IMPACT IPSA LOQUITUR: A REVERSE HAND RULE FOR CONSUMER FINANCE

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TABLE OF CONTENTS

INTRODUCTION 1134
I. LENDING DISCRIMINATION AND THE EFFECTS OF AI 1142
A. *Defining Terms: Discrimination and Unfairness* 1143
1. Discrimination: Historic, Systemic, and Algorithmic 1143
2. Algorithmic Discrimination and Predation 1145
a. Beyond Credit Constraint 1145
b. Discriminatory Pricing, Pricing Discretion, and the Implications of Algorithmic Lending 1146
c. Terms Discrimination 1148
d. Predation in Credit Marketing 1149
e. Discriminatory Predation 1150
B. *The Particular Perils of AI: Scope and Transparency* 1151
1. Scope and Granularity 1151
2. Transparency and Accountability 1152
II. LENDING DISCRIMINATION: LEGISLATION AND REGULATION 1153
A. *Discrimination: Civil Rights Statutes and the Allocation of Enforcement Power* 1154
1. Discriminatory Treatment 1154
2. Disparate Impact 1154
3. Regulatory Enforcement 1159
4. Questions about AI 1163
B. *Regulating Discrimination Through Jurisdiction Over Unfair and Abusive Practices* 1164

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III. A REVERSE HAND RULE FOR ALGORITHMIC LENDING: *IMPACT IPSA LOQUITUR*....1167
A. *Circumstantial Proof of Negligence*....1168
1. The Hand Rule....1168
2. Reverse Hand Rules....1169
a. *Res Ipsa Loquitur*....1169
b. Circumstantial Proof of Causation....1171
B. *Proof of Algorithmic Discrimination*....1172
1. Proof of Discrimination, Unfairness, and Causation....1173
2. Algorithmic Discriminatory Predation—Linking Liability and Causation....1174
a. *Impact Ipsa Loquitur*—Discrimination....1174
b. *Impact Ipsa Loquitur*—Predation and Presumed Causation....1175
CONCLUSION....1175

INTRODUCTION

The topic of this symposium—*Automating Bias*—considers how artificial intelligence can produce, reinforce, and hide racial and other forms of discrimination in consumer finance.[1] The animating intuition is that the complexity and opacity of algorithms and artificial intelligence in consumer lending create a greater need for disparate impact analysis to combat lending discrimination. This view was articulated forcefully by the current Director of the Consumer Financial Protection Bureau (CFPB), Rohit Chopra, when he was still a commissioner at the Federal Trade Commission (FTC):

> It is rare to uncover direct evidence of racist intent. That's why disparate impact analysis is a critical tool to uncover hidden forms of discrimination, not only in this context but throughout the economy. Companies are collecting an ever-growing universe of personal data, and through sophisticated machine learning tools and other forms of predictive technology, this data can produce proxies for race and other

1 We use the terms "consumer lending" and "consumer finance" to include residential mortgages, although the Federal Reserve defines "consumer credit" as "outstanding credit extended to individuals for household, family, and other personal expenditures, *excluding loans secured by real estate*." *Consumer Credit—G.19*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/releases/g19/about.htm [https://perma.cc/T8U8-368R] (Dec. 20, 2022) (emphasis added). For consistency and clarity, we only use the term "consumer credit" consistent with the narrow definition applied by the Federal Reserve Board.

> protected classes. Often this discrimination is invisible to its victims, making it especially important that regulators work proactively to root it out.[2]

We share Chopra's intuition and concern, but we would go further.

Algorithmic lending practices do not simply render discrimination "invisible to its victims."[3] The sources of discriminatory effects within an algorithm may similarly be invisible to regulators and private litigants who seek to protect borrowers, and therefore unprovable to the courts with jurisdiction to apply these regulations and statutes. Because machine learning tools are black boxes, even the lenders that rely on AI in their financial decision-making may not understand that these tools use broad-based data that may lead to decisions that adversely impact protected groups.[4]

Accordingly, this Article makes three points. Two are relatively obvious extensions of Director Chopra's insight. The third is novel. The first obvious point is that the black-box nature of AI, and the way it interacts with legacy discrimination, increases the need for disparate impact liability in the consumer lending context. The second obvious point is that algorithmic lending discrimination comprises more than credit denial. It also includes lending on discriminatory (or even predatory) terms ("algorithmic discrimination"), as well as algorithmic marketing of predatory loans to vulnerable populations ("algorithmic predation"). While AI increases the risk of algorithmic discrimination and predation, consumers have suffered earlier forms of this sort of discrimination since risk-based pricing became commonplace. The novel point is that the addition of unfairness jurisdiction as an overlapping statutory basis to combat bias in consumer lending fundamentally changes the way that rebuttal works in disparate impact cases. If a plaintiff raises an inference of either disparate racial impact or predatory lending practices (whether unfair, deceptive, or abusive), the defendant must be prepared to establish both that the algorithm is nondiscriminatory and that the resulting lending practices are fair.

As Director Chopra observes, intentional discrimination is comparatively rare and difficult to prove. This has been the case since well

2 Statement of Comm'r Rohit Chopra, Fed. Trade Comm'n on *In the Matter of Liberty Chevrolet, Inc. d/b/a Bronx Honda* Commission File No. 1623238 (May 27, 2020), https://www.ftc.gov/system/files/documents/public_statements/1576002/bronx_honda_final_rchopra_bronx_honda_statement.pdf [https://perma.cc/N7Z3-AYN7].

3 *Id.* at 2.

4 Exec. Order No. 14110, § 7.3(b), 88 Fed. Reg. 75191, 75213 (Nov. 1, 2023).

before the automation of consumer finance and other markets.[5] At least since the Supreme Court's decision in *Griggs v. Duke Power Co.*,[6] courts have viewed the prohibition against "discrimination" as including both discriminatory treatment and discriminatory effects.[7]

AI increases the importance of a disparate impact analysis of lender behavior, both with regard to discrimination and predatory marketing. AI masks human agency and thus may mask intentional discriminatory treatment[8] and conceal the reason for discriminatory effects.[9] At the same time, lenders and other firms relying on AI are likely to assert that the standard set out in *Griggs* is satisfied with this sort of machine learning since AI is increasingly viewed as a legitimate business practice without less discriminatory options.[10] As the CFPB and other regulators decide how their enforcement and regulatory powers should address algorithmic lending discrimination and unfair, deceptive, and abusive financial loans and loan terms produced through machine learning,[11] enforcement

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5 This is true even though proof of intentional discrimination does not require evidence of "bad faith, ill will or any evil motive on the part of [any actor]." Williams v. City of Dothan, 745 F.2d 1406, 1414 (11th Cir. 1984).

6 401 U.S. 424 (1971).

7 For discussion of the origins of this historical development, see Olatunde C. Johnson, *The Agency Roots of Disparate Impact*, 49 HARV. C.R.-C.L. L. REV. 125 (2014); James A. Burns, Jr., *An Empirical Analysis of the Equal Credit Opportunity Act*, 13 U. MICH. J.L. REFORM 102 (1979). The distinction between discriminatory treatment and discriminatory effects has long been blurred, in part, because circumstantial evidence may be relied on to prove either intentional treatment or unintentional effects. Courts may accept disparate impact as circumstantial evidence of intent; at other times, courts may treat disparate impact as an independent basis for liability. For detailed discussion of the caselaw governing these overlapping standards, see C.R. DIV., U.S. DEP'T OF JUST., TITLE VI LEGAL MANUAL [hereinafter DOJ MANUAL], https://www.justice.gov/media/1121301/dl?inline [https://perma.cc/C2TT-W2B6].

8 *See, e.g.*, Exec. Order No. 13960, 85 Fed. Reg. 78939 (Dec. 3, 2020); *see also* FRANK PASQUALE, THE BLACK BOX SOCIETY: THE SECRET ALGORITHMS THAT CONTROL MONEY AND INFORMATION (2015).

9 *See* Working Grp. on Regul. & Exec. Action, Nat'l A.I. Advisory Comm., Rationales, Mechanisms, and Challenges to Regulating AI: A Concise Guide and Explanation (July 2023), https://www.ai.gov/wp-content/uploads/2023/07/Rationales-Mechanisms-Challenges-Regulating-AI-NAIAC-Non-Decisional.pdf [https://perma.cc/DCM5-V8SG] ("AI systems can create, perpetuate, or exacerbate and scale bias against particular demographic groups, including through algorithmic discrimination."); *see also* Danielle Keats Citron & Frank Pasquale, *The Scored Society: Due Process for Automated Predictions*, 89 WASH. L. REV. 1 (2014).

10 *See, e.g.*, Anya E.R. Prince & Daniel Schwarcz, *Proxy Discrimination in the Age of Artificial Intelligence and Big Data*, 105 IOWA L. REV. 1257, 1305 (2020) (arguing that disparate impact litigation is "simply not capable of effectively policing against proxy discrimination by AIs" since firms using AI "will typically have little problem showing that this practice is consistent with business necessity and in rebuffing any attempt to show the availability of a less discriminatory alternative").

11 We mostly focus in this Article on the regulatory and enforcement powers of the CFPB, while acknowledging that the FTC, the Department of Housing and Urban Development (HUD),

agents must recognize that disparate impact analysis may work somewhat differently depending on whether the challenged behavior is credit denial, terms discrimination, or algorithmic predation.

Questioning the source, content, and structure of this standard is particularly important to the consumer finance setting because the CFPB asserts multiple statutory bases for its jurisdiction to police lending discrimination, including both antidiscrimination statutes, such as the Equal Credit Opportunity Act (ECOA),[12] and the CFPB's jurisdiction to regulate "unfair, deceptive, and abusive" acts and practices (its so-called "UDAAP jurisdiction").[13] Moreover, the CFPB shares jurisdiction over discrimination in lending markets with a handful of regulators with similar but distinct sources of jurisdiction, such as the Federal Trade Commission Act (FTC Act),[14] Fair Housing Act (FHA),[15] and Community Reinvestment Act (CRA).[16] These questions are not academic. They are situated at the center of pending enforcement actions.[17]

One example of an action brought to eradicate AI-driven predation in consumer lending can be found in a recent suit brought by the CFPB and the New York Attorney General against Credit Acceptance

and the Civil Rights Division of the Department of Justice (DOJ) all hold overlapping jurisdiction to address discrimination in consumer finance markets. For discussion of the emerging coordination among these regulators, see Joint Statement from Rohit Chopra, Dir. of the Consumer Fin. Prot. Bureau, Kristen Clarke, Assistant Att'y Gen. for the Just. Dept.'s C.R. Div., Charlotte A. Burrows, Chair of the Equal Emp. Opportunity Comm'n & Lina M. Khan, Chair of the Fed. Trade Comm'n on Enforcement Efforts Against Discrimination and Bias in Automated Systems [hereinafter Automated Systems Joint Statement], https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_joint-statement-enforcement-against-discrimination-bias-automated-systems_2023-04.pdf [https://perma.cc/9R7A-4Z72]. This coordination has been prompted by executive order. *See* Exec. Order No. 14091, § 8(f), 88 Fed. Reg. 10825, 10832 (Feb. 16, 2023) (directing agencies to consider opportunities to "prevent and remedy discrimination, including by protecting the public from algorithmic discrimination").

12 15 U.S.C. §§ 1691–1691f; *see also* Equal Credit Opportunity Act (Regulation B), 12 C.F.R. pt. 1002 (2024).

13 For relevant federal statutory prohibitions, see 12 U.S.C. §§ 5531, 5536, which prohibits "unfair, deceptive, or abusive acts or practices"; and 12 U.S.C. § 5531(c), (d), which defines "unfairness" and "abusive." For the agencies' relevant enforcement authorities, see 12 U.S.C. §§ 1786(i), (k)(2), 1818(b), (i)(2), 5531, 5536, 5561–5566. The CFPB also has authority to issue regulations governing "unfair, deceptive, or abusive acts or practices." 12 U.S.C. § 5531(b).

14 15 U.S.C. § 45 (prohibiting unfair or deceptive acts or practices).

15 42 U.S.C. §§ 3601–3619, 3631.

16 12 U.S.C. §§ 2901–2908.

17 *See* Fair Lending Report of the Consumer Financial Protection Bureau, 88 Fed. Reg. 43087, 43088 (July 6, 2023).

Corporation (CAC).[18] There, the CFPB and the New York AG alleged that CAC used its lending algorithm not to predict the ability of a borrower to pay, but instead to "predict how much it [would] collect from consumers over the life of a loan—not just from consumers' monthly payments, but also from potential collection efforts, repossessions, auctions, and deficiency judgments."[19] Based on the results of this algorithm, CAC would calculate the "price" of a car both to evade state usury limits and maximize its return on investment, regardless of the borrower's ability to pay this price.[20] On loans like these,[21] lenders make money, even if the borrower defaults and loses the car.[22]

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18 Consumer Fin. Prot. Bureau v. Credit Acceptance Corp., No. 23-cv-00038, 2023 WL 5013303, at *1 (S.D.N.Y. Aug. 7, 2023). This case, like many other enforcement actions brought by the CFPB, has been stayed pending resolution by the Supreme Court in *Consumer Financial Protection Bureau v. Community Financial Services Association of America*, No. 22-448 (argued Oct. 3, 2023). The authors thank Elena Gonzalez of the CFPB for pointing out this example. For additional information about this complaint, see *CFPB and New York Attorney General Sue Credit Acceptance for Hiding Auto Loan Costs, Setting Borrowers Up to Fail*, CONSUMER FIN. PROT. BUREAU (Jan. 4, 2023), https://www.consumerfinance.gov/about-us/newsroom/cfpb-and-new-york-attorney-general-sue-credit-acceptance-for-hiding-auto-loan-costs-setting-borrowers-up-to-fail [https://perma.cc/U78C-X2DN]. For discussion of settlement of a similar cause of action brought by the Massachusetts Attorney General against CAC, see Press Release, Off. of the Att'y Gen., Commonwealth of Mass., In Largest Settlement of Its Kind, AG Healey Secures $27 Million for Thousands of Massachusetts Consumers from Subprime Auto Lender (Sept. 1, 2021), https://www.mass.gov/news/in-largest-settlement-of-its-kind-ag-healey-secures-27-million-for-thousands-of-massachusetts-consumers-from-subprime-auto-lender [https://perma.cc/2WS4-LCXA].

19 Complaint ¶ 3, *Consumer Fin. Prot. Bureau*, No. 23-cv-00038 (Jan. 1, 2023).

20 *Id.* ¶ 1–6. Plaintiffs in this case allege that the high interest rates CAC charged were intended to evade state usury limits by inflating the purchase cost of the cars and masking the true interest rate behind fees.

21 Neither the motive of, nor the harms caused by, this predatory lending are explicitly tied to race in the complaint filed against CAC. However, the costs of the algorithmic lending practices described in it likely fall hardest on borrowers living close to the margin. For discussion and empirical analysis of discrimination in auto lending markets, see Adam J. Levitin, *The Fast and the Usurious: Putting the Brakes on Auto Lending Abuses*, 108 GEO. L.J. 1257 (2020); Jonathan A. Lanning, Testing Models of Economic Discrimination Using the Discretionary Markup of Indirect Auto Loans (Oct. 14, 2021) (unpublished manuscript), https://www.atlantafed.org/-/media/documents/news/conferences/2021/10/14/racial-inequality-and-disparities-in-financial-markets/lanning.pdf [https://perma.cc/6VCM-V9BU]; Alexander W. Butler, Erik J. Mayer & James P. Weston, *Racial Discrimination in the Auto Loan Market* (Mar. 31, 2021) (unpublished manuscript), https://files.consumerfinance.gov/f/documents/cfpb_mayer_racial-discrimination-in-the-auto-loan-market.pdf [https://perma.cc/VC5C-QKFU]; and Pamela Foohey, *Consumers' Declining Power in the Fintech Auto Loan Market*, 15 BROOK. J. CORP. FIN. & COM. L. 5 (2020).

22 Even if the loan defaults, CAC and used car lenders like them can make money on exorbitant interest rates, late fees, and other credit terms, knowing that they will find protection in the collateral value of the car upon repossession. For general discussion of this "model" of consumer lending, see Ronald J. Mann, *Bankruptcy Reform and the "Sweat Box" of Credit Card Debt*, 2007 U. ILL. L. REV. 375, 379, 385. For discussion in the popular press on this form of "sweat box" lending in

This Article considers how disparate impact analysis can and should be translated into the context of algorithmic consumer and household lending, especially algorithmic lending that might also be viewed as extended on predatory terms. The burden-shifting formulas set out in *Griggs* and its progeny[23] do not translate easily to the underwriting and marketing decisions inherent in consumer lending markets.[24] This is especially true in markets for subprime loans, where applicants often are not *denied* credit for discriminatory reasons, but instead are *granted* credit along a range of contract terms that may discriminate among borrowers on the basis of race, color, or national origin.

The difficulty of proving discriminatory effects in consumer finance markets—especially the effects of algorithmic discrimination—is further magnified by the presence of algorithmic lending in important ways. First, "several government agencies and officials have recognized generally that AI systems can be infected by bias, have discriminatory impacts, and harm marginalized communities."[25] Second, because AI weighs many types of data, not just consumers' credit histories and credit scores, it is far more difficult to determine which data points correlate with credit risk and which with race.[26] Third, proof of causation is especially fraught in consumer lending markets powered by AI given the

used car markets, see Jason Guerrasio, *John Oliver Explains All the Ways Some Used-Car Dealerships Take Advantage of People*, BUS. INSIDER, (Aug. 15, 2016, 10:04 AM), https://www.businessinsider.com/john-oliver-explains-auto-lending-2016-8 [https://perma.cc/27S7-58EA].

23 *Griggs v. Duke Power Co.*, 401 U.S. 424 (1971), decided by the Supreme Court in 1971, has been followed and at the same time narrowed by subsequent Supreme Court case law. *See, e.g.*, Wards Cove Packing Co. v. Atonio, 490 U.S. 642, 657 (1989) (requiring disparate impact plaintiffs to show specific business practices and their impact, and that company refused to adopt different, nondiscriminatory practices); Tex. Dep't of Hous. & Cmty. Affs. v. Inclusive Cmtys. Project, Inc., 576 U.S. 519 (2015). *But see* Meacham v. Knolls Atomic Power Lab'y, 554 U.S. 84, 87 (2008) (holding that disparate impact causes of action are cognizable under the Age Discrimination in Employment Act, and that an employer claiming "reasonable factors other than age" must, "not only produce evidence raising the defense, but also persuade the factfinder of its merit" (quoting 29 U.S.C. § 623(f)(1))).

24 *See, e.g.*, Aaron Klein, *Credit Denial in an Age of AI*, BROOKINGS (April 11, 2019), https://www.brookings.edu/articles/credit-denial-in-the-age-of-ai [https://perma.cc/TX2B-XM9U] ("Policymakers need to rethink our existing anti-discriminatory framework to incorporate the new challenges of AI, ML, and big data.").

25 FED. TRADE COMM'N, COMBATTING ONLINE HARMS THROUGH INNOVATION 44 (2022), https://www.ftc.gov/system/files/ftc_gov/pdf/Combatting%20Online%20Harms%20Through%20Innovation%3B%20Federal%20Trade%20Commission%20Report%20to%20Congress.pdf [https://perma.cc/J3TV-MY4X].

26 *See* Prince & Schwarcz, *supra* note 10, at 1258 ("[A]s AIs become even smarter and big data becomes even bigger, proxy discrimination will represent an increasingly fundamental challenge to anti-discrimination regimes that seek to limit discrimination based on potentially predictive traits.").

history of race-based lending in these markets.[27] As a result, the lessons of critical race theory are central to understanding the dangers that algorithmic lending will ossify this racial history.

One solution to the problems created by the burden-shifting standards set out in *Griggs* is to supplement the various civil rights statutes by characterizing discriminatory effects as unfair, deceptive, or abusive acts or practices. The CFPB recently signaled its intent to rely on its UDAAP jurisdiction as an additional basis for regulating discrimination in consumer lending.[28] Vested with similar jurisdictional authority,[29] the FTC and various state attorneys general also have brought enforcement actions alleging that lenders, and those working in tandem with lenders, engaged in unfair and deceptive acts and practices (UDAP) with discriminatory effects.[30] And yet, because statutory definitions of "unfair" and "abusive" practices might well be characterized as premised on balancing and burden-shifting standards resembling those in *Griggs* and its progeny, the turn to UDAAP may not be sufficient to resolve the problems that AI creates for prima facie proof of disparate impact.

In our view, this expansion of the statutory basis for challenging algorithmic discrimination requires reconsideration of the prima facie and rebuttal burdens of proof in algorithmic discrimination cases, regardless of which regulator is bringing suit and under what statutory regime. Disparate impact analysis in discrimination law must be viewed in context. Circumstantial evidence has long been relied on to establish intent and causation in other contexts. As early as 1601, so-called "badge[s] of fraud" were used to establish intent to "hinder, delay, or defraud creditors."[31] Similarly, the existence of certain "red flags" were used to establish a lack of "good faith" for the purposes of certain

27 *See* Aaron Klein, *Reducing Bias in AI-Based Financial Services*, BROOKINGS (July 10, 2020), https://www.brookings.edu/articles/reducing-bias-in-ai-based-financial-services [https://perma.cc/U9FA-8MJP] ("Our current financial system suffers not only from centuries of bias, but also from systems that are themselves not nearly as predictive as often claimed.").

28 CONSUMER FIN. PROT. BUREAU, EXAMINATION MANUAL: UNFAIR, DECEPTIVE, OR ABUSIVE ACTS OR PRACTICES (2022), https://web.archive.org/web/20230629135926/https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_unfair-deceptive-abusive-acts-practices-udaaps_procedures.pdf.

29 *See supra* text accompanying note 11.

30 *See* Fair Lending Report of the Consumer Financial Protection Bureau, 88 Fed. Reg. 43087 (July 6, 2023) (discussing fair lending enforcement actions in annual report to Congress). For discussion of similar enforcement actions brought by the FTC, see Letter from Malini Mithal, Assoc. Dir., Div. of Financial Pracs., Fed. Trade Comm'n, to Patrice Alexander Ficklin, Assistant Dir., Off. of Fair Lending & Equal Opportunity, Bureau of Consumer Fin. Prot. (Feb. 1, 2023) [hereinafter FTC Letter], https://www.ftc.gov/system/files/ftc_gov/pdf/p154802ecoareport2022.pdf [https://perma.cc/T7V8-MUKY].

31 Twyne's Case (1601), 76 Eng. Rep. 809, 810–11 (KB); 3 Co. Rep. 80b.

purchaser protections under the Uniform Commercial Code.[32] Disentangling the balancing and evidentiary burdens associated with proof of discriminatory impact through facially neutral algorithms, we turn to the rules permitting a prima facie case of tort liability to be established through circumstantial evidence of, for example, intent, responsibility, or causation.[33]

The classic example of burden shifting in tort law involves the doctrine of *res ipsa loquitur*, where the facts are said to speak for themselves; proof of such facts shifts the burden of going forward with the evidence and places this burden on the defendant.[34] Viewed from the context of disparate impact, the burden-shifting formula first identified in *Griggs* similarly rests on the view that the discriminatory effects "speak for themselves"—*impact ipsa loquitur*. The definition of "unfairness" found in the FTC Act and Consumer Financial Protection Act (CFPA) also imply a similar prima facie presumption that "substantial injury" to consumers should subject relevant actors to a burden of justification.[35]

Burden-shifting rules of this type have emerged in tort law to address information asymmetries associated with establishing negligence, and also to address problems of proving causation in cases involving joint tortfeasors, multiple causes, and baseline risks. Guido Calabresi labeled these as "reverse Learned Hand test[s]."[36]

The same evolution has not occurred in disparate impact litigation, however. In fact, courts have doubled down on the need to establish numerous factual predicates, presumably without the benefit of burden shifting, an approach we view as wrongheaded, especially as applied to consumer finance. For example, in *Texas Department of Housing and*

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32 Stephen L. Sepinuck, *The Various Standards for the "Good Faith" of a Purchaser*, 73 BUS. LAW. 581, 602–06 (2018) (citing cases finding such red flags).

33 It bears noting that in tort law, the liability for defective consumer products is strict liability, and for certain types of products—generic drugs, for example—liability can be assessed based on market share. Sindell v. Abbott Labs, 607 P.2d 924 (Cal. 1980). We stop short, in this Article, of advocating such treatment, but it bears mentioning that many of the consumer loans that are underwritten and marketed using algorithms would fit the definition of consumer products. Susan Block-Lieb & Edward Janger, *Fit for its Ordinary Purpose: Implied Warranties and Common Law Duties for Consumer Finance Contracts*, 59 HOUS. L. REV. 551 (2022).

34 Byrne v. Boadle (1863), 159 Eng. Rep. 299, 301; 2 H. & C. 722.

35 12 U.S.C. § 5531(c)(1); 15 U.S.C. § 45(n).

36 *See, e.g.*, Guido Calabresi & Jon T. Hirschoff, *Toward a Test for Strict Liability in Torts*, 81 YALE L.J. 1055, 1059 (1972) (inventing the term "reverse Learned Hand test"). Tort theorists are fiercely divided on the extent to which the relationship between the wrong and the wrongdoer must be established. *See* Palsgraf v. Long Island R.R., 248 N.Y. 339, 343–44 (1928). *Compare, e.g.*, John C.P. Goldberg & Benjamin C. Zipursky, *The Moral of Macpherson*, 146 U. PA. L. REV. 1733, 1755 (1998), *with, e.g.*, Douglas A. Kysar, *The Constitutional Claim to Individuation in Tort—a Tale of Two Centuries, Part 2* (Oct. 9, 2023) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4596502.

Community Affairs v. Inclusive Communities, a case on discriminatory liability under the Fair Housing Act, the Supreme Court notably emphasized that proof of causation remains part of the initial prima facie case of discriminatory effects.[37] The role of causation is made particularly complex in housing and consumer lending markets, however, by decades of systematic and institutionalized discrimination in those markets.[38]

This Article proceeds in three steps. First, it considers how artificial intelligence, algorithms, and big data can combine to facilitate predation and hide discrimination. Second, it explores the existing legal landscape and finds gaps in the relationship between discrimination and predatory lending doctrines. Third, it places both disparate impact analysis and UDAAP doctrines within the broader context of balancing and burden-shifting rules in tort law and considers how this analysis might be tailored for the new algorithmic lending environment. We conclude that predatory discrimination should permit consideration of two types of circumstantial evidence: evidence of disparate racial impact and evidence of unfair lending practices. We argue this because the legacy of systemic racism and the nontransparency of algorithmic lending together mean that unfair (predatory) practices are likely to have discriminatory impact. To put it another way: discrimination in consumer credit is unfair; and that unfairness may well have disproportionate impact on victims of legacy discrimination and other vulnerable populations. Therefore, regardless of the doctrinal basis of the complaint or enforcement action, defendants in suits premised on algorithmic discrimination should be prepared to justify its use of an algorithm by presenting evidence of both racial neutrality and fairness.

I. LENDING DISCRIMINATION AND THE EFFECTS OF AI

Algorithms in consumer finance can entrench, exacerbate, and conceal bias. In this Part, we define what we mean by discrimination and consider how machine learning and other predictive technology alter this landscape. In particular, we emphasize that AI exacerbates the information asymmetries already present in the consumer lending environment. Further, by relying on data that incorporates the effects of

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[37] Tex. Dep't of Hous. & Cmty. Affs. v. Inclusive Cmtys. Project, Inc., 576 U.S. 519, 527 (2015).

[38] *See, e.g.*, EXEC. OFF. OF THE PRESIDENT, BIG DATA: A REPORT ON ALGORITHMIC SYSTEMS, OPPORTUNITY, AND CIVIL RIGHTS 12–13 (2016), https://obamawhitehouse.archives.gov/sites/default/files/microsites/ostp/2016_0504_data_discrimination.pdf [https://perma.cc/Q7RX-W9L2]; Press Release, U.S. Dep't of Just., Department Announces New Initiative to Combat Redlining (Oct. 22, 2021), https://perma.cc/6NYA-HHZF (joint announcement of DOJ, OCC and CFPB regarding resolution of lending discrimination claims against Trustmark National Bank).

past systemic racism, AI ossifies that legacy. We disaggregate the concept of algorithmic lending to show that while discrimination and predatory lending are distinct, they are also interrelated. For that reason, in the next Part, we explore the differences between the tests for discrimination under antidiscrimination statutes and for discrimination as unfairness under UDAAP and UDAP statutes. We consider the dual statutory bases for combatting discrimination in consumer lending: antidiscrimination legislation (e.g., FHA and ECOA) and regulation of unfairness, deception, and abuse in consumer finance markets (e.g., FTC Act and CFPA). In the final Part, we turn to tort law concepts of burden shifting to develop a unified approach.

A. *Defining Terms: Discrimination and Unfairness*

This Section steps away from the statutes themselves to define the forms discrimination may take. It explores the concepts of discriminatory credit access, discriminatory credit terms, predation, and discriminatory predation.

1. Discrimination: Historic, Systemic, and Algorithmic

Although there is no "right to borrow," credit constraint is wrongful if it is the result of overt discrimination, intentional discriminatory treatment, or disparate impact. These three invidious forms of discrimination have long affected the access of some borrowers to banking and other financial services, access to credit, and the terms on which credit is extended, not just on the basis of their creditworthiness, but also on the basis of race, color, religion, national origin, sex, marital status, or age.

A key lesson of history is that discrimination is systemic and its effects are structural—so deeply embedded in the fabric of our society that one need not intend to discriminate to cause discriminatory harm.[39] Unequal access for communities of color—to education, employment, housing, as well as to the ability to borrow or finance the purchase of a

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39 While this insight is sometimes attributed to scholars rooted in critical race theory, we are convinced, and treat this insight not as "theory," but as "fact." *See, e.g.*, RICHARD ROTHSTEIN, THE COLOR OF LAW: A FORGOTTEN HISTORY OF HOW OUR GOVERNMENT SEGREGATED AMERICA (2017); RACIAL JUST. & EQUAL ECON. OPPORTUNITY PROJECT, NAT'L CONSUMER L. CTR., PAST IMPERFECT: HOW CREDIT SCORES AND OTHER ANALYTICS "BAKE IN" AND PERPETUATE PAST DISCRIMINATION 5–6 (2016), https://www.nclc.org/wp-content/uploads/2022/09/Past_Imperfect.pdf [https://perma.cc/YKU6-ZVPB] (listing about a dozen studies showing racial disparities in credit scores).

home, a car, or attend college—is partly a product of longstanding and overt discriminatory treatment, both in the private sector and with regulatory policy.[40] It is also, partly, the product of ostensibly colorblind structural and systemic impediments to such access.[41]

People of color historically have been (and often remain to this day) unable to borrow on the same terms as white borrowers. FICO scores correlate with race,[42] whether as a consequence of overt discrimination in the construction of the algorithm or (more likely) as a consequence of generations of bias that have resulted in people of color having less accumulated wealth, living in poorer neighborhoods, and having limited access to conventional financial services and sources for building credit histories.[43] The intuition that discrimination has persistent effects and may not be overt gave rise to the Supreme Court's acceptance in *Griggs* that proving a statistical disparity should satisfy a prima facie case of discrimination and shift the burden of justification to the defendant.[44]

These insights are doubly relevant where decisions are made using AI, which will both reflect and conceal its reliance on inputs that may themselves be rooted in discrimination.[45] Algorithmic lending practices intersect with the legacy of past discrimination in at least two ways.

First, in terms of its inputs. AI is dependent on the data input to produce machine learning. A popular term among computer programmers is GIGO—"garbage in–garbage out."[46] A model is only as good (or as bad) as the data that it processes. And data relevant to lending decisions can itself be a product of discrimination. For example, redlining policies worked by identifying locations where mortgage lending and related financial services were unavailable.[47] Although redlining practices were outlawed with enactment of the Fair Housing Act, this history of federally-sanctioned segregation in housing and residential lending

40 *See* KEEANGA-YAMAHTTA TAYLOR, RACE FOR PROFIT: HOW BANKS AND THE REAL ESTATE INDUSTRY UNDERMINED BLACK HOMEOWNERSHIP (2019).

41 *See* ROTHSTEIN, *supra* note 39; TAYLOR, *supra* note 40.

42 For a review of nearly a dozen studies showing racial disparities in FICO and related credit scores, see RACIAL JUST. & EQUAL ECON. OPPORTUNITY PROJECT, *supra* note 39.

43 *Id.*

44 Griggs v. Duke Power Co., 401 U.S. 424, 430 (1971) (noting that "practices, procedures, or tests neutral on their face, and even neutral in terms of intent, cannot be maintained if they operate to 'freeze' the status quo of prior discriminatory employment practices").

45 *See, e.g.*, Prince & Schwarcz, *supra* note 10.

46 *Work with New Electronic 'Brains' Opens Field for Army Math Experts*, HAMMOND TIMES, Nov. 10, 1957, at 65.

47 *See* ROTHSTEIN, *supra* note 39, at 145–46.

persists today.[48] Additionally, banks and ATMs may be less present in communities of color, whose residents rely on check-cashing, pay-day-loan, and other storefront financial service products for day-to-day access to funds.[49]

Algorithmic lending practices also implicate historic legacies of discrimination in terms of the outputs they enable. Without the financial services of data aggregators, consumer lending would be stuck in early twentieth-century brick and mortar pawn shops and rent-to-own retailers located in segregated and impoverished neighborhoods. Conventional lenders mostly did not extend credit to consumer borrowers, especially not to poor borrowers or borrowers of color. With AI, credit is less constrained, but its cost and terms are determined through the use of potentially biased algorithms that rely on big data and digital footprints.[50]

2. Algorithmic Discrimination and Predation

Discrimination law has been, historically at least, mostly concerned with remediating a lack of access to credit. But when we speak of "algorithmic bias" in consumer lending, we worry that the historical focus on credit constraint alone may ignore a more harmful set of problems with algorithmic lending: discriminatory pricing of credit products and what we call "discriminatory predation" in the terms and marketing of such credit.

a. Beyond Credit Constraint

One can discriminate by denying credit or one can discriminate by granting credit on unequal price and nonprice terms. Credit constraint is, thus, not the only problem legislation and regulation seeks to redress. Moreover, it may not be the worst problem in modern consumer finance markets. An even greater aggregate harm may arise from predatory

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48 Indeed, enforcement actions for violation of the FHA and ECOA continue to focus on illegal redlining. *See, e.g.*, Press Release, U.S. Dep't of Just., Justice Department and Consumer Financial Protection Bureau Secure Agreement with Trident Mortgage Company to Resolve Lending Discrimination Claims (July 27, 2022), https://www.justice.gov/opa/pr/justice-department-and-consumer-financial-protection-bureau-secure-agreement-trident-mortgage [https://perma.cc/RSM5-Q7KY] (discussing settlement of redlining cause of action); Press Release, U.S. Dep't of Just., *supra* note 38.

49 *See, e.g.*, Sheila R. Foster, *Breaking Up Payday: Anti-Agglomeration Zoning and Consumer Welfare*, 75 OHIO ST. L.J. 57 (2014).

50 Tobias Berg, Valentin Burg, Ana Gombović & Manju Puri, *On the Rise of the FinTechs: Credit Scoring Using Digital Footprints*, 33 REV. FIN. STUDS. 2845, 2846 (2020).

(whether unfair, deceptive, or abusive) practices and contract design that encourage improvident borrowing by vulnerable populations.

As such, there are three categories of lending discrimination: (1) discriminatory credit denial; (2) lending, but through discriminatory inclusion of price and nonprice terms;[51] and (3) discriminatory predation—marketing expensive credit to vulnerable populations. All these forms of discrimination can have adverse effects on populations of color. AI holds implications for each of these discriminatory effects both because the data that machine learning relies on is culled from existing and past episodes of institutionalized racism, and because mechanized underwriting and other lending practices cannot fully remove human involvement.

b. Discriminatory Pricing, Pricing Discretion, and the Implications of Algorithmic Lending

One historic source of discrimination is the discretion a lender or loan officer might exercise when deciding to grant a loan and under what terms. In an era of government-sanctioned redlining, discretion in housing and mortgage markets worked to constrain populations of color from accessing conventional sources of credit.[52] The FHA and ECOA prohibit discrimination across consumer lending markets and mostly eradicate redlining, but discriminatory practices nonetheless continue.[53] Discretionary underwriting has worked to allow access to lending markets but through segregated pricing.

For example, in the lead-up to the mortgage foreclosure crisis in the early 2000s, discretionary yield spread pricing fostered discriminatory effects in high-priced subprime mortgage markets.[54] Loan officers, mortgage brokers, and others involved in the negotiation of residential mortgages were paid more for extending credit on more expensive terms

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51 Economists use the term "price discrimination" to refer to pricing that discriminates among consumers (here, borrowers) based on their demand elasticity (how much they are willing to pay). Here, we modify that formal definition in two ways. First, we recognize that where lending is involved, the "price" of a loan can be affected by ostensibly nonprice terms such as default interest rates, prepayment penalties, enhanced remedies, and others. Second, we use discrimination in the legal rather than the economic sense, referring both to the discriminatory treatment (intentional) and effects (unintentional) of the price and nonprice terms on which credit is extended to members of protected groups.

52 *See* ROTHSTEIN, *supra* note 39, at 11, 28.

53 For discussion of enforcement actions brought jointly by the DOJ and CFPB and alleging violations of the ECOA and FHA due to redlining by a nonbank mortgage lender, see Press Release, U.S. Dep't of Just., *supra* note 38.

54 The literature on yield spread premiums is vast. For one such article, see Justin P. Steil, Len Albright, Jacob S. Rugh & Douglas S. Massey, *The Social Structure of Mortgage Discrimination*, 33 HOUS. STUD. 759 (2018).

based on what were referred to as "yield spread premiums" (YSPs).[55] As a result, lending agents were incentivized not simply to "price discriminate"—the term that economists use to describe sellers' incentives to price a product up to the limit that each buyer or borrower is willing to pay[56]—but also to offer financial products and services to customers on prices that systematically differed depending on the race, national origin, or other protected attribute of these borrowers.[57] This discretionary pricing violates discrimination laws (both the FHA and ECOA) to the extent of its disparate impact, but Congress viewed ex post litigation as an insufficient remedy to this problem and effectively prohibited YSPs in residential mortgage markets.[58]

This statutory prohibition of YSPs was, however, limited to mortgage markets. Moreover, the lure of individualized discretionary pricing has been hard to regulate in other markets. For example, in the market for car loans,[59] economists continue to view price discrimination as beneficially enabling sellers and service providers to maximize profits through discretionary pricing.[60] But the economic practice of price discrimination may overlap with invidious discrimination as a matter of law.[61] Where price discrimination is due to different estimations of credit risk, it is not problematic. Where it is due to or results in racial bias that affects credit availability or terms, it is problematic. Although dealer markups may lead to price competition among dealers for lending relationships, this price discrimination works to the detriment of consumer borrowers where the market is not competitive, or information or power asymmetries are present.

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55 *See, e.g.*, Senate Banking Committee Hearing on Predatory Mortgage Lending Practices: Abusive Uses of Yield Spread Premiums (Jan. 8, 2002) (testimony of Prof. Howell E. Jackson) https://www.govinfo.gov/content/pkg/CHRG-107shrg84933/html/CHRG-107shrg84933.htm [https://perma.cc/2W49-8NEJ].

56 *See generally* Hal R. Varian, *Price Discrimination*, *in* 1 HANDBOOK OF INDUSTRIAL ORGANIZATION (Richard Schmalensee & Robert Willig eds., 1989).

57 Jackson, *supra* note 55, at 2.

58 Dodd-Frank Act Wall Street Reform and Consumer Protection Act § 1403, 15 U.S.C. § 1639b(c)(4).

59 *See, e.g.*, Butler, Mayer & Weston, *supra* note 21; *see also* Levitin, *supra* note 21, at 1279.

60 *See* Varian, *supra* note 56. Economists and policymakers are divided on the desirability of price discrimination, in that producers will provide the efficient amount of a product, albeit at a higher price to price inelastic consumers. Policymakers continue to find it problematic, prohibiting it in various contexts. *See* Robinson-Patman Act of 1936, 15 U.S.C. § 13(a).

61 *See generally* Ian Ayres, *Market Power and Inequality: A Competitive Conduct Standard for Assessing When Disparate Impacts are Unjustified*, 95 CALIF. L. REV. 669, 719 (2007) (distinguishing presumed competitive benefits from price discrimination and their problematic implications for disparate impact laws; concluding that it "would not be a misuse of competition or consumer protection law to restrict disparate impacts that are caused by anti-competitive conduct").

For this reason, economic price discrimination remains illegal to the extent it disparately impacts protected classes of borrowers, regardless of the credit market or the financial service provider that lends or enables such lending. An important exception remains, however. Lobbying to protect certain lending groups, especially in the car loan markets, has mostly succeeded in producing regulatory carveouts to protect this industry. For example, car dealers are excluded from the reach of the CFPB, regardless of the statutory source of its jurisdiction.[62]

Within the past few years, the FTC and state attorneys general have brought enforcement actions under the ECOA to redress legally discriminatory dealer markups in new and used car markets. These suits have resulted in large settlements with car dealers.[63] While the CFPB is restrained from bringing enforcement actions against car dealers, it nonetheless possesses jurisdiction over lenders to those dealers.[64] Its recent enforcement action against CAC, premised on its UDAAP jurisdiction, demonstrates the breadth of this shared enforcement jurisdiction.[65] Unlike the FTC suits against dealers, the CFPB suit against a car lender was not premised on the disparate impact of discretionary pricing models, but rather on the predatory contract design that AI enabled.

c. Terms Discrimination

Just as algorithms may be used to determine access to credit and credit pricing, they can also be used to establish the terms on which credit is extended. Algorithms can be used to determine the riskiness of a loan, and therefore what loan products will be made available to particular borrowers and on what terms. Just as credit histories and credit scores may determine the interest rate on a loan, the data collected by an algorithm may do the same, only with less transparency. To the extent

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62 Consumer Financial Protection Act of 2010 § 1029, 12 U.S.C. § 5519. The car dealership exemption in Dodd-Frank was the result of lobbying. *See, e.g.*, Steven Davidoff Solomon, *Protection Bureau's Stormy Path to Reform the Auto Finance Industry*, N.Y. TIMES: DEALBOOK (Dec. 1, 2015) https://web.archive.org/web/20230324150031/https://www.nytimes.com/2015/12/02/business/dealbook/protection-bureaus-stormy-path-to-reform-the-auto-finance-industry.html.

63 For discussion of actions brought against car dealers in Massachusetts, Illinois, Maryland, and New York, see FTC Letter, *supra* note 30. This letter notes that the FTC retained jurisdiction to bring enforcement actions under ECOA against nonbank entities, thus, it has jurisdiction to sue car dealers even though the CFPB has no jurisdiction over car dealers under the CFPA. *Id.*

64 *See, e.g.*, Adam J. Levitin, *The Fast and the Usurious: Putting the Brakes on Auto Lending Abuses*, 108 GEO. L. J. 1257, 1312 n.257 (2020) (noting that, despite car dealership exemption in the CFPA, the CFPB asserts "rulemaking authority over indirect lenders as 'covered persons,' 12 U.S.C. § 5481(6) and assignees are liable under TILA/Regulation Z for facial violations of the statute," and, in any event, possesses jurisdiction "applicable to indirect lenders under its UDAP power to prohibit deceptive acts and practices" (citations omitted)).

65 For discussion of the CFPB suit against CAC, see *supra* notes 18–22 and accompanying text.

that the algorithm relies on data that correlates with race, the effect will entrench past discrimination as an algorithmic fact and, further, produce effects that we argue should be cognizable as a matter of law. Professors Prince and Schwarcz describe the product of AI's reliance on proxy variables as "proxy discrimination."[66]

But scholars have not considered the invidious possibilities for AI's reliance on data scraped from across the Internet to affect more than access to credit at prices that resemble those available to others. This gap exists because the literature fails to address the practical fact that interest rates are not the only terms that may change with the algorithm's risk determination. Default interest and penalties, arbitration, class waivers, kill switches, and other remedial provisions and practices may be chosen by AI and, thus, mask the true cost of the loan.

Regulators have not missed this practical reality, fortunately. The enforcement action brought by the CFPB against CAC is premised on precisely this issue—the "sweat box" lending terms that in past markets only the most desperate borrowers would agree to.[67] With AI driven marketing and contract design, lenders can—and increasingly are—learning about a larger circle of vulnerable borrowers. Problematically, we fear that these vulnerable borrowers will be disproportionately borrowers of color.

d. Predation in Credit Marketing

But there is a yet more insidious use of AI in consumer lending. Big data and machine learning can be combined for marketing purposes to identify customers who might be willing to purchase high-cost credit or to ignore credit offered on hidden terms and the "financial products" containing these terms. Once potential borrowers are identified and complex contracts designed for various sorts of borrowers, AI can be relied on to sort among both—to propose price and nonprice lending terms on an individuated basis to maximize lenders' profits but not minimize borrowers' risk of default.

We have written previously about how predatory lending can cause consumer harms, even in competitive credit markets.[68] The key is in recognizing that consumers are subject to a variety of cognitive and heuristic biases as well as time-inconsistent preferences.[69] Consumers are

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66 *See* Prince & Schwarcz, *supra* note 10, at 1305.

67 *See* Mann, *supra* note 22.

68 Susan Block-Lieb & Edward J. Janger, *The Myth of the Rational Borrower: Rationality, Behaviorism, and the Misguided "Reform" of Bankruptcy Law*, 84 TEX. L. REV. 1481, 1484 (2006) [hereinafter Block-Lieb & Janger, *Myth*]; Edward J. Janger & Susan Block-Lieb, *Consumer Credit and Competition: The Puzzle of Competitive Credit Markets*, 6 EUR. COMPETITION J. 68 (2010).

69 Block-Lieb & Janger, *Myth*, *supra* note 68, at 1489–544.

susceptible to overindebtedness because of cognitive error, and because some consumers are hardwired to privilege present over future consumption.[70] Consumer finance facilitates present consumption, but the cost in future periods can be quite severe. As we have discussed elsewhere, lenders may seek to exploit this, encouraging consumption up to the point that the risk of nonrepayment or default becomes material.

At a certain point, the risk of default and nonpayment may render the consumer loans unprofitable for the lender. But consumer borrowers often make payments on loans in default;[71] and they may be especially motivated to continue to make payments in this sort of "sweat box" of a loan to protect their cars or their homes.[72] There is often a significant gap between what a clear-eyed consumer might choose as a future debt load and the one that maximizes profits to lenders. In our opinion, seeking to saddle consumers with profitable, but excessive, debt is an important example of unconscionable predation in consumer protection law and unfair or abusive lending in consumer protection regulation.

e. Discriminatory Predation

Big data can help lenders identify targets for predation. It can identify consumers who are willing to buy goods on credit. It can identify homeowners with credit card debt as targets for refinancing their residential mortgage or a home equity line of credit (HELOC). It can identify other characteristics of vulnerability. Big data and AI can help consumer lenders identify vulnerable customers who may be willing to borrow on predatory terms.

These sorts of predatory terms might include: (1) interest rates significantly in excess of that indicated by the debtor's payment history; (2) terms that indicate that the loan may not be sustainable, such as negative amortization; (3) large prepayment penalties, especially if coupled with a high underlying interest rate; (4) harsh remedies that exceed the anticipated loss associated with the borrower's default, such as high default rates, cross-collateralization and cross-defaulting with other loans, and hair triggers that give rise to immediate acceleration.[73] Algorithmic marketing of credit may encourage borrowers to get in over their heads; predatory terms give the lenders the power to yank the rug out from under borrowers' feet.

Predatory credit disproportionately impacts borrowers along racial and ethnic lines, not because of race per se, but because of the legacy of

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70 *Id.* at 1536–45.

71 Mann, *supra* note 22, at 384–86.

72 *Id.* at 389–91.

73 Block-Lieb & Janger, *supra* note 33.

racism.[74] Once the algorithm is set, individual borrowers may be denied credit or may borrow on terms unnecessarily harsh or expensive, regardless of whether the AI accurately has identified them as a borrower of color. The consequent harms—overindebtedness, expensive credit, and harsh remedies—need not arise from lenders' intent to discriminate or even their indifference to discriminatory effects. They are independently problematic. But the harms of predation and discrimination may overlap in "predatory discrimination" that reinforces systemic inequalities. The disparate impact of algorithmic bias further compounds the harm of this algorithmic predation.

B. *The Particular Perils of AI: Scope and Transparency*

The behaviors discussed above—credit constraint, terms discrimination, and predation—are not new. This Section considers how those behaviors and the ability to regulate them are transformed by AI. AI increases the ability of lenders to identify and characterize potential borrowers for both underwriting and marketing purposes. Second, these decisions are not transparent, either with regard to the data used or the identity of the decision maker.

1. Scope and Granularity

For some, it is not hard to remember when consumer lending was largely a local enterprise, dominated by store credit and charge cards issued by merchants. It was not until the 1980s that national credit card networks emerged. These networks were enabled by developments in computerization, which created the possibility for risk-based pricing and differentiation among credit products.[75] Initially, differentiation among credit card holders and other consumer borrowers was largely dependent on the credit-reporting agencies, which, in turn, relied on the creditors in the financial markets to furnish the information on which the agencies relied. Universal credit-reporting agencies enabled national credit card networks and other markets based on risk-based pricing, but the differentiation was not particularly fine-grained.

With the advent of big data and data aggregation, however, lenders acquired access to vast amounts of information about potential borrowers, including borrowers who had not yet developed a

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74 Abbye Atkinson, *Rethinking Credit as Social Provision*, 71 STAN. L. REV. 1093, 1132–37 (2019); TAYLOR, *supra* note 40, at 3–4.

75 Block-Lieb & Janger, *Myth*, *supra* note 68, at, 1510–15.

conventional credit history. Facebook, Amazon, and data aggregators of all sorts mine clickstream data to draw detailed pictures of potential borrowers.[76] Access to big data did not simply broaden the range of information available to consumer lenders. AI also enables the disaggregation of data on as many narrowly defined grounds as a user of AI can imagine, including enabling lenders to find and market their financial products to the most vulnerable borrowers.

AI, thereby, allows consumer lenders to underwrite loans to a wider variety of people on bespoke terms. Personalized pricing has long been referred to by economists as "price discrimination."[77] The finer-grained comprehension of borrowers and their limits enabled through AI has opened the possibility for algorithmic discrimination.[78]

2. Transparency and Accountability

Underwriting decisions—lenders' determinations as to whom they should lend and on what terms—are rarely transparent. What motivates a lender to grant or deny a loan is information that is in the hands of the lender and not the borrower—at least in theory.[79]

Using AI for marketing and underwriting decisions ensures that lenders' decision-making processes are even less transparent. With traditional targeted marketing, a live person would set the screening criteria for advertising or loan approval and, in the event of litigation or regulatory inquiry, could be deposed on the content of this criteria. With AI, data requests may be chosen by the algorithm itself, including both the relevant data fields and their appropriate weights. Algorithmic decisions are, thus, made in a black box.

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76 Of course, data mines are fine grained but still imperfect. For example, one of the authors of this essay (a middle-aged man) was thought by the internet to be a teenaged girl due to his holiday buying patterns.

77 The economic literature on price discrimination is vast. For an early use and explanation of this term, see generally Ralph Cassady, Jr., *Techniques and Purposes of Price Discrimination*, 11 J. MARKETING 135 (1946).

78 For recognition of the implications of AI to modern consumer credit markets, see NAT'L A.I. ADVISORY COMM., YEAR 1, 33 (2023) (describing the "proliferation of AI and automated systems" used in credit markets as both "strain[ing] on civil rights agencies' ability to combat algorithmic discrimination, while simultaneously preventing and remedying traditional discrimination").

79 Inability to access this information complicates proof of discrimination. Adverse action is amenable to discovery in litigation. Documents can be reviewed, and decision-makers can be interviewed, but this would be an impossibly expensive way for consumers to access this information. For this reason, the federal consumer laws mandate disclosure of their rationale for "adverse action" in two places: the Equal Credit Opportunity Act § 701, 15 U.S.C. § 1691(d), and the Fair Credit Reporting Act, 15 U.S.C. § 1681(m).

In addition to obscuring the criteria used in credit marketing and underwriting decisions, AI also obscures the identity of the entity making the lending decision. Jack Balkin has written about algorithmic accountability.[80] Indeed, his point has been made graphic in Rebecca Crootof's postulation of so-called "killer robots."[81] There is something deeply disturbing about a person turning an autonomous algorithm loose on the world and then disavowing any harm caused by claiming that the "algorithm" or the "robot" did it. Yet, that is the potential effect of credit marketing or underwriting by means of AI. Aggregated data can be searched for attributes of susceptibility, or attributes of creditworthiness, or to maximize along both axes to increase the value of a portfolio as a whole.

Balkin would locate agency with the person who activated the algorithm.[82] Regulatory actors may well agree. But the algorithm may complicate fixing accountability absent regulatory authority to peer into the black box; it may also obscure the need for enforcement agents to ask questions about what's inside the black box in the first instance.

II. LENDING DISCRIMINATION: LEGISLATION AND REGULATION

The contours of discrimination in consumer lending were detailed above, as were the promises and perils associated with reliance on AI in consumer finance markets. This Part turns to law. The law proscribing discrimination, including discrimination in consumer credit and residential mortgage markets, is complex. It is also out of date in that it mostly fails to reflect the quickly evolving technological landscape of algorithmic lending. In addition to considering the statutory bases for liability for discrimination in consumer lending, this Part explains how the growth of AI in credit and other financial services has strained "civil rights agencies' ability to combat algorithmic discrimination."[83]

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80 Jack M. Balkin, Lecture, *The Three Laws of Robotics in the Age of Big Data*, 78 OHIO ST. L.J. 1217, 1219 (2017); *see also* Frank Pasquale, Lecture, *Toward a Fourth Law of Robotics: Preserving Attribution, Responsibility, and Explainability in an Algorithmic Society*, 78 OHIO ST. L.J. 1243 (2017).

81 Rebecca Crootof, *War, Responsibility, and Killer Robots*, 40 N.C. J. INT'L L. & COM. REG. 909, 910 (2015).

82 *See* Balkin, *supra* note 80.

83 NAT'L A.I. ADVISORY COMM., *supra* note 78, at 33 ("The proliferation of AI and automated systems used in education, healthcare, housing, employment, credit, policing and criminal justice, and access to consumer goods has therefore placed more strain on civil rights agencies' ability to combat algorithmic discrimination, while simultaneously preventing and remedying traditional discrimination.").

A. *Discrimination: Civil Rights Statutes and the Allocation of Enforcement Power*

Through numerous civil rights statutes applicable in various contexts—including obligations of fair lending under either the Fair Housing Act or the Equal Credit Opportunities Act—Congress has prohibited both (intentional) discriminatory treatment and selection criteria that have (unintentional) discriminatory effect.

1. Discriminatory Treatment

According to the FDIC: "The existence of illegal disparate treatment may be established either by statements revealing that a lender explicitly considered prohibited factors (overt evidence) or by differences in treatment that are not fully explained by legitimate nondiscriminatory factors (comparative evidence)."[84]

Disparate treatment claims require proof of discriminatory intent, but this proof can involve either direct or indirect evidence of such intent.[85] Moreover, this evidence need not show "bad faith, ill will or any evil motive on the part of [the recipient]."[86] Any intentional use of race, whether for malicious or "benign" motives, is subject to heightened scrutiny.[87] Discriminatory intent need not be the sole motive, but the evidence must demonstrate that a practice was adopted "'because of,' not merely 'in spite of,' its adverse effects upon an identifiable group."[88]

2. Disparate Impact

Discriminatory effect (also referred to as disparate impact) claims do not require proof of intent. Instead, "a plaintiff bringing a disparate-impact claim challenges practices that have a 'disproportionately adverse effect on minorities' and are otherwise unjustified by a legitimate rationale."[89]

84 FDIC, CONSUMER COMPLIANCE EXAMINATION MANUAL, at IV–1.2 (2021), https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/documents/4/iv-1-1.pdf [https://perma.cc/BB8B-8NP6].

85 *See, e.g.*, DOJ MANUAL, *supra* note 7.

86 Williams v. City of Dothan, 745 F.2d 1406, 1414 (11th Cir. 1984).

87 City of Richmond v. J.A. Croson Co., 488 U.S. 469, 493 (1989); Adarand Constructors, Inc. v. Pena, 515 U.S. 200, 226 (1995).

88 Pers. Adm'r of Mass. v. Feeney, 442 U.S. 256, 279 (1979).

89 Tex. Dep't of Hous. & Cmty. Affs. v. Inclusive Cmtys. Project, Inc., 576 U.S. 519, 524 (2015) (quoting Ricci v. DeStefano, 557 U.S. 557, 577 (2009)).

The Supreme Court has defined the term "discrimination" to include unintentional disparate impact in the context of employment discrimination under Title VII of the Civil Rights Act of 1964 (Title VII)[90] and the Age Discrimination in Employment Act of 1967 (ADEA).[91] More recently the Court extended this reasoning to discrimination claims under the FHA with its decision in *Texas Department of Housing and Community Affairs v. Inclusive Communities Project, Inc.*[92] The implications of *Inclusive Communities* extend beyond the facts of that case to include the residential mortgage industry, given the breadth of the FHA.[93] Considerable overlap exists between discriminatory lending claims brought under the FHA and those brought under the ECOA.[94] As is generally true of civil rights legislation, the statutory prohibition of discrimination is broadly stated under the ECOA.[95] Despite this overlap, the Supreme Court has not, in *Inclusive Communities* or elsewhere, explicitly addressed whether the ECOA also should be viewed as permitting disparate impact claims.[96]

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90 Griggs v. Duke Power Co., 401 U.S. 424, 431–32 (1971). Congress subsequently codified the holding of *Griggs* in Title VII. *See* 42 U.S.C. § 2000e-2(k).

91 Meacham v. Knolls Atomic Power Lab'y, 554 U.S. 84, 95–96 (2008).

92 576 U.S. at 534.

93 The Fair Housing Act, Title VIII of the Civil Rights Act of 1968, as amended, prohibits discrimination in the sale, rental, or financing of dwellings and in other housing-related activities on the basis of race, color, religion, sex, disability, familial status, or national origin. 42 U.S.C. §§ 3601–3606.

94 The ECOA prohibits "creditor[s]" from discriminating in "any aspect of a credit transaction." 15 U.S.C. § 1691(a). The ECOA is broader than the FHA prohibition of financial discrimination in that the ECOA covers both housing- and non-housing-related financial transactions; it is narrower than the FHA in that the ECOA covers only discrimination in credit transactions and not in the sale or lease related to such financing. *Compare id.*, *with* 42 U.S.C. §§ 3601–3606.

95 *See* 15 U.S.C. § 1691(a) ("It shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction—(1) on the basis of race, color, religion, national origin, sex or marital status, or age (provided the applicant has the capacity to contract); (2) because all or part of the applicant's income derives from any public assistance program; or (3) because the applicant has in good faith exercised any right under this chapter."). The ECOA expressly grants to "applicants" a private right of action supported by the possibility of both actual and statutory damages and a right to proceed through class action.

96 Enacted in 1974, it would be fair to assume that the ECOA embodied the same transformative and reparative agenda as the other roughly contemporary antidiscrimination statutes, and every circuit court to address the issue has agreed with this logic. For further discussion of this legislative history and doctrinal support, see Winnie F. Taylor, *The ECOA and Disparate Impact Theory: A Historical Perspective*, 26 J.L. & POL'Y 575 (2018); Francesca Lina Procaccini, *Stemming the Rising Risk of Credit Inequality: The Fair and Faithful Interpretation of the Equal Credit Opportunity Act's Disparate Impact Prohibition*, 9 HARV. L. & POL'Y REV. S43 (2015). *But see* Peter N. Cubita & Michelle Hartmann, *The ECOA Discrimination Proscription and Disparate Impact—Interpreting the Meaning of the Words That Actually Are There*, 61 BUS. LAW. 829 (2006). Perhaps importantly, courts of appeals have uniformly viewed Title VI of the Civil Rights Act of 1968 as prohibiting both discriminatory treatment and impact, although the Supreme Court has not ruled on this precise issue. DOJ MANUAL, *supra* note 7, § VII.A.

Discriminatory effects standards address distinct policy problems than discriminatory treatment.[97] As explained by the Supreme Court in *Griggs v. Duke Power Co.*, "[P]ractices, procedures, or tests neutral on their face, and even neutral in terms of intent, cannot be maintained if they operate to 'freeze' the status quo of prior discriminatory employment practices."[98] In this regard, undoing the legacy of past discrimination was and is intrinsic to the concept of shifting the burden of justification upon a showing of disparate impact.

The standard for disparate impact is generally understood in terms of a three-part test involving (1) an initial "prima facie" showing of discriminatory effect, (2) which may be rebutted with proof of the existence of a legitimate justification for the action or policy, so long as it is not shown that (3) there is an alternative that would achieve the same legitimate objective without (or with significantly less) discriminatory impact.[99] In *Inclusive Communities*, the Supreme Court noted that a plaintiff's prima facie case also requires proof of causation and emphasized the importance of "a robust causality requirement" to ensure that entities are not "held liable for racial disparities they did not create."[100] Although the precise role of causation in a prima facie case of disparate impact remains unclear, so far courts have mostly looked to statistical tests of causation.[101] How this requirement of causation interacts with the goal of undoing past discrimination is unclear. But, at the very least, use of algorithms to make lending decisions should not have the effect of making matters worse.

Although courts have applied this three-part test in all sorts of disparate impact cases regardless of their context, as a practical matter, it may be more difficult to satisfy a test of discriminatory impact under the ECOA than other civil rights statutes. The prima facie case for disparate impact requires identification of the specific policy or practice at issue. Markets that are closed or set obstacles to entry for a protected class of

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97 Proof of discriminatory treatment requires evidence of actual intent to discriminate, a standard that may be satisfied through circumstantial evidence of such intent. But it would be a mistake to view discriminatory effect standards as limited to circumstantial evidence of discriminatory intent. *See* DOJ MANUAL, *supra* note 7, § VII.A ("While a discriminatory impact or effect may also be evidence of intentional discrimination or disparate treatment, this section discusses disparate impact as a cause of action independent of any intent.").

98 Griggs v. Duke Power Co., 401 U.S. 424, 430 (1971).

99 Much of this Supreme Court precedent has arisen in the context of private litigation and public enforcement actions. Nonetheless, it is widely accepted that the same three-part test should "serve[] as a useful paradigm" governing assessment of non-adversary administrative investigations. *See* DOJ MANUAL, *supra* note 7, § VII.C.

100 Tex. Dep't of Hous. & Cmty. Affs. v. Inclusive Cmtys. Project, Inc., 576 U.S. 519, 542 (2015) (citing Wards Cove Packing Co. v. Atonio, 490 U.S. 642, 653 (1989), *superseded by statute on other grounds*, 42 U.S.C. § 2000e-2(k)).

101 *See, e.g.*, DOJ MANUAL, *supra* note 7, § VII.D.

borrowers would meet the prima facie standard for discriminatory effect and the ECOA looks to assist plaintiffs in making this prima facie case by entitling "applicant[s] against whom [an] adverse action [has been] taken" to a written statement "contain[ing] the specific reasons for the adverse action taken."[102]

The ECOA's disclosure mandates regarding adverse action are only partly helpful to litigants, however, because they only apply to one sort of discriminatory injury: credit constraint. Modern consumer lending markets are rarely closed outright to protected classes of borrowers.[103] Discriminatory effects in credit markets may also be accomplished by setting conditions to access rather than closing the door, as noted above.[104] In other words, the disparate impact of consumer lending on communities of color is a consequence of what lenders actually do—seek to profit off of poor people. They do this by forcefully marketing expensive consumer credit to poor people on harsh terms. As Abbye Atkinson has masterfully demonstrated, access to credit is not a panacea and should not be confused with social provision.[105] If credit is extended, rather than constrained, there was no adverse action and, thus, no way to require lenders to disclose their lending motives. Access to credit that is unsustainable and expensive can cause serious harm—perhaps more harm to individual borrowers than the societal harm that follows from credit constraint.[106] Discriminatory impact credit access may involve price and nonprice terms that differ along racial lines but do not present

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102 15 U.S.C. § 1691(d).

103 This is not to say that discriminatory credit constraint is nowhere to be found in current lending markets. For a complaint alleging exclusion of racial minorities from residential mortgages, see Amended Complaint ¶ 5, Bureau of Consumer Fin. Prot. v. Townstone Fin., Inc., No. 20-cv-4176, 2023 WL 1766484 (N.D. Ill. Feb. 3, 2023); and Press Release, Consumer Fin. Prot. Bureau, Consumer Financial Protection Bureau Files Suit Against Mortgage Creditor for Discriminatory Mortgage-Lending Practices (July 15, 2020), https://www.consumerfinance.gov/about-us/newsroom/cfpb-files-suit-against-mortgage-creditor-discriminatory-mortgage-lending-practices [https://perma.cc/5MKM-72SU].

104 *See* Christian E. Weller, *Credit Access, the Costs of Credit and Credit Market Discrimination*, 36 REV. BLACK POL. ECON. 7, 12, 13 tbl.2 (2009) (finding among other things that "[m]inorities and lower-income families paid more relative to their debt than whites and higher-income families").

105 *See* Atkinson, *supra* note 74, at 1098–104.

106 Predatory pricing and credit terms are not recent phenomena. For a fifty-year-old reflection on these issues, see, generally, DAVID CAPLOVITZ, THE POOR PAY MORE: CONSUMER PRACTICES OF LOW-INCOME FAMILIES (1967). For a more modern discussion, see, for example, MEHRSA BARADARAN, THE COLOR OF MONEY: BLACK BANKS AND THE RACIAL WEALTH GAP (2017).

barriers to consumer credit markets—a concept we call predatory discrimination.[107]

Statistical analysis of discriminatory impact is difficult enough where the impact is alleged to be credit constraint. Where the discriminatory effects instead involve disparate access and terms, statistical analysis no longer simply compares the demographics of those let in versus those kept out. It now must compare the terms on which some were let in as compared to the terms on which others enjoyed access—a statistical analysis that involves far greater complexity.

Even if plaintiffs succeed in making a prima facie case of disparate impact in this context, lenders might easily satisfy the next step by claiming that their failures to extend credit (inactions) or termination of an open account (actions) were not taken "on the basis of race" or some other protected category but, instead, for a "substantial legitimate justification"—especially concerns about the borrowers' creditworthiness. Because *Inclusive Communities* suggests that courts should allow defendants great "leeway to state and explain the valid interests served by their policies," lenders may succeed at this stage of the litigation by proving that race or some other protected class is historically correlated to default—even though that would turn implicit discrimination suits on their head by viewing systemic racism as a defense to liability.[108]

Finally, assuming defendants meet their burden of proof, plaintiffs might still prevail in their allegations of disparate impact if they show that lenders had a less or nondiscriminatory alternative available to them and did not use it. Plaintiffs' burden of proof on this third prong of the disparate impact test is never an easy one to bear given their limited access to industry-wide underwriting options.[109] Moreover, proof of less discriminatory alternatives is likely to be especially problematic in the lending context, given lenders' likely claim that the proposed alternative to their offer to lend would be to dry up credit markets for segments of the market and leave at least certain borrowers without the funds they voluntarily seek to access.[110] If the doors to consumer lending markets are

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107 The Court in *Inclusive Communities* noted that "[p]olicies . . . are not contrary to the disparate-impact requirement unless they are 'artificial, arbitrary, and unnecessary barriers'" and that "[c]ourts should avoid interpreting disparate-impact liability to be so expansive as to inject racial considerations into every housing decision." Texas Dep't of Hous. & Cmty. Affs. v. Inclusive Cmtys. Project, Inc., 576 U.S. 519, 521 (2015) (quoting Griggs v. Duke Power Co., 401 U.S. 424, 431 (1971)).

108 *Id.* at 541.

109 *See* Kevin Tobia, Note, *Disparate Statistics*, 126 YALE L.J. 2382, 2411 (2017).

110 RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 497 (8th ed. 2011) ("[P]eople who cannot borrow from a bank because they have poor credit may need a loan desperately, in which

opened to all on the condition that the cost of credit is higher for some, courts may view the policy implications of specific contractual terms as outside the scope of their competence.

3. Regulatory Enforcement

We suspect that regulators may be less reluctant than courts to engage in the balancing of interests inherent in regulating implicit discrimination in lending markets. But executive agents are governed by the same (or at least a similar) three-part test as are litigants (whether private or public) in setting out regulations to implement policies of disparate impact[111] under the FHA[112] and the ECOA.[113]

The Department of Housing and Urban Development (HUD) holds express statutory authority to interpret and enforce the FHA, including the power to make rules implementing the FHA.[114] HUD "has long interpreted the Act to prohibit practices with an unjustified discriminatory effect, regardless of whether there was an intent to discriminate."[115] Although all twelve circuit courts of appeal had held that the FHA prohibited both discriminatory treatment and discriminatory impact in covered housing transactions, "a small degree of variation has

event, if a ceiling is placed on interest rates, these unfortunates may be unable to borrow because the ceiling may be too low for the interest rate to compensate the lender for the risk of default.").

111 Since administrative investigations and the regulatory actions that follow such investigations are not "adversarial" in a strict sense, concepts of burden shifting may not be applicable. *See* DOJ MANUAL, *supra* note 7, § VII.C ("Agency investigations, however, often follow a non-adversarial model in which the agency collects all relevant evidence then determines whether the evidence establishes discrimination. Under this model, agencies often do not shift the burdens between complainant and recipient when making findings.").

112 42 U.S.C. § 3605(a)–(b)(1) (prohibiting discrimination on the basis of race, color, religion, sex, handicap, familial status, or national origin in any "residential real estate-related transaction," which includes "making or purchasing of loans or providing other financial assistance").

113 15 U.S.C. § 1691(a) ("It shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction—(1) on the basis of race, color, religion, national origin, sex or marital status, or age (provided the applicant has the capacity to contract); (2) because all or part of the applicant's income derives from any public assistance program; or (3) because the applicant has in good faith exercised any right under this chapter.").

114 42 U.S.C. § 3608(a)–(c). However, the CFPB holds neither enforcement nor regulatory jurisdiction under the FHA, even as relates to mortgage lending or mortgage lenders.

115 Implementation of the Fair Housing Act's Discriminatory Effects Standard, 78 Fed. Reg. 11460, 11460 (Feb. 15, 2013) (to be codified at 24 C.F.R. pt. 100) (subsequently revised by further regulation). HUD holds exclusive regulatory jurisdiction under the FHA, although aspects of the CFPB's regulatory jurisdiction under the ECOA might overlap with that of HUD under the FHA. The two agencies can but are not statutorily obliged to coordinate on their overlapping jurisdiction.

developed in the methodology of proving a claim of discriminatory effects liability."[116]

Under the Obama administration, HUD promulgated a regulation to clarify implementation of the FHA's discriminatory effects standard, which became final in 2013.[117] In 2020, the Trump administration's HUD sought to revise these regulations ostensibly to reflect the Supreme Court's decision in *Inclusive Communities*, but in fact watered down the test for disparate impact in this context.[118] "However, a preliminary injunction prevented the 2020 rule from ever going into effect. On June 25, 2021, HUD published a proposed rule to recodify the 2013 rule."[119] The Biden administration HUD regulation entered into effect in May 2023.[120]

Regulatory jurisdiction is also expressly granted under the ECOA. Initially, Congress granted regulatory jurisdiction to the Federal Reserve Board to implement the ECOA and the Board promulgated Regulation B within a short time after legislative enactment.[121] The Dodd-Frank Act shifted this grant of regulatory jurisdiction from the Federal Reserve Board to the CFPB in 2010, as well as gave the CFPB jurisdiction to regulate most "unfair, deceptive, and abusive" financial transactions.[122] In 2011, the CFPB restated the Federal Reserve's implementing regulation,[123] and in 2013 further amended Regulation B to reflect specific requirements set out in the Dodd-Frank Act.[124] Regulation B was also subsequently revised to create additional notice requirements in 2017,[125] 2021,[126] and 2023.[127]

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116 *Id.*

117 *Id.*

118 HUD's Implementation of the Fair Housing Act's Disparate Impact Standard, 85 Fed. Reg. 60288, 60288 (Sept. 24, 2020) (to be codified at 24 C.F.R. pt. 100) (enjoined). For decision enjoining the 2020 rule, see *Massachusetts Fair Housing Center v. Dept. of Housing and Urban Development*, 496 F. Supp. 3d 600 (D. Mass. 2020).

119 Reinstatement of HUD's Discriminatory Effects Standard, 88 Fed. Reg. 19450, 19450 (Mar. 31, 2023) (to be codified at 24 C.F.R. pt. 100).

120 *Id.*

121 12 C.F.R. pt. 202 (1975).

122 12 U.S.C. § 5531.

123 Equal Credit Opportunity (Regulation B), 76 Fed. Reg. 79442, 79444 n.15 (proposed Dec. 21, 2011) (to be codified at 12 CFR pt. 1002).

124 *Id.* at 79442–43 (requiring provision of free copies of all appraisals and other written valuations related to residential mortgage applications, as well as requiring creditors to notify applicants in writing that copies of all appraisals will be provided to them promptly).

125 *See* 12 C.F.R. pt. 1002 (2017) (relating to collection of certain data).

126 *See* 12 C.F.R. pt. 1002 (2021).

127 *See* 12 C.F.R. pt. 1002 (2023) (requiring covered financial institutions to collect and report to the CFPB data on applications for credit for small businesses, including those owned by women or minorities, as consistent with section 1071 of the Dodd-Frank Act).

Aspects of Regulation B, including those initially drafted by the Federal Reserve Board, remain controversial. Regulation B explicitly adopts the position that the ECOA prohibits both discriminatory treatment and discriminatory effects.[128] The regulation defines "applicants" broadly,[129] although perhaps not so broadly that it includes applicants whose loans were originated by car dealers.[130] Regulation B also clarifies that the ECOA "covers creditor activities before, during, and after the extension of credit,"[131] and that creditors are prohibited from making "oral or written statement[s], 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."[132]

To aid borrowers and agents of consumer protection, the ECOA requires detailed notice of adverse action, but is limited in that it only requires "creditors" to disclose specified adverse actions. On the question of compliance with obligations to provide notice of adverse actions that are the result of AI in lending, the CFPB recently clarified an earlier blog

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128 *See, e.g.*, Taylor, *supra* note 96.

129 The ECOA defines an "applicant" to mean "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." 15 U.S.C. § 1691a(b). As defined by Regulation B, an "applicant" includes "any person who requests or who has received an extension of credit from a creditor." 12 C.F.R. § 1002.2(e) (2021), *quoted in* Fralish v. Bank of Am., N.A., No. 20-cv-418, 2021 WL 4453735, at *2 (N.D. Ind. Sept. 29, 2021); Tewinkle v. Cap. One, N.A., No. 19CV1002V, 2019 WL 8918731, at *2 (W.D.N.Y. Dec. 11, 2019), *report and recommendation adopted*, No. 19-cv-1002, 2020 WL 2812519 (W.D.N.Y. May 29, 2020).

130 The CFPB initially issued a Bulletin providing guidance on compliance with the ECOA and reflecting the view that indirect car lenders are "creditors" within the meaning of the ECOA and Regulation B if "they regularly participate in a credit decision," even if they are also otherwise exempted car dealers. Consumer Fin. Prot. Bureau, CFPB Bulletin 2013-02, Indirect Auto Lending and Compliance with the Equal Credit Opportunity Act (Mar. 21, 2013), https://files.consumerfinance.gov/f/201303_cfpb_march_-Auto-Finance-Bulletin.pdf [https://perma.cc/GTQ9-D9UB]. This "rule" was reversed by Congress under its Congressional Review Act authority. *See* S.J. Res. 57, 115th Cong. (2018) (enacted); *see also* Kris D. Kully, Christa L. Bieker & Elyse S. Moyer, *Congress Invalidates CFPB's Indirect Auto Lending Guidance*, MAYER BROWN: CONSUMER FIN. SERVS. REV. (May 8, 2018), https://www.cfsreview.com/2018/05/congress-invalidates-cfpbs-indirect-auto-lending-guidance [https://perma.cc/6BC5-DPJ3].

131 Equal Credit Opportunity (Regulation B); Revocations or Unfavorable Changes to the Terms of Existing Credit Arrangements, 87 Fed. Reg. 30097, 30101 (May 18, 2022) (quoting BUREAU OF CONSUMER FIN. PROT., CFPB CONSUMER LAWS AND REGULATIONS, EQUAL CREDIT OPPORTUNITY ACT 1 (2015), https://files.consumerfinance.gov/f/documents/201510_cfpb_ecoa-narrative-and-procedures.pdf [https://perma.cc/QK9N-BKD4]).

132 12 C.F.R. § 1002.4(b) (2023). Enforcement actions brought jointly by the CFPB and DOJ under the ECOA and FHA typically involve discouragement, often coupled with evidence of intentional discrimination.

post.[133] Importantly, the CFPB issued a Circular that explains that lenders are obliged to provide this notice even though they may struggle to access this information.[134] A joint task force including the CFPB recently announced their intent to prosecute algorithmic discrimination, but pushback remains and further congressional action may be needed.[135]

An important difference between claims for liability under the ECOA and the FHA involves public access to the data needed to construct statistical analysis of disparate impact. The Home Mortgate Disclosure Act (HMDA) requires mortgage lenders to obtain and disclose data on residential mortgage borrowers, thus simplifying FHA antidiscrimination suits, but HMDA does not govern data on loans that are not secured by real estate, whether secured by personal property or unsecured consumer credit. Section 1071 of the CFPA directed the CFPB to enlarge Regulation B to mimic some of the requirements of the HMDA.[136] Recently, the CFPB finalized amendments to Regulation B to require covered persons to collect and report to the CFPB data on applications for credit for small businesses, including those that are owned by women or minorities.[137] Although directed by Congress to take this step, litigation was brought to question the CFPB's jurisdiction, and a federal district court has enjoined implementation of this final rule pending resolution of Supreme Court litigation on the constitutionality of the CFPB's source of financing.[138]

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133 Consumer Financial Protection Circular 2022-03: Adverse Action Notification Requirements in Connection with Credit Decisions Based on Complex Algorithms, 87 Fed. Reg. 35864, 35865 (June 14, 2022); *see* Robert Savoie & Brian Fink, *FinTech Regulatory Scrutiny Begins to Reflect a Maturing Industry*, 78 BUS. LAW. 581, 584–85 (2023).

134 *See* Consumer Financial Protection Circular 2022-03: Adverse Action Notification Requirements in Connection with Credit Decisions Based on Complex Algorithms, 87 Fed. Reg. at 35865 ("ECOA and Regulation B do not permit creditors to use complex algorithms when doing so means they cannot provide the specific and accurate reasons for adverse actions.").

135 Automated Systems Joint Statement, *supra* note 11; Press Release, Consumer Fin. Prot. Bureau, CFPB and Federal Partners Confirm Automated Systems and Advanced Technology Not an Excuse for Lawbreaking Behavior (April 25, 2023), https://www.consumerfinance.gov/about-us/newsroom/cfpb-federal-partners-confirm-automated-systems-advanced-technology-not-an-excuse-for-lawbreaking-behavior [https://perma.cc/G49N-TV4R]; Consumer Financial Protection Circular 2022-03: Adverse Action Notification Requirements in Connection with Credit Decisions Based on Complex Algorithms, 87 Fed. Reg. 35864.

136 15 U.S.C. § 1691c-2.

137 12 C.F.R. §§ 1002.107, 1002.109 (2023).

138 *See* Tex. Bankers Ass'n v. Consumer Fin. Prot. Bureau, No. 23-cv-00144, 2023 WL 4872398 (S.D. Tex. July 31, 2023).

4. Questions about AI

It is not a simple task to apply the multitier test of disparate impact, as set out in *Griggs*, *Inclusive Communities*, and related cases, to lending discrimination. Multiple bases for enforcement power in markets for consumer lending—discrimination and fairness—complicate this analysis. This task is made even more complex by the advent of AI.[139]

In a recent Request for Information, the CFPB focused in part on AI and consumer credit markets:

> [F]inancial institutions are starting to deploy artificial intelligence (AI) and machine learning (ML) across a range of functions. For example, they are used as virtual assistants that can fulfill customer requests, in models to detect fraud or other potential illegal activity, as compliance monitoring tools, and in credit underwriting. Should the Bureau provide more regulatory clarity under ECOA and/or Regulation B to help facilitate innovation in a way that increases access to credit for consumers and communities in the context of AI/ML without unlawful discrimination? If so, in what way(s)?[140]

We view the questions asked in this request as too narrow. It asks whether the CFPB should provide "regulatory clarity under ECOA and/or Regulation B" to help facilitate the possibilities for "innovation" through AI. By focusing solely on "innovation," the request failed to inquire about the potential for predatory practices through machine learning. The CFPB should have sought advice on the scope of its jurisdiction to prescribe unfair, deceptive, and abusive acts and practices that are predatory or discriminatory.

More recently, perhaps because of a change in administration, the CFPB has begun to consider relying on its fairness jurisdiction to address lending discrimination, including algorithmic discrimination that may not otherwise be explicitly covered by the ECOA or the other existing federal consumer regulation.[141] We discuss this extension of its unfairness jurisdiction in the Section below.

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139 *See, e.g.*, Prince & Schwarcz, *supra* note 10 (discussing, generally, difficulties in applying standards of proof of disparate action when AI governs decision making); Press Release, Dep't of Treasury, U.S. Treasury Department Issues White Paper on Online Marketplace Lending Industry (May 10, 2016), https://home.treasury.gov/news/press-releases/jl0452 [https://perma.cc/TV6E-A7XT] ("[D]ata-driven algorithms may expedite credit assessments and reduce costs[;] they also carry the risk of disparate impact in credit outcomes and the potential for fair lending violations.").

140 Request for Information on the Equal Credit Opportunity Act and Regulation B, 85 Fed. Reg. 46600, 46603 (Aug. 30, 2020).

141 *See, e.g.*, Fair Lending Report of the Consumer Financial Protection Bureau, 88 Fed. Reg. 43087 (July 6, 2023).

B. *Regulating Discrimination Through Jurisdiction Over Unfair and Abusive Practices*

Federal law prohibits "unfair, deceptive, and abusive acts and practices" (UDAAPs) and grants the CFPB jurisdiction to effectuate this prohibition through enforcement actions and rulemaking.[142] The CFPA broadly defines "unfairness" in consumer lending and other consumer finance markets as involving:

> (A) the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers; and
>
> (B) such substantial injury is not outweighed by countervailing benefits to consumers or to competition.[143]

Given the breadth of the definition of "unfairness," and the boundaries set in the ECOA and related legislation and regulation, the CFPB recently announced in a revised Supervision and Examination Manual that it had begun to explore "the interplay between unfair, deceptive, or abusive acts or practices and other consumer protection and antidiscrimination statutes."[144]

This statement prompted widespread objection. Industry actors questioned the propriety of the CFPB's reliance on its unfairness jurisdiction to remediate lending discrimination, emphasizing that a change of this nature should not occur through backdoor revisions to the Supervision and Examination Manual.[145] Indeed, the U.S. Chamber of

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142 12 U.S.C. § 5531(a); *cf.* 15 U.S.C. §§ 45(a)(1), 46(g) (granting similar jurisdiction to the Federal Trade Commission).

143 12 U.S.C. § 5531. Section 5531 also grants jurisdiction over "abusive" practices. They are defined as those that:

> (1) materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or
>
> (2) takes unreasonable advantage of—
>
> (A) a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
>
> (B) the inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service; or
>
> (C) the reasonable reliance by the consumer on a covered person to act in the interests of the consumer.

Id.

144 CONSUMER FIN. PROT. BUREAU, *supra* note 28, at 1.

145 *See, e.g.*, L. Jean Noonan, *Is Different Pricing for Non-Credit Products and Services Illegal Discrimination? Yes, Says the CFPB, Massachusetts, and the FTC*, JDSUPRA (Dec. 5, 2022),

Commerce and other industry actors sued to enjoin implementation of the Manual.[146] That litigation has stalled due to litigation pending in the Supreme Court relating to the constitutionality of the funding of the CFPB.[147] Presumably due to this litigation, the CFPB has not yet brought an enforcement action alleging disparate impact in any consumer lending market and seeking remediation premised solely on its UDAAP jurisdiction.

We view these industry objections as overblown. Although the statutory mandate to police "unfairness" in financial markets extends beyond issues of discrimination, we have no doubt that discriminatory treatment, as well as acts that have disparate impact on a protected class or classes, are "likely to cause substantial injury to consumers" covered by this jurisdictional grant.[148] To put it a different way, we have no doubt that lending discrimination is unfair and, for reasons discussed below, we believe that a showing of disparate impact should be sufficient to establish a prima facie case of unfairness.

Moreover, the overlap between the CFPB's antidiscrimination jurisdiction and its UDAAP jurisdiction is especially important when applied to predatory discrimination, as we have described it. Predatory discrimination certainly would fall within the "unfairness" jurisdiction simply because of the predatory nature of the conduct. Predatory discrimination occurs through contractual design involving unfair, deceptive, or abusive contract terms or practices. And while the ECOA might be viewed as a more specific grant of jurisdiction to combat discrimination in lending markets, liability under the ECOA protects only "applicants" against discrimination by "creditors." By contrast,

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https://www.jdsupra.com/legalnews/is-different-pricing-for-non-credit-2025128 [https://perma.cc/Y48Y-ESG7] ("[T]he CFPB's pronouncement raises many troubling issues. The first is whether this pronouncement is a proper use of the CFPB's authority. A close second, and one that the CFPB also committed to pursuing, is challenging *unintentional* discrimination under a disparate impact theory, which has no equivalent in unfairness law.").

146 Alan S. Kaplinsky, *U.S. Chamber of Commerce and Other Trade Groups File Lawsuit Against CFPB Challenging UDAAP Update to Exam Manual*, CONSUMER FIN. MONITOR (Sept. 29, 2022), https://www.consumerfinancemonitor.com/2022/09/29/u-s-chamber-of-commerce-and-other-trade-groups-file-lawsuit-against-cfpb-challenging-udaap-update-to-exam-manual [https://perma.cc/AZ9R-ZZ9X].

147 This litigation is stalled given the Supreme Court's grant of certiorari in *Consumer Financial Protection Bureau v. Community Financial Services Ass'n of America, Ltd.*, which would upend the CFPB's funding and jurisdiction more generally. 143 S. Ct. 978 (2023) (mem).

148 CONSUMER FIN. PROT. BUREAU, *supra* note 28, at 2 (noting that "substantial injury" usually involves monetary harm but that "[f]oregone monetary benefits or denial of access to products or services, like that which may result from discriminatory behavior, may also cause substantial injury" and that "in certain circumstances, such as unreasonable debt collection harassment or discriminatory conduct, emotional impacts or dignitary harms may amount to or contribute to substantial injury.").

UDAAP jurisdiction applies to "covered persons" under the CFPA––a much broader group of potential defendants or regulated entities. In addition, the ECOA creates a private right of action, while there is no private right of action to pursue UDAAP claims. The ability to combat unfairness in consumer lending markets, thus, applies only to regulators––the CFPB, FTC, and state attorneys general.

It is helpful that the structure of proof under the two standards resemble each other. Like the test for disparate impact, the test of unfairness under the CFPA is a burden-shifting and balancing test that starts with a finding of substantial injury, but then allows the defendant to show that an act or practice is not unfair despite the "substantial injury" it causes[149] because the consumer could reasonably have avoided this injury. In addition, even unavoidable and substantial injury may not fit within the definition of unfairness if injury to consumers is "outweighed by countervailing benefits to consumers or to competition."[150]

This is similar to the burden-shifting approach applied through *Griggs* and *Inclusive Communities*, albeit in a two-, instead of three-, step fashion. Subsection (A) requires a showing that the lending practice is likely to cause substantial injury; subsection (B) allows the lender to validate the practice as legitimate either in terms of benefits to the consumer or to competition in the marketplace.[151] If anything, the rebuttal prong in subsection (B) of the test of unfairness constitutes a broader balancing test than that found in either *Griggs* or *Inclusive Communities* or related cases. This expansion is appropriate. Because the test of unfairness extends beyond discriminatory effects, it invites consideration of a wider variety of benefits to offset the harm than merely whether the commercial practice minimizes discriminatory impact.

Although the statutory definitions of "unfair" and "abusive" practices might well be characterized as premised on similar balancing and burden-shifting standards as those set out in *Griggs*, *Inclusive Communities*, and their progeny, industry actors have contested positions taken by the CFPB that discrimination might fit within its UDAAP enforcement jurisdiction.[152] Pressure for an expansive scope of authority exists, however, because the ability to contain algorithmic discrimination under this preexisting disparate impact doctrine is unclear.[153] But reliance on UDAAP (or UDAP) jurisdiction may be insufficient to resolve the problems that AI creates for prima facie proof

149 The definition of "unfairness" under the CFPA is (and was designed to be) nearly identical to that granted to the FTC under the FTC Act. *See* 12 U.S.C. § 5531(c)(1); *cf.* 15 U.S.C. § 45(n).

150 12 U.S.C. § 5531(c)(1)(B).

151 *Id.* § 5531(c)(1)(A)–(B).

152 *See supra* text accompanying notes 145–47.

153 *See, e.g.*, Klein, *supra* note 24; Klein, *supra* note 27; Prince & Schwarcz, *supra* note 10.

of disparate impact or causation because similar burden-shifting problems arise here, too.

In the next Part, we turn to tort law to better understand how balancing and burden-shifting standards work and how to unify the tests for discrimination and discrimination as unfairness.

III. A REVERSE HAND RULE FOR ALGORITHMIC LENDING: *IMPACT IPSA LOQUITUR*

This Article began with CFPB Director Chopra's remarks on the importance of disparate impact analysis to address algorithmic lending discrimination. In Part II, we described the standard for disparate impact as involving an initial prima facie case followed by two opportunities for rebuttal; we also sought to place discrimination within a broader context of unfairness and existing consumer protection regulation of predation. In this Part, we seek to unify the two approaches in the context of algorithmic lending.

We situate disparate impact analysis within a family of tort law rules that Calabresi and Klevorick refer to as "reverse Hand rules."[154] Under these rules, the burden of proof for establishing an element of a tort shifts upon presentation of circumstantial evidence.[155] This "burden shift" can occur with regard to either breach of duty, scienter, or causation of harm.

We noted above that use of AI to make underwriting or marketing decisions increases the information asymmetry between lenders and those who would enforce antidiscrimination and fairness norms. Moreover, since AI relies on data that incorporates the effects of past discrimination, use of AI to make lending decisions is likely to entrench and exacerbate those patterns through the use of unfair or predatory loan terms. If both of those assumptions hold, the effects are far reaching.

On the one hand, if AI generated underwriting or marketing is shown to have a disparate impact, it may not be sufficient to show that there is a correlation with default. It may be further necessary to show that any risk adjustments are fair under the circumstances and not overreaching. On the other hand, unfair practices themselves may disproportionately harm people of color, such that a showing of predatory lending or marketing should cause the regulator or court to inquire into the racial impact of the practice. In other words, a showing of either disparate impact *or* unfairness should trigger an obligation to

154 Guido Calabresi & Alvin K. Klevorick, *Four Tests for Liability in Torts*, 14 J. LEGAL STUD. 585, 588 (1985); Calabresi & Hirschoff, *supra* note 36, at 1058–59.

155 Byrne v. Boadle (1863), 159 Eng. Rep. 299; 2 H. & C. 722.

prove that the algorithm is not discriminatory *and* that the credit it offered is not on unfair terms.

A. *Circumstantial Proof of Negligence*

The *Griggs* test of discriminatory effects was not expressly contained in the FHA as originally enacted, but neither was this disparate impact approach written on a clean slate.[156] Mental states like intent and complex standards like negligence are often difficult to prove with direct evidence. Only rarely will a defendant say what they are thinking out loud, revealing their racism, misogyny, carelessness, or bad faith. Courts have long addressed information asymmetries by allowing mental states to be proven through circumstantial evidence. The so-called "badge[s] of fraud" look at the attributes of a transaction to determine whether it is designed to hide assets.[157] The so-called "red flag" doctrine has allowed courts to identify bad faith in commercial law based on objective criteria.[158] In these cases, circumstantial evidence triggers a burden shift that satisfies the plaintiff's prima facie case of liability and shifts the burden to the defendant to justify their behavior. In tort law, these burden-shifting rules are sometimes referred to as "reverse Hand rules."[159] Rather than requiring the plaintiff to bear the full burden of proving negligence or causation, courts allow circumstantial evidence to shift the burden of going forward with the evidence to the defendant.

1. The Hand Rule

The starting point for understanding "reverse Hand rules" is first to understand the "Hand rule" for determining whether a defendant has

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156 For discussion of the legislative and regulatory sources for the *Griggs* doctrine, see Olatunde C.A. Johnson, *The Agency Roots of Disparate Impact*, 49 HARV. C.R.-C.L. L. REV. 125 (2014).

157 Twyne's Case (1601), 76 Eng. Rep. 809, 810–11 (KB).

158 *See generally* Sepinuck, *supra* note 32.

159 Embedded in shifting burdens of proof are deeper concerns about risk tolerance and the difficulties of accomplishing social welfare through litigation premised on an adversarial system of dispute resolution. Tort law, like other laws, also addresses these difficulties through balancing tests that accept the presence of some levels of otherwise prohibited behavior on the grounds that efforts to eradicate such behaviors will have countervailing implications. Tort law does not find actors liable for the failure to take every possible preventative measure; nor does it find liability on the basis of mere "but for" causation. Similarly, antidiscrimination laws accept proof of business necessity to balance allegations of disparate impact; proof of "substantial injury" to consumers may not establish the "unfairness" of the act or practice complained of if the consumer could have avoided her own injury or if the injury is "outweighed by countervailing benefits to consumers or to competition." 12 U.S.C. § 5531(c)(1)(B).

exercised reasonable care. In *United States v. Carroll Towing Co.*,[160] an unattended grain barge sank when it was struck by another boat that had come loose from its mooring. The question presented was whether the owner was contributorily negligent because there was no "bargee" present on the boat when the accident occurred. In ruling, Judge Learned Hand asked whether the cost of precaution (paying the bargee) was greater than the foreseeable harm discounted by the probability that an accident might occur.

The key point for our purposes is not the formulation of the negligence standard, so much as that proof of negligence was part of the plaintiff's prima facie case.[161] Without evidence of a lack of precaution, the case would have been dismissed. In many cases, however, the information needed to prove lack of care will be in the control of the defendant and inaccessible to the plaintiff. Under the Hand formulation, plaintiffs are out of luck.

This is precisely the situation that arises in lending discrimination cases and that is enhanced through the use of nontransparent algorithms. The plaintiff may be able to establish racially disparate lending patterns but does not have access to the algorithm and, therefore, cannot show the source of discrimination.

2. Reverse Hand Rules

The Hand rule (requiring a showing of breach of duty as part of the plaintiff's prima facie case) has the effect of entrenching and rewarding information asymmetries. To counter such asymmetries, tort law often adopts a burden-shifting rule.

a. *Res Ipsa Loquitur*

One doctrine of this sort is the doctrine of *res ipsa loquitur*, classically articulated in *Byrne v. Boadle*.[162] There, a barrel fell out of a building and injured a bystander. The plaintiff had no way of knowing why or how the barrel had gotten loose, but as the court pointed out:

> There are certain cases of which it may be said *res ipsa loquitur*, and this seems one of them . . . . A barrel could not roll out of a warehouse

160 159 F.2d 169 (2d Cir. 1947).

161 For discussion of the numerous possible foundations for the Hand rule, see Stephen G. Gilles, *On Determining Negligence: Hand Formula Balancing, the Reasonable Person Standard, and the Jury*, 54 VAND. L. REV. 813, 819–20 (2001), which finds five distinct possible norms to justify the Hand rule: wealth maximization, social welfare maximization, social contract, egalitarianism, and virtue.

162 Byrne v. Boadle (1863), 159 Eng. Rep. 299; 2 H. & C. 722.

> without some negligence, and to say that a plaintiff who is injured by it must call witnesses from the warehouse to prove negligence seems to me preposterous.[163]

No additional proof was necessary because the "thing spoke for itself."[164]

The doctrine of *res ipsa loquitur* describes a set of facts where the occurrence of an accident is alone sufficient to raise an inference of negligence: something occurred that does not ordinarily occur without negligence, the instrument of harm was in the defendant's exclusive control, and there was no evidence of contributory negligence.

Reverse Hand rules have been used to remedy information asymmetries in tort litigation, even where exclusive control is contested. In *Ybarra v. Spangard*,[165] a medical malpractice case, for example, a plaintiff hospitalized for an appendectomy ended up with a shoulder injury. Because it was difficult for the plaintiff to understand how an appendectomy might have led to a shoulder injury, absent negligence in the procedure or its aftermath, suit was brought. The problem in that case was exclusive control. There were six doctors and nurses in the operating theater, hence none had "exclusive control" over the plaintiff. The court concluded, however, that the team had control and that all members of the team would be considered negligent (and jointly and severally liable) unless fault could be placed on any one member of the team, or a team member was able to present affirmative evidence to exclude themselves.[166] The inference of negligence and shifting of various burdens of proof were necessary in these cases because information regarding the events leading up to the accident was solely in the control of the defendant.[167]

The structure of *res ipsa loquitur* resembles disparate impact analysis in discrimination cases. It also resembles the unfairness standard in that its two-pronged test balances proof of harm to consumers against the benefits that may accrue (whether on an individuated basis or as applied to the market as a whole). Discriminatory impact adds strength to a case of unfairness, for example, if predatory terms are unevenly inserted in some lending agreements and not others. It is strengthened further if the pattern of this predation is uneven across protected classes.

In short, if it can be shown that an algorithm produces disparate impact, it should trigger a burden to establish that the disparate impact is not caused by discrimination present or past. But also, if it can be shown

163 *Id.* at 301.

164 *See Res Ipsa Loquitur*, MERRIAM-WEBSTER, https://www.merriam-webster.com/legal/res%20ipsa%20loquitur [https://perma.cc/N6U5-9GMU].

165 154 P.2d 687 (Cal. 1944).

166 *Id.* at 689–90.

167 *Id.* at 691.

that the algorithm is being used to impose harsh terms or identify vulnerable populations—if it is unfair—then that too should trigger a burden shift to justify the decisions in consumer benefit.

b. Circumstantial Proof of Causation

Tort liability is not just a function of proving culpable behavior (negligence, discrimination, or predation). It is also necessary to show that the culpable behavior caused harm. Again, tort law provides examples of information-forcing burden shifts to assure that culpable behavior does not slip through the cracks: "self-proving causation" and "lost chance causation." One deals with the situation where a harm might result from multiple possible causes, and the other deals with situations where there is an existing baseline risk, but negligence increases the probability that the harm will occur.

Both of these concepts are important when addressing claims of discrimination in a multi-factor decision like extending credit. In deciding *Inclusive Communities*, the Supreme Court emphasized the importance of proof of causation to the satisfaction of a plaintiff's initial prima facie case.[168] Causation may be difficult to prove in this context where there are multiple actors involved in the algorithmic decision making and especially where the claim is that predatory discrimination targeted a vulnerable borrower that was, by design, likelier to default than most.

Self-Proving Causation—Substantial Factor. An injury may have multiple causes. Two forest fires may merge and burn down a house;[169] two hunters may negligently fire simultaneously and injure their companion.[170] Causation-in-fact must be proven by a preponderance of the evidence, but sometimes it is mathematically impossible to do so, even where the universe of possible causes is finite. The solution is to use a reverse Hand rule—to shift the burden to the defendant to exclude themselves.

In *Zuchowicz v. United States*,[171] a patient was prescribed the drug Danocrine to address her endometriosis. However, the prescription erroneously instructed her to take twice the recommended dosage. As a result of the misprescription, Ms. Zuchowicz allegedly developed pulmonary hypertension, which resulted in complications during pregnancy from which she ultimately died. The problem was proving that the overdose caused the illness and death.

168 Tex. Dep't of Hous. & Cmty. Affs. v. Inclusive Cmtys. Project, Inc., 576 U.S. 519, 527 (2015).

169 Kingston v. Chicago & N.W. Ry., 211 N.W. 913, 914 (Wis. 1927).

170 Summers v. Tice, 199 P.2d 1, 1–2 (Cal. 1948) (in bank).

171 140 F.3d 381 (2d Cir. 1998).

Judge Calabresi weighed in on circumstantial proof of causation. To raise an inference of causation, the plaintiff needed to show that negligence was a substantial factor in causing the injury. To do so, it was sufficient to show that the negligent act (the overdose) increased the risk of a certain type of injury (pulmonary hypertension) and that the risk materialized, at least in part, due to the negligent act.[172] It remained open to the defendant to rebut the inference and show that the injury was probably not caused by the overdose, but in cases such as this, the burden of going forward is often dispositive.

The effect of the *Zuchowicz* rule is to encourage precaution. If one takes a step that increases a known risk (i.e., negligently prescribing a drug), then one is potentially on the hook should things go wrong. To do otherwise would allow negligent defendants to slip out from negligence any time proof of harm was a matter of probability.

Lost Chance Causation—Background Risks. A second problem faced by tort plaintiffs is the problem of background risk. Whenever you drive in a car, for example, there is a nonnegligible background risk of an accident, regardless of your own reasonable care. In *Herskovits v. Group Health Cooperative of Puget Sound*,[173] a lung cancer patient's chance of survival was reduced by a delayed diagnosis. The problem the court faced in addressing claims of negligence brought by the patient's survivors was that, given the earlier diagnosis, the patient's probability of death was still greater than fifty percent. As a result, even if his chances of death were increased due to the defendant's negligence, the plaintiffs could not show by a preponderance of the evidence that the delayed diagnosis caused the plaintiff's death. The court solved the problem by focusing on the reduced chance of survival. Change in the background risk was sufficient to satisfy the requirement of causation.[174]

B. *Proof of Algorithmic Discrimination*

These lessons from tort law can assist in thinking about how to approach disparate impact analysis in the algorithmic lending context in three ways. First, they provide a rationale for the balancing tests used in both disparate impact and unfairness analyses. Second, they identify the

[172] *Id.* at 391.

[173] 664 P.2d 474 (Wash. 1983).

[174] There was a disagreement between the majority and a concurring judge over whether the lost chance was sufficient to establish the negligence as the cause of death (majority), or only that the harm was recharacterized as the lost probability of surviving (concurrence). *Compare id.* at 474, *with id.* at 485–86 (Pearson, J., concurring). This disagreement did not matter with regard to allowing the case to go forward, but it would have affected the calculation of damages.

rationales for shifting the burden of going forward embodied in reverse Hand rules. Third, they help us to address the multiple sources of statutory authority for regulating algorithmic lending discrimination, so that the relationship and synergy between discrimination and unfairness can be explained.

1. Proof of Discrimination, Unfairness, and Causation

When considering proof of lending discrimination causation in the context of lending discrimination, the dual bases of liability comes into play. If the trigger for liability is unfairness, then the question is whether the algorithm is the reason for the claim of substantial injury. If the trigger is disparate impact, the question is whether the algorithm caused the discrepancy in effects. The lesson of *Zuchowicz* is that, when thinking about a burden shift (*impact ipsa loquitur*), it is crucial to identify the harm that the algorithm is causing and to consider the resulting burden of justification. Is it denying access to credit for discriminatory reasons? Is it imposing harsh terms also for discriminatory reasons? Is it identifying targets for predation?

Each of these might be a basis for liability, but the causal link will differ depending on the allegations and, hence, whether a burden shift is triggered. This lesson can be applied to both antidiscrimination and unfairness doctrines. Under the ECOA, where the predicate is discrimination, logically the "impact" trigger will be either a disparate impact on credit access or credit terms. By contrast, if the predicate for liability is under the CFPB's unfair and abusive jurisdiction or a state UDAAP statute, the "impact" trigger will likely be the presence of a potentially predatory term, or the use of a potentially predatory marketing practice (a "dark pattern").

But there is a second, perhaps more important lesson from *Zuchowicz.* Self-proving causation finds causation-in-fact if the negligence increases the risk of harm. The discussion above suggests a synergistic interaction between liability based on discrimination and liability based on unfairness. On the one hand, unfairness increases the risk of discrimination, due to the residual effects of systemic racism. But on the other hand, discrimination raises the probability of unfairness through discriminatory terms or predatory marketing. Each burden shift does double duty with regard to causation.

This implication of self-proving causation has a crucial practical impact with regard to justification. Circumstantial proof of discrimination through disparate impact raises an inference of unfairness. Circumstantial proof of unfairness through evidence of unfair terms or predation may raise an inference of discrimination. This result

might seem harsh, but it should be noted that the black box nature of AI makes such rules imperative if one is to achieve the goal of repairing and reversing historic racism.

The distinct lesson from *Herskovitz* is even more important when thinking about algorithmic discrimination and predation. Lending decisions are always multi-factor inquiries. Consumer credit decisions always involve calculating and pricing the risk of default. Showing that the algorithm predicts default might appear to justify the use of AI. Similarly, showing that a particular piece of marketing data identifies willing customers might be sufficient to show a business justification and to rebut causation. But *Herskovitz* makes clear that discrimination or predation need not be the *only* or principal cause of predation or discrimination. They need only be implicated as part of the decision.

2. Algorithmic Discriminatory Predation—Linking Liability and Causation

There are, thus, a host of reasons why algorithmic underwriting and marketing of consumer loans is likely to produce credit decisions and credit terms that disproportionately harm communities of color. Moreover, the use of an algorithm is likely to make the source of that impact less transparent, and to increase the scale of its effect. Nor will issues of liability turn on whether the algorithm is adopted with any discriminatory scienter. As noted above, ECOA and other antidiscrimination statutes were adopted to disentrench legacy discrimination. *Herskovitz* suggests that linking the theories of liability—discrimination in underwriting and marketing—to the legacy of structural discrimination creates additional justifications for burden shifting, both with regard to liability and causation. Indeed, the synergy is striking, and strikingly different from the employment context. When consumer credit decisions are involved, disparate impact can raise an inference of both discriminatory harm and predatory harm, thus, creating the need for a double rebuttal that we call *impact ipsa loquitur*.

a. *Impact Ipsa Loquitur*—Discrimination

A showing of disparate racial impact is a prima facie basis for liability under *Griggs*, *Inclusive Communities*, and related case law. This doctrine shifts the burden of establishing a nondiscriminatory purpose of the algorithm to the creditor. The discussion above shows that disparate racial impact should be sufficient to shift the burden of justification for either credit underwriting or credit marketing. This is what we mean by *impact ipsa loquitur*. If harsher credit terms are present in loans offered to borrowers of color than other borrowers, we should be concerned both

about their discriminatory effects and the fairness of these predatory financial transactions. For the lender to evade liability altogether, it should, thus, be necessary to demonstrate both that the loans are being offered on equal terms and that the terms themselves are fair in light of the credit risk associated with the borrower.

b. *Impact Ipsa Loquitur*—Predation and Presumed Causation

The lessons of *Zuchowicz* and *Herskovitz* are that proving that the algorithm increased the probability of a loan denial might be sufficient to prove discrimination, but it might also have contributed to the imposition of a predatory interest rate. Disparate impact can cause unfairness, and evidence of predation increases the risk of discrimination. The presence of *either* predatory terms or disparate impact should raise an inference of discriminatory harm.

This linking of predation and discrimination has implications both for the prima facie case of disparate impact and for the nature of its rebuttal. A prima facie showing of disparate impact across a market for consumer lending raises an inference of discrimination, but lending, rather than refusing to lend, may also raise an inference of predation, whether through unfair or abusive conduct.

This has an important consequence along the causation axis, in two ways. Disparate impact is likely to cause predatory harm and predation is likely to have disparate impact. First, a consumer lender whose loan portfolio demonstrates disparate impact should be required to show not just that the criterion set out through AI is correlated with default risk, but also that the loans were offered on fair terms. Second, a lender who is shown to have engaged in unfair lending practices resulting in predatory discrimination should expect it to be part of its rebuttal burden to show not only that there is a legitimate business purpose for such terms, but also that the terms do not disproportionately impact a protected group. CAC, for example, should have faced an enforcement action framed both under the CFPB's unfairness jurisdiction and its jurisdiction to address discriminatory effects. That the lender is not bound to collect and report data on its loan portfolio, because this portfolio sits outside the scope of the HMDA and Regulation B, should not alter this burden of proof.

CONCLUSION

AI can serve useful functions in increasing access to credit and making lending more efficient, but it is also black boxes that enhance information asymmetries already present in consumer lending markets. The black box nature of AI also obscures reliance on data that reflect legacies of discrimination and thus serve as proxies for race and other

prohibited considerations. This opacity can frustrate both consumers seeking redress and regulators seeking to prevent algorithmic discrimination, predation, and predatory discrimination. Should the fact that AI reflects existing patterns absolve or implicate the algorithm? We argue against absolution in this Article.

One potential solution to these problems of proof would be to expand the jurisdictional basis of antidiscrimination litigation to include disparate impact with UDAAP and UDAP jurisdiction. We argued in this essay that these two jurisdictional grounds should be combined, with one supplementing the other, and that the burden-shifting rules that shift the obligation to present evidence from the plaintiff to the defendant inherent in both disparate impact and unfairness litigation should be "reversed" to address the problems of proof endemic to AI. In tort law, similar information-forcing burden shifts are sometimes called reverse Hand rules. Room for similar reverse Hand rules already exists in discrimination statutes like the ECOA and consumer protection statutes like the CFPA. We have shown how they can work together to combat both unfair and predatory practices.

Finally, the use of AI for underwriting and marketing decisions must be considered against the backdrop of a national history of structural and systemic discrimination. This unfortunate reality causes a synergy at the rebuttal or justification stage of the analysis. Unfair or predatory terms may correlate with race, and a showing of disparate impact may correlate with unfair terms. As a result, no matter whether the burden shift was triggered by discrimination or unfairness, the defendant should be required to justify the algorithm as both nondiscriminatory and fair.