

DISCRIMINATORY MAINTENANCE OF REO PROPERTIES AS A VIOLATION OF THE FEDERAL FAIR HOUSING ACT

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I. INTRODUCTION

As the foreclosure crisis continues to work a devastating path through the nation’s neighborhoods, it is leaving in its wake a glut of bank-owned homes, known as Real Estate Owned (REO) properties in the finance and housing industries. Many of these REO properties have been allowed to fall into deplorable states of disre-

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pair, causing harm to neighbors, communities, and local governments.

News reports regarding blighted REO properties describe an unpalatable litany of damage: one house with burst pipes, smashed and boarded up windows, and “overwhelming” odors of rotting food and decay;¹ another with chest-high weeds, a rodent infestation spilling over into the neighbor’s property, and surrounded by increased gang activity;² a third with a “disintegrating front porch,” exposed wiring, piles of rubbish, and infestations of rats, snakes, ants, bees, and termites.³ These properties were each owned by one of the nation’s largest banks at the time their condition was reported.⁴ Nor are properties like these the exception. A 2012 survey of approximately 400 REO properties in Los Angeles found that fully half of the homes were in a “state of blight,” and nearly a third were “seriously blighted.”⁵

Not surprisingly, poorly maintained REOs create a host of problems for neighborhoods and communities. Blighted properties pose health and safety risks in impacted communities due to pests, decay, and vulnerability to crime.⁶ Local governments are forced to spend millions of dollars to address code violations, perform maintenance mitigating dangerous or blighted conditions, demolish unsafe structures, and identify and contact those responsible for vacant properties.⁷ These expenditures strain budgets that could be used for other community priorities. The impact on the

¹ Tim Reid, *U.S. Cities Struggle with Blighted Bank-Owned Homes*, REUTERS (June 8, 2012), <http://www.reuters.com/article/2012/06/08/us-usa-housing-blight-idUSBRE85707320120608>.

² Jessica Garrison & Angel Jennings, *Second Bank Is Sued Over Blight*, L.A. TIMES (July 12, 2012), <http://articles.latimes.com/2012/jul/17/local/la-me-us-bank-slum-lord-20120717>.

³ Megan O’Matz & John Maines, *Bad-Neighbor Banks Neglect Thousands of South Florida Homes*, *Sun Sentinel Finds*, SUN SENTINEL (Apr. 28, 2012), http://articles.sun-sentinel.com/2012-04-28/news/fl-bad-neighbor-banks-20120428_1_banks-shift-vacant-homes-vacant-properties/3.

⁴ Each of the banks involved ranked among the top thirty banks in the U.S. by assets in 2013. See David Benoit, *The Top 50 U.S. Banks by Assets*, WALL ST. J. (Sep. 26, 2013), <http://blogs.wsj.com/moneybeat/2013/09/26/the-top-50-u-s-banks-by-assets/>.

⁵ Tim Reid, *supra* note 1.

⁶ See, e.g., Lea Deutsch, *Collateral Damage: Mitigating the Effects of Foreclosure in Communities*, 22 TEMP. POL. & CIV. RTS. L. REV. 203, 207–08 (2012).

⁷ U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-12-34, VACANT PROPERTIES: GROWING NUMBER INCREASES COMMUNITIES’ COSTS AND CHALLENGES 37 (2011) [hereinafter GAO-12-34], available at <http://www.gao.gov/products/GAO-12-34>; see also WILLIAM AGPAR, MARK DUDA & ROCHELLE NAWROCKI GOREY, HOMEOWNERSHIP PRES. FOUND., THE MUNICIPAL COST OF FORECLOSURES: A CHICAGO CASE STUDY (2005), available at <http://www.nw.org/network/neighborworksProgs/foreclosuresolutionsOLD/documents/2005Apgar-DudaStudy-FullVersion.pdf>.

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housing market is also significant. Vacant and foreclosed properties are well known to depress surrounding home values;⁸ poor maintenance can only exacerbate that effect. And as shoddy maintenance and neglect result in deteriorating appearances and physical conditions for REO properties, their availability for sale is adversely affected, constraining housing options in impacted communities.

These adverse effects have prompted an array of policy initiatives and lawsuits designed to combat the problem of poorly maintained REO properties. Federal regulators have developed standards for REO maintenance by lenders who are subject to their supervision.⁹ Major cities, including Los Angeles and Cincinnati, have sued big banks over blighted REO properties on a nuisance theory of liability.¹⁰ Chicago and more than a thousand other municipalities have enacted ordinances requiring registration of vacant properties and setting standards for their maintenance and repair.¹¹ Each of these efforts offers an important opportunity to create higher standards of accountability for financial institutions that own vacant residential properties.

Although these efforts are admirable, they overlook a disturbing reality in the servicing and maintenance of REO properties: a dimension of race discrimination in minority neighborhoods. Numerous reports have shown that communities of color were disproportionately targeted for the most expensive and toxic mortgages pedaled during the bubble, and as a result suffered disproportionately high foreclosures.¹² Now evidence sug-

⁸ See GAO-12-34, *supra* note 7, at 44–45.

⁹ OFFICE OF THE COMPTROLLER OF THE CURRENCY, COMPTROLLER'S HANDBOOK: OTHER REAL ESTATE OWNED 14 (2013), available at <http://www.occ.gov/topics/credit/commercial-credit/other-real-estate-owned.html>; FED. RESERVE BD., QUESTIONS AND ANSWERS FOR FEDERAL RESERVE-REGULATED INSTITUTIONS RELATED TO THE MANAGEMENT OF OTHER REAL ESTATE OWNED (OREO) ASSETS (2012), available at <http://www.federalreserve.gov/bankinforeg/srletters/sr1210.htm>.

¹⁰ See Garrison & Jennings, *supra* note 2 (discussing Los Angeles suits against U.S. Bankcorp and Deutsche Bank); Kermit J. Lind, *Can Public Nuisance Law Protect Your Neighborhood from Big Banks?*, 44 SUFFOLK U. L. REV. 89, 110 (2011) (discussing Cincinnati's suits against Wells Fargo and Deutsche Bank).

¹¹ See Mary Ellen Podmolik, *Chicago Loses Court Challenge to Vacant Building Registry*, CHI. TRIB. (Aug. 26, 2013), http://articles.chicagotribune.com/2013-08-26/business/chi-chicago-vacant-building-registry-20130825_1_fhfa-federal-housing-finance-agency-fannie-mae. A federal court recently held, however, that such local ordinances could not be applied to Fannie Mae and Freddie Mac under the doctrines of preemption and federal immunity to state and local taxation. Fed. Hous. Fin. Agency v. City of Chicago, 962 F. Supp. 2d 1044, 1056 (N.D. Ill. 2013).

¹² Robert B. Avery et al., *The 2006 HMDA Data*, 93 FED. RES. BULL. A95–97 (2007), available at <http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final>

gests that the history of residential racial discrimination by banks is repeating itself yet again: the financial institutions that own REO properties adhere to lower standards of maintenance and upkeep in neighborhoods of color than they do in white neighborhoods.

For example, the National Fair Housing Alliance (NFHA) has published two reports, one in 2011 and another in 2012, documenting the results of its investigation of racial disparities in REO maintenance.¹³ NFHA found that

[w]hile REO properties in White neighborhoods were more likely to have well-maintained lawns, secured entrances, and professional sales marketing, REO properties in African-American and Latino neighborhoods were more likely to have poorly maintained yards, unsecured entrances, look vacant or abandoned, and have poor curb appeal.¹⁴

NFHA and more than a dozen of its member fair housing organizations have filed administrative complaints with the U.S. Department of Housing and Urban Development (HUD) directly challenging the racial disparities in REO maintenance as a violation of federal civil rights law.

This Essay explains how racial disparities in the maintenance and marketing of REO properties by lenders after foreclosure may result in violations of the federal Fair Housing Act.¹⁵ In Section

.pdf (documenting racial disparities in high-priced mortgages); DEBBIE GRUENSTEIN BOCIAN ET AL., *CTR. FOR RESPONSIBLE LENDING, LOST GROUND*, 2011: DISPARITIES IN MORTGAGE LENDING AND FORECLOSURES 5, 11, 19–23 (2011), available at <http://www.responsiblelending.org/mortgage-lending/research-analysis/Lost-Ground-2011.pdf>; RICK COHEN, *THE KIRWAN INST. FOR THE STUDY OF RACE & ETHNICITY AT OHIO ST. UNIV., A STRUCTURAL RACISM LENS ON SUBPRIME FORECLOSURES AND VACANT PROPERTIES* 4–5 (2008), available at http://www.kirwaninstitute.osu.edu/reports/2008/10_2008_StructuralRacismandSubprimeRickCohen.pdf; Geoff Smith & Sara Duda, *Lender Owned Largely Vacant Properties Disproportionately Impact Communities of Color*, WOODSTOCK INST. (Nov. 13, 2008), <http://www.woodstockinst.org/blog/2008/lender-owned-largely-vacant-properties-disproportionately-impact-communities-color>.

¹³ See NAT'L FAIR HOUS. ALLIANCE, *HERE COMES THE BANK, THERE GOES OUR NEIGHBORHOOD: HOW LENDERS DISCRIMINATE IN THE TREATMENT OF FORECLOSED HOMES* (2011) [hereinafter *HERE COMES THE BANK*], available at <http://www.nationalfairhousing.org/LinkClick.aspx?fileticket=UF6xIHF35rI%3D&tabid=3917&mid=9405>; NAT'L FAIR HOUS. ALLIANCE, *THE BANKS ARE BACK, OUR NEIGHBORHOODS ARE NOT: DISCRIMINATION IN THE MAINTENANCE AND MARKETING OF REO PROPERTIES* (2012), available at http://www.nationalfairhousing.org/Portals/33/the_banks_are_back_web.pdf.

¹⁴ *HERE COMES THE BANK*, *supra* note 13, at 2.

¹⁵ 42 U.S.C. §§ 3601–3619, 3631 (2012). Although this Essay focuses on the federal Fair Housing Act, other civil rights laws may also apply to the racially disparate neglect of lender-owned REOs. For example, 42 U.S.C. § 1982 guarantees that “all citizens of the United States shall have the same right . . . as is enjoyed by white citizens thereof to inherit, purchase, lease, sell, hold, and convey real and personal property.” The U.S. Supreme Court has recognized that the statute may be violated where the chal-

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II(A), we demonstrate that lenders' comparative neglect of REO properties in Black and Latino neighborhoods constitutes prohibited racial discrimination under the Act. Then in Section II(B), we turn to an analysis of statutory language, case law, and HUD regulations supporting three distinct bases of liability for discriminatory neglect of REO properties in neighborhoods of color. First, the neglect of REO properties in neighborhoods of color significantly and adversely affects their availability for purchase in violation of sections 3604(a) and 3605.¹⁶ Second, racial disparities in maintenance constitute discrimination in the terms, conditions, and privileges of sale of a dwelling and in the provision of services in connection therewith, in violation of section 3604(b).¹⁷ Finally, discriminatory maintenance of REOs "perpetuates segregation" in ways that are prohibited by the Fair Housing Act.¹⁸

II. APPLICATION OF THE FAIR HOUSING ACT TO DISCRIMINATORY MAINTENANCE OF REO PROPERTIES

The legal theories discussed below constitute a fairly straightforward extension of well-established precedent to the maintenance and sale of REO properties. Indeed, these claims are the natural extension of jurisprudence holding that redlining and other forms of housing discrimination based on neighborhood racial composition are forbidden by the Fair Housing Act.

A. *The Fair Housing Act's Application to Neighborhood-Based Discrimination Is Well Established*

Discrimination in housing services based on the racial composition of a neighborhood is a familiar practice in American housing markets, and it is forbidden by the Fair Housing Act.¹⁹ Courts have long held, for example, that the Fair Housing Act forbids "racial steering" where real estate agents "direct[] prospective home buyers interested in equivalent properties to different areas according to their race" and the race of the relevant neighborhoods.²⁰ It is

lenged conduct "depreciate[s] the value of the property owned by [B]lack citizens." *City of Memphis v. Greene*, 451 U.S. 100, 123 (1981). Evidence that blighted REOs do indeed "depreciate[] the value of property" owned by Black and Latino citizens suggests that § 1982 may provide a remedy to homeowners adversely affected by lenders' failure to maintain REOs in their neighborhoods. *See id.*

¹⁶ *See infra* Section II(B)(1).

¹⁷ *See infra* Section II(B)(2).

¹⁸ *See infra* Section II(B)(3).

¹⁹ *Ring v. First Interstate Mortg., Inc.*, 984 F.2d 924, 927–28 (8th Cir. 1993).

²⁰ *Gladstone Realtors v. Vill. of Bellwood*, 441 U.S. 91, 94 (1979); *see also* *Zuch v. Hussey*, 394 F. Supp. 1028, 1047 (E.D. Mich. 1975), *aff'd and remanded*, 547 F.2d 1168

equally well established that the Fair Housing Act prohibits “redlining,” or discrimination in the provision of housing-related financial services based on the race of a neighborhood.²¹

The term *redlining* takes its name from color-coded maps included in lending manuals produced in the 1930s by the federal Home Owners Loan Corporation (HOLC).²² Undesirable neighborhoods—which were defined in part by the presence or predicted increase of racial and ethnic minorities, particularly African Americans—were marked with red lines and described as a poor credit risk.²³ HOLC’s redlined maps profoundly influenced mortgage lending throughout the country as both private banks and the Federal Housing Administration (responsible for federal home loan guarantees) adopted HOLC’s criteria, including the focus on neighborhood racial composition.²⁴

After the passage of the Fair Housing Act, federal courts held that the Act prohibited redlining in private mortgage lending because it injected “racial considerations” into the availability of housing and related financial services.²⁵ Next, application of the Act was

(6th Cir. 1977) (confirming that § 3604(a) of the FHA makes it unlawful to channel a prospective buyer into or away from an area based on the buyer’s race).

²¹ See *Simms v. First Gibraltar Bank*, 83 F.3d 1546, 1551 n.12 (5th Cir. 1996) (“Redlining means ‘mortgage credit discrimination based on the characteristics of the neighborhood surrounding the would-be borrower’s dwelling.’”); *Old West End Ass’n v. Buckeye Fed. Sav. & Loan*, 675 F. Supp. 1100 (N.D. Ohio 1987) (mortgage redlining violates the Fair Housing Act); *accord Laufman v. Oakley Bldg. & Loan Co.*, 408 F. Supp. 2d 489 (S.D. Ohio 1976). See also *N.A.A.C.P. v. Am. Family Mut. Ins. Co.*, 978 F.2d 287, 300 (7th Cir. 1992) (“*American Family*”) (redlining in homeowner’s insurance is forbidden by the Fair Housing Act); *accord Nationwide Mut. Ins. Co. v. Cisneros*, 52 F.3d 1351, 1359–60 (6th Cir. 1995); *Nat’l Fair Hous. Alliance v. Prudential Ins. Co. of Am.*, 208 F. Supp. 2d 46, 60–61 (D.D.C. 2002).

²² DOUGLAS S. MASSEY & NANCY A. DENTON, *AMERICAN APARTHEID: SEGREGATION AND THE MAKING OF THE UNDERCLASS* 51–52 (1993); see also *Simms*, 83 F.3d at 1551 n.12 (“The term [redlining] derives from loan officers evaluating home mortgage applications based on a residential map where integrated and minority neighborhood are marked off in red as poor risk areas.”).

²³ MASSEY & DENTON, *supra* note 23, at 51–52.

²⁴ *Id.* at 52–55, 105. See also NAT’L COMM’N ON FAIR HOUS. & EQUAL OPPORTUNITY, *How We Got Here: The Historical Roots of Housing Segregation*, in *THE FUTURE OF FAIR HOUSING* (2008) (“[T]o ‘assist’ with lending decisions, the Federal Housing Authority prepared ‘neighborhood security maps’ that were based largely on the racial, ethnic, and economic status of residents. . . . Because federally-backed mortgages were rarely available to residents of ‘transitional,’ racially mixed, or minority neighborhoods, lenders began ‘redlining’ those neighborhoods.”); Calvin Bradford & Anne Schlay, *Assuming a Can Opener: Economic Theory’s Failure to Explain Discrimination in FHA Lending Markets*, 2 CITYSCAPE 77, 78–79 (1996), available at <http://www.huduser.org/periodicals/cityscape/vol2num1/bradford.pdf>.

²⁵ See, e.g., *Laufman*, 408 F.Supp. at 493.

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extended to redlining in homeowners' insurance discrimination.²⁶ Following the evolution of lending discrimination, courts have more recently recognized so-called "reverse redlining" claims where lenders target predominantly minority areas for predatory mortgages.²⁷

A mortgage redlining case from the late 1980s, *Old West End Association v. Buckeye Federal Savings & Loan (Buckeye)*,²⁸ provides a useful illustration of a claim based on the race of a neighborhood, rather than the race of the particular plaintiff. In *Buckeye*, the court considered a redlining claim brought by white buyers who were denied a mortgage loan for a home in a minority neighborhood even though the sale price was supported by an independent appraisal and the buyers were creditworthy.²⁹ The bank argued that the buyers could not prove discrimination.³⁰ The court rejected this argument because plaintiffs had put forward expert evidence showing "statistically significant differences between Buckeye's treatment of conventional mortgage loan applications originating from white neighborhoods and Buckeye's treatment of similar applications from integrated or minority neighborhoods."³¹ The race of the particular buyers was "irrelevant" to the determination of whether the bank's lending practices were racially discriminatory—precisely because discrimination on the basis of neighborhood racial composition is sufficient to support a claim under the Fair Housing Act.³²

The same theory applies with equal force in the case of neighborhood disparities in lenders' REO property maintenance. Indeed, in many ways this new phenomenon is simply a continuation of our country's long history of residential discrimination by financial institutions: first mortgages were withheld from neighborhoods of color, then more recently neighborhoods of color were targeted for expensive and unfair mortgages,³³ and now financial

²⁶ *Am. Family Mut. Ins. Co.*, 978 F.2d at 300; *Nationwide Mut. Ins. Co.*, 52 F.3d at 1359–60; *Nat'l Fair Hous. Alliance*, 208 F. Supp. 2d at 60–61 (D.D.C. 2002).

²⁷ *Steed v. EverHome Mortg. Co.*, 308 Fed. App'x. 364, 368 (11th Cir. 2009); *City of Memphis v. Wells Fargo Bank, N.A.*, 09-2857-STA, 2011 WL 1706756, at *14 n. 56 (W.D. Tenn. May 4, 2011) (collecting cases demonstrating that reverse redlining violates the FHA and supports a claim of disparate treatment).

²⁸ 675 F. Supp. 1100 (N.D. Ohio 1987).

²⁹ *Id.* at 1103.

³⁰ *Id.* at 1105.

³¹ *Id.*

³² *See id.* at 1102–03.

³³ *See, e.g.*, Robert G. Schwemm & Jeffrey L. Taren, *Discretionary Pricing, Mortgage Discrimination, and the Fair Housing Act*, 45 HARV. C.R.-C.L. L. REV. 375, 385–86,

institutions are allowing REO properties in neighborhoods of color to deteriorate due to a lack of proper maintenance. Although the harmful conduct has varied over time, the geographic nature of discrimination remains unchanged, and is thus equally cognizable under the Fair Housing Act. Evidence that there are differences in the services provided to REO properties according to the race of the neighborhood is thus sufficient to establish a prima facie case of racial discrimination under the FHA.³⁴

B. Discriminatory REO Maintenance Impedes Availability, Constitutes Discrimination in the Provision of Services, and Perpetuates Segregation

This section outlines three independent bases of liability under the Fair Housing Act. First, neglect of REOs in neighborhoods of color significantly and adversely affects the “availability” of those properties for sale, in violation of sections 3604(a) and 3605.³⁵ Second, discrimination in the maintenance of REO properties falls squarely within the language of section 3604(b), which prohibits discrimination in the “terms, conditions, or privileges” of the sale of a dwelling “or in the provision of services . . . in connection therewith.”³⁶ Third, the impact of REO properties on surrounding properties perpetuates segregation by constricting the mobility of households of color and discouraging others from moving into Black and Latino neighborhoods.

1. The Neglect of REO Properties in Neighborhoods of Color Significantly and Adversely Affects Their Availability for Purchase

The discriminatory provision of maintenance services to REO properties in neighborhoods of color can create significant barriers to the prospective purchase of those properties. This adverse impact on the availability of housing in neighborhoods of color creates a cause of action under section 3604(a), which makes it

398–400 (2010) (describing historical and recent forms of mortgage lending discrimination).

³⁴ See *Buckeye*, 675 F. Supp. at 1105.

³⁵ Section 3604(a) provides that it shall be unlawful “to refuse to negotiate for the sale or rental of, or otherwise make unavailable or deny, a dwelling to any person because of race” 42 U.S.C. § 3604(a) (2012) (emphasis added); section 3605 provides that it shall be unlawful for any entity “whose business includes engaging in residential real estate-related transactions to discriminate against any person *in making available such a transaction* . . . because of race” *Id.* § 3605 (emphasis added).

³⁶ *Id.* § 3604(b).

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unlawful “to refuse to negotiate for the sale or rental of, or otherwise make unavailable or deny, a dwelling to any person because of race[.]”³⁷ For the same reason, the conduct constitutes a violation of § 3605, under which it is illegal for entities “whose business includes engaging in real estate-related transactions,” like selling REO properties, to discriminate “in making available such a transaction, or in the terms or conditions of such a transaction.”³⁸

In some cases, the damage resulting from discriminatory neglect may be so severe that the premises are uninhabitable, thereby rendering REO residential properties literally “unavailable” for sale or rental. The consequences of withholding maintenance and repairs from properties in neighborhoods of color can impede the sale of a dwelling in other ways, even where the damage is not so extreme. First, the visible condition of the property may suggest that the property is not for sale or may discourage buyers from looking at the property. This barrier to access is actionable under the line of cases interpreting “refus[al] to negotiate” as encompassing discriminatory actions that discourage or restrict the choices of housing available in the market.³⁹ Second, the physical damage to properties in neighborhoods of color resulting from REO neglect will discourage potential buyers and may preclude the closing of a sale where the appraisal does not support the loan amount requested.

In cases regarding racial steering, courts have held that conduct that discourages or restricts the choices of dwellings in the marketplace on the basis of race constitutes a violation of § 3604(a).⁴⁰ To determine whether conduct was sufficiently “discouraging” to trigger a claim under section 3604(a), courts look “to whether the statement or conduct would have an untoward effect on a reasonable person under the circumstances who is seek-

³⁷ *Id.* § 3604(a).

³⁸ *Id.* § 3605. Subsection (b)(2) of that provision includes “[t]he selling . . . of residential real property” in the definition of “residential real-estate related transactions.” The section is thus applicable to the banks that hold title to the properties, as trustees or otherwise, because they regularly engage in the sale of REO residential properties.

³⁹ *See* *Vill. of Bellwood v. Dwivedi*, 895 F.2d 1521 (7th Cir. 1990); *Zuch v. Hussey*, 394 F. Supp. 1028, 1047 (E.D. Mich. 1975), *aff’d and remanded*, 547 F.2d 1168 (6th Cir. 1977).

⁴⁰ *See, e.g., Bellwood*, 895 F.2d at 1529 (noting that “any effort to discourage” may be sufficient to make out a racial steering claim under § 3604(a)); *Zuch*, 394 F. Supp. at 1047 (noting that “any action by a real estate agent which in any way impedes, delays, or discourages on a racial basis a prospective home buyer from purchasing housing is unlawful”).

ing housing.”⁴¹

Although courts have normally confronted conduct that restricts buyers’ choices on the basis of race in steering cases against realtors, the proposition that housing may be made “unavailable” through actions that discourage a buyer from inspecting a property is capable of broader application. HUD regulations demonstrate the breadth of § 3604(a) in this regard. 24 C.F.R. § 100.70(a) provides in pertinent part that “[i]t shall be unlawful, because of race . . . to discourage or obstruct choices in a community, neighborhood or development.”⁴² Subsection (c) of the same provision clarifies that prohibited actions under (a) “include, but are not limited to: (1) Discouraging any person from inspecting, purchasing, or renting a dwelling because of race . . . , or because of the race . . . of persons in a community, neighborhood or development.”⁴³

This regulatory language is broad enough to cover allegations of discrimination grounded in racially disparate maintenance of REO properties. Where REOs in Black and Latino neighborhoods are disproportionately likely to show visible defects—like an accumulation of trash or debris, overgrown grass and shrubbery, unsecured or broken doors and windows, unsecured holes in the structure, or broken and missing steps and handrails—such deterioration “would have an untoward effect on a reasonable person” seeking housing.⁴⁴ Such deplorable conditions will discourage the average person from inspecting or purchasing an REO dwelling, thus “obstruct[ing]” housing choices in communities of color.⁴⁵ A court or HUD could determine that racial discrimination in the provision of property maintenance services violates 24 C.F.R. § 100.70 and 42 U.S.C. § 3604(a).

Beyond the physical appearance of the property, buyers may also be discouraged by the prospect of costly repairs to remediate the damage from improper and inconsistent maintenance of REOs located in minority neighborhoods. In the 2011 study mentioned in the introduction to this Essay, the Government Accountability Office (GAO) reported on efforts by city officials and community organizations to “mitigate the damage” caused by such properties

⁴¹ *Heights Cmty. Cong. v. Hilltop Realty, Inc.*, 774 F.2d 135, 140 (6th Cir. 1985).

⁴² 24 C.F.R. § 100.70(a) (2013).

⁴³ *Id.* § 100(c). Note that this regulatory language also explicitly recognizes that the Fair Housing Act prohibits discrimination on the basis of neighborhood racial composition, as we argue in *supra* Part II(A).

⁴⁴ *See Heights Cmty. Cong.*, 774 F.2d at 140.

⁴⁵ 24 C.F.R. § 100.70(a), (c).

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by acquiring and rehabilitating them.⁴⁶ Although GAO found that “many view acquisition and rehabilitation as a strong strategy to combat the problems of vacant properties,” the study reported that the high costs of rehabilitating damaged properties sometimes make such efforts infeasible.⁴⁷ The GAO noted that “[w]ith costly rehabilitation and low housing values, governments, community development organizations, or investors may not be able to recoup their costs for rehabilitating properties in poor condition by reselling them.”⁴⁸

Evidence suggests that REO properties in neighborhoods of color are disproportionately likely to suffer from physical damage that would be costly to repair, like unsecured holes in doors, windows, and structure—problems which are very likely to give rise to even more costly complications like mold and infestations.⁴⁹ If relatively deep-pocketed municipalities, investors, and organizations that are purposefully seeking to rehabilitate foreclosed properties are put off by the high costs of repairs resulting from inadequate maintenance, individual homebuyers will be likewise deterred. As a result, the poor maintenance of properties in neighborhoods of color may operate to effectively remove those properties from the market. Moreover, even in those cases where buyers enter into a contract to buy damaged properties, banks may refuse to finance the sale if the condition of the property leads to an appraisal below the purchase price, defeating the transaction altogether.⁵⁰ The costly problems resulting from inadequate maintenance are thus another mechanism through which the discriminatory conduct of banks and property servicers impedes the sale of properties in neighborhoods of color, discouraging and restricting the choice of housing on the basis of race, in violation of the Fair Housing Act.⁵¹ This conduct by lenders makes their REO properties “unavailable” for purchase on a discriminatory basis in violation of sections 3604(a) and 3605.⁵²

⁴⁶ GAO-12-34, *supra* note 7, at 52.

⁴⁷ *Id.* at 54–55.

⁴⁸ *Id.*

⁴⁹ *See, e.g.*, sources cited *supra* note 13.

⁵⁰ *See* Steptoe v. Sav. of Am., 800 F. Supp. 1542, 1546 (N.D. Ohio 1992) (recognizing that “[a]n appraisal sufficient to support a loan request is a necessary condition precedent to a lending institution making a home loan”).

⁵¹ *See* 24 C.F.R. § 100.70(a), (c); *see generally* Vill. of Bellwood v. Dwivedi, 895 F.2d 1521, 1529 (7th Cir. 1990).

⁵² Our § 3604(a) argument is fundamentally different from the one considered by the Seventh Circuit three decades ago in a case regarding a county’s failure to maintain vacant tax-sale properties in Black neighborhoods, Southend Neighborhood Im-

2. Racial Disparities in REO Maintenance Constitute Discrimination in the Terms, Conditions, and Privileges of Sale of a Dwelling and in the Provision of Services in Connection Therewith

Section 3604(b) of the Fair Housing Act provides that it shall be unlawful “[t]o discriminate against any person in the terms, conditions, or privileges of sale or rental of a dwelling, or in the provision of services or facilities in connection therewith, because of race[.]”⁵³ HUD’s regulations implementing this section specify that “[p]rohibited actions under this section include, but are not limited to . . . [f]ailing or delaying maintenance or repairs of sale or rental dwellings” because of race.⁵⁴

The maintenance of REO properties unquestionably constitutes the “provision of services” in connection with dwellings that are on the market.⁵⁵ Regardless of the reach of § 3604(b) in connection with the provision of services after the initial acquisition of housing, a source of some disagreement among circuits, courts have not doubted that the statute applies to services provided in connection with the sale of housing.⁵⁶

Moreover, where discriminatory neglect results in physical damage to the premises or a deterioration of the landscaping, the buyer in any sales transaction is denied the “privileges” of maintenance afforded by the REO owner in similar sales transactions in white neighborhoods.⁵⁷ Additionally, as a consequence, sales transactions involving poorly maintained REOs in neighborhoods of color result in the transfer of title to the dwelling under less favorable “terms” and “conditions” that place on buyers the respon-

provement Association v. St. Clair County, 743 F.2d 1207 (7th Cir. 1984). In that case, nearby homeowners argued that the blighted vacant properties “damaged their interest in neighboring properties” by lowering home values and interfering with their ability to secure loans. *Id.* at 1208, 1210. The Seventh Circuit rejected their claims, reasoning that Section 3604(a) covered only conduct affecting the “availability” of housing, not home values. *Id.* at 1210. The *Southend* court did not consider the impact of poor maintenance on the prospective “availability” for sale of vacant properties. *See id.*

⁵³ 42 U.S.C. § 3604(b) (2012).

⁵⁴ 24 C.F.R. § 100.65(b)(2) (2013).

⁵⁵ *See* 42 U.S.C. § 3604(b).

⁵⁶ *Clifton Terrace Assocs., Ltd. v. United Techs. Corp.*, 929 F.2d 714, 720 (D.C. Cir. 1991) (Sec. 3604(b) concerns “services and facilities provided in connection with the sale or rental of housing”); *Cox v. City of Dallas*, 430 F.3d 734, 746 (5th Cir. 2005) (arguing that the language regarding services should not be “unmoor[ed]” from the sale or rental of a dwelling).

⁵⁷ *See* 42 U.S.C. § 3604(b).

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sibility of undertaking repairs and cleaning up the property.⁵⁸

While the applicability of the statute seems plain, the regulation enacted by HUD is even more direct: “[f]ailing or delaying maintenance or repairs” of dwellings for sale based on race is a “prohibited action[]” under section 3604(b).⁵⁹ REO properties are nearly by definition dwellings intended for sale, and the evidence suggests that certain lenders and their property maintenance servicers are “failing or delaying maintenance or repairs” to some REO properties on a discriminatory basis. HUD regulations interpreting the Fair Housing Act are entitled to and have routinely been granted deference from courts under the *Chevron* doctrine since Congress delegated to the agency the legal authority to issue interpretive regulations under the Fair Housing Act in 1989.⁶⁰ By expressly listing discriminatory failure to maintain dwellings for sale as a “prohibited action” under the Act, the regulatory provision thus resolves any doubt about the applicability of section 3604(b) to the maintenance of vacant homes.⁶¹

The failure to provide adequate maintenance and repairs to REOs in neighborhoods of color, while adhering to higher standards in white neighborhoods, falls under the plain language of the regulation. This discriminatory treatment of properties in different neighborhoods, then, should be understood as discrimina-

⁵⁸ See *id.*

⁵⁹ 24 C.F.R. § 100.65(b)(2).

⁶⁰ See, e.g., *NAACP v. Am. Family Mut. Ins.*, 978 F.2d 287, 300 (citing *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837 (1984)) (deferring to a HUD regulation interpreting the Act to prohibit insurance redlining); *Meyer v. Holley*, 537 U.S. 280, 287–88 (2003).

⁶¹ This regulation essentially overrules the § 3604(b) holding of the *Southend* case discussed earlier. See *supra* note 52. In that case, the Seventh Circuit held that the county’s failure to maintain vacant tax sale properties in Black neighborhoods was not actionable under § 3604(b) because that provision covered municipal services “such as police and fire protection or garbage collection,” not the maintenance of county-owned properties. *Southend*, 743 F.2d at 1210. Even setting aside the HUD regulation, the restriction of § 3604(b) to core municipal services is no longer good law. The Seventh Circuit itself has subsequently entertained § 3604(b) suits against private parties. See, e.g., *Am. Family Mut. Ins.*, 978 F.2d at 299 (property insurance is a “service” in connection with housing); see also *Bloch v. Frischholz*, 587 F.3d 771, 780 (7th Cir. 2009) (claim against condo association could proceed because ongoing governance by the association was a “condition” of plaintiffs’ purchase of their unit). Other courts have directly rejected *Southend*’s restriction to core municipal services. See, e.g., *Clifton*, 929 F.2d at 720 (noting the lack of authority and analysis to support *Southend*’s conclusion); see also ROBERT SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION § 12B:1 (2013) (noting that “anyone who commits one of the acts proscribed by the statute’s substantive provisions is liable to suit, unless he is covered by one of the exemptions contained in § 3603(b) or § 3607”).

tion “in the provision of services” in connection with dwellings, in violation of § 3604(b).

3. Discrimination in the Maintenance of REOs Perpetuates Segregation

The Fair Housing Act is also violated by acts that perpetuate housing segregation.⁶² As explained by the Seventh Circuit, the basis for a perpetuation of segregation theory is that “[c]onduct that has the necessary and foreseeable consequence of perpetuating segregation can be as deleterious as purposefully discriminatory conduct in frustrating the national commitment to replace the ghettos by truly integrated and balanced living patterns.”⁶³

The same reasoning underscores why providing lower quality maintenance services to REOs in Black and Latino neighborhoods harms interests that are central to the protections of the Fair Housing Act. The racial disparities in maintenance act to perpetuate segregation through their effects on property values and stability of minority neighborhoods. The prospects for integration in the affected neighborhood will also be diminished because white buyers will be deterred—along with others—from purchasing homes there, leaving the existing segregated racial composition of these neighborhoods unchanged. Additionally, the presence of a deteriorated and possibly dangerous REO in a neighborhood inevitably affects home values for surrounding homeowners.⁶⁴ Lower home values, in turn, will restrict the ability of minority homeowners to move into majority white or integrated neighborhoods by reducing the equity they can use to buy a new home. Allowing properties in neighborhoods of color to so deteriorate has the “necessary and foreseeable consequence of perpetuating segregation” by re-entrenching the economic dynamics that maintain racial segregation.⁶⁵

⁶² See Schwemm, *supra* note 62, § 10:7 (“[T]he perpetuation of segregation theory is an independent way of establishing a Fair Housing Act violation[.]”); *Huntington Branch, NAACP v. Town of Huntington*, 844 F.2d 926, 937–38 (2d Cir. 1988); *United States v. City of Parma*, 494 F. Supp. 1049, 1097, 1099–1100 (N.D. Ohio 1980), *aff'd*, 661 F.2d 562, 575–76 (6th Cir. 1981); *Metro. Hous. Dev. Corp. v. Vill. of Arlington Heights*, 558 F.2d 1283, 1290 (7th Cir. 1977) [hereinafter *Arlington Heights II*]; *United States v. City of Black Jack, Mo.*, 508 F.2d 1179, 1184–1186 (8th Cir. 1974).

⁶³ *Arlington Heights II*, 558 F.2d at 1289 (citing *Trafficante v. Metro. Life Ins. Co.*, 409 U.S. 205, 211) (internal quotations omitted).

⁶⁴ The GAO report cited earlier relays findings “that vacant foreclosed properties may have reduced prices of nearby homes by \$8,600 to \$17,000 per property in specific cities.” GAO-12-34, *supra* note 7 at 1, 44–45.

⁶⁵ See *Arlington Heights II*, 558 F.2d at 1290; see also Richard Thompson Ford, *The Boundaries of Race: Political Geography in Legal Analysis*, 107 HARV. L. REV. 1841, 1844–60

III. CONCLUSION

Redlining is no more acceptable in the provision of maintenance services than it is in the provision and pricing of mortgages or homeowner's insurance. Banks and their maintenance servicers have assumed the responsibility of maintaining REO dwellings for eventual sale in the marketplace; they must accept their responsibility to provide those services equally across all neighborhoods, regardless of racial composition. The failure to do so results in racial discrimination in the provision of services with regard to housing; in the terms, conditions, and privileges of sale of REO properties in neighborhoods of color; and in the availability of those properties to prospective purchasers. These harms, when imposed on the basis of race, violate the Fair Housing Act.

(June 1994) (describing how racialized disparities in neighborhood conditions perpetuate segregation).

