) the loans were given on unfavorable terms; and (4) the creditor continues to loan to similarly situated persons on favorable terms.[76] However, if plaintiffs can show that the lender intentionally targeted them for unfair loans on a prohibited basis, they will not need to show that the lender loans to similarly situated persons on more favorable terms. Recent reverse redlining decisions have departed from *Matthews*; these cases instead use disparate impact analysis to determine whether a reverse redlining plaintiff can show a discriminatory effect from a lender's practice.[77]

F. The Equal Credit Opportunity Act's Notification Requirements

The Equal Credit Opportunity Act establishes strict notification requirements that creditors must follow with respect to applications for credit. The Act requires that, within thirty days of receiving a complete application for credit, a creditor must notify the applicant of the action taken on the application. If the action taken on the application is adverse, the Act requires the creditor to send an adverse action notice containing a written statement of denial.[78] The notice must state the specific reasons for the denial or identify the person or office from which a statement of the reasons for the denial may be obtained.[79] Unlike the antidiscrimination provisions, the notification requirements of the Act do not require an allegation of discrimination to be pled.[80]

Bait-and-Switch Tactics. The adverse action notice requirements of the Equal Credit Opportunity Act can be particu-

[72]See *Garcia v. Johanns,* 444 F.3d 625 (D.C. Cir. 2006) (dismissing claim for disparate impact because statistics failed to account for variables that affected analyses of whether fewer Hispanic farmers were U.S. citizens, had worse credit, and had less experience).

[73]See *Taylor*, 580 F. Supp. 2d 1062. See also *Hernandez v. Sutter West Capital*, No. C 09-03658 CRB, 2010 WL 3385046 (N.D. Cal. 2010) (plaintiff's reliance on a study from Center for Responsible Lending that found Hispanics received loans worse than those received by similarly situated Caucasian borrowers was sufficient to make disparate impact claim plausible on its face).

[74]*Taylor*, 580 F. Supp. 2d 1062.

[75]See e.g., Andrew Lichtenstein, *United We Stand, Disparate We Fall: Putting Individual Victims of Reverse Redlining in Touch with Their Class*, 43 Loyola of Los Angeles Law Review 1339 (2010) (discussing reverse redlining as new face of lending discrimination).

[76]*Matthews v. New Century Mortgage Corporation*, 185 F. Supp. 2d 874 (S.D. Ohio 2002). For a discussion on reverse redlining jurisprudence, see Raymond H. Brescia, *Subprime Communities: Reverse Redlining, the Fair Housing Act and Emerging Issues in Litigation Regarding the Subprime Mortgage Crisis*, 2 Albany Government Law Review 164 (2009), http://bit.ly/nLOkCw.

[77]See e.g., *Hernandez*, 2010 WL 3385046; *Taylor*, 580 F. Supp. 2d 1062; *Ramirez*, 633 F. Supp. 2d 922.

[78]15 U.S.C. § 1691(d)(2).

[79]*Id.* § 1691(d)(2)(B).

[80]*Kivel v. Wealthspring Mortgage Corporation*, 398 F. Supp. 2d 1049 (D. Minn. 2005); *Cannon v. Metro Ford Incorporated*, 242 F. Supp. 2d 1322 (S.D. Fla. 2002).

larly useful in challenging a foreclosure where the lender has used "bait-and-switch tactics" to procure the loan. "Bait and switch" occurs when a lender presents a borrower with a set of loan terms some time during the loan application and then, at the closing or shortly before, presents the borrower with a new set of terms that the borrower has not had time to review.[81] The Act defines "adverse action" to mean a "refusal to grant credit in substantially the amount or on substantially the terms requested in an application."[82] Thus a lender who changes the terms of a loan from those that were expressly agreed to, or originally requested, by the borrower could be deemed to have taken adverse action.[83]

However, when using the notice provisions to challenge a creditor's bait-and-switch practices, advocates should be aware that under Regulation B an adverse action does not occur if the applicant *uses* or *expressly accepts* the credit offered.[84] Therefore, in circumstances in which a borrower has been coerced into accepting and using the loan with the new terms, the borrower may be unable to use the Equal Credit Opportunity Act's notice provisions to challenge the validity of the loan. However, in such cases, advocates should examine whether the lender communicated the new terms within the thirty-day statutory time frame. Under the Act, a creditor must notify an applicant of a counteroffer within thirty days of receiving a completed application.[85] For borrowers, a violation of the timing requirement can be a separate, independent claim under the Act.[86]

Applicability to Loan Modifications. The foreclosure crisis has brought tremendous scrutiny to loan servicers regarding their administration of loss mitigation programs. Loss mitigation generally refers to a loan servicer's efforts to mitigate or prevent foreclosure. A loan modification is the loss mitigation tool most often used by loan servicers to help homeowners keep their homes and avoid foreclosure. Because loan modifications often involve some sort of deferral of payment, whether the Equal Credit Opportunity Act and Regulation B apply is unclear. In a consumer letter in December 2009 the Federal Reserve Board advised financial institutions that the Act's adverse action notice requirements apply to the U.S. Department of the Treasury's Home Affordable Modification Program and other loan modification programs.[87] According to the Federal Reserve Board's interpretation, a loan modification by a loan servicer would constitute an "extension of credit" under the Act because under a loan modification the servicer extends the right to defer payment of a debt by capitalizing accrued interest and certain escrow advances, reducing the interest rate, extending the loan term, or providing for principal forbearance.[88] The Federal Reserve Board's interpretation has been accepted by several courts since loan servicers' noncompliance with the Act's adverse action provisions has increasingly been the subject of litigation.[89]

[81]See Frederick L. Miller, *Bait and Switch in the Mortgage Market: Coping with High-Rate Sleight of Hand*, Michigan Bar Journal, Oct. 2006, at 21 (2006), http://bit.ly/nETyTe.

[82]15 U.S.C. § 1691(d)(6).

[83]See, e.g., *Johnson v. Equity Title and Escrow Company of Memphis*, 476 F. Supp. 2d 873 (W.D. Tenn. 2007) (defendants' failure to give notice under Equal Credit Opportunity Act in bait-and-switch scheme was sufficient to state claim).

[84]12 C.F.R. § 202.2(c)(1)(i).

[85]15 U.S.C. § 1691(d)(1).

[86]*Newton v. United Companies Financial Corporation*, 24 F. Supp. 2d 444 (E.D. Pa. 1998).

[87]Letter from Sandra F. Braunstein, Director, Division of Consumer and Community Affairs of the Federal Reserve Board, to Officers and Managers in Charge of Consumer Affairs Sections (Dec. 4, 2009), http://1.usa.gov/pEvgsA.

[88]*Id.*

[89]See, e.g., *Boyd*, 2011 WL 1374986; *Bourdelais v. J.P. Morgan Chase Bank National Association*, No. 3:10CV670-HEH, 2011 U.S. Dist. LEXIS 35507 (E.D. Va. April 1, 2011); *Davis v. Citimortgage Incorporated*, No. 10-12136, 2011 WL 891209 (E.D. Mich. March 11, 2011).

However, because Regulation B's definition of "adverse action" excludes actions taken in connection with an applicant's default or delinquency, the Federal Reserve Board concludes that notice is not required if the applicant is currently delinquent or in default.[90] This exclusion effectively limits the usefulness of the notice provisions for borrowers at risk of foreclosure since they are typically behind in their mortgage payments. If the servicer violates the timing requirements of the Equal Credit Opportunity Act when responding to the borrower's loan modification application, the borrower can raise a separate, independent claim for such a violation.[91]

■ ■ ■

The absence of fair lending enforcement and the deregulation of the subprime lending market encouraged lending practices that disadvantaged minorities and other vulnerable groups. As a result, a disproportionate number of minorities have lost their homes to foreclosure, and many more remain at risk. The Equal Credit Opportunity Act can be a powerful tool for preventing further foreclosures and ending this systematic targeting of the most vulnerable groups in society. However, more government enforcement is needed to ensure that lenders and other players in the residential lending market know that they may no longer engage in illegal discriminatory practices. Until then, advocates can use the Act to transform this subprime lending crisis into a win for the unfairly targeted consumers and restore the dreams that foreclosures threaten to shatter.

[90] Braunstein, *supra* note 87.

[91] See *Coulibaly v. J.P. Morgan Chase Bank National Association*, 2011 WL 3476994, at *16 (D. Md. Aug. 8, 2011).

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