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District Court Dismisses CFPB's Case against Townstone, Refusing to Extend ECOA Protections to "Prospective Applicants"

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LESLIE A. SOWERS
WASHINGTON:
202.378.2384
LESLIE.SOWERS@
HUSCHBLACKWELL.COM

On February 3, the U.S. District Court for the Northern District of Illinois dismissed with prejudice the lawsuit filed by the Consumer Financial Protection Bureau (CFPB) against Townstone Financial, Inc. (Townstone), a nonbank residential mortgage lender and broker. The suit by the CFPB alleged that Townstone discouraged African-American prospective applicants in the Chicago metro area from applying for mortgages with Townstone due to remarks made by the Townstone President and CEO, Barry Sturner, on T*he Townstone Financial Show*. The court declined to expand the reach of the Equal Credit Opportunity Act (ECOA) beyond the "express and unambiguous language of the statute" to include language from the CFPB's implementing regulation, Regulation B, prohibiting discouragement of "prospective applicants" on a prohibited basis. The decision demonstrates the importance of the statutory language of consumer finance laws, even if implementing regulations exist and are well established.

The complaint

The CFPB's original complaint, filed in July 2020, alleged that Townstone had violated the protections under ECOA based on Regulation B's language that prohibits discouraging, on a prohibited basis, applications for credit. Specifically, Regulation B states:

A creditor shall not make any oral or written statement, in advertising or otherwise, to applicants **or prospective applicants** that would **discourage** on a prohibited basis a reasonable person from making or pursuing an application. 12 C.F.R. § 1002.4(b) (emphasis added)

The CFPB's allegations of discouraging prospective applicants in violation of Regulation B were based on (1) comments made on the *Townstone Financial Show*, a radio show used as a marketing channel by Townstone to generate mortgage loan applications; and (2) Home Mortgage Disclosure Act (HMDA) data reported by Townstone as compared to HMDA data reported by its "peer" lenders from African-American applicants in the Chicago-Naperville-Elgin Metropolitan Statistical Area (Chicago MSA) during the years 2014-2017. In other words, the CFPB's complaint alleged that Townstone's low application rate from African-American applicants in the Chicago MSA (as compared to the rates of other lenders in the area) demonstrated that the radio show comments were, in fact, discouraging African Americans from applying with Townstone.

The dismissal

The motion to dismiss by Townstone stated that the CFPB attempted to expand the reach of ECOA beyond the language of the statute and argued that ECOA does not regulate behavior relating to prospective applicants that have not yet applied for credit. The CFPB's argument in response noted that the discouragement prohibition in Regulation B "is authorized by and necessary to the ECOA" and recognized by courts "even when applied to prospective applicants." In order to analyze the arguments by both the CFPB and Townstone, the court used a two-step framework identified in *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837. As noted in the Townstone decision, the first step in the *Chevron* analysis is to identify "whether Congress has spoken to the precise question at issue." *Id.*

In the Court's review for this first step, the language of ECOA itself was analyzed. Specifically, the Court focused on the following language in ECOA:

> It shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction—on the basis of race, color, religion, national origin, sex or marital status, or age (provided the applicant has the capacity to contract). 15 U.S.C. § 1691(a).
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> "Applicant" means "any person who applies to a creditor directly for an extension, renewal, or continuation of credit, or applies to a creditor indirectly by use of an existing credit plan for an amount exceeding a previously established credit limit." Id. § 1691a(b).

Based on the above language, the court found that Congress had spoken directly and unambiguously and, therefore, ECOA only prohibits discrimination against applicants, not *prospective* applicants. In reaching this conclusion, the court did not address the second step of *Chevron* and did not provide deference to the language of Regulation B § 1002.4, which specifically refers to the discouragement of prospective applicants.

The court's decision cited additional case law that supported its interpretation that the plain language of ECOA defines "applicant," pointing out that the entire statutory scheme of ECOA is focused on applicants. It also addressed the CFPB's authority to enact regulations, noting that such authority is not "limitless."

What's next

The decision in Townstone should not be seen to completely diminish the regulatory authority granted to the CFPB for ECOA, and since it is only one case in one court, the CFPB is likely to continue to use its Regulation B interpretation at least in its future supervisory examinations, as are other regulators that rely on the CFPB's Regulation B. However, the decision may limit the CFPB in certain future enforcement actions, especially related to its recent focus on redlining claims in the nonbank mortgage lender context and discrimination in marketing and artificial intelligence algorithms more generally in the financial services industry. This decision could prove particularly impactful for non-mortgage credit products because such products are not governed by the Fair Housing Act, under which the prohibitions against discrimination for mortgage lending are not limited only to "applicants." For these non-mortgage credit products (e.g., credit cards, personal loans, small business loans, or payday loans), the dismissal of this particular claim for discrimination against prospective applicants may encourage the CFPB to utilize the recent expansion of the UDAAP exam manual to include discrimination as an unfair practice in future actions.

The dismissal of the CFPB's case against Townstone is an important reminder of the deference given to statutory language as drafted and enacted by Congress. This deference exists, not only for ECOA, but also for all other statutes over which the CFPB has supervisory and enforcement authority. If, and when, a dispute regarding interpretation of statutory authority arises, the same *Chevron* analysis must be applied to resolve it. The decision should also serve as a reminder that words matter, conflicts of interpretation between a statute and its implementing regulation have a real impact, and courts will look first to the language Congress intended. Although this decision is only binding in the Northern District of Illinois, it could be cited as persuasive authority by any court. In other words, we don't recommend overhauling your current day-to-day fair lending compliance procedures that prohibit discouraging prospective applicants on a prohibited basis.

Contact us

If you have any questions about ECOA, Regulation B, or anything else consumer finance related, please reach out to Maureen Clark, Leslie Sowers or your Husch Blackwell attorney.