

the GSE, the Secretary notes that the GSE will have already had a total of 60 days to develop the first two plans. At that point, the GSE's plan should be sufficiently developed so that an additional 30 days is unnecessary to develop a third plan. Accordingly, this provision has not been changed.

Subpart C—Fair Housing

The GSEs' Role

While expressing their strong commitment to participating in the elimination of discriminatory practices in the mortgage lending process, both GSEs, in similar arguments, objected to certain features of Subpart C—Fair Housing.

Both enterprises outlined their efforts to encourage fair lending practices by primary mortgage lenders through outreach, consumer education, and innovative products. The GSEs stressed their interest in contributing to the elimination of unlawful discrimination in the mortgage finance industry. However, both objected to a fair housing enforcement role which they argued the proposed rule would have imposed on them.

Fannie Mae saw its appropriate role in fair lending as being a provider of outreach, consumer education, and flexible, innovative mortgage products to its customers. Freddie Mac also maintained that its primary role should be to provide a ready source of financing for all creditworthy borrowers and to provide market leadership. Freddie Mac took issue with what it saw as the proposed rule's implication that it should be doing more with respect to fair lending.

Several other commenters endorsed the GSEs' position in this regard and stated that, for the GSEs, the role of regulator is inconsistent with the business partnership relationship that exists between the GSEs and their customers. A major mortgage company commented that GSEs ought not be required to develop fair lending plans, because such plans would, in effect, establish the GSEs as "primary market regulators." Referencing its long established business partnership with both GSEs, the commenter said it did not want these entities "to also be our regulators."

On the other hand, the San Diego Housing Commission had no objection to an expanded role for GSEs associated with fair housing:

The proposed rule essentially requires the GSEs to cooperate with HUD in providing data and other information to assist in the investigation of mortgage discrimination by a lender with which either does business.

In general Fannie Mae and Freddie Mac have been successful in expanding the availability of credit, lowering interest rates, and in stabilizing and liquefying the finance market. However, there have been shortcomings in the extent to which they help meet the housing needs of households at the lower end of the housing market. Given their size and the key role they play in housing finance, they are in a position to wield a significant amount of influence.

This final rule follows the clearly expressed intention of Congress that the GSEs comply with the Fair Housing Act and the Equal Credit Opportunity Act ("ECOA") and aid the efforts of investigators.⁴⁵ HUD does not intend that the GSEs will become the Federal government's regulatory or enforcement operation for the primary mortgage market. The Federal fair lending enforcement agencies, not the GSEs, enforce the fair lending laws.

HUD has carefully examined the various points made by the GSEs and other commenters on subpart C of the proposed rule. This final rule contains modifications which respond to the commenters' concerns about the proposed rule's nondiscrimination requirements, assessment of disparate results, and information and recordkeeping requirements. Additionally, many suggestions made by the commenters for language changes and modifications of other aspects of the proposal have been accepted and incorporated. These revisions are discussed elsewhere in this preamble.

Disparate Impact

Freddie Mac argued that section 1325(1) of FHEFSSA reaches only *intentional* discrimination and that application of a disparate impact test is therefore unauthorized. Both GSEs claimed that, even if the disparate impact standard was supported by FHEFSSA, HUD had misstated the standard as articulated by the courts, and had shifted the burden of proof from the plaintiff to the GSE. Other commenters shared this view, although there was little comment in support of Freddie Mac's assertion that FHEFSSA prohibits only intentional discrimination. Fannie Mae claimed that there is no statutory basis and little case law in support of applying a disparate impact analysis to matters arising under ECOA or the Fair Housing Act.

Several other industry commenters joined in this criticism of the proposed rule. The ABA, the MBA, the Western League of Savings Institutions and a major mortgage lender all characterized the application of disparate impact

analysis or an "effects test" standard in this particular rule as premature and a potential source of marketplace uncertainty.

Both GSEs urged HUD to postpone application of the disparate impact standard in this rule until the issue is addressed in the HUD's broader Fair Housing Act regulations. Adopting the standard in FHEFSSA rules first, the GSEs claimed, would create confusion and increase the likelihood of the development of divergent standards governing mortgage finance. Both GSEs and several major industry organizations argued that subpart C would result in a dual enforcement mechanism, applicable to their operations but not to other segments of the housing marketplace, and would subject them to the application of legal theories that are "largely untested in mortgage finance." The GSEs urged the Secretary not only to delay implementation of a disparate impact standard in advance of a fair lending addition to HUD's Fair Housing regulations, but also to coordinate the development of any such revisions with primary market financial institution regulators and the Department of Justice. Fannie Mae claimed that none of these regulators or enforcers has provided industry-wide guidance to date.

The American Bankers Association questioned the proposed rule's explanation of business necessity, suggesting that it failed to afford the GSEs adequate guidance. It further maintained that HUD's position on the meaning of business necessity was inconsistent with and constituted a more difficult legal test than the understanding of the term reflected in the Interagency Policy Statement on Discrimination in Lending ("Interagency Policy Statement").⁴⁶

Fannie Mae also claimed that the proposed rule would create a potential "litigation and enforcement nightmare" for the GSEs and that the rule would inhibit innovation. Freddie Mac argued that the rule would also inhibit the GSEs' efforts to identify and eradicate barriers in their underwriting guidelines.

Section 1325(1) of FHEFSSA requires the Secretary to prohibit the GSEs from discriminating "in any manner"—including a prohibition on any consideration of the age or location of a dwelling or neighborhood in a manner that has a "discriminatory effect." The use of the phrases "in any manner" and "discriminatory effect" in section 1325(1) makes clear Congress's intent

⁴⁵ See S. Rep. at 43–44.

⁴⁶ 59 FR 18266 (1994).