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Fairness in Financial Services: Racism and Discrimination in Banking

Chair Brown, Ranking Member Toomey, and distinguished Members of the Committee, thank you for the opportunity to provide my testimony on "Fairness in Financial Services: Racism and Discrimination in Banking."

My name is Devon Westhill and I am the president and general counsel of the Center for Equal Opportunity. CEO is a non-partisan, non-profit research and educational organization that for nearly 30 years has conducted studies and produced reports, monitored and advised on government action, and educated the public with the goal of promoting colorblind equal opportunity and nondiscrimination in America.

That mission is of both professional and personal importance to me. I have written and spoken widely on this topic including before the U.S. Congress earlier this year on discrimination and the civil rights of Asian Americans.[1] More fundamentally, I am a black man from the American South with a Vietnamese wife with whom I share, like many others in this country, two beautifully multiracial babies.

My primary concern today is how the mission to promote nondiscrimination is carried out. In particular, I am worried about the decision of the Consumer Financial Protection Bureau (CFPB) to utilize a disparate impact analysis to identify unlawful discrimination in financial services.

I will comment on why I think the concept is generally problematic. I will then cover potential issues I see with the CFPB implementation of disparate impact. I close by suggesting a better way forward and a warning of potential legal risks.

I. DISPARATE IMPACT GENERALLY

Disparate impact claims are distinct from disparate treatment claims because plaintiffs are not required to show any intent to discriminate under disparate impact theory. To establish a disparate impact claim, a government agency or private plaintiff must show that a practice or policy that is nondiscriminatory by its terms, in its intent, and in its application disparately affects members of a protected class. If a claimant shows a disparate effect on a protected class, typically the defendant must offer a "legitimate business justification" for the practice or policy. If the defendant satisfies this burden, then the claimant must demonstrate either that the justification is phony or that another practice known to the defendant both serves the same business purpose and has a smaller disparate effect on the protected class. It need not be alleged nor proved, and it does not even matter if the defendant proves that there was no discriminatory motive.

i. It is hardly ever a question of whether disparate impact will result from a decision or policy but instead, by how much and whether it is a direct cause.

Disparity is not discrimination.

[1] Discrimination and the Civil Rights of the Muslim, Arab, and South Asian American Communities: Hearing Before House Committee on the Judiciary, Subcommittee on the Constitution, Civil Rights, and Civil Liberties, 117 Cong. 1 (2022) (Statement of Devon Westhill) https://www.congress.gov/117/meeting/house/114438/witnesses/HMTG-117-JU10-Wstate-WesthillD-20220301.pdf.

It makes little sense to equate imbalances in one way or another, such as in the racial composition of loan recipients, with discrimination. Imbalances often have a multitude of contributing factors and do not always disfavor minorities. The sentiment is well summed up, as so often is the case, by economist Thomas Sowell in his book *Discrimination and Disparities*:

"If there is not equality of outcomes among people born to the same parents and raised under the same roof, why should equality of outcomes be expected—or assumed—when conditions are not nearly so comparable?"[2]

Indeed, to disregard this obvious truth leads to topsy-turvy unintended consequences as Justice Samuel Alito cogently illustrated in his dissent in *Texas Department of Housing and Community Affairs v. Inclusive Communities Project, Inc.*[3] where he wrote: "No one wants to live in a rat's nest."[4] He was referencing the earlier *Gallagher v. Magner* case involving a claim by slumlords in St. Paul, Minnesota that the city's efforts to combat rodent infestation would have a disparate impact on racial minorities because of the resulting rent increases for them.[5] Justice Alito concluded: "Something has gone badly awry when a city can't even make slumlords kill rats without fear of a lawsuit."[6]

II. CFPB USE OF DISPARATE IMPACT MAY HARM MINORITIES MOST

i. Encourage race-based decision-making in financial services.

The outcome-focused approach to disparate impact analysis disincentivizes for potential defendants the use of legitimate and race-neutral policies and instead, encourages race-based decision making—just the opposite of what civil rights laws like the Equal Credit Opportunity Act (ECOA) are meant to do—for fear of liability. Put more directly, creditors will be perversely incentivized to judge consumers in part by the color of their skin rather than, as should be the case, their financial risk based on generally accepted credit assessment in order to achieve a predetermined racial balance. Taking race into consideration in making any decision has never been a boon to minorities in America.

ii. Creating profound business uncertainty and whiplash that flows to consumers.

With the change of political administrations, the racial or ethnic balance required to satisfy disparate impact analysis is subject to change. There is no limiting principle that restrains any given administration from requiring businesses ensure the numbers come out in any particular way. For example, one administration, under a disparate impact regime, may see fit to require creditors ensure Asian American consumers receive loans at a rate commensurate with their representation in the general population while another may demand the rate be commensurate with the regional population. Still others may require parity with state or local populations.

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[2] Thomas Sowell, DISCRIMINATION AND DISPARITIES (2018).
[3] Texas Dep't of Housing and Community Affairs v. Inclusive Communities Project, Inc., 576 U.S. 519 (2015).
[4] *Id* at 557 (Alito, J., dissenting).
[5] Gallagher v. Magner, 619 F.3d 823 (8th Cir. 2010).
[6] Inclusive Communities, 576 U.S. 519 at 558 (Alito, J., dissenting).

Moreover, if the precedent is established such that this change can be effectuated outside of formal notice-and-comment rulemaking, as the CFPB has done by merely publishing an updated supervision and examination manual,[7] it can and will be done on a whim causing substantial uncertainty among regulated entities and whiplash effect that benefits no one and perhaps, places burdens on minorities most.

iii. Disregard for plain language of the ECOA and caselaw.

The Supreme Court has consistently held that statutes that provide a disparate impact cause of action contain "effects" or "results" language like the Court has found in the Fair Housing Act, Age Discrimination in Employment Act, and Title VII of the Civil Rights Act of 1964. [8] Conversely, the Court has refused to hold disparate impact claims cognizable under statutes that lack such language such as Title VI. The ECOA, like Title VI, contains no effects-based or consequences-oriented language.[9]

iv. Disparate impact masks reasons and will stifle efforts to address why there are a disproportionate number of a certain group not meeting standards.

Factors such as a consumer's income, continuity of income, and adequacy of collateral, among other factors that are differentially distributed among applicants, are all relevant to credit decisions. An undue focus on a numbers-driven theory can paper over fundamental issues within certain demographic populations contribute to a failure to meet lending standards. Such obfuscation can in turn lead to these issues being neglected with, again, minorities perhaps the most acutely affected.

Studies on financial inclusion suggest important ways to raise lending standard success for the greatest number especially, low-income and young consumers, minorities, and immigrants are innovation, competition by lowering barriers to entry, and consumer empowerment through financial education. Undue emphasis on achieving racial balance can stifle business decisions which might otherwise spur innovation in financial services to improve financial inclusion for traditionally underrepresented populations.

v. Increased cost of doing business.

Disparate impact liability can raise costs for businesses through, especially, litigation or the threat of litigation which may then flow disproportionately to lower income Americans who on average are disproportionately minorities.

III. CONCLUSION

[7] *See generally* Consumer Finance Protection Bureau, SUPERVISION AND EXAMINATION MANUAL, https://files.consumerfinance.gov/f/documents/cfpb_supervision-and-examination-manual.pdf
[8] *E.g.* O'Connor v. Consol. Coin Caterers Corp., 517 U.S. 308 (1996); Bank of Am. Corp. v. City of Miami, 581 U.S. 189 (2017).
[9] Equal Credit Opportunity, 15 U.S.C. §1691(a)(1), in pertinent part prohibits discrimination "on the basis of race, color, religion, national origin, sex or marital status, or age."

We ought to carefully and thoughtfully work to reduce racial discrimination as much as possible in a country that in so many ways over its history has sanctioned it. Not just for preferred races, but for every single individual. This is good and serious work and, as I have indicated, I am both professionally and personally committed to it. However, it is my position that the CFPB, or any agency, should refrain from adopting disparate impact theory as a tool to presume discrimination—much less to prove discrimination—for the consequences we can anticipate, the failure in logic that entails, and the likelihood of many other costs we cannot yet envision. There is a better way.

i. Employ discriminatory intent fact-intensive balancing test.

Justice Kennedy's opinion in *Inclusive Communities* recognizes that the disparate-impact approach can lead to very bad results and suggests a fact-intensive inquiry instead is vitally important—similar to the approach outlined in *Village of Arlington Heights v. Metropolitan Housing Development Corp*.[10] For example, Justice Kennedy warns the lower courts against "second-guess[ing]" the nondiscriminatory reasons for challenged policies, requires a "robust causality requirement" rather than relying simply on racial disproportions, and recognizes that "racial quotas" and "racial considerations" and "abusive . . . claims" can result from threatened and actual lawsuits.

ii. Shrinking liberty, expanding government, and inviting legal challenge.

The disparate impact approach to civil rights enforcement which presumes discrimination rather than a data point among many to root it out, is on shaky ground from a legal and policy perspective. It disregards nondiscriminatory decisions and policies and encourages race-conscious decision-making without congressional or judicial permission. That is a disturbing abuse of power at the expense of liberty and, if done by federal agencies, the constitutionally limited federal government. The federal government has an interest in circumstances evincing racial discrimination, but the disparate impact approach is typically used precisely because disparate treatment of the basis of race has not been shown. The issue deepens here since it is the federal government encouraging race conscious decision-making—which invites a potential equal protection challenge.

And, as stated above, one should anticipate an additional legal challenge given the Supreme Court's consistent position that disparate impact claims are not cognizable under statutes lacking effects-based language. That challenge could reach a Supreme Court potentially sympathetic to the view Justice Clarence Thomas put forward in his dissent in *Inclusive Communities*, just seven years ago:

"Statutes prohibiting on their face intentional discrimination should not be extended by judicial or administrative fiat to encompass disparate impact theories."[11]

iii. Upset efforts to address racial equity.

[10] *See* Village of Arlington Heights v. Metro. Hous. Dev. Corp., 429 U.S. 252 (1977).
[11] Inclusive Communities, 576 U.S. 519 at 581 (Thomas, J., dissenting).

Finally, every Fortune 100 company—and many others—has now adopted DEI programs.[12] For example, the Fortune 1 company, Wal-Mart, has devoted $100 million to its "Center for Racial Equity." Governmental zeal to aggressively implement disparate impact analysis in its oversight of the private sector may inadvertently frustrate these efforts and potentially, discourage additional large, medium, and small-sized enterprises from launching and allocating resources for such efforts. If one supports these efforts, it is prudent to provide space for them to play-out and to study their progress in addressing potential issues of diversity, equity, and inclusion.

Again, I thank you for the opportunity to provide my testimony and look forward to your questions.

[12] Christopher Rufo, *The DEI Regime*, City Journal, July 13, 2022, https://www.city-journal.org/the-diversity-equity-and-inclusion-regime.