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The FTC Pursues Its Own Seat at the Table of Fair Lending Enforcement

The Federal Trade Commission's ("FTC" or "Commission") recent mortgage loan pricing settlements reveal a new, aggressive approach to fair lending enforcement, thus creating an even greater lack of analytical continuity across government agencies and making it more difficult for even the most well-intentioned lenders to properly analyze loan pricing for fair lending compliance. On September 17, 2010, the Commission announced a settlement with California-based regional mortgage lender Golden Empire Mortgage, Inc. (the "company") and its owner in his individual status. The settlement involved a $1.5 million payment for consumer redress to resolve claims that the company and its owner violated the Equal Credit Opportunity Act ("ECOA") by discriminating against Hispanic borrowers in the pricing of home mortgage loans.

Though the FTC historically has used its authority under the FTC Act to pursue claims against businesses for unfair and deceptive trade practices such as fraudulent advertising or mislabelling, the recent settlement, as well as the 2008 settlement with Pennsylvania-based lender Gateway Funding, has revealed the Commission's relatively new focus on ECOA enforcement, including discrimination based on race and ethnicity. Even though ECOA authorizes the FTC to refer discrimination matters to the Department of Justice for enforcement, the FTC chose to bring its own civil action against the company, clearly demonstrating the agency's desire to have its own seat at the table of fair lending enforcement.

Similar to many of the private lawsuits brought by class action plaintiffs against lenders, the crux of the FTC's claim was that the company implemented a "Discretionary Pricing Policy," which simply means that the company, like most lenders, granted its loan officers discretion in pricing retail loans to borrowers, and that the loan price would affect the loan officer's commission. In other words, loan officers could charge a borrower more or less for a loan depending on factors such as competition, negotiation, and time and effort spent on the transaction. The FTC claimed that this discretion had a disparate impact on Hispanic borrowers, who more often than not were charged overages that resulted in higher prices, and that the company failed to monitor these pricing differences at the management level. Of course, the agency's concern over discretionary pricing will be somewhat defused by the Federal Reserve Board's amendments to Regulation Z, and comparable provisions under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), which eliminate overage incentives for loan officers.[i]

The company strongly denied that it had discriminated, and refused to cave in when the FTC initially presented its settlement demands, forcing the agency to file a lawsuit in federal court. Ultimately, though the company was prepared to contest the lawsuit and present strong defenses, mounting costs of litigation caused the modestly sized lender to settle with the agency.

The FTC's recent focus on fair lending may be somewhat troubling for players in the mortgage industry, as the Commission has revealed it may not be content to follow traditional ECOA interpretation. Indeed, various components of the FTC settlement indicate the maverick attitude of the agency.

Most notably, the FTC sought money damages from the company's owner in his individual capacity, alleging only that he was the president and sole owner of a closely held corporation and actively participated in the general operation of the company's business. The FTC did not, however, claim that the owner had any knowledge of the alleged discriminatory practices against Hispanic borrowers, making the Commission's focus on him as an individual particularly troubling. Assessing individual liability based solely on an allegation of ownership and general control could subject the owner of every business to personal risk. Moreover, this interpretation seems to contravene FTC Act precedent, as well as the United States Supreme Court's holding in *Meyer v. Holley*, 537 U.S. 280 (2003), which rejected the argument that officers may be liable simply on the basis that they own or control actions of their employees.

Furthermore, in its public filings against the company in the Central District of California, the FTC also articulated its unique belief that ECOA's two-year statute of limitations, which applies to both private actions and government actions, does not apply to civil actions brought by the agency. However, the new five-year statute of limitations for ECOA, once effective, will render any controversy surrounding this issue moot.[ii]

Finally, the settlement itself indicates the FTC's desire to be involved in, and even dictate, the many details of a lender's fair lending monitoring program. While other agencies may have accorded a reasonable degree of deference to a lender's business decisions and would have permitted a lender to tailor its own fair lending monitoring program, the FTC's settlement lists with specificity each component of the company's future fair lending monitoring program, including the controls the FTC would permit in a statistical analysis of loan pricing. For example, the settlement document permits only four factors to be considered in a discretionary pricing analysis; notably missing from these factors is any consideration for Metropolitan Statistical Area ("MSA"). It is ironic that the agency charged in part with promoting competition among businesses would fail to acknowledge the legitimacy of pricing differences among varying markets. Further, the failure to include MSA as an acceptable explanatory factor for pricing differences directly conflicts with the analytical approach of the federal banking agencies that have regulated loan pricing for decades. Although the settlement's unusual monitoring dictates will be somewhat mitigated by the new loan officers compensation limitations under Regulation Z and Dodd-Frank, it will still impair the company's ability to account for market differences if, for example, the company opts to permit and monitor underages.

The FTC's settlement contains other distinguishing features. For example, the FTC's lawsuit did not make any allegation of disparities in Annual Percentage Rate ("APR") between minorities and non-minorities.

Through its settlements with the company and Gateway, the FTC has made it clear that it intends to join the already long list of government agencies that actively enforce fair lending laws. Although Dodd-Frank moves ECOA *regulation* from the Federal Reserve Board to the newly created Bureau of Consumer Financial Protection (the "Bureau"), Dodd-Frank will not foil the FTC's ECOA enforcement objectives. Dodd-Frank grants the FTC concurrent authority to enforce ECOA through the FTC Act, requiring only that the FTC coordinate with the Bureau.[iii]

The FTC's fair lending approach and analytical framework cause concern because they differ from those of other regulators and enforcement agencies, such that the exact same facts under the exact same law could be analyzed differently depending on the agency investigating the matter. This will further complicate an already difficult challenge for lenders earnestly trying to evaluate their fair lending compliance, and would support a policy argument that fair lending enforcement should be consolidated under the Bureau. Settlements have little precedential value, but lenders subject to the jurisdiction of the FTC should pay heed.

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[i] 75 Fed. Reg. 185 (Sept. 24, 2010) (amending 12 C.F.R. § 226.36 ("Regulation Z"); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-205, § 129(B)(c).

[ii] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-205, § 1085(7) (amending 15 U.S.C. § 1691e(f)).

[iii] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-205, §§ 1024 and 1025.