M E M O R A N D U M

IDENTIFYING LENDER PRACTICES THAT MAY FORM THE BASIS OF A PATTERN OR PRACTICE REFERRAL TO THE DEPARTMENT OF JUSTICE

**Background and Definitions**

The General Accounting Office has recommended that the Department of Justice provide the bank regulatory agencies with updated guidance on the characteristics of a referable pattern or practice of discrimination. While we think that the Equal Credit Opportunity Act requires each agency to refer any matter that gives it reason to believe the lender has engaged in a pattern or practice of discrimination, we recognize that there will be some instances where the facts uncovered in an examination or investigation may reveal a pattern or practice of discrimination that does not rise to a level requiring suit by this department. On the basis of our understanding of the ECOA's requirements, as well as our experience with referrals over the past five years, we believe that the agencies should not resolve their doubts as to whether a particular set of facts is referable by making a unilateral decision not to refer.

In the past two years, we have developed procedures (jointly with the OCC and the FRB) through which compliance staff members from the agencies can telephone designated members of our Housing Section staff members to discuss the facts of a potential referral. The goal of these informal conversations has been to arrive at agreement on (1) whether the facts show a pattern or practice of discrimination, and (2), if so, whether the Chief of the Housing Section is able to make a preliminary determination that if a referral is made, it will be returned to the agency for administrative action. Once there is agreement that these two conditions have been met, the agency forwards a brief written description of the facts with a signature line acknowledging that the referral should be returned to the agency.

To date, these procedures have resulted in many more returned than accepted referrals (as shown by the table of referrals set forth in the GAO report). These procedures have contributed a great deal to a mutual understanding of what facts do not constitute the kind of pattern or practice this Department should act on, but they have not fully answered the question as to what should be referred with the understanding that we will investigate it to determine whether legal action should be taken.

Thus, in the context of the discussion below on the legal and factual aspects of a "pattern or practice," we begin with definitions that draw a distinction between referrals that we would return to the agency for administrative resolution and

those that we would pursue upon referral:

A. Characteristics of pattern or practice referrals that would likely be returned to the referring agency

The practice meets all of the following criteria:

1. The practice has ceased, and there is little chance that it will be repeated;

2. The violation may have been accidental and isolated, or it arose from carelessness or ignorance of the law's more obscure requirements (for example, spousal signature violations and minor price breaks for certain age groups not entitled to preferential treatment); and

3. Where there were large numbers of victims, the harm was de minimis, or where there were few victims but serious harm, the victims have been made whole.

B. Characteristics of pattern or practice referral that the Department of Justice would treat as candidates for legal action

The practice does not meet all of the above criteria and meets at least one of the following criteria:

1. The practice is serious in terms of its potential for either financial or emotional harm to members of protected classes (for example, discrimination in processing or underwriting, pricing, or marketing of lender services);

2. The practice is not likely to cease without court action;

3. The protected class members harmed by the practice cannot be fully compensated without court action;

4. Damages for victims, beyond out-of-pocket losses, are necessary to deter the lender (or others like it) from treating the cost of detection as a cost of doing business; or

5. The agency believes the practice to be sufficiently common in the lending industry, or raises an important issue, so as to require its public disclosure as a deterrent to other lenders.

## I. Introduction

The Equal Credit Opportunity Act, 15 U.S.C. §§ 1691 et seq., requires federal financial regulatory agencies to refer matters to the Attorney General for prosecution when the agencies have a reasonable belief that the creditor in question has engaged in a pattern or practice of discrimination in violation of the ECOA. 15 U.S.C. § 1691e(g).1 The Fair Housing Act, 42 U.S.C. §§ 3601 et seq., allows the Attorney General to file a civil action against, inter alia, a lender when the Attorney General has "reasonable cause to believe" that the lender has engaged in a pattern or practice of discrimination. 42 U.S.C. § 3614. This memorandum is intended to provide a working definition of "pattern or practice" for purposes of fair lending reviews and investigations.

The meaning of the term "pattern or practice" has been addressed by courts in a number of our enforcement areas, but there is no magic definition of this term. See United States v. Di Mucci, 879 F.2d 1488, 1497 n. 11 (7th Cir. 1989) (pattern or practice is not a term of art); Ste. Marie v. Eastern R. Ass'n, 650 F.2d 395, 406 (2d Cir. 1981) (definition of pattern or practice is not capable of a mathematical formulation). Courts often say that it means "more than an isolated instance," but such descriptions are not very helpful. Congress used the term in the Fair Housing Act to distinguish between the smaller, individual matters which should be handled in the first instance by HUD, and broader-based discrimination matters which would be subject to the initial authority of the Department. There is substantial overlap in these concepts, and, in the non-lending context, the Department often alleges a pattern or practice when we receive a HUD referral of an individual instance of discrimination.

## II. Standards for Proving Pattern or Practice in Litigation

To prove a pattern or practice of purposeful discrimination in litigation, the Department must show that it was a regular, rather than the unusual, practice of the defendant to act a discriminatory manner. International Brotherhood of Teamsters v. United States, 431 U.S. 324, 336 (1977). A pattern may be established in the absence of proof of willful conduct. United States v. Security Management Co., Inc., 96 F.3d 260 (7th Cir. 1996) (citing United States v. Balistrieri, 981 F.2d 916, 930 (7th Cir. 1992), cert. denied 510 U.S. 812 (1993)). The practice need not be uniform. United States v. Yonkers Board of Education, 624 F. Supp. 1276, 1293 (S.D.N.Y. 1985), aff'd, 837 F.2d 1181 (2d Cir. 1987), cert. denied, 486 U.S. 1055 (1988). The United States does not have to show that a defendant always discriminates, United States v. Lansdowne Swim Club, 894 F.2d 83, 89 (3d Cir. 1990) (Title II); United States v. Real Estate Development Corp., 347 F. Supp 776, 783 (N.D. Miss. 1972) (Fair Housing Act), and there is no minimum number of incidents which must be proven as a prerequisite to finding a pattern or practice, United States v. Ramsey, 331 F.2d 824, 837 nn. 19 & 20 (5th Cir. 1964) (Rives, J., concurring in part, dissenting in

part).

The extent and duration of the pattern, like the question of whether a pattern exists, "is a factual finding" to be made by the factfinder. United States v. Balistrieri, 981 F.2d 916, 930 (7th Cir. 1992), cert. denied 510 U.S. 812 (1993). The factfinder must view the evidence related to proving a pattern or practice of discrimination as a whole, because "[t]he character and effect of a general policy is to be judged in its entirety, and not by dismembering it as if it consisted of unrelated parts. Even intrinsically lawful acts may lose that character when they are constituent elements of an unlawful scheme." United States v. City of Parma, Ohio, 494 F. Supp. 1049, 1055 (N.D. Ohio 1980), aff'd, 661 F.2d 562 (6th Cir. 1981), cert. denied, 456 U.S. 926 (1982) (citations omitted). Both direct and circumstantial evidence are relevant to a finding of discriminatory purpose and "[i]nvidious discriminatory purpose may often be inferred from the totality of relevant facts." Washington v. Davis, 426 U.S. 229, 242 (1976); Village of Bellwood v. Dwivedi, 895 F.2d 1521, 1533-34 (7th Cir. 1990) (under the FHA, intent can be shown by either direct or circumstantial evidence). Cf. Moore v. United States Department of Agriculture, 55 F.3d 991, 995 (5th Cir. 1995) (under ECOA, if direct evidence is available, court does not need to go through McDonnell Douglas burden shifting that is required by circumstantial evidence).

Proof of a pattern or practice of discrimination does not require a showing that race (or national origin, sex, and age) was the sole motive for the defendant's actions. Village of Arlington Heights v. Metropolitan Housing Development Corporation, 429 U.S. 252, 265-66 (1977). Rather, if any or all of these protected categories is a "motivating factor" in the actions, illegal discrimination exists. Id. Proof of discriminatory intent requires a "sensitive inquiry into such circumstantial and direct evidence of intent as may be available." Id.

## III. Pattern or Practice Sufficient for a Referral

While the standards set forth above are not precise, they give a good indication of what courts look for when the Department has alleged a pattern or practice of discrimination. The Department's standards for referrals under the Equal Credit Opportunity Act and the Fair Housing Act are not as high as those articulated above. Because the Department will conduct its own investigation before commencing litigation, the regulatory agencies need not have overwhelming proof of an extensive pattern or practice of discrimination before making a referral.

The ECOA and the Fair Housing Act require that the Attorney General have a reasonable belief that a pattern or practice of discrimination exists before she may initiate a lawsuit. 15 U.S.C. § 1691e(h); 42 U.S.C. s 3614(a). The Attorney General

believes that the reasonable belief standard is the standard that the agencies should use. If an agency has a reasonable belief, that is, a belief that is based on an articulable reason, that a bank has engaged in more than one instance of the same or similar kind of discriminatory behavior in violation of the ECOA or the Fair Housing Act, the agency should make a referral to the Department for further investigation and possible prosecution.

In determining whether a pattern or practice of discrimination exists, the federal financial regulators should draw upon their experience with the term "pattern or practice. See e.g., 12 U.S.C. § 2605(f); 24 C.F.R. § 33500.21; 12 C.F.R. 5.46(f)(1); 12 C.F.R. § 226.32(e). Cf. 15 U.S.C. § 1607(e)(2) ("clear and consistent pattern or practice"). For example, in making determinations whether to allow changes in a bank's capital requirements, the OCC must determine whether a bank has engaged in a "pattern or practice of violations which may have a significant impact on the bank." 12 C.F.R. § 5.46(f)(1)(ii). Similarly, the Federal Reserve Board must determine whether a creditor has engaged in a pattern or practice of extending credit based on collateral in situations where the creditor anticipates the borrower will be unable to comply with the terms of the loan. 12 C.F.R. § 226.32(e)(1). While the regulators' experience in making determinations under their own regulations does not directly translate to the fair lending context, the standards developed for determining whether a pattern or practice is not dissimilar.2 Ultimately, the determination as to whether a lender has engaged in a pattern or practice of discrimination is fact-based, and should be viewed in the same manner as the regulators' search for patterns or practices in other contexts.

It is worth noting that the ECOA **requires** the agencies to refer matters to the Attorney General when an agency has reason to believe that "1 or more creditors has engaged in a pattern or practice" of discriminatory behavior, but **allows** the agencies to refer matters to the Attorney General whenever the agency has reason to believe that "1 or more creditors has violated section 1691(a). 15 U.S.C. § 1691(e)(g). The Department welcomes any discretionary referrals in which the agency is uncertain whether a creditor's practices suffice to reveal a pattern or practice.

## IV. Investigative Methods for Determining the Existence of a Pattern or Practice